



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

Reco: Buy	↔
CMP: Rs. 626	
Price Target: Rs. 720	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

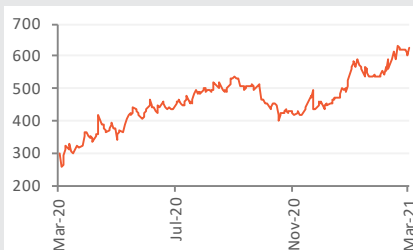
Company details

Market cap:	Rs. 47,803 cr
52-week high/low:	Rs. 639/240
NSE volume: (No of shares)	93.0 lakh
BSE code:	512070
NSE code:	UPL
Free float: (No of shares)	55.13 cr

Shareholding (%)

Promoters	28
FII	35
DII	16
Others	20

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	15.9	43.2	17.7	109.3
Relative to Sensex	15.7	33.8	-13.4	42.7

Sharekhan Research, Bloomberg

Agri Chem	Sharekhan code: UPL	Company Update
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Summary

- Management expects sustainable 8%-10% revenue growth p.a., given its focus to expand revenue share of differentiated & sustainable solutions (biosolutions – growing at 15%) and production innovation in off-patented business.
- UPL's recent strategic collaboration with FMC for Rynaxypyr has the potential to add \$200 million (4%-5% of FY2021E revenue); management targets to add more products for distribution to expand its product portfolio and drive revenue growth.
- On track to achieve net debt/EBITDA to 2x by March 21 (further reduced debt by \$300 million in February 2020); management has also addressed investor concern on corporate governance (helps improve investor sentiments).
- UPL's valuation of 11.4x its FY2023E EPS is attractive, given strong earnings outlook, improving margin/RoE profile at 22%/18% in FY23E, and focus to deleverage its balance sheet. Hence, we retain Buy on UPL with a revised price target (PT) of Rs. 720.

We interacted with the management of UPL Limited (UPL) to get an update on its business outlook. UPL's management is quite optimistic of sustained 8%-10% annual revenue growth over the next couple of years as compared to 2%-3% growth for the global agrochemical industry. Growth would be driven by the company's focus to expand revenue share of high-margin differentiated & sustainable solutions (including bio-solutions, which is growing at 15% annually) for farmers and new product launches in post patent products. Management has guided to take the share of differentiated & sustainable solutions to 50% over the next 3-5 years from 30% currently, and the same would improve margin to 23%-24% from 19% in FY2020. Furthermore, the recent strategic collaboration with FMC Corporation for Rynaxypyr has the potential to add \$200 million (4%-5% of FY2021E revenue) and UPL could further add more products for distribution, which would expand its product portfolio and drive revenue growth. Management does not expect any material impact on revenue (less than 1% impact) from the recent fire at Jhagadia plant as majority of the products were dispatched to the overseas market and demand remains low in the domestic market due to seasonality factor. In terms of Q4FY2021, management expects growth across geographies (with strong growth from North America and Europe, given a seasonally strong quarter) and margin expansion on a sequential basis. We have increased our FY2022-FY2023 earnings estimate to factor in higher margin assumption and expect EBITDA/PAT CAGR of 13%/16% over FY2021E-FY2023E along with RoE of ~18%. Additionally, management has adequately addressed investor concern on corporate government and focuses on improving the balance sheet (has reduced debt by \$700 million with repayment on loan of \$400 million in December 2020 and \$300 million in February 2021) and is on track to achieve net debt/EBITDA target of 2x by March 2021. We maintain our Buy rating on UPL with a revised PT of Rs. 720.

Our Call

Valuation - Retain Buy on UPL with a revised PT of Rs. 720: We expect UPL's earnings profile to improve given our expectation of 8%-9% annual revenue growth and ~183 bps EBITDA margin improvement over FY2021E-FY2023E, led by launch of 4-5 new products every year, synergies from Arysta's acquisition, efficient raw-material sourcing, and potential rise in the share of high-margin, bio-pesticides products. This would mean a 16% PAT CAGR over FY2021E-FY2023E and RoE of 18% in FY2023E. Moreover, management has adequately addressed investor concerns on corporate government and is very focused to improve its balance sheet (on target to achieve net debt/EBITDA of 2x by March 2021), which would improve overall investor sentiments for UPL. Valuation of 11.4x FY2023E its EPS is attractive, given discount of 13% to historical average one-year forward PE of 13x. Hence, we maintain our Buy rating on UPL with a revised PT of Rs. 720 (increase in PT reflects upwards revision in FY23 earnings estimate).

Key risk

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. Fresh ongoing US-China trade war post COVID-19 crisis might have an impact on commodity prices.

Valuation

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Revenue	21,837	35,756	37,901	41,123	44,618
OPM (%)	17.5	18.9	21.0	22.1	22.9
Adjusted PAT	1,942	2,399	3,153	3,705	4,206
% YoY growth	(6.9)	23.5	31.4	17.5	13.5
Adjusted EPS (Rs.)	25.4	31.4	41.2	48.4	55.0
P/E (x)	24.6	20.0	15.2	12.9	11.4
P/BV (x)	3.3	2.9	2.6	2.2	1.9
EV/EBIDTA (x)	19.4	10.3	8.6	7.4	6.4
RoCE (%)	9.7	9.3	10.9	12.6	13.5
RoNW (%)	16.3	15.5	18.0	18.4	17.9

Arysta's financials included in FY2019 numbers since February 1, 2019; hence, they are not comparable
Source: Company Data; Sharekhan estimates

We interacted with the management of UPL. Following are the key takeaways.

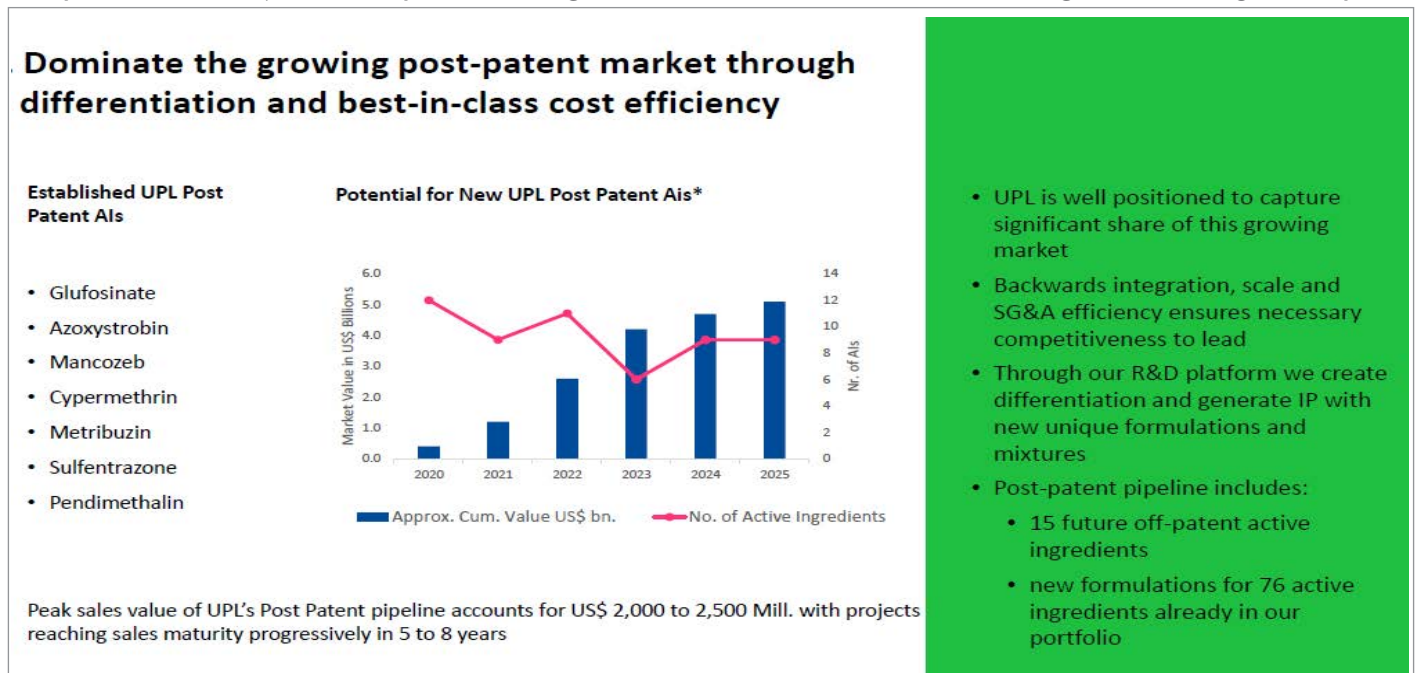
Focus on differential solutions and new launches in off-patent products – to drive sustainable 8%-10% annual revenue growth

Management commentary was positive with respect to sustainable 8%-10% annual growth in revenue (much higher than global industry growth of 2%-3%), given: 1) product innovation to gain market share in off-patent products and 2) UPL's focus to increase the share of differentiated & sustainable solutions in revenue to 50% from 30% currently. Biosolution (growing at 15% annually) to play a key driver as its revenue share is expected to reach 15%-20% by FY2025E from our estimate of 8% in FY2021E.

Focus on off-patent products and product innovation to drive growth for post-patent business

UPL generates 70% of its revenue from the post patent product business and 30% revenue from differentiated & sustainable solutions (including bio-solutions). UPL is focused on research and development (R&D) to create innovative combination products (off-patent products) for various crops. The company's global distribution reach and first-mover advantage help to push off patent products in global markets. Agrochemical products worth ~\$4 billion are going off-patent over 2017-2022, which would drive sustainable revenue growth for UPL's off-patent business as the company plans to introduce 4-5 new products annually.

Post patent AIs include (15 future off patent active ingredients and new formulations of 76 active ingredients already in UPL's portfolio

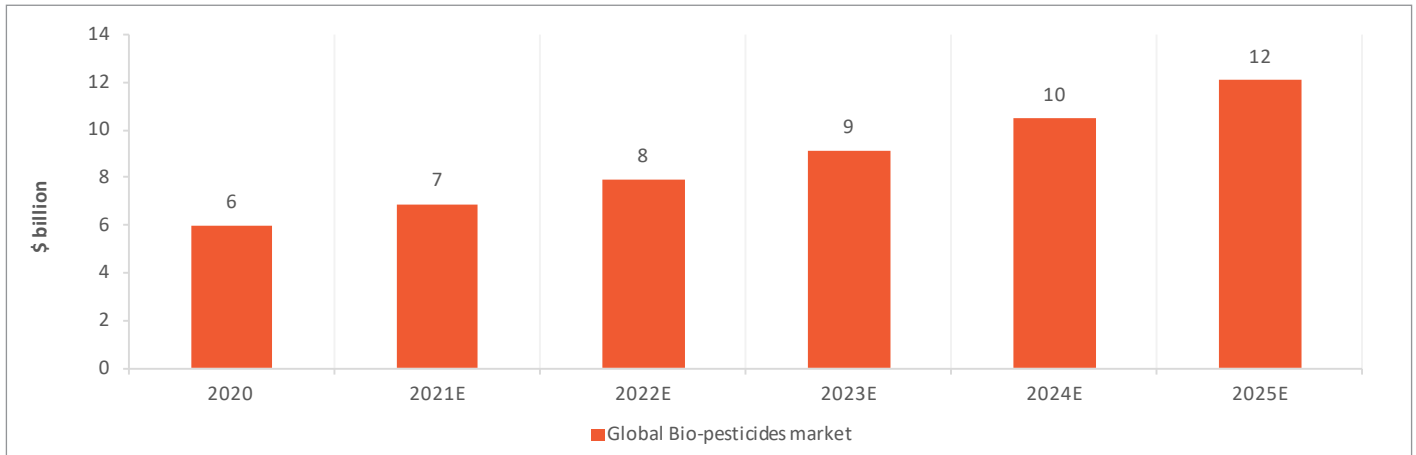


Source: Company

Target to increase revenue share of differentiated & sustainable solution to 50% over next 3-5 years - Biosolution is the key driver as it growing by 15% annually: Management expects differentiated & sustainable solutions (including BioSolutions) to grow at a much higher rate than traditional agrochemical products and would be the key driver for the industry leading revenue growth for UPL over the next couple of years. The company targets to increase the share of differentiated & sustainable solutions to 50% over 3-5 years from 30% currently. 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 BioSolution global market size is estimated at ~\$6 billion and is expected to grow at 15% annually (versus only 2%-3% growth for global agrochemicals). The acquisition of Arysta has provided UPL access to BioSolutions space; and the company intends to build on products such as ProNutiva crop packages for accelerated growth. Thus, UPL is focused on increasing the share of BioSolutions in overall revenue to

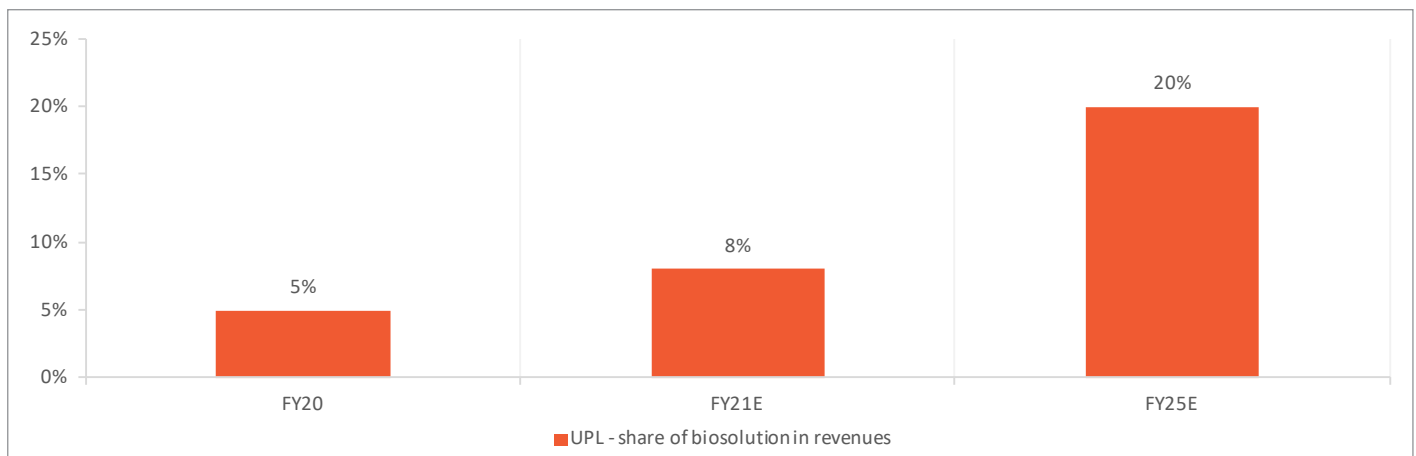
15%-20% in the coming years, as compared to only 8% currently. The company is aggressively pushing for products with crop chemicals and BioSolutions, as the same would improve farm yield and productivity.

Global bio-pesticides market expected to grow 15% annually



Source: Industry, Sharekhan Research

UPL focused to increase share of Biosolution in revenues



Source: Company, Sharekhan Research
Note: UPL does not provide share of BioSolutions

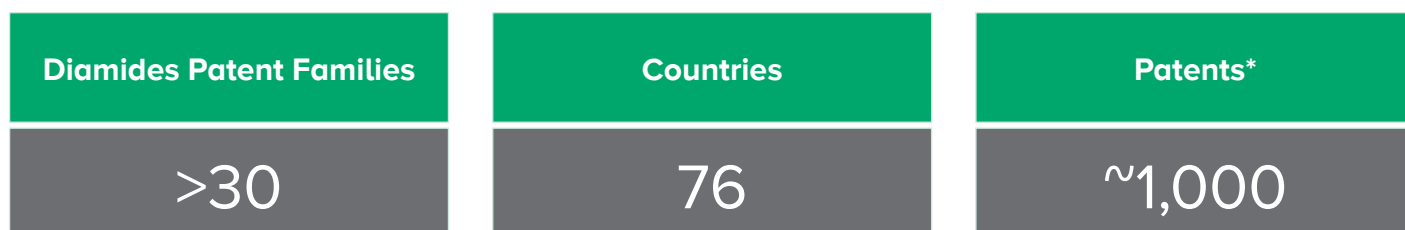
Strategic alliance with FMC for Rynaxypyr (insecticide – global market size of ~\$2 billion) - Peak revenue potential of \$200 million for UPL

UPL has recently announced a long-term strategic collaboration with FMC Corporation (a leading global agricultural sciences company) to toll manufacture Rynaxypyr active (leading insecticide product of FMC) in India and supply Rynaxypyr to FMC. Moreover, FMC will supply the active ingredient (AI) to UPL depending on the market. The agreement provides UPL access in key markets prior to patent expiration, to commercialise Rynaxypyr active. The collaboration clearly demonstrates UPL’s commitment to OpenAg to create an agriculture network for sustainable growth. We expect UPL to enter into agreements for more products and strengthen its product portfolio.

Management has said that the global market size for Rynaxypyr active is estimated at \$2 billion and AI is expected to grow at 10-12% annually over the next couple of years. The product patent for Rynaxypyr active will expire globally by over August 2022 – August 2023 and the process patent by December 2025 - April 2026. Majority of Rynaxypyr production is used for rice (30% usage), fruits and vegetables (20-22%), and soybean (24%). The company expects peak revenue potential of \$200 million from Rynaxypyr active and will start the distribution on Rynaxypyr in 2021.

Types of patents for Rynaxypyr

Patent Type	Summary
Composition of Matter Patents (AI and certain intermediates)	Protects proprietary molecular structure of active ingredient (AI) and molecular structure of certain intermediates.
Process Patents (AI and key intermediates)	Protects the manufacturing processes for the AI and the key intermediates used to make the AI.
Formulation Patents	Protects product formulations that use the AI.
Use Patents	Protects how a product is used.
Application Patents	Protects the methods or approaches to apply products.

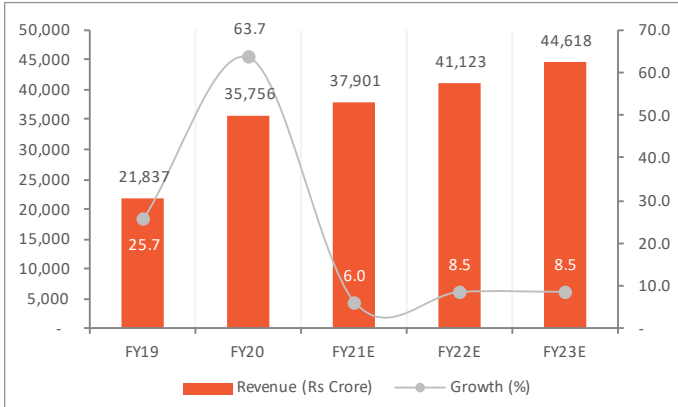


Source: FMC

* Granted and pending

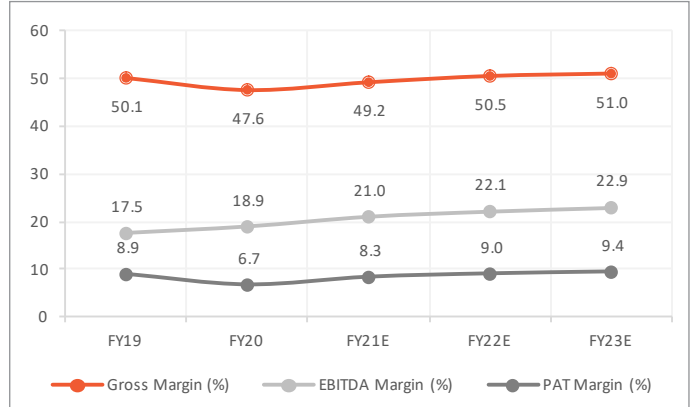
Financials in charts

Revenue to report 9% CAGR over FY202/FY2023E



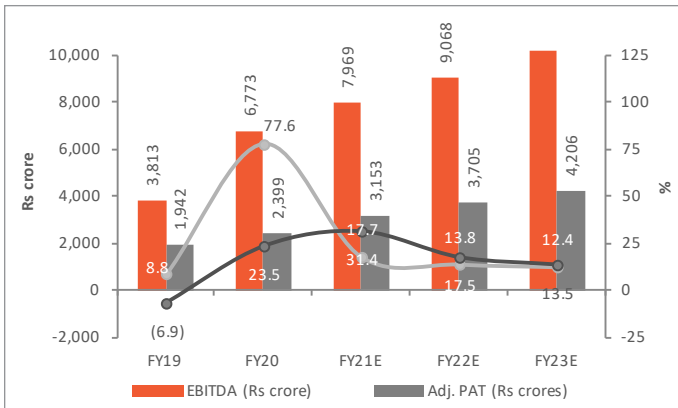
Source: Company, Sharekhan Research

Gross and EBITDA margin to improve given large scale



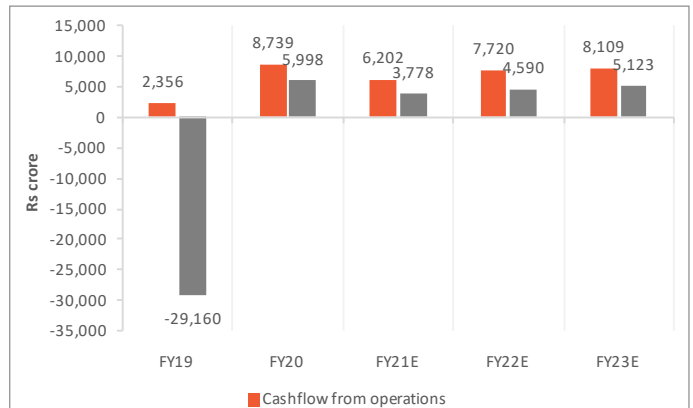
Source: Company, Sharekhan Research

EBITDA/PAT to post 13%/16% CAGR over FY2021E-FY2023E



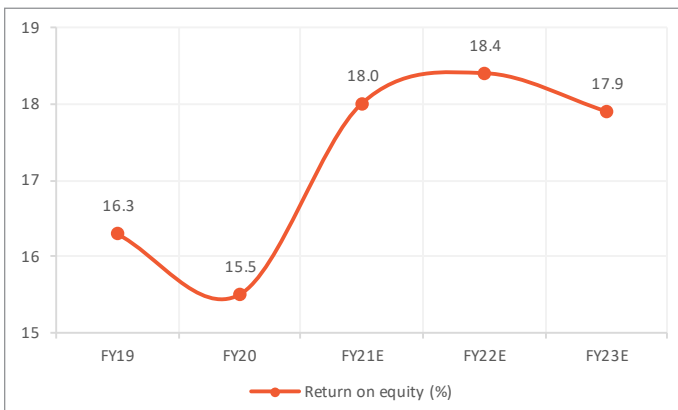
Source: Company, Sharekhan Research

Robust FCF to help deleverage balance sheet



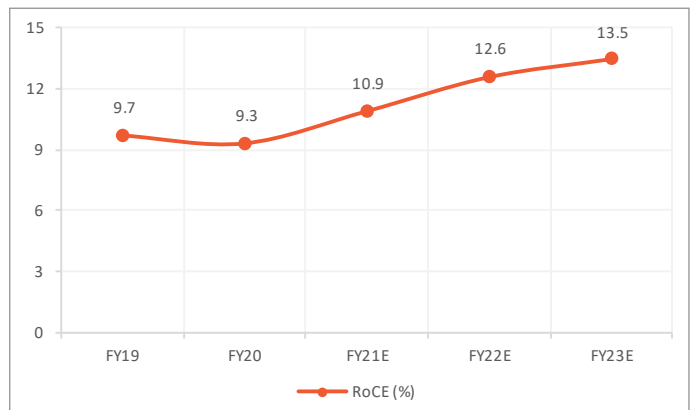
Source: Company, Sharekhan Research

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 (government passed key agri-sector reforms namely Farmers Produce Trade and Commerce Bill 2020 and Farmers (empowerment and protection) Agreement of Price Assurance and Farm Services Bill) and the vast opportunity from products going off-patent. The government's focus is to double farmers' income (higher MSPs for crops). A near-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 (grew by 7.6% in CY2019) 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.

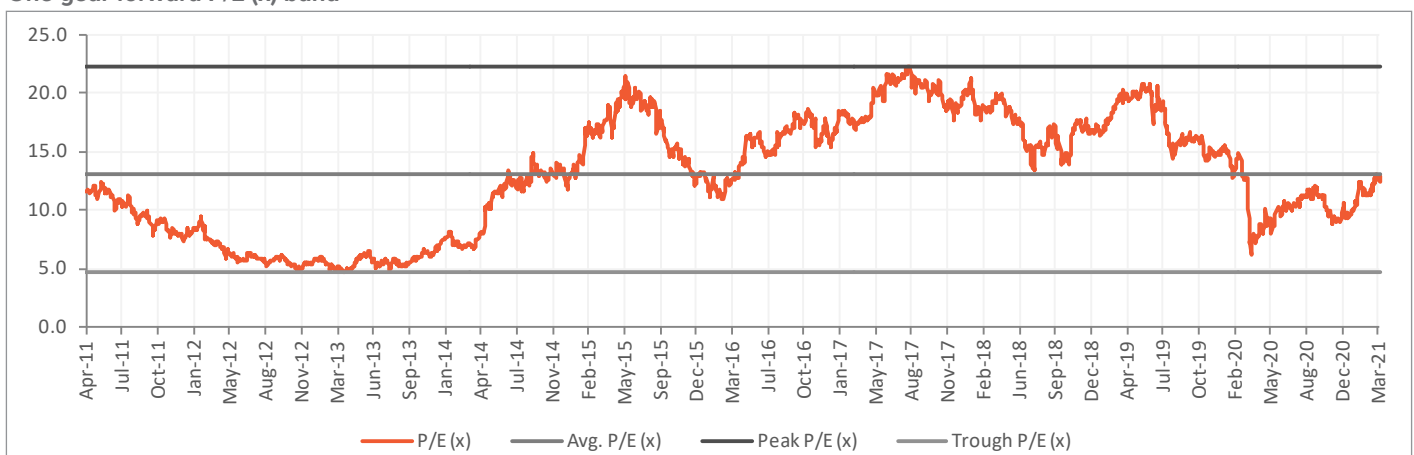
■ Company Outlook – Strong growth outlook across regions; Focus on balance sheet deleveraging

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 and repay debt (Rs. 23,841 crore of net debt with net debt/EBITDA of 3.2x in FY2020).

■ Valuation – Maintain Buy on UPL with a revised PT of Rs. 720

We expect UPL's earnings profile to improve given our expectation of 8%-9% annual revenue growth and ~183 bps EBITDA margin improvement over FY2021E-FY2023E, led by launch of 4-5 new products every year, synergies from Arysta's acquisition, efficient raw-material sourcing, and potential rise in the share of high-margin, bio-pesticides products. This would mean a 16% PAT CAGR over FY2021E-FY2023E and RoE of 18% in FY2023E. Moreover, management has adequately addressed investor concerns on corporate government and is very focused to improve its balance sheet (on target to achieve net debt/EBITDA of 2x by March 2021), which would improve overall investor sentiments for UPL. Valuation of 11.4x FY2023E its EPS is attractive, given discount of 13% to historical average one-year forward PE of 13x. Hence, we maintain our Buy rating on UPL with a revised PT of Rs. 720 (increase in PT reflects upwards revision in FY23 earnings estimate).

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 - GLOBAL	3.7
3	Norges Bank	3.7
4	Vanguard Group Inc/The	2.6
5	BlackRock Inc	2.2
6	ICICI Prudential Life Insurance	1.6
7	Skagen AS	1.5
8	Sun Life Financial Inc	1.4
9	Lazard Ltd	1.4
10	Invesco Ltd	1.2

Source: Bloomberg

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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 deteriorating 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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