



**HDFC securities**

Equity  
Research

Pick<sub>of the</sub>  
week

Industry	CMP	Recommendation	Add on dips to	Target	Time Horizon
<b>Agrochemicals</b>	Rs. 801	Buy at CMP and add on Dips	Rs. 801-740	Rs. 988	4 Quarters

Incorporated in 1969, United Phosphorus Ltd. is a global generic crop protection, chemicals and seeds company. The company manufactures and markets agrochemicals, industrial chemicals, chemical intermediates, and specialty chemicals in 130+ countries across all six continents. The Company's segments include Agro activity and Non-agro activity. The Agro activity segment includes the manufacturing and marketing of conventional agrochemical products, seeds and other agricultural related products. The Non-agro activity segment includes the manufacturing and marketing of industrial chemicals and other non-agriculture related products. It offers products like fungicides, herbicides, insecticides, plant growth and regulators, rodenticides, industrial and specialty chemicals, and nutrifeds. The Company sells its products in approximately 130 countries. It has 14 Manufacturing units in India and 19 outside India.

We recommend UPL as a Buy at CMP of Rs. 801 and add on decline of Rs. 740 for the target of Rs.988 (18x of FY20 EPS) for the time frame of 4 Quarters.

### Investment Rationale:

#### Dominant Player in the High Entry Barrier Industry

India is the fourth largest global producer of agrochemicals in the world after US, Japan and China. This segment generated a value of US \$4.4bn in FY15 and is expected to grow at 7.5% per annum to reach US \$6.3bn by FY20.

UPL is the 2<sup>nd</sup> largest post-patent crop protection chemical company and the 9<sup>th</sup> largest agrochemical company in the world. It has done 25+ acquisitions in more than two decades of time. Acquisitions were done to gain access to the overseas markets, and to increase their distribution, brands and registrations. Most of these acquisitions were turned around successfully and boosted UPL's presence globally.

Crop protection market is a mature industry and has very high entry barriers because of three key factors, high upfront investments, high R&D Cost and strict regulations. Companies have to incur huge capex for plants, machinery etc. before they see any sales in this industry. Even the R&D cost for the development of new products is quite high for this industry. The overall process of product registration in various geographies remains tedious and time-consuming. For instance, in the USA, it takes 3-3.5 years to register a product. Europe and Japan have even longer periods for product registration with 4-5 years and 8-9 years respectively.

HDFC Scrip Code	UNIPHO
BSE Code	512070
NSE Code	UPL
Bloomberg	UPLL IN
CMP as on 19 Jan'18	801
Equity Capital (Rsmn)	1017
Face Value (Rs)	2
Equity O/S (mn)	508
Market Cap (Rs mn)	4,07,473
Book Value (Rs)	145
Avg. 52 Week Vol	1519193
52 Week High	902
52 Week Low	680

Shareholding Pattern (%)	
Promoters	27.9
Institutions	51.7
Non Institutions	20.5

PCG Risk Rating*	Yellow
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\* Refer Rating explanation

#### FUNDAMENTAL ANALYST

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## KEY HIGHLIGHTS

- ***UPL Ltd is a global agrochemical company catering to crop protection chemical, seeds and post-harvest products.***
- ***UPL is the Dominant Player in the High Entry Barrier Industry.***
- ***Company has superior & innovative product and wider geographic range.***
- ***Budget is likely to focus more on Agri sector***
- ***UPL is consistently outperforming the global crop protection chemical industry for the last five consecutive years.***
- ***UPL has cost advantage over other peers because of backward integration.***
- ***We recommend UPL as a Buy at CMP of Rs. 801 and add on decline of Rs. 740 for the target of Rs.988 (18x of FY20 EPS).***

## Superior & Innovative product and wider geographic range

UPL is not just a product driven company; over the period of time company has evolved itself as service-driven organization. The company is now a one stop solution for farmers in their all agriculture related needs. It has presence in manufacturing seed, protecting seeds and post-harvest storage solutions also. UPL has 5934 of product registrations across countries. It not only manufactures and markets agrochemicals but also industrial chemicals, chemical intermediates, and specialty.

UPL is constantly doing R&D for developing new and innovative product. It has shown tremendous progress improving its product mix over the past few years, with innovation rate rising from 2.5% in FY14 to 15% in FY17.

The Company sells its products in approximately 130 countries. It has 14 Manufacturing units in India and 19 outside India. Almost 80% of the revenue comes from Outside India. Regions of Latin America, Europe, and the North America continue to remain largest markets outside India. This helps company in getting balanced revenue throughout the year and reduces the risk of fluctuating demand from any one region.

### Presence across value chain:



**Budget Expectations**

The agriculture sector in India is expected to perform better in the next few years due to increased investments in agricultural infrastructure such as irrigation facilities, warehousing and cold storage. Government will continue to push for doubling the farm income. Almost every year the Union Budget brings some cheer for the Agriculture sector. Last year provisions for crop insurance, Agri-credit loan, micro Irrigation Fund etc. were introduced giving an added boost to the sector. Overall support to agriculture sector was raised by 24% to Rs.1.87trn.

This year, the expectation from the Union Budget is that it may announce a number of proposals which will result to an improvement in the credit flow to farmers, an increase in irrigation acreage, crop insurance and a boost to farm incomes. With these measures, the income of farmers will increase leaving them with higher disposable income and this in turn will benefit all agri-input companies like UPL.

**Cost Advantage via Backward Integration**

China is the largest producer of raw materials used in the agro chemicals. But now due to increasingly stringent environmental norms in China their supply to the global market is reducing. 60-65% of manufacturing takes place in-house for UPL giving it a significant advantage over other industry players who are dependent on China as a supplier of raw materials.

**Strong Financials**

UPL is consistently outperforming the global crop protection chemical industry for the last five consecutive years. This year also it has outperformed the global crop protection chemical industry by reporting a revenue growth of 17% against the broad sectors de-growth of 2.5%. This outperformance is remarkable considering that the overall sector posted its second consecutive de-growth year.

In FY17, Company has posted excellent numbers. Sales rose 16%, EBITDA grew 24.6% while Net Profit jumped 73% aided by other income. Going ahead we expect UPL to post a growth of 13% in revenue and 15% in PAT and CAGR over FY17-20E and margin to increase 100bps over the same period of time. Net D/E is expected to reach 0.1x in FY20E from c.0.4x.

**View & Valuation:**

UPL remains the preferred pick among the industry because of Superior & Innovative product and wider geographic range, Stable working capital cycle and cost advantage via of Backward Integration. Populist budget will focus more on Agri sector and this in turn will bust demand for UPL's products.

UPL is consistently outperforming the global crop protection chemical industry for the last five consecutive years. It has been included in the prestigious NSE's Nifty 50 index from 29<sup>th</sup> September 2017.

We recommend UPL as a Buy at CMP of Rs. 801 and add on decline of Rs. 740 for the target of Rs.988 (18x of FY20 EPS) for the time frame of 4 Quarters.

**Risk & Concerns:**

- Almost 80% of the revenue comes from overseas so currency fluctuation might hurt the profitability.
- Agriculture sector is always influenced by the politics and any regulatory changes might hurt or can give benefit to company.
- The majority of the suppliers of the industry are from China. They are witnessing capacity cuts. So the fluctuation of raw material prices might be seen in near future.

**Quarterly Financials Snapshot (Consolidated)**

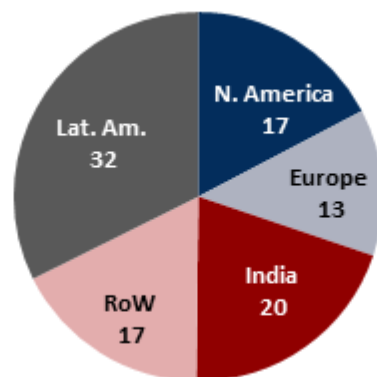
(Rs mn)	2QFY18	2QFY17	YoY (%)	1QFY18	QoQ (%)
<b>Net Sales</b>	<b>37,700</b>	<b>35,410</b>	<b>6.5</b>	<b>37,230</b>	<b>1.3</b>
Material Expenses	16,560	16,490	0.4	16,470	0.5
Employee Expenses	4,460	3,990	11.8	4,120	8.3
Other Expenses	9,910	9,450	4.9	9,730	1.8
<b>EBITDA</b>	<b>6,770</b>	<b>5,480</b>	<b>23.5</b>	<b>6,910</b>	<b>(2.0)</b>
Depreciation	1,650	1,540	7.1	1,580	4.4
<b>EBIT</b>	<b>5,120</b>	<b>3,940</b>	<b>29.9</b>	<b>5,330</b>	<b>(3.9)</b>
Other Income	760	820	(7.3)	1,010	(24.8)
Interest	1,820	1,800	1.1	800	127.5
<b>PBT</b>	<b>4,060</b>	<b>2,960</b>	<b>37.2</b>	<b>5,540</b>	<b>(26.7)</b>
Tax	750	430	74.4	480	56.3
<b>PAT</b>	<b>3,310</b>	<b>2,530</b>	<b>30.8</b>	<b>5,060</b>	<b>(34.6)</b>
Minority Interest/Associate	620	310	100.0	120	416.7
<b>RPAT</b>	<b>2,690</b>	<b>2,220</b>	<b>21.2</b>	<b>4,940</b>	<b>(45.5)</b>
<b>AEPS (Rs/sh)</b>	<b>4.7</b>	<b>3.3</b>	<b>43.4</b>	<b>9.3</b>	<b>(49.9)</b>

Source: Company, HDFC sec Research

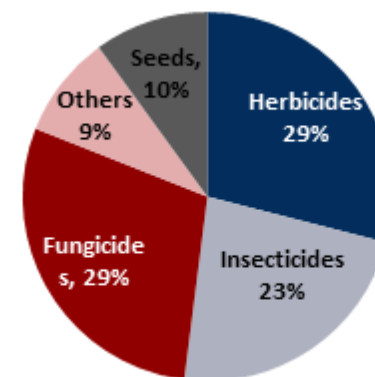
**Segmental Revenues**

	2QFY18	2QFY17	YoY (%)	1QFY18	QoQ (%)
North America	3,930	3,750	4.8	6,810	(42.3)
India	9,970	9,090	9.7	12,460	(20.0)
Europe	3,630	3,410	6.5	5,850	(37.9)
RoW	6,320	5,990	5.5	6,020	5.0
Latin America	13,850	13,170	5.2	7,370	87.9
<b>Total</b>	<b>37,700</b>	<b>35,410</b>	<b>6.5</b>	<b>38,510</b>	<b>(2.1)</b>

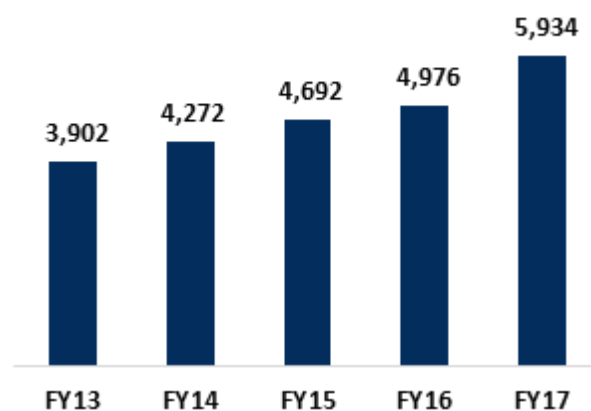
Source: Company, HDFC sec Research

**Revenue Break up geographiy wise (FY17)**


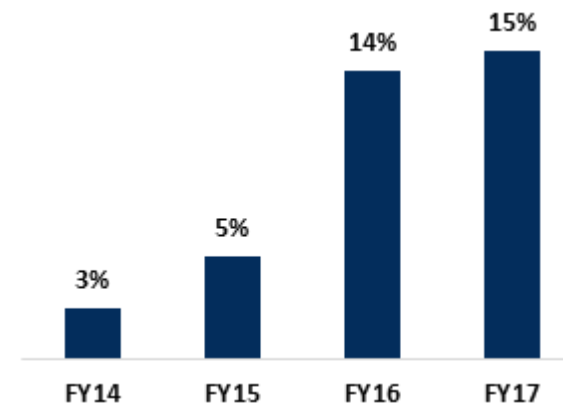
Source: Company, HDFC sec Research

**Well diversified and strong product portfolio (FY17)**


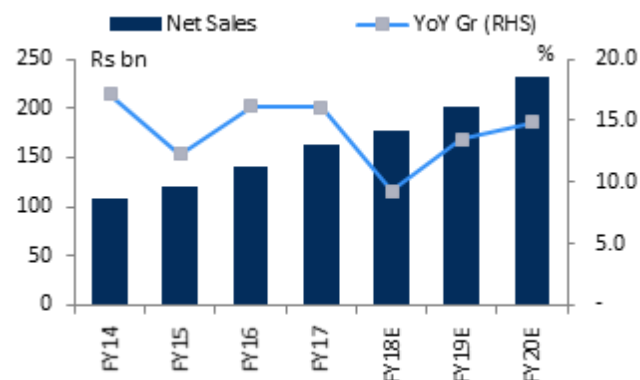
Source: Company, HDFC sec Research

**Number of Product Registrations**


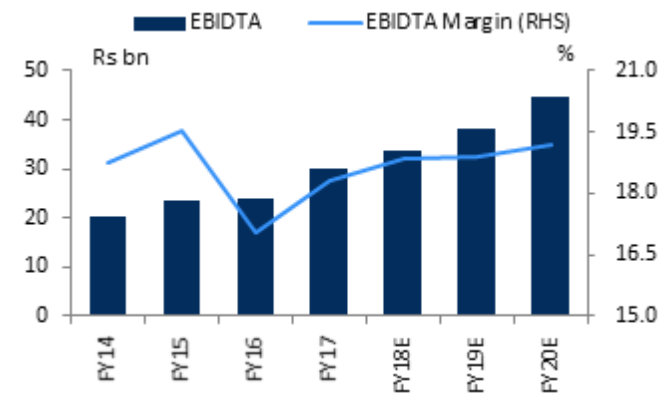
Source: Company, HDFC sec Research

**Innovation rates (sales of new products/ overall sales)**


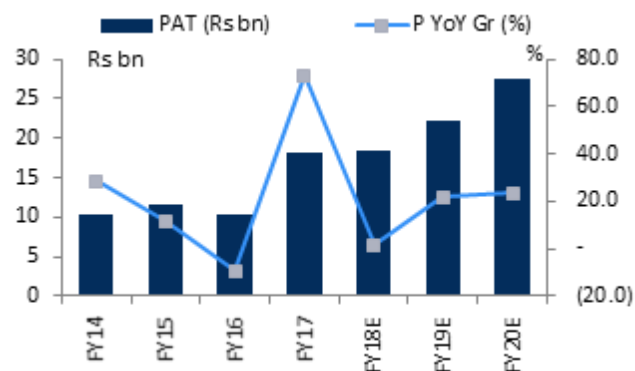
Source: Company, HDFC sec Research

**Revenue may see~ 5% CAGR over FY17-20E**


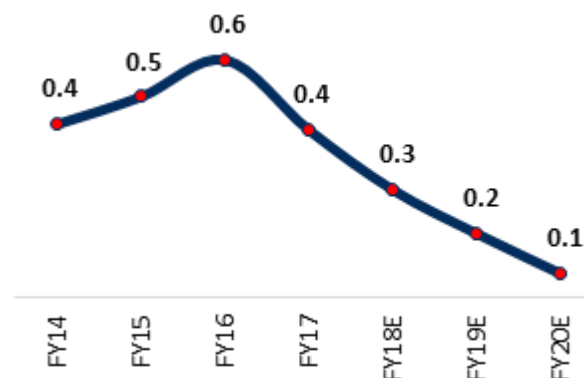
Source: Company, HDFC sec Research

**EBITDA and EBITDA Margin**


Source: Company, HDFC sec Research

**Retrun Ratios**


Source: Company, HDFC sec Research

**Declining Trend of Net Debt to Equity**


Source: Company, HDFC sec Research



**Income Statement (Consolidated)**

(Rs mn)	FY16	FY17	FY18E	FY19E	FY20E
<b>Net Sales</b>	<b>1,40,480</b>	<b>163,120</b>	<b>178,210</b>	<b>202,233</b>	<b>232,381</b>
Growth (%)	16.2	16.1	9.3	13.5	14.9
Material Expenses	67,800	78,160	85,095	98,083	113,867
Employee Expenses	14,340	16,270	17,897	20,224	23,257
Other Operating Expenses	34,390	38,840	41,629	45,684	50,694
<b>EBIDTA</b>	<b>23,950</b>	<b>29,850</b>	<b>33,589</b>	<b>38,242</b>	<b>44,563</b>
<i>EBIDTA Margin (%)</i>	<i>17.0</i>	<i>18.3</i>	<i>18.8</i>	<i>18.9</i>	<i>19.2</i>
<i>EBIDTA Growth (%)</i>	<i>1.4</i>	<i>24.6</i>	<i>12.5</i>	<i>13.9</i>	<i>16.5</i>
Depreciation	6,760	6,720	6,994	7,260	7,489
<b>EBIT</b>	<b>17,190</b>	<b>23,130</b>	<b>26,594</b>	<b>30,982</b>	<b>37,074</b>
Other Income	1,870	3,630	3,552	3,670	3,750
Interest & Financial Charges	7,040	7,350	6,526	6,286	6,139
<b>PBT</b>	<b>12,020</b>	<b>19,410</b>	<b>23,620</b>	<b>28,366</b>	<b>34,685</b>
Tax	1,650	1,890	4,724	5,673	6,937
<b>RPAT</b>	<b>10,370</b>	<b>17,520</b>	<b>18,896</b>	<b>22,693</b>	<b>27,748</b>
Profit From Associates	(850)	(190)	(590)	(390)	(190)
EO (Loss) / Profit (Net Of Tax)	(903)	(731)	-	-	-
<b>APAT</b>	<b>10,423</b>	<b>18,061</b>	<b>18,306</b>	<b>22,303</b>	<b>27,558</b>
<i>APAT Growth (%)</i>	<i>(9.4)</i>	<i>73.3</i>	<i>1.4</i>	<i>21.8</i>	<i>23.6</i>
<b>AEPS</b>	<b>20.4</b>	<b>35.4</b>	<b>35.9</b>	<b>43.7</b>	<b>54.0</b>
<i>AEPS Growth (%)</i>	<i>(9.4)</i>	<i>73.3</i>	<i>1.4</i>	<i>21.8</i>	<i>23.6</i>

Source: Company, HDFC sec Research

**Balance Sheet (Consolidated)**

(Rs mn)	FY16	FY17	FY18E	FY19E	FY20E
<b>SOURCES OF FUNDS</b>					
Share Capital	860	1,010	1,020	1,020	1,020
Reserves	58,030	72,960	86,595	104,235	126,030
<b>Total Shareholders Funds</b>	<b>58,890</b>	<b>73,970</b>	<b>87,615</b>	<b>105,255</b>	<b>127,050</b>
Minority Interest	440	330	240	240	240
Long-term Debt	22,660	53,500	52,000	50,500	49,000
Short-term Debt	25,050	7,080	5,580	4,080	2,580
<b>Total Debt</b>	<b>47,710</b>	<b>60,580</b>	<b>57,580</b>	<b>54,580</b>	<b>51,580</b>
Long-term Provisions & Others	5,020	4,040	4,040	4,040	4,040
<b>TOTAL SOURCES OF FUNDS</b>	<b>1,12,060</b>	<b>138,920</b>	<b>149,475</b>	<b>164,115</b>	<b>182,910</b>
<b>APPLICATION OF FUNDS</b>					
<b>Net Block</b>	<b>34,450</b>	<b>36,520</b>	<b>37,446</b>	<b>41,186</b>	<b>44,697</b>
CWIP	4,840	7,920	11,000	11,000	11,000
Goodwill on Consolidation	4,170	4,190	4,190	4,190	4,190
Investments	3,350	3,780	3,780	<b>3,780</b>	<b>3,780</b>
LT Loans & Advances	5,910	7,720	7,720	7,720	7,720
Inventories	37,870	41,560	43,942	49,866	57,299
Debtors	51,000	56,560	61,031	69,258	79,582
Cash & Equivalents	11,890	28,950	33,604	37,592	44,204
ST Loans & Advances	2,700	1,190	1,190	1,190	1,190
Other Current Assets	8,610	8,720	8,720	8,720	8,720
<b>Current Assets</b>	<b>1,12,070</b>	<b>136,980</b>	<b>148,487</b>	<b>166,626</b>	<b>190,996</b>
Creditors	39,540	48,750	53,707	60,947	70,033
Other Current Liabilities & Provi	17,090	14,450	14,450	14,450	14,450
Current Liabilities	56,630	63,200	68,157	75,397	84,483
<b>Net Current Assets</b>	<b>55,440</b>	<b>73,780</b>	<b>80,330</b>	<b>91,229</b>	<b>106,513</b>
<b>Net Deferred Tax Asset</b>	<b>3,900</b>	<b>5,010</b>	<b>5,010</b>	<b>5,010</b>	<b>5,010</b>
<b>TOTAL APPLICATION OF FUNDS</b>	<b>1,12,060</b>	<b>138,920</b>	<b>149,475</b>	<b>164,115</b>	<b>182,910</b>

Source: Company, HDFC sec Research

**Cash Flow Statement (Consolidated)**

(Rs mn)	FY16	FY17	FY18E	FY19E	FY20E
Reported PBT	13,310	20,220	23,620	28,366	34,685
Non-operating & EO Items	(1,690)	(2,980)	(3,552)	(3,670)	(3,750)
Interest Expenses	7,040	7,350	6,526	6,286	6,139
Depreciation	6,760	6,720	6,994	7,260	7,489
Working Capital Change	(7,040)	(1,210)	(1,896)	(6,911)	(8,673)
Tax Paid	(4,420)	(3,410)	(4,724)	(5,673)	(6,937)
<b>OPERATING CASH FLOW ( a )</b>	<b>13,960</b>	<b>26,690</b>	<b>26,969</b>	<b>25,658</b>	<b>28,953</b>
Capex	(10,140)	(12,590)	(12,000)	(12,000)	(12,600)
<i>Free Cash Flow (FCF)</i>	<i>3,820</i>	<i>14,100</i>	<i>14,969</i>	<i>13,658</i>	<i>16,353</i>
Investments	(660)	(430)	-	-	-
Non-operating Income	3,160	4,440	3,552	3,670	3,750
Others	(9,550)	(1,410)	-	-	-
<b>INVESTING CASH FLOW ( b )</b>	<b>(17,190)</b>	<b>(9,990)</b>	<b>(8,448)</b>	<b>(8,330)</b>	<b>(8,850)</b>
Debt Issuance/(Repaid)	12,840	10,790	(3,000)	(3,000)	(3,000)
Interest Expenses	(7,040)	(7,350)	(6,526)	(6,286)	(6,139)
<i>FCFE</i>	<i>9,620</i>	<i>17,540</i>	<i>5,442</i>	<i>4,372</i>	<i>7,214</i>
Share Capital Issuance	-	-	10	-	-
Dividend	(2,290)	(2,280)	(4,391)	(4,664)	(5,762)
Others	1,030	(830)	(10)	0	0
<b>FINANCING CASH FLOW ( c )</b>	<b>4,540</b>	<b>330</b>	<b>(13,917)</b>	<b>(13,949)</b>	<b>(14,902)</b>
<b>NET CASH FLOW (a+b+c)</b>	<b>1,310</b>	<b>17,030</b>	<b>4,604</b>	<b>3,379</b>	<b>5,202</b>
EO Items, Others	(440)	30	-	-	-
Closing Cash & Equivalents	<b>11,890</b>	<b>28,950</b>	<b>33,604</b>	<b>37,592</b>	<b>44,204</b>

Source: Company, HDFC sec Research

**Key Ratios**

	FY16	FY17	FY18E	FY19E	FY20E
<b>PROFITABILITY (%)</b>					
GPM	51.7	52.1	52.3	51.5	51.0
EBITDA Margin	17	18.3	18.8	18.9	19.2
APAT Margin	7.4	11.1	10.3	11.0	11.9
RoE	18.5	27.2	22.7	23.1	23.7
RoCE	16	19.7	16.3	17.4	18.7
<b>EFFICIENCY</b>					
Tax Rate (%)	13.7	9.7	20.0	20.0	20.0
Asset Turnover (x)	1.4	1.3	1.2	1.3	1.3
Inventory (days)	98	93	90	90	90
Debtors (days)	133	127	125	125	125
Payables (days)	103	109	110	110	110
Cash Conversion Cycle (days)	113	100	95	99	102
Debt/EBITDA (x)	2	2.0	1.7	1.4	1.2
Net D/E	0.6	0.4	0.3	0.2	0.1
Interest Coverage	2.4	3.1	4.1	4.9	6.0
<b>PER SHARE DATA (Rs/sh)</b>					
EPS	20.4	35.4	35.9	43.7	54.0
CEPS	33.7	48.6	49.6	58.0	68.7
DPS	4.2	6.9	7.0	7.4	9.2
BV	115.5	145.0	171.8	206.4	249.1
<b>VALUATION</b>					
P/E	39	22.5	22.2	18.2	14.7
P/BV	6.9	5.5	4.6	3.9	3.2
EV/EBITDA	18.2	15.1	13.2	11.4	9.6
Dividend Yield (%)	0.5	0.8	0.9	0.9	1.1
OCF/EV (%)	3.2	5.9	6.1	5.9	6.8
FCF/EV (%)	0.9	3.1	3.4	3.1	3.8
FCFE/Mcap (%)	(0.8)	1.6	2.0	1.8	2.4

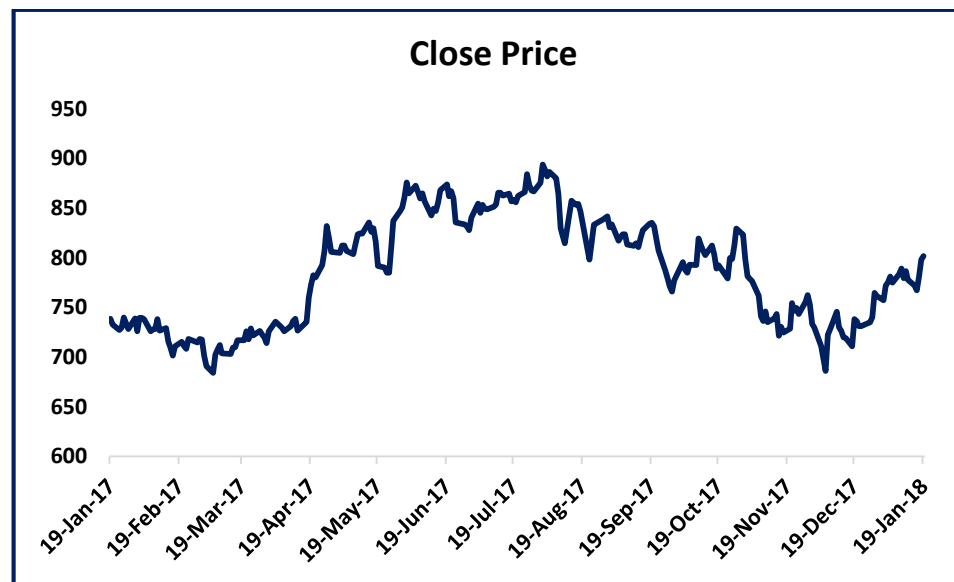
Source: Company, HDFC sec Research

**Rating Chart**

R E T U R N	HIGH			
	MEDIUM			
	LOW			
		LOW	MEDIUM	HIGH
		RISK		

**Ratings Explanation:**

RATING	Risk - Return	BEAR CASE	BASE CASE	BULL CASE
BLUE	LOW RISK - LOW RETURN STOCKS	IF RISKS MANIFEST PRICE CAN FALL 20% OR MORE	IF RISKS MANIFEST PRICE CAN FALL 15% & IF INVESTMENT RATIONALE FRUCTFIES PRICE CAN RISE BY 15%	IF INVESTMENT RATIONALE FRUCTFIES PRICE CAN RISE BY 20% OR MORE
YELLOW	MEDIUM RISK - HIGH RETURN STOCKS	IF RISKS MANIFEST PRICE CAN FALL 35% OR MORE	IF RISKS MANIFEST PRICE CAN FALL 20% & IF INVESTMENT RATIONALE FRUCTFIES PRICE CAN RISE BY 30%	IF INVESTMENT RATIONALE FRUCTFIES PRICE CAN RISE BY 35% OR MORE
RED	HIGH RISK - HIGH RETURN STOCKS	IF RISKS MANIFEST PRICE CAN FALL 50% OR MORE	IF RISKS MANIFEST PRICE CAN FALL 30% & IF INVESTMENT RATIONALE FRUCTFIES PRICE CAN RISE BY 30%	IF INVESTMENT RATIONALE FRUCTFIES PRICE CAN RISE BY 50% OR MORE

**Rating Definition:**

Buy: Stock is expected to gain by 10% or more in the next 1 Year.

Sell: Stock is expected to decline by 10% or more in the next 1 Year.

**Disclosure:**

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Any holding in stock –NO

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