Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

Ashok Leyland Ltd

Strong performance in Q4; Positive growth prospects

Automobiles		Sharekhan code: ASHOKLEY		
Reco/View: Buy	↔	CMP: **Rs. 130**	Price Target: **Rs. 165**	↓

↑ Upgrade ↔ Maintain ↓ Downgrade

3R MATRIX

	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

ESG Disclosure Score NEW

ESG RISK RATING 37.97

Updated Feb 08, 2022

High Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

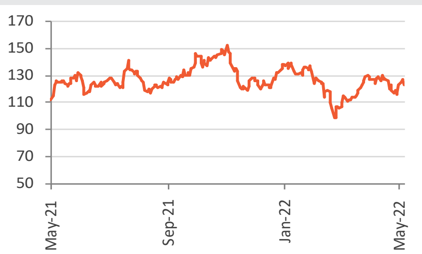
Company details

Market cap:	Rs. 38,162 cr
52-week high/low:	Rs. 153/93
NSE volume: (No of shares)	150 lakh
BSE code:	500477
NSE code:	ASHOKLEY
Free float: (No of shares)	143.49 cr

Shareholding (%)

Promoters	51.1
FII	13.4
DII	21.8
Others	13.7

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-3.6	-7.6	-18.0	9.6
Relative to Sensex	4.0	1.7	-5.3	1.3

Sharekhan Research, Bloomberg

Summary

- We retain our Buy rating on Ashok Leyland Limited (ALL) with a revised PT of Rs 165, owing to growth recovery in the CV industry, led by improvement in economic and infrastructure activities
- Strong performance in Q4FY22 with revenue, EBITDA and PAT were ahead of expectations by 5.2%, 28.9% and 56.7% respectively.
- ALL is expected to benefit from its aggressive strategy of growing its market share through increased penetration across all regions, new product launches and well placed to benefit from e-mobility movement.
- The stock is trading below its average historical multiples at P/E of 18x and EV/EBITDA of 10.1x its FY2024E estimates.

Ashok Leyland (ALL) reported strong operational performance in Q4FY22. Net revenue, EBITDA and PAT were ahead of expectations by 5.2%, 28.9% and 56.7% respectively. Standalone net revenues were up 24.9% y-o-y to Rs8,744 crore, led by a 10.1% improvement in average sales realisation and a 13.4% increase in volumes. EBITDA margin for Q4FY22 expanded 480 bps q-o-q to 8.9% (160 bps higher than estimates), led by operating leverage benefits and cost reductions, partially offset by a 30bps increase in raw material costs. As a result, EBITDA and PAT for Q4FY22 improved 45.3% y-o-y and 111.5% to Rs776 crore and Rs 431 crore respectively. We continue to maintain our positive view on ALL and expect it to be a strong beneficiary of recovery in commercial vehicle (CV) sales in domestic markets, led by an improving macro environment, higher infrastructure spending, and replacement demand. The company expects good opportunities to continue to grow exports, defence, power solutions, light commercial vehicles (LCV), and parts business even as it expands the reach and products of the core medium and heavy commercial vehicle (MHCV) business. ALL's subsidiary, Switch Mobility Limited (SML) is likely to be a beneficiary of the electric vehicle (EV) mobility movement through its strong presence in the UK, India, and Continental Europe. We expect ALL's profitability to improve significantly, with its EBITDA growing at a 91.6% CAGR for FY2022-FY2024E, led by a sharp improvement in operating leverage. Thus, we remain positive on ALL's growth prospects and retain our Buy rating on the stock with a revised price target (PT) of Rs. 165.

Key positives

- Net revenue, EBITDA and PAT were ahead of expectations by 5.2%, 28.9% and 56.7% respectively in Q4FY22, led by a strong improvement in operational performance.
- The company witnessed faster growth in higher tonnage trucks, led by an increase in construction and mining activities.
- EBITDA margin for Q4FY22 expanded 480 bps q-o-q to 8.9% (160 bps higher than estimates), led by operating leverage benefits and cost reductions, partially offset by a 30bps increase in raw material costs.
- ALL's market share in trucks improved 170 bps y-o-y to 30.6% in Q4FY22 versus 28.9% in Q4FY21, driven by the success of the AVTR range of trucks and the launch of the CNG range in ICVs.

Key negatives

- Gross margin declined 30 bps q-o-q to 21.8% in Q4, led by input costs inflation.
- Semi-conductor shortage- continues to impact LCV sales.

Management Commentary

- The management gave a positive outlook for the CV industry and continues to grow opportunities for exports, defence, power solutions, LCV and parts business even as it expands the reach and products of the core MHCV business.
- The management continues to focus on greener technology with a renewed focus on EV products. The company launched two CNG variants of ECOMET during Q4FY22.
- The bus segment is showing signs of strong recovery and is expected to show strong sales growth in FY23E, driven by normalcy in the economy.

Our Call

Valuation - Maintain Buy with a revised PT of Rs. 165: We expect ALL to benefit from the faster recovery in CV volumes and improvement in EBITDA margins, led by operating leverage benefits. ALL is well placed in the industry to benefit from increased economic activities related to infrastructure, mining, and e-commerce, aided by its focus on growing its market share through increased penetration across all regions and new product launches. The company's profitability is expected to improve significantly in the medium term, with its EBITDA expected to post a 166% CAGR over FY2021-FY2023E. Investments by investors and strategic partners in its EV subsidiary can lead to value unlocking and re-rating of the stock going forward. The stock is trading below its average historical multiples at P/E of 18x and EV/EBITDA of 10.1x its FY2024E estimates. We retain our Buy rating on the stock with a revised PT of Rs165.

Key Risks

Pricing pressures to defend domestic market share would affect margins.

Valuation (Standalone) Rs cr

Particulars	FY21	FY22	FY23E	FY24E
Revenues	15,301	21,688	28,303	33,964
Growth (%)	(12.4)	41.7	30.5	20.0
EBIDTA	535	995	2,715	3,651
OPM (%)	3.5	4.6	9.6	10.7
Net Profit	(302)	31	1,355	2,114
Growth (%)	(176.3)	(110.3)	4,271.8	56.0
EPS	(1.0)	1.8	4.6	7.2
P/E	NA	70.4	28.2	18.0
P/BV	5.5	5.8	5.3	4.5
EV/EBIDTA	73.7	39.7	14.2	10.1
ROE (%)	(4.4)	0.5	19.0	24.8
ROCE (%)	(1.8)	2.1	15.9	20.6

Source: Company; Sharekhan estimates

Strong performance in Q4FY22: Ashok Leyland (ALL) reported strong operational performance in Q4FY22. Net revenue, EBITDA and PAT were ahead of expectations by 5.2%, 28.9% and 56.7% respectively. Standalone net revenues were up 24.9% y-o-y to Rs8,744 crore, led by a 10.1% improvement in average sales realisation and a 13.4% increase in volumes. The volume improvement was aided by an increase in infrastructure, mining and e-commerce activities in the country. The improvement in average sales realisation was aided by price hikes and improvement in product mix. EBITDA margin for Q4FY22 expanded 480 bps q-o-q to 8.9% (160 bps higher than estimates), led by operating leverage benefits and cost reductions, partially offset by a 30bps increase in raw material costs. As a result, EBITDA and PAT for Q4FY22 improved 45.3% y-o-y and 111.5% to Rs776 crore and Rs431 crore respectively.

Improvement in ALL's market share in the truck segment: ALL's market share in trucks improved 170 bps y-o-y to 30.6% in Q4FY22 versus 28.9% in Q4FY21, driven by the success of the AVTR range of trucks and the launch of the CNG range in ICVs. The demand for M&HCVs and ICVs remains buoyant backed by strong performance in core sectors such as infrastructure, mining and e-commerce sectors. In FY22, ALL's M&HCV Truck sales registered a growth of 41.7% y-o-y to 61,301 units. The government's increased allocations and spending would further put a thrust on the growth. The management expects the CV segment to do well over the next 3-4 years. The LCV is also performing well and is likely to benefit from the growth in last mile. In FY22, ALL's LCV sales increased by 11.9% y-o-y to 52,222 units.

Bus segment: The bus segment is showing signs of strong recovery and is expected to show strong sales growth in FY23E, driven by normalcy in the economy. ALL is a leader in the bus segment and is expected to see strong growth in the bus sub-segment. In FY22, ALL's bus segment grew by 35.5% y-o-y to 3,789 units.

Switch mobility: The company's EV subsidiary, Switch Mobility Ltd. (SML) has made inroads in the UK, India, and Continental Europe. ALL (SWITCH) has current STU orders of ~655 e-buses in Bengaluru, Mumbai, Gujarat, Chandigarh and Bihar. Currently, there are SWITCH's 115 e-buses running across three cities in India – Chandigarh, Patna and Ahmedabad. Also, Switch has expanded to nine States across three countries – UK, Spain and India. ALL continues to focus on greener technology with a renewed focus on EV products. SML is setting up a new advanced manufacturing facility in Valladolid, Spain, which is expected to produce buses in a year's time. The plant will comprise two state-of-the-art production lines and will be entirely carbon neutral from inception. With Euro 100 million of investment planned for the site over the next decade, the facility will play a key role in rejuvenating the Soto de Medinilla area around Valladolid. Phase-1 of the new development will house the production of SML's new 12-metre bus, designed for the European market. Phase-2 and Phase-3 will add battery-assembly capabilities and production of SML's zero-carbon LCV from 2024. We believe SML is well poised to benefit from the increasing requirements for EVs in Europe. The EV subsidiary is looking out for partners and strategic investors, which will put growth on a faster track.

Exports: International operations saw a growth of 37.7% y-o-y in FY22 to 11,014 units in the CV segment and remains a focus area for the company. ALL is planning to increase its distribution network in Africa and other Southeast Asian countries to boost exports. With the 'Atmanirbhar Bharat' push in the defence sector, the government is targeting increased sourcing from domestic private players, which would benefit players such as ALL. In exports, the company is improving its base in Africa and the Middle East, while strengthening its position in SAARC countries.

Management outlook: The management is positive for growth in the medium term, as India's GDP is expected to grow by 9.5% in FY22. The company sees good opportunities to continue to grow the exports, defence, power solutions, LCV and parts business even as it expands the reach and products of the core MHCV business. The increase in economic activities related to infrastructure, mining and e-commerce would fuel demand for LCVs and M&HCVs. The management expects demand for passenger segments to improve after the opening of schools, offices and normalcy of other activities. The vaccination drive would further help in advancing the demand for passenger vehicles. Also, the normal hygiene and social distancing would lead to fewer passengers in a bus, which would add to bus demand in the medium term. Management continues to focus on greener technology with a renewed focus on EV products. The company expects industry demand to improve as the economy opens up and business activities gain momentum.

Focus on digitisation and new launches: ALL's focus on digitisation remains a key focus for driving demand for CV business. The company's focus on its digital marketplace platform has helped it to tap market shares from unorganised aftersales and services markets. The digit platforms help in monitoring the fleet utilisation and productivity and alarm customers of any critical issues in the fleet. The company's new launches such as Dost, Bada Dost and ATVR have received positive feedback from customers. The company to grow its businesses from new launches. The phoenix platform on which Dost and Bada Dost were launched, is expected to receive more launches over the next few years. The company launched 4 AVTR range of M&HCV trucks and 2 CNG variants of Ecomet in the truck segment during Q4FY22. Further, the company plans to launch the development of CNG/LNG products across the range including DOST, BADA Dost, ECOMET, AVTR and buses.

Positive outlook going forward: The company expects the industry demand to improve as the economy opens up and business activities gain momentum. ALL expect the CV industry to report growth over the next few quarters. The company is witnessing divergent trends for various segments in the CV industry. Tippers, multi-axle vehicles, and light and intermediate commercial vehicles are performing better, while the bus segment is showing strong signs of recovery. ALL are expected to benefit from new launches in intermediate commercial vehicles (ICV). The Bada Dost in LCV has been well received by the market. We expect Bada Dost to contribute to ALL's strong growth going forward. We expect ALL's profitability to improve significantly, with its EBITDA growing at a 91.6% CAGR for FY2022-FY2024E, led by sharp improvement in operating leverage.

Results (Standalone) Rs cr

Particulars	Q4FY22	Q4FY21	YoY (%)	Q3FY22	QoQ (%)
Net sales	8,744	7,000	24.9	5,535	58.0
Total operating expenses	7,968	6,466	23.2	5,311	50.0
Operating profit	776	534	45.3	224	246.6
Depreciation	195	218	-10.6	190	3.0
Interest	76	77	-0.8	67	14.4
Other Income	24	38	-36.3	18	37.0
PBT	528	277	91.0	(15)	NA
Tax	97	73	33.7	21	356.5
Reported PAT	901	241	273.7	6	NA
Adjusted PAT	431	204	111.5	(36)	NA
Recurring EPS	1.5	0.7	111.5	-0.1	NA

Source: Company, Sharekhan Research

Key ratios (Standalone)

Particulars	Q4FY22	Q4FY21	YoY (bps)	Q3FY22	QoQ (bps)
Gross margin (%)	21.8	23.1	-130	22.1	-30
EBIDTA margin (%)	8.9	7.6	120	4.0	480
EBIT margin (%)	6.6	4.5	210	0.6	600
Net profit margin (%)	4.9	2.9	200	(0.7)	NA
Effective tax rate (%)	18	26	-790	NA	NA

Source: Company, Sharekhan Research

Volume Analysis (Rs per Vehicle)

Particulars	Q4FY22	Q4FY21	YoY (%)	Q3FY22	QoQ (%)
Volumes (units)	48,719	42,950	13.4	34077	43.0
Realisation	17,94,842	16,29,916	10.1	16,24,310	10.5
RM/vehicle	14,04,415	12,53,409	12.0	12,65,695	11.0
Gross Profit/Vehicle	3,90,427	3,76,508	3.7	3,58,614	8.9
EBITDA/Vehicle	1,59,289	1,24,368	28.1	65,701	142.4
PAT/vehicle	88,489	47,455	86.5	-10,641	NA

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Expect a strong recovery in CV sales

We see strong underlying demand for CVs domestically. We expect the strongest recovery in the CV segment in FY2022 and FY2023, driven by improved economic activities, low-interest rate regime, and better financing availability. We expect strong improvement in M&HCV sales to continue, driven by a rise in e-commerce, agriculture, infrastructure, and mining activities post normalisation of COVID.

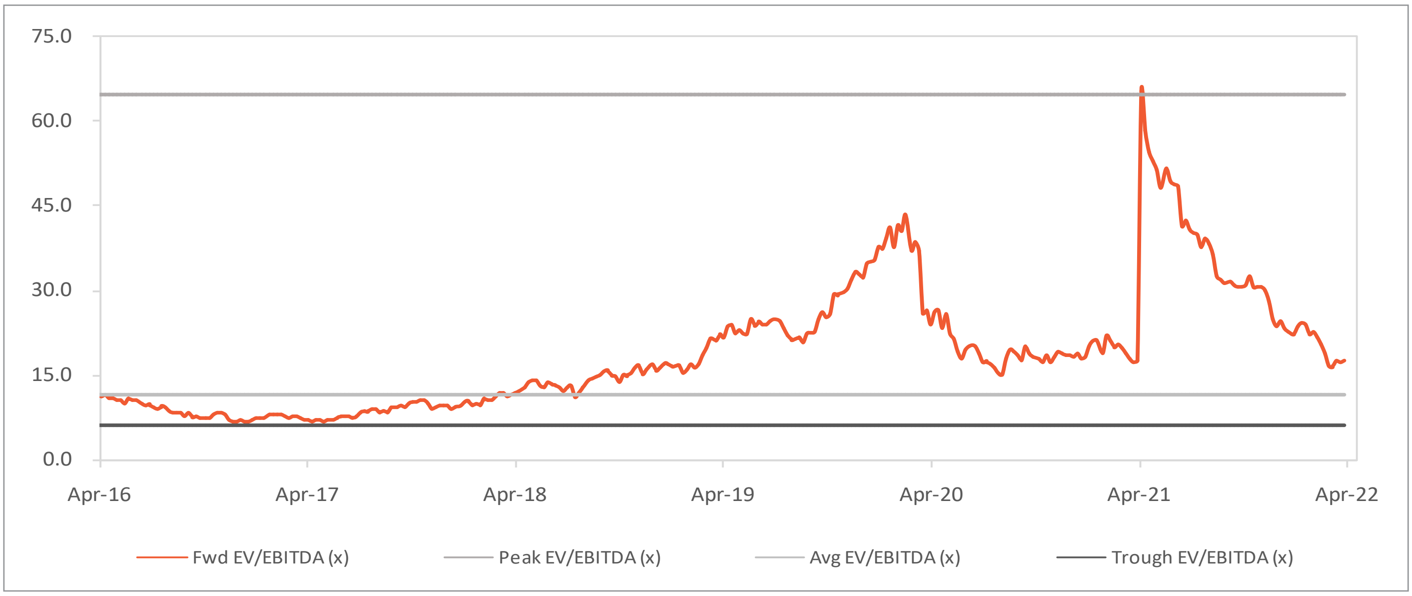
■ Company outlook - Growth strategies in place to drive growth in medium term

ALL is likely to be the key beneficiary from the expected recovery in the domestic CV industry, as the lockdowns are lifted in the country and economy normalises. There has been a continuous uptick in economic activities after the government announced unlock measures. There has been substantial improvement in infrastructure, road construction, and mining activities. ALL will benefit from replacement demand, which is likely to arise due to lower ownership costs for BS-VI vehicles as compared to BS-IV vehicles. Demand for the passenger segment is set to improve after the opening of schools and offices and the normalcy of other activities. The vaccination drive would further help in advancing the demand for passenger vehicles. Moreover, normalisation of hygiene and social distancing would lead to fewer passengers in a bus, which would add to bus demand in the long term. The company is well placed to benefit from growth in exports, defence, power solutions, LCV, and parts business even as it expands the reach and products of the core MHCV business.

■ Valuation - Maintain Buy with a revised PT of Rs. 165

We expect ALL to benefit from faster recovery in CV volumes and improvement in EBITDA margins, led by operating leverage benefits. ALL is well placed in the industry to benefit from increased economic activities related to infrastructure, mining, and e-commerce, aided by its focus on growing its market share through increased penetration across all regions and new product launches. The company's profitability is expected to improve significantly in the medium term, with its EBITDA expected to post a 166% CAGR over FY2021-FY2023E. Investments by investors and strategic partners in its EV subsidiary can lead to value unlocking and re-rating of the stock going forward. The stock is trading below its average historical multiples at P/E of 18x and EV/EBITDA of 10.1x its FY2024E estimates. We retain our Buy rating on the stock with a revised PT of Rs165.

One-year forward EV/EBITDA (x) band



Source: Sharekhan Research

Peer Comparison

Companies	CMP (Rs cr)	P/E (x)			EV/EBITDA (x)			ROCE (%)		
		FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E
Ashok Leyland	130	NA	70.4	28.2	73.7	39.7	14.2	-	0.5	19.0
Tata Motors	418	-	-	22.6	7.0	8.4	5.8	4.7	1.2	5.7
Mahindra & Mahindra	905	27.5	21.3	17.9	15.3	12.0	10.0	13.8	15.7	16.9

Source: Company; Sharekhan Research

About company

ALL is the flagship company of Hinduja Group and is the second-largest domestic manufacturer of MHCVs. ALL derives 70% of its volumes from the MHCV segment, while 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% to the revenue, while exports contribute the balance 13%.

Investment theme

We believe the CV industry is poised for an upturn in the market due to faster-than-expected recovery in economic activities. There has been a continuous uptick in economic activities after the government announced unlock measures. ALL is the second largest MHCV manufacturer with 32% market share. In MHCV buses, ALL is the market leader commanding market share of 45%, while its market share stands at 29% in MHCV trucks. ALL is focusing on reducing its dependence on the cyclical truck business, which constitutes about 65% of revenue currently. ALL is improving its LCV business and is targeting market share gains with the launch of new products. We are positive on ALL due to faster-than-expected recovery in economic activities, especially in infrastructure development, road construction, and mining, which would likely spur demand for new trucks. Demand for CVs is expected to arise from replacement as well as new demand. Moreover, ALL is focusing on enhancing CV exports (by introducing new products and network expansion) and increasing revenue from replacement (driven by increased digitisation and network enhancement) and defence segment (through the government's Atmanirbhar Bharat push). The government is finalising a scrappage scheme for the automotive sector. An incentive-based scrappage scheme (providing incentives on new truck purchase in lieu of scrapping old trucks) would significantly boost demand and would be positive for the company. Hence, we retain our Buy rating on the stock.

Key Risks

- Prolonged COVID-19 pandemic can disrupt economic sentiments and affect prospects of the CV industry's recovery.
- Pricing pressures to defend domestic market share would affect margins. Also, if the commodity prices continue to rise going forward, can affect the company's profitability.

Additional Data

Key management personnel

Mr Dhiraj Hinduja	Chairman
Vipin Sondhi	Managing Director and Chief Executive Officer
Gopal Mahadevan	Director and Chief Financial Officer
K M Balaji	Vice President – Corporate Finance

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Hinduja Automotive Ltd	34.7
2	Citibank NA	11.2
3	Hinduja Bank Switzerland	4.9
4	Mirae Asset Fund	2.5
5	Nippon Life India Trustee Ltd	2.3
6	Schroder International Selection Fund	1.8
7	Platinum International Fund	1.6
8	Matthews Pacific Tiger Fund	1.5
9	Life Insurance Corp of India	1.4
10	HDFC Life Insurance	1.0

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

Sharekhan

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