

United Phosphorus

| BSE SENSEX | S&P CNX | CMP: INR144 | TP: INR196 | Buy | | | | | | |
|-----------------------|-------------------|-------------|------------|-------------|---------|----------|---------|----------|----------|-----------|
| 16,863 | 5,087 | | | | | | | | | |
| Bloomberg | UNTP IN | | | | | | | | | |
| Equity Shares (m) | 461.8 | | | | | | | | | |
| 52-Week Range (Rs) | 171/120 | | | | | | | | | |
| 1,6,12 Rel. Perf. (%) | 4/-6/11 | | | | | | | | | |
| M.Cap. (INR b) | 66.4 | | | | | | | | | |
| M.Cap. (USD b) | 1.3 | | | | | | | | | |
| Year End | Net Sales (INR m) | PAT (INR M) | EPS (INR) | EPS Gr. (%) | P/E (X) | P/BV (X) | RoE (%) | RoCE (%) | EV/Sales | EV/EBITDA |
| 03/10A | 54,585 | 5,491 | 11.9 | -6.4 | 12.1 | 2.1 | 19.4 | 16.1 | 1.2 | 7.5 |
| 03/11A | 58,045 | 5,701 | 12.3 | 3.8 | 11.6 | 1.8 | 17.0 | 17.0 | 1.2 | 6.8 |
| 03/12E | 81,097 | 6,378 | 13.8 | 11.9 | 10.4 | 1.6 | 16.1 | 18.1 | 1.0 | 5.8 |
| 03/13E | 92,417 | 9,082 | 19.7 | 42.4 | 7.3 | 1.4 | 20.0 | 18.2 | 0.8 | 4.6 |

United Phosphorus (UNTP) reported lower than expected numbers for 3QFY12. EBITDA margin (ex OI) was 18.1% (v/s our estimate of 19%) despite higher than estimated revenue. While margins were impacted by higher staff cost, recurring PAT was impacted by higher tax.

Key highlights

- Revenue grew 58% to INR19.3b (v/s our estimate of INR18.7b), driven by ~33% organic growth. While volume growth was ~31%, favorable forex contributed ~19% and pricing contributed ~8% to revenue growth.
- Gross margin declined 210bp YoY (expanded 70bp QoQ) to 36.6%, impacted by higher RM cost and full period consolidation of DVA Agro (Brazil). However, higher operating leverage diluted the impact of RM cost push, resulting in flat YoY (-20bp QoQ) EBITDA margin at 18.1% (v/s our estimate of 19%). Further, higher tax restricted adjusted PAT growth at ~36% to INR1.14b (v/s our estimate of INR1.44b).
- UNTP accounted for loss of INR110m for its recently acquired 50% associate company, Sipcam Isagro (Brazil), for the July-September quarter, resulting in INR216m loss from associates.
- Based on strong demand environment, the management has maintained its revenue growth guidance of 35-40% and EBITDA margin guidance of 19-20%.

We are downgrading our EPS estimates by ~8% to INR13.8 for FY12 and to INR19.7 for FY13 to factor in higher staff cost and higher tax. The stock trades at 10.4x FY12E and 7.3x FY13E EPS. Maintain **Buy**, with a target price of INR196 (~10x FY13E EPS).

Quarterly Performance (Consolidated)

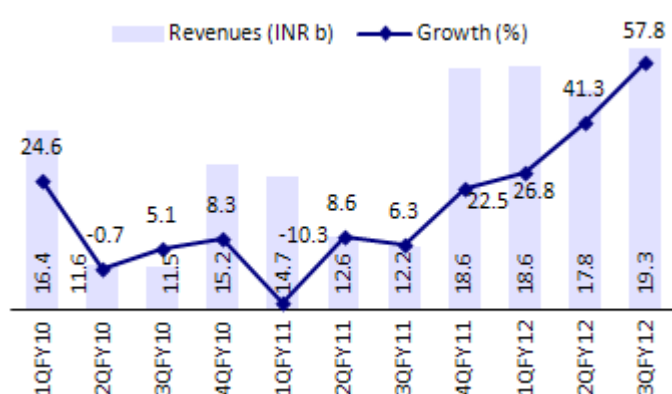
| Y/E March | (INR Million) | | | | | | | | FY11 | FY12E |
|--------------------------|---------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| | FY11 | | | | FY12 | | | | | |
| | 1Q | 2Q | 3Q | 4Q | 1Q | 2Q | 3Q | 4QE | | |
| Net Revenues | 14,686 | 12,569 | 12,221 | 18,569 | 18,621 | 17,757 | 19,288 | 25,430 | 58,045 | 81,097 |
| YoY Change (%) | -10.3 | 8.6 | 6.3 | 22.5 | 26.8 | 41.3 | 57.8 | 36.9 | 6.3 | 39.7 |
| Total Expenditure | 11,794 | 10,243 | 10,007 | 14,896 | 15,173 | 14,502 | 15,804 | 20,466 | 46,939 | 65,945 |
| EBITDA | 2,892 | 2,326 | 2,215 | 3,673 | 3,449 | 3,255 | 3,484 | 4,964 | 11,106 | 15,151 |
| Margins (%) | 19.7 | 18.5 | 18.1 | 19.8 | 18.5 | 18.3 | 18.1 | 19.5 | 19.1 | 18.7 |
| Depreciation | 472 | 515 | 491 | 661 | 628 | 719 | 785 | 785 | 2,138 | 2,917 |
| Interest | 1,004 | 652 | 893 | 571 | 714 | 1,918 | 826 | 750 | 3,120 | 4,208 |
| Other Income | 186 | 238 | 262 | 250 | 226 | 196 | 107 | 150 | 937 | 678 |
| PBT before EO Expense | 1,603 | 1,397 | 1,093 | 2,691 | 2,332 | 814 | 1,979 | 3,579 | 6,785 | 8,704 |
| Extra-Ord Expense | 0 | 0 | 0 | 140 | 0 | 144 | 13 | 0 | 140 | 157 |
| PBT after EO Expense | 1,603 | 1,397 | 1,093 | 2,551 | 2,332 | 670 | 1,966 | 3,579 | 6,645 | 8,548 |
| Tax | 156 | 250 | 266 | 58 | 466 | 151 | 626 | 723 | 731 | 1,966 |
| Rate (%) | 9.8 | 17.9 | 24.4 | 2.3 | 20.0 | 22.5 | 31.8 | 20.2 | 11.0 | 23.0 |
| Reported PAT | 1,447 | 1,147 | 827 | 2,493 | 1,866 | 519 | 1,340 | 2,856 | 5,914 | 6,582 |
| Income from Associate Co | -23 | 0 | 12 | -314 | -23 | 51 | -216 | -136 | -234 | -275 |
| Adjusted PAT | 1,424 | 1,147 | 839 | 2,317 | 1,843 | 713 | 1,137 | 2,720 | 5,805 | 6,428 |
| YoY Change (%) | -19.2 | 12.0 | 33.5 | 7.8 | 29.5 | -37.8 | 35.5 | 17.4 | 3.9 | 10.7 |
| Margins (%) | 9.7 | 9.1 | 6.9 | 12.5 | 9.9 | 4.0 | 5.9 | 10.7 | 10.0 | 7.9 |

E: MOSL Estimates

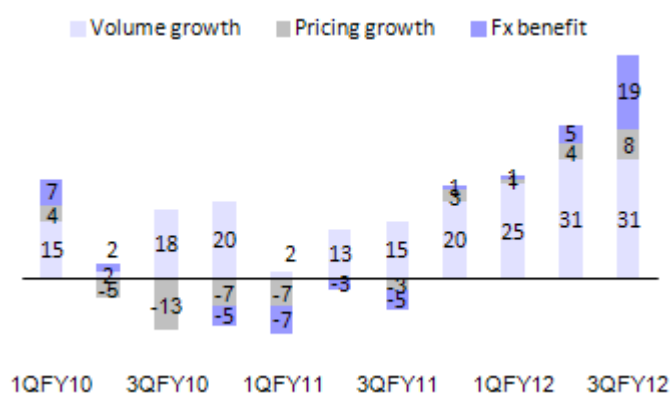
Volume pick-up, favorable forex and acquisition drive revenue growth

- Consolidated revenues grew by 58% YoY to INR19.3b, driven by 31% volume growth, 8% higher realizations and 19% favorable forex movement. Organic growth would be ~33%.
- Revenue growth was strong in all markets, except India. RoW markets grew by ~90% YoY (reflection of DVA acquisition), US recovery continued with ~62% YoY and EU business grew ~31%. India business grew by ~15% YoY.
- 3QFY12 had contribution of DVA Agro Brazil, which contributed ~INR3b to revenues (~25% to growth).
- US business's constant currency revenue growth would be ~30-35% in 3QFY12.

Revenue growth driven by organic and inorganic growth



Break-down of revenue growth (%)



Source: Company/MOSL

Trend in market mix (INR m)

| | 3QFY12 | 3QFY11 | YoY (%) | 2QFY12 | QoQ (%) | FY12E | FY11 | YoY (%) |
|------------------------|---------------|---------------|-------------|---------------|------------|---------------|---------------|-------------|
| Domestic Business | 3,810 | 3,320 | 14.8 | 5,690 | -33.0 | 18,270 | 14,940 | 22.3 |
| Contribution (%) | 19.6 | 26.6 | | 31.7 | | 22.3 | 25.3 | |
| International Business | 15,580 | 9,160 | 70.1 | 12,260 | 27.1 | 63,505 | 44,050 | 44.2 |
| Contribution (%) | 80.4 | 73.4 | | 68.3 | | 77.7 | 74.7 | |
| US | 3,590 | 2,220 | 61.7 | 2,990 | 20.1 | 16,358 | 12,830 | 27.5 |
| Contribution (%) | 18.5 | 17.8 | | 16.7 | | 20.0 | 21.7 | |
| EU | 2,650 | 2,020 | 31.2 | 2,230 | 18.8 | 13,475 | 12,250 | 10.0 |
| Contribution (%) | 13.7 | 16.2 | | 12.4 | | 16.5 | 20.8 | |
| RoW | 9,340 | 4,920 | 89.8 | 7,040 | 32.7 | 33,672 | 18,970 | 77.5 |
| Contribution (%) | 48.2 | 39.4 | | 39.2 | | 41.2 | 32.2 | |
| Total | 19,390 | 12,480 | 55.4 | 17,950 | 8.0 | 81,775 | 58,990 | 38.6 |

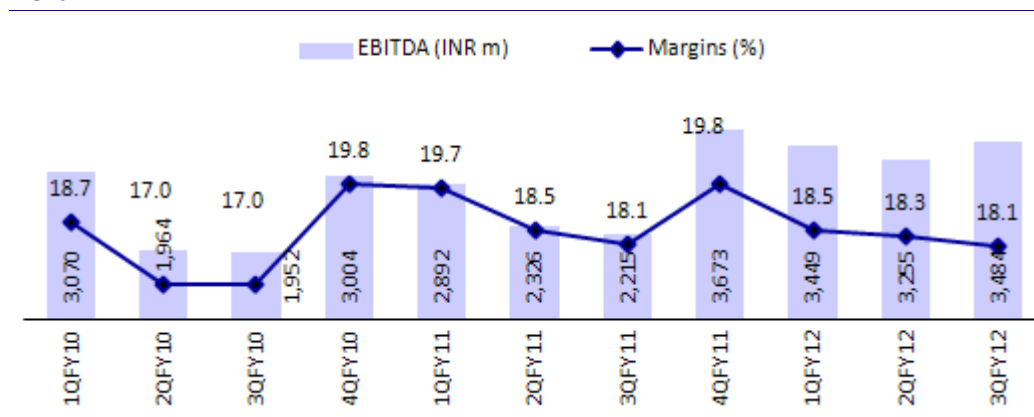
Source: Company/MOSL

RM cost, higher contribution of Brazil business impacts margins

- Gross margins declined by 210bp YoY to 36.6%, impacted by higher RM cost and higher contribution from Brazilian acquisition (enjoys gross margins of 28-30%). However, higher operating leverage diluted impact of RM cost push, resulting in flat YoY (-20bp QoQ) EBITDA margins to 18.1% (v/s est 19%).
- Staff cost was higher by ~29% QoQ due to full consolidation of DVA Agro (Brazil) and weak INR.
- As a result, EBITDA grew by 57% YoY to INR3.48b (v/s est INR3.54b). Further, higher tax restricted adj PAT growth to ~36% to INR1.14b (v/s est INR1.44b).

- During 3QFY12, it provided for net forex loss of INR16m (net of ~INR800m gain on forex hedges) and extra-ordinary expense of INR13m relating to recent acquisitions of SIP UPL Brazil and DVA Agrocem Brazil.
- The management indicated that managing RM cost and working capital would be a key challenge going forward, despite strong demand environment.

Trend in EBITDA



Source: Company/MOSL

Common Size Statement (%)

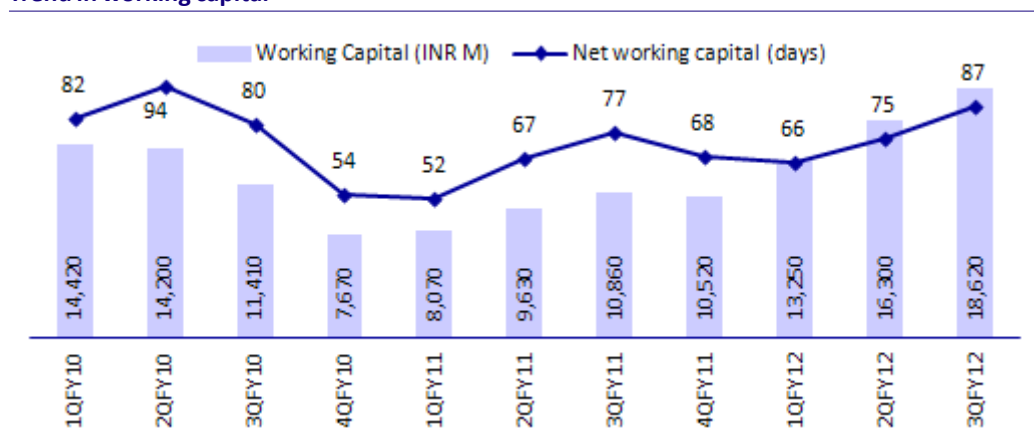
| | 3QFY12 | 3QFY11 | Chg (bp) | 2QFY12 | Chg (bp) | FY12E | FY11 | Chg (bp) |
|---------------|-------------|-------------|------------|-------------|------------|-------------|-------------|------------|
| Sales | 100 | 100 | | 100 | | 100 | 100 | |
| RM Cost | 53.4 | 46.6 | 680 | 54.6 | -120 | 54.6 | 51.5 | 310 |
| Staff Cost | 10.1 | 10.6 | -50 | 8.5 | 160 | 8.6 | 8.9 | -30 |
| Other Exp | 18.4 | 24.7 | -630 | 18.5 | -10 | 18.2 | 20.5 | -240 |
| EBITDA | 18.1 | 18.1 | -10 | 18.3 | -30 | 18.7 | 19.1 | -50 |

Source: Company/MOSL

Working capital cycle continues to increase

- Working capital has further increased during 3QFY12, after seeing substantial savings since 4QFY09. During 3QFY12, working capital increased by 10 days YoY to 87 days (v/s 75 days as on Sep-11).
- Its overall investment in working capital is at INR18.6b (v/s INR10.8b as of 3QFY11 v/s INR16.3b as of 2QFY12).
- Increase in working capital is reflection of strong demand growth, increasing presence in Brazil which has higher working capital intensity, and building inventory for peak season in US, EU and LatAm.

Trend in working capital



Source: Company/MOSL

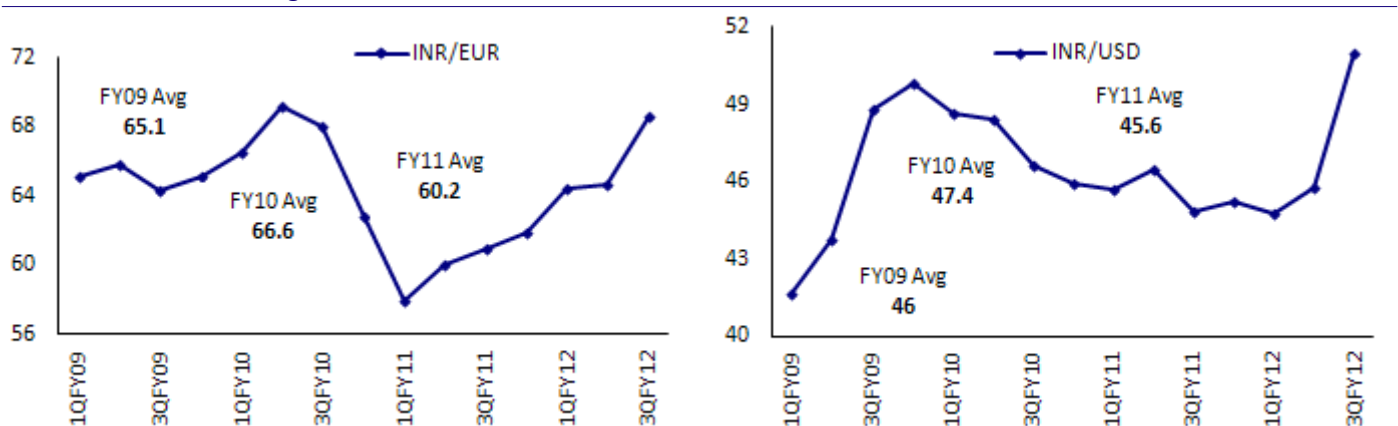
Maintains guidance

- For FY12, it has maintained its guidance for revenue to 35-40% growth as demand environment is very robust. Its guidance implies organic growth of 20-22%.
- It has guided for EBITDA margins of 19-20% as RM cost continues to tighten.
- However, it has increased tax guidance to 23-25% (v/s ~20% earlier), implied PAT growth of ~10%.

Business gaining momentum as headwinds turning into tailwinds

- UNTP’s FY10 and FY11 performance was impacted by macro headwinds, adverse climatic patterns in key geographies, adverse INR movement against EUR and USD and price erosion. This coupled with lack of any acquisitions due to expensive valuations, resulted in 8% revenue CAGR (FY09-11), ~90bp margin erosion and marginal PAT decline.
- However, business environment for the agro-chemical industry is expected to witness gradual improvement in operating environment, driven by strong agri-commodity prices and low base effect. Also, adverse impact of pricing and forex movement is expected to be reverse.
- Over next 5 years, it is targeting revenue CAGR of 15% driven by strong growth in emerging markets and ~USD5.5b products going off-patent over next 3-4 years. Also, it is working towards improving margins to 24-25% (pre-Cerexagri acquisition level) by further strengthening its cost competitiveness and increasing share of branded products.
- Further, with acquisitions of SIB and DVA Agro Brazil, it has established a strong foothold in one of the largest markets for agro-chemicals. While these acquisitions will be they key growth driver over next 2-3 years, they also reduce seasonality in its business as it now has reasonable presence in both northern and southern hemisphere.

Forex movement is turning favorable



Source: Company/MOSL

Other takeaways

- It indicated that it will take about 3-4 quarters for integrating DVA Agro (Brazil), post which it's gross margins should improve from current 28-30% to UPL's average of 37-38%.
- It has gross debt of INR39b and liquid cash of INR14b, with average interest cost of 7-7.5%.
- It plans capex (including maintenance capex) of INR3-4b in FY12.
- For Sipcam Isagro (Brazil), its associate company, it expects its share of loss of INR300m in FY12.

Valuation and view

- We are downgrading our EPS estimates by ~8% for FY12/ FY13 to INR13.8/ INR19.7, to factor in for higher staff cost and tax.
- Business environment for the agro-chemical industry is witnessing gradual improvement in operating environment.
- While long term outlook remains positive with realization of integration benefits from SIB and DVA Agro over next 3-4 quarters, there are no short term catalyst for re-rating of the stock.
- The stock trades at 10.4x FY12 EPS and 7.3x FY13 EPS. Maintain **Buy** with target price of INR196 (~10x FY13E EPS).

Revised estimates (INR M)

| | FY12E | | | FY13E | | |
|------------|--------|--------|---------|--------|--------|---------|
| | Rev | Old | Chg (%) | Rev | Old | Chg (%) |
| Net Sales | 81,097 | 80,256 | 1.0 | 92,417 | 92,503 | -0.1 |
| EBITDA | 15,151 | 15,838 | -4.3 | 17,852 | 18,965 | -5.9 |
| Net Profit | 6,378 | 6,908 | -7.7 | 9,082 | 9,870 | -8.0 |
| EPS (INR) | 13.8 | 15.0 | -7.7 | 19.7 | 21.4 | -8.0 |

Source: Company/MOSL

United Phosphorus: an investment profile

Company description

United Phosphorus is a USD1.3b company with a strong presence in crop protection and industrial chemicals. With around 80% of its revenues coming from international markets, the company has emerged as the third largest generic player in the world. United Phosphorus' growth strategy is built around filing its own registrations globally and acquiring tail end brands of global majors in regulated markets.

Key investment argument

- One of the largest (and most competitive) global generic players in crop protection – well poised to leverage the increasing conversion to generics globally.
- Improving cash flows gives it a war chest to scale up new registrations and acquisitions.
- Increasing share of global revenues (80% in FY10E) to improve profitability and reduce dependence on the volatile Indian market.

Key investment risks

- Volatility in raw material prices, rupee appreciation could subdue margins, if adequate price hikes cannot be taken.

- Business is working capital intensive, thereby restricting the free cash available to seed growth.

Recent developments

- Nil.

Valuation and view

- The stock trades at 10.4x FY12 EPS and 7.3x FY13 EPS.
- Maintain **Buy** with target price of INR196 (~10x FY13E EPS).

Sector view

- Short term business environment for the agro-chemical industry is challenging, but long term potential intact.
- High degree of consolidation in the market, strong entry barriers and limited price erosion make the generics opportunity very attractive for established players.
- Companies that have achieved critical scale and established strong relationships with major distributors are expected to benefit the most.

EPS: MOSL forecast v/s consensus (INR)

| | MOSL Forecast | Consensus Forecast | Variation (%) |
|------|------------------|-----------------------|------------------|
| FY12 | 13.8 | 15.2 | -9.2 |
| FY13 | 19.7 | 18.6 | 5.9 |

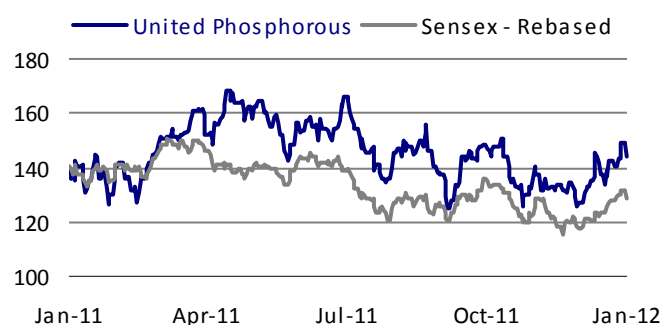
Shareholding pattern (%)

| | Dec-11 | Sep-11 | Dec-10 |
|---------------|--------|--------|--------|
| Promoter | 27.3 | 26.6 | 26.6 |
| Domestic Inst | 15.6 | 15.6 | 17.1 |
| Foreign | 37.9 | 39.3 | 38.0 |
| Others | 19.1 | 18.5 | 18.4 |

Target price and recommendation

| Current Price (INR) | Target Price (INR) | Upside (%) | Reco. |
|------------------------|-----------------------|---------------|-------|
| 144 | 196 | 36.1 | Buy |

Stock performance (1 year)



Financials and Valuation

| Consolidated Income Statement | | | | (INR Million) | |
|-------------------------------|--------|--------|--------|---------------|--------|
| Y/E March | 2009 | 2010 | 2011 | 2012E | 2013E |
| Net Revenue | 50,260 | 54,585 | 58,045 | 81,097 | 92,417 |
| Change (%) | 33.6 | 8.6 | 6.3 | 39.7 | 14.0 |
| Total Expenditure | 39,868 | 44,589 | 46,939 | 65,945 | 74,565 |
| EBITDA | 10,392 | 9,996 | 11,106 | 15,151 | 17,852 |
| Margin (%) | 20.7 | 18.3 | 19.1 | 18.7 | 19.3 |
| Depreciation | 1,927 | 2,147 | 2,138 | 2,917 | 3,281 |
| EBIT | 8,465 | 7,849 | 8,968 | 12,234 | 14,571 |
| Int. and Finance Charge | 2,919 | 1,938 | 3,120 | 4,208 | 3,466 |
| Other Income - Rec. | 418 | 343 | 937 | 678 | 720 |
| PBT before EO Expense | 5,964 | 6,254 | 6,784 | 8,704 | 11,824 |
| EO Expense/(Income) | 101 | 267 | 140 | 157 | 0 |
| PBT after EO Expense | 5,864 | 5,987 | 6,644 | 8,548 | 11,824 |
| Tax | 269 | 854 | 731 | 1,966 | 2,720 |
| Tax Rate (%) | 4.6 | 14.3 | 11.0 | 23.0 | 23.0 |
| Profit after Tax | 5,594 | 5,133 | 5,914 | 6,582 | 9,105 |
| Add: Share of profits of | 200 | 188 | -234 | -275 | 57 |
| Less: Minority Interest | 25 | 59 | 104 | 50 | 80 |
| Reported PAT | 5,769 | 5,262 | 5,576 | 6,257 | 9,082 |
| Adjusted PAT | 5,865 | 5,491 | 5,701 | 6,378 | 9,082 |
| Change (%) | 37.5 | -6.4 | 3.8 | 11.9 | 42.4 |
| Margin (%) | 11.7 | 10.1 | 9.8 | 7.9 | 9.8 |

| Consolidated Balance Sheet | | | | (INR Million) | |
|------------------------------------|--------|--------|--------|---------------|--------|
| Y/E March | 2009 | 2010 | 2011 | 2012E | 2013E |
| Equity Share Capital | 879 | 879 | 924 | 924 | 924 |
| Reserves & Surplus | 25,851 | 29,039 | 36,337 | 40,973 | 48,164 |
| Net Worth | 26,730 | 29,918 | 37,261 | 41,897 | 49,087 |
| Minority Interest | 95 | 140 | 180 | 188 | 197 |
| Total Loans | 20,914 | 24,308 | 25,215 | 38,333 | 38,333 |
| Capital Employed | 47,739 | 54,366 | 62,655 | 80,417 | 87,618 |
| Gross Block | 29,603 | 30,009 | 36,317 | 44,717 | 47,717 |
| Less: Accum. Deprn. | 12,348 | 12,286 | 13,109 | 16,026 | 19,308 |
| Net Fixed Assets | 17,255 | 17,723 | 23,209 | 28,691 | 28,410 |
| Capital WIP | 1,239 | 406 | 658 | 1,000 | 750 |
| Investments | 4,332 | 7,612 | 8,232 | 7,957 | 8,014 |
| Curr. Assets | 41,173 | 43,242 | 49,914 | 68,574 | 80,374 |
| Inventory | 16,849 | 10,084 | 14,055 | 21,107 | 24,054 |
| Account Receivables | 11,406 | 12,135 | 14,795 | 18,886 | 21,522 |
| Cash and Bank Balance | 5,539 | 15,778 | 15,659 | 17,139 | 21,759 |
| Other CA | 7,380 | 5,246 | 5,406 | 11,442 | 13,040 |
| Curr. Liability & Prov. | 16,260 | 14,616 | 19,358 | 25,805 | 29,931 |
| Account Payables | 15,402 | 13,591 | 18,117 | 22,218 | 25,320 |
| Provisions | 858 | 1,025 | 1,241 | 3,587 | 4,611 |
| Net Current Assets | 24,913 | 28,626 | 30,557 | 42,769 | 50,444 |
| Appl. of Funds | 47,739 | 54,366 | 62,655 | 80,417 | 87,618 |

E: MOSL Estimates

| Ratios | | | | | |
|-------------------------------|------|------|------|-------|-------|
| Y/E March | 2009 | 2010 | 2011 | 2012E | 2013E |
| Basic (INR) | | | | | |
| EPS | 13.3 | 12.5 | 12.3 | 13.8 | 19.7 |
| Fully diluted EPS | 12.7 | 11.9 | 12.3 | 13.8 | 19.7 |
| Cash EPS | 17.7 | 17.4 | 17.0 | 20.1 | 26.8 |
| BV/Share | 60.8 | 68.1 | 80.7 | 90.7 | 106.3 |
| DPS | 1.5 | 2.0 | 2.0 | 3.0 | 3.5 |
| Payout (%) | 13.8 | 20.0 | 18.2 | 24.6 | 20.8 |
| Valuation (x) | | | | | |
| P/E | | | 11.6 | 10.4 | 7.3 |
| Cash P/E | | | 8.5 | 7.1 | 5.4 |
| P/BV | | | 1.8 | 1.6 | 1.4 |
| EV/Sales | | | 1.2 | 1.0 | 0.8 |
| EV/EBITDA | | | 6.8 | 5.8 | 4.6 |
| Dividend Yield (%) | | | 1.4 | 2.1 | 2.4 |
| Return Ratios (%) | | | | | |
| RoE | 23.9 | 19.4 | 17.0 | 16.1 | 20.0 |
| RoCE | 20.6 | 16.1 | 17.0 | 18.1 | 18.2 |
| Working Capital Ratios | | | | | |
| Asset Turnover (x) | 1.1 | 1.0 | 0.9 | 1.0 | 1.1 |
| Debtor (Days) | 83 | 81 | 93 | 85 | 85 |
| Inventory (Days) | 122 | 67 | 88 | 95 | 95 |
| Leverage Ratio | | | | | |
| Debt/Equity (x) | 0.8 | 0.8 | 0.7 | 0.9 | 0.8 |

| Consolidated Cash Flow Statement | | | | | |
|----------------------------------|--------|--------|--------|---------|--------|
| Y/E March | 2009 | 2010 | 2011 | 2012E | 2013E |
| Profit/(Loss) before Tax | 8,603 | 8,522 | 9,998 | 10,943 | 14,386 |
| Direct Taxes Paid | -828 | -853 | -885 | -1,966 | -2,720 |
| (Inc)/Dec in WC | -7,304 | 4,024 | -1,884 | -10,732 | -3,055 |
| CF from Operations | 471 | 11,693 | 7,229 | -1,755 | 8,611 |
| EO Expense | 274 | -267 | -140 | 157 | 0 |
| CF frm Oper. incl EO exp | 197 | 11,426 | 7,089 | -1,598 | 8,611 |
| (Inc)/Dec in FA | -4,140 | -2,285 | -8,028 | -8,742 | -2,750 |
| (Pur)/Sale of Investmer | -731 | 76 | -1,620 | 275 | -57 |
| CF from Investments | -4,871 | -2,209 | -9,648 | -8,467 | -2,807 |
| (Inc)/Dec in Debt | 3,639 | 2,191 | 2,680 | 13,118 | 0 |
| Dividend Paid | -513 | -769 | -1,091 | -1,621 | -1,891 |
| CF from Fin. Activity | 3,127 | 1,423 | 1,590 | 11,497 | -1,891 |
| Inc/Dec of Cash | -1,547 | 10,639 | -969 | 1,432 | 3,913 |
| Add: Beginning Balance | 7,609 | 6,062 | 16,701 | 15,732 | 17,163 |
| Closing Balance | 6,062 | 16,701 | 15,732 | 17,163 | 21,077 |

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| 3. Broking relationship with company covered | No |
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