

BUY

TP: Rs 650 | ▲ 36%

UPL

| Agrochemicals

| 01 August 2020

Mixed results; FY21 growth guidance healthy

UPL's Q1FY21 EBITDA was an 11% beat despite an 8% sales miss. EBITDA margin outperformed at 23.4% on higher gross margins, lower opex and forex gains. Adj. for forex benefit, EBITDA was a 3% beat. Order deferrals due to logistical disruptions should recover in Q2. UPL is also selectively hiking prices to counter LATAM currency headwinds. Revenue/EBITDA guidance of 6-8%/10-12% growth for FY21 is healthy and in line, while 23-24% margins for the next three years is positive. We roll to a new Sep'21 TP of Rs 650 (vs. Rs 600).

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Revenue miss (ex-India)...: Q1 revenue was widely affected by shipment delays across regions. North America (-13% YoY) was hit by the pre-buying effect, whereas BRL devaluation in LATAM (-15% YoY) led to order postponement. Europe grew 1% YoY. UPL expects Q2 to offset the Q1 miss backed by healthy agronomic conditions, product price increase in LATAM, and a growing market shift from Dicamba/Glyphosate to Gluphosinate in the US. India (+27% YoY) was robust and ROW (+5% YoY) modest due to the forex impact in Africa.

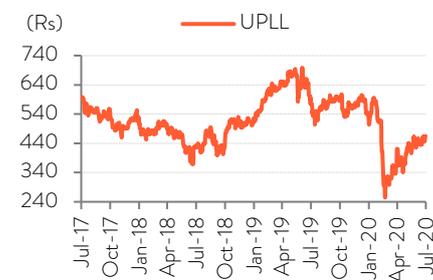
Ticker/Price	UPLL IN/Rs 478
Market cap	US\$ 4.9bn
Shares o/s	765mn
3M ADV	US\$ 38.4mn
52wk high/low	Rs 618/Rs 240
Promoter/FPI/DII	28%/44%/10%

Source: NSE

...but beat on margins: Adjusted for 1.6ppt in forex gains, EBITDA margin was at 22% (18% est.) in Q1, led by a better product mix and reduction in staff cost (-10% QoQ) and SGA (-3% QoQ), with more room for cost savings.

Retains 2x net debt/EBITDA target by FY21: Net working capital is under control at 84 days (from 80 days QoQ and 115 days YoY). Management sees an opportunity to raise payables by 15-20 days at least in FY21 and retains its commitment to achieving ~2x net debt/EBITDA by FY21 (from 2.7x in FY20).

STOCK PERFORMANCE



Earnings call takeaways: (1) Q1 capex of US\$ 72mn should moderate. (2) In LATAM, expect late-FY21 launch for a soybean antirust fungicide – market size US\$ 1.5bn. (3) Cash level high at Rs 104bn due to global pandemic.

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20P	FY21E	FY22E	FY23E
Total revenue (Rs mn)	218,350	357,560	381,968	421,409	459,804
EBITDA (Rs mn)	38,110	66,910	75,912	89,197	101,318
Adj. net profit (Rs mn)	18,140	23,782	26,082	33,809	41,750
Adj. EPS (Rs)	23.7	31.1	34.1	44.2	54.6
Adj. EPS growth (%)	0.6	31.1	9.7	29.6	23.5
Adj. ROAE (%)	13.5	13.1	13.4	15.8	17.4
Adj. P/E (x)	20.2	15.4	14.0	10.8	8.8
EV/EBITDA (x)	10.6	7.7	8.0	6.6	5.7

Source: Company, BOBCAPS Research

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Important disclosures, including any required research certifications, are provided at the end of this report.



FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q1FY21	Q1FY20	YoY (%)	Q4FY20	QoQ (%)	Q1FY21E	Var (%)	FY20	FY19
Net Sales	78,330	79,060	(0.9)	111,410	(29.7)	85,235	(8.1)	357,560	218,370
EBITDA	18,320	12,400	47.7	19,040	(3.8)	16,485	11.1	66,930	38,130
Depreciation	5,220	5,770	-	5,950	-	5,650	-	21,430	9,690
EBIT	13,100	6,630	97.6	13,090	0.1	10,835	-	45,500	28,440
Interest	5,510	3,980	-	1,870	-	3,900	-	14,810	9,630
Other Income	670	390	-	210	-	300	-	1,040	2,400
PBT	8,260	3,040	171.7	11,430	(27.7)	7,235	14.2	31,730	21,210
Less: Taxation	1,430	120	-	2,110	-	1,302	-	5,210	1,650
Less: Minority Interest	1,025	384	-	1,440	-	1,300	-	3,634	430
Recurring PAT	5,805	2,536	128.9	7,880	(26.3)	4,632	25.3	22,886	19,130
Exceptional items	(250)	(720)	-	(1,710)	-	0	-	(6,230)	(4,510)
Reported PAT	5,555	1,816	205.9	6,170	(10.0)	4,632	19.9	16,656	14,620
Key Ratios (%)									
Gross Margin	54.7	45.9	-	43.9	-	50.0	-	47.4	50.1
EBITDA Margin	23.4	15.7	-	17.1	-	19.3	-	18.7	17.5
Tax / PBT	17.3	3.9	-	18.5	-	18.0	-	16.4	7.8
NPM	7.4	3.2	-	7.1	-	5.4	-	6.4	8.8
EPS (Rs)	7.6	3.3	-	10.3	-	6.1	-	29.9	25.0

Source: Company, BOBCAPS Research

FIG 2 – SEGMENT SALES

(Rs mn)	Q1FY21	Q1FY20	YoY (%)	Q4FY20	QoQ (%)	Q1FY21E	Var (%)	FY20	FY19
North America	10,270	11,859	(13.4)	25,401	(59.6)	14,515	(29.2)	56,350	36,970
Europe	17,030	16,603	2.6	20,417	(16.6)	18,263	(6.8)	53,760	35,320
LATAM	20,150	23,718	(15.0)	34,222	(41.1)	22,589	(10.8)	137,640	74,570
ROW	15,780	15,021	5.1	24,389	(35.3)	16,824	(6.2)	71,530	38,370
India	15,110	11,859	27.4	6,971	116.8	13,045	15.8	38,280	33,140
Net Sales	78,340	79,060	(0.9)	111,400	(29.7)	85,235	(8.1)	357,560	218,370

Source: Company, BOBCAPS Research

Valuation methodology

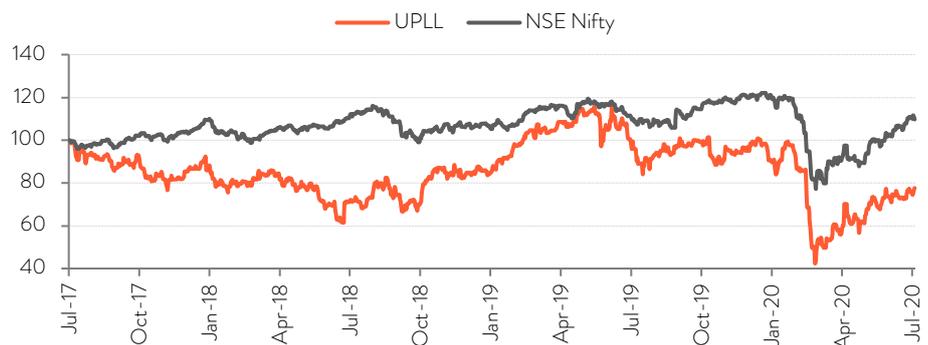
We see a convincing case for UPL to gain further market share across key geographies and to transform into a significantly underlevered company by FY23, thereby unlocking value and paving the way for a stock rerating. In our view, strong execution across a wide portfolio, synergies from the Arysta LifeScience acquisition, >18% earnings growth through to FY24, working capital efficiency and robust annual cash flows of >US\$ 600mn can lead to substantial deleveraging, from ~3.2x to 1.3x by FY24.

We retain our FY21/FY22 EPS estimates of Rs 34/Rs 44. In our view, near-term concerns of a stressed balance sheet are in the price and current valuations are attractive at 6.4x FY22E EV/EBITDA. We revise our target price to Rs 650 (from Rs 600) as we roll valuations over to Sep'22. Our TP is arrived at based on unchanged probability weights for our scenario analysis – viz. 50% weight for the base case, 40% for bull, 10% for bear – refer Fig 3); the implied 7.4x forward EV/EBITDA is 40% below the five-year mean. Maintain BUY.

FIG 3 – TARGET PRICE CALCULATION – PROBABILITY ADJUSTED

(Rs mn)	Base case	Bull case	Bear case
Operating cash flow	86,247	88,544	78,985
Free cash flow	50,154	53,082	42,403
DCF value (a)*	776,986	936,859	545,136
EBITDA	101,318	104,190	92,230
(includes: Arysta synergies US\$ mn)	240	240	216
Target EV/EBITDA (x)	9.0	11.0	7.0
EV (b)	911,862	1,146,085	645,609
Total EV (average of a + b)	844,424	1,041,472	595,372
Net Debt	176,542	164,515	197,732
Net Debt-to-EBITDA (x)	1.7	1.6	2.1
Equity Value	667,881	876,957	397,640
Per share (Average of DCF based & EV/EBITDA less @ 22% Minority stake in UPL Corp)	698	909	419
(+) Buyback of TPG/ADIA stake (FY24 NPV basis)^	-	186	-
Value per Share (Rs)	698	1,094	419
% Upside/(Downside)	88.2	195.0	13.1
Probability weights (%)	50.0	40.0	10.0
Price target Mar-23	829		
% Upside	73		
Sep'21 Price target (Rs/sh) (@18% discount rate)	650		
% upside	36		
Implied EV/EBITDA – Sep'22 (x)	7.4		
Implied P/E – Sep'22 (x)	13.2		

Source: Company, BOBCAPS Research | *We use a discount rate/terminal growth rate of 12%/4% in base case, 11%/4% in bull & 13%/3% in bear case. ^20% discount rate assumes buyback value escalates 20% from base price

FIG 4 – RELATIVE STOCK PERFORMANCE

Source: NSE

Key risks

- **Adverse climatic conditions:** Demand for UPL's crop solutions is influenced by climatic conditions, agri-commodity pricing and pest infestations. For instance, drought may reduce the need for fungicides, which could result in fewer sales and higher unsold inventories in the market, whereas excessive rain could lead to increased plant disease or weed growth, requiring growers to purchase and use more pesticides. Also, adverse agri-commodity prices could negatively impact grower profits, affecting demand for UPL's products.
- **Changing regulatory environment:** Changes in regulatory environment, particularly in the US, Brazil, China, Argentina and the EU, could adversely affect our growth estimates and margins. UPL is most sensitive to this general regulatory risk given the need to obtain and maintain pesticide registrations in every country. Many countries require re-registration of pesticides to meet new and more challenging requirements. Compliance with changing laws and regulations may involve significant costs or capital expenditures or require shifts in business practice that could result in reduced profitability.
- **Limited access to external debt financing:** UPL's near-term liquidity position is constrained by high debt leverage and depends upon its credit ratings. This could limit the company's ability to refinance borrowings, in turn restricting growth opportunities and adversely affecting operating results.
- **Shortfall in Arysta integration synergies:** Roughly 13-15% of our FY21-FY24 EBITDA is driven by Arysta-related synergies. So far, the anticipated cost savings and revenue synergies are ahead of management guidance for FY20. However, any failure in realising targeted synergies could adversely affect our margin and growth estimates.

- **Higher raw material prices:** A sharp increase in crude oil prices can affect the prices of raw materials and production cost, impacting profitability. To mitigate this, UPL has backward integrated most of its operations and is less dependent on outside supply.
- **Adverse economic and political changes:** These include inflation rates, recession, trade restrictions, tariff increases or potential new tariffs and taxes that can affect UPL's business.
- **Forex risk:** The company operates in multiple markets with the US dollar, Euro, Japanese yen and British pound as major transaction currencies. Also, 85-90% of its debt is US dollar denominated. UPL takes adequate forward covers based on net open exposures as its exports act as a natural hedge.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20P	FY21E	FY22E	FY23E
Total revenue	218,350	357,560	381,968	421,409	459,804
EBITDA	38,110	66,910	75,912	89,197	101,318
Depreciation	9,690	21,430	24,082	25,022	25,962
EBIT	28,420	45,480	51,830	64,175	75,356
Net interest income/(expenses)	(9,630)	(14,857)	(16,982)	(16,052)	(14,213)
Other income/(expenses)	1,580	2,061	3,476	3,569	2,834
Exceptional items	0	0	0	0	0
EBT	20,370	32,684	38,324	51,691	63,976
Income taxes	1,650	4,903	6,898	10,338	12,795
Extraordinary items	(3,690)	(6,200)	0	0	0
Min. int./Inc. from associates	580	3,999	5,343	7,543	9,431
Reported net profit	14,450	17,582	26,082	33,809	41,750
Adjustments	(3,690)	(6,200)	0	0	0
Adjusted net profit	18,140	23,782	26,082	33,809	41,750

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20P	FY21E	FY22E	FY23E
Accounts payables	93,970	108,737	116,160	128,155	139,831
Other current liabilities	15,250	12,801	13,751	15,171	16,553
Provisions	21,840	35,764	38,206	42,151	45,991
Debt funds	289,970	277,178	312,885	262,181	232,281
Other liabilities	0	0	0	0	0
Equity capital	1,020	1,530	1,530	1,530	1,530
Reserves & surplus	208,412	218,344	235,247	257,581	285,561
Shareholders' fund	209,432	219,874	236,777	259,111	287,091
Total liabilities and equities	630,462	654,355	717,778	706,767	721,747
Cash and cash eq.	28,510	53,928	85,111	57,625	55,739
Accounts receivables	118,160	118,670	136,043	150,091	163,766
Inventories	92,700	78,500	100,463	107,373	117,156
Other current assets	47,190	60,785	64,934	71,640	78,167
Investments	7,062	7,062	7,062	7,062	7,062
Net fixed assets	46,540	45,110	44,028	43,006	40,050
CWIP	17,830	17,830	17,830	17,830	17,830
Intangible assets	272,470	272,470	262,306	252,142	241,978
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	630,462	654,355	717,778	706,767	721,747

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20P	FY21E	FY22E	FY23E
Net income + Depreciation	24,140	39,012	50,165	58,832	67,712
Interest expenses	9,630	14,857	16,982	16,052	14,213
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(63,680)	26,337	(32,671)	(10,303)	(13,086)
Other operating cash flows	0	0	0	0	0
Cash flow from operations	(29,910)	80,206	34,476	64,580	68,840
Capital expenditures	(341,640)	(20,000)	(23,000)	(24,000)	(23,007)
Change in investments	3,278	0	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(338,362)	(20,000)	(23,000)	(24,000)	(23,007)
Equities issued/Others	0	510	0	0	0
Debt raised/repaid	222,580	(12,792)	35,706	(50,704)	(29,900)
Interest expenses	(9,630)	(14,857)	(16,982)	(16,052)	(14,213)
Dividends paid	(4,240)	(7,650)	(9,180)	(11,475)	(13,770)
Other financing cash flows	159,132	0	10,164	10,164	10,164
Cash flow from financing	367,842	(34,789)	19,708	(68,067)	(47,719)
Changes in cash and cash eq.	(430)	25,418	31,184	(27,487)	(1,886)
Closing cash and cash eq.	28,510	53,928	85,111	57,625	55,739

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20P	FY21E	FY22E	FY23E
Reported EPS	18.9	23.0	34.1	44.2	54.6
Adjusted EPS	23.7	31.1	34.1	44.2	54.6
Dividend per share	8.0	10.0	12.0	15.0	18.0
Book value per share	229.9	243.5	265.6	294.8	331.4

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20P	FY21E	FY22E	FY23E
EV/Sales	1.8	1.4	1.6	1.4	1.3
EV/EBITDA	10.6	7.7	8.0	6.6	5.7
Adjusted P/E	20.2	15.4	14.0	10.8	8.8
P/BV	2.1	2.0	1.8	1.6	1.4

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20P	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	89.1	72.8	68.1	65.4	65.3
Interest burden (PBT/EBIT)	71.7	71.9	73.9	80.5	84.9
EBIT margin (EBIT/Revenue)	13.0	12.7	13.6	15.2	16.4
Asset turnover (Revenue/Avg TA)	16.6	17.9	18.2	19.7	22.1
Leverage (Avg TA/Avg Equity)	2.5	2.8	2.7	2.5	2.2
Adjusted ROAE	13.5	13.1	13.4	15.8	17.4

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY19A	FY20P	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	25.6	63.8	6.8	10.3	9.1
EBITDA	8.7	75.6	13.5	17.5	13.6
Adjusted EPS	0.6	31.1	9.7	29.6	23.5
Profitability & Return ratios (%)					
EBITDA margin	17.5	18.7	19.9	21.2	22.0
EBIT margin	13.0	12.7	13.6	15.2	16.4
Adjusted profit margin	8.3	6.7	6.8	8.0	9.1
Adjusted ROAE	13.5	13.1	13.4	15.8	17.4
ROCE	9.1	9.5	10.6	12.7	15.0
Working capital days (days)					
Receivables	198	121	130	130	130
Inventory	155	80	96	93	93
Payables	157	111	111	111	111
Ratios (x)					
Gross asset turnover	0.7	1.1	1.1	1.1	1.1
Current ratio	2.2	2.0	2.3	2.1	2.0
Net interest coverage ratio	3.0	3.1	3.1	4.0	5.3
Adjusted debt/equity	1.6	1.5	1.5	1.2	0.9

Source: Company, BOBCAPS Research

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Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

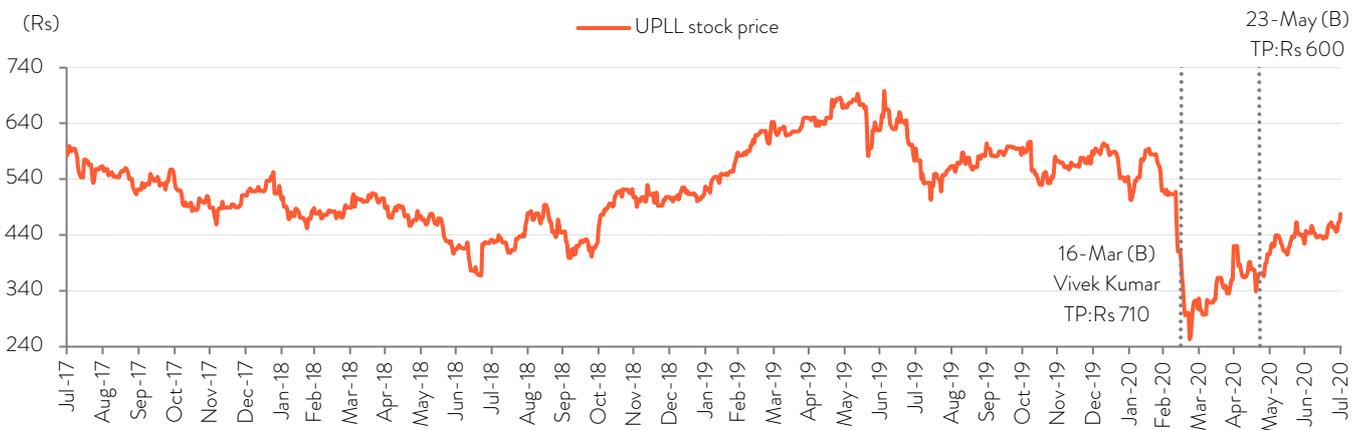
ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

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B – Buy, A – Add, R – Reduce, S – Sell

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