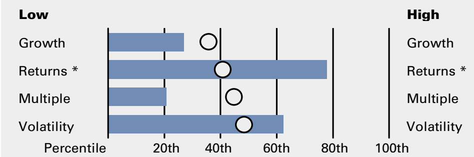
February 13, 2009

ACTION
Buy
United Phosphorus (UNPO.BO)
Return Potential: 29%

Relatively defensive stock; limited earnings downside; Buy

Source of opportunity
We reiterate our Buy rating on United Phosphorus (Uphos) with a 12-month P/B-based TP of Rs120, implying potential upside of 29%. We view the crop protection industry as relatively defensive in the agriculture space since basic demand for crop protection products exist even at low crop prices for the following reasons: 1) they act as insurance for maintaining farm yields; and 2) they constitute only about 10%-15% of total farm costs. Moreover, we believe Uphos, unlike Indian fertilizer companies, is operating in a fully unregulated environment and hence has the most compelling investment argument in the sector. We believe Uphos can generate EPS CAGR of 15% over FY09E-11E.

Investment Profile



United Phosphorus (UNPO.BO)

Asia Pacific Chemicals Peer Group Average

* Returns = Return on Capital

For a complete description of the investment profile measures please refer to the disclosure section of this document.

Catalyst
1) Improvement in margins through successful integration with Cerexagri, likely to reflect from 1QFY10E; 2) management delivering on inorganic growth through acquisitions; and 3) new registrations in key markets such as Europe and Latin America.

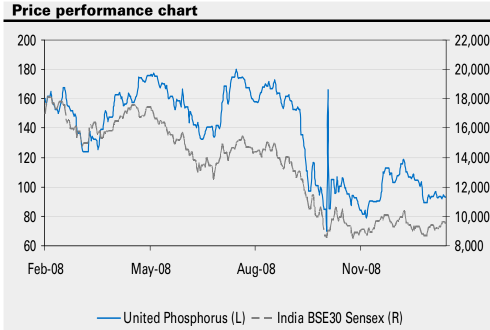
Key data	Current
Price (Rs)	92.85
12 month price target (Rs)	120.00
Market cap (Rs mn / US$ mn)	20,194.9 / 413.4
Foreign ownership (%)	--

	3/08	3/09E	3/10E	3/11E
EPS (Rs) New	**5.80**	**9.86**	**12.24**	**13.03**
EPS revision (%)	0.0	(3.4)	0.6	8.2
EPS growth (%)	(17.3)	69.8	24.2	6.4
EPS (dil) (Rs) New	**5.80**	**9.86**	**12.24**	**13.03**
P/E (X)	16.0	9.4	7.6	7.1
P/B (X)	1.7	1.5	1.3	1.1
EV/EBITDA (X)	10.7	6.3	5.3	4.7
Dividend yield (%)	2.2	2.0	2.0	2.0
ROE (%)	15.0	19.5	20.5	18.4

Valuation
Our 12-month P/B-based target price of Uphos is Rs120, which implies a P/E of 10X FY10E EPS. The company is likely to report ROE of more than 20% in FY10E, as per our estimates. We estimate DCF value for Uphos of Rs146. We adjusted our FY09/10/11E EPS estimates by -3%/+1%/+8% to factor in our revised volume assumptions and higher finance costs in FY09E.

The stock is currently trading at 7.6X FY10E P/E against its historical trading band of 6.0X-18.0X. While the company has demonstrated its organic growth capabilities in FY08, we note that it may have to pursue in-organic growth opportunities in order to sustain current volume growth.

Price performance chart



Share price performance (%)	3 month	6 month	12 month
Absolute	(6.3)	(46.5)	(41.9)
Rel. to India BSE30 Sensex	(5.6)	(14.0)	1.9

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 2/12/2009 close.

Key risks
1) Margin erosion due to inability to pass on price increases to consumers; 2) the possibility of future equity dilution for inorganic growth; 3) pledged shares coming into the market.

INVESTMENT LIST MEMBERSHIP
Asia Pacific Buy List

Coverage View: Cautious
India:
Agriculture

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United Phosphorus: Summary financials

Profit model (Rs mn)	3/08	3/09E	3/10E	3/11E
Total revenue	**35,155.1**	**44,999.1**	**41,399.1**	**43,469.1**
Cost of goods sold	(24,317.0)	(30,284.4)	(27,116.4)	(28,646.1)
SG&A	(5,933.3)	(5,819.9)	(4,802.9)	(5,190.0)
R&D	--	--	--	--
Other operating profit/(expense)	2,150.6	0.0	0.0	0.0
EBITDA	**7,055.4**	**8,894.8**	**9,479.8**	**9,633.0**
Depreciation & amortization	(1,522.7)	(1,949.1)	(1,793.2)	(1,882.8)
EBIT	**5,532.7**	**6,945.8**	**7,686.7**	**7,750.2**
Interest income	311.2	318.9	311.0	311.8
Interest expense	(1,688.0)	(2,537.4)	(1,786.3)	(1,252.9)
Income/(loss) from uncons. subs.	222.8	500.0	500.0	500.0
Others	0.0	0.0	0.0	0.0
Pretax profits	**4,378.7**	**5,227.3**	**6,711.4**	**7,309.1**
Income tax	(424.0)	(470.5)	(805.4)	(1,023.3)
Minorities	(9.8)	0.0	0.0	0.0
Net income pre-preferred dividends	**3,944.9**	**4,756.8**	**5,906.0**	**6,285.8**
Preferred dividends	0.0	0.0	0.0	0.0
Net income (pre-exceptionals)	**3,944.9**	**4,756.8**	**5,906.0**	**6,285.8**
Post-tax exceptionals	(1,144.0)	0.0	0.0	0.0
Net income	**2,800.9**	**4,756.8**	**5,906.0**	**6,285.8**
EPS (basic, pre-except) (Rs)	6.92	10.93	13.57	14.45
EPS (basic, post-except) (Rs)	6.92	10.93	13.57	14.45
EPS (diluted, post-except) (Rs)	5.80	9.86	12.24	13.03
DPS (Rs)	2.00	1.86	1.86	1.86
Dividend payout ratio (%)	28.9	17.0	13.7	12.9
Free cash flow yield (%)	(7.9)	(14.1)	13.4	11.4

Growth & margins (%)	3/08	3/09E	3/10E	3/11E
Sales growth	52.1	28.0	(8.0)	5.0
EBITDA growth	24.4	26.1	6.6	1.6
EBIT growth	37.8	25.5	10.7	0.8
Net income growth	(0.7)	69.8	24.2	6.4
EPS growth	(8.1)	58.0	24.2	6.4
Gross margin	30.8	32.7	34.5	34.1
EBITDA margin	20.1	19.8	22.9	22.2
EBIT margin	15.7	15.4	18.6	17.8

Cash flow statement (Rs mn)	3/08	3/09E	3/10E	3/11E
Net income pre-preferred dividends	3,944.9	4,756.8	5,906.0	6,285.8
D&A add-back	1,522.7	1,949.1	1,793.2	1,882.8
Minorities interests add-back	0.0	0.0	0.0	0.0
Net (inc)/dec working capital	(2,406.9)	(7,891.8)	1,494.7	(736.9)
Other operating cash flow	(2,797.4)	0.0	0.0	0.0
Cash flow from operations	**(646.7)**	**(1,685.9)**	**8,693.9**	**6,931.7**
Capital expenditures	(3,396.3)	(2,000.0)	(2,000.0)	(1,500.0)
Acquisitions	(2,650.1)	(2,600.0)	0.0	0.0
Divestitures	0.0	0.0	0.0	0.0
Others	724.8	0.0	0.0	0.0
Cash flow from investments	**(5,321.6)**	**(4,600.0)**	**(2,000.0)**	**(1,500.0)**
Dividends paid (common & pref)	(14.4)	(809.7)	(809.7)	(809.7)
Inc/(dec) in debt	(3,278.9)	6,920.0	(5,000.0)	(6,756.0)
Common stock issuance (repurchase)	10,527.7	0.0	0.0	0.0
Other financing cash flows	712.4	0.0	0.0	0.0
Cash flow from financing	**7,946.8**	**6,110.3**	**(5,809.7)**	**(7,565.7)**
Total cash flow	**1,978.5**	**(175.6)**	**884.2**	**(2,134.0)**

Balance sheet (Rs mn)	3/08	3/09E	3/10E	3/11E
Cash & equivalents	7,086.0	6,910.5	7,794.7	5,660.8
Accounts receivable	8,540.5	14,794.2	13,610.7	14,291.2
Inventory	10,853.4	13,539.0	12,142.8	12,823.0
Other current assets	4,240.6	4,240.6	4,240.6	4,240.6
Total current assets	**30,720.5**	**39,484.3**	**37,788.8**	**37,015.6**
Net PP&E	6,686.8	7,712.3	8,815.7	9,374.3
Net intangibles	3,195.6	2,221.1	1,324.5	383.1
Total investments	5,429.5	5,929.5	6,429.5	6,929.5
Other long-term assets	0.0	0.0	0.0	0.0
Total assets	**52,710.8**	**64,625.5**	**63,636.9**	**62,981.0**
Accounts payable	12,513.9	13,561.4	12,476.5	13,100.3
Short-term debt	0.0	0.0	0.0	0.0
Other current liabilities	959.0	959.0	959.0	959.0
Total current liabilities	**13,472.9**	**14,520.4**	**13,435.5**	**14,059.3**
Long-term debt	15,682.6	22,602.6	17,602.6	10,846.6
Other long-term liabilities	1,115.9	1,115.9	1,115.9	1,115.9
Total long-term liabilities	16,798.5	23,718.5	18,718.5	11,962.5
Total liabilities	**30,271.4**	**38,238.9**	**32,154.0**	**26,021.8**
Preferred shares	**0.0**	**0.0**	**0.0**	**0.0**
Total common equity	**22,379.6**	**26,326.7**	**31,423.1**	**36,899.2**
Minority interest	59.8	59.8	59.8	59.8
Total liabilities & equity	**52,710.8**	**64,625.5**	**63,637.0**	**62,981.1**
BVPS (Rs)	**55.28**	**60.51**	**72.22**	**84.81**

Ratios	3/08	3/09E	3/10E	3/11E
ROE (%)	15.0	19.5	20.5	18.4
ROA (%)	5.6	8.1	9.2	9.9
ROACE (%)	17.2	18.5	17.3	17.0
Inventory days	159.8	147.0	172.8	159.1
Receivables days	73.9	94.6	125.2	117.1
Payable days	187.8	157.1	175.2	162.9
Net debt/equity (%)	38.3	59.5	31.2	14.0
Interest cover - EBIT (X)	4.0	3.1	5.2	8.2

Valuation	3/08	3/09E	3/10E	3/11E
P/E (analyst) (X)	16.0	9.4	7.6	7.1
P/B (X)	1.7	1.5	1.3	1.1
EV/EBITDA (X)	10.7	6.3	5.3	4.7
Dividend yield (%)	2.2	2.0	2.0	2.0

Note: Last actual year may include reported and estimated data.

Source: Company data, Goldman Sachs Research estimates.

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Defensive stock in uncertain economic environment

Steady earnings growth with low downside risks

We forecasts Uphos to grow at 15% CAGR over FY09E-11E despite an uncertain economic environment. Since crop protection products act as insurance for maintaining yield and crop protection constitutes just about 10-15% of the total farm cost, we expect the basic demand to exist even in the scenario of declining crop prices. In our view, Uphos being one of the top 10 global agri-chem companies is better poised to serve this basic demand than many of its peers.

Exhibit 1: Our net income estimates for Uphos are 9%-14% below consensus
Net income estimates of GS, market implied and consensus

Rs mn	FY09E	FY10E	FY11E	CAGR FY09E-11E
GS estimates	4,757	5,906	6,286	15%
YoY growth		24%	6%	
Consensus estimates	5,223	6,675	7,328	18%
YoY growth		28%	10%	

Source: Bloomberg, Goldman Sachs Research estimates

Prices to decline reflecting reduction in raw material costs

We expect the end product prices to decline going forward reflecting low raw material costs. Some of the key raw materials such as white phosphorus declined by about 60%-70% from its peak, and we expect Uphos to correspondingly adjust its end product prices downwards. Uphos already marked down its high cost inventory acquired during 1HFY09, on concerns of raw material shortage. We expect the margins to remain flat as lower raw material costs results in lower revenues due to pass-through of cost savings.

However, Uphos management indicated that pass-through of costs savings may not be uniform across various products, and they may retain some costs savings leading to margin expansion. We expect the benefits of Cerexagri re-structuring to be reflected in the margins from FY10E onwards

Volumes key for earnings growth

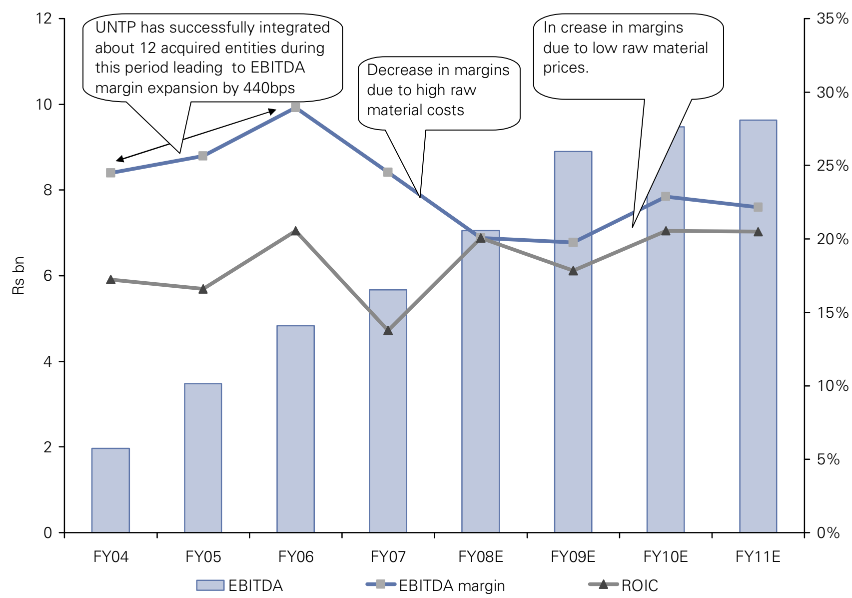
In a steady margin environment, volume growth is critical for earnings growth. The company currently has about 10%-14% of spare capacity available to meet the incremental volumes without incremental capex. We believe Uphos can achieve volume growth of about 6% in FY2010 through penetration of existing markets by fresh registrations and key Latin American markets, such as Argentina, Costa Rica and Ecuador.

Growth limited through organic route; in-organic growth may be required

United phosphorus delivered 17% organic volume growth for 9MFY09 in a very attractive operating environment. Keeping aside the above normal growth the industry witnessed in last 2 years, global agri-chemical industry grew at an average annual rate of 2%-3% since 1990. In the absence of pricing power as compared to the patented players, and in view of the low capex guidance, we believe it may be difficult for Uphos to deliver organic volume growth in excess of 10%-15%.

We believe Uphos may have to go for in-organic growth, either acquiring companies or the molecules coming off patent. We forecast the company to have US$150mn of cash on the balance sheet as of FY09E and with net debt/equity ratio of 0.6X they could leverage their balance sheet. A raising of US$200mn to fund any potential acquisition plans would imply a net debt/equity of 1.0X. Historically, Uphos has successfully integrated the acquired companies that resulted in EBITDA margin expansion of 440bps over FY04-06.

Exhibit 2: UNTP historically has demonstrated successful integration of acquired companies through improvement in EBITDA margins
Movement of EBITDA margins and Return on Invested capital



Source: Company data, Goldman Sachs Research estimates.

Data points indicate steady macro environment

Agri commodities out-performed rest of the commodity basket

Fundamentals in the agricultural have held up relatively better given the more-insulated nature of demand for grains and oilseeds that is partly tied to population growth and government-mandated bio-fuel usage and for lower-priced proteins that benefit as cash-strapped consumers trade down.

The agriculture commodities have performed well during the month of December 2008 when we saw most of other commodities testing their lows. This demonstrates the defensiveness of the agricultural commodities against global economic slowdown. **Even though the underlying demand for agri chemicals is less sensitive to commodity prices, we expect continued sustenance of agri commodity prices at current levels would help offer downside protection to the agri-chemical demand.**

US FDA projects increase in net farm income and lower debt levels

Net farm income is forecasted by the US FDA to be $86.9 billion in 2008, little changed from the record $86.8 billion farmers are estimated to have earned in 2007, and 42 percent above the 10-year average of $61.1 billion. The net to assets ratio of the farm sector is about 9% which is much below the peak of 22% in 1985.

European Union regulatory changes; no material impact

The proposals to impose greater restrictions on agrochemical industry have been voted by the European government in Jan 2009. However, the proposals need to be formally adopted by the ministers before becoming law.

The new regulation would replace the EU agrochemical registration directive (91/414), which would ban the active ingredients because of their hazardous properties rather than on the basis of the assessment of risk. Uphos management has indicated that most of their active ingredients do not come under preview of the proposed new regulation and they see little business impact if it were to become law. Also, the new regulation would impact only those Active Ingredients (AI) that are up for renewal.

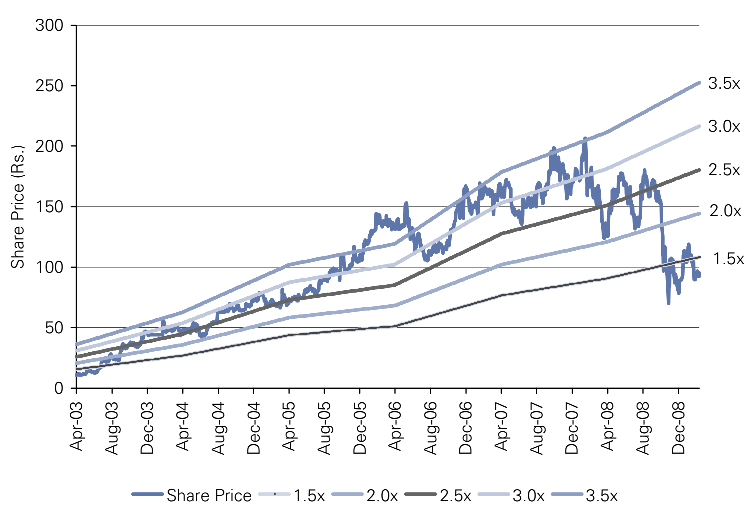
Target price of Rs120 implies potential upside of 29%

We valued Uphos on 12-months forward P/BV. Our target price of Rs120 is based on ROE adjusted trough P/BV multiple of 2X, which implies a P/E of 10X FY10E EPS. Uphos is trading at lows on P/B since 2005, even though ROEs have remained steady. We forecast Uphos ROE to be about 19% in FY10E, which is higher than FY05-09 average ROE of 18%. Having regard to the steady ROEs, de-rating of FY10 P/B from 3.5X to 1.3X is not warranted, in our view.

As per company disclosure to SEBI, Uphos has pledged about 5.1% of the shares in order to fund the subscription of warrants issues in FY08. UPL has allotted 62.2mn warrants to the promoters in Oct 2007 with a plan to buy 20.8mn shares every year over FY08-10. The promoters have so far converted 12.17mn warrants.

Exhibit 3: Uphos is currently trading at historic lows on P/B, even though the ROEs have been steady

P/B band chart of UNTP



Source: Datastream, Goldman Sachs Research estimates.

We adjusted our FY09/10/11E EPS estimates by -3%/+1%/+8% to factor in our revised volume assumptions and higher finance costs, following the release of the 3QFY09 results.

Exhibit 4: Uphos is trading at a discount to global comps on most valuation parameters

		Price	Market cap	P/E (X)			EPS growth (%)			P/BV			EV/EBITDA (X)			ROE (%)			Div yield
Company name	**Rating**	**Feb 11**	**(US$mn)**	**2008E**	**2009E**	**2010E**	**2008E**	**2009E**	**2010E**	**2008E**	**2009E**	**2010E**	**2008E**	**2009E**	**2010E**	**2008E**	**2009E**	**2010E**	**2008E**
Monsanto (US$)	Neutral	80.85	45,276	22.1	16.5	15.3	85.0	34.1	8.1	4.8	3.8	3.1	13.3	10.3	9.7	24.3%	25.5%	22.3%	0.9%
Syngenta (SF)	Neutral	235.80	25,690	17.3	23.9	NA	36.9	(27.6)	(10.4)	3.2	3.0	2.9	11.0	13.9	14.8	23.1%	15.0%	12.9%	2.4%
Anhui Huaxing Chemical (CNY)	NC	17.08	408	12.6	8.3	16.1	220.3	51.1	(48.2)	NA	NA	NA	12.7	13.5	13.3	24.5%	21.2%	19.6%	0.5%
BASF	Neutral	24.67	29,564	7.0	66.4	84.8	(16.2)	(89.4)	(21.7)	1.1	1.2	1.2	3.6	5.6	5.5	15.9%	1.6%	1.3%	8.1%
Bayer	Buy	42.76	42,614	11.2	15.3	14.4	0.8	(26.9)	5.6	1.8	1.8	1.8	6.7	7.9	7.8	17.5%	12.1%	12.7%	3.5%
United Phosphorus (a)	Buy	89.45	862	9.1	7.3	6.9	20.6	24.2	6.4	1.5	1.2	1.1	5.9	4.9	4.4	18.1%	18.8%	17.0%	2.1%
MAI	NC	1,580	1,276	7.5	7.0	6.5	NA	19.1	4.1	0.9	0.8	0.7	3.8	3.5	3.8	17.1%	17.8%	17.5%	NA
Nufarm (b)	NC	9.53	3,805	11.4	9.3	8.4	NA	37.5	11.4	1.5	1.3	1.2	7.5	6.2	5.9	17.0%	16.6%	16.2%	NA
Average				**13.0**	**12.5**	**11.3**	**72.7**	**15.9**	**(3.3)**	**2.3**	**2.0**	**1.8**	**8.7**	**8.6**	**8.5**	**20%**	**18%**	**17%**	**2%**

Note: (a) As of March 31 (e.g. the E for P/E 2007E is the E for the year-ending on March 31, 2008)
(b) Year ending July 31. Valuation multiples are calculated using 50% of previous year and 50% of the current year
For important disclosures, please go to http://www.gs.com/research/hedge.html

Source: Datastream, Bloomberg, Goldman Sachs Research estimates.

Reg AC

I, Durga Dath, hereby certify that all of the views expressed in this report accurately reflect my personal views about the subject company or companies and its or their securities. I also certify that no part of my compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

Investment profile

The Goldman Sachs Investment Profile provides investment context for a security by comparing key attributes of that security to its peer group and market. The four key attributes depicted are: growth, returns, multiple and volatility. Growth, returns and multiple are indexed based on composites of several methodologies to determine the stocks percentile ranking within the region's coverage universe.

The precise calculation of each metric may vary depending on the fiscal year, industry and region but the standard approach is as follows:

Growth is a composite of next year's estimate over current year's estimate, e.g. EPS, EBITDA, Revenue. **Return** is a year one prospective aggregate of various return on capital measures, e.g. CROCI, ROACE, and ROE. **Multiple** is a composite of one-year forward valuation ratios, e.g. P/E, dividend yield, EV/FCF, EV/EBITDA, EV/DACF, Price/Book. **Volatility** is measured as trailing twelve-month volatility adjusted for dividends.

Quantum

Quantum is Goldman Sachs' proprietary database providing access to detailed financial statement histories, forecasts and ratios. It can be used for in-depth analysis of a single company, or to make comparisons between companies in different sectors and markets.

Disclosures

Coverage group(s) of stocks by primary analyst(s)

Durga Dath: Asia Pacific Chemicals.

Asia Pacific Chemicals: Chambal Fertilisers and Chemicals, Cheil Industries, Far Eastern Textile, Formosa Chemicals & Fibre, Formosa Plastics, Hanwha Chemical, Honam Petrochemical, Kingboard Chemical Holdings, Kingboard Laminates Holdings, LG Chem, Nan Ya Plastics, Rashtriya Chemicals & Fertilisers, Sinopec Yizheng Chemical Fibre (A), Sinopec Yizheng Chemical Fibre (H), Tata Chemicals, United Phosphorus.

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Goldman Sachs expects to receive or intends to seek compensation for investment banking services in the next 3 months: United Phosphorus (Rs92.85)

Distribution of ratings/investment banking relationships

Goldman Sachs Investment Research global coverage universe

	Rating Distribution			Investment Banking Relationships		
	Buy	Hold	Sell	Buy	Hold	Sell
Global	23%	56%	21%	54%	48%	40%

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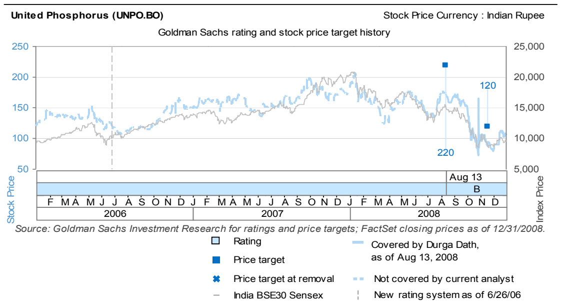
Price target and rating history chart(s)



The price targets shown should be considered in the context of all prior published Goldman Sachs research, which may or may not have included price targets, as well as developments relating to the company, its industry and financial markets.

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Disclosures required by United States laws and regulations

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