

**BUY**

TP: Rs 650 | ▲ 43%

**UPL**

Agrochemicals

30 October 2020

## In-line Q2 led by strong volume growth; FY21 guidance retained

UPL's Q2FY21 results were broadly in line with 14%/15% YoY growth in revenue/EBITDA. Reported EBITDA margin was a slight miss at 18.6% (20% est.) on lower gross margins and forex loss. Adj. for forex, EBITDA was a 6% beat. Favourable agronomic conditions across the US, EU and LATAM and continued price hikes in LATAM to counter currency headwinds should drive a better H2. Management maintains revenue/EBITDA growth guidance at 6-8%/10-12% for FY21 and expects 23-24% margins for the next three years. We retain our Sep'21 TP of Rs 650.

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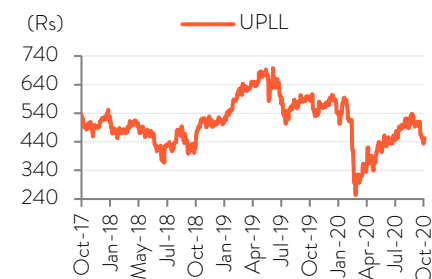
**Volume-led revenue growth recovery:** Q2 revenue grew a healthy 14% YoY on strong 19% volume growth (forex -4%, price +1%) and market share gains. North America (+25% YoY) benefited from good weather and robust miticide demand. In LATAM (+12%), strong volumes offset BRL devaluation. Europe sales grew 13%. India (+18%) saw robust growth led by rice herbicides and bio-solutions while ROW (+13%) gained from weather normalisation. UPL expects a better H2 backed by healthy agronomic conditions, product price hikes in LATAM, and a market shift from Dicamba/Glyphosate to Glufosinate in the US.

Ticker/Price	UPLL IN/Rs 453
Market cap	US\$ 4.7bn
Shares o/s	765mn
3M ADV	US\$ 35.8mn
52wk high/low	Rs 618/Rs 240
Promoter/FPI/DII	28%/44%/10%

Source: NSE

**Margins to improve in H2:** Q2 gross margin was subdued at 49.6% (55% in Q1) due to currency devaluation in LATAM. Ex-forex impact, EBITDA margin was at 20%. UPL continues to hike prices to offset the gross margin decline and is confident of further fixed cost optimisation to support EBITDA margins in H2.

## STOCK PERFORMANCE



**Earnings call takeaways:** (1) Capex at US\$ 76mn in Q2 and US\$ 148mn in H1. (2) Net debt/EBITDA of ~2x to be reached by FY21-end. (3) UPL not worried about Europe vote to ban Mancozeb given wide portfolio basket. (4) Q2 exceptional loss of US\$ 28mn was due to Netherland plant closure as a part of rationalisation; expect similar amount in H2. (5) Net working capital at 106 days (from 120 days YoY) led by strong collection in India/inventory reduction.

## KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	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	23,981	26,233	33,927	42,028
Adj. EPS (Rs)	23.7	31.3	34.3	44.3	54.9
Adj. EPS growth (%)	0.6	32.2	9.4	29.3	23.9
Adj. ROAE (%)	13.5	13.2	13.5	15.8	17.5
Adj. P/E (x)	19.1	14.5	13.2	10.2	8.3
EV/EBITDA (x)	10.1	7.4	7.7	6.3	5.5

Source: Company, BOBCAPS Research

BOB Capital Markets Ltd is a wholly owned subsidiary of Bank of Baroda

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



**FIG 1 – QUARTERLY PERFORMANCE**

(Rs mn)	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	Q2FY21E	Var (%)	H1FY21	H1FY20	YoY (%)
<b>Net Sales</b>	<b>89,390</b>	<b>78,170</b>	<b>14.4</b>	<b>78,330</b>	<b>14.1</b>	<b>87,167</b>	<b>2.6</b>	<b>167,720</b>	<b>157,230</b>	<b>6.7</b>
<b>EBITDA</b>	<b>16,670</b>	<b>14,470</b>	<b>15.2</b>	<b>18,320</b>	<b>(9.0)</b>	<b>17,099</b>	<b>(2.5)</b>	<b>34,990</b>	<b>26,870</b>	<b>30.2</b>
Depreciation	5,330	4,760	-	5,220	-	5,324	-	10,550	10,530	-
<b>EBIT</b>	<b>11,340</b>	<b>9,710</b>	<b>16.8</b>	<b>13,100</b>	<b>(13.4)</b>	<b>11,775</b>	<b>-</b>	<b>24,440</b>	<b>16,340</b>	<b>49.6</b>
Interest	3,430	3,810	-	5,510	-	3,900	-	8,940	7,790	-
Other Income	750	240	-	670	-	670	-	1,420	630	-
<b>PBT</b>	<b>8,660</b>	<b>6,140</b>	<b>41.0</b>	<b>8,260</b>	<b>4.8</b>	<b>8,545</b>	<b>1.3</b>	<b>16,920</b>	<b>9,180</b>	<b>84.3</b>
Less: Taxation	1,120	990	-	1,430	-	1,538	-	2,550	1,110	-
Less: Minority Interest	800	440	-	1,025	-	1,025	-	1,825	824	-
<b>Recurring PAT</b>	<b>6,740</b>	<b>4,710</b>	<b>43.1</b>	<b>5,805</b>	<b>16.1</b>	<b>5,982</b>	<b>12.7</b>	<b>12,545</b>	<b>7,246</b>	<b>73.1</b>
Exceptional items	(2,110)	(3,050)	-	(250)	-	0	-	(2,360)	(3,770)	-
<b>Reported PAT</b>	<b>4,630</b>	<b>1,660</b>	<b>178.9</b>	<b>5,555</b>	<b>(16.7)</b>	<b>5,982</b>	<b>(22.6)</b>	<b>10,185</b>	<b>3,476</b>	<b>193.0</b>
<b>Key Ratios (%)</b>										
Gross Margin	49.6	50.6	-	54.7	-	50.0	-	52.0	48.2	-
EBITDA Margin	18.6	18.5	-	23.4	-	19.6	-	20.9	17.1	-
Tax / PBT	12.9	16.1	-	17.3	-	18.0	-	15.1	12.1	-
NPM	7.5	6.0	-	7.4	-	6.9	-	7.5	4.6	-
<b>EPS (Rs)</b>	<b>8.8</b>	<b>6.2</b>	<b>-</b>	<b>7.6</b>	<b>-</b>	<b>7.8</b>	<b>-</b>	<b>16.4</b>	<b>9.5</b>	<b>-</b>

Source: Company, BOBCAPS Research

**FIG 2 – SEGMENT SALES**

(Rs mn)	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	Q2FY21E	Var (%)	H1FY21	H1FY20	YoY (%)
North America	7,730	6,210	24.5	10,270	(24.7)	7,336	5.4	18,000	18,069	(0.4)
Europe	10,220	9,070	12.7	17,030	(40.0)	9,977	2.4	27,250	25,673	6.1
LATAM	42,330	37,670	12.4	20,150	110.1	41,437	2.2	62,480	61,388	1.8
ROW	15,030	13,280	13.2	15,780	(4.8)	15,272	(1.6)	30,810	28,301	8.9
India	14,090	11,950	17.9	15,110	(6.8)	13,145	7.2	29,200	23,809	22.6
<b>Net Sales</b>	<b>89,400</b>	<b>78,180</b>	<b>14.4</b>	<b>78,340</b>	<b>14.1</b>	<b>87,167</b>	<b>2.6</b>	<b>167,740</b>	<b>157,240</b>	<b>6.7</b>

Source: Company, BOBCAPS Research

## Valuation methodology

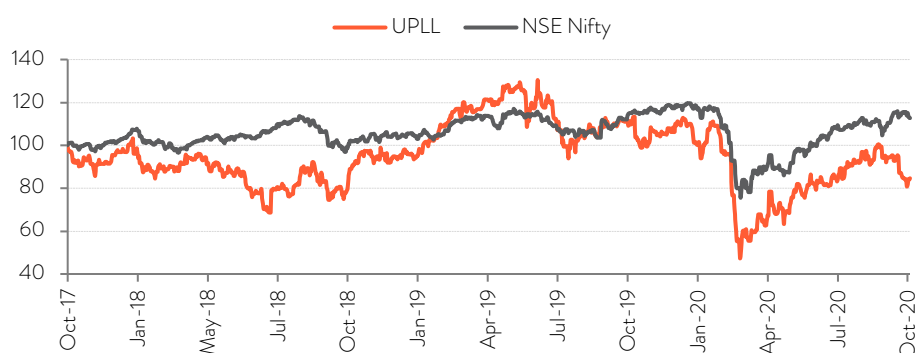
We see a convincing case for UPL to gain further market share across key geographies and to transform into a significantly underlevered company by FY23, thereby unlocking value and paving the way for a stock rerating. In our view, strong execution across a wide portfolio, synergies from the Arysta LifeScience 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/FY23 EPS estimates of Rs 34/Rs 44/Rs 55. 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 maintain our Sep'21 target price of Rs 650, 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
<b>Target EV/EBITDA (x)</b>	<b>9.0</b>	<b>11.0</b>	<b>7.0</b>
EV (b)	911,862	1,146,085	645,609
<b>Total EV (average of a + b)</b>	<b>844,424</b>	<b>1,041,472</b>	<b>595,372</b>
Net Debt	176,542	164,515	197,732
Net Debt-to-EBITDA (x)	1.7	1.6	2.1
<b>Equity Value</b>	<b>667,881</b>	<b>876,957</b>	<b>397,640</b>
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	-
<b>Value per Share (Rs)</b>	<b>698</b>	<b>1,094</b>	<b>419</b>
% Upside/(Downside)	88.2	195.0	13.1
Probability weights (%)	50.0	40.0	10.0
<b>Price target Mar-23</b>	<b>829</b>		
% Upside	73		
<b>Sep'21 Price target (Rs/sh) (@18% discount rate)</b>	<b>650</b>		
% upside	43		
<b>Implied EV/EBITDA – Sep'22 (x)</b>	<b>7.4</b>		
<b>Implied P/E – Sep'22 (x)</b>	<b>13.2</b>		

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 FY21. 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	FY20A	FY21E	FY22E	FY23E
<b>Total revenue</b>	<b>218,350</b>	<b>357,560</b>	<b>381,968</b>	<b>421,409</b>	<b>459,804</b>
EBITDA	38,110	66,910	75,912	89,197	101,318
Depreciation	9,690	21,430	22,953	23,893	24,833
EBIT	28,420	45,480	52,959	65,304	76,485
Net interest income/(expenses)	(9,630)	(14,857)	(16,982)	(16,052)	(14,213)
Other income/(expenses)	1,580	2,394	2,858	2,867	2,324
Exceptional items	0	0	0	0	0
EBT	20,370	33,017	38,835	52,119	64,595
Income taxes	1,650	4,953	6,990	10,424	12,919
Extraordinary items	(3,690)	(6,200)	0	0	0
Min. int./Inc. from associates	580	4,083	5,612	7,767	9,648
<b>Reported net profit</b>	<b>14,450</b>	<b>17,781</b>	<b>26,233</b>	<b>33,927</b>	<b>42,028</b>
Adjustments	(3,690)	(6,200)	0	0	0
<b>Adjusted net profit</b>	<b>18,140</b>	<b>23,981</b>	<b>26,233</b>	<b>33,927</b>	<b>42,028</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	93,970	102,330	116,160	128,155	139,831
Other current liabilities	15,250	16,540	13,751	15,171	16,553
Provisions	21,840	47,067	50,280	55,471	60,525
Debt funds	289,970	286,690	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	218,083	235,136	257,588	285,846
Shareholders' fund	209,432	219,613	236,666	259,118	287,376
<b>Total liabilities and equities</b>	<b>630,462</b>	<b>672,240</b>	<b>729,741</b>	<b>720,096</b>	<b>736,566</b>
Cash and cash eq.	28,510	67,240	96,098	67,718	65,065
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	66,640	64,934	71,640	78,167
Investments	7,062	5,580	5,580	5,580	5,580
Net fixed assets	46,540	55,960	56,007	56,114	54,288
CWIP	17,830	20,730	20,730	20,730	20,730
Intangible assets	272,470	258,920	249,885	240,850	231,815
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
<b>Total assets</b>	<b>630,462</b>	<b>672,240</b>	<b>729,741</b>	<b>720,096</b>	<b>736,566</b>

Source: Company, BOBCAPS Research

### Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	24,140	39,211	49,186	57,820	66,861
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)	29,116	(23,376)	(9,057)	(11,872)
Other operating cash flows	0	0	0	0	0
<b>Cash flow from operations</b>	<b>(29,910)</b>	<b>83,185</b>	<b>42,792</b>	<b>64,816</b>	<b>69,202</b>
Capital expenditures	(341,640)	(20,000)	(23,000)	(24,000)	(23,007)
Change in investments	3,278	1,482	0	0	0
Other investing cash flows	0	0	0	0	0
<b>Cash flow from investing</b>	<b>(338,362)</b>	<b>(18,518)</b>	<b>(23,000)</b>	<b>(24,000)</b>	<b>(23,007)</b>
Equities issued/Others	0	510	0	0	0
Debt raised/repaid	222,580	(3,280)	26,194	(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	(660)	9,035	9,035	9,035
<b>Cash flow from financing</b>	<b>367,842</b>	<b>(25,937)</b>	<b>9,067</b>	<b>(69,196)</b>	<b>(48,848)</b>
<b>Changes in cash and cash eq.</b>	<b>(430)</b>	<b>38,730</b>	<b>28,858</b>	<b>(28,380)</b>	<b>(2,653)</b>
<b>Closing cash and cash eq.</b>	<b>28,510</b>	<b>67,240</b>	<b>96,098</b>	<b>67,718</b>	<b>65,065</b>

### Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	18.9	23.2	34.3	44.3	54.9
Adjusted EPS	23.7	31.3	34.3	44.3	54.9
Dividend per share	8.0	10.0	12.0	15.0	18.0
Book value per share	229.9	243.8	266.1	295.4	332.4

### Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	1.8	1.4	1.5	1.3	1.2
EV/EBITDA	10.1	7.4	7.7	6.3	5.5
Adjusted P/E	19.1	14.5	13.2	10.2	8.3
P/BV	2.0	1.9	1.7	1.5	1.4

### DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	89.1	72.6	67.5	65.1	65.1
Interest burden (PBT/EBIT)	71.7	72.6	73.3	79.8	84.5
EBIT margin (EBIT/Revenue)	13.0	12.7	13.9	15.5	16.6
Asset turnover (Revenue/Avg TA)	16.6	17.8	18.1	19.7	22.1
Leverage (Avg TA/Avg Equity)	2.5	2.8	2.7	2.5	2.2
Adjusted ROAE	13.5	13.2	13.5	15.8	17.5

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

### Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
<b>YoY growth (%)</b>					
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	32.2	9.4	29.3	23.9
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	17.5	18.7	19.9	21.2	22.0
EBIT margin	13.0	12.7	13.9	15.5	16.6
Adjusted profit margin	8.3	6.7	6.9	8.1	9.1
Adjusted ROAE	13.5	13.2	13.5	15.8	17.5
ROCE	9.1	9.5	10.6	12.7	15.1
<b>Working capital days (days)</b>					
Receivables	198	121	130	130	130
Inventory	155	80	96	93	93
Payables	157	104	111	111	111
<b>Ratios (x)</b>					
Gross asset turnover	0.7	1.1	1.1	1.1	1.1
Current ratio	2.2	2.0	2.2	2.0	2.0
Net interest coverage ratio	3.0	3.1	3.1	4.1	5.4
Adjusted debt/equity	1.6	1.5	1.5	1.2	0.9

Source: Company, BOBCAPS Research



## Disclaimer

### Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

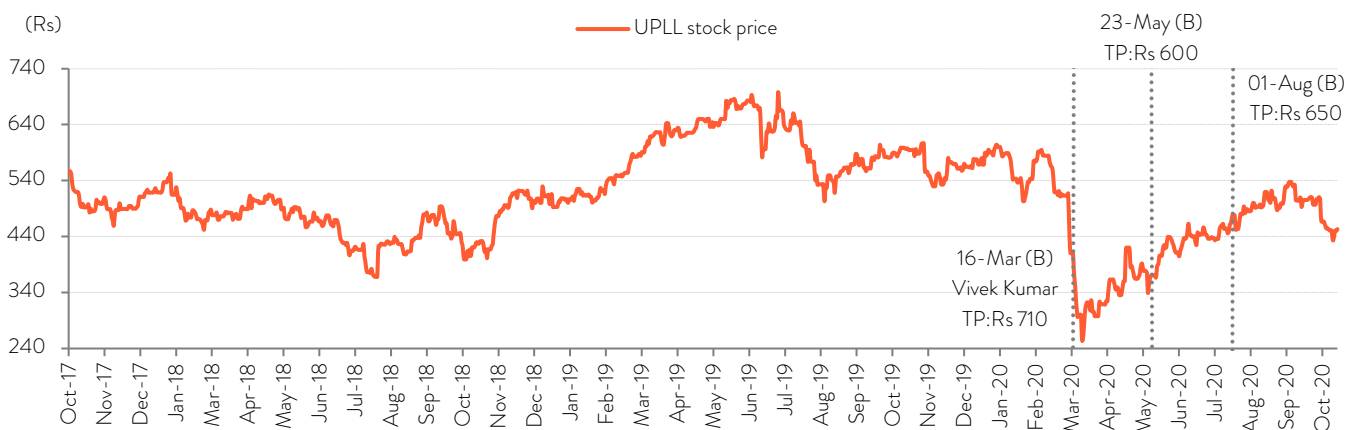
**ADD** – Expected return from >+5% to +15%

**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)

### HISTORICAL RATINGS AND TARGET PRICE: UPL (UPL IN)



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

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