

UPL

25 June 2019

Reuters: UPLL.NS; Bloomberg: UPLL IN

Storm clouds to clear over time

UPL fell 5.22% last week and is down 8.26% from a month ago, although up 46.29% YoY. The sharp fall last week has been attributed to concerns over potential demand slow down, financial leverage and potential increase in tax payout. We believe that some of these concerns are either premature or unsubstantiated at this stage and in any case largely priced in, following the above correction in the stock. The more pertinent concerns are related to accounting, earnings and cashflows from the Arysta business. We maintain our forecasts and upgrade our rating on the stock from Accumulate to Buy based on our TP of Rs1,129 that implies 20.4% upside from CMP.

Our take on the concerns that lead to the sell-off in the stock last week:

i) CPC demand slowdown – This is believed to be linked to a) the recent deaths of Chinese swine flock due to African Swine-flu that could hurt that country's imports of soya beans used as pig fodder, which in turn is expected to be negative for soya bean related CPC demand from LatAm, especially Brazil and b) the floods in the US Midwest hurting key CPC end-use crops especially corn. We believe that the concerns over swine-flu on LatAm CPC demand is a bit too early to assess, as the peak CPC sales in LatAm occurs in Oct-March period, by which time, the extent of the impact of the swine-flu is likely to be more visible (see Exhibit 1). The other concerns on China supplies and costs may linger in H1FY19, which we have considered in our forecast.

ii) UPL's leverage, this in our view is based on the FY19 Net debt/EBITDA of 6.82x. We expect this ratio to be lower at 1.59x by FY21E as we see improved earnings and cashflows over FY19-21E, based on the Arysta portfolio and synergy benefits. A 10% hit on EBITDA compared to our base case estimates implies an increase in Net debt/EBITDA to 1.96 in FY21E (see Exhibit 2). In any case the concerns over leverage on the Arysta bullet loan that is due for repayment in 5 years is a bit premature at this stage. We do have concerns on the potential increase in short term debt (Rs 24.8bn in FY19) to fund its working capital (cash collection cycle of 185 days, and 165 days, respectively, over FY20E, and FY21E vs. 194.9 days in FY19 including the two months impact of Arysta merger (and 103.3 days in FY18)

iii) The persisting US-China tariff war posing risk to supplies and the cost of CPC intermediates sourced from China. This is indeed relevant and we have assumed an increase in input costs in FY20E; this is likely to soften and get normalized by FY21E (raw material cost/sales at 55.9% in FY20E vs. 49.9% in FY19).

iv) Potential increase in UPL's tax liability. We would be a bit cautious on this issue given the political and legal implications, although the company is believed to have ruled out any potential increase in tax payout. (See Exhibit 3 for impact of increase in tax rate)

BUY
Sector: Chemical

CMP: Rs938

Target Price: Rs1,129

Upside: 20.4%

Amit Agarwal

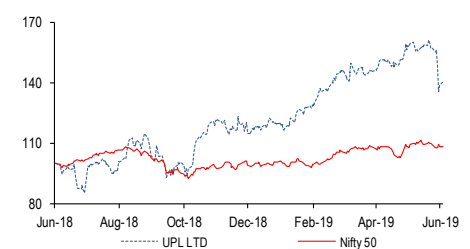
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Key Data

Current Shares O/S (mn)	509.3
Mkt Cap (Rsb/US\$bn)	477/6.9
52 Wk H / L (Rs)	1,045/537
Daily Vol. (3M NSE Avg.)	2,311,084

One Year Indexed Stock Performance

Price Performance (%)

	1-M	6-M	1-Yr
UPLL	(8.3)	27.2	46.29
Nifty Index	(1.22)	9.7	8.11

Source: Bloomberg

Overall the longer term growth prospects from the UPL pre-Arysta portfolio as well as the monetization of the Arysta assets should in our view offset the near term concerns over i) weather and other factors casting a shadow on CPC demand growth ii) higher input costs hurting margins and iii) the risk to earnings posed by the impact of legacy costs related to Arysta deal (over and above the integration costs), which the company has been unable to quantify in terms of the value or timeline.

Every US\$100m increase of Arysta related costs implies 16.6% and 11.5% downside to our FY20E and FY21E EPS, respectively. This implies a potential 8.6% cut in our FY21E based TP to Rs 1031 from our base case TP that we maintain at Rs1,129.

Exhibit 1: Cropping cycle of corn across regions

Geography	Planting	Harvesting
US	Planting begins in April and continues through June	Harvesting commences in October and finishes by the end of November
Europe	Mid-April through early June	Mid-August through late October
LatAm	Corn planting begins in central and southern Brazil between September – November, which is also the monsoon season for Brazil	February through May
India	Corn is a rain-fed kharif crop where sowing is primarily done in June-July. Other sowing months are September-October and January-February	-
China	Planting begins in mid-March through early June	Harvesting takes place August to October

Source: Nirmal Bang Institutional Equities Research

Exhibit 2: Impact analysis on Net debt/EBITDA

	EBITDA		Net debt		Net debt /EBITDA	
	(Rsmn)		(Rsmn)		(x)	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Base case	78,912	96,703	1,95,609	1,53,326	2.48	1.59
10% fall in EBITDA	71,021	87,032	2,03,500	1,70,887	2.87	1.96

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Potential impact of higher tax rate

	Base Case	Case 1	Case 2	Case 3
Tax Rate %	15.5	20	25	30
FY21E EPS Rs	81.4	77.4	72.7	68
Target Price	1129	1070	1010	950

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: Impact of Arysta Deal related costs

	EBITDA		EPS		Target Price
	(Rsmn)		(Rs)		(Rs)
	FY20E	FY21E	FY20E	FY21E	
Base case	78,912	96,703	54.44	81.41	1,129
Increase in costs by \$100mn due to Arysta Deal	71,702	89,253	45.39	72.06	1,031
% Ch.	-	-	(16.6)	(11.5)	(8.6)

Source: Company, Nirmal Bang Institutional Equities Research

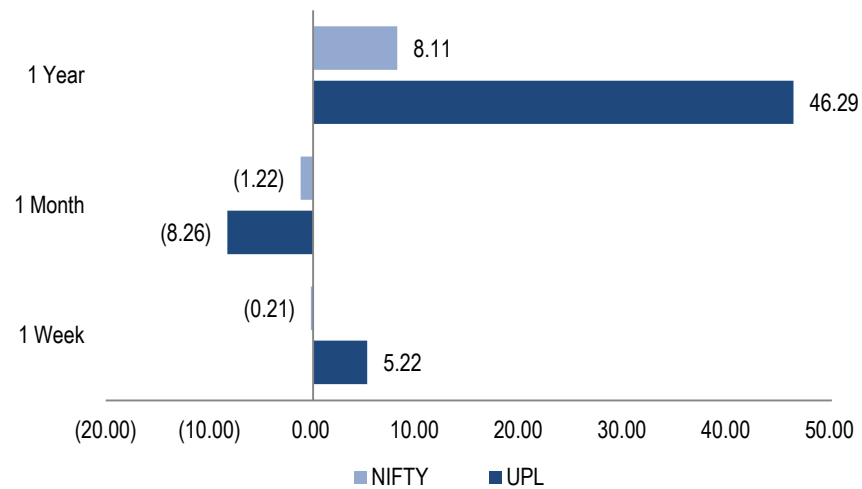
Post the recent sell off UPL trades at 11.4x PE and 6.5X EV/E and 9.9%FCF yield on FY21E. This compares with the global peer group average PE of 12.04x and EV/E 7.3x on FY21E.

Exhibit 5: Peer Group Comparison

	Code	CMP	Mkt. cap.	Revenue \$mn		Net Profit \$mn		Assets \$bn	Cons EPS est.FY21E	PE FY21E	EV/ EBITDA
			\$bn	FY19E	FY20E	FY19E	FY20E	FY18		(x)	(x)
Indian Peers											
Bayer cropScience	BYRCS IN Equity	Rs 3,360	1.7	454	559	49	70	0.4	1.80	26.72	14.81
PI Industries	PI IN Equity	Rs 1,174	2.3	496	592	75	92	0.5	0.67	25.34	17.97
International peers											
Bayer AG	BAYN GR Equity	EUR 55	57.8	52,563	54,274	7,503	8,499	144.6	8.66	7.12	6.52
Corteva Inc.	CTVA US Equity	USD 27	20.4	14,058	14,682	852	1,082	42.7	1.44	18.88	8.24
BASF SE	BAS GR Equity	EUR 62	64.9	72,873	75,565	5,269	5,756	99.1	6.47	10.87	7.05
FMC Corp.	FMC US Equity	USD 83	10.9	4,540	4,790	764	855	10.0	6.65	12.42	10.38
ADAMA*	000553 CH Equity	CNY 11	3.9	4,122	4,470	260	310	6.4	0.13	13.38	6.18
Nufarm**	NUF AU Equity	AUD 4	1.1	2,475	2,626	73	118	3.8	0.30	9.58	5.42
Global Average										12.04	7.3

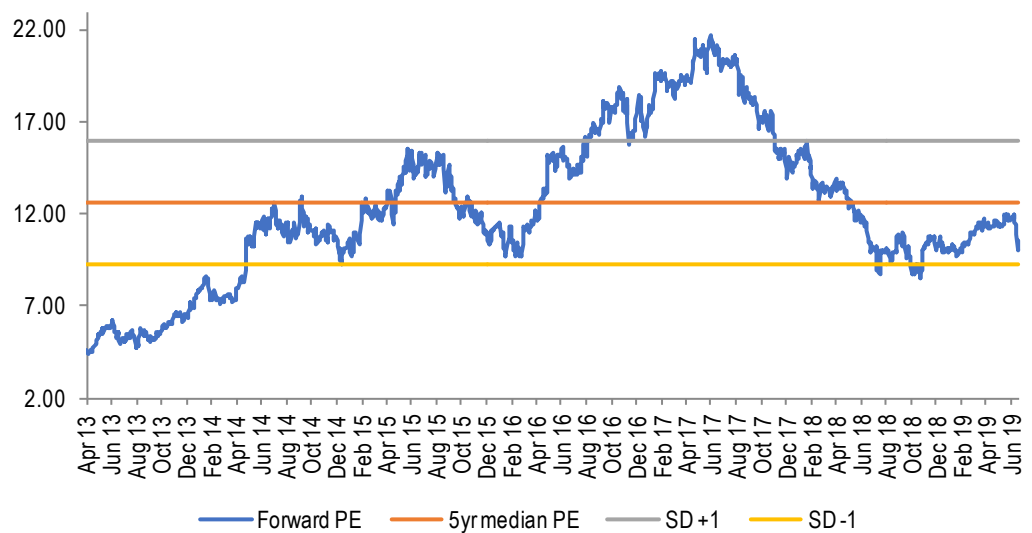
*December ending, **July ending; Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: UPL and NIFTY price performance (%)



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: UPL's five-year forward P/E (x)



Source: Company, Nirmal Bang Institutional Equities Research

Financials

Exhibit 8: Income statement

Y/E March (Rsmn)	FY17	FY18	FY19	FY20E	FY21E
Revenues	163,120	173,780	218,370	367,985	428,896
y/y (%)	16.11	6.54	25.66	68.51	16.55
Raw materials expenses	78,160	81,120	109,040	205,701	236,624
Raw material/sales(%)	47.92	46.68	49.93	55.90	55.17
Employee cost	16,270	17,130	20,950	38,361	47,366
Other expenditure	36,460	40,370	47,260	43,271	46,171
Fx (gain)/loss	2,380	110	2,990	1,739	2,032
EBITDA	29,850	35,050	38,130	78,912	96,703
EBITDA Margin (%)	18.30	20.17	17.46	21.44	22.55
Depreciation & Amortisation	6,720	6,750	9,690	22,243	23,740
EBIT	23,130	28,300	28,440	56,669	72,963
Finance cost	6,260	6,470	9,580	13,990	13,285
FX +MTM (gain)/(loss incl in Reported Finance cost	1,090	1,360	50	4,670	1,720
Other income	4,440	4,140	2,400	2,400	3,400
Exceptional Income/(Expense)	(810)	(630)	(4,510)	(3,605)	(2,235)
PBT reported	19,410	23,980	16,700	36,805	59,123
Income tax (current+deferred tax)	1,890	3,540	1,650	6,182	9,520
PAT reported	17,520	20,440	15,050	30,623	49,603
PAT excluding exceptional item	18,330	21,070	19,560	34,228	51,838
Share of profits/loss in associates	(190)	(930)	140	140	140
Minority Interest	60	80	720	6,639	10,513
Consolidated profit adjusted	18,080	20,060	18,980	27,729	41,465
y/y (%)	69.15	10.95	(5.38)	46.10	49.54
Diluted EPS	35.66	39.39	37.27	54.44	81.41

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 10: Balance sheet

Y/E March (Rs.mn)	FY17	FY18	FY19	FY20E	FY21E
Equity	1,830	1,020	1,020	1,020	1,020
Reserves	72,140	90,670	145,430	164,461	197,579
Net worth	73,970	91,690	146,450	165,481	198,599
Minority interest	330	190	33,580	40,219	50,733
Accounts payables	48,750	56,750	94,230	94,375	109,979
Other ST liabilities	14,450	13,330	36,630	43,600	43,600
Short-term loans	7,080	6,340	24,780	24,780	14,780
Total current liabilities	70,280	76,420	155,640	162,755	168,359
Long-term loans	53,500	58,730	263,830	249,663	246,181
Other LT liabilities	5,730	3,400	30,980	60,359	61,430
Total Equity & Liabilities	203,810	230,430	630,480	678,478	725,302
Net block	40,710	44,370	319,010	317,549	314,333
Other LT assets + WIP	22,340	25,480	34,490	33,908	33,584
Long-term investments	3,780	10,270	7,060	7,060	7,060
Inventories	41,560	45,380	92,700	126,022	146,882
Debtors	56,560	60,560	118,120	84,535	84,277
Cash & ST Investments	30,140	30,480	29,040	79,344	109,105
Other current assets	8,720	13,890	30,060	30,060	30,060
Total assets	203,810	230,430	630,480	678,478	725,302

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 9: Cash flow

Y/E March (Rsmn)	FY17	FY18	FY19	FY20E	FY21E
EBIT	23,130	28,300	28,440	56,669	72,963
Add: Depreciation and other non cash charges	6,720	6,750	16,330	22,243	23,740
Change in W/C	1,120	6,590	59,250	(7,379)	5,959
Opg cashflow after W/C change	28,730	28,460	(14,480)	86,291	90,744
Income tax	3,410	2,320	3,540	5,442	8,549
Cashflow from Operations (A)	25,320	26,140	(18,020)	80,849	82,194
Capex (inc in Tang and Intang assets)	11,890	15,680	16,050	20,000	20,000
Inv in equity method	(10)	2,120	220	-	-
long term inv	440	4,370	1,000	-	-
LT Loans and Adv	390	(740)	(550)	100	100
Other Non Current Assets	1,330	(160)	(910)	-	-
Payment for Arysta	-	-	309,890	-	-
total investments - Non current	14,040	21,270	325,700	20,100	20,100
Free Cashflow to firm	11,280	4,870	(343,720)	60,749	62,094
Change in Current Inv	-	70	(50)	-	-
Cashflow from Investing (B)	-	-	(325,650)	-	-
Ch in Borrowing	12,870	4,490	238,110	(14,167)	(13,482)
Ch in equity	-	-	85,300	-	-
Other long term liab.and Provisions	(980)	(1,520)	27,580	28,640	100
Arysta Cash On Acquisition	-	-	10,480	-	-
Other income/(expense)	(3,960)	(6,020)	(14,014)	(16,683)	(15,996)
Others incl. exceptionals, Fx Adjustments and Ass. Profit	(2,140)	(2,920)	(4,420)	(8,135)	(3,815)
Cashflow from Financing (C)	5,790	(5,900)	343,036	(10,344)	(33,194)
change in other LT FIN assets	40	(1,090)	1,350	100	100
Ch in Cash and Cash equiv	17,030	(10)	(430)	50,304	28,801
opg cash	11,770	28,950	28,940	28,510	78,814
cl osing cash	28,800	28,940	28,510	78,814	107,615

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 11: Key ratios

Y/E March	FY17	FY18	FY19	FY20E	FY21E
Profitability & return ratios					
EBITDA margin (%)	18.30	20.17	17.46	21.44	22.55
EBIT margin (%)	14.18	16.28	13.02	15.40	17.01
Adj Net profit margin (%)	10.59	11.64	6.63	6.56	9.15
RoE (%)	27.22	24.22	15.94	16.76	22.78
Pre-Tax RoCE (%)	20.86	19.68	9.05	11.44	13.60
RoIC (%)	21.92	23.43	9.51	10.93	13.99
Working capital ratios					
Receivables (days)	126.56	127.20	197.43	150.00	130.00
Inventory (days)	93.00	95.31	154.95	125.00	125.00
Payables (days)	109.08	119.20	157.50	90.00	90.00
Cash conversion cycle	110.47	103.32	194.88	185.00	165.00
Leverage ratios					
Net debt (Rsmn)	31,630	36,060	260,080	195,609	153,326
Net Debt (cash)/Equity (X)	0.43	0.39	1.44	0.95	0.61
FCF Yield (%)	2.21	0.95	-46.59	9.02	9.84
Valuation ratios					
EV/sales (x)	3.12	2.96	3.38	1.83	1.47
EV/EBITDA (x)	17.06	14.66	19.35	8.53	6.53
EV/FCF	45.16	105.50	-2.15	11.08	10.16
P/E (x)	26.30	23.81	25.17	17.23	11.52
P/BV (x)	6.46	5.21	3.26	2.89	2.41

Source: Company, Nirmal Bang Institutional Equities Research

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BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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