

BUY

TP: Rs 725 | ▲ 29%

UPL

Agrochemicals

30 January 2021

Mixed Q3; LATAM sales pushed to Q4 – growth tailwinds strong

UPL reported a mixed Q3 with in-line EBITDA and a 9% sales miss. Gross margin uptick to 54.9% was a key positive, offsetting the sales impact, and stemmed from price hikes, a favourable product mix and cost synergies. Revenue grew 3% YoY led by 7% volume growth (forex -5%, price +1%) and market share gains. Q4 is guided to remain strong given healthy agronomic conditions and sustained price hikes. FY21 revenue/EBITDA growth guidance remains at 6-8%/10-12% with 23% margins over the next three years. We roll to a Mar'22 TP of Rs 725 (vs. Rs 650).

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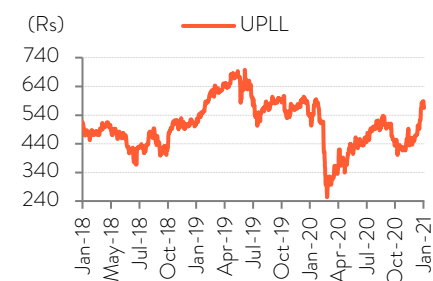
Europe/India helm growth; LATAM revenue delayed to Q4: Strong growth in Europe (+30% YoY) was fueled by new launches (esp. biologic product Argos). LATAM sales declined 8% YoY due to a drought in Brazil, delayed soybean planting and BRL devaluation. Commodity prices and recent rains support a positive Q4 outlook. ROW sales grew 6% YoY (China acceleration, Glufosinate demand) and India grew 21% (robust herbicide sales despite market slowdown).

Ticker/Price	UPLL IN/Rs 561
Market cap	US\$ 5.9bn
Shares o/s	765mn
3M ADV	US\$ 73.1mn
52wk high/low	Rs 601/Rs 240
Promoter/FPI/DII	28%/44%/10%

Source: NSE

In-line EBITDA but healthy gross margin uptick: Despite currency headwinds in LATAM, the reported Q3 gross margin was strong at 54.9% (+470bps YoY) due to price hikes, COGS savings, a favourable product mix and synergy benefits. EBITDA margin expansion was limited to 50bps YoY at 24% due to higher staff bonus provisions. UPL continues to hike prices and is confident of further fixed-cost optimisation to support margins over the next two years.

STOCK PERFORMANCE



Source: NSE

Earnings call takeaways: (1) Capex at Rs 13.6bn in 9M (Rs 10.2bn for total assets); FY21 to end at Rs 17.5bn. (2) Net debt at Rs 242bn in Q3 vs. Rs 239bn in Q2. (3) Lower net working capital at 117 days (-19 days YoY) led by account payables; set to reduce further in Q4, taking FY21 below FY20 levels. (4) On track to achieve net debt/EBITDA of ~2x by FY21. (5) Cost/Revenue synergy from Arysta at Rs 2.6bn/4.1bn in Q3. Cumulative synergy at US\$ 188mn/354mn.

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)	23.6	17.9	16.3	12.6	10.2
EV/EBITDA (x)	12.2	8.7	8.8	7.3	6.3

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)	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	Q3FY21E	Var (%)	9MFY21	9MFY20	YoY (%)
Net Sales	91,260	88,920	2.6	89,390	2.1	1,00,181	(8.9)	2,58,980	2,46,150	5.2
EBITDA	22,020	21,020	4.8	16,670	32.1	21,680	1.6	57,010	47,890	19.0
Depreciation	5,420	4,950	-	5,330	-	5,756	-	15,970	15,480	-
EBIT	16,600	16,070	3.3	11,340	46.4	15,924	-	41,040	32,410	26.6
Interest	7,450	5,150	-	3,430	-	3,602	-	16,390	12,940	-
Other Income	670	200	-	750	-	750	-	2,090	830	-
PBT	9,820	11,120	(11.7)	8,660	13.4	13,072	(24.9)	26,740	20,300	31.7
Less: Taxation	1,090	1,990	-	1,120	-	2,353	-	3,640	3,100	-
Less: Minority Interest	1,570	1,370	-	800	-	880	-	3,395	2,194	-
Recurring PAT	7,160	7,760	(7.7)	6,740	6.2	9,839	(27.2)	19,705	15,006	31.3
Exceptional items	780	(750)	-	(2,110)	-	(1,110)	-	(1,580)	(4,520)	-
Reported PAT	7,940	7,010	13.3	4,630	71.5	8,729	(9.0)	18,125	10,486	72.8
Key Ratios (%)										
Gross Margin	54.9	50.2	-	49.6	-	49.0	-	53.0	48.9	-
EBITDA Margin	24.1	23.6	-	18.6	-	21.6	-	22.0	19.5	-
Tax / PBT	11.1	17.9	-	12.9	-	18.0	-	13.6	15.3	-
NPM	7.8	8.7	-	7.5	-	9.8	-	7.6	6.1	-
EPS (Rs)	10.4	9.2	-	6.1	-	12.9	-	23.7	13.7	-

Source: Company, BOBCAPS Research

FIG 2 – REVENUE MIX

(Rs mn)	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	Q3FY21E	Var (%)	9MFY21	9MFY20	YoY (%)
North America	13,520	12,880	5.0	7,730	74.9	13,914	(2.8)	31,520	30,949	1.8
Europe	11,200	8,610	30.1	10,220	9.6	8,437	32.7	38,450	34,283	12.2
LATAM	38,490	42,030	(8.4)	42,330	(9.1)	47,914	(19.7)	100,970	103,418	(2.4)
ROW	18,990	17,900	6.1	15,030	26.3	21,666	(12.4)	49,800	46,201	7.8
India	9,060	7,500	20.8	14,090	(35.7)	8,250	9.8	38,260	31,309	22.2
Net Sales	91,260	88,920	2.6	89,400	2.1	100,181	(8.9)	259,000	246,160	5.2

Source: Company, BOBCAPS Research

Valuation methodology

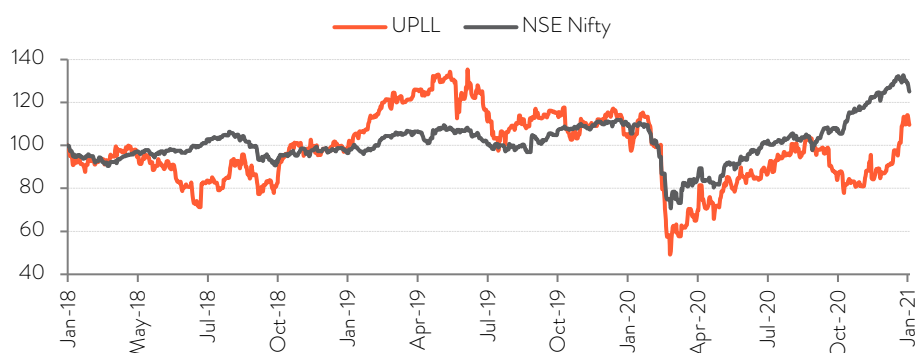
We see a convincing case for UPL to gain further market share across key geographies and to transform into a significantly underlevered company by FY23, thereby unlocking value and paving the way for a stock rerating. In our view, strong execution across a wide portfolio, synergies from the Arysta LifeScience acquisition, >18% earnings growth expected 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 raise our target price to Rs 725 (Rs 650 earlier) as we roll valuations over to Mar'23. Our TP is 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	86,021	88,318	78,759
Free cash flow	51,142	54,070	43,391
DCF value (a)*	795,459	958,255	560,300
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)	853,660	1,052,170	602,954
Net Debt	167,215	155,502	187,002
Net Debt-to-EBITDA (x)	1.7	1.5	2.0
Equity Value	686,445	896,668	415,952
Per share (Average of DCF based & EV/EBITDA less @ 22% Minority stake in UPL Corp)	720	932	440
(+) Buyback of TPG/ADIA stake (FY24 NPV basis)^	-	189	-
Value per Share (Rs)	720	1,121	440
% Upside/(Downside)	28.5	100.2	(21.4)
Probability weights (%)	50.0	40.1	9.9
Price target Mar-23	853		
% Upside	52		
Mar'22 Price target (Rs/sh) (@18% discount rate)	725		
% upside	29		
Implied EV/EBITDA – Mar'23 (x)	7.4		
Implied P/E – Mar'23 (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 FY21. However, any failure in realising targeted synergies could affect our margin and growth estimates.

- **Higher raw material prices:** A sharp increase in crude oil prices can impact the prices of raw materials and production cost, hurting 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 impede 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
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	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
Reported net profit	14,450	17,781	26,233	33,927	42,028
Adjustments	(3,690)	(6,200)	0	0	0
Adjusted net profit	18,140	23,981	26,233	33,927	42,028

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
Total liabilities and equities	630,462	672,240	729,741	720,096	736,566
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
Total assets	630,462	672,240	729,741	720,096	736,566

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
Cash flow from operations	(29,910)	83,185	42,792	64,816	69,202
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
Cash flow from investing	(338,362)	(18,518)	(23,000)	(24,000)	(23,007)
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
Cash flow from financing	367,842	(25,937)	9,067	(69,196)	(48,848)
Changes in cash and cash eq.	(430)	38,730	28,858	(28,380)	(2,653)
Closing cash and cash eq.	28,510	67,240	96,098	67,718	65,065

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	2.1	1.6	1.8	1.5	1.4
EV/EBITDA	12.2	8.7	8.8	7.3	6.3
Adjusted P/E	23.6	17.9	16.3	12.6	10.2
P/BV	2.4	2.3	2.1	1.9	1.7

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
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	32.2	9.4	29.3	23.9
Profitability & Return ratios (%)					
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
Working capital days (days)					
Receivables	198	121	130	130	130
Inventory	155	80	96	93	93
Payables	157	104	111	111	111
Ratios (x)					
Gross asset turnover	0.7	1.1	1.1	1.1	1.1
Current ratio	2.2	2.0	2.2	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

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Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

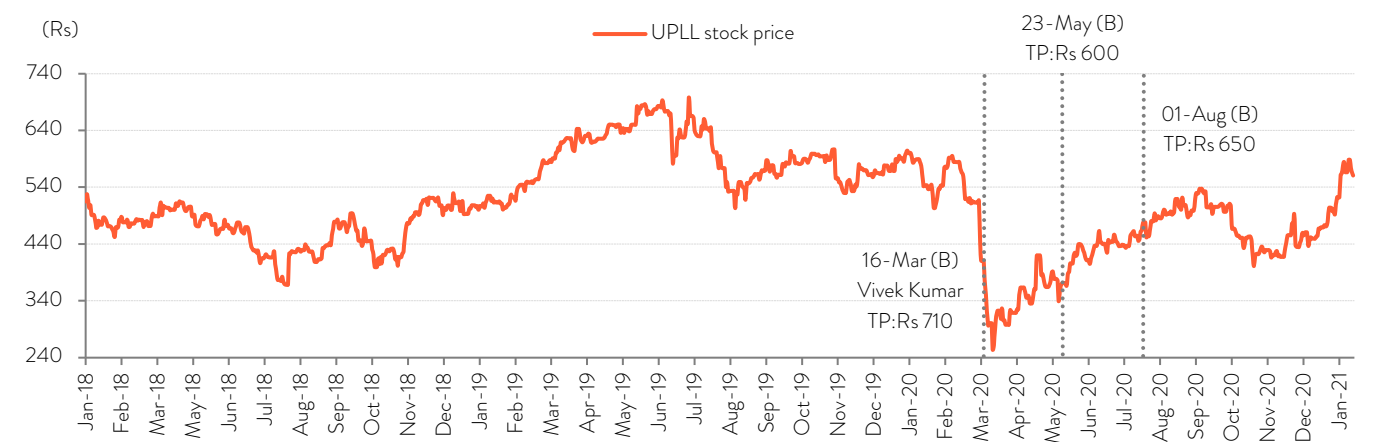
ADD – Expected return from >+5% to +15%

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)

RATINGS AND TARGET PRICE (3-YEAR HISTORY): UPL (UPL IN)



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

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