UPL Limited

Sowing seeds of sustainable growth

Agri Chem	Sharekhan code: UPL	Company Update

3R MATRIX

	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 792**	
Price Target: **Rs. 930**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

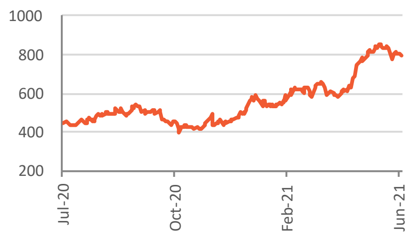
Company details

Market cap:	Rs. 60,482 cr
52-week high/low:	Rs. 865 / 399
NSE volume: (No of shares)	85.0 lakh
BSE code:	512070
NSE code:	UPL
Free float: (No of shares)	55.04 cr

Shareholding (%)

Promoters	28
FII	38
DII	16
Others	18

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-5.5	22.5	67.3	78.9
Relative to Sensex	-6.4	16.1	58.7	33.0

Sharekhan Research, Bloomberg

Summary

- UPL has carved out a strategic business unit – the Natural Plant Protect (NPP), aiming to double revenue from biosolutions to $700 million by FY24-25. The step is in line with its strategy to increase share of high growth/margin differentiated products & sustainable solutions in overall revenues to 50% by FY2026.
- Strong R&D pipeline (peak revenue potential of $4-4.5bn) and tie-ups with FMC and Meiji for launch of a new formulations makes us confident that UPL can achieve the higher end of long-term revenue growth guidance of 7-10%.
- **Q1FY22 outlook** - Strong mid double-digit growth for India, Latin America and Rest of World while the US and Europe may witness flat-to-moderate growth, with price hikes on cards across regions. Focus on deleveraging balance sheet to continue with a plan to further reduce debt by $500 million in FY2022.
- Robust earnings growth outlook (expect a CAGR of 22% in PAT over FY21-FY24E) would help UPL to generate robust cumulative FCF of Rs. 11,642 crore over FY22-FY24 and help further balance sheet deleveraging and drive re-rating Hence, we retain Buy on UPL with a revised price target (PT) of Rs. 930.

We interacted with the management of UPL Limited (UPL) to get an update on its business outlook. UPL has carved out a strategic business unit – the Natural Plant Protect (NPP) with a separate COO to focus on expansion of the biosolutions business. The product would be marketed under NPP brand (i.e. products made from natural sources like microbes, fungi, bacteria, viruses, etc, which do not have any chemical components) and the management targets to double revenues from biosolutions to $700 million by FY24-25 from $350 million (7% of overall revenues in FY2021). The setting up of the NPP as a new business unit is in line with the company's strategy to take share of high-margin differentiated products and sustainable solutions in overall revenues to 50% by FY2026. Moreover, UPL has strong R&D product pipeline (15 new products in late stage of development) with total risk adjusted peak revenue potential of $4-4.5 billion and have entered into new collaborations (with FMC in March 2021 and Meiji in May 2021), which would aid launch of several new formulations. In terms of Q1FY22 outlook, management indicated strong mid double-digit growth for India, Latin America and Rest of World (RoW) while the US and Europe may witness flat-to-moderate growth (given non season for these geographies) and hinted at price hikes to continue across regions of operations given high crop price globally. We believe that focus on high growth biosolutions, strong R&D product pipeline and recent new ties-up with MNCs would help UPL to achieve upper end of long-term revenue growth guidance (7-10% per annum) while margin to witness expansion as share of high-margin differentiated products and sustainable solutions would increase over FY2022-FY2026. We strong expect revenue/EBITDA/PAT CAGR of 10%/14%/22% over FY2021-FY2024E along with an RoE of ~20%. Moreover, concern on debt is also receding, as the company is focused on repaying debt (repaid $700 million of debt in FY2021 and target to reduce debt further by $500 million in FY2022) and aims to improve net debt/EBITDA to 2x in FY2022). Hence, we maintain our Buy rating on UPL with a revised PT of Rs. 930. At CMP, the stock trades at 12.6x FY2023E EPS and 10.8x FY23E EPS.

Our Call

Valuation - Retain Buy on UPL with a revised PT of Rs. 930: We have marginally increased our FY2022-FY2023 earnings estimate on back of higher revenue growth assumption and have also introduce our FY2024 earnings estimate in this report. A robust earnings growth outlook (expect a CAGR of 22% in PAT over FY2021-FY2024E) would help UPL to generate robust cumulative FCF of Rs. 11,642 crore over FY22E-FY24E` and help further balance sheet deleveraging and drive re-rating. Moreover, UPL's recent collaboration with MNCs for new products and target to achieve 50% of revenue from differentiated & sustainable solutions) would improve margin/earnings profile and drive sustainable growth. Valuations are attractive at 12.6x FY2023E its EPS and 10.8x FY2024E EPS. Hence, we maintain a Buy rating on UPL with a revised PT of Rs. 930.

Key Risks

Slowdown in the global agrochemical industry and delay in the flow of benefits from Arysta's integration might impact performance. Currency fluctuations might impact the company, as UPL has a significant presence in various geographies. A fresh ongoing trade war between the US and China trade post COVID-19 crisis might impact commodity prices.

Valuation Rs cr

Particulars	FY20	FY21	FY22E	FY23E	FY24E
Revenue	35,756	38,694	42,563	46,820	51,502
OPM (%)	18.9	21.6	22.8	23.6	23.9
Adjusted PAT	2,399	3,109	4,164	4,819	5,614
% YoY growth	*23.5*	*29.6*	*33.9*	*15.7*	*16.5*
Adjusted EPS (Rs)	31.4	40.6	54.4	63.0	73.4
P/E (x)	25.2	19.5	14.5	12.6	10.8
P/BV (x)	3.7	3.4	2.8	2.3	2.0
EV/EBIDTA (x)	12.2	9.5	8.1	7.0	6.1
RoCE (%)	9.3	12.0	13.7	14.5	14.7
RoNW (%)	15.5	18.2	21.1	20.4	19.8

Source: Company; Sharekhan estimates

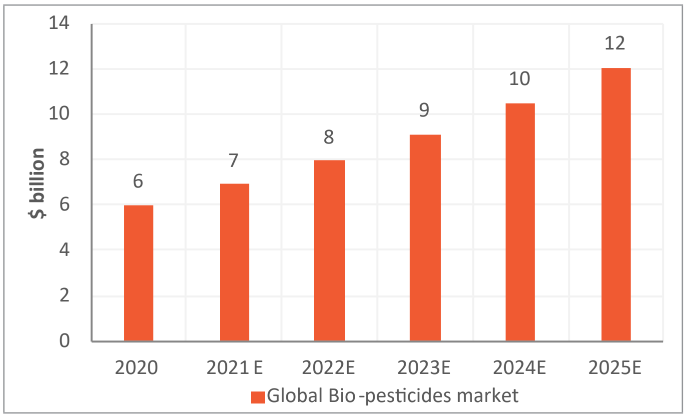
New Natural Plant Protect (NPP) unit formed – eyeing doubling of revenues from biosolutions in 3-4 years

UPL has carved out a strategic business unit – the Natural Plant Protect (NPP) with a separate COO to focus on expansion of the biosolutions business. The product would be marketed under NPP brand (i.e. products made from natural sources like microbes, fungi, bacteria, viruses, etc, which do not have any chemical components) and the management targets to double revenues from biosolutions to $700 million by FY24-25 from $350 million (7% of overall revenues in FY2021). The setting up of the NPP as a new business unit is in line with the company's strategy to take share of high-margin differentiated products and sustainable solutions in overall revenues to 50% by FY2026.

Aiming to increase revenue share of differentiated & sustainable solutions to 50% in 3-5 years

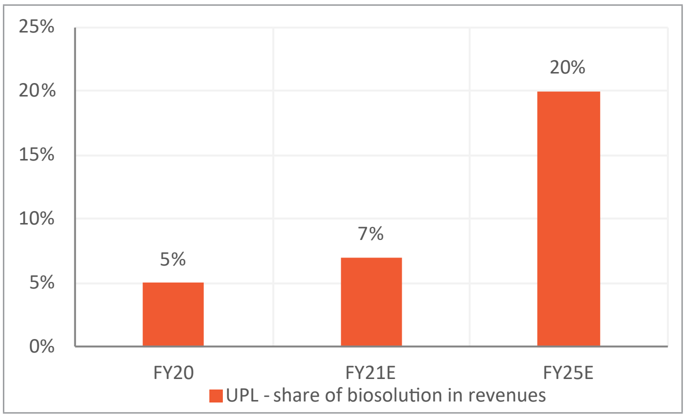
The management expects differentiated & sustainable solutions (including biosolutions) to grow at a much higher rate than traditional agrochemical products and would be the key driver behind industry-leading revenue growth for UPL in the next couple of years. The company targets to increase the share of differentiated & sustainable solutions to 50% over 3-5 years from 29% in FY2021. The key driver of the same would be rising demand for biosolutions, which is at a nascent stage currently but is expected to gain acceptance due to environmental benefits and as it offers improvement in crop yields. The global biosolutions market size is estimated at ~$6 billion and is expected to grow at 15% annually (versus just a 2-3% growth for the global agrochemicals market). Thus, UPL is focused on increasing the share of biosolutions in overall revenue to 15%-20% in the coming years, as compared to 7-8% currently. The company is aggressively pushing for products with crop chemicals and biosolutions, as the same would improve farm yield and productivity.

Global bio-pesticides market expected to grow 15% annually



Source: Industry, Sharekhan Research

UPL focused to increase share of Biosolution in revenues

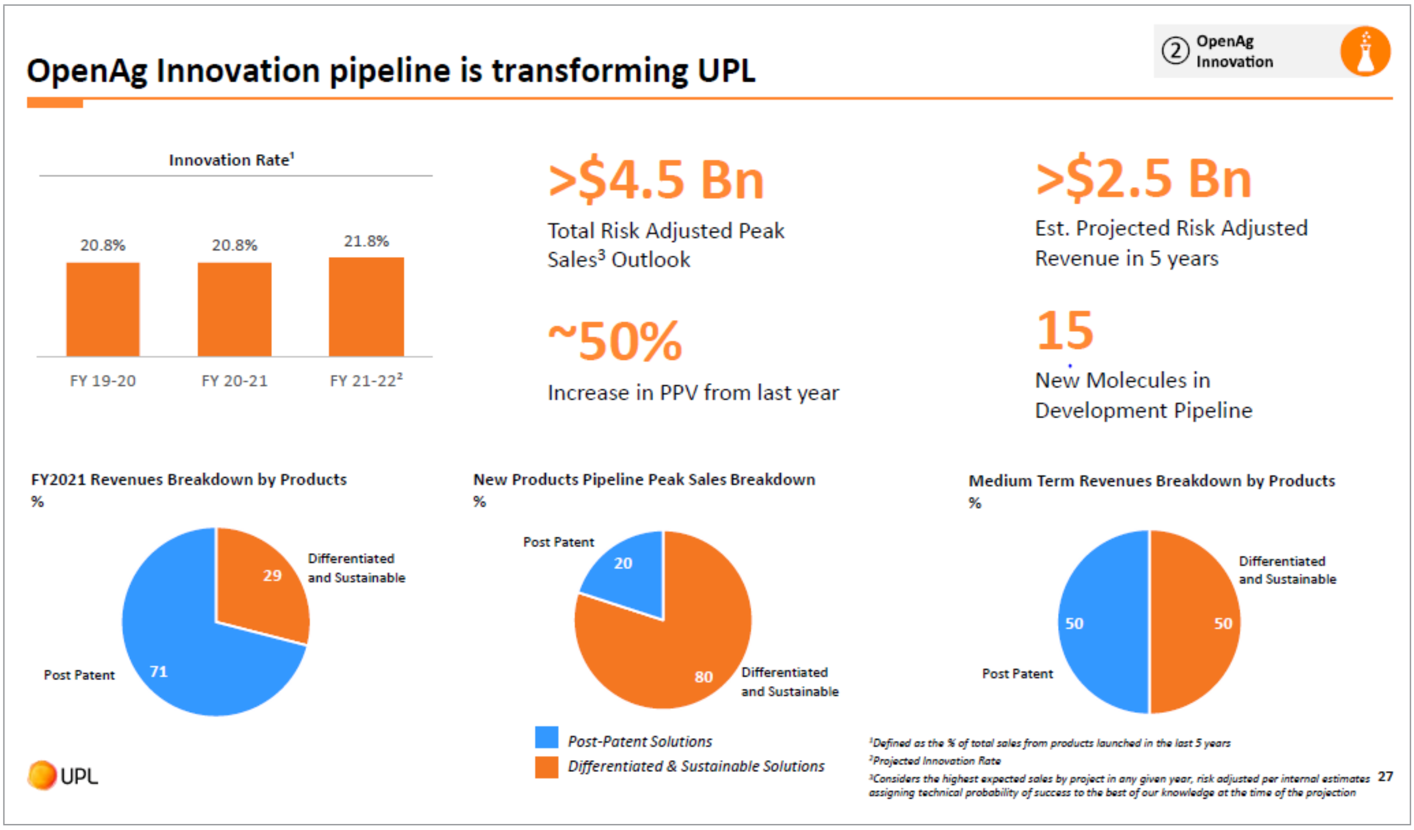


Source: Industry, Sharekhan Research

Strong R&D pipeline with peak revenue potential of $4-4.5 billion

UPL has strong R&D pipeline (15 new products in late stages of development) with total risk adjusted peak revenue potential of $4-4.5 billion. Additionally, the management expects that 80% of revenues from product pipeline would be derived from high-margin differentiated products and sustainable solutions and 20% from post patent products. This bodes well for improvement in gross/EBITDA margin and management expect margin to gradually increase to 25% in the next 3-5 years as compared to 21.6% in FY2021. Moreover, the company has recently entered new collaborations with FMC in March 2021 (total addressable market of $5 billion) and Meiji in May 2021 (total addressable market of $2.5 billion), which would aid the launch of several new formulations. This bodes well for sustained long-term revenue growth and margin expansion.

OpenAg Innovation pipeline



Source: Company

OpenAg Collaboration (FMC)

Enhanced Tool Kit of Solutions

Partner	FMC
Date	March 2021
AI/Service	Chlorantraniliprole
TAM	$5.0 Bn

Description

- Addition of core active ingredient to develop **new family of value-added solutions to growers, with 17 formulations in the pipeline**
- **Early access** to commercialize Chlorantraniliprole (CTPR) insecticide in key markets **prior to patent expiration**
- UPL to toll manufacture/ supply Chlorantraniliprole to FMC in India

Source: Company

OpenAg Collaboration (Meiji)

Enhanced Tool Kit of Solutions

Partner	meiji
Date	2018, 2020 and May 2021
AI/Service	Flupyrimin, **IP Protected**
TAM	~$2.5 Bn

Description

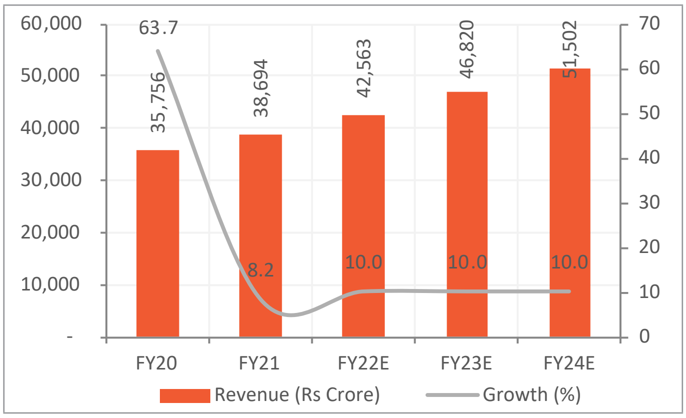
- Flupyrimin, discovered by Meiji, is a **patented insecticide** with a **new MOA subgroup**
- Latest license agreement provides UPL exclusive access to Flupyrimin formulations for foliar application on **Rice in several countries**[1] **in Southeast Asia**
- Prior agreements provide exclusive access for **Rice in India** plus **Crop Establishment applications** globally with exclusions[2]
- With these agreements, UPL will now have a **complete portfolio for Rice** in Asia and India, while also strengthening our Crop Establishment offering

[1] *Countries include Indonesia, Philippines, Malaysia, Thailand, Vietnam, Myanmar, Cambodia, Pakistan, and Bangladesh*
[2] *Excluding territories: Japan, South Korea and Taiwan; non-exclusive arrangement in China*

Source: Company

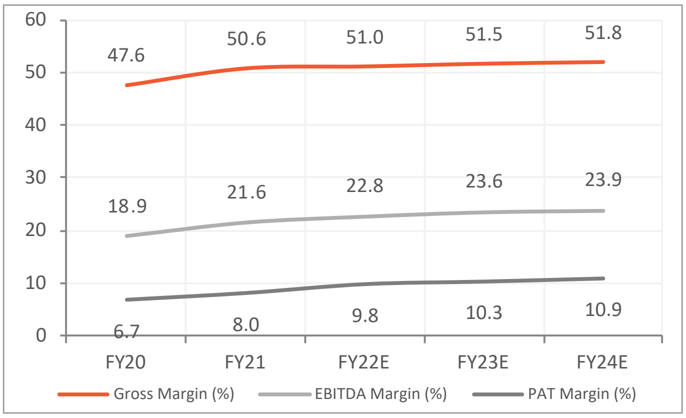
Financials in charts

Revenue to report a 10% CAGR over FY2021-FY2024E



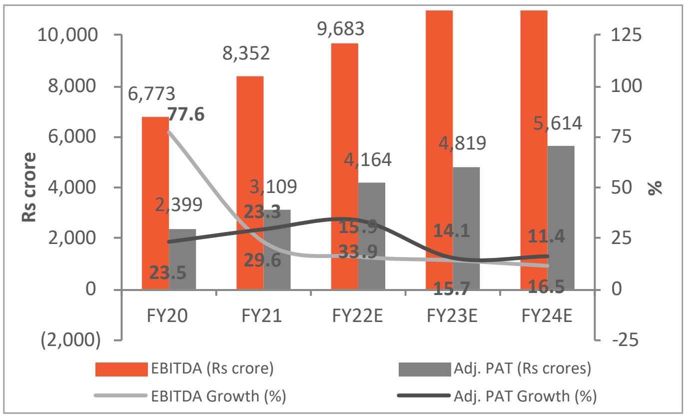
Source: Company, Sharekhan Research

Gross and EBITDA margin to improve on better product mix



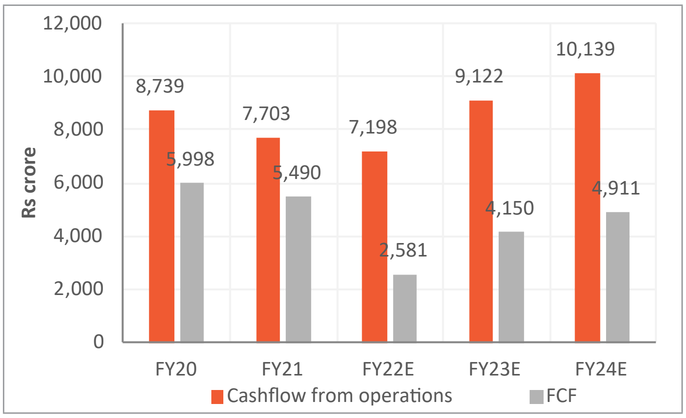
Source: Company, Sharekhan Research

EBITDA/PAT to post a 14%/22% CAGR over FY21-FY2024E



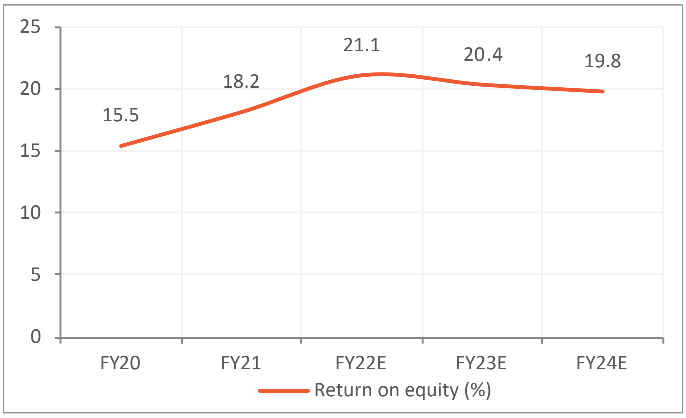
Source: Company, Sharekhan Research

Robust FCF to help deleverage the balance sheet



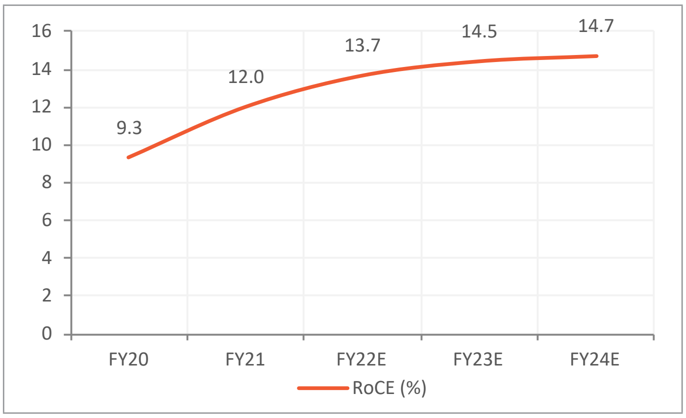
Source: Company, Sharekhan Research

RoE trend



Source: Company, Sharekhan Research

RoCE trend



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector View - Rising food demand provides ample growth opportunities for agri-input players

The outlook for the Indian agrochemical industry is encouraging, primarily driven by rising foodgrain production and domestic demand, favourable regulatory reforms for farmers and the vast opportunity from products going off-patent. The government's focus is to double farmers' income (through higher crop MSPs). An above-normal monsoon and higher reservoir levels would augment demand for agri-input in India. We also expect exports from India to grow at a strong pace as India is being looked as the preferred supplier for agri-input products given supply disruption from China. Thus, we expect India's agrochemical industry to witness 7-8% growth annually on a sustained basis over the next few years. Moreover, international markets such as Latin America would continue to grow at a robust pace supported by higher demand for crop protection and farm solutions mitigating slower growth in the US and Europe.

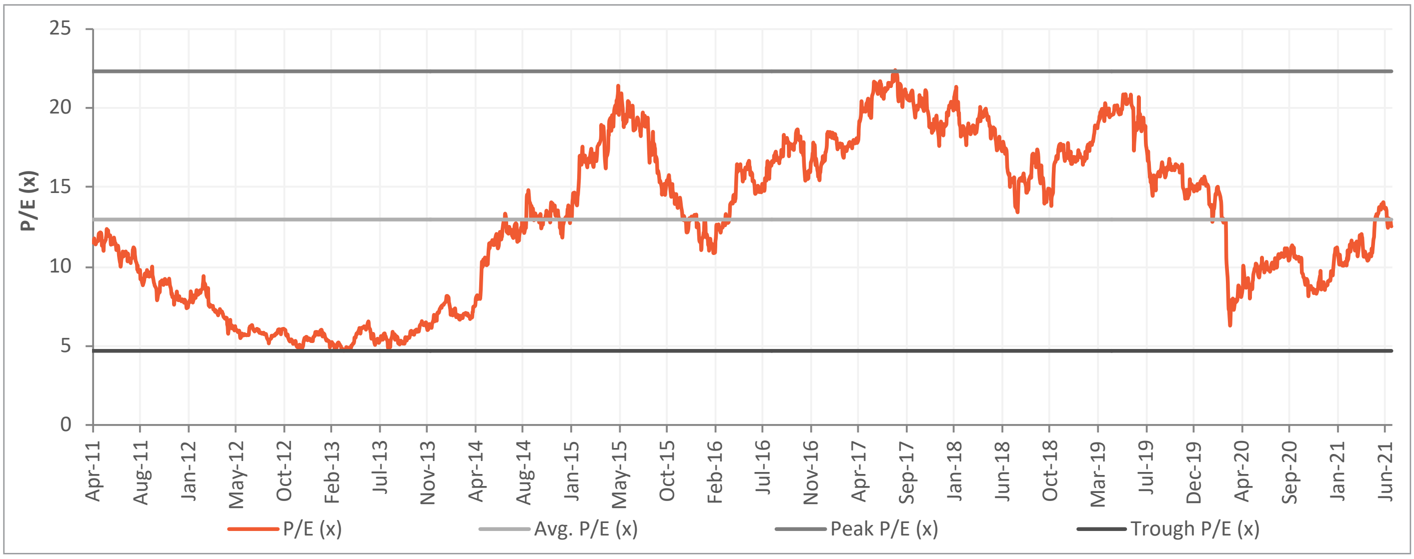
■ Company outlook - Strong growth outlook across regions; focus on balance sheet deleveraging:

The management anticipates good agronomic conditions in most key markets, which is expected to drive robust demand going forward. Revenue synergies via cross-selling of products and price hikes in a few markets are expected to drive revenue growth, while cost synergies and cost efficiencies would enhance margins. The company is expected to generate healthy cash flows, which would help reduce debt further (from net debt of Rs. 18,992 crore with net debt/ EBITDA ratio of 2.2x in FY2021).

■ Valuation - Maintain Buy on UPL with a revised PT of Rs. 930

We have marginally increased our FY2022-FY2023 earnings estimate on back of higher revenue growth assumption and have also introduce our FY2024 earnings estimate in this report. A robust earnings growth outlook (expect a CAGR of 22% in PAT over FY2021-FY2024E) would help UPL to generate robust cumulative FCF of Rs. 11,642 crore over FY22E-FY24E` and help further balance sheet deleveraging and drive re-rating. Moreover, UPL's recent collaboration with MNCs for new products and target to achieve 50% of revenue from differentiated & sustainable solutions) would improve margin/earnings profile and drive sustainable growth. Valuations are attractive at 12.6x FY2023E its EPS and 10.8x FY2024E EPS. Hence, we maintain a Buy rating on UPL with a revised PT of Rs. 930.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

UPL is a global leader in agricultural solutions and has a healthy mix of high-value crops and high-growth geographies. The company is well positioned to achieve sustainable growth as it is present across the agricultural input segment, ranging from seeds to crop-protection products and post-harvest activities. Arysta's acquisition strengthens UPL's global positioning and helps it to emerge as an end-to-end solutions provider in the global agri input space. The company has manufacturing facilities across 48 locations (earlier 34) and is present across more than 138 countries. The company's thrust on research and innovation has helped it garner 1,023 patent and over 12,400 registrations. The acquisition has strengthened UPL's long-term growth prospects as product registration has doubled from its earlier levels of 6,500, considering the fact that it takes between 2-5 years for getting products registered. The company has a workforce representation of over 75 countries with total employee strength of over 10,300.

Investment theme

UPL has moved up in global ranking to the fifth position post Arysta's acquisition (earlier seventh). The company has successfully integrated 25+ companies post the acquisition in the past 20 years. The company is among the top five post patent agrochemical manufacturers in the world and is the largest producer of agrochemicals in India. UPL has mostly outperformed the industry's growth rate. The acquisition (UPL + Arysta) brings in a prudent mix of own manufacturing and outsourcing, which is expected to lead to improved margin profile coupled with capital efficiencies resulting in better return ratios. New product launches in key geographies and flowing of synergy benefits of Arysta's acquisition are likely to fuel growth at a faster pace.

Key Risks

- Slowdown in the global agrochemical industry and a delay in flow of benefits from Arysta's integration might impact performance.
- Currency fluctuation might have an impact, as UPL has a significant presence in various geographies.
- Fresh ongoing US-China trade war post the COVID-19 crisis might have an impact on commodity prices.

Additional Data

Key management personnel

Rajnikant Devidas Shroff	Chairman and Managing Director
Sandra Rajnikant Shroff	Vice Chairman
Jaidev Rajnikant Shroff	Global CEO of the Group
Vikram Rajnikant Shroff	Executive Director
Arun Chandrasen Ashar	Executive Director Finance
Diego Casanello	Global COO - Crop Protection
Rajendra Darak	Group CFO
Anand Vora	Global CFO

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corp.of India	8.2
2	Government Pension Fund	3.7
3	Norges Bank	3.7
4	Vanguard Group.	3.2
5	Massachusetts Financial Services	3.0
6	BlackRock Inc.	2.2
7	ICICI Prudential Life Insurance Co. Ltd	1.6
8	Lazard Ltd	1.5
9	SBI Funds Management Pvt. Ltd	1.2
10	Skagen AS	1.1

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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