

Ashok Leyland

CV recovery gathers steam

Clearing up of dealer inventory boosted volumes QoQ: Ashok Leyland (ALL) registered a sequential improvement in revenues by 73% to Rs 15.8bn, driven by an 86% growth in volumes to 14,297 units. The company had a subdued Q1, where most of the pipeline inventory was cleared off. On a YoY basis, however, volumes dipped 17% as commercial vehicle (CV) volumes were running strong in H1 last year and the decline began only in the second half. The current quarter's performance was marginally lower than our expectations on two counts: a) the engine business saw a decline due to a slowdown in tower expansion in the telecom sector, and b) supplies to the defence sector were lower than normal, leading to lower realisations per vehicle.

Lower raw material cost and operating leverage boost margins: ALL's EBITDA margin during the quarter stood at 10.5%, an improvement of 820bps sequentially and 230bps over the same quarter last year. The strong improvement QoQ can be largely attributed to the following: a) higher operating leverage, as volumes increased 86% sequentially; b) benefits of lower raw material price, after liquidation of higher-cost pipeline inventory and input price re-negotiations with vendors (which led to a decline of ~Rs 40,000/vehicle in raw material costs); and c) cost-cutting initiatives taken by the company.

Interest cost during the quarter was also lower as ALL was able to bring down its working capital from Rs 15bn to Rs 9bn by paring inventory and introducing the cash-and-carry mode on vehicles. Net profit stood at Rs 895mn against a loss in the previous quarter.

Faster than expected recovery in CVs: The pace of recovery in the CV cycle has been faster than expected. We are revising our FY10 and FY11 volume growth estimates for ALL to 12% and 23% respectively. We expect commissioning of the Uttaranchal plant in January '10 to help the company increase its margins by more than 100bps for FY11 and also save on income tax outgoings. In FY12, if the economy continues to grow at 6–8%, the benefit of full utilisation of the Uttaranchal plant could provide a significant booster shot to ALL's financial performance.

Upgrade to Buy: The quicker pace of recovery in the CV segment and benefits from the Uttaranchal plant support an upward revision in our FY10 and FY11 EPS by 18% and 36% respectively. We value the company at 14x FY11E EPS of Rs 3.7 arriving at a target price of Rs 52, an upside of ~14%. At our target price the implied EV/EBITDA for the stock is 9.3x. We upgrade ALL from Hold to Buy.

Financial highlights

(Rs mn)	FY08	FY09	FY10E	FY11E
Revenue	77,426	59,811	68,630	84,625
Growth (%)	8.0	(22.8)	14.7	23.3
Adj net income	4,955	2,035	3,119	4,970
Growth (%)	9.1	(58.9)	53.3	59.3
FDEPS (Rs)	3.7	1.5	2.3	3.7
Growth (%)	7.6	(58.9)	53.3	59.3

Profitability and return ratios

(%)	FY08	FY09	FY10E	FY11E
EBITDA margin	10.6	7.8	9.7	11.1
EBIT margin	8.3	4.9	6.5	8.0
Adj PAT margin	6.4	3.4	4.5	5.9
ROE	24.5	7.2	8.8	13.2
ROIC	18.5	6.3	6.2	8.7
ROCE	19.3	7.4	7.3	10.3

What's New? Target Rating Estimates

CMP	TARGET	RATING	RISK
Rs 46	Rs 52	BUY	HIGH

BSE	NSE	BLOOMBERG
500477	ASHOKLEY	AL IN

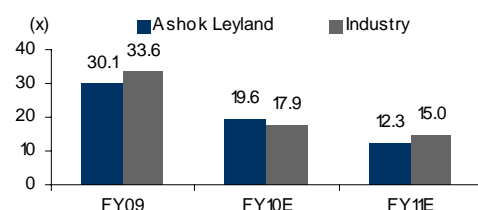
Company data

Market cap (Rs mn / US\$ mn)	61,183 / 1,291
Outstanding equity shares (mn)	1,330
Free float (%)	61.4
Dividend yield (%)	2.2
52-week high/low (Rs)	40 / 12
2-month average daily volume	4,519,010

Stock performance

Returns (%)	CMP	1-mth	3-mth	6-mth
Ashok Ley.	46	7.9	25.5	114.1
BSE Auto	6,307	(5.4)	11.8	80.3
BSE Sensex	15,896	(7.2)	3.3	39.4

P/E comparison



Valuation matrix

(x)	FY08	FY09	FY10E	FY11E
P/E @ CMP	12.3	30.1	19.6	12.3
P/E @ Target	14.0	34.2	22.3	14.0
EV/EBITDA @ CMP	9.8	17.0	12.0	8.5





Result highlights

Fig 1 - Actual vs estimated performance

(Rs mn)	Actual	Estimate	% Variance
Revenue	15,777	17,375	(9.2)
EBITDA	1,661	1,826	(9.0)
Adj net income	895	1,145	(21.9)
FDEPS (Rs)	0.7	0.9	(21.9)

Source: RHH

Fig 2 - Quarterly performance

(Rs mn)	Q2FY10	Q2FY09	% Chg YoY	Q1FY10	% Chg QoQ
Sales volume (units)	14,297	17,207	(16.9)	7,698	85.7
Net sales	15,777	18,664	(15.5)	9,125	72.9
Expenditure	14,116	17,125	(17.6)	9,003	56.8
Operating profit	1,661	1,539	7.9	122	-
Other income	56	285	(80.5)	91	(39.0)
Interest	170	246	(30.8)	258	(34.1)
Depreciation	506	505	0.1	435	16.3
PBT	1,032	930	11.0	25	-
Tax	146	236	(38.2)	(53)	-
PAT	895	838	6.8	(427)	-
EBITDA margin (%)	10.5	8.2	230 bps	1.3	820 bps
EPS (Rs)	0.7	0.6	6.7	(0.3)	-

Source: Company, RHH

Fig 3 - Revised estimates

Key parameters (Rs mn)	FY10E			FY11E		
	Old	New	% Chg	Old	New	% Chg
Revenue	66,762	68,630	2.8	77,493	84,625	9.2
EBITDA margin (%)	9.6	9.7	10 bps	10.6	11.1	50 bps
Net profit	2,648	3,119	17.8	3,649	4,970	36.2
FDEPS (Rs)	2.0	2.3	17.8	2.7	3.7	36.2

Source: RHH

Below estimates due to lower dispatches to the defence sector and poor performance in engines segment

Clearing up of pipeline inventory in Q1 boosted volumes

Lower interest costs as working capital reduced from Rs 15bn to Rs 9bn

Higher estimates for volumes next year and higher margins from the Uttaranchal plant



Consolidated financials

Profit and Loss statement

Y/E March (Rs mn)	FY08	FY09	FY10E	FY11E
Revenues	77,426	59,811	68,630	84,625
Growth (%)	8.0	(22.8)	14.7	23.3
EBITDA	8,174	4,694	6,674	9,397
Growth (%)	16.3	(42.6)	42.2	40.8
Depreciation & amortisation	1,774	1,784	2,215	2,637
EBIT	6,401	2,910	4,459	6,760
Growth (%)	15.9	(54.5)	53.2	51.6
Interest	497	1,187	1,109	1,224
Other income	613	361	549	677
EBT	6,516	2,084	3,899	6,213
Income taxes	1,688	185	780	1,243
Effective tax rate (%)	25.9	8.9	20.0	20.0
Extraordinary items	-	-	-	-
Min into / inc from associates	-	-	-	-
Reported net income	4,828	1,900	3,119	4,970
Adjustments	(127)	(135)	-	-
Adjusted net income	4,955	2,035	3,119	4,970
Growth (%)	9.1	(58.9)	53.3	59.3
Shares outstanding (mn)	1,330.1	1,330.1	1,330.1	1,330.1
FDEPS (Rs) (adj)	3.7	1.5	2.3	3.7
Growth (%)	7.6	(58.9)	53.3	59.3
DPS (Rs)	1.5	1.0	1.2	1.5

Cash flow statement

Y/E March (Rs mn)	FY08	FY09	FY10E	FY11E
Net income + Depreciation	6,745	3,838	5,335	7,607
Non-cash adjustments	(255)	(794)	766	463
Changes in working capital	3,749	(9,131)	5,047	1,529
Cash flow from operations	10,240	(6,088)	11,148	9,599
Capital expenditure	(6,095)	(7,579)	(7,017)	(6,500)
Change in investments	101	(171)	(2,632)	(3,263)
Other investing cash flow	(2,232)	1,001	-	-
Cash flow from investing	(8,226)	(6,749)	(9,649)	(9,763)
Issue of equity	-	-	-	-
Issue/repay debt	4,261	7,873	(463)	1,993
Dividends paid	-	(2,335)	(1,556)	(1,796)
Other financing cash flow	(69)	(7)	-	-
Change in cash & cash eq	6,205	(7,306)	(520)	33
Closing cash & cash eq	8,157	880	360	393

Economic Value Added (EVA) analysis

Y/E March	FY08	FY09	FY10E	FY11E
WACC (%)	13.6	13.3	13.3	13.3
ROIC (%)	18.5	6.3	6.2	8.7
Invested capital (Rs mn)	27,421	56,159	59,091	64,888
EVA (Rs mn)	1,345	(3,902)	(4,198)	(2,966)
EVA spread (%)	4.9	(6.9)	(7.1)	(4.6)

Balance sheet

Y/E March (Rs mn)	FY08	FY09	FY10E	FY11E
Cash and cash eq	8,157	881	360	393
Accounts receivable	3,758	9,580	5,819	5,321
Inventories	12,239	13,300	11,272	12,164
Other current assets	8,241	7,895	7,412	7,823
Investments	6,099	2,636	5,267	8,531
Gross fixed assets	29,424	49,533	58,533	67,033
Net fixed assets	15,255	33,991	40,776	46,639
CWIP	5,292	9,983	8,000	6,000
Intangible assets	-	-	-	-
Deferred tax assets, net	(2,538)	(2,634)	(2,434)	(2,234)
Other assets	223	97	97	97
Total assets	56,728	75,728	76,570	84,734
Accounts payable	12,926	11,100	10,560	11,788
Other current liabilities	6,342	7,588	6,559	7,664
Provisions	3,452	2,681	3,686	4,598
Debt funds	8,876	19,581	19,118	21,111
Other liabilities	3,643	38	238	438
Equity capital	1,330	1,330	1,330	1,330
Reserves & surplus	20,159	33,409	35,078	37,804
Shareholder's funds	21,490	34,739	36,408	39,134
Total liabilities	56,728	75,728	76,570	84,734
BVPS (Rs)	17.2	27.1	28.4	30.4

Financial ratios

Y/E March	FY08	FY09	FY10E	FY11E
Profitability & Return ratios (%)				
EBITDA margin	10.6	7.8	9.7	11.1
EBIT margin	8.3	4.9	6.5	8.0
Net profit margin	6.4	3.4	4.5	5.9
ROE	24.5	7.2	8.8	13.2
ROCE	19.3	7.4	7.3	10.3
Working Capital & Liquidity ratios				
Receivables (days)	21	41	41	24
Inventory (days)	73	105	91	71
Payables (days)	73	98	80	67
Current ratio (x)	1.7	1.7	1.5	1.3
Quick ratio (x)	0.4	0.6	0.4	0.3
Turnover & Leverage ratios (x)				
Gross asset turnover	2.8	1.5	1.3	1.3
Total asset turnover	1.5	0.9	0.9	1.0
Interest coverage ratio	12.9	2.5	4.0	5.5
Adjusted debt/equity	0.4	0.6	0.5	0.5
Valuation ratios (x)				
EV/Sales	1.0	1.3	1.2	0.9
EV/EBITDA	9.8	17.0	12.0	8.5
P/E	12.3	30.1	19.6	12.3
P/BV	2.7	1.7	1.6	1.5



Quarterly trend

Particulars	Q2FY09	Q3FY09	Q4FY09	Q1FY10	Q2FY10
Revenue (Rs mn)	18,664	10,008	12,181	9,125	15,777
YoY growth (%)	6.9	(44.4)	(52.5)	(51.6)	(15.5)
QoQ growth (%)	(0.9)	(46.4)	21.7	(25.1)	72.9
EBITDA (Rs mn)	1,539	331	1,148	122	1,661
EBITDA margin (%)	8.2	3.3	9.4	1.3	10.5
Adj net income (Rs mn)	838	(289)	569	(427)	895
YoY growth (%)	4	(124)	(69)	(151)	7
QoQ growth (%)	(1)	(135)	NM	NM	NM

DuPont analysis

(%)	FY07	FY08	FY09	FY10E	FY11E
Tax burden (Net income/PBT)	75.2	76.0	97.6	80.0	80.0
Interest burden (PBT/EBIT)	109.5	101.8	71.6	87.4	91.9
EBIT margin (EBIT/Revenues)	7.7	8.3	4.9	6.5	8.0
Asset turnover (Revenues/Avg TA)	175.5	153.6	90.3	90.1	104.9
Leverage (Avg TA/Avg equitiy)	247.0	249.3	235.6	214.1	213.5
Return on equity	27.5	24.5	7.2	8.8	13.2

Company profile

Ashok Leyland (ALL) is the second largest manufacturer of medium and heavy commercial vehicles (M&HCV) in India with a market share of 28.1% and volumes of 82,506 vehicles. About 8.5% of these volumes came from exports. ALL has six manufacturing plants- the mother plant at Ennore near Chennai, two plants at Hosur (Tamil Nadu) and assembly plants at Alwar (Rajasthan) and Bhandara (Maharashtra). The company is also setting up a greenfield project at Uttarakhand.

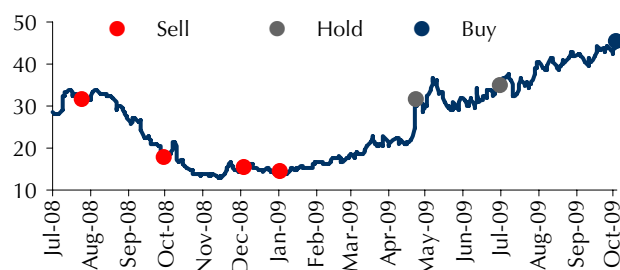
Shareholding pattern

(%)	Mar-09	Jun-09	Sep-09
Promoters	38.6	38.6	38.6
FII's	9.8	10.2	11.0
Banks & FIIs	18.9	19.7	20.9
Public	32.7	31.5	29.5

Recommendation history

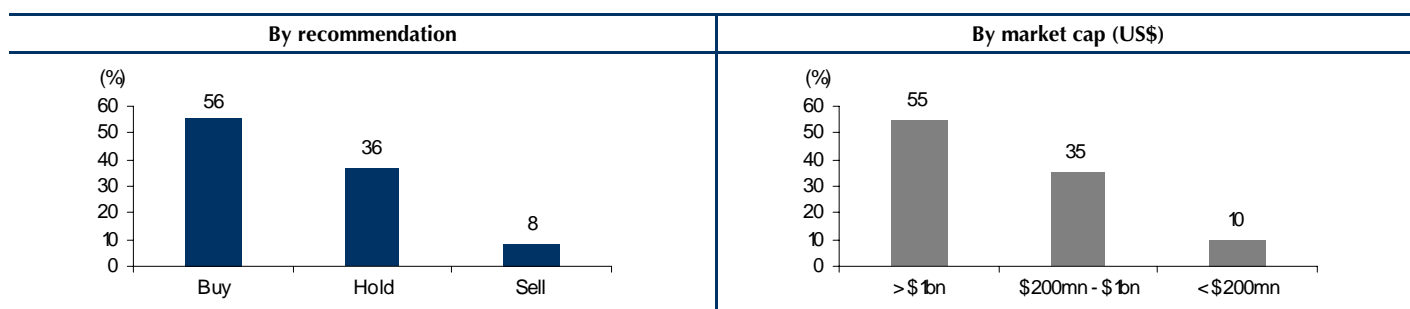
Date	Event	Reco price	Tgt price	Reco
21-Aug-08	RHH Compendium	32	32	Sell
27-Oct-08	Results Review	17	20	Sell
2-Jan-09	Quarterly Preview	15	15	Sell
30-Jan-09	Results Review	14	11	Sell
20-May-09	Results Review	31	28	Hold
28-Jul-09	Results Review	35	33	Hold
31-Oct-09	Results Review	46	52	Buy

Stock performance





Coverage Profile



Recommendation interpretation

Recommendation	Expected absolute returns (%) over 12 months
Buy	More than 15%
Hold	Between 15% and -5%
Sell	Less than -5%

Recommendation structure changed with effect from March 1, 2009

Expected absolute returns are based on share price at market close unless otherwise stated. Stock recommendations are based on absolute upside (downside) and have a 12-month horizon. Our target price represents the fair value of the stock based upon the analyst's discretion. We note that future price fluctuations could lead to a temporary mismatch between upside/downside for a stock and our recommendation.

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