

UPL

8 November 2019

Reuters: UPLL.NS; Bloomberg: UPLL IN

US court award mars 2Q PAT- Maintain Buy

UPL 2QFY20 results have come in line with NBIE estimates at the topline of Rs78bn. Gross margins were better than expectations by 84 bps, contributed by reduction in raw material expenses. EBITDA margin came in higher at 18.5% vs our estimate of 17.7% on revenue reported at Rs78bn. Consolidated reported PAT has come in 65% lower vs. NBIE estimates due to one-time exceptional cost related to punitive damages of Rs2.2bn awarded against the company by a trial jury in the Agro Fresh litigation. Adjusted PAT came in at Rs3.94bn vs. our estimate of Rs3.24bn. During the call, the management sounded optimistic about improved volumes (across Emerging Markets and Europe), operating leverage and synergy benefits to support long term growth prospects. However, the overall 1HFY20 run rate in revenue as well as PAT is lagging street and our expectations. Hence, we are cutting our estimates over FY20-FY22E 27%/3.3%/9.6% to align growth expectations in line with YTD trends. As a result, we are trimming our TP 3.3% to Rs665 on Sept 21E PE of 14.1x. In the near term, the stock may remain subdued due to weak growth, the US litigation and concerns on the shifting goal posts on merger synergies post Arysta merger, especially those from revenue. We however maintain Buy based on long term growth prospects, once the combined UPL-Arysta portfolio starts delivering the full potential as expected by management. Maintain Buy on TP Rs665, 19% upside from CMP

Pro-forma financials above EBITDA level look healthy YoY: UPL-Arysta combines' pro-forma figures for top line and EBITDA for 2QFY20 reveals 11% growth in revenue YoY at Rs78bn, gross contribution margin at 42% and EBITDA growth of 11% at Rs14.5n. EBITDA margin came in flat YoY at 20% (pl refer discussion under call takeaways).

Synergy benefits are now stated as a combined target of Rs35bn over 3 years with Year 1 target of Rs11.2bn. The run rate achieved in 1HFY20 at Rs3.2bn vs. Year 1 accrual target of Rs5.6bn. Integration costs have been provided as exceptional at Rs88mn. The management is now confining itself to cost and revenue synergies taken together, arguing that it is difficult to identify revenue benefits separately post integration.

Demand: Demand in India was impacted by untimely heavy rainfall in Central India along with pricing pressure on key molecules. Declining sugar beet prices, Brexit, France legislation and weather impacted revenue growth in Europe. Competitive pricing pressure on Lifeline molecule impacted revenue growth in North America. ROW performance was impacted by severe drought faced by South East Asia, Australia and parts of Africa. UPL expects conditions for Europe and North America to improve, especially in H2FY20 and higher share of Europe that offers better margins, which should boost earnings going forward.

UPL expects second half to be better than first half of FY20

- 55-60% business comes from profitable geographies in 2nd half which is expected to give better margins
- Revenue and cost synergies on track
- Deleveraging of debt by US\$500mn (Rs31-35bn)

BUY

Sector: Chemicals

CMP: Rs559

Target Price: Rs665

Upside: 19%

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Key Data

Current Shares O/S (mn)	763.9
Mkt Cap (Rsbn/US\$bn)	427.1/6.0
52 Wk H / L (Rs)	709/477
Daily Vol. (3M NSE Avg.)	3,260,467

Price Performance (%)

	1-M	6-M	1-Y
UPL	(3.8)	(11.8)	14.9
Nifty Index	7.9	4.4	13.2

Source: Bloomberg

Y/E March (Rsmn)	2QFY19	2QFY20	Ch YoY %	1QFY20	Ch QoQ %	2QFY20E	Var. (%)
Net sales	42,570	78,170	83.63	79,060	(1.13)	78,111	0.08
Cost of goods	18,760	38,650	106.02	42,750	(9.59)	42,961	(10.04)
Contribution	23,810	39,520	65.98	36,310	8.84	35,150	12.43
Employee benefits expenses	4,670	8,310	77.94	8,610	(3.48)	8,610	(3.48)
Other expenses	11,270	16,740	48.54	15,300	9.41	12,740	31.40
EBITDA	7,870	14,470	83.86	12,400	16.69	13,800	4.85
EBITDAM (%)	18.49	18.51	2bps	15.68	283bps	17.67	84
Depreciation	1,810	6,080	235.91	5,770	5.37	5,770	5.37
Other income	320	240	(25.00)	390	(38.46)	390	(38.46)
Interest expenses	1,810	3,810	110.50	3,980	(4.27)	4,100	(7.07)
Exceptional Income/(Expense)	-570	-3,050	435.09	-720	323.61	-720	(523.61)
Reported PBT	4,000	1,770	(55.75)	2,320	(23.71)	3,600	(64.88)
Reported Tax	1,160	660	(43.10)	120	450.00	648	1.85
Share of profits/loss in associates	-80	-80	-	-40	100.00	-40	100.00
Minority Interest	60	140	133.33	380	(63.16)	380	(63.16)
Consolidated PAT adjusted	3,270	3,940	20.49	2,500	57.60	3,252	21.15
NPM (%)	8	5	(264bps)	3	188 bps	4	88 bps

Source: Company, Nirmal Bang Institutional Equities Research; Note: *2QFY19 doesn't include Arysta and therefore cannot be compared with 2QFY20

Please refer to the disclaimer towards the end of the document.

Rating Rationale

We have revised earnings to adjust FY20-FY22E, to align our estimates with the trend 1HFY20. Post these changes, we arrive at a Sept 21E EPS of Rs47.32. We have trimmed our TP 3.3% to Rs665 based on 14.1x PE on Sept 21 E PE (5% discount to peer group PE average). The stock looks attractive at 10.5x PE on FY22E based on CAGR of 57% in EPS and healthy ROE of 18.3-21.7% over FY21-22E

Exhibit 1: Change in estimates

Rs Mn	Revised estimate			Earlier estimate			% Revision		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue	322,342	357,609	402,544	365,045	411,813	476,124	(11.7)	(13.2)	(15.5)
EBITDA	63,545	77,958	93,729	72,258	78,654	100,177	(12.1)	(0.9)	(6.4)
EBITDA margin (%)	19.71	21.80	23.28	19.79	19.10	21.04	-	-	-
EBIT	41,302	54,218	68,689	50,015	54,914	75,137	(17.4)	(1.3)	(8.6)
EBIT margin	12.81	15.16	17.06	13.70	13.33	15.78	-	-	-
PAT	17,294	30,231	42,081	23,755	31,270	46,547	(27.2)	(3.3)	(9.6)
EPS	22.64	39.57	55.08	31.09	40.93	60.92	(27.2)	(3.3)	(9.6)
TP		665			688			(3.3)	

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Key financials

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
Revenues	173,780	218,370	322,342	357,609	402,544
EBITDA	35,050	38,130	63,545	77,958	93,729
Consolidated Net Profit Adj	20,060	18,980	17,294	30,231	42,081
EPS (Rs)	26.26	24.84	22.64	39.57	55.08
EPS gr (%)	10.95	-5.38	-8.88	74.81	39.20
EBITDA Margin (%)	20.2	17.5	19.7	21.8	23.3
P/E	22.0	23.3	25.5	14.6	10.5
EV/EBITDA	20.0	18.4	11.0	9.0	7.5
Dividend Yield (%)	0.92	0.92	0.87	1.30	1.73
Net Debt (cash)/Equity (X)	0.4	1.8	1.1	0.8	0.4
Pre-tax RoCE (%)	19.7	9.0	8.5	10.6	14.1
RoE (%)	24.2	15.9	11.2	18.3	21.7

Source: Company, Nirmal Bang Institutional Equities Research;

Exhibit 3: Margin Analysis

Margins %	2QFY19	2QFY20	Ch YoY bps	1QFY20	Ch QoQ bps
Contribution	56	51	-537	46	463
EBITDA	18.5	18.5	2	15.7	283
PBT	10.7	6.2	-457	3.8	232
PAT	8.0	5.3	-269	3.7	-163
Tax rate	25.4	13.7	-1,169	3.9	975

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: Segment Analysis

Rs Mn	2QFY19	2QFY20	Ch % YoY	Q1FY20	Ch % QoQ
Segment Revenue					
Agro Activities	41,090	75,420	83.5	76,960	-2.0
Non Agro Activities	2,300	3,460	50.4	3,740	-7.5
Unallocated	10	20	100.0	20	0.0
Total	43,400	78,900	81.8	80,720	-2.3
Less : Inter Segment Revenue	830	730	-12.0	1,660	-56.0
Revenue from Operations	42,570	78,170	83.6	79,060	-1.1
Segment EBIT					
Agro Activities	7,290	9,300	27.6	7,910	17.6
Non Agro Activities	380	880	131.6	890	-1.1
Total	7,670	10,180	32.7	8,800	15.7
Less: Finance Cost	1,810	3,810	110.5	3,980	-4.3
Less Unallocable Expense / Income (net)	1,290	1,550	20.2	1,780	-12.9
Less: Exceptional Items	570	3,050	435.1	720	323.6
PBT	4,000	1,770	-55.8	2,320	-23.7

Source: Company, Nirmal Bang Institutional Equities Research

Note:*2QFY19 doesn't include Arysta and therefore cannot be compared with Q1FY20.

Exhibit 5: Geography wise revenue analysis

Rsmn	2QFY19	2QFY20	Ch YoY %	1QFY20	Ch QoQ %
India	11,250	11,950	6.22	11,250	6.22
LatAm	30,310	37,670	24.28	23,718	58.82
NA	6,300	6,210	-1.43	13,810	-55.03
Europe	8,980	9,070	1.00	6,300	43.97
ROW	13,810	13,280	-3.84	15,021	-11.59
Consolidated Revenue	70,650	78,180	10.66	70,099	11.53

Source: Company, Nirmal Bang Institutional Equities Research;

Key takeaways from UPL 2QF20 results conference call

UPL is confident of achieving its revenue and cost synergies

Gross debt of Rs385.8bn to come down by US\$500mn (Rs35bn) over FY20

The gross debt increased by Rs17.5bn in 1HFY20 due to increase in working capital and capex of Rs6.78bn. Operating cash flows came in at Rs15.15bn. Net debt stood at Rs286.34bn.

The company stated that tighter working capital management and the repayment of debt would help to lower interest costs over time.

Pro-forma financials

Pro-forma revenue growth of 11% YoY for new UPL (including Arysta), driven by 15% volume growth and 1%/3% each impact from pricing and forex. This compares with 5% volume growth and 1% each in impact from pricing and forex in 1QFY20.

Exhibit 6: Proforma Results (UPL plus Arysta) update

	2QFY19	2QFY20	Ch %YoY	1QFY20	Ch %QoQ
Revenue	70,660	78,170	10.6	79,060	-1.1
Raw Material	39,160	45,460	16.1	45,080	0.8
Contribution	31,500	32,710	3.8	33,980	-3.7
Other Expenses	17,660	17,300	-2	17,390	-0.5
EBITDA	13,840	15,410	11.3	16,590	-7.1
Gross Margin %	44.58	41.84	-	42.98	-
EBITDA margin %	19.59	19.71	-	20.98	-

Source: Company, Nirmal Bang Institutional Equities Research; Note: Previous year numbers have been regrouped for comparison purpose

Net working capital has dipped by 4 days to 116 days. Inventory is down from 111 to 109 days. Receivable is down from 141 to 121 days. Payable is down from 132 to 114 days.

Segment revenues: Europe at 12% share is key for future margin expansion

India grew in single digits by 6% and Europe was up by 1% with 15%/12% share in total revenue, respectively. LatAm led the pack with revenue growth of 24% and had 48% share of UPL's revenue pie.

North America revenue declined marginally by 1% and RoW was down 4%.

Europe with 12% share of the pie is key for future growth in volumes and margins. The UPL leadership is hopeful of improved growth prospects as compared to the dull performance from the region during this quarter.

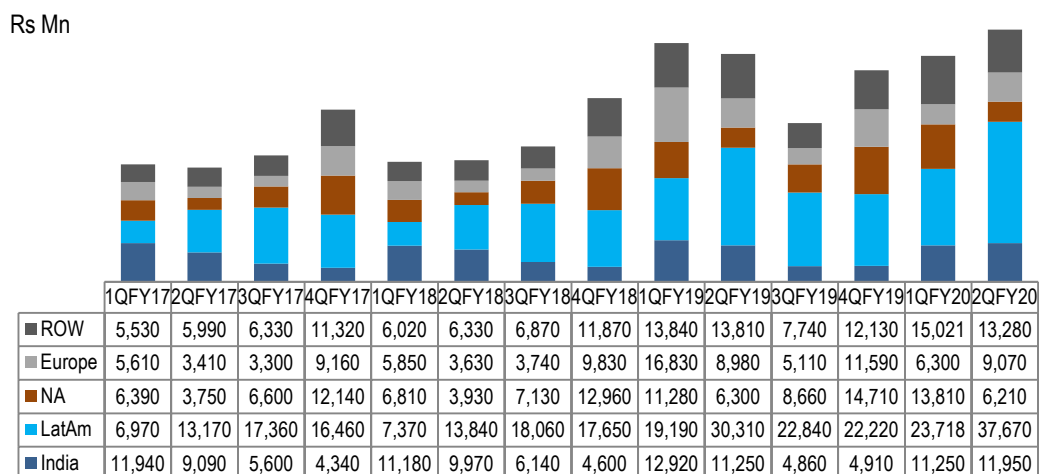
LatAm still dominates the revenue pie with 48% share and 25% growth. Management sounded positive on growth sustaining from LatAm despite concerns over weak trends in sowing and the robust growth from this region over the last three years.

Exceptional Item:

Litigation cost of Rs2.17bn has been provided for in 2QFY20 as an exceptional item due to the verdict of the US federal district court against the company and its subsidiary Decco on alleged infringement of patent, loss of profit and unjust enrichment. The company claims it for alleged violation of trade secrecy law as the patent for the technology in question has been invalidated. The company plans to appeal against this, as in its view the company had obtained the said molecule from a consultant who was also working for the plaintiff. Rs880mn pertains to integration cost of Arysta group.

Adoption of IND AS 116 increased total expense by Rs140mn in 1HFY20 and Rs70mn in 2QFY20.

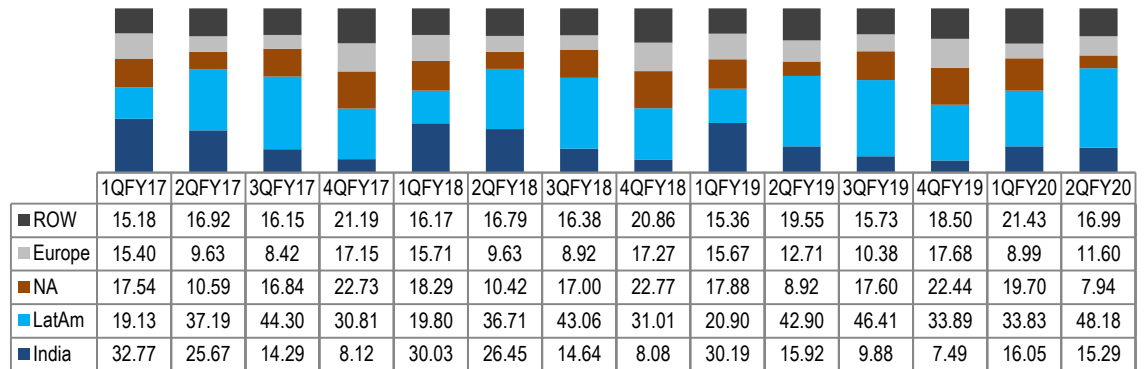
Exhibit 7: Geography wise Quarterly Revenue Share trend



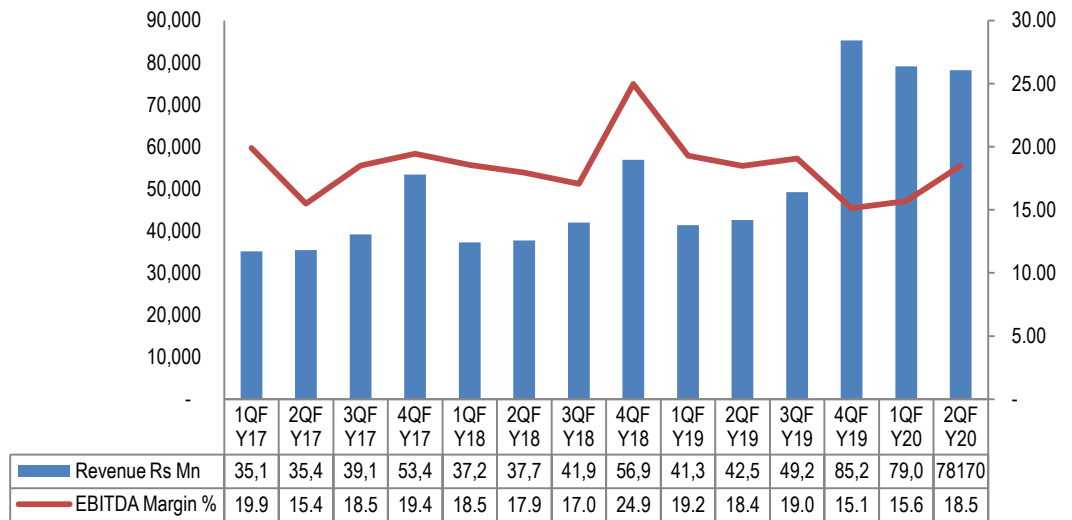
Source: Company, Nirmal Bang Institutional Equities Research; Note: Figures of 1HFY19, 1HFY20 and 4QFY19 are including Arysta

Exhibit 8: Geography wise Quarterly Revenue Pie %

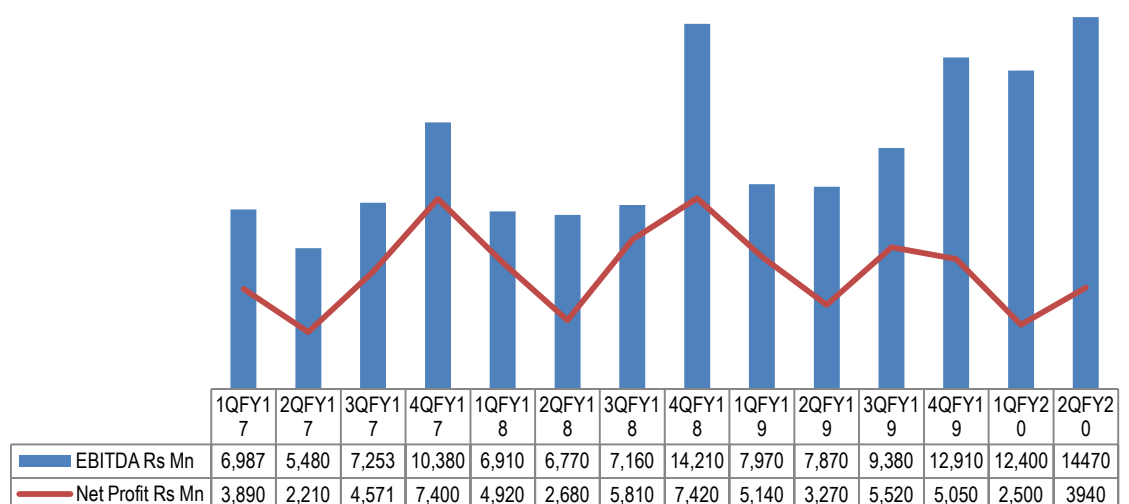
In %



Source: Company, Nirmal Bang Institutional Equities Research

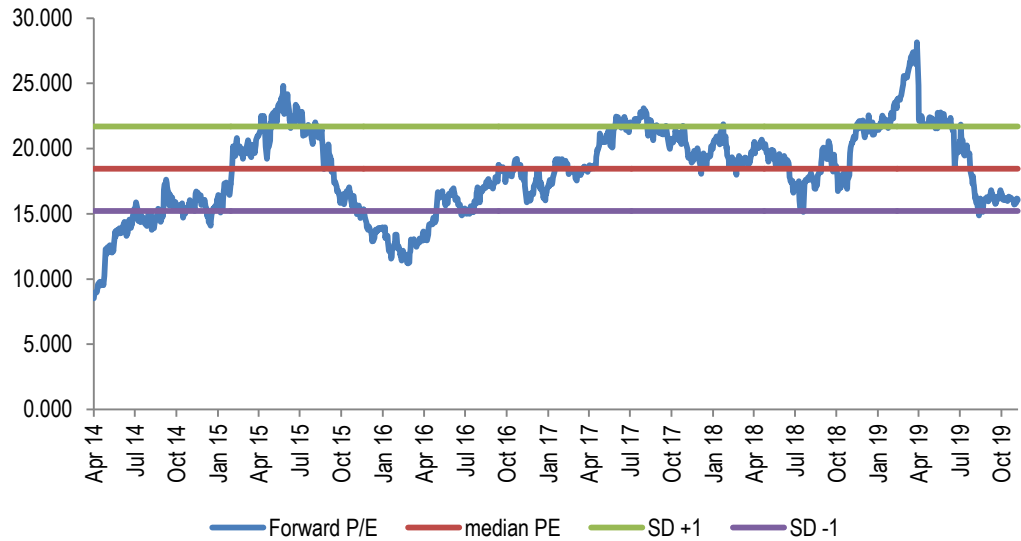
Exhibit 9: Quarterly trend in Revenue and EBITDA margin (RHS)


Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 10: Trend in Quarterly EBITDA and PAT (RHS)


Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 11: Five-year forward P/E



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 12: Estimate vs Actual vs Consensus

Rs Bn	2QFY20E	2Q FY20A	Var %	Bloomberg Consensus	Var %
Net Revenue	78.11	78.17	0.08	78.74	(0.72)
EBITDA	13.80	14.47	4.85	16.28	(11.10)
PAT	3.25	3.94	21.15	5.16	(23.69)

Source: Company, Nirmal Bang Institutional Equities Research

Financials

Exhibit 13: Income statement

Y/E Mar (Rsmn): Consolidated	FY18	FY19	FY20E	FY21E	FY22E
Net Revenue	173,780	218,370	322,342	357,609	402,544
y/y	6.54	25.66	47.61	10.94	12.57
Raw Material Expenses	81,120	109,040	177,288	185,957	201,272
RM/Sales %	46.7	49.9	55.0	52.0	50.0
Employee cost	17,130	20,950	36,019	44,195	50,784
Other expenses	40,480	50,250	45,491	49,499	56,759
EBITDA	35,050	38,130	63,545	77,958	93,729
y/y	17.42	8.79	66.65	22.68	20.23
Depreciation	6,750	9,690	22,243	23,740	25,040
EBIT	28,300	28,440	41,302	54,218	68,689
Interest Expense	7,830	9,630	18,430	13,161	10,318
Other Income	4,140	2,400	1,630	2,900	3,400
PBT (adjusted)	24,610	21,210	24,501	43,958	61,770
Income Tax Expense	3,540	1,650	3,863	6,945	9,764
Exceptional Income	-630	-4510	-5770	-2160	0
Associates inc/loss(+/-)	930	140	140	140	130
Minority Interest	80	720	3,484	6,922	10,055
Consolidated Net Profit Adj	20,060	18,980	17,294	30,231	42,081
EPS (Rs)	26.26	24.84	22.64	39.57	55.08
y/y	10.95	-5.38	-8.88	74.81	39.20

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 15: Balance sheet

Y/E Mar (Rsmn): Consol.	FY18	FY19	FY20E	FY21E	FY22E
Equity	1,020	1,020	1,020	1,020	1,020
Reserves	90,670	145,430	153,134	175,475	209,915
Net worth	91,690	146,450	154,154	176,495	210,935
Non controlling interests	190	33,580	37,064	43,986	54,042
Long Term Borrowings	58,730	263,830	249,378	239,371	225,599
Other LT liabilities	3,400	30,980	60,084	60,839	61,868
Total Non-Current Liabilities	62,320	328,390	346,526	344,196	341,508
Short Term Borrowings	6,340	24,780	24,780	14,780	14,780
Trade Payables	56,750	94,230	83,047	92,070	103,725
Other curr liab	13,330	36,630	43,600	43,600	43,600
Total Current Liabilities	76,420	155,640	151,427	150,450	162,105
Total Capital And Liabilities	230,430	630,480	652,107	671,141	714,548
Net block plus WIP	57,560	336,840	334,597	330,857	320,817
Other LT assets	12,290	16,660	16,860	17,060	17,260
Long-term investments	10,270	7,060	7,060	7,060	7,060
Total Non-Current Assets	80,120	360,560	358,517	354,977	345,137
Inventories	45,380	92,700	97,144	107,772	121,315
Trade Receivables	60,560	118,120	58,286	61,136	66,172
Cash And Cash Equivalents	28,940	28,260	107,569	115,705	150,375
Other Current Assets	15,430	30,840	30,590	31,550	31,550
Total Current Assets	150,310	269,920	293,590	316,164	369,412
Total Assets	230,430	630,480	652,107	671,141	714,548

Exhibit 14: Cash flow

Y/E Mar (Rsmn): Consolidated	FY18	FY19	FY20E	FY21E	FY22E
EBIT	28,300	28,440	41,302	54,218	68,689
Add: Depreciation and other non cash charges	6,750	8,810	22,243	23,740	25,040
Change in W/C	6,590	5,640	(51,176)	5,415	6,923
Opg cashflow after W/C change	28,460	31,610	114,721	72,543	86,806
Income tax	2,320	3,540	3,399	6,290	8,835
Cashflow from Operations (A)	26,140	28,070	111,322	66,253	77,971
Capex (inc in Tang and Intang assets)	15,680	15,530	20,000	20,000	15,000
Investments	6,560	(3,270)	0	0	0
Payment for Arysta	0	309,890	0	0	0
Other Non Current Assets	(540)	(2,470)	200	200	200
Free Cashflow	4,440	(291,610)	91,122	46,053	62,771
Cashflow from Investing (B)	(21,700)	(319,680)	(20,200)	(20,200)	(15,200)
Ch in Borrowing	4,490	219,670	(14,452)	(20,007)	(13,772)
Ch in equity	0	83,580	0	0	0
Other Long term Liability	(1,520)	0	28,640	100	100
Arysta Cash On Acquisition	0	10,480	0	0	0
Dividends	(3,690)	(4,240)	(3,820)	(5,730)	(7,640)
Interest exp	(6,470)	(10,070)	(13,985)	(13,161)	(10,318)
Other income/(expense)	2,740	(8,140)	(8,446)	880	3,530
Cashflow from Financing (C)	(4,450)	291,280	(12,063)	(37,917)	(28,101)
Ch in Cash and Cash equiv	(10)	(330)	79,059	8,136	34,670
opg cash	28,950	28,590	28,510	107,569	115,705
closing cash	28,940	28,260	107,569	115,705	150,375

Exhibit 16: Key ratios

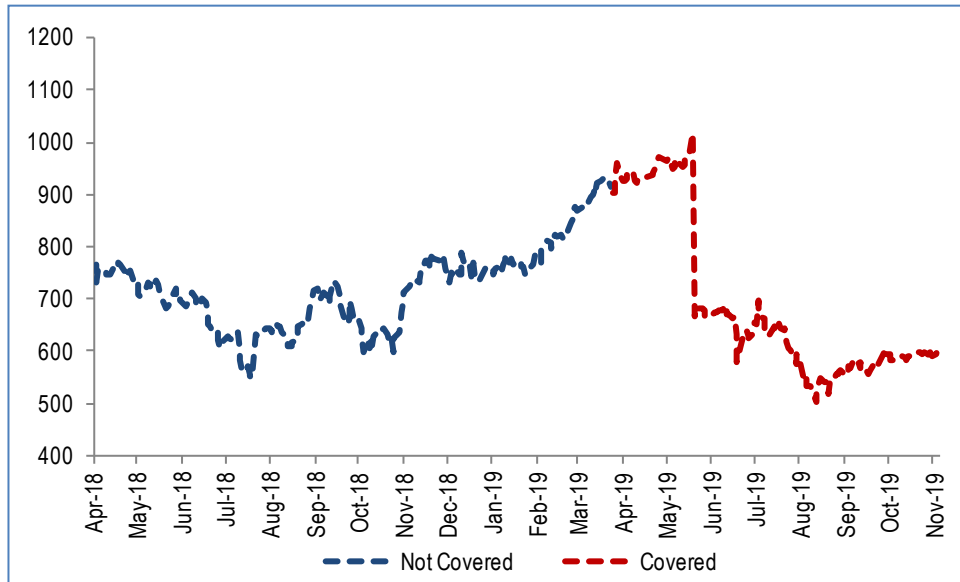
Y/E December	FY18	FY19	FY20E	FY21E	FY22E
Profitability & return ratios					
EBITDA margin (%)	20.2	17.5	19.7	21.8	23.3
EBIT margin (%)	16.3	13.0	12.8	15.2	17.1
Net profit margin (%)	11.6	6.6	3.6	7.8	10.5
RoE (%)	24.2	15.9	11.2	18.3	21.7
Pre-tax RoCE (%)	19.7	9.0	8.5	10.6	14.1
RoIC (%)	23.4	9.5	8.8	11.5	14.6
Working capital ratios					
Receivables (days)	127.2	197.4	120.0	120.0	120.0
Inventory (days)	95.3	154.9	110.0	110.0	110.0
Payables (days)	119.2	157.5	114.0	114.0	114.0
Cash conversion cycle	103.3	194.9	116.0	116.0	116.0
Leverage ratios					
Net debt (Rsmn)	36,060	260,080	166,568	138,426	89,983
Net Debt (cash)/Equity (X)	0.39	1.78	1.08	0.78	0.43
Net Debt/EBITDA	1.03	6.82	2.62	1.78	0.96
Valuation ratios					
EV/sales (x)	3.95	3.15	2.13	1.92	1.71
EV/EBITDA (x)	19.61	18.02	10.81	8.81	7.33
EV/FCF	152.36	-2.36	7.54	14.92	10.95
P/E (x)	21.29	22.50	24.70	14.13	10.15
P/BV (x)	4.66	2.92	2.77	2.42	2.02
FCF Yield (%)	1.06	-68.28	21.34	10.78	14.70
Dividend Yield (%)	0.95	0.95	0.89	1.34	1.79
Per share ratios					
EPS	26.26	0.00	0.00	0.00	0.00
Cash EPS	35.09	37.53	51.75	70.64	87.85
BVPS	120.01	191.68	201.77	231.01	276.09
DPS	5.33	5.33	5.00	7.50	10.00

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
26 th March 2019	Buy	913	1,134
20 th May 2019	Accumulate	1,019	1,129
1 August 2019	Buy	594	753
9 October 2019	Buy	588	688
8 November 2019	Buy	559	665

Rating track graph



DISCLOSURES

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BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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