Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

Ashok Leyland Ltd

Focus on profitable volume growth

Automobiles	Sharekhan code: ASHOKLEY

Reco/View: Buy	↔	CMP: Rs. 150	Price Target: Rs. 181	↔

↑ 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	14.60
Updated May 08, 2023	

Low Risk

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

Source: Morningstar

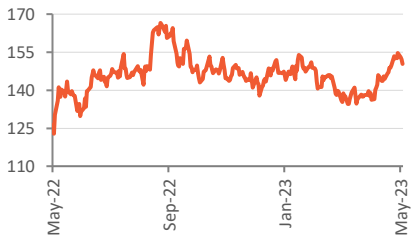
Company details

Market cap:	Rs. 44,033 cr
52-week high/low:	Rs. 169 / 127
NSE volume: (No of shares)	88.7 lakh
BSE code:	500477
NSE code:	ASHOKLEY
Free float: (No of shares)	143.5 cr

Shareholding (%)

Promoters	51.1
FII	14.9
DII	22.2
Others	11.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	10.4	0.3	-1.6	19.0
Relative to Sensex	6.8	-0.5	-1.8	5.0

Sharekhan Research, Bloomberg

Summary

- We retain our Buy rating on Ashok Leyland Limited (ALL) with a revised PT of Rs. 181 on expectation of an 11% volume CAGR along with 110bps expansion in EBITDA margin in the next two years, recovery in the bus segment, and RM cost tailwind.
- Operating margin performance in Q4FY2023 was marginally above estimates.
- ALL is expected to benefit from its aggressive strategy of growing its market share through increased penetration across all regions and new product launches.
- The stock is trading at a P/E of 17.6x and EV/EBITDA of 8.5x its FY2025E.

Ashok Leyland Limited's (ALL) operating performance in Q4FY2023 was marginally above estimates and translated into better-than-estimated bottom-line performance. Revenue increased by 28.7% q-o-q to Rs. 11,626 crore (vs. estimate of Rs. 11,730 crore) on account of a 25.5% q-o-q increase in volumes and a 2.6% q-o-q increase in ASPs. EBITDA increased by 60% q-o-q to Rs. 1,276 crore (vs. our estimate of Rs. 1,236 crore). EBITDA margin expanded by 210 bps q-o-q to 11% (vs. estimate of 10.5%) on account of 70bps q-o-q expansion in gross margin and operating leverage. With this operating performance, APAT increased by 96.1% q-o-q to Rs. 695 crore (against estimate of Rs. 633 crore). The company has announced a dividend of Rs. 2.6/share for FY2023. Going forward, the company has shared a positive outlook for the CV industry in FY24E and has guided 10-12% growth in the CV segment in FY2024. Further, ALL aims to outperform the industry's growth, led by expanding market share in the north and east parts of the country, network expansion, and regular product launches. We believe the industry may observe moderation in growth in Q1FY2024 on account of strong pre-buying in Q4FY2023 and the CV industry would resume its traction from Q2FY2024. ALL's subsidiary, Switch Mobility Limited (SML) is likely to benefit from the electric vehicle (EV) mobility movement through its strong presence in the U.K., India, and Continental Europe. We remain positive on ALL's growth prospects and retain our Buy rating on the stock with a revised price target (PT) of Rs. 181.

Key positives

- Gross margin expansion (70 bps q-o-q) and operating leverage translated into a 210 bps q-o-q expansion in EBITDA margin to 11% against expectation of 10.5%.
- Interest rate came down from Rs. 80 crore in Q3FY2023 to Rs. 63 crore in Q4FY2024 and supported the bottom-line growth.
- Despite 67% growth in revenue in FY2023, capex stands at Rs. 500 crore in FY2023 compared to Rs. 400 crore in FY2022.

Key negatives

- 28.7% topline growth was largely driven by 25.5% q-o-q volume growth as ASP grew by mere 2.6% q-o-q and, hence, its topline missed estimates by 0.9%.
- While gross margin expanded by 70 bps q-o-q, RM cost/unit still increased by 1.7% q-o-q, marginally lower than ASP growth of 2.6%.

Management Commentary

- The CV industry is expected to grow at a double-digit rate in FY2024 on account of revival in replacement demand, strong traction in the bus segment, and increased infra spending.
- ALL aims for double-digit EBITDA margin in the medium term on account of RM cost tailwind and lower discounting trend.
- Export volumes are expected to improve in FY2024 because of recovery in a few of its export markets.

Our Call

Valuation – Maintain Buy with an unchanged PT of Rs. 181: Post reporting marginally above estimated operating performance, management has guided for double-digit volume growth in the CV industry in FY2024 and targets to outperform the CV industry's growth. Management assumes that recovery in replacement demand and revival in few of its export markets would support volume traction in FY2024. ALL is strategically expanding its dealer network and launching new products to gain market share. We believe the shift of the industry from discount-based volume growth model to a profitability-driven volume growth model would augur well for the industry. Management targets for double-digit EBITDA margin in the medium term on account of reduction in discounts, RM cost tailwinds, and healthy volume growth. 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. Further, the company is optimistic on its EV road map via Switch Mobility. We maintain our Buy rating on the stock with an unchanged target price (TP) of Rs. 181 on expectation of an 11% volume CAGR along with a 110bps expansion in EBITDA margin in the next two years, recovery in the bus segment, and RM cost tailwind.

Key Risks

Pricing pressures to defend the domestic market's share would affect margins and adverse macroeconomic trends.

Valuation (Standalone) Rs cr

Particulars	FY21	FY22	FY23P	FY24E	FY25E
Revenues	15,301	21,688	36,144	41,039	45,557
Growth (%)	.	41.7	66.7	13.5	11.0
EBIDTA	535	995	2,931	3,488	4,214
OPM (%)	3.5	4.6	8.1	8.5	9.3
APAT	(302)	31	1,296	1,957	2,495
Growth (%)	-	-	-	51.0	27.5
AEPS	(1.0)	0.1	4.4	6.7	8.5
P/E	-	-	34.0	22.5	17.6
P/BV	6.3	6.0	5.2	4.6	3.9
EV/EBIDTA	82.0	41.9	13.7	10.8	8.5
ROE (%)	-4.3	0.4	15.4	20.3	22.2
ROCE (%)	-0.7	3.0	13.0	17.7	19.5

Source: Company; Sharekhan estimates

Optimistic outlook

- The CV industry may witness growth moderation in Q1FY2024 due to robust pre-buying in Q4FY2023; however, growth momentum is expected to pick up from Q2FY2024.
- Management has shared its optimistic outlook for the CV industry for FY2024 and has guided for 10-12% growth in the CV industry on account of revival in the bus segment, recovery in replacement demand, and continued traction in the MHCV segment, led by rising infra spending.
- Further, the company aims to outperform the industry via increasing market share in its relatively weak territories (North and East markets), dealership expansion, and regular product launches.
- Export volumes are expected to register healthy growth in FY2024 on expectation of recovery in few of its export markets.
- The revival in the CNG segment would drive its performance in FY2024 as its CNG products are well accepted in the market.
- Capex: Rs. 600-750 crore for FY2024.

EBITDA margin : Looking for double-digit margin

- With soft RM cost trend, new product launches, and regular price hikes, management targets for a double-digit margin in the medium term.
- ALL has increased prices by 2% in April to pass on the increase in input cost to customers.
- The shift of industry from discount-based growth model to profit-based discount model would support EBITDA margin expansion in the medium term.

Switch mobility: a long-term EV play

- ALL is optimistic on the growth prospects in the EV space and assumes that switch mobility would have healthy penetration in the EV space in domestic as well as export markets.
- It has lined up multiple products to launch in the EV space in the coming period.
- ALL has planned an investment of Rs. 1,200 crore in Switch Mobility in the next 12 months.

Change in estimates

	Earlier		New		% change	
	FY24E	FY25E	FY24E	FY25E	FY24E	FY25E
Revenue	40462	46531.5	41,039	45,557	1.4%	-2.1%
EBITDA	3422	4,114	3,488	4,214	2.0%	2.4%
EBITDA margin	8.5%	8.8%	8.5%	9.3%		
PAT	1928	2,481	1,957	2,495	1.5%	0.6%
EPS	6.6	8.5	6.7	8.5	1.5%	0.6%

Source: Company; Sharekhan Research

Results (Standalone) Rs cr

Particulars	Q4FY23	Q4FY22	YoY (%)	Q3FY23	QoQ (%)
Net sales	11,626	8,744	33.0	9,030	28.7
Total operating expenses	10,350	7,968	29.9	8,232	25.7
Operating profit	1,276	776	64.4	797	60.0
Depreciation	184	195	(5.9)	189	(2.7)
Interest	63	76	(17.9)	80	(21.9)
Other Income	39	24	61.1	32	23.2
PBT	1,068	528	102.1	560	90.9
Tax	373	97	283.5	205	81.8
Reported PAT	751	901	(16.6)	361	108.0
Adjusted PAT	695	431	61.2	354	96.1
Recurring EPS	2.37	1.47	61.2	1.2	96.1

Source: Company; Sharekhan Research

Key ratios (Standalone)

Particulars	Q4FY23	Q4FY22	YoY (bps)	Q3FY23	QoQ (bps)
Gross margin (%)	24.4	21.8	270	23.7	70
EBIDTA margin (%)	11.0	8.9	210	8.8	210
Net profit margin (%)	6.0	4.9	100	3.9	210
Effective tax rate (%)	34.9	18.4	1,650	36.7	(170)

Source: Company; Sharekhan Research

Volume Analysis (Rs per Vehicle)

Particulars	Q4FY23	Q4FY22	YoY (%)	Q3FY23	QoQ (%)
Volumes (units)	59,697	48,719	22.5	47,562	25.5
Realisation	19,47,446	17,94,842	8.5	18,98,505	2.6
RM/vehicle	14,72,213	14,04,415	4.8	14,47,763	1.7
Gross Profit/Vehicle	4,75,233	3,90,427	21.7	4,50,742	5.4
EBITDA/Vehicle	2,13,703	1,59,289	34.2	1,67,642	27.5
PAT/vehicle	1,16,418	88,489	31.6	74,513	56.2

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector Outlook – Expect steady recovery in CV sales

While the CV segment may witness growth moderation in FY2024 due to a high base, but we believe the CV industry would grow in high single-digit or low double-digit rate in FY2024, largely driven by the recovery in replacement demand and rise in demand for the bus segment. However, the traction would be visible more from Q2FY2024 and the industry would follow the trend in infra spending and macro activities.

■ Company Outlook – Growth strategies in place to drive growth in the medium term

ALL is likely to be the key beneficiary of the expected traction in the domestic CV industry, driven by traction in the macro economy. Further, ALL has been looking for an improvement in EBITDA margin, led by focusing on profit-driven market share expansion strategy. ALL will benefit from replacement demand, which is likely to arise due to aging of vehicle population and requirement of cost-effective transportation solutions. 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 an unchanged PT of Rs. 181

Post reporting marginally above estimated operating performance, management has guided for double-digit volume growth in the CV industry in FY2024 and targets to outperform the CV industry's growth. Management assumes that recovery in replacement demand and revival in few of its export markets would support volume traction in FY2024. ALL is strategically expanding its dealer network and launching new products to gain market share. We believe the shift of the industry from discount-based volume growth model to a profitability-driven volume growth model would augur well for the industry. Management targets for double-digit EBITDA margin in the medium term on account of reduction in discounts, RM cost tailwinds, and healthy volume growth. 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. Further, the company is optimistic about its EV road map via Switch Mobility. We maintain our Buy rating on the stock with an unchanged target price (TP) of Rs. 181 on an expectation of an 11% volume CAGR along with a 110bps expansion in EBITDA margin in the next two years, recovery in the bus segment, and RM cost tailwind.

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%, while exports contribute to the balance 13%.

Investment theme

We believe the CV industry is poised for a steady upturn in the market due to a faster-than-expected recovery in economic activities. ALL is the second largest MHCV cargo player in the domestic market and enjoys healthy market share in domestic MHCV passenger carrier market. Its market share in MHCV cargo segment stood at 32.3% and in MHCV passenger carrier stood at 28.03% in Fy23. We are positive on ALL due to the 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 and 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). An incentive-based scrappage scheme (providing incentives on new truck purchases 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

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

Dhiraj Hinduja	Chairman
Shenu Agarwal	MD & CEO
Gopal Mahadevan	Director and Chief Financial Officer
K M Balaji	Vice President – Corporate Finance

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Hinduja Automotive Ltd	34.7
2	Citigroup Inc	12.0
3	Hinduja Bank Switzerland	4.9
4	Matthews International Capital Management LLC	2.4
5	Mirae Asset Global Investments Co Ltd	2.1
6	ICICI Prudential Asset Management Co Ltd/India	1.9
7	Vanguard Group Inc/The	1.8
8	Schroders PLC	1.5
9	HDFC Life Insurance Co Ltd	1.4
10	SBI Funds Management Ltd	1.4

Source: Bloomberg

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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

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