

Ashok Leyland

BSE Sensex	S&P CNX
19,692	5,980
Bloomberg	AL IN
Equity Shares (m)	2,660.7
M.Cap. (INR b)/(USD b)	58.8/1.1
52-Week Range (INR)	29/20
1,6,12 Rel. Perf. (%)	-7/-24/-38

CMP: INR22**TP: INR26****Buy**

Ashok Leyland's (AL) 4QFY13 operating performance was sharply below estimates. Net sales declined by 13.5% YoY to INR37.3b (v/s est INR36.7b). EBITDA at INR1.98b declined by 57.8% YoY (+94% QoQ). EBITDA margin at 5.3% (-560bp YoY, +100bp QoQ) was below est of 9.6%. Reported PAT at INR1.5b (-42% YoY, +102% QoQ) was boosted by extraordinary gains of INR1.3b and lower tax provision on MAT credit. Adj PAT declined by 90% YoY (-129% QoQ) to INR251m (v/s est INR1.23b).

Financials & Valuation (INR b)

Y/E March	2013	2014E	2015E
Sales	125.1	143.0	167.5
EBITDA	8.8	10.9	14.3
NP	1.7	3.0	5.6
Adj. EPS (INR)	0.6	1.1	2.1
EPS Gr. (%)	(70.4)	80.4	84.6
BV/Sh. (INR)	16.7	17.1	18.1
RoE (%)	3.9	6.7	11.9
RoCE (%)	6.5	7.9	11.0
Payout (%)	95.6	61.9	43.1
Valuations			
P/E (x)	35.2	19.5	10.6
P/BV (x)	1.3	1.3	1.2
EV/EBITDA (x)	10.9	8.9	6.8
Div. Yield (%)	2.7	3.2	4.1

Earnings call highlights:

- Expects demand to bottom out in 1HFY14; FY14 domestic MHCV industry and AL growth guided at 3-4% and 4-5% respectively. FY14 LCV volumes (Dost, Stile, Partner) to increase by over 50%.
- Focus to reduce discounts from INR130,000/unit in 4QFY13 to ~INR100,000 in FY14.
- EBITDA margin guided at 7.5% (v/s 7% in FY13), ex-LCV Dost margin guidance at 9.5%.
- AL plans to reduce debt by INR3b to INR40b by FY14-end. Hence, it plans to raise further INR4-5b through sale of few non-core investments.
- FY14 capex and investment guidance at INR5b (v/s INR15.4b in FY13).
- Board announced a dividend of INR0.6/share (v/s INR1 in FY12).

Valuation and view: Considering the weak 4Q performance and muted FY14 margin guidance, we cut FY14E EPS estimates by 34%/15%. AL, being a pure CV play, is expected to benefit from expected economic recovery from 2HFY14. The stock trades at 19.5x/10.6x FY14E/FY15E earnings of INR1.1/2.1 respectively. Maintain **Buy** with a revised target price of INR26 (7.5x FY15E EV/EBITDA).

Quarterly Performance

	FY12				FY13				FY12	FY13	(INR Million)	
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q			Est. 4QE	Var. (%)
Total Volumes (nos)	19,277	23,869	23,175	36,406	27,487	29,840	22,666	34,627	102,727	114,620	34,481	0.4
Growth %	-9.9	-2.9	25.7	22.7	42.6	25.0	-2.2	-4.9	9.2	11.6	-4.2	
Realizations ('000)	1,303	1,305	1,253	1,184	1,094	1,105	1,050	1,077	1,252	1,089	1,066	1.0
% change	18.8	18.2	3.7	-8.7	-16.1	-15.4	-16.2	-9.1	5.6	-13.0	-11.0	
Net Sales	25,127	31,148	29,035	43,110	30,074	32,960	23,805	37,285	128,619	124,812	36,751	1.5
Change (%)	7.0	14.8	30.4	12.0	19.7	5.8	-18.0	-13.5	15.3	-3.0	-14.8	
Total Cost	22,681	27,837	26,931	38,411	27,666	29,620	22,782	35,302	115,859	116,047	33,143	
EBITDA	2,446	3,312	2,104	4,699	2,407	3,341	1,023	1,983	12,760	8,765	3,609	(45.0)
EBITDA Margins (%)	9.7	10.6	7.2	10.9	8.0	10.1	4.3	5.3	9.9	7.0	9.8	-450bp
Other Income	74	135	86	109	129	239	141	115	404	624	142	(18.6)
Interest	567	658	603	724	834	1,036	1,071	828	2,553	3,769	1,227	(32.6)
Depreciation	847	859	866	956	893	984	931	1,000	3,528	3,808	980	2.0
PBT before EO Exp	1,107	1,929	720	3,128	810	1,559	-838	271	7,083	1,812	1,542	(82.5)
EO Exp/(Inc)	0	0	0	-16	0	0	-1,563	-1,344	-16	-2,896	0	
PBT	1,107	1,929	720	3,144	810	1,559	725	1,614	7,099	4,707	1,542	4.6
Tax	245	388	51	557	140	133	-17	114	1,240	370	310	
Effective Tax Rate (%)	22.1	20.1	7.0	17.7	17.3	8.5	-2.3	7.1	17.5	7.9	20.1	
Rep. PAT	862	1,541	669	2,587	670	1,426	741	1,500	5,859	4,337	1,232	21.8
Change (%)	-29.6	-7.8	54.3	-13.2	-22.3	-7.5	10.8	-42.0	-12.1	-26.0	-52.4	
Adj. PAT	862	1,541	669	2,574	670	1,426	-858	251	5,846	1,669	1,232	(79.6)
Change (%)	-29.6	-7.8	54.3	-13.7	-22.3	-7.5	-228.2	-90.2	-12.3	-71.4	-52.1	

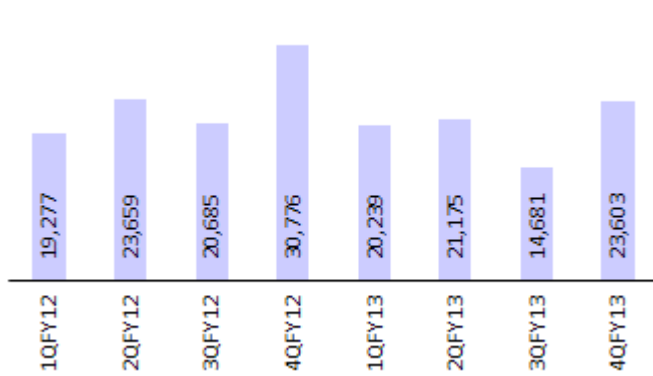
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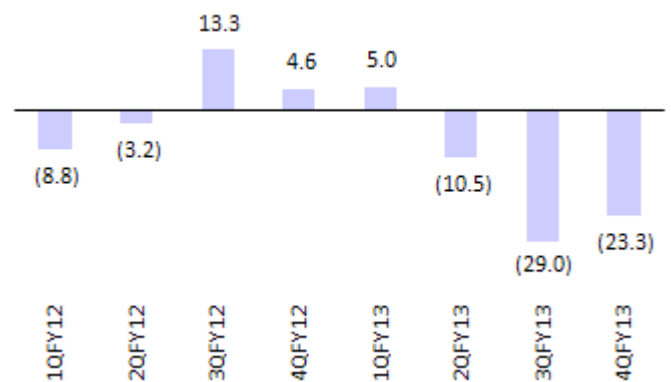
4Q performance below est as all major cost items witness QoQ jump

- Net sales declined by 13.5% YoY to INR37.3b (v/s est INR36.7b). Volumes declined by 4.9% to 34,619 units (v/s 34,481 units), while realizations were marginally ahead of estimates at INR1.08m (est INR1.07m).
- MHCV volumes declined by 23% YoY (+61% QoQ) to 23,603 units, while LCV Dost witnessed a growth of 125% YoY (+38% QoQ) to 11,024 units.
- Despite overall market being sluggish given challenging macro-economic environment, AL has gained market share across markets and product segments as the benefits of aggressive network expansion initiatives undertaken over the past 2-3 years are being reaped. During FY13, AL has gained 3% market share in the MHCV space led by over 5% market share gains in the ICV space (7.5-12T segment).
- Within the bus segment, AL has gained share in the private segment in all regions. However in the STU (State Transport Undertaking) space, due to higher discounting offered by competitors the company foregone some share.
- Significant inroads into new international markets primarily Africa and Middle East have helped to offset the demand weakness from the Sri Lankan market. Management expects exports to clock 10k units (v/s 9k units in FY13).
- During the 4th quarter, sale of LCV Dost outside Tamil Nadu stood at 28%.
- The company had undertaken a pricing action of 1.6% in Jan-13, however it was offset by increase in discounts by INR15-20k/unit to INR130,000/unit considering weak demand conditions. Rise in discounts have negated pricing action undertaken since Apr-12.
- Realizations improved by 2.5% sequentially with relatively lower volume share of LCV Dost.
- RM cost increased by 390bp QoQ to 75.8% (v/s est 71.7%) due to higher AMC charges (~100bp) increase in discounts (100-150bp), lower kit sales (50bp) and higher share of LCV Dost (120bp)
- Staff cost increased by 14.3% YoY (+7.8% QoQ) due to higher variable pay to executives (INR300m) partially offset by reduction employee cost (INR100m) on lower working days in Jan/Feb. Other expenditure increased by 38.5% QoQ (+10% YoY) driven by increase in activity levels (volumes)
- Higher RM cost, staff cost and other expenditure restricted EBITDA margin expansion to 100bp QoQ to 5.3% (v/s est 9.8%).
- EBITDA at INR1.98b (v/s est INR3.6b) declined by 57.8% YoY (+94% QoQ).
- During 4Q, AL booked a gain of INR1.34b on sale of IndusInd bank stake, partially offset by diminution in value recognized with respect to few other long term investments.

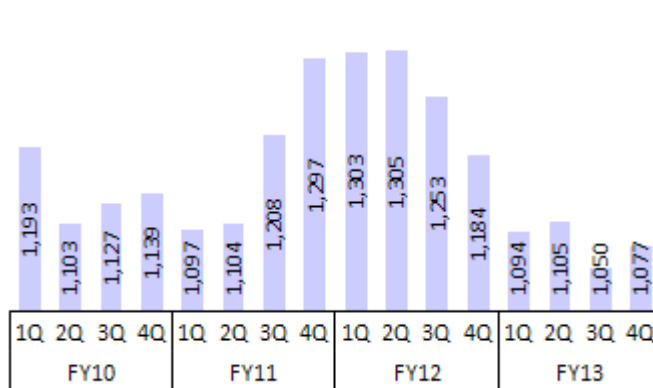
MHCV volumes improved on a sequential basis...



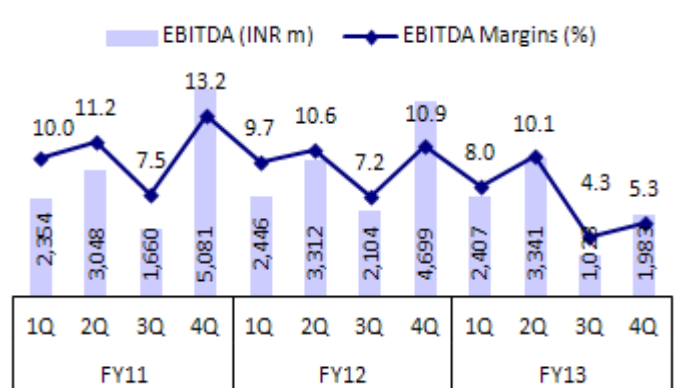
...however, on a YoY basis it remains significantly weak



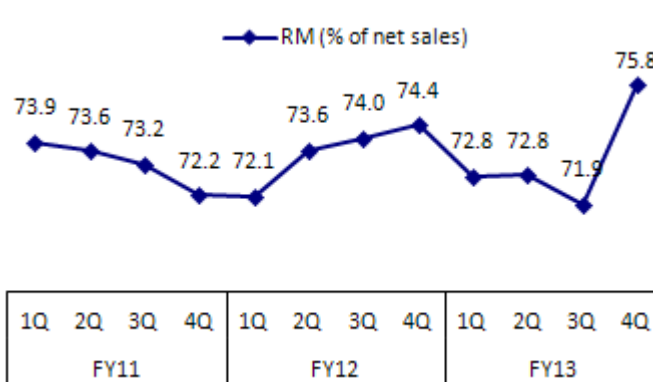
Realizations improves sequentially (INR '000/unit)



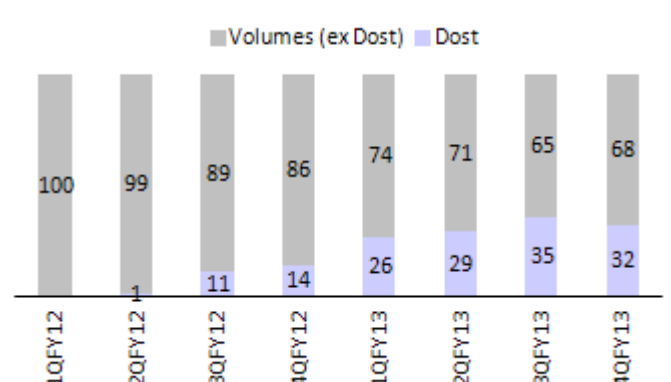
EBITDA margin expansion QoQ restricted to 100bp...



... due to sharp rise in RM cost



Share of Dost have moderated in 4QFY13 (%)



Source: Company, MOSL

Reported PAT boosted by gains on stake sale of IndusInd bank

- EBITDA at INR1.98b came 45% lower than estimate. However, interest cost came below our expectations of INR828m (est INR1.23b)
- PAT was boosted by exceptional gains of INR1.34b on sales of IndusInd bank stake, partially offset by diminution in value recognized with respect to few other long term investments
- The company also recognized a MAT credit of INR520m. This led to tax provision being lower at INR114m v/s est 310m.
- Adjusted PAT stood at INR251m (v/s est INR1.23b) due to weak operating performance.

FY14 outlook: MHCV volume guidance at 4-5%, margins at 7.5%, LCV growth over 50%

- **FY14 MHCV volume growth guidance at 4-5% for AL:** AL expects demand for MHCV industry to remain weak and lower YoY during 1HFY14. However, driven by economic recovery and low base, expects growth in 2HFY14 MHCV volumes. For FY14 overall, AL expects MHCV industry volumes to grow by 3-4%, while AL plans to grow its MHCV volumes ahead of the industry at 4-5%. Exports are expected to rise to 10,000 units in FY14 (v/s 9k in FY13).
- **FY14 AL's LCV volumes to increase more than 50%:** AL plans to launch Stile LCV (six seater passenger vehicle) and a cargo carrier Partner (5T).
- **Margin guidance at 7.5% for FY14:** AL expects to improve its FY14 margins by 50bp to 7.5%. Excluding LCV (Dost), margin guidance stands at 9.5%. For this, AL has undertaken a pricing action of 1.7% in Apr-13. Moreover, reduction in discounts (by INR30k/unit), increase in volumes and, higher Pantnagar contribution (40k in FY14 v/s 30k in FY13) would be other drivers for margin improvement.
- **FY14 capex and investment guidance at INR5b** (INR2.5b each) as compared to ~INR15.4b in FY13.
- **Plans to contain debt at INR40b:** AL plans to reduce debt by INR3b to INR40b by FY14-end. Reduction in working capital reduction, lower capex and investment requirement together with sale of non-strategic investments will help in reducing debt.

Valuation and view

- Considering weak 4Q performance and muted FY14 margin guidance, we cut our FY14E EPS by 33.8%/15.1%. AL, being a pure CV play is expected to benefit from expected economic recovery 2HFY14 onwards. The stock trades at 19.5x/10.6x FY14E/FY15E earnings of INR1.1/2.1 respectively. Maintain Buy with a revised TP of INR26.
- While near term M&HCV volumes are expected to remain weak, we expect recovery from 2HFY14 onwards driven by expected improvement in economic activity led by policy action and easing monetary policy together with lower base.
- AL, being a pure CV play is expected to benefit from expected economic recovery 2HFY14 onwards. The stock trades at 19.5x/10.6x FY14E/FY15E earnings of INR1.1/2.1 respectively. Maintain **Buy** with a revised TP of INR26.

Revised Forecast (INR m)

	FY14E			FY15E		
	Rev	Old	Chg (%)	Rev	Old	Chg (%)
Volumes (units)	133,872	134,831	-0.7	153,149	156,721	-2.3
Net Sales	143,002	141,095	1.4	167,514	166,466	0.6
EBITDA margins (%)	7.6	10.1	-240bp	8.5	10.1	-160bp
Net Profit	3,011	4,546	-33.8	5,560	6,548	-15.1
EPS (INR)	1.1	1.7	-33.8	2.1	2.5	-15.1

Source: MOSL

Ashok Leyland: an investment profile

Company description

Ashok Leyland (AL), the flagship company of Hinduja Group, is the 2nd largest MHCV with ~26% market share and the largest Bus manufacturer in India. To expand its product offerings, AL has entered into 50:50 JV with Nissan for LCVs and John Deere for construction equipment.

Key investment arguments

- While near term M&HCV volumes are expected to remain under pressure, 2HFY14 onwards we expect recovery in growth driven by expected improvement in economic activity led by policy action and easing monetary policy together with lower base.
- Launch of LCV Dost by AL-Nissan JV plugs gap in product portfolio and marks entry in high growth LCV segment. While Dost would impact standalone margins, it is accretive at EBITDA/PAT level.
- Ramp-up at Pantnagar plant and operating leverage shall offset margin pressure arising from higher discounts and higher Dost contribution in FY14/15.

Key investments risks

- Delay in recovery in the MHCV demand could impact volumes and margins adversely.
- Intensifying competition, particularly from Daimler (Bharat Benz) and Volvo Eicher could materially alter

the duopoly structure over the long term.

Recent developments

- Market share gains of 3% in trucks segment in FY13 benefiting from aggressive network expansion undertaken over the last 2-3 years
- Board announced dividend of ~INR0.6/share (v/s INR1/share in FY12).

Valuation and view

- AL, being a pure CV play is expected to benefit from expected economic recovery 2HFY14 onwards.
- The stock trades at 19.5x/10.6x FY14E/FY15E EPS of INR1.1/2.1 respectively.
- Maintain **Buy** with a revised TP of INR26.

Sector view

- Over the near term MHCV industry is expected to remain under pressure. However, with expected improvement in economic activity driven by Govt. policy actions and easing monetary policy, MHCV industry is expected to recover in FY14/15.
- Over the longer term, we expect MHCV industry to grow at a healthy rate of 1.2-1.5x of IIP growth
- While several new entrants have entered the industry, the industry is expected to remain largely duopolistic in nature over the near to medium term.

Comparative valuations

		Ashok Leyland	Eicher Motors	Tata Motors
P/E (x)	FY14E	19.5	21.3	23.0
	FY15E	10.6	17.8	18.3
EPS Gr (%)	FY14E	80.4	19.4	25.1
	FY15E	84.6	19.7	17.2
RoE (%)	FY14E	6.7	21.5	22.3
	FY15E	11.9	22.1	21.2
EV/EBITDA (x)	FY14E	8.9	14.7	4.2
	FY15E	6.8	10.7	3.8

EPS: MOSL forecast v/s consensus (INR)

	MOSL Forecast	Consensus Forecast	Variation (%)
FY14	1.1	1.9	-40.8
FY15	2.1	2.6	-19.3

Target price and recommendation

Current Price (INR)	Target Price (INR)	Upside (%)	Reco.
22	26	18.2	Buy

Stock performance (1 year)



Shareholding pattern (%)

	Mar-13	Dec-12	Mar-12
Promoter	38.7	38.7	38.7
Domestic Inst	13.1	13.6	14.7
Foreign	31.4	31.4	30.6
Others	16.9	16.4	16.1

Financials and Valuation

Income Statement		(INR Million)			
Y/E March	2012	2013	2014E	2015E	
Net Sales	128,420	125,056	143,002	167,514	
Change (%)	14.9	-2.6	14.3	17.1	
Expenditure	115,859	116,292	132,087	153,208	
Less Expenses Capital	70	90	87	87	
EBITDA	12,561	8,765	10,915	14,306	
% of Net Sales	9.8	7.0	7.6	8.5	
Depreciation	3,528	3,808	4,155	4,365	
EBIT	9,033	4,957	6,760	9,941	
Interest & Fin. Charges	2,553	3,769	3,719	3,692	
Other Income	404	624	670	700	
PBT	6,900	4,707	3,711	6,949	
Tax	1,240	370	700	1,390	
Effective Rate (%)	18.0	7.9	18.9	20.0	
Rep. PAT	5,660	4,337	3,011	5,560	
Change (%)	-10.3	-23.4	-30.6	84.6	
Adjusted PAT	5,647	1,669	3,011	5,560	
Change (%)	-10.6	-70.4	80.4	84.6	

Balance Sheet		(INR Million)			
Y/E March	2012	2013	2014E	2015E	
Share Capital	2,661	2,661	2,661	2,661	
Reserves	39,421	41,890	42,722	45,499	
Net Worth	42,082	44,551	45,383	48,160	
Loans	32,630	43,000	44,500	45,000	
Deferred Tax Liability	4,904	5,244	5,429	5,777	
Capital Employed	79,657	92,836	95,354	98,978	
Gross Fixed Assets	72,564	83,796	85,796	88,796	
Less: Depreciation	23,429	25,588	29,743	34,108	
Net Fixed Assets	49,135	58,208	56,053	54,689	
Capital WIP	5,482	1,500	2,000	3,000	
Investments	15,345	23,376	25,876	27,876	
Curr.Assets, L & Adv.	49,195	47,883	51,215	57,960	
Inventory	22,306	18,960	19,589	22,947	
Sundry Debtors	12,302	14,194	14,888	16,522	
Cash & Bank Balances	326	139	282	(326)	
Loans & Advances	14,261	14,589	16,455	18,817	
Current Liab. & Prov.	39,501	38,132	39,790	44,547	
Sundry Creditors	27,725	24,854	27,425	29,831	
Other Liabilities	6,807	9,406	7,836	9,179	
Provisions	4,969	3,872	4,530	5,537	
Net Current Assets	9,695	9,751	11,424	13,413	
Application of Funds	79,657	92,836	95,354	98,978	

E: MOSL Estimates

Ratios		(INR Million)			
Y/E March	2012	2013	2014E	2015E	
Basic (INR)					
EPS	2.1	0.6	1.1	2.1	
EPS Fully Diluted	2.1	0.6	1.1	2.1	
EPS Growth (%)	-55.3	-70.4	80.4	84.6	
Cash EPS	3.4	2.1	2.7	3.7	
Book Value per Share	15.8	16.7	17.1	18.1	
DPS	1.0	0.6	0.7	0.9	
Payout (Excl. Div. Tax) %	47.1	95.6	61.9	43.1	
Valuation (x)					
P/E		35.2	19.5	10.6	
Cash P/E		10.7	8.2	5.9	
EV/EBITDA		10.9	8.9	6.8	
EV/Sales		0.8	0.7	0.6	
Price to Book Value		1.3	1.3	1.2	
Dividend Yield (%)		2.7	3.2	4.1	
Profitability Ratios (%)					
ROE	13.8	3.9	6.7	11.9	
RoCE	12.5	6.5	7.9	11.0	
Turnover Ratios					
Debtors (Days)	35	41	38	36	
Inventory (Days)	63	55	50	50	
Creditors (Days)	79	73	70	65	
Fixed-Asset Turnover (x)	2.6	2.1	2.6	3.1	
Leverage Ratio					
Debt/Equity (x)	0.8	1.0	1.0	0.9	

Cash flow Statement		(INR Million)			
Y/E March	2012	2013	2014E	2015E	
OP/(Loss) before Tax	9,033	4,957	6,760	9,941	
Interest/Dividends Re.	404	624	670	700	
Depreciation & Amorti	3,528	3,808	4,155	4,365	
Direct Taxes Paid	-775	-30	-514	-1,042	
(Inc)/Dec in Working C	-2,580	-242	-1,530	-2,597	
Other Items	0	0	0	0	
CF after EO Items	9,625	12,012	9,540	11,367	
(Inc)/Dec in FA+CWIP	-5,645	-7,250	-2,500	-4,000	
(Pur)/Sale of Invest.	-3,045	-8,032	-2,500	-2,000	
CF from Inv. Activity	-8,690	-15,282	-5,000	-6,000	
Issue of Shares	1,330	0	0	0	
Inc/(Dec) in Debt	5,897	10,370	1,500	500	
Interest Rec./ (Paid)	-2,553	-3,769	-3,719	-3,692	
Dividends Paid	-3,092	-1,855	-2,179	-2,783	
CF from Fin. Activity	1,582	4,746	-4,398	-5,975	
Inc/(Dec) in Cash	2,517	1,476	142	-608	
Add: Beginning Balanc	1,755	4,272	5,748	5,890	
Closing Balance	4,272	5,748	5,890	5,282	

N O T E S

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3. Broking relationship with company covered	No
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