



MEGACHEM LIMITED
Registration No.198803293M

**RESPONSES TO QUESTIONS FROM THE SECURITIES INVESTORS ASSOCIATION
(SINGAPORE) AND SHAREHOLDERS**

The Board of Directors (the “**Board**”) of Megachem Limited (“**Megachem**” or the “**Company**”, and together with its subsidiaries and associated companies, collectively the “**Group**”) refers to:

(a) the annual report of the Company for the financial year ended 31 December 2019 (the “**Annual Report**”);

(b) the notice of annual general meeting (“**AGM**”) issued on 3 June 2020 informing shareholders that the Company’s AGM will be convened and held by way of electronic means on **Thursday, 25 June 2020 at 2.30 pm.**

The Company has received questions from the Securities Investors Association (Singapore) (“**SIAS**”) in relation to the Annual Report. Please refer to SIAS website at https://sias.org.sg/media/qareport/3%20Questions_Megachem%20Limited%202020.pdf for the list of questions received from SIAS, and Annex A hereto for the Management and the Board’s responses to its questions.

The Company would like to thank shareholders for submitting their questions in advance of our AGM. Please refer to Annex B hereto for the list of questions received from shareholders, and the Management and the Board’s responses to these questions.

By order of the Board

Chew Choon Tee
Managing Director

23 June 2020

ANNEX A RESPONSES TO QUESTIONS FROM SIAS

Question 1

As mentioned in the chairman's statement, the group achieved stable sales volume but recognised a 3.5% dip in revenue to \$113.8 million due to lower prices as compared to a year ago. The group experienced the greatest increase of 11.6% to Europe, with revenue from Europe increasing to \$9.3 million. On the flip side, revenue from Australia experienced a substantial decrease, dropping 25.8% to \$4.04 million.

(i) Can the board help shareholders understand if its customers are generally "sticky" and orders tend to be recurring in nature?

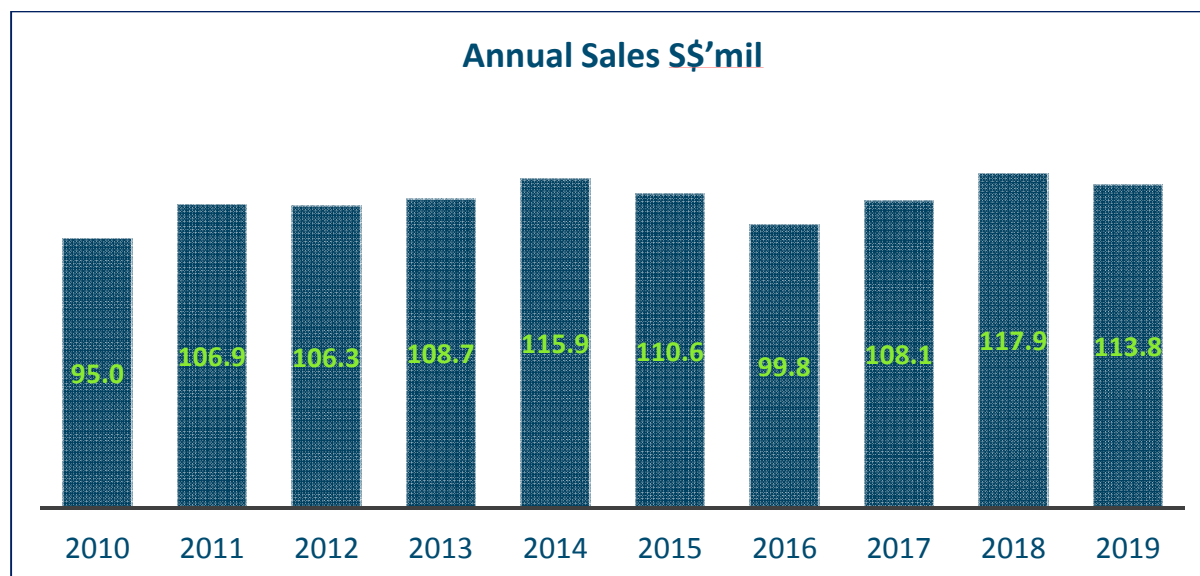
Answer

Due to stringent approval processes for the products and suppliers set by the customers as well as regulations set by authorities for certain types of chemical products, customers in this industry do not switch suppliers often and prefer sticking to the same supplier, as long as the partnership remains beneficial for both ends.

In contract manufacturing, we add value by blending materials according to our customers' formulation and specific requirements. Likewise, once formulation is approved, it is not likely to change much, and is largely recurring in nature.

(ii) What are the main reasons for the high variance in sales?

Answer



As can be seen from the chart above detailing our annual sales from FY2010 to FY2019, our sales have been quite stable over the years. This is attributed to our diversified business model and stable customer base. Over the years, we have developed partnerships with a wide range of customers comprising largely multi-national companies spread across a plethora of industries, which protects us against the impact of market volatility.

With regard to the sales revenue in FY2019, the fall reflects lower chemical prices due to lower feedstock prices. The volume of products sold was actually quite stable.

As shown in the group's business model (page 13 of the annual report), the group sources globally and distributes globally.



(Source: company annual report)

(iii) On pages 14 & 15, the company has listed its competitive strengths. Given that a distribution business is fairly commoditised, can management elaborate further on the group's unique value-add that sets it apart from its competitors?

Answer

Megachem's business can be broadly categorised into two segments – distribution and manufacturing/custom blending. Both business segments are synergistic, where we are able to provide customers with a one-stop, integrated solutions. We also possess in-depth knowledge of products and its application and functionality in the specialty chemicals industry, which is more knowledge-based.

In term of our distribution business, we offer customers ease and convenience. We have an extensive network to serve multi-national companies on a regional or global scale, coupled with proximity to customers allowing for just-in-time delivery premium service level and optimised inventory planning. One of our strongest value-add is that customers can rely on us as one single point of contact for a full-suite of products at competitive prices. We consolidate chemical materials requirements, and source and order products for customers, store them in close proximity to their production locations and deliver them "just-in-time" as they are needed, effectively reducing operational costs such as warehousing and inventory obsolescence.

(iv) How does management maintain/increase its profit margin?

Answer

Being in specialty chemicals, our margins are higher than general chemical industry or commodity chemical companies. Demand for specialty chemicals is less price sensitive as well.

We intend to improve our margins through a sharper focus on premium products, and by building up value added services such as contract manufacturing and widening our product range in higher-margin products.

In addition, in FY2014, revenue from distribution and manufacturing were approximately \$113 million and \$3.4 million respectively. In FY2019, they were \$110 million and \$3.7 million respectively.

(v) Has the group reached a level where organic growth is limited?

Answer

As chemicals are used across a wide spectrum of industries, its demand is closely correlated to economic and industrial activities. With the outbreak of COVID-19, Megachem's growth prospect is likely to be weighed down in the near-term. We remain confident in our business model and long track record that will weather us through macro uncertainties. Built on strong foundations, the Group has remained profitable since inception and withstood past crises such as the SARS epidemic in 2003 and the US Financial Crisis in 2008. Coupled with our financial discipline, we are in a strong position to overcome the negative impact of this pandemic.

Beyond the immediate term, Megachem believes that we still have many opportunities for organic growth. As stated in our Annual Report, we see Asia as the driver of our next phase of growth. There are many untapped market segments in Asia, such as in the industries of infrastructure and construction, electronics, nutraceuticals and pharmaceuticals. We believe our Asia-centric network and diversified industry coverage will provide us the platform to take advantage of the vast opportunities in this region.

Question 2

Revenue from the group's manufacturing segment remained steady at \$3.7 million. As shown in Note 31 (page 167 – Financial information by segments), the segment results were \$548,000. The major industry coverage of the group are Performance Coatings & Polymers, Advanced Polymer Composites, Surface Technology, Biotech, Oil & Gas and Resources. The breakdown can be seen on page 30.

(i) What are some of the major opportunities in the next 18-24 months?

Answer

As stated in our response to the previous question, the Asia region remains the main driver of global growth for the Group for the next decade, especially in the infrastructure and construction, electronics, nutraceuticals and pharmaceuticals industries.

Chemical producers may start to have a heavier reliance on distributors to penetrate the markets in Asia. Our extensive footprint in Asia places us in a strategic position to ride on the opportunities in this region.

Additionally, we foresee more and more customers to streamline their operations in the future. Our role as a one-stop solution provider aims to ease customers into this by assisting with consolidating their supply sources.

(ii) Are there plans to carry out manufacturing/blending in markets other than Singapore?

Answer

We currently do not have plans to expand our custom-blending activities beyond Singapore. Singapore has an unrivalled reputation for its strict adherence to intellectual property rules, which is a quality we value and appreciate. Additionally, the nature of the activity is non-labour intensive.

(iii) Did the group see any opportunities during the COVID-19 pandemic? This could be in terms of product innovation, supply of critical chemicals or even acquisitions.

Answer

The pandemic brought about greater demand for chemicals used in the cleaning industry, in line with the demand surge for deep cleaning services and disinfection and sterilisation, as well as pharmaceutical chemicals. Moreover, the disruption of the global supply chain led to many product shortages, hence raising the demand and price of such products.

We also note that there are opportunities for acquisition if we are able to find a company with a good strategic fit with our business and growth models.

Question 3

As noted in the written terms of reference of the nominating committee (“NC”), one of the responsibilities of the NC is to (page 51):

developing and maintaining a formal and transparent process for director appointments and re-nomination and making recommendations to the Board on director appointment and re-appointment (including the appointment of alternate Directors, if any), and recommending to the Board re-nominations of existing Directors for re-election in accordance with the Company’s Constitution, having regard to their competencies, commitment, contribution and performance and taking into consideration the composition and progressive renewal of the Board;

The company further stated that it does not have a formal criterion of selection for the appointment of new directors to the board and that the NC may rely on search companies, personal contacts and recommendations for the right candidates.

The three independent directors were appointed in 2003, 2007 and 2013.

(i) Would the company help shareholders understand its thinking on the progressive renewal of the board?

Answer

As listed on page 52 of the Annual Report, the Company does not have a formal criterion of selection for the appointment of new Director to the Board. When the need for a new Director arises, or where it is considered that the Board would benefit from the services of a new Director with particular skills or to replace a retiring Director, the NC, in consultation with the Board, will determine the selection criteria and will select candidates with the appropriate expertise and experience for the position.

Board appointments are made by the Board after the NC has, upon reviewing the resume of the proposed Director and conducting appropriate interviews, recommended the appointment to the Board. The NC is also in charge of re-nominating the Directors, having regard to their contribution and performance.

Pursuant to the Constitution of the Company, one-third of the Directors shall retire from office at the Company’s annual general meeting every year, provided that all Directors shall retire from office at least once every three years. Newly appointed Director by the Board is required to retire at the next annual general meeting following his appointment.

The following are our independent directors (“IDs”). Together, they possess a breadth of experience in a wide range of industries. Future renewals will have continuity in terms of the range of skillsets, experience and knowledge.

- Lee Bon Leong, who is an experienced lawyer and has served in the boards of other listed companies, and who is the current Chairman of the Board, succeeding Sidney Chew Choon Tee with effect from 1 March 2020
- Chan Kam Loon, who has served in the boards of other listed companies, has vast experience in finance
- Tay Kin Bee, who has an excellent knowledge of the chemicals industry, brings a wealth of experience he has garnered from the industry.

(ii) Would the board disclose its board diversity policy, as required by Provision 2.4 of the Code of Corporate Governance 2018?

Answer

Currently, the Company does not have a defined board diversity policy as required by Provision 2.4 of the Code of Corporate Governance 2018. However, diversity is one of the key considerations in the board renewal process to ensure that the Board is appropriately balanced to support the long-term success of the Company. For us, we view diversity in terms of skillsets, experience and value-adding to our business and growth strategy. The Board provides an appropriate balance of diversity of skills, experience, and knowledge of the Company, with core competencies in accounting and finance, legal expertise, business and management experience, industry knowledge, strategic planning and customer-based experience and knowledge. This enables the Management to benefit from the external and expert perspectives of the Directors who collectively possess the core competencies relevant to the direction and growth of the Group.

(iii) How does the company’s search and nomination process support its board diversity policy?

Answer

In the selection of director, we will take into consideration among many factors, his/her ability to value add to the business growth and to exercise independent judgement. Diversity of knowledge, experience and skillsets will remain one of the key feature in the composition of the Board, without any discrimination against gender or age.

ANNEX B

RESPONSES TO SUBSTANTIAL AND RELEVANT QUESTIONS FROM SHAREHOLDERS

Question 1

Does the company intend to expand or acquire other business since the valuations are low currently?

Answer

Megachem believes that there are many untapped opportunities for organic growth within our existing markets. As stated in our Annual Report, we see Asia as the driver of our next phase of growth. There are many market segments in Asia that possess potential for further expansion, such as in the industries of infrastructure and construction, electronics, nutraceuticals and pharmaceuticals. We believe our Asia-centric network and diversified industry coverage will provide us the platform to take advantage of the vast opportunities in this region.

Apart from organic growth, we will explore opportunities for acquisition if we are able to find a company with a good strategic fit with our business and growth models, and at fair valuation.

Question 2

How has the recent oil price fluctuation affected Megachem's business?

Answer

The impact of the oil price fluctuations on the chemicals industry can be felt both directly and indirectly. These effects include:

- i. When oil prices fall, costs of the raw materials used to make chemicals may decrease, leading to lower product cost of chemicals.
- ii. Fall in oil prices may lead to lower product cost which in turn stimulates demand and the overall chemicals industry

Commodity chemicals, which are commonly used in more upstream production, have a higher content of oil and are hence more susceptible to oil price fluctuations. Comparatively, specialty chemicals, which are more commonly downstream products, have a lower oil content and hence more immune to oil price fluctuation.

The demand for specialty chemicals is also less price sensitive as compared to commodity chemicals and its usage in finished products is also lower.

As Megachem mainly operates in the specialty chemicals business, the impact of oil price fluctuations is less as compared to a commodity chemicals company. This is evident in the fairly stable gross profit margin that we have maintained over the years.

Lower energy costs will also allow Megachem to reap cost-savings.

This announcement has been reviewed by the Company's Sponsor, SAC Capital Private Limited (the "Sponsor"),

This announcement has not been examined or approved by the Singapore Exchange Securities Trading Limited ("the "Exchange") and the Exchange assumes no responsibility for its content, including the correctness of any of the statements or opinions made, or reports contained in this online Q&A.

The contact person for the Sponsor is Ms Tay Sim Yee (Tel: (65) 6232 3210) at 1 Robinson Road, #21-00 AIA Tower, Singapore 048542.