HDFC securities

INSTITUTIONAL RESEARCH

RESULTS REVIEW 1QFY19 | 18 JUL 2018

Ashok Leyland

BUY

INDUSTRY			AUTOS
CMP *(as on 18 Jul 2018)*			Rs 111
Target Price			Rs 143
Nifty			10,980
Sensex			36,373
KEY STOCK DATA			
Bloomberg			AL IN
No. of Shares (mn)			2,935
MCap (Rs bn) / ($ mn)			324 / 4,731
6m avg traded value (Rs mn)			2,500
STOCK PERFORMANCE (%)			
52 Week high / low			Rs 168 / 99
	3M	6M	12M
Absolute (%)	(26.0)	(8.6)	4.8
Relative (%)	(32.0)	(11.7)	(9.9)
SHAREHOLDING PATTERN (%)			
Promoters			51.27
FIs & Local MFs			9.85
FPIs			23.26
Public & Others			15.62

Source : BSE

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Opportunities is on the way

Ashok Leyland (AL) delivered in line rev and operating performance. Revenue came at Rs. 62.5bn (+47.5% YoY) led by 47% growth in vol (42.1k units) on low base (BSIV and GST transitions). EBIDTA jumped 110% YoY to Rs 6.4bn, with margin at 10.4% (+317bps YoY).

We believe M&HCV truck growth will taper down in the short term owing to the new GVW norms, however, growth momentum will continue to be strong for medium to long term, driven by 1) Pick-up in infra, construction and mining activities, 2) pre-purchases for BS-VI in FY20 and 3) introduction of scrappage policy in FY21. The recent sharp correction in AL provides a buying opportunity given the strong ROIC (+40%) and FCF profile of the company (net cash & cash equivalents at Rs 36bn)

Management expects, stricter overloading ban will likely offset the impact of increase in rated freight-carrying capacity (15-17%) of the industry (60-70% trucks are already overloaded by 25-50%); thus, it may be positive surprise for CV industry. Weakness on truck sales can be seen in near term owing to time required for upgraded products (the process of product modification may take 2-4 weeks, and ARAI certification would require another 3-4 weeks). However sharp jump in replacement demand can be seen once the redesigned trucks hit the market. As per the management large portion of existing fleet relating to Tippers, ICVs, Oil/Water tankers, Car/4W carriers etc, are not expected to be impacted by higher axle load norms (as dependent on dimensions). We cut EPS estimates 9/12% for FY19/FY20E, factoring in short term moderation in truck demand. Expect 21% EPS CAGR over FY18-20E. Maintain Buy with TP Rs 143 (18x FY20E EPS) vs Rs 166 earlier.

Highlights of the quarter

- **Market share trend:** Al's market share in MHCVs segment decreased 450bps YoY to 30% in 1QFY19 due to higher competition intensity and dealer inventory build-up by peers. AL expects to regain share in subsequent quarters driven by innovative product launches and expansion of network in East and North India. The company has shown impressive growth in LCV (+33% YoY) and export (+22%YoY) volume.
- **Capex:** It plans to invest Rs 10bn in FY19. Out of which, 40% will be used for capacity related expansion and 60% will be used for R&D (BS 1V technology and EV) and new product development.
- **Near-term outlook:** Expect subdued volume in 2Q, owing to impact of new GVW norms.

Financial Summary

(Rs mn)	1QFY19	1QFY18	*YoY (%)*	4QFY18	*QoQ (%)*	FY17	FY18	FY19E	FY20E
Net Sales	62,501	42,579	*46.8*	87,725	*(28.8)*	201,401	262,479	300,200	336,404
EBITDA (adj.)	6,475	3,061	*111.5*	10,327	*(37.3)*	22,025	27,390	32,671	37,838
APAT	3,848	1,113	*245.8*	6,671	*(42.3)*	11,923	15,618	20,282	23,216
Diluted EPS (Rs)	1.31	0.38	*245.8*	2.3	*(42.3)*	4.3	5.3	6.9	7.9
P/E (x)						25.8	20.8	16.0	14.0
EV / EBITDA (x)						14.2	10.6	8.5	7.2
RoE (%)						20.7	23.5	26.4	26.4

Source: Company, HDFC sec Inst Research

AL's topline growth was in line with est, with 48% YoY increase in revenue supported by volume growth (+47% YoY)

M&HCV volumes jumped 54% YoY (30.64k), and LCV volumes increased by 33 %(11.48k) in 1Q

Revenue mix were -domestic Trucks 62%, domestic Buses 9-10%, Exports 9%, aftermarket 8%, and Defense 3-4%.

Aftermarket segment revenue grew 28%, while exports grew 24%.

Gross margin improved sequentially owing to price hike taken in April-18(~3%) and lower discount

EBIDTA margin improved 317bps YoY owing to oplev

Quarterly Financials Snapshot: Standalone

(Rs mn)	1QFY19	1QFY18	YoY (%)	4QFY18	QoQ (%)
Volumes (in units)	42,127	28,495	*47.8*	58,735	*(28.3)*
Net ASP (Rs/veh)	1,483,638	1,494,247	*(0.7)*	1,493,571	*(0.7)*
Revenue	**62,501**	**42,579**	***46.8***	**87,725**	***(28.8)***
Material Expenses	43,512	29,415	*47.9*	63,060	*(31.0)*
Employee Expenses	4,930	4,217	*16.9*	4,549	*8.4*
Other Operating Expenses	7,584	5,885	*28.9*	9,788	*(22.5)*
EBITDA	**6,475**	**3,061**	***111.5***	**10,327**	***(37.3)***
Depreciation	1,430	1,321	*8.3*	1,463	*(2.2)*
EBIT	**5,045**	**1,740**	***190.0***	**8,864**	***(43.1)***
Other Income	437	357	*22.3*	636	*(31.3)*
Interest Cost	116	366	*(68.4)*	201	*(42.2)*
PBT	**5,366**	**1,731**	***210.1***	**9,300**	***(42.3)***
Tax	1,519	492	*208.4*	2,626	*(42.2)*
APAT	**3,848**	**1,238**	***210.7***	**6,674**	***(42.4)***
EO Items (Adj For Tax)	147	126	*16.6*	3	*4,783.3*
RPAT	**3,701**	**1,113**	***232.7***	**6,671**	***(44.5)***
Adj EPS	**1.3**	**0.4**	***210.7***	**2.3**	***(42.4)***

Source: Company, HDFC sec Inst Research

Margin Analysis: Standalone

	1QFY19	1QFY18	YoY (BPS)	4QFY18	QoQ (BPS)
Material Expenses % Net Sales	69.6	69.1	*53*	71.9	*(227)*
Employee Expenses % Net Sales	7.9	9.9	*(202)*	5.2	*270*
Other Expenses % Net Sales	12.1	13.8	*(169)*	11.2	*98*
EBITDA Margin (%)	10.4	7.2	*317*	11.8	*(141)*
Tax Rate (%)	28.3	28.5	*(15)*	28.2	*7*
APAT Margin (%)	6.2	2.9	*325*	7.6	*(145)*

Source: Company, HDFC sec Inst Research

We see limited impact of new GCV norm for truck demand as a significant part of the industry is unlikely to be affected

Tippers, ICV, Bulkers), Oil /Water tankers, 2W/4W carriers' account for ~55% volumes don't get impacted significantly by norms as the load for these categories are also dependent on dimensions.

Post increase in axle load limits, overloading restrictions are expected to be enforced strictly and can push the demand. Overloading varies from 25-50%.

New vehicles need to be slightly modified (changes in tyres, drivetrain, chassis, brakes, wheelbase, engine torque, etc may be required), and need to take ARAI certification to meet new axle load norms.

Volume Assumptions

(in units)	FY16	FY17	FY18	FY19E	FY20E
Domestic MHCV	98,814	102,313	116,534	127,502	141,074
% YoY	*48.7*	*3.5*	*13.9*	*9.4*	*10.6*
LCV	30,695	31,770	42,078	48,390	55,648
% YoY	*12.7*	*3.5*	*32.4*	*15.0*	*15.0*
Domestic volumes	***129,509***	***134,083***	***158,612***	***175,891***	***196,722***
% YoY	*38.2*	*3.5*	*18.3*	*10.9*	*11.8*
Exports	***10,948***	***10,979***	***16,239***	***19,162***	***22,994***
% YoY	*(2.4)*	*0.3*	*47.9*	*18.0*	*20.0*
Total sales	***140,457***	***145,062***	***174,851***	***195,053***	***219,717***
% YoY	*33.9*	*3.3*	*20.5*	*11.6*	*12.6*

Source: SIAM, HDFC sec Inst Research

Change in Estimates

In Rs mn	New		Old		% chg	
	FY19E	FY20E	FY19E	FY20E	*FY19E*	*FY20E*
Volume	195,053	219,717	199,166	226,545	*(2.1)*	*(3.0)*
Net Sales	300,200	336,404	307,064	348,140	*(2.2)*	*(3.4)*
EBITDA	32,671	37,838	35,571	42,330	*(8.2)*	*(10.6)*
Adj PAT	20,282	23,216	22,341	26,361	*(9.2)*	*(11.9)*
Adj EPS (in Rs)	6.9	7.9	7.6	9.0	*(9.2)*	*(11.9)*

Source: HDFC sec Inst Research

We expect most of OEMs will take significant price hike on upgraded products

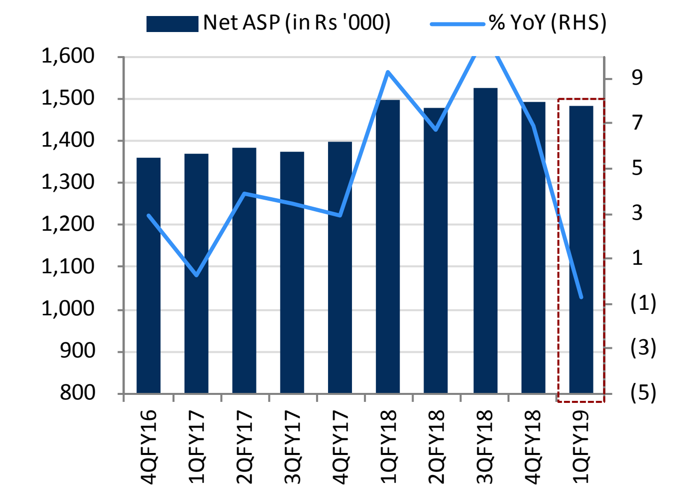
AL's is also focus on new growth areas by increasing the share of LCVs, exports, spare parts and defense

In the LCV segment, currently, ALs products are restricted to the 2.5-3.5 tonne range. It is looking to expand this range from 1.5 to 7.5 tonne, including the high-selling 3.5 tonne pick-up segment

Capex and Investments expected at Rs10bn in FY19. Capex would be incurred towards LCV product portfolio expansion, BS6 technology, EV technology, development of modular platform, Investment in Andhra Pradesh plant for bus body building and de-bottlenecking of capacity

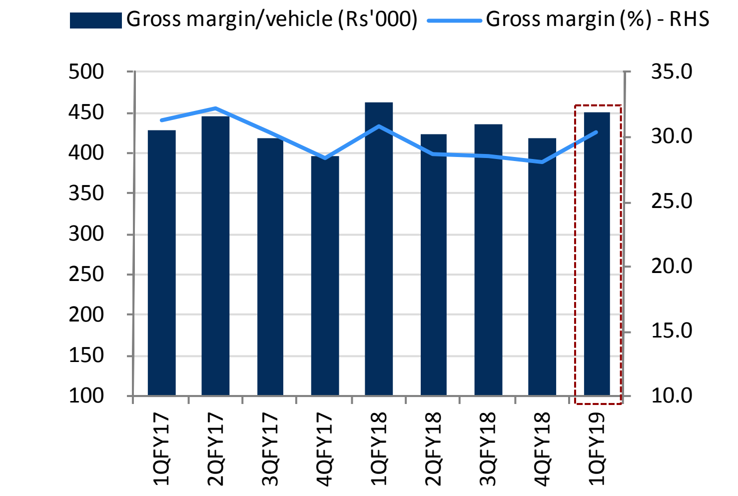
Management does not see need for Greenfield expansion in near term

ASP Remain Flat YoY



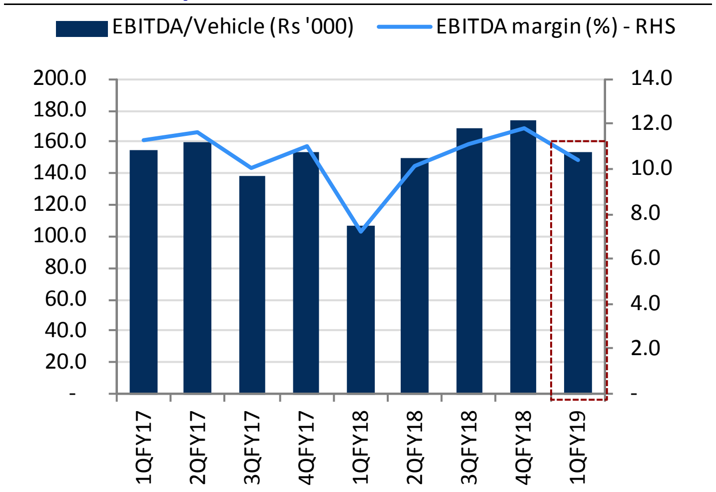
Source: Company, HDFC sec Inst Research

GM Improved QoQ



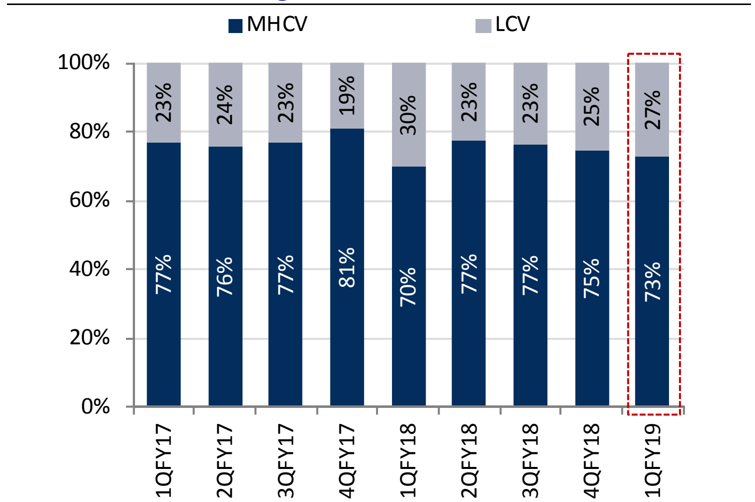
Source: Company, HDFC sec Inst Research

EBITDAM Expanded YoY



Source: Company, HDFC sec Inst Research

LCV Volume Gaining Traction



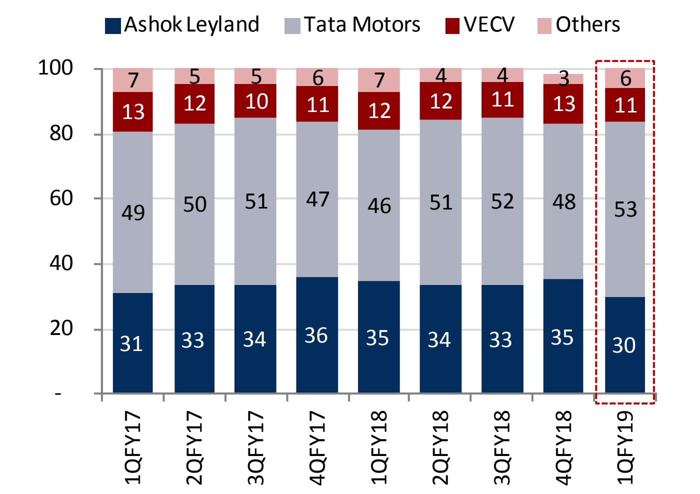
Source: Company, HDFC sec Inst Research

AL's market share slid 450bps YoY in M&HCV as focused on profitability (not participated for market share gain through discount) and dealer inventory build-up by peers.

The working capital came down from 7 days to -27 days at FY18-end. This decline was mainly on account of 24 days decrease in inventory. Last year inventory days was exceptionally higher mainly attributable to increase in the unsold stock of BSIII vehicles and higher inventory at Hinduja Foundries.

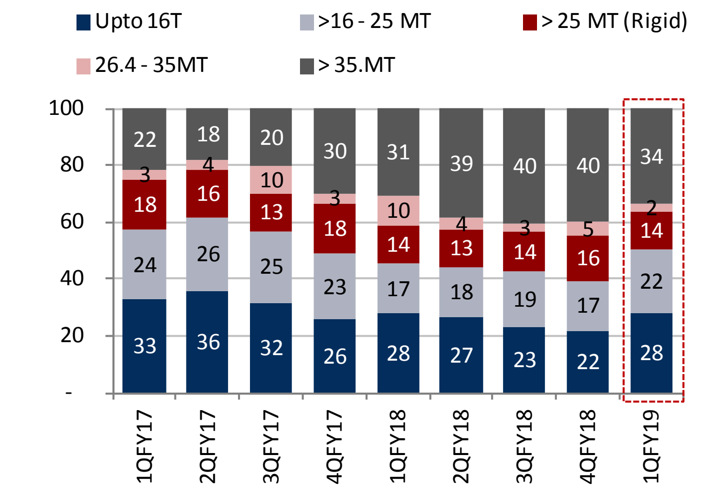
Helped by healthy FCF, net cash(including current investment) has improved from Rs 3.4bn at FY17-end to Rs 36bn at 1QFY19-end

AL's Market Share In Dom MHCV Slid In 1Q



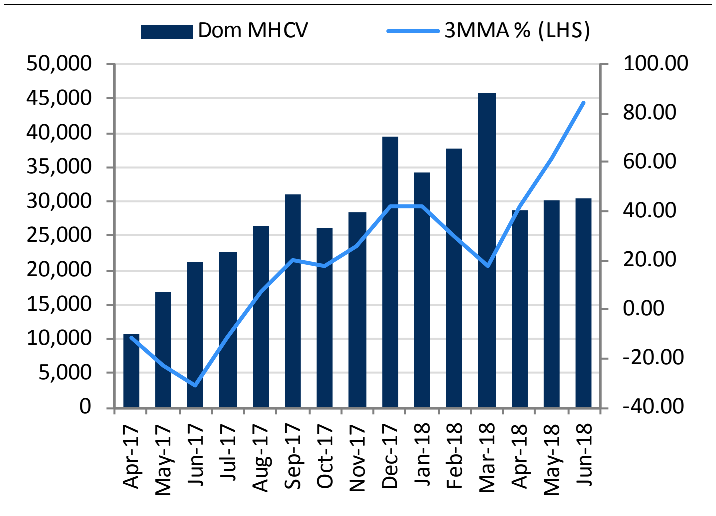
Source: SIAM, HDFC sec Inst Research

Tonnage Mix Turned Favourable YoY



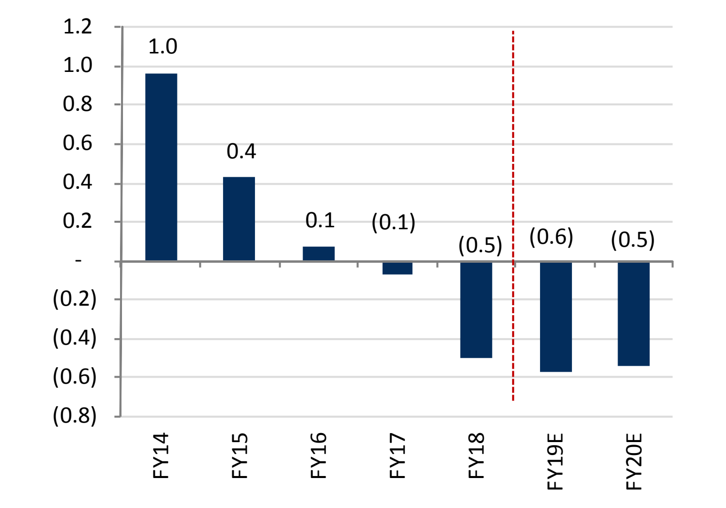
Source: SIAM, HDFC sec Inst Research

MHCV Volume Escalated On Low Base



Source: SIAM, HDFC sec Inst Research

Strong FCF To Drive Down AL's Gearing



Source: Company, HDFC sec Inst Research

Peer Set Comparison

	Mcap (Rs bn)	CMP (Rs/sh)	Reco	TP	Adj EPS (Rs/sh)			P/E (x)			EV/EBITDA (x)			RoE (%)		
					FY18	FY19E	FY20E	FY18	FY19E	FY20E	FY18	FY19E	FY20E	FY18	FY19E	FY20E
Maruti Suzuki	2,830	9,368	NEU	9,432	255.6	322.4	377.3	36.6	29.1	24.8	23.4	19.3	16.6	19.8	21.6	21.7
Bajaj Auto	898	3,105	BUY	3,717	139.5	170.4	198.2	22.3	18.2	15.7	15.2	12.1	9.9	22.5	24.2	24.5
Tata Motors*	856	252	NR	416	20.7	25.3	31.0	12.2	10.0	8.1	7.7	4.7	3.8	9.1	8.7	9.8
Hero Motocorp	699	3,501	BUY	4,405	185.1	206.8	231.8	18.9	16.9	15.1	12.2	10.8	9.4	33.8	33.0	32.5
Ashok Leyland	**324**	**111**	**BUY**	**143**	**5.3**	**6.9**	**7.9**	**20.8**	**16.0**	**14.0**	**10.2**	**8.2**	**7.0**	**23.5**	**26.4**	**26.4**
Force Motors*	32	2,403	NR	3,432	112.2	145.2	190.7	21.4	16.5	12.6	11.4	9.2	7.4	8.5	10.1	11.9
SML Isuzu	11	760	BUY	1,023	5.9	35.2	56.8	129.5	21.6	13.4	28.0	10.5	7.5	2.1	12.2	17.8

Source: Company, HDFC sec Inst Research, * Fair Value

Income Statement Standalone

(Rs mn)	FY16	FY17	FY18	FY19E	FY20E
Net Revenues	**189,373**	**201,401**	**262,479**	**300,200**	**336,404**
Growth (%)	***39.6***	***6.4***	***30.3***	***14.4***	***12.1***
Material Expenses	131,949	139,734	186,213	211,502	237,024
Employee Expenses	13,851	14,801	18,119	20,656	23,341
Other Operating Expenses	21,027	24,842	30,757	35,371	38,201
EBITDA	**22,546**	**22,025**	**27,390**	**32,671**	**37,838**
EBITDA Margin (%)	***11.9***	***10.9***	***10.4***	***10.9***	***11.2***
EBITDA Growth (%)	***119.6***	***(2.3)***	***24.4***	***19.3***	***15.8***
Depreciation	4,879	5,179	5,546	5,732	6,466
EBIT	**17,667**	**16,847**	**21,844**	**26,939**	**31,372**
Other Income (Including EO Items)	1,176	1,363	1,898	2,011	2,132
Interest	2,476	1,554	1,312	385	338
PBT	**16,367**	**16,655**	**22,429**	**28,566**	**33,166**
Tax (Incl Deferred)	4,369	1,070	6,681	8,284	9,950
RPAT	**11,998**	**15,585**	**15,748**	**20,282**	**23,216**
EO (Loss) / Profit (Net Of Tax)	8,203	3,662	130	-	
APAT	**3,795**	**11,923**	**15,618**	**20,282**	**23,216**
Adjusted EPS (Rs)	**13.3**	**214.2**	**31.0**	**29.9**	**14.5**
EPS Growth (%)	***1.4***	***4.3***	***5.3***	***6.9***	***7.9***

Source: Company, HDFC sec Inst Research

Balance Sheet Standalone

(Rs mn)	FY16	FY17	FY18	FY19E	FY20E
SOURCES OF FUNDS					
Share Capital - Equity	2,846	2,846	2,927	2,927	2,927
Reserves	52,296	58,415	68,721	79,104	90,990
Total Shareholders' Funds	**55,142**	**61,262**	**71,648**	**82,032**	**93,919**
Minority Interest					
Long-term Debt	26,451	21,920	10,038	4,457	3,958
Short-term Debt	-	-	-	-	
Total Debt	**26,451**	**21,920**	**10,038**	**4,457**	**3,958**
Net Deferred Taxes	3,291	1,269	2,984	3,269	3,933
Long-term Provisions & Others	3,119	6,509	8,713	9,584	10,542
TOTAL SOURCES OF FUNDS	**88,004**	**91,104**	**93,382**	**99,344**	**112,354**
APPLICATION OF FUNDS					
Net Block	47,920	49,708	49,742	52,639	54,825
Goodwill	547	1,576	2,129	2,152	2,412
Investments	19,804	20,017	27,475	29,475	31,475
LT Loans & Advances	14,775	16,219	18,768	18,012	23,548
Total Non-current Assets	**83,046**	**87,520**	**98,114**	**102,278**	**112,260**
Inventories	16,250	26,301	17,099	21,384	23,963
Debtors	12,509	8,686	9,937	13,159	16,590
Cash & Equivalents	15,931	17,891	40,595	51,108	55,118
Total Current Assets	**44,691**	**52,879**	**67,631**	**85,652**	**95,671**
Creditors	25,877	31,170	46,586	57,946	64,938
Other Current Liabilities & Provns	14,929	18,270	25,776	30,643	30,643
Total Current Liabilities	**40,805**	**49,440**	**72,363**	**88,588**	**95,581**
Net Current Assets	**3,886**	**3,439**	**(4,731)**	**(2,937)**	**90**
TOTAL APPLICATION OF FUNDS	**88,004**	**91,105**	**93,383**	**99,344**	**112,355**

Source: Company, HDFC sec Inst Research

Cash Flow Standalone

(Rs mn)	FY16	FY17	FY18	FY19E	FY20E
Reported PBT	16,367	16,655	22,429	28,566	33,166
Non-operating & EO items	(8,203)	(3,662)	(130)	-	-
Interest expenses	2,476	1,554	1,312	385	338
Depreciation	4,879	5,179	5,546	5,732	6,466
Working Capital Change	8,932	5,852	27,397	5,479	(3,593)
Tax Paid	(4,369)	(1,070)	(6,681)	(8,284)	(9,950)
OPERATING CASH FLOW (a)	**20,082**	**24,507**	**49,874**	**31,878**	**26,428**
Capex	387	(7,971)	(6,134)	(8,652)	(8,652)
Free cash flow (FCF)	*20,469*	*16,537*	*43,740*	*23,225*	*17,775*
Investments	2,600	(213)	(7,458)	(2,000)	(2,000)
Non-operating Income	1,444	(6,010)	143	286	492
INVESTING CASH FLOW (b)	**4,430**	**(14,193)**	**(13,449)**	**(10,367)**	**(10,160)**
Debt Issuance/(Repaid)	(13,560)	(6,029)	(8,750)	(715)	(499)
Interest Expenses	(2,476)	(1,554)	(1,312)	(385)	(338)
FCFE	*4,432*	*8,953*	*33,678*	*22,125*	*16,939*
Share Capital Issuance	-	5,095	126	-	-
Dividend	(3,197)	(5,969)	(7,626)	(9,898)	(11,331)
FINANCING CASH FLOW (c)	**(19,234)**	**(8,458)**	**(17,562)**	**(10,998)**	**(12,167)**
NET CASH FLOW (a+b+c)					
Closing Cash & Equivalents	15,931	17,891	40,595	51,108	55,118

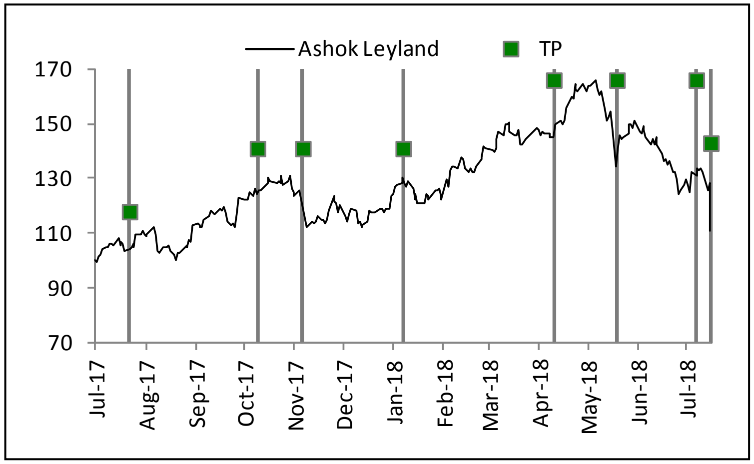
Source: Company, HDFC sec Inst Research

Key Ratios Standalone

	FY16	FY17	FY18	FY19E	FY20E
PROFITABILITY (%)					
GPM	30.3	30.6	29.1	29.5	29.5
EBITDA Margin	11.9	10.9	10.4	10.9	11.2
APAT Margin	2.0	5.9	6.0	6.8	6.9
RoE	7.2	20.7	23.5	26.4	26.4
RoIC (or Core RoCE)	18.6	26.3	31.4	49.1	51.5
RoCE	6.7	17.4	21.2	24.2	24.5
EFFICIENCY					
Tax Rate (%)	26.7	6.4	29.8	29.0	30.0
Fixed Asset Turnover (x)	3.6	3.4	4.2	4.2	4.2
Inventory (days)	*31.3*	*47.7*	*23.8*	*26.0*	*26.0*
Debtors (days)	*24.1*	*15.7*	*13.8*	*16.0*	*18.0*
Payables (days)	*49.9*	*56.5*	*64.8*	*70.5*	*70.5*
Other Current Liab & Provns (days)	*28.8*	*33.1*	*35.8*	*37.3*	*33.2*
Cash Conversion Cycle (days)	5.6	6.9	(27.2)	(28.5)	(26.5)
Debt/EBITDA (x)	1.2	1.0	0.4	0.1	0.1
Net D/E (x)	0.1	(0.1)	(0.5)	(0.6)	(0.5)
Interest Coverage (x)	7.1	10.8	16.6	69.9	92.9
PER SHARE DATA (Rs)					
EPS	1.4	4.3	5.3	6.9	7.9
CEPS	3.0	6.0	7.2	8.9	10.1
Dividend	1.0	2.1	3.0	3.5	4.0
Book Value	19.4	21.5	24.5	28.0	32.1
VALUATION					
P/E (x)	81.1	25.8	20.8	16.0	14.0
P/BV (x)	5.7	5.2	4.5	4.0	3.5
EV/EBITDA (x)	14.2	14.2	10.6	8.5	7.2
EV/Revenues (x)	1.7	1.5	1.1	0.9	0.8
OCF/EV (%)	6.3	7.9	17.2	11.5	9.7
FCF/EV (%)	6.4	5.3	15.1	8.3	6.5
FCFE/Mkt Cap (%)	1.4	2.8	10.4	6.8	5.2
Dividend Yield (%)	0.9	1.9	2.7	3.2	3.6

Source: Company, HDFC sec Inst Research

RECOMMENDATION HISTORY



Date	CMP	Reco	Target
25-Jul-17	104	BUY	118
11-Oct-17	126	BUY	141
9-Nov-17	119	BUY	141
9-Jan-18	127	BUY	141
12-Apr-18	145	BUY	166
22-May-18	134	BUY	166
9-Jul-18	132	BUY	166
18-Jul-18	111	BUY	143

Rating Definitions

BUY : Where the stock is expected to deliver more than 10% returns over the next 12 month period

NEUTRAL : Where the stock is expected to deliver (-)10% to 10% returns over the next 12 month period

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