Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

UPL Ltd

Mixed Q1; guidance cut given challenging environment

Agri Chem	Sharekhan code: UPL
Reco/View: Buy ↔	CMP: Rs. 624 / Price Target: Rs. 745 ↓

↑ Upgrade ↔ Maintain ↓ Downgrade

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		↔	

ESG Disclosure Score NEW

ESG RISK RATING 22.28

Updated Jun 08, 2023

Medium Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

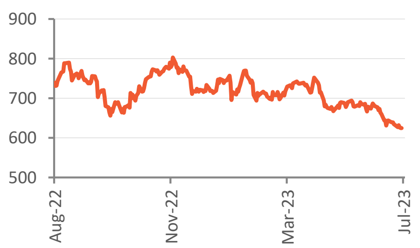
Company details

Market cap:	Rs. 47,703 cr
52-week high/low:	Rs. 807 / 621
NSE volume: (No of shares)	21.4 lakh
BSE code:	512070
NSE code:	UPL
Free float: (No of shares)	50.79 cr

Shareholding (%)

Promoters	32
FII	38
DII	15
Others	14

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-7.9	-13.0	-15.7	-18.9
Relative to Sensex	-14.5	-25.8	-27.1	-33.3

Sharekhan Research, Bloomberg

Summary

- Q1 consolidated revenue/EBITDA declined by 17%/32% y-o-y to Rs. 8,963 crore/Rs. 1592 crore due to an industry-wide slowdown given high channel inventories and pricing pressure. However, adjusted EBITDA was 4% above our estimate, led by an 186 bps beat in EBITA margin at 17.8% (down 389 bps y-o-y) given strong seeds margin and better product mix.
- CPC business' performance were hit by a steep 17%/10% y-o-y decline in volume/pricing, which led to steep revenues de-growth across geographies. UPL SAS was impacted by delayed sowing/price pressures, while seeds business posted strong performance with 26%/54% y-o-y jump in revenue/EBITDA.
- Management cut FY24 revenue/EBITDA growth guidance to 1-5%/3-7% from earlier guidance of 6-10%/8-12%. The new guidance would be dependent upon a recovery in H2FY24. We thus cut our FY24/FY25 earnings estimate by 6%/7%.
- Although near term challenges persists for agro-chem players but the steep fall in UPL's stock price largely factors in concerns and valuation of 10.5x/8.4x FY24E/FY25E EPS seems attractive. Hence, we maintain a Buy on UPL but with a lower PT of Rs. 745.

UPL Limited (UPL) Q1FY24 performance was a mixed bag with 7% miss in consolidated revenues to Rs. 8963 crore (down 17% y-o-y) due challenging business environment (post-patent product price and high channel inventory) across business segments, while EBITDA margin of 17.8% (down 389 bps y-o-y) was 186 bps above our estimate of 15.9% due to strong margins in the seeds business. Thus, consolidated adjusted EBITDA of Rs. 1592 crore (down 32% y-o-y) was marginally ahead of our estimate of Rs. 1,527 crore. CPC/UPL SAS/UPL specialty chemical faced challenging industry environment (weak volume/pricing) and thus witnessed a steep decline of 23.5%/13.8%/19.7% y-o-y in revenues to Rs. 5855 crore/Rs. 1259 crore/Rs. 3112 crore. However, seeds business performance was robust with a 26% y-o-y revenue growth (+14%/+9%/+3% benefit of volume/pricing/FX) and EBITDA margin expansion of 626 bps y-o-y to 34.3%. Consolidated adjusted PAT of Rs. 209 crore (down 78% y-o-y) missed our estimate due to negative contribution of Rs. 57 crore from share of Profit/(Loss) from Associates versus a positive contribution of Rs. 128 crore in Q1FY23.

Key positives

- Beat in EBITDA margin led by 626 bps y-o-y margin expansion for seeds business.

Key negatives

- Weakness in crop protection business – Revenue decline of 56%/15%/19%/10% y-o-y from North America/Latam/Europe/RoW.
- Cut in FY24 revenue and EBITDA guidance.

Management Commentary

- Company lowered FY24 revenue/EBITDA growth guidance to be 1-5%/3-7% respectively with recovery in H2FY24 led by volume growth.
- Crop protection business faced a tough market environment due to significant price correction for most post-patent products and de-stocking in distribution channels.
- Management expects demand on the crop protection side to recover as channel inventory approaches a near-normal levels.
- The management has guided for a capital expenditure of $300 million for FY24 (down from earlier guidance of $325 to $350 million).
- UPL lowered net debt by $150 million y-o-y to $3.2 billion in Q1FY24 basis with a plan to bring it down further during the year.

Revision in estimates – We have lowered our FY24-25 earnings estimate to factor lower revenue growth assumption given demand/pricing pressure.

Our Call

Valuation – Maintain Buy on UPL with a revised PT of Rs. 745: Although near term challenges on growth/pricing persist for agro-chem players but the steep fall of 29% in UPL's stock price from the 52-week high of Rs. 807 largely factors in concerns and a valuation of 10.5x/8.4x FY24E/FY25E EPS seems attractive. UPL's target to increase revenue share from differentiated and sustainable solutions would improve margin/earnings profile and drive sustainable growth in the medium to long term. Hence, we maintain a Buy rating on UPL but with a lower PT of Rs. 745 (reflects in cut FY25E EPS and lower PE of 10x).

Key Risks

A slowdown in the global agrochemical industry and delayed product launches could affect revenue growth. Currency fluctuations might hit the company, as UPL has a significant presence in various geographies. The continued oversupply of post-patented products may keep pricing/margins under check.

Valuation (Consolidated) Rs cr

Particulars	FY22	FY23E	FY24E	FY25E
Revenue	46,240	53,576	56,255	60,755
OPM (%)	22.0	20.8	21.2	22.4
Adjusted PAT	3,950	3,740	4,438	5,585
% YoY growth	27.1	(5.3)	18.7	25.8
Adjusted EPS (Rs)	51.6	49.9	59.2	74.5
P/E (x)	12.1	12.5	10.5	8.4
P/BV (x)	2.2	1.7	1.5	1.3
EV/EBITDA (x)	7.0	6.2	5.3	4.6
RoCE (%)	13.4	13.4	14.3	14.9
RoNW (%)	20.0	15.4	15.4	16.8

Source: Company; Sharekhan estimates

Mixed Q1; revenue miss gets offset by margin beat as seed business performed well

Q1FY24 performance was a mixed bag with 7% miss in consolidated revenues to Rs. 8963 crore (down 17% y-o-y) due challenging business environment (post-patent product price and high channel inventory) across business segments, while EBITDA margin of 17.8% (down 389 bps y-o-y) was 186 bps above our estimate of 15.9% due to strong margins in the seeds business. Thus, consolidated adjusted EBITDA of Rs. 1592 crore (down 32% y-o-y) was marginally ahead of our estimate of Rs. 1,527 crore. CPC/UPL SAS/UPL specialty chemical faced challenging industry environment (weak volume/pricing) and thus witnessed a steep decline of 23.5%/13.8%/19.7% y-o-y in revenues to Rs. 5855 crore/Rs. 1259 crore/Rs. 3112 crore. However, seeds business performance was robust with a 26% y-o-y revenue growth (+14%/+9%/+3% benefit of volume/pricing/FX) and EBITDA margin expansion of 626 bps y-o-y to 34.3%. Consolidated adjusted PAT of Rs. 209 crore (down 78% y-o-y) missed our estimate due to negative contribution of Rs. 57 crore from share of Profit/(Loss) from Associates versus a positive contribution of Rs. 128 crore in Q1FY23.

Key segmental performance Rs cr

Segmental Revenue	Q1FY24	Q1FY23	YoY (%)	Comments
Crop protection (ex-India)	5,855	7,658	-23.5	**Volume:** -17%, **Price:** -10%, FX: +3%. Significant decline in herbicide volume and prices, and product bans in Europe.
UPL SAS	1,203	1,395	-13.8	**Volume:** -7% YoY, **Price:** -7% YoY. Revenue impacted by delayed Kharif sowing activities, pricing pressure on post-patent side, and high channel inventory.
Advanta	1,061	842	26.0	**Volume:** +14%, **Price:** +9%, FX: +3%. Revenue Growth driven by robust traction in field corn, fresh corn and Grain Sorghum.
UPL Specialty	3,112	3,877	-19.7	Decline in revenue primarily led by slowdown in the agro-chemical and broader chemical industry.
EBITDA	**Q1FY24**	**Q1FY23**	**YoY (%)**	
Crop protection	564	1,614	-65.1	
UPL SAS	215	316	-32.0	
Advanta	364	236	54.2	Margin improvement led by improved product mix and good recovery in India vegetable business.
UPL Specialty	440	492	-10.6	
EBITDA Margin (%)			**bps**	
Crop protection (ex-India)	9.6	21.1	-530	
UPL SAS	17.9	22.7	-478	
Advanta	34.3	28.0	628	
UPL Specialty	14.1	12.7	145	

Source: Company; Sharekhan Research

Q1FY24 earnings call highlights

- **Revenue/EBITDA guidance lowered –** Company guided FY24 revenue/EBITDA growth to be 1-5%/3-7% respectively with the volume to grow around 15%-20%. In Q2, the company expects price decline similar to Q1 (high single digit). The management expects revenue to see recovery only in H2FY24 mainly led by volume growth with slight recovery in prices.
- **Recovery in Demand expected in H2FY24 –** The management expects recovery from Q3 onward mainly due to normalization of channel inventories, increased demand for herbicides and new product launches.
- **Global crop protection business –** On last two quarters, global crop protection business faced tough market environment due to significant price decline for most post-patent products and destocking in distribution channels. The management expects demand on the crop protection side to recover as channel inventory approaches near-normal levels.
- **Specialty Chemicals business –** Shareholders have approved carving out of the specialty chemicals business as a separate subsidiary. This will accelerate growth in this segment through improved access to capital.

- **Impact on Q1 revenues –** Pricing pressure and volume decline in herbicide segment (glufosinate, Glyphosate, Clethodim, and Smetolachlor) especially in North America and Brazil led to decline in revenue.
- **Impact on Q4 margins –** Lower prices led to margin compression. Despite of decline in margin the company has improved the share of differentiated segment from 24% last year to 35% in Q1FY24 as company launched new products like new Evolution and Feroce.
- **Capex –** To conserve cash, the company can delay some projects. The management has guided the capital expenditure of $300 million for FY24 (down from earlier guidance of $325 to $350 million).
- **Debt –** The company reduced its net debt by $160 million in Q1FY24 on y-o-y basis with a plan to bring it down further during the year.
- **Working capital –** In Q1FY24, the working capital days increased by 14 days on y-o-y basis mainly due to lower payables and a reduction in factoring. Management expects end of the year working capital to be 65-70 days.
- **Channel inventory –** The channel inventory is approaching a near-normalized level. The demand for crop protection product is expected to recover as inventory correction is almost done.

Results (Consolidated) Rs cr

Particulars	Q1FY24	Q1FY23	Y-o-Y %	Q4FY23	Q-o-Q %
Revenue	**8,963**	**10,821**	**(17.2)**	**16,569**	**(45.9)**
Total expenditure	7,690	8,675	(11.4)	13,847	(44.5)
Reported operating profit	1,273	2,146	(40.7)	2,722	(53.2)
Adjusted operating profit	**1,592**	**2,343**	**(32.1)**	**3,055**	**(47.9)**
Other Income	101	73	38.4	211	(52.1)
Depreciation	636	588	8.2	727	(12.5)
Interest	700	519	34.9	906	(22.7)
PBT	(5)	1,034	NA	1,271	NA
Tax	(164)	59	NA	311	NA
Reported PAT	166	877	(81.1)	792	(79.0)
Adjusted PAT	**209**	**955**	**-78.1**	**821**	**(74.5)**
Adjusted EPS (Rs.)	2.8	12.5	-77.7	10.9	(74.5)
Margins (%)			**BPS**		**BPS**
OPM	14.2	19.8	(563)	16.4	(223)
OPM	17.8	21.7	(389)	18.4	(67)
NPM	2.3	8.8	(649)	5.0	(262)
Tax rate	NA	5.7	NA	24.5	NA

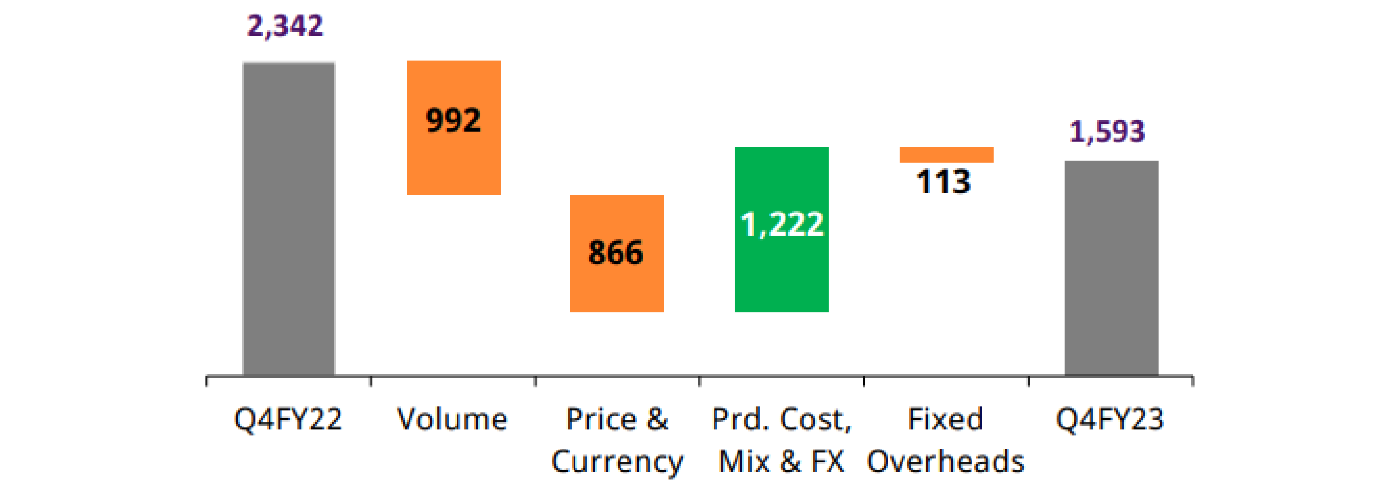
Source: Company; Sharekhan Research

Geographical revenue break-up Rs cr

Particulars	Q1FY24	Q1FY23	Y-o-Y %	Q4FY23	Q-o-Q %
Latin America	2,708	3,189	-15.1	6,444	-58.0
Europe	1,264	1,571	-19.5	2,800	-54.9
North America	675	1,551	-56.5	3,009	-77.6
India	3,109	3,163	-1.7	1,588	95.8
Rest of the World	1,207	1,347	-10.4	2,727	-55.7
Total	**8,963**	**10,821**	**-17.2**	**16,569**	**-45.9**

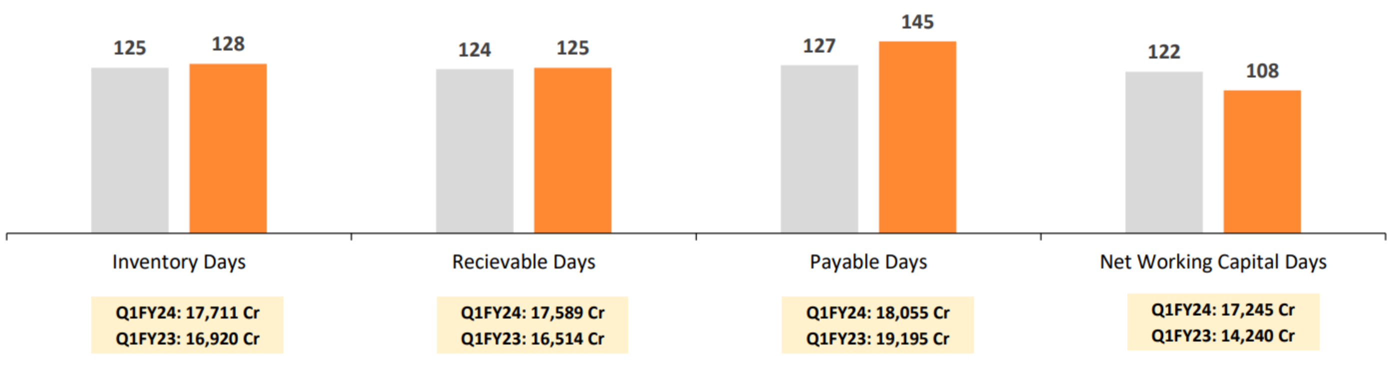
Source: Company; Sharekhan Research

Q1FY24 EBITDA Bridge versus Q1FY23



Source: Company Data

NWC declined by 5 days to 64 days in FY23



Source: Company Data

Q1FY24 Net Debt Position as on 30 June 2023

Gross & Net Debt Position – June 2023 vs June 2022

All figures are in US$ Mn and ₹ Crore

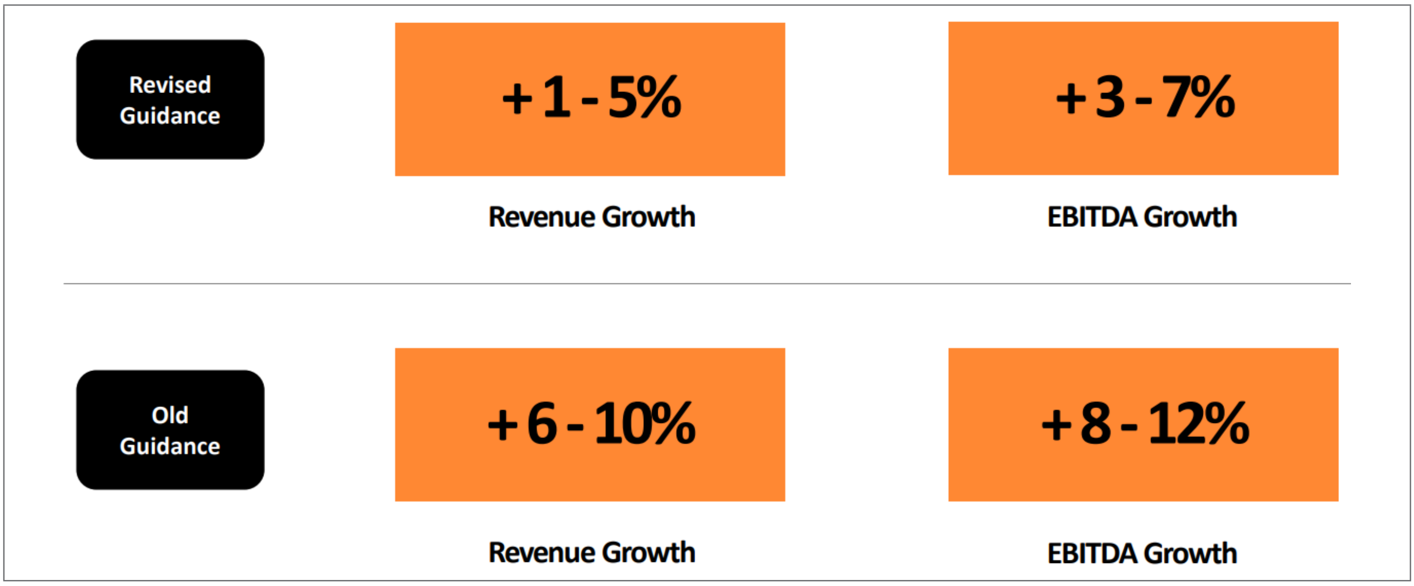
Particulars	June'23	June'22	Change
Gross Debt	$3,667 30,083	$3,814 30,123	($147) (40)
Cash and cash equivalent	$474 3,889[2]	$461 3,643	$13 246
Reported Net Debt	$3,193 **26,194**	$3,353 **26,480**	($160) **(286)**
Net Debt Adjusted for Currency Impact	***25,216[1]***	***26,480***	***(1,264)***

- **In USD terms, net debt at $3.19 Bn as of June'23 - lower by $160 Mn YoY.**
  - Adjusted for lower factoring, net debt would have stood at $2.94 Bn (down by $410 Mn YoY)
- Cash generated by business (before WC)*: ₹ 268 crores in Q1FY24 (vs ₹ 1,420 crores in Q1FY23)

Note: *[1]INR depreciated from 78.98 as on 30 June 2022 to 82.04 as on 30 June 2023. [2]Includes liquid investment of INR 124 crore as of Jun'23*
**Operating CF before WC less interest, tax and other cash expenses*

Source: Company Data

Management lowered Revenue/EBITDA growth guidance for FY24



Source: Company Data

Outlook and Valuation

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

The Indian agrochemical industry's outlook is encouraging, primarily driven by rising foodgrain production and domestic demand, favourable regulatory reforms for farmers and a vast opportunity from products going off-patent. The government's focus is to double farmers' income (higher MSPs for crops). Above-normal monsoons and higher reservoir levels would augment demand for agri-inputs in India. We also expect exports from India to grow strongly as India is being looked upon as the preferred supplier for agri-inputs, given supply disruptions in 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 robustly, supported by higher demand for crop protection and farm solutions mitigating slower growth in the US and Europe.

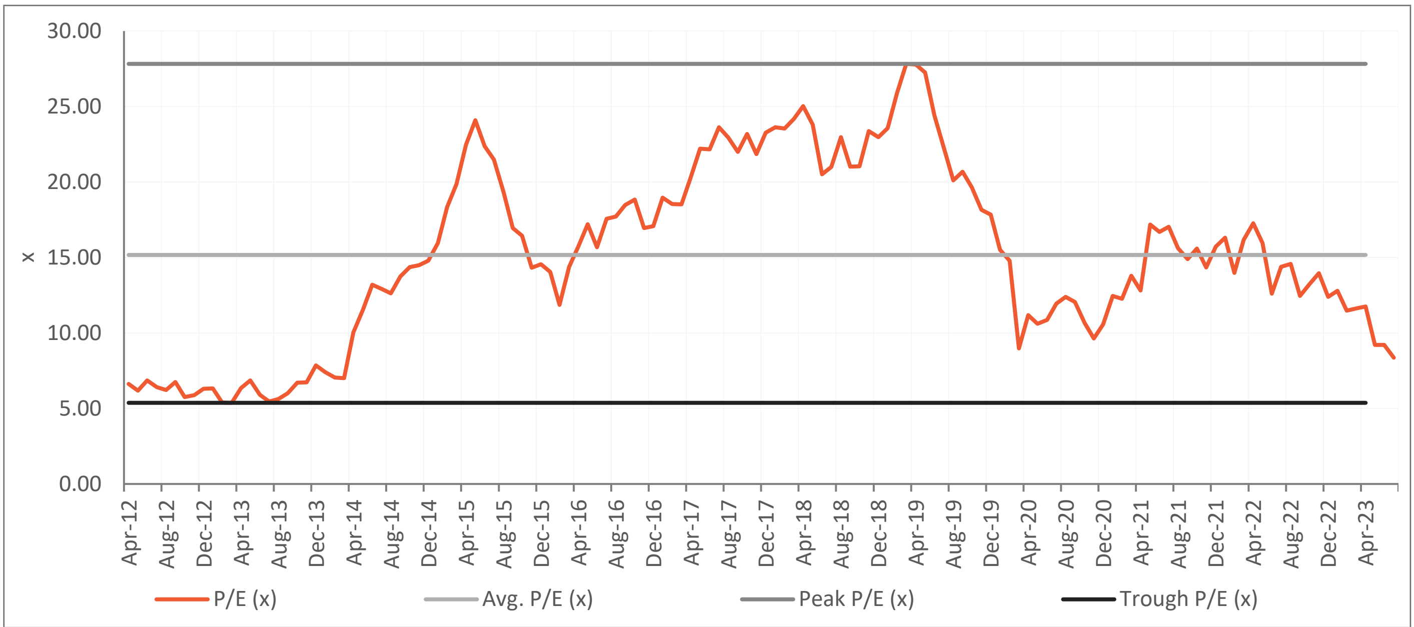
■ Company Outlook – Near concerns; focus on differentiated & sustainable solutions bodes well for long term growth

High channel inventory and pricing pressure amid rising Chinese supply would make growth challenging for global as well as domestic agrochemical companies. Having said that, UPL's focus on potential market share gains given its global scale, backward integration, and focus on high-growth bio-solutions space would drive medium to long-term growth. Differentiated and sustainable solutions would be a key growth driver as this segment is growing at 15-20% and its gross margins are 1,000-1,500 bps higher versus normal products.

■ Valuation – Maintain Buy on UPL with a revised PT of Rs. 745

Although near term challenges on growth/pricing persist for agro-chem players but the steep fall of 29% in UPL's stock price from the 52-week high of Rs. 807 largely factors in concerns and a valuation of 10.5x/8.4x FY24E/FY25E EPS seems attractive. UPL's target to increase revenue share from differentiated and sustainable solutions would improve margin/earnings profile and drive sustainable growth in the medium to long term. Hence, we maintain a Buy rating on UPL but with a lower PT of Rs. 745 (reflects in cut FY25E EPS and lower PE of 10x).

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 position 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 patents 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 delay in the 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.
- Continued oversupply of post-patented products may keep pricing/margin under check.

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
Mike Frank	Group COO
Dhruv Sawhney	COO, nurture.farm
Anand Vora	Global CFO

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	JPMorgan Chase & Co	7.4
2	Life Insurance Corp of India	7.23
3	Massachusetts Financial Services C	4.19
4	Vanguard Group Inc/The	3.3
5	GOVERNMENT PENSI	2.56
6	BlackRock Inc	2.31
7	Norges Bank	2.23
8	SBI Funds Management Ltd	1.41
9	ICICI Prudential Asset Management	1.41
10	Dimensional Fund Advisors LP	1.3

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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Other registrations of Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669.

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