

## 2Q beats but challenges persist; Maintain Neutral

Ashok Leyland's (ALL) 2QFY13 operating results were ahead of our estimates with EBITDA margins at 10.1% compared to our estimate of 7.8% largely driven by better than expected realization growth. ASP for the quarter grew 1.3% despite higher contribution from low realization Dost (we believe this was largely on account of strong export realizations). Based on our calculations, we believe that domestic realizations have dropped 1.4% during the quarter. While, we are upgrading our earnings estimates by 9% and 14% for FY13E and FY14E respectively driven by better performance in 2Q, we continue to believe that current discounts and negligible rise in fleet operators' pricing power suggest weak demand environment for M&HCV goods segment. We expect the recovery to be gradual for the M&HCV goods segment over 2HFY13-FY14E and await meaningful signs of recovery in the investment cycle before re-rating the stock. As a result, we maintain our Neutral rating on the stock with a revised target price of Rs26.8 in line with the earnings upgrade.

- **Operating performance in line:** Revenues stood at Rs.33bn compared to our estimate of Rs.30.2bn. Higher than expected ASP (growth of 1.3% QoQ) coupled with containment in other overheads led to better than expected operating performance. EBITDA margins stood at 10.1% compared to our estimate of 7.8%. Further tax rate came lower at 8.5% compared to our estimate of 17.3%. As a result, Adjusted PAT stood at Rs.1.4bn compared to our estimate of 702mn.
- **Conference call highlights:** 1) the management expects overall M&HCV industry to register a drop of 5-10% for FY13E. However, overall volume growth for AL is likely to remain flat 2.) Inventory during the quarter stood lower at 8,400 units compared to 10,000 units at end of 1Q 3.) Discounts continue to remain at elevated levels (Rs.80k vs. Rs.60-65k in 1Q) and are expected to continue given weak demand conditions 4.) The company has guided for capex of Rs.6-6.5bn and investments in the range of Rs.6-7bn in FY13E.

| Y/E Mar (Rsmn)                | Q2FY13        |               | YoY (%)       | Q1FY13        |             | Q2FY13        |             |
|-------------------------------|---------------|---------------|---------------|---------------|-------------|---------------|-------------|
|                               | Rev           | EBITDA        |               | Rev           | EBITDA      | Rev           | EBITDA      |
| <b>Net sales</b>              | <b>32,960</b> | <b>30,946</b> | <b>6.5</b>    | <b>30,073</b> | <b>9.6</b>  | <b>30,152</b> | <b>9.3</b>  |
| <b>Cons. of raw materials</b> | 23,993        | 22,757        |               | 21,887        |             | 22,011        |             |
| % of sales                    | 72.8          | 73.5          | (74) bp       | 72.8          | 2 bp        | 73.0          | (21) bp     |
| Employee costs                | 2,638         | 2,515         |               | 2,679         |             | 2,679         |             |
| % of sales                    | 8.0           | 8.1           |               | 8.9           |             | 8.9           | (88) bp     |
| Other expenditure             | 2,986         | 2,362         |               | 3,101         |             | 3,101         |             |
| % of sales                    | 9.1           | 7.6           |               | 10.3          |             | 10.3          | (123) bp    |
| <b>Operating profit</b>       | <b>3,343</b>  | <b>3,312</b>  | <b>0.9</b>    | <b>2,407</b>  | <b>38.9</b> | <b>2,361</b>  | <b>41.6</b> |
| OPM (%)                       | 10.1          | 10.7          | (56) bp       | 8.0           | 214 bp      | 7.8           | 231 bp      |
| Dep. & amortisation           | 984           | 859           |               | 893           |             | 913           |             |
| Interest                      | 1,036         | 627           |               | 834           |             | 700           |             |
| EBT                           | 1,322         | 1,825         | (27.6)        | 681           | 94.3        | 749           | 76.6        |
| Other income                  | 239           | 103           |               | 129           |             | 100           |             |
| <b>PBT</b>                    | <b>1,561</b>  | <b>1,929</b>  | <b>(19.1)</b> | <b>809</b>    | <b>92.9</b> | <b>849</b>    | <b>83.9</b> |
| Provision for tax             | 133           | 388           |               | 140           |             | 147           |             |
| -effective tax rate           | 8.5           | 20.1          |               | 17.3          |             | 17.3          |             |
| PAT (Adjusted)                | 1,428         | 1,541         |               | 669           |             | 702           |             |
| PAT (Reported)                | 1,428         | 1,541         | (7.3)         | 669           | 113.3       | 702           | 103.4       |
| NPM (%)                       | 4.3           | 5.0           | (65) bp       | 2.2           | 211 bp      | 2.3           | 200 bp      |

Source: Company, Centrum Research

- **Valuations and Recommendations:** At the CMP of Rs26, the stock trades at 12.6x FY13E EPS of Rs2.0 and 9.8x FY13E EPS of Rs2.6. We continue to maintain Neutral rating on the stock with a revised target price of Rs26.8.

| Y/E Mar (Rsmn) | Rev     | YoY (%) | EBITDA | EBITDA (%) | Adj PAT | YoY (%) | Fully DEPS | RoE (%) | RoCE (%) | P/E (x) | EV/EBITDA (x) |
|----------------|---------|---------|--------|------------|---------|---------|------------|---------|----------|---------|---------------|
| FY11           | 111,177 | 53.5    | 11,684 | 10.5       | 5,821   | 37.4    | 0.9        | 6.6     | 5.6      | 27.1    | 11.0          |
| FY12           | 128,420 | 15.5    | 12,560 | 9.8        | 5,627   | (3.3)   | 0.9        | 5.6     | 5.6      | 29.8    | 11.0          |
| FY13E          | 136,009 | 5.9     | 13,258 | 9.7        | 5,423   | (3.6)   | 2.0        | 12.5    | 10.2     | 12.6    | 8.0           |
| FY14E          | 158,181 | 16.3    | 15,800 | 10.0       | 6,969   | 28.5    | 2.6        | 15.1    | 11.5     | 9.8     | 6.9           |
| FY15E          | 185,838 | 17.5    | 18,722 | 10.1       | 8,739   | 25.4    | 3.3        | 17.5    | 12.7     | 7.8     | 6.0           |

Source: Company, Centrum Research Estimates

Please refer to important disclosures/disclaimers inside

Centrum Equity Research is available on Bloomberg, Thomson Reuters and FactSet

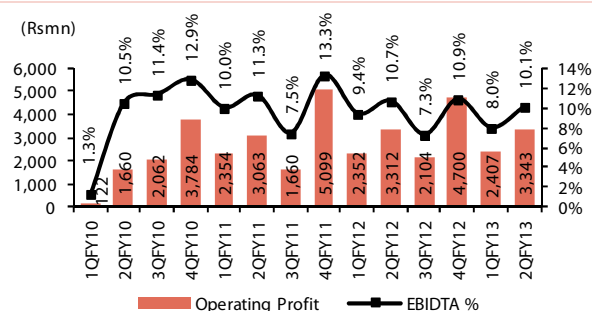
### Key Data

|                               |           |                          |            |
|-------------------------------|-----------|--------------------------|------------|
| Target Price                  | Rs26.8    | Bloomberg Code           | AL IN      |
| CMP                           | Rs25.7*   | Reuters Code             | ASOK.BO    |
| Upside                        | 4.3%      | Current Shares O/S (mn)  | 2,660.7    |
| <b>Stock to Sector</b>        | Neutral   | Diluted Shares O/S(mn)   | 2,660.7    |
| <b>Sector to Market</b>       | Neutral   | Mkt Cap (Rsbn/USDbn)     | 68.4/1.2   |
| <b>Price Performance (%)*</b> |           | 52 Wk H / L (Rs)         | 34/19      |
|                               | <b>1M</b> | <b>6M</b>                | <b>1Yr</b> |
| AL                            | 8.0       | (6.5)                    | (9.3)      |
| NIFTY                         | 0.2       | 15.4                     | 10.0       |
|                               |           | Daily Vol. (3M NSE Avg.) | 5,281,407  |
|                               |           | Face Value (Rs)          | 1          |
|                               |           | <b>1 USD = Rs54.8</b>    |            |

Source: Bloomberg, Centrum Research

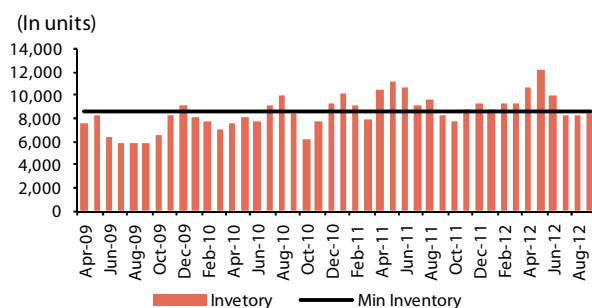
\*as on 9 November 2012

### Trend in EBITDA margin (%)



Source: Company, Centrum Research

### Inventory situation estimate



Source: Company, Centrum Research

### Earnings revision

| (Rsmn)              | Old Estimates  |                | Revised Estimates |                | Change (%)   |              |
|---------------------|----------------|----------------|-------------------|----------------|--------------|--------------|
|                     | FY13E          | FY14E          | FY13E             | FY14E          | FY12E        | FY13E        |
| <b>Volumes</b>      | <b>96,384</b>  | <b>107,138</b> | <b>96,022</b>     | <b>105,821</b> | <b>(0.4)</b> | <b>(1.2)</b> |
| <b>Net Sales</b>    | <b>131,935</b> | <b>153,290</b> | <b>136,009</b>    | <b>158,181</b> | <b>3.1</b>   | <b>3.2</b>   |
| EBITDA              | 12,567         | 14,737         | 13,258            | 15,800         | 5.5          | 7.2          |
| EBITDA margin (%)   | 9.5            | 9.6            | 9.7               | 10.0           | 22 bp        | 37 bp        |
| <b>Adjusted PAT</b> | <b>5,120</b>   | <b>6,510</b>   | <b>5,423</b>      | <b>6,969</b>   | <b>5.9</b>   | <b>7.0</b>   |
| FDEPS (Rs)          | 2.0            | 2.6            | 2.0               | 2.6            | 0.4          | (0.8)        |

Source: Company, Centrum Research Estimates

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## Financials

### Exhibit 1: Income Statement

| Y/E March (Rsmn)        | FY11           | FY12           | FY13E          | FY14E          | FY15E          |
|-------------------------|----------------|----------------|----------------|----------------|----------------|
| <b>Sales Volume</b>     | <b>94,104</b>  | <b>94,368</b>  | <b>96,022</b>  | <b>105,821</b> | <b>118,629</b> |
| % Growth                | 48.2           | 0.3            | 1.8            | 10.2           | 12.1           |
| <b>Net Sales</b>        | <b>111,177</b> | <b>128,420</b> | <b>136,009</b> | <b>158,181</b> | <b>185,838</b> |
| % Growth                | 53.5           | 15.5           | 5.9            | 16.3           | 17.5           |
| Raw Materials           | 80,645         | 91,215         | 94,303         | 108,604        | 127,227        |
| Personnel               | 9,746          | 10,204         | 11,224         | 12,347         | 13,581         |
| Manufact. & Other Exp.  | 9,102          | 14,441         | 17,224         | 21,431         | 26,308         |
| EBITDA                  | 11,684         | 12,560         | 13,258         | 15,800         | 18,722         |
| EBITDA Margin (%)       | 10.5           | 9.8            | 9.7            | 10.0           | 10.1           |
| Depn. & Amortn          | 2,674          | 3,528          | 3,835          | 4,110          | 4,360          |
| <b>EBIT</b>             | <b>9,009</b>   | <b>9,032</b>   | <b>9,423</b>   | <b>11,690</b>  | <b>14,362</b>  |
| Interest Expenses       | 1,637          | 2,553          | 3,253          | 3,658          | 3,928          |
| EBT                     | 7,373          | 6,480          | 6,170          | 8,032          | 10,434         |
| Other Income            | 153            | 404            | 444            | 466            | 489            |
| Extraord. (Income)/Exp. | -              | (16)           | -              | -              | -              |
| <b>PBT</b>              | <b>7,526</b>   | <b>6,867</b>   | <b>6,614</b>   | <b>8,498</b>   | <b>10,923</b>  |
| Tax-Total               | 1,705          | 1,240          | 1,190          | 1,530          | 2,185          |
| Tax Rate (%) - Total    | 22.7           | 18.1           | 18.0           | 18.0           | 20.0           |
| Reported PAT            | 5,821          | 5,627          | 5,423          | 6,969          | 8,739          |
| <b>Adjusted PAT</b>     | <b>5,821</b>   | <b>5,627</b>   | <b>5,423</b>   | <b>6,969</b>   | <b>8,739</b>   |
| PAT Margin              | 5.2            | 4.4            | 4.0            | 4.4            | 4.7            |
| % Growth                | 37.4           | -3.3           | -3.6           | 28.5           | 25.4           |

Source: Company, Centrum Research Estimates

### Exhibit 2: Balance Sheet

| Y/E March (Rsmn)            | FY11          | FY12          | FY13E         | FY14E         | FY15E          |
|-----------------------------|---------------|---------------|---------------|---------------|----------------|
| <b>SOURCES OF FUNDS</b>     |               |               |               |               |                |
| Capital                     | 1,330         | 2,661         | 2,661         | 2,661         | 2,661          |
| Reserves & Surplus          | 38,299        | 39,421        | 41,989        | 45,289        | 49,426         |
| Shareholders' Funds         | 39,630        | 42,082        | 44,650        | 47,949        | 52,087         |
| Minority Interest           |               |               |               |               |                |
| Secured Loans               | 11,823        | 9,600         | 15,600        | 18,600        | 21,600         |
| Unsecured Loans             | 13,860        | 23,544        | 23,544        | 23,544        | 23,544         |
| Total Loan Funds            | 25,683        | 33,144        | 39,144        | 42,144        | 45,144         |
| Deferred Tax Liabi. - Net   | 5,338         | 4,904         | 4,904         | 4,904         | 4,904          |
| <b>Total</b>                | <b>70,650</b> | <b>80,130</b> | <b>88,698</b> | <b>94,997</b> | <b>102,135</b> |
| <b>APPLICATION OF FUNDS</b> |               |               |               |               |                |
| Gross Block                 | 66,919        | 73,695        | 79,695        | 84,695        | 89,695         |
| Accumulated Dep.            | (20,581)      | (23,429)      | (27,264)      | (31,374)      | (35,733)       |
| Capital WIP                 | 3,580         | 4,352         | 4,352         | 4,352         | 4,352          |
| Net Fixed Assets            | 49,918        | 54,617        | 56,782        | 57,673        | 58,313         |
| Investments                 | 12,300        | 15,345        | 21,845        | 26,845        | 31,845         |
| Goodwill                    |               |               |               |               |                |
| Inventories                 | 22,089        | 22,306        | 26,829        | 30,336        | 35,640         |
| Sundry Debtors              | 11,852        | 12,302        | 13,415        | 15,601        | 18,329         |
| Other Current Assets        |               |               |               |               |                |
| Cash & Bank Balances        | 1,795         | 326           | 1,864         | 1,695         | 1,562          |
| Loans and Advances          | 7,936         | 13,428        | 10,208        | 11,835        | 13,872         |
| Total CA, Loans & Adv.      | 43,672        | 48,362        | 52,316        | 59,467        | 69,403         |
| Current Liabilities         | 30,379        | 33,268        | 36,455        | 42,268        | 49,542         |
| Provisions                  | 4,903         | 4,969         | 5,833         | 6,763         | 7,927          |
| Total Current Liab. & Prov. | 35,283        | 38,237        | 42,288        | 49,030        | 57,469         |
| Net Current Assets          | 8,390         | 10,125        | 10,027        | 10,437        | 11,934         |
| Miscellaneous Expend.       | 43            | 43            | 43            | 43            | 43             |
| <b>Total assets</b>         | <b>70,650</b> | <b>80,130</b> | <b>88,698</b> | <b>94,997</b> | <b>102,135</b> |

Source: Company, Centrum Research Estimates

### Exhibit 3: Cash flow

| Y/E March (Rsmn)        | FY11          | FY12          | FY13E         | FY14E         | FY15E         |
|-------------------------|---------------|---------------|---------------|---------------|---------------|
| <b>SOURCES</b>          | <b>6,720</b>  | <b>14,059</b> | <b>12,403</b> | <b>10,409</b> | <b>11,498</b> |
| Cash Profit             | 9,089         | 9,652         | 9,258         | 11,078        | 13,098        |
| (-) Dividends           | 5,753         | 3,113         | 2,855         | 3,669         | 4,601         |
| Retained Earnings       | 3,336         | 6,539         | 6,403         | 7,409         | 8,498         |
| Issue of Equity/Premium | (269)         | 58            | 0             | 0             | 0             |
| Others                  | 9             | 0             | 0             | 0             | 0             |
| Borrowings              | 3,644         | 7,462         | 6,000         | 3,000         | 3,000         |
| <b>APPLICATIONS</b>     | <b>10,336</b> | <b>12,328</b> | <b>12,403</b> | <b>10,409</b> | <b>11,498</b> |
| Capital Expenditure     | 4,698         | 7,548         | 6,000         | 5,000         | 5,000         |
| Investments             | 9,038         | 3,045         | 6,500         | 5,000         | 5,000         |
| Net Current Assets      | (6)           | 3,205         | (1,636)       | 579           | 1,630         |
| Others                  | 0             | 0             | 0             | 0             | 0             |
| Net cash increase/(dec) | (3,394)       | (1,470)       | 1,539         | (170)         | (133)         |

Source: Company, Centrum Research Estimates

### Exhibit 4: Key Ratios

| Y/E March                   | FY11  | FY12  | FY13E | FY14E | FY15E |
|-----------------------------|-------|-------|-------|-------|-------|
| O/s Shares                  | 2,661 | 2,661 | 2,661 | 2,661 | 2,661 |
| Fully Diluted Shares        | 2,661 | 2,661 | 2,661 | 2,661 | 2,661 |
| <b>Per share (Rs)</b>       |       |       |       |       |       |
| Basic EPS                   | 0.9   | 0.9   | 2.0   | 2.6   | 3.3   |
| Fully diluted EPS           | 0.9   | 0.9   | 2.0   | 2.6   | 3.3   |
| Book value                  | 14.9  | 15.8  | 16.8  | 18.0  | 19.6  |
| <b>Valuation (x)</b>        |       |       |       |       |       |
| P/E                         | 27.1  | 29.8  | 12.6  | 9.8   | 7.8   |
| P/BV                        | 1.7   | 1.6   | 1.5   | 1.4   | 1.3   |
| EV/EBITDA                   | 11.0  | 11.0  | 8.0   | 6.9   | 6.0   |
| EV/Sales                    | 0.8   | 0.8   | 0.8   | 0.7   | 0.6   |
| <b>Margin Ratio (%)</b>     |       |       |       |       |       |
| EBITDA Margin               | 7.5   | 7.2   | 9.7   | 10.0  | 10.1  |
| EBIT Margin                 | 5.1   | 4.4   | 6.9   | 7.4   | 7.7   |
| PAT Margin                  | 2.3   | 1.8   | 4.0   | 4.4   | 4.7   |
| <b>Return Ratio (%)</b>     |       |       |       |       |       |
| ROE                         | 6.6   | 5.6   | 12.5  | 15.1  | 17.5  |
| ROCE                        | 5.6   | 5.6   | 10.2  | 11.5  | 12.7  |
| <b>Other Ratios</b>         |       |       |       |       |       |
| Interest coverage ratio (%) | 3.5   | 2.2   | 2.9   | 3.2   | 3.7   |
| Debt-equity (x)             | 0.6   | 0.8   | 0.9   | 0.9   | 0.9   |
| Liquidity ratio (x)         | 1.2   | 1.3   | 1.2   | 1.2   | 1.2   |
| Other income contrib. (%)   | 3.6   | 11.4  | 6.7   | 5.5   | 4.5   |
| Dividend Payout (%)         | 211.5 | 116.3 | 45.0  | 45.0  | 45.0  |
| Asset TO (x)                | 1.8   | 1.8   | 1.7   | 1.8   | 2.0   |

Source: Company, Centrum Research Estimates

## Appendix A

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| Stock to Sector     | Sector to Market | Stock to Market |
|---------------------|------------------|-----------------|
| <b>Outperform</b>   | Outperform       | Buy             |
|                     | Neutral          | Buy             |
|                     | Underperform     | Accumulate      |
| <b>Neutral</b>      | Outperform       | Neutral         |
|                     | Neutral          | Neutral         |
|                     | Underperform     | Neutral         |
| <b>Underperform</b> | Outperform       | Reduce          |
|                     | Neutral          | Sell            |
|                     | Underperform     | Sell            |

**Accumulate: Add on decline; Reduce: Sell on rise**

- **Stock to Sector** – This is the relative rating of the stock to the sector and reflects its relative attractiveness vis-à-vis other coverage stocks in the sector.
- **Sector to Market** – This is the relative rating of the sector vis-à-vis the other sectors in the coverage space. This is derived based on the conviction of the analyst on a sector and macro view outlined in market strategy.
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**CAPITAL MARKET SEBI REGN. NO.:** BSE: INB011454239, NSE: INB231454233

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**CDSL DP ID:** 12200. **SEBI REGISTRATION NO.:** IN-DP-CDSL-661-2012

**PMS REGISTRATION NO.:** INP000004383

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