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Background

India's chemicals story is one of outperformance and promise. A consistent value creator, the chemical industry remains an attractive hub of opportunities even in an environment of global uncertainties. Worldwide trends affecting the global chemical industry could lead to near-term opportunities for chemical companies in India.



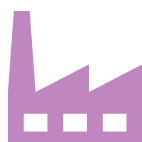
Covers >80,000 products, inevitable part of daily life



India contributes ~2.5% of global chemical sales



India is ranked 6th in the world and 4th in Asia for chemical sales



Contributes 8.8% of India's manufacturing GVA



Contributes 1.3% of India's exports



4th largest producer of agrochemicals and 2nd largest in dyes globally

Data Source: PWC Report

India's chemical industry is a supplier to diverse sectors including textiles, automotive, agriculture, packaging, pharmaceuticals, healthcare, construction, and electrical and electronics. Indian Chemical industry stands at cusp of taking majority of the world's market share, with several legal and pollution issues in China. By capturing sizeable share of global market away from China, Indian Chemical Industry can potentially double in size by encouraging investment through incentives and ease of doing business.

Specialty Chemicals

The chemicals industry can be classified into two broad segments based on value addition - basic and specialty. Basic chemicals are generally high-volume and low-value products that are sold to other

industries for further processing. On the other hand, specialty chemicals are low-volume and high-value products sold on the basis of their quality or utility, rather than composition. Since specialty chemicals are mainly used to add value to the finished product, they are primarily sold on a B2B basis.

Some Key Usage Areas for Specialty Chemicals

Agriculture	>	Fertilisers	>	Crop protection Applications				
Electronics	>	Printed Circuit Boards	>	Other Components				
Housing	>	Chemicals for Construction Materials	>	Sealants, Coatings, Paints and Plastics				
Consumer Goods	>	Perfumes	>	Detergents	>	Paper Products	>	Pharmaceuticals

The speciality chemicals industry is a mature sector with proven benefits accruing to a wide range of end-use customers. It comprises about 17% of the global

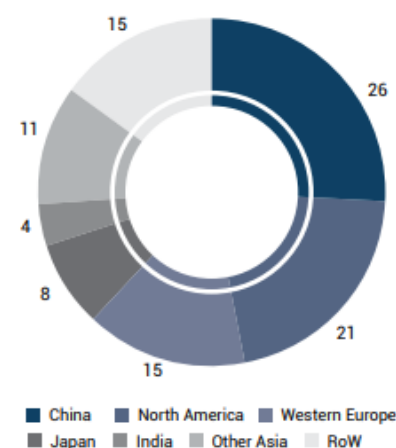
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chemicals market and is expected to grow at an average of 5.3% between 2019 and 2024, picking up pace on the back of emerging usage applications in a variety of industrial sectors.

The last two decades have seen a significant shift in the global specialty chemicals industry with developed countries losing their production supremacy (particularly the US) to emerging market nations in Asia. Key facilitators for this shift include stricter environmental norms in western countries and cost advantages enjoyed by emerging markets in terms of logistics and labour.

China, over last many decades, had been a key beneficiary in this shift from developed to emerging markets, gaining the largest share in the domain, due to availability of feedstock, cheap labour, government support, cheap capital, ease of setting up facilities and a sizable end-use market.

Specialty Chemical share by country

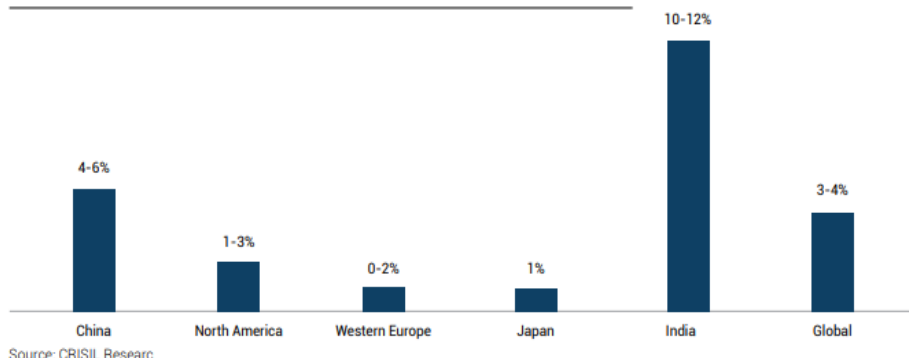


Data Source: Company Annual Report – Aarti Industries

Key growth drivers for specialty chemicals industry in India

Indian specialty chemicals market can witness sharp growth compared with other regions. In terms of region-wise demand, India's specialty chemicals industry is expected to witness growth of 10-12% CAGR between 2020 to 2025.

Region-wise expected growth in specialty chemicals (CY 2020-2025 CAGR)



Source: CRISIL Research

China's losing its dominance:

China's specialty chemicals market has seen a downturn in recent years due to various factors. Some major factors that have contributed to a slowdown in the specialty chemicals market in China includes stringent compliance

of environmental norms, rising labour costs, slowing domestic demand, tightening of financial availability, appreciation of Chinese currency, etc. As a result of these, Chinese chemical companies are witnessing a rise in capital expenditure and operational costs, making them less competitive in the export market. This recent downturn observed in China's specialty chemicals industry is serving as an opportunity for Indian manufacturers, who have now gained a cost advantage over their Chinese counterparts. The changing regulatory and policy environment in China has led global companies to adopt China+1 policy to diversify supply risk, thereby improving opportunities for Indian players. Since, India has the requisite scale, technology, skilled labour, intellectual property protection, stronger governance and compliance practices, availability of raw materials and government support, it is best suited to leverage on this opportunity.

Increase in domestic consumption intensity compared with the developed world, the penetration of specialty chemicals within India's end-user markets is low. The per capita consumption in India is ~USD 23 (in value terms) vis-à-vis global average of USD 100. Furthermore, India's urban population is expected

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to increase by 275 million people by 2030. This will result in high consumption-led growth for specialty chemicals (as it is a key input in most consumption goods – Electronics, consumer goods, home improvements, etc.) in key end markets and an increased need for better products and services.

Trade war will create opportunity for Indian players. Trade conflicts have erupted around the world, especially amongst China, the United States and western Europe. These have led to shifts in global supply chains, affecting bilateral trade between China and the US. The trade-war induced imposition of tariffs would impact the trade between US/Europe and China adversely. Thus, many downstream multinational companies that imported the bulk of their chemical requirements from China may consider supplementing this supply from elsewhere. Large chemical markets that remain accessible in this scenario could present opportunities for Indian chemical companies.

Specialty chemicals is where India will dominate. Global Specialty chemical market is ~USD 800 bn. where India's share is 1/4th that of China. Indian companies have just scratched the surface. Some of the largest specialty chemical companies in India have less than USD 1 bn sales compared to global market size of USD 800bn. This provides a long runway for growth for these companies. More importantly, specialty chemical is more profitable business compared to commodity chemicals and India has right to win in this segment due to structural advantage apart from tailwinds of the geopolitics and environmental concerns in China. In the near term, risks of volatility in margins due to rising input inflation remains high.

Edelweiss Equity Funds are capitalising this opportunity

Most long-only portfolios are currently overweight on chemical/specialty chemical sector. Following are some key holdings in chemical sector across long-only funds.

Companies	Edelweiss Flexi Cap Fund	Edelweiss Large & Mid Cap Fund	Edelweiss Long Term Equity Fund	Edelweiss Mid Cap Fund	Edelweiss Small Cap Fund
Navin Fluorine International Ltd.	1.04	1.73	1.00	2.51	1.64
Atul Ltd.		0.71			
Aarti Industries Ltd.			0.87	0.86	
SRF	2.76	1.72	1.30	3.01	1.38
Tata Chemicals Ltd.				0.45	0.45
Vinati Organics Ltd.				0.48	0.44
Deepak Nitrite Ltd.					0.45
Fine Organic Industries Ltd.					1.36
Nocil Ltd.					0.45
Sudarshan Chemical Industries Ltd.					0.67

Portfolio holdings as on Feb 28, 2022. Exposure as a % of NAV. The above stocks are currently part of the portfolio. There is no assurance or guarantee of future position in the above stocks.

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Disclaimer

The purpose of this product is to offer a brief & simplified rationale behind our investments in certain businesses/themes in our long only portfolios. This is not meant to be an elaborate research report or a recommendation. In this note we explain why we are positive on India's Specialty Chemical Sector. This Note is for information purposes only for distributors and does not constitute an offer or recommendation to buy or sell any scheme of Edelweiss Mutual Fund. This also does not constitute an offer or recommendation to buy or sell any financial products offered by Edelweiss. Any action taken by you on the basis of the information contained herein is your responsibility alone and Edelweiss Asset Management Limited (the AMC)/Edelweiss Trusteeship Company Limited/ Edelweiss Mutual Fund or its directors or employees will not be liable in any manner for the consequences of such action taken by you. The AMC takes no responsibility of updating any data/information in this material from time to time. The information shall not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of the AMC.

For fund riskometers please visit [link](#)

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