"UPL Limited
Q3 FY2020 Earnings Conference Call"

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ANALYST:	**MR. NITIN AGARWAL – IDFC SECURITIES**
MANAGEMENT:	**MR. DIEGO CASANELLO – GLOBAL CHIEF OPERATING OFFICER CROP PROTECTION - UPL LIMITED** **MR. RAJENDRA DARAK – GROUP CHIEF FINANCIAL OFFICER – UPL LIMITED** **MR. ANAND VORA – GLOBAL CHIEF FINANCIAL OFFICER – UPL LIMITED** **MR. ASHISH NARKAR – GENERAL MANAGER (INVESTOR RELATIONS) – UPL LIMITED** **MR. JAI SHROFF – GLOBAL CHIEF EXECUTIVE OFFICER – UPL LIMITED**

Moderator: Ladies and gentlemen, good day, and welcome to the UPL Limited Q3 FY2020 Earnings Conference Call hosted by IDFC Securities Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal the operator by pressing "*" then "0" on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Nitin Agarwal from IDFC Securities. Thank you and over to you Sir!

Nitin Agarwal: Thank you Lizaan. Good afternoon everyone and a very warm welcome to UPL Limited's Q3 FY2020 Earnings Call hosted by IDFC Securities. On the call, we have the entire senior management of UPL Limited on the call today. I hand over the call to Mr. Anand Vora, our Global CFO to take the call forward from here on. Please go ahead Sir!

Anand Vora: Thank you Nitin. Good afternoon everyone. We have with us here today Mr. Diego Casanello, he is our Global COO; we have Mr. Rajendra Darak, Group CFO; we have Ashish Narkar, General Manager, Investor Relationship; and myself, Anand Vora, the Global CFO. Mr. Jai Shroff will be joining us shortly. Before I go on to sharing with you the numbers for Q3 and for the 9 months period ended December, I would hand over to Diego to take us to give us an update on the market and maybe add some color on the financial results. Over to you Diego!

Diego Casanello: Thanks Anand. Good afternoon everyone. In the third quarter, we are pleased to have reported the year-over-year growth of 7% in revenue and 22% on EBITDA on a pro forma basis and with this performance we are significantly outperforming a difficult market, which year-to-date is expected to decline in the single digits.

Our teams around the world have done a terrific job, gaining market share in almost all territories, capitalizing on revenue synergies, launching great new innovations and strengthening our relationship with key farmers and distribution partners. UPL is offering today complete package solutions in key crops like soy in Brazil or cotton in India, and our offerings include both cost-competitive post patent products and innovative specialty products, making UPL a one-stop shop partner to many customers. We have the right breadth of portfolio and we have the scale.

We are also a reliable partner. We have today an international manufacturing footprint with core assets in India and many of our customers are seeking to reduce the risk, the supply risk after recent supply disruptions in China and we are offering, as we speak a welcome alternative to them.

Product margins have also improved. You will recall that in Q2 we reported weaker margins resulting from price pressure on a few of our products driven by low export prices from Chinese competitors. As we anticipated during our last earnings call in Q3 we managed to close the gap on product margins compared to the last quarter. This is the result of significant efforts to continue to strengthen our manufacturing cost leadership in key product lines as well as a strong focus on high-margin products like biosolutions and specialty herbicides.

Overall, year-to-date, we continue to close the initial gap on contribution margin despite the unfavorable geographical mix. In addition, we are well ahead in implementation of our fixed-cost synergy targets. We have made great progress with cost savings in warehousing, software and hardware licenses, insourcing of formulation, tolling activities, insourcing of experimental field trials, consolidation of offices, consolidation of plants and many more.

Throughout the entire time, we have put emphasis on speed of execution. In particular, when it came to announcing a new organization and providing clarity to our employees about the elimination of roles and the definition of new ones, we have been very, very fast.

A 9% reduction of our fixed overhead year-over-year in Q3 has contributed significantly to our EBITDA margin expansion of around 2 percentage points. In terms of our regional performance, the trade tensions between the U.S. and China, depressed demand for crop protection products in the U.S., and bolstered demand in Brazil. Our team in Brazil was able to outperform the market. They were able to drive revenue synergies from a very complementary customer and product portfolio in that country.

Our business in North America was affected by the shift in soy and corn demand to Latin America. Despite this fact we are gaining market share, especially share of wallet in many of our customers that are seeking to reduce the uncertainty of supply from China. We have seen share gains in some of our key herbicides, products like Interline, for example.

The Western European markets continue to slow. We have seen tough weather conditions impacting farmers in the first half. This has increased channel stocks of many competitors in that market and has impacted demand in the second half. We are seeing however market conditions in Q4 slowly improving.

As the leader in biosolutions, we are profiting from the higher focus of European farmers and distributors in this alternative ways of managing pests and abiotic stresses like drought. Europe is a great growth platform for UPL when it comes to biosolutions.

India has been a great contributor to our results in Q3 thanks to a strong Rabi season supported by heavy rains in large parts of the country. We also continue to gain market share in insecticide segments with high-value specialties, for example, like our product Ulala.

Coming back to UPL as a whole in the first 3 quarters of the year, total revenue has increased by 8% with EBITDA growth of 15%. On the back of these positive results, we are well positioned to achieve our targets for the year and therefore we want to reaffirm our revenue and EBITDA guidance for the full year.

On February 1, 2020, we were excited to celebrate the 1-year anniversary of the Arysta acquisition. We are very proud of the progress we have made in integrating 2 very large companies in only 12 months of time. We are seeing our teams across the world build a common culture based on the strengths of both companies, creating something new and exciting that really differentiates UPL in the market. We have become a very agile organization, and we are best positioned to shape the market in this new decade. We want to use the chance to say thanks to all our employees for this huge achievement and to thank farmers and partners for trusting us with their businesses. This personally gives me a lot of confidence to lead the way in the crop protection market and to deliver superlative financial results and value to our shareholders in the coming years. Thank you.

Anand Vora: Thanks Diego. Before taking you through to the key numbers for the third quarter, we take as having read the safe harbor statement and would also like to highlight that the financial results for the quarter and 9 months are being compared with the pro forma financials of the previous quarter and 9 months in order to make them comparable. The pro forma financial means the UPL plus Arysta combined financial results for the previous year.

I will now take you through the key numbers for Q3 FY2020. The gross revenue for the quarter ending December 2019 are Rs.8892 Crores as compared to Rs.8273 Crores for the quarter ending December 2018, a growth of 7%. The gross margins for Q3 increased to Rs.3726 Crores from Rs.3508 Crores in the previous year, an increase of 6%. Lower growth is attributed to revenue mix in the quarter. Revenues from Europe and U.S. were lower than last year resulting in overall lower gross margins.

EBITDA for the quarter was Rs.2075 Crores as compared to Rs.1697 Crores, a strong growth of 22%. EBITDA as a percentage of revenue was 23%, showing an improvement of 283 basis points over that of the same period last year. This strong showing was primary due to integration, cost synergies and other ongoing cost-saving initiatives.

Of the sales growth of 7%, we saw volume growth of 10%. There was a negative price variance of 1%, giving a constant currency growth of 9%. The exchange impact was unfavorable by 2%.

Comparing the financial results for Q3 FY2020 with Q3 FY2019, on an as-reported basis, the Q3 financial 2020 figures are excluding the PPA adjustment of Rs.7 Crores of variable costs relating to Bioquim acquisition. This is an acquisition, which we did in Costa Rica. Rs.48 Crores relates to depreciation and amortization, and Rs.19 Crores relates to deferred tax associated with the aforesaid 2 items.

The Q3 FY2019 figures are as reported in the previous year, which are UPL financials excluding that of Arysta, we saw revenue growth of 81% from Rs.4922 Crores to Rs.8892 Crores. EBITDA grew by 104% from Rs.1018 Crores to Rs.2075 Crores and profit after-tax associated income and minority interest was at Rs.811 Crores, a growth of 47% over that of the previous year. Exceptional costs in Q3 were Rs.75 Crores, this pertains to integration and severance costs.

The pro forma revenue breakdown in terms of geography is as follows:

Latin America had a growth of 21% from Rs.3462 Crores to Rs.4203 Crores. Europe had de-growth of 27% from Rs.1056 Crores to Rs.767 Crores. Rest of the world grew by 7% from Rs.1757 Crores to Rs.1884 Crores. North America degrew by 12% from Rs.1468 Crores to Rs.1288 Crores. India revenues posted a strong growth of 42% from Rs.530 Crores to Rs.750 Crores.

Moving on to numbers for the first 9 months of the financial year 2020 on a pro forma basis, we saw the gross revenues at Rs.24615 Crores compared to Rs.22744 Crores, a growth of 8%. Gross margins after excluding PPA adjustments of Rs.349 Crores went up to Rs.10396 Crores from Rs.9823 Crores in the same period last year, an increase of 6%.

EBITDA increased to Rs.5283 Crores from Rs.4572 Crores in the previous year, a growth of 16%. EBITDA as a percentage of revenue was 21%, an improvement of 136 basis points over that of the previous year.

The overall sales growth at 8% comprises of 10% growth in volumes, a decline of 1% in prices, giving us a constant currency growth of 9% and decline in 1% was due to the currency impact.

While comparing the financial results for first 9 months of FY2020 versus the same period in the previous year, as on reported basis, the figures excludes PPA adjustments of Rs.349 Crores in variable costs, Rs.88 Crores associated with depreciation and amortization and Rs.138 Crores related to deferred taxes associated with the above 2 items.

The first 9 months result of FY2019 figures are as reported in the previous year. These are UPL numbers excluding that of Arysta. We saw revenue growth of 85% from Rs.13312 Crores to Rs.24615 crores; EBITDA growth of 95% from Rs.2703 Crores to Rs.5283 crores; and profit after tax associated income and minority interest of Rs.1909 Crores, a growth of 37% over that of the previous year.

Exceptional costs of Rs.452 Crores for the first 9 months of FY2020 include Rs.217 Crores pertaining to the provisions for AgroFresh litigation verdict, and the balance was largely related to redundancy costs and other associated integration costs.

The pro forma first 9 months of financial year 2020 revenues broken down in terms of geography are as follows: Latin America revenues were at Rs.10372 Crores amounting to 42% of the total revenues and representing 23% growth over that of the previous year. Europe de-grew by 9% to Rs.3306 Crores. It represented 13% of our total revenues, rest of the world grew by 4% to Rs.4698 Crores representing 19% of our total revenue, North America de-grew by 4% to Rs.3103 Crores representing 13% of our total revenue and India region grew by 6% to Rs.3136 Crores, and it represented 13% of our total revenue.

As per the net working capital, as of December 2019 the net working capital remained flat at 126 days. Inventory levels were constant at 111 days. Receivables saw a decrease of 15 days to 124 days. Payables saw a decrease of 15 days to 109 days. The working capital days for both periods are based on trailing 12-month sales.

As we highlighted in our Q2 2020 earnings call, considering the seasonality of business, net working capital during the financial year increases quarter-on-quarter and it peaked in the third quarter ending December and thereafter we see a significant drop in Q4.

Now on to debt and cash levels as of Dec 2019, the gross debt stood at Rs.31612 Crores versus Rs.29370 Crores (as of Dec2018). Cash balance was at Rs.1958 Crores versus Rs.2859 Crores as of March 31, 2019. Hence, the net debt stood at Rs.29654 Crores showing an increase over March of Rs.3135 Crores. Of the Rs.3135 Crores, Rs.819 Crores is on account of exchange rate and therefore the net increase in debt is for the 9 months is Rs.2316 Crores.

Cash flow from the operations for the first 9 months stood at Rs.4961 Crores. Some of the other key cash numbers to impact the cash flows are as follows: We had an increase in working capital of Rs.2524 Crores. Capital expenditure spends for the 9 months was at Rs.1623 Crores. As explained earlier during the half year earnings call, we paid Rs.683 Crores additional towards working capital for the Arysta acquisition. We spent Rs.165 Crores towards acquisition of Bioquim, a company in Costa Rica; and onetime exceptional costs stood at Rs.203 Crores. There was a dividend outflow of Rs.436 Crores besides the interest payment of Rs.1257 Crores and tax payment of Rs.657 Crores.

As regards to synergies, we continue to remain on track or rather I would say we are ahead of our targets, which we have set for ourselves. As you know we had proposed a synergy cost savings of about $80 million translating about Rs.560 Crores for the full year. For the first 9 months, we have already got synergy benefits, which are credited to the P&L of about Rs.535 Crores roughly amounting to $76 million.

In terms of revenue synergies too, we are doing pretty good. We have delivered revenue synergies as of December 31, 2019 of Rs.746 Crores representing roughly in dollar terms at $106 million.

I would like to also highlight here that we have completed the purchase price allocation exercise. We had given this assignment to one of the big four chartered accountant firms and they have come up with their report. The total consideration, which we have paid for Arysta acquisition, which was Rs.31615 Crores, now we have the fair value of all the assets, and the breakdown is as follows: Intangible assets were about Rs.10665 Crores of the Rs.31615 Crores, tangible assets stood at Rs.1059 Crores, working capital was Rs.6076 Crores and we had other small amounts in terms of investments and tax liability, noncontrolling interest and other, resulting in a net amount of goodwill of about Rs.16652 Crores. So of the total consideration of Rs.31615 Crores there is a goodwill component of Rs.16652 Crores.

As a result, now that we have the final purchase price allocation numbers, we have to restate our depreciation and amortization numbers. As was reported in H1, we had depreciation and amortization of Rs.1185 Crores. The adjustment on account of PPA has been negative Rs.263 Crores. Depreciation and amortization for Q3 now stands at Rs.494 Crores. Therefore, the depreciation and amortization for the first 9 months now stands at Rs.1416 Crores.

I would also like to provide you an update as was reported in the press earlier. The income tax authorities have visited and conducted a search at multiple locations of the company premises in India. During the course of this process, they have collected documents and have interviewed key personnel of the company. Based on this, the company believes that they wanted to understand and review the company's international operations and transactions. We continue our engagement with the authorities and expect this process of review will continue for some time. The company conducts its business with all applicable provisions of law across the globe. The search and investigation by tax authorities were on UPL Limited and not on any individual or a group of individuals as reported in some media items.

With this, I would like to now move on to take question and answers. Thank you very much for your attention.

Moderator: Thank you. The first question is from the line of Nihal Jham from Edelweiss. Please go ahead.

Nihal Jham: So my first question was on the U.S. and the Europe region. I do understand there has been a bit of de-growth, so first of all just wanted to understand that, is it that the market has also de-grown at a similar rate or was that specifically for us we have higher stocks because of which we have seen a bigger impact for this quarter?

Diego Casanello: Yes. Year-to-date, our performance in both Europe and North America remains above the market performance, so we are confident that we are gaining market share in those countries. Now to the situation in North America, in particular, there has been a shift of demand from North America to Brazil due to the trade tensions between the U.S. and China and especially on soybeans. We have capitalized on that in Brazil because we have a very high participation in Brazil. Let us say in Europe it is more really the impact of the weather extremes that we have perceived at the beginning of the year, hot and then very wet conditions that have depressed demand for several of our insecticide and fungicide brands, but let us say we are very confident that as soon as that market comes back and we are seeing actually recovering in this quarter we are going to be very well positioned to grow in those countries too.

Nihal Jham: Any specific reason both these markets seeing a sharp contraction especially in this quarter because in the earlier quarters you are seeing 4%, 5% kind of a run rate, but this quarter has been exceptionally sharp.

Diego Casanello: No, we have seen the weakness in those 2 countries already for some months already, so it is not new. I think one effect that you can sum in Q3 is that actually there are 2 things and one Arysta used to have in December it is closing. So we are now having actually our closing in March with the new UPL and part of that business that used to be done in December will move into Q4. That is one effect and then in Europe in particularly, in France there is a change basically in some regulations with respect to the ability of companies to offer incentives to basically to stocking and as that is not happening anymore, those regulations basically prohibit companies to do that. Then the sales into the French industry go basically closer or will be done closer to application and that means they move into Q4 and partially also into Q1 next year.

Anand Vora: Also just to add to what Diego said. Last year 2019 particularly in France we had a robust sales of some of our products because there was from January 1, 2019 there would be ecotax, which was being levied and that coming in the play resulted in a lot of purchases being done by farmers and distributors just to avoid the ecotax, which would be getting applicable from January 1, 2019. So we had a robust last quarter in the previous year then therefore when you see this, you see a huge dip in Q3 this year.

Nihal Jham: What would be France's share approximately in Europe?

Anand Vora: France would be about 20% odd of our Europe sales.

Nihal Jham: I have a few more questions. I will get back in the queue.

Moderator: Thank you. The next question is from the line of Sonali Salgaonkar from Jeffries. Please go ahead.

Sonali Salgaonkar: Sir my question is regarding what is the impact that you perceive of the coronavirus in various geographies or products of Europe and secondly on the pricing power now it is about 3 quarters that we are seeing some subdued pricing power, so your comment on the global channel inventories, Sir?

Diego Casanello: So it is early to say, right, because we are seeing this unfolding and to make a prediction right now I think it would not be prudent. We are obviously watching. We are well positioned because most of our manufacturing footprint is here in India. Some of our customers are starting to ask, let us say, for material because they want to hedge their positions. Let us say that it is too early to say I think we need to watch in general, I think what I can tell you are that we are very well covered from the standpoint of our risk management approach so you should be concerned about seeing disruptions in our business moving forward.

Sonali Salgaonkar: Then on the pricing power?

Diego Casanello: Can you repeat that question because acoustically we could not hear it, sorry?

Sonali Salgaonkar: Sure. So for the past 3 quarters we have been seeing subdued pricing power as compared to say 9 months FY2019 so any comment on the global channel inventories?

Diego Casanello: So let us say, there is a certain segment of our business that is competing with some products that are coming from China and thus we have seen in the last quarter some of that price in China came down and we have to follow and go actually to make sure that we secure and increase our volumes, but as we speak in Q3 and that we were already forecasting this in Q2 we are actually seeing a recovery of our margins. Also in those segments because we are taking cost out, production cost out in particular and in general we are moving our business more and more towards higher-value products and especially our biosolutions business. So overall if you look at our margin performance quarter-to-quarter, you see an improvement, and we are confident that we are also capitalizing in the next few quarters from, call it, lower raw material prices, right, that you have not seen in the first half, but you should see moving forward.

Moderator: Thank you. The next question is from the line of Saurabh Jain from HSBC. Please go ahead.

Saurabh Jain: Again, my question is on the U.S. and Europe geographies. So you highlighted that there you are now already seeing some improvement in this quarter, but will this going to be a significant improvement or what performance in Q3 like a 12% decline and 27% decline in these 2 geographies, can it be a significant growth because I believe fourth quarter the revenue mix is more in favor of U.S. and Europe?

Diego Casanello: So you will see an improvement or we are expecting to see an improvement. Obviously, in the U.S. right now we are off-season, so the industry is preparing for the next season. So we have to see how weather unfolds. If you look at the weather conditions last season, this has been really an extreme situation in both the U.S. and Europe. I do not want to make weather predictions, but we are hoping that we will see a more normal situation and as we gain share of wallet in most of our key customers and we are gaining market share in herbicides in the U.S., for example. We are gaining market share with our fungicide lines in Europe, with biosolutions, once that market comes back, we should profit not only for more revenue, but also from the higher margin of those regions.

Saurabh Jain: So like you mentioned that there was a pricing pressure in Q3 so is that already behind and we are gaining margins in these geographies?

Diego Casanello: So the margin pressure we have seen was particularly in Q2 and in Q3 if you look at our margin profile despite the geographic mix because we are doing more business in this quarter with LatAm, which is lower margin compared to Europe and North America so despite that our margins is very, very close to last year. I think it is only actually, yes, 42%, 42%. So that shows you that we are actually improving the margin power overall.

Saurabh Jain: So I just wanted to highlight that even if you strip out the cost synergies from this quarter's numbers, it seems that our core business margins have improved almost like 200 bps, so is this solely attributable to significantly improving margins in U.S. and Europe?

Diego Casanello: The improvement quarter-to-quarter on gross margins is because 2 things: one is the product mix, second is also COGS synergies, so we are executing on synergies in our cost of goods and that is helping us and also there is some raw material improvements that are going to be even more present in next quarter and that is offsetting the unfavorable, call it, regional mix, right, which is more structural, call it, right, not related to a situation right now in terms of pricing pressure.

Saurabh Jain: You believe this will be sustainable?

Diego Casanello: Yes, we believe, from this point in time, we believe this is sustainable.

Saurabh Jain: I will get back in the queue. Thank you.

Moderator: Thank you. The next question is from the line of Neha from JPMorgan. Please go ahead.

Neha: Sir, in your opening remarks, you mentioned that we are tracking ahead of our target for both fixed cost and for revenues. First, is there an upside risk to our cost synergies that we have guided to for the year and therefore from the acquisition and second could you give us a little color on where we are seeing the revenue synergies coming from?

Anand Vora: On the cost side, I do not see a risk because we have said that we were targeting $80 million or about Rs.560 Crores and by end of 9 months we were at Rs.535 Crores. So we will clearly end the year much ahead of what we had guided for, so we are pretty much on track. On the revenue synergies I will ask Diego to share his views.

Neha: I was asking if there is an upside to the target that you would given for the 3 year, for the total cost synergies that we have indicated?

Anand Vora: For this year, we are trending ahead of target and therefore I assume because these are synergies which are there particularly the personnel, those will remain. Those will not go away. So clearly, based on what we have seen in the 9 months numbers, we are ahead, and we will end up much more than what we had guided for.

J.R. Shroff: Yes. So just to answer your question this is Jai. I think as we progress and reorganize these 2 large companies, we believe that there will be some more opportunities to streamline business operations and those are work-in-progress. We believe that there is a good chance as we continue to rationalize and look at target areas where we need to focus for our growth. A bit early to specify amounts, but we believe there is room for improvement.

Diego Casanello: Yes. On the revenue synergies, we are seeing good progress in geographies like, for example, in Latin America, in Europe. In Latin America, for example, if I think about Brazil, legacy UPL used to be very strong in the Mato Grosso region, and legacy Arysta used to be strong with the coops in the south of Brazil. So here, obviously, cross-selling opportunities are helping a lot, and both customer groups have accepted the new UPL very well. We see also revenue synergies from a complete portfolio offer. So we are developing offers in most crops, actually, that we call

ProNutiva. ProNutiva solutions are combinations of conventional crop protection and biosolutions to target higher yields, to target higher profitability for farmers, reduce residues in the food and this is actually tractioning very well across the world, and it is a real synergy from the combination of both companies.

Neha: Understood. Thank you so much.

Moderator: Thank you. Ritesh, your line is unmuted. Please go ahead.

Ritesh Gupta: Just on the directional side on the gross margins, before the Arysta acquisition UPL was consistently expanding the gross margins over FY2014 to FY2019 and this year we are seeing some bit of pressure on the gross margin side. Could you just give us some direction on let us say next 2- to 3-year gross margins how should we think about it, are there some initiatives that the management is taking so that gross margins can improve further, so if you would just talk about that?

Anand Vora: Sure. So as I mentioned, largely, this quarter and maybe for the 9 months, the gross margin drop is largely on account of the geographical mix. As you know, Europe and U.S. are large contributors, they have better margins compared to some of the LatAm countries and other parts of other geographies. So we believe that this is not a permanent phenomena where we will always have some geographies doing better, some not doing better depending upon the weather conditions and I think the 42%, 43% gross margins, which we see are proper reflection of our business as we move more and more business to branded products and specialty products besides the biosolutions portfolio that we have today so we would like to say that we will continue to see improvements in these margins as we move forward.

Diego Casanello: I think what Anand is saying, I think if you look at our EBITDA margin, it is expanding also compared to the status quo of legacies before and as these markets come back on stream that we have the potential here to significantly expand margins in the future.

Ritesh Gupta: Sure and on the manufacturing side are you taking some initiatives to like kind of backward integrate Arysta a bit?

J.R. Shroff: So yes, I mean we are large here, but we are constantly looking at improving our cost position. We have developed a whole team of outsourcing over the last 4 years. We have been talking about it on and off. A lot of key intermediates, which we are either making ourselves or outsourcing to get our costs in line and just staying in line. A lot of these projects are in progress. We believe further to your earlier question also that this will significantly impact our competitiveness over the period. We have been closely working with all the partners we have in Japan and other business partners, which we have inherited from the legacy Arysta business. We have been able to increase volumes and we have been able to talk to them about reducing costs. All those things we believe will kick in any time from the first quarter this year onwards. So we think that renegotiating a lot of these supply agreements is going to help us to be much more competitive. As you can see that across the board, UPL had gained market share, in almost every market and every product category, we have gained market share and that will really help us to the cost benefit of renegotiating and making some of the key intermediate ourselves also and will help us to improve our margins in some of those markets where we are losing market share.

Moderator: Thank you. The next question is from the line of Bharat Shettigar from Standard Chartered Bank. Please go ahead.

Bharat Shettigar: A couple of questions. Firstly, on the $500 million debt reduction target, if I look at the first 9 months number, net debt has actually gone up by about Rs.3000 odd Crores so can you throw some color on how we are tracking the debt number for the full year?

Anand Vora: Sure, Bharat. So Bharat, as I mentioned 2 things: One is out of the Rs.3200 odd Crores Rs.819 Crores is attributed to the exchange impact, so this is notional. We have a net increase of Rs.2316 Crores. Also I did mention that due to the seasonality of our business, we see working capital going up quarter-on-quarter until Q3 and then you will see a sharp decline in Q4, which is largely as we see the money being collected out of Latin America as well as most of our sales in Q4, which is largely the season for Europe and U.S. where it is off-season now, but the placements for the next season begins now and most of this we use the nonrecourse financing which results in money, but therefore the sharp reduction in working capital as we convert most of our inventory into cash and therefore as of now we are quite confident of giving the guidance, which we have given in terms of debt reduction of $500 million and maybe off by about $20-25 million there, but we are all working towards seeing that we accomplish this target.

Moderator: Thank you. The next question is from the line of Girish P from Morgan Stanley. Please go ahead.

Girish P: Just on the new subsidiary that was formed, AFS Agtech Private Limited, I think, on the contract farming, that if you can just explain the thought process on that one and the acquisition that you have made during the quarter, if you could give some color around annualized revenue a bit and PAT for that and the business of that entity as well?

J.R. Shroff: So happy to answer that. UPL has a lot of unique technologies and to bring some of these technologies, we have to have a very close relationship with farmers, and we have been expanding. Some of you may have seen or maybe heard that we have a large service business. This service business is more and more being driven through technology platforms and we have created a special SPV for this because we are hiring talent who come from the tech world and much easier to get them excited if we have an end-to-end visibility of their performance. We are looking at enabling a number of technology platforms including some kind of resilience products and some other very useful things to improve farmers' protection from this. We can elaborate details later on, but there is a lot of new technology being rolled out and that team will operate within the AFS Company as a separate SPV. It is a completely tech-driven platform.

Anand Vora: The acquisition, as we shared with the announcement it is a company in China. Needless to mention some of the work at this stage is at standstill in terms of diligence. Our team has been there for diligence and the diligence is going on.

J.R. Shroff: They are not there now.

Anand Vora: Not there now. They have gone and we have pulled them back. Jai, thanks and we expect to close the transaction maybe effective March 31, 2020, but all depends on how the situation normalizes over the next few, let us see how the situation normalizes.

Moderator: Thank you. The next question is from the line of Vishnu Kumar from Spark Capital. Please go ahead.

Vishnu Kumar: Specifically on Brazil, we have grown super strong for the entire year and if the U.S.-China trade deal gets resolved, should we see some shift in the agri flow from Brazil to U.S. and how would that impact us?

Diego Casanello: So the growth that you see also in Latin America, it is not only in Brazil, by the way, it is also all the Andean region, which has grown significantly and these are export markets in terms of food export markets and specialty crops and in Brazil the story is not only in terms of the overall market for us, but it is also our market share, we are increasing market share in Brazil significantly, not only on soybeans but also on corn, on specialty crops, on sugarcane, on cotton. So it is, let us say, broader than just a shift in demand from the U.S. If the U.S. comes back next year there might be some impact on soybeans, but we do not feel that this impact is currently significant.

Diego Casanello: Exactly. Because U.S. will pick up, but our business in Brazil is actually distributed among many crops.

J.R. Shroff: Yes, just to add to that, if what we hear on the trade deal and that is executed, U.S. will see a big growth. Our market share in U.S. has grown substantially. This year we believe we have gained a lot of market share and that will continue. Sentiment will improve and we think a substantial part of that will move towards there.

Vishnu Kumar: With the revised allocation price for Arysta what impact would it have on the P&L, my sense is about 100 odd Crores in depreciation, is there any other number that you change in the P&L?

Anand Vora: No, that is not. Nothing else. Primary is that and there is some small change in the COGS, but beyond that there is not much change. Small change in the cost of goods sold, which we have shared in the press release. You have those numbers.

Moderator: Thank you. The next question is from the line of Sumant Kumar from Motilal Oswal Securities. Please go ahead.

Sumant Kumar: So when we talk about the product mix changes, so can you describe which product mix changes in Latin America and India, like glufosinate, you are growing at faster pace, so that is the product mix can you give us other example in India and Latin America?

J.R. Shroff: In India, we have seen good growth on the cotton segment. Actually the soybean segment was washed out. So that category of products, we had a real setback in soybean this year. I think it will recover very nicely. My expectation is with the import duty on palm oil should see a benefit in the coming year, in terms of product mix it is so much related to the crop, and crop will be done very well in Maharashtra, particularly in the grape-growing area. We have probably the industry leading growth. Our India business has done exceptionally well this year. They have really done exceptionally well across the board. So I do not know whether we give out more specifics on product categories.

Diego Casanello: Yes. We do not disclose product margins, obviously, but we can also say is that we have a growing pipeline of new products and as we speak we are launching new products in many geographies. We have already mentioned in our Capital Markets Day that we have valued the big sales potential of our pipeline in more than $3 billion and these products are higher in margin because they are differentiated. So this, obviously, as we continue to advance this helps our margin profile too. Biosolutions are higher in margin in general and we have the #1 in biosolutions and we are growing double digit. That is helping our margins. We have several key blockbuster products in the area of herbicides and insecticide that has been launched in the last, I would say, 5 to 7 years that continue to grow. So all this is structuring our mix in the right way.

Moderator: The next question is from the line of Shalini Vasanta from DSP Mutual Fund. Please go ahead.

Shalini Vasanta: Sir, on the acquisition debt, I understand you have a loan covenant of 3.5x debt-to-EBITDA, which as we reach the March 2020, would you be able to meet that or are you trying realize that?

Anand Vora: No. I do not know where you got that number from. That is not the right number. We retain our investment grade and the rating agencies have given us time until March 2021 to bring down from our current levels to what is expected of an investment grade company. So our current levels are based on our expectation we should end the year with about 3.2, 3.3 net debt-to-EBITDA.

Moderator: Thank you. The next question is from the line of Prashant Nair from Citigroup. Please go ahead.

Prashant Nair: Yes. So just one question on the gross margin level so I understand last couple of quarters have been impacted by the geographic mix. Once, say, your mix normalizes in this new entity from UPL plus Arysta, where will your gross margin settle you had reached around 41% to 42% range, maybe around 40% to 43% range a few quarters back. Is that the kind of normalized level we should be looking at or would it be a bit different?

Diego Casanello: I think that 42%, 43%, what you are seeing how margin trends right now, that are the normal level, I would say and yes you can take that as a reference.

Prashant Nair: Thank you. That is it from me.

Moderator: Thank you. Ladies and gentlemen that was the last question. I now hand the conference over to Mr. Nitin Agarwal for his closing comments.

Nitin Agarwal: Comments Sir before we close the call.

Anand Vora: That is it. Thank you very much. Thanks Nitin and your team for hosting us and thank you ladies and gentlemen for joining us on this call. Thank you very much. If there is any followup questions, feel free to reach out to Ashish Narkar or myself and we will be happy to answer the questions. Thank you.

Moderator: Thank you. Ladies and gentlemen, on behalf of IDFC Securities, that concludes this conference call. Thank you for joining us. You may now disconnect your lines.