

## Sector: Automobiles

## Company Update

	Change
Reco: <b>Buy</b>	↔
CMP: <b>Rs. 78</b>	
Price Target: <b>Rs. 98</b>	↑
↑ Upgrade	↔ No change
↓ Downgrade	

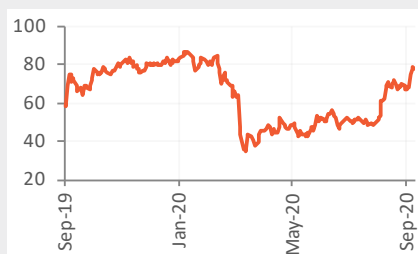
## Company details

Market cap:	Rs. 22,985 cr
52-week high/low:	Rs. 88 / 34
NSE volume: (No of shares)	2.7 lakh
BSE code:	500477
NSE code:	ASHOKLEY
Sharekhan code:	ASHOKLEY
Free float: (No of shares)	141.1 cr

## Shareholding (%)

Promoters	51.5
FII	15.7
DII	14.1
Others	18.7

## Price chart



## Price performance

(%)	1m	3m	6m	12m
Absolute	14.4	53.1	21.7	31.4
Relative to Sensex	13.2	39.1	-13.3	24.8

Sharekhan Research, Bloomberg

Ashok Leyland Ltd (ALL) is witnessing month on month improvement in MHCV sales as economic activities pick up with the Government opening the economy. A progressive improvement in Index of Industrial Production (IIP) point at picking up of industrial activities which is leading to increased MHCV demand. We expect MHCV industry to witness stronger recovery cycle from FY22 driven by normalisation of economic activity and pent up demand post two consecutive years of downcycle in FY20 and FY21. With the launch of a new LCV platform, ALL has closed an important gap in its product portfolio and is expecting to double its addressable market size. Margins are expected to improve 370 bps y-o-y driven by operating leverage. We expect strong 56% earnings CAGR over FY20-23 period. Also, the introduction of an incentive based scrapping policy would significantly boost MHCV volumes benefitting core MHCV players like ALL. At CMP, stock is trading at 7.8x FY23 EV/EBIDTA which is lower than its long-term historical average of 12x. We revise our TP to Rs 98 as we rollover to FY23 earnings. We retain Buy rating on the stock.

**Stronger recovery cycle for MHCV from FY22; market share gains in LCV:** MHCV volumes are improving with the pick-up in economic activities post the unlock measures. Also, the narrowing decline in IIP indicates improvement in industrial activity. ALL MHCV volumes decline has narrowed from 98% y-o-y in May 2020 to 52% y-o-y in August 2020. ALL expects month on month improvement to continue and expects September 2020 sales to be better than August 2020. While FY21 would be impacted by COVID-19, we expect a stronger recovery cycle from FY22 driven by normalization of economic activity and pent up demand considering FY20 and FY21 would be two consecutive years of downcycle. Also, with ALL unveiling its new LCV platform (with launch of Bada Dost and plans to launch variants in future), it expects addressable LCV market to double to 65% and expects market share gains. Increasing proportion of LCV business would further reduce its dependence on the highly cyclical MHCV space.

## Our Call

**Rollover to FY23 earnings; Maintain Buy with revised PT of Rs 98:** With a stronger recovery cycle in MHCV industry from FY22, market share gains in LCV segment, better mix and price hikes, we expect the ALL topline to grow at strong 15% CAGR over FY2020-2023 period. Margins are expected to improve sharply by 370 bps y-o-y driven by benefits of operating leverage. We expect strong 56% earnings CAGR over FY20-23 period. We have introduced FY2023 earnings in this note. At CMP, the stock is trading at 7.8x FY23 EV/EBIDTA which is lower than its long-term historical average of 12x. We increase our TP to Rs 98 as we rollover to FY23 earnings. We retain Buy rating on the stock.

## Key Risks

Prolonged COVID-19 infection can weaken economic sentiments and delay recovery. Pricing pressures to defend domestic market share would affect margins.

Valuation Particulars	Rs cr				
	FY19	FY20	FY21E	FY22E	FY23E
Net sales (Rs cr)	29,055.0	17,467.5	13,871.0	20,564.7	26,853.9
Growth (%)	10.2%	-39.9%	-20.6%	48.3%	30.6%
EBIDTA (Rs cr)	3,135.7	1,173.7	663.9	1,736.2	2,796.8
OPM (%)	10.8%	6.7%	4.8%	8.4%	10.4%
PAT (Rs cr)	2,040.7	395.3	(87.4)	690.7	1,491.6
Growth (%)	16.9%	-80.6%	NA	NA	127.5%
FD EPS (Rs)	7.0	1.3	(0.3)	2.4	5.1
P/E (x)	11.2	57.9	NA	33.1	15.4
P/BV (x)	2.7	3.2	3.2	3.1	2.8
EV/EBITDA (x)	7.0	20.9	36.1	13.3	7.8
RoCE (%)	22.6	4.0	(0.7)	8.2	15.8
RoE (%)	24.5	5.4	-1.2	9.3	18.3

Source: Company; Sharekhan estimates

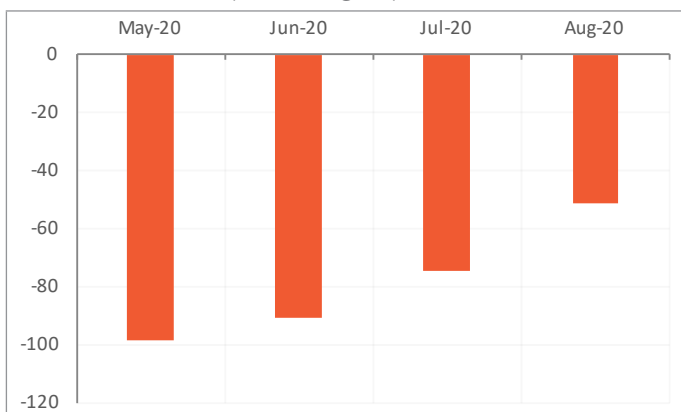
**Launches LCV “Bada Dost” on new platform; to double addressable market:** Recently, Ashok Leyland Ltd (ALL) unveiled the “Bada Dost” light commercial vehicle. Bada Dost is based on a new LCV platform developed in-house by the company with an investment of Rs 350 cr. ALL launched Bada Dost with two variants i3 (2.99 tonne Gross Vehicle Weight) and i4 (3.49 tonne Gross vehicle weight). ALL current LCV line up has Dost (2.5 to 2.8 tonnes) and Partner (7.2 to 7.5 tonnes) and Bada Dost will fill an important product gap. Also, Bada Dost has been launched with left hand drive which would boost ALL volumes in export markets (80% of ALL export markets are left hand drive markets). ALL plans to launch a new product every quarter on the platform which would double its addressable market in LCV’s from current 34% to 65%. We expect the company to gain market share in the LCV space and expect LCV proportion to improve going forward. Increased proportion of LCV would reduce ALL dependence on highly cyclical MHCV industry.

**ALL LCV line up**

2.5 to 2.8 tonnes	<b>2.99 to 3.49 tonnes</b>	7.2 to 7.49 tonnes
Dost (Existing product)	<b>Bada Dost (New launch)</b>	Partner (Existing product)

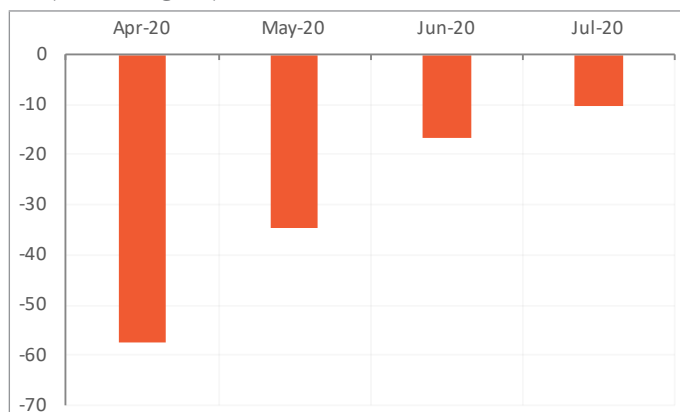
**MHCV volumes picking up; stronger recovery cycle from FY22:** With the Government opening up the economy under the unlock measures, business activities are picking up. Key indicators such as IIP are also showing improvement on a month on month basis indicating a pickup in industrial activities. With improving economy, MHCV volumes are picking up on month on month basis. From 98% y-o-y drop in May 2020, ALL MHCV volumes decline has narrowed down to 52% y-o-y in August 2020. ALL expects month on month improvement to continue with September 2020 volumes expected to be better than August and the company is further raising production capacity. While FY21 would be impacted by COVID-19, we expect MHCV industry to witness strong recovery cycle from FY22. Expected normalization of economic activity coupled with pent up demand (FY20 and FY21 would be two consecutive years of downcycle) would boost MHCV volumes from FY22.

**ALL MHCV volumes (YoY Change %)**



Source: Company, Sharekhan Research

**IIP (YoY Change %)**



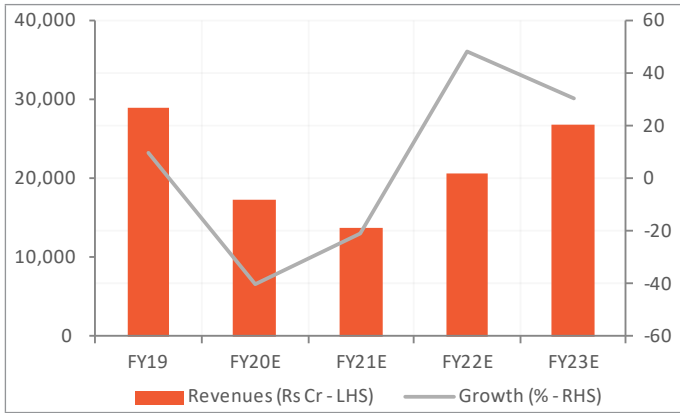
Source: Company, Sharekhan Research

**Operating leverage to drive margin expansion:** ALL MHCV volumes are expected to grow in strong double-digits from FY22 driven by normalisation of economic activity and pent up demand. Also, LCV volumes are expected to increase with the launch of “Bada Dost” variant and doubling of addressable market. We expect ALL volumes to grow at robust 10% CAGR over FY20-23 period driven by uptick in MHCV and increased LCV volumes. With increased share of higher tonnage trucks and price increases due to BS6, we expect ALL revenues to grow at strong 15% CAGR over FY20-23 period. ALL is likely benefit from the operating leverage due to strong topline growth. We expect ALL margins to improve sharply 370 bps y-o-y to 10.3% in FY23.

**Incentive based Scrappage policy can significantly boost volumes:** The Government of India is close to finalizing a scrappage policy for the automotive sector. MHCV are expected to be biggest beneficiaries of the scrappage policy given the higher population of older vehicles. An incentive based scrappage policy is likely to encourage fleet owners to scrap their old vehicles and replace them with new trucks thereby boosting the demand.

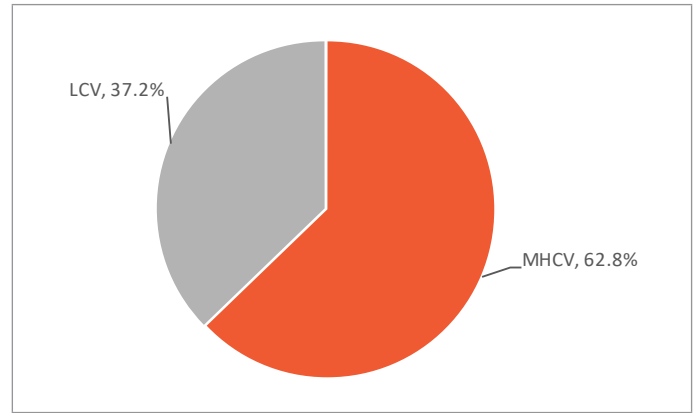
**Financials in charts**

**Revenue trend**



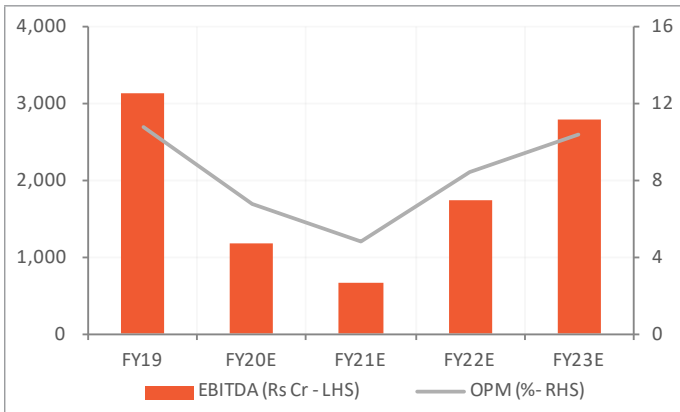
Source: Company, Sharekhan Research

**Segmental mix**



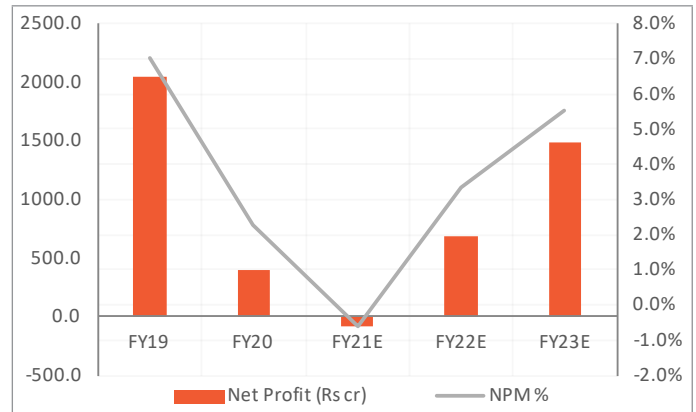
Source: Company, Sharekhan Research

**EBIDTA-OPM trend**



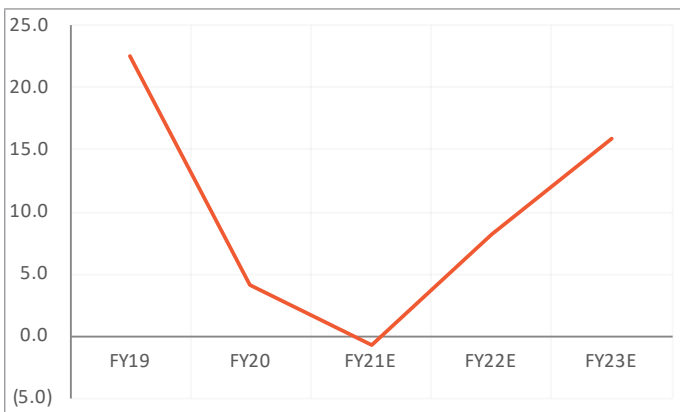
Source: Company, Sharekhan Research

**Net Profit trend**



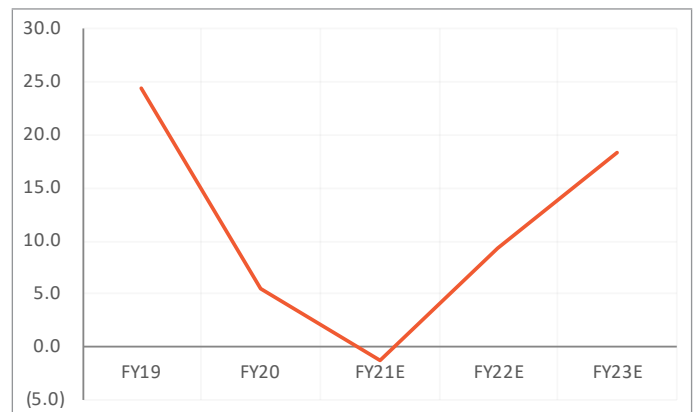
Source: Company, Sharekhan Research

**ROCE trend**



Source: Company, Sharekhan Research

**ROE Trend**



Source: Company, Sharekhan Research

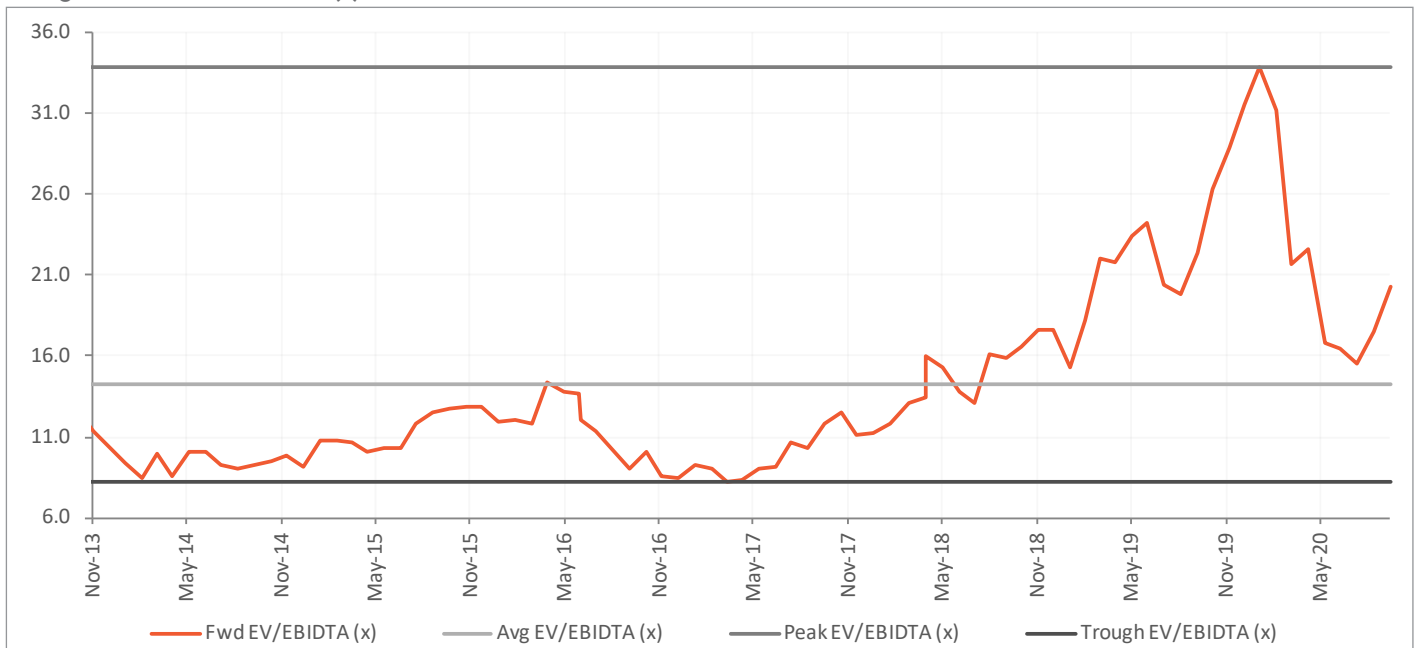
**Outlook**

**Stronger recovery cycle for MHCV from FY22; market share gains in LCV:** MHCV volumes are improving with a pick-up in economic activities post the unlock measures. Also, the narrowing decline in IIP indicates improvement in industrial activity. ALL MHCV volumes decline has narrowed from 98% y-o-y in May 2020 to 52% y-o-y in August 2020. ALL expects month on month improvement to continue and expects September 2020 sales to be better than August 2020. While FY21 would be impacted by COVID-19, we expect stronger recovery cycle from FY22 driven by normalization of economic activity and pent up demand considering FY20 and FY21 would be two consecutive years of downcycle. Also, with ALL unveiling its new LCV platform (with the launch of Bada Dost and plans to launch variants in future), it expects addressable LCV market to double to 65% and expects market share gains. Increasing proportion of LCV business would further reduce ALL dependence on highly cyclical MHCV space.

**Valuation**

**Rollover to FY23 earnings; Maintain Buy with revised PT of Rs 98:** With stronger recovery cycle in MHCV industry from FY22, market share gains in LCV segment, better mix & price hikes, we expect ALL topline to grow at strong 15% CAGR over FY2020-2023 period. Margins are expected to improve sharply by 370 bps y-o-y driven by benefits of operating leverage. We expect strong 56% earnings CAGR over FY20-23 period. We have introduced FY2023 earnings in this note. At CMP, stock is trading at 7.8x FY23 EV/EBIDTA which is lower than its long-term historical average of 12x. We increase our TP to Rs 98 as we rollover to FY23 earnings. We retain our Buy rating on the stock.

One-year forward EV/EBIDTA (x) band



Source: Sharekhan Research

## About company

Ashok Leyland (ALL) is the flagship company of the Hinduja Group and is the second-largest domestic manufacturer of medium and heavy commercial vehicles (MHCVs). ALL derives 70% of volumes from MHCV segment, while light commercial vehicles (LCVs) form the balance 30%. ALL is the market leader for MHCV buses with a market share of 41%, while it is the second-largest player in MHCV trucks having a market share of 33%. Domestic revenue contributes 87% of the revenues while exports contribute the balance 13%.

## Investment theme

Ashok Leyland Ltd (ALL) is witnessing month on month improvement in MHCV sales as economic activities pick up with Government opening up economy. Progressive improvement in IIP point at picking up of industrial activities which is leading to increased MHCV demand. We expect MHCV industry to witness stronger recovery cycle from FY22 driven by normalisation of economic activity and pent up demand post two consecutive years of downcycle in FY20 and FY21. With the launch of new LCV platform, ALL has closed an important gap in its product portfolio and is expecting to double its addressable market size. Margins are expected to improve 370 bps y-o-y driven by operating leverage. We expect strong 56% earnings CAGR over FY20-23 period. Also, the introduction of incentive based scrapping policy would significantly boost MHCV volumes benefitting core MHCV players like ALL. At CMP stock is trading at 7.8x FY23 EV/EBIDTA which is lower than its long-term historical average. Hence, we retain Buy rating on the stock.

## Key Risks

- ◆ Prolonged COVID-19 infection can weaken economic sentiments and delay recovery.
- ◆ Pricing pressures to defend domestic market share would affect margins.

## Additional Data

### Key management personnel

Mr Dhiraj Hinduja	Chairman
Vipin Sondhi	Managing Director & CEO
Gopal Mahadevan	Chief Financial Officer
Nitin Seth	Chief Operating Officer

Source: Company Website

### Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Hinduja Automotive Ltd	34.73
2	Hinduja Bank Switzerland	4.94
3	JP Morgan Chase & Co	4.4
4	Kuwait Investment Authority	1.72
5	Government Pension Fund Global	1.63
6	Norges Bank	1.63
7	ICICI Prudential Life Insurance Company	1.5
8	Vangaurd Group Inc	1.47
9	Blackrock Inc	1.43
10	Life Insurance Corp of India	1.36

Source: Bloomberg

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# Sharekhan

by BNP PARIBAS

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