

Ashok Leyland

29 June 2020

Reuters: ASOK.NS; Bloomberg: AL IN

Decent Quarter, Bleak CV Outlook

Ashok Leyland's (AL) reported 4QFY20 adj PAT of Rs114mn was down ~98% YoY mainly on account of lower EBITDA margin and higher depreciation and was below our estimate. AL reported an exceptional loss of Rs654mn during the quarter (Rs1bn for FY20) towards provision for impairment of investments in Optare. Net revenue of Rs38.4bn, down 56.6% YoY, was ahead of our estimate. ASP grew by 1.3% YoY and 16.9% QoQ due to better product mix. EBITDA margin stood at 4.8%, down 80bps QoQ and was 120bps below our estimate. This decline was largely due to higher employee expenses (10.7% of revenue vs estimated 8%), partially offset by improvement in gross margin (+240bps QoQ) on better product mix, lower discounts, benign commodity costs and cost reduction efforts. Higher depreciation and interest cost, partially offset by higher other income led to PBT (adj for exceptional item) loss of Rs34mn. Domestic demand scenario continues to remain weak on account of weak underlying economic growth. However, some segments within M&HCVs (like tippers) have started showing improvement in demand. Demand for Buses is expected to see a slower recovery as people shift away from public transport. Products on its modular platform 'AVTR' are seeing good initial traction and the management expects to see strong benefits out of it going ahead in terms of market share gains, higher costs savings, better inventory management and better operational efficiency. The management stated that AL is very well positioned in SCV and LCV market with market share gains over the last few years. AL will be focusing on increasing the addressable market by filling production gap. New LCV platform 'Phoenix' will be launched within the next 3 months, which will further boost its market position and help in further market share gains. Overall, the management expects that there will be pent-up demand over the next 60-90 days, which will start reflecting in 2QFY21. The management believes that industry has likely bottomed out and will witness some pick-up in demand in 2QFY21 and expects demand to be much better from 3QFY21 onwards on the back of economic recovery. AL is using this slowdown as an opportunity to implement some structural measures, including cost reduction, focus on productivity and cash flows and new product development, which the management believes will make the company more resilient. The cost reduction program (K54) helped save Rs5.4bn in FY20 and the company is looking at another Rs6-6.5bn saving in FY21. FY20 capex was down to about ~Rs12.3bn vs earlier guided Rs18bn. Most of its capex towards new platforms and BS-VI transition has come to an end and will incur only maintenance capex going forward. It has been raising buffer liquidity by way of debt, but its net debt as on date stands at ~Rs40bn (~0.45x equity). It has placed ICDs worth Rs5bn with its parent's group companies as part of treasury management operation. These ICDs are short term in nature and will earn 3-4% higher return than bank deposits (yields are ~9.5%-10.5%). We have revised our volume forecast by -23.8%/-14.3% and PAT forecast by -75.4%/-7.0% for FY21E/22E, respectively. We expect a revival in CV cycle only from FY22, led by economic recovery and favorable base. We reduce our target price to Rs51.7 based on target multiple of 17x. We downgrade our rating to ACCUMULATE given the sharp rally in the share price in the last two months.

Downgrade to Accumulate

Sector: Automobiles

CMP: Rs52

Target Price: Rs51.7

Downside: 1%

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Key Data

Current Shares O/S (mn)	2,935.5
Mkt Cap (Rsbn/US\$bn)	154/2.0
52 Wk H / L (Rs)	91/34
Daily Vol. (3M NSE Avg.)	46,957,630

Price Performance (%)

	1 M	6 M	1 Yr
Ashok Leyland	20.4	(34.0)	(38.8)
Nifty Index	15.0	(14.4)	(12.4)

Source: Bloomberg

Y/E March (Rsmn)	4QFY19	3QFY20	4QFY20	YoY (%)	QoQ (%)	FY19	FY20	YoY (%)
Volume (units)	59,518	31,200	25,504	(57.1)	(18.3)	197,366	125,240	(36.5)
Avg. realisation (Rs)	1,486,261	1,287,067	1,505,042	1.3	16.9	1,472,136	1,394,720	(5.3)
Net sales	88,459	40,157	38,385	(56.6)	(4.4)	290,550	174,675	(39.9)
COGS	64,293	29,532	27,290	(57.6)	(7.6)	206,796	123,692	(40.2)
% of sales	72.7	73.5	71.1	(1.6)	(2.4)	71.2	70.8	(0.4)
Gross margin %	27.3	26.5	28.9	160bps	240bps	28.8	29.2	40bps
Employee costs	5,735	2,728	4,097	(28.6)	50.2	20,988	16,151	(23.0)
% of sales	6.5	6.8	10.7	4.2	3.9	7.2	9.2	2.0
Other expenses	8,578	5,645	5,168	(39.7)	(8.4)	31,409	23,096	(26.5)
% of sales	9.7	14.1	13.5	3.8	(0.6)	10.8	13.2	2.4
EBITDA	9,854	2,252	1,830	(81.4)	(18.7)	31,357	11,737	(62.6)
EBITDA margin %	11.1	5.6	4.8	(630bps)	(80bps)	10.8	6.7	(410bps)
Depreciation	1,598	1,575	1,877	17.5	19.2	6,210	6,698	7.9
Interest expenses	166	337	331	99.3	(1.7)	704	1,095	55.5
Other income	91	223	344	279.3	54.2	1,099	1,233	12.2
Exceptional exp/(inc)	117	22	687	-	-	575	1,558	-
PBT	8,064	542	(721)	(108.9)	(233.1)	24,968	3,619	(85.5)
Tax	1,535	264	(148)	(109.6)	(155.9)	5,136	1,224	(76.2)
Effective tax rate %	19.0	48.8	20.5	-	-	20.6	33.8	-
Reported PAT	6,529	278	(573)	(108.8)	(306.6)	19,832	2,395	(87.9)
Adj PAT	6,646	299	114	(98.3)	(61.9)	20,407	3,953	(80.6)
Adj PAT margin %	7.5	0.7	0.3	(720bps)	(40bps)	7.0	2.3	(430bps)
EPS	2.3	0.1	0.04	(98.3)	(61.9)	7.0	1.3	(80.6)

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 1: Financial summary

Y/E March (Rsmn)	FY18	FY19	FY20	FY21E	FY22E
Volume (units)	174,851	197,366	125,240	101,240	133,127
YoY growth (%)	20.5	12.9	(36.5)	(19.2)	31.5
Net sales	262,479	290,550	174,675	160,933	215,321
YoY growth (%)	31.1	10.7	(39.9)	(7.9)	33.8
EBITDA	27,390	31,357	11,737	9,817	18,948
EBITDA margin (%)	10.4	10.8	6.7	6.1	8.8
Adjusted PAT	15,748	20,407	3,953	1,508	8,919
EPS	5.4	7.0	1.3	0.5	3.0
YoY change (%)	35.1	29.6	(80.6)	(61.9)	491.4
RoCE (%)	29.8	29.2	5.9	3.2	11.3
RoE (%)	22.0	24.5	5.4	2.1	11.3
P/E (x)	9.7	7.5	38.6	101.3	17.1
EV/Sales (x)	0.3	0.4	0.8	0.9	0.6
EV/EBITDA (x)	3.3	3.7	12.2	14.4	6.9

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Change in our estimates

Y/E March (Rsmn)	New estimate		Old estimate		Change (%)	
	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
Volume	101,240	133,127	132,818	155,358	(23.8)	(14.3)
Net sales	160,933	215,321	191,252	230,452	(15.9)	(6.6)
EBITDA	9,817	18,948	14,535	19,127	(32.5)	(0.9)
EBITDA margin (%)	6.1	8.8	7.6	8.3	(150bps)	50bps
Adj. PAT	1,508	8,919	6,131	9,586	(75.4)	(7.0)

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Deviation of consensus estimates from actual performance in 4QFY20

(Rsmn)	Actual	Our estimate	Deviation
	4QFY20	4QFY20	(%)
Net sales	38,385	34,115	12.5
EBITDA	1,830	2,047	(10.6)
EBITDA (%)	4.8	6.0	(120bps)
Adj. PAT	114	382	(70.1)

Source: Nirmal Bang Institutional Equities Research

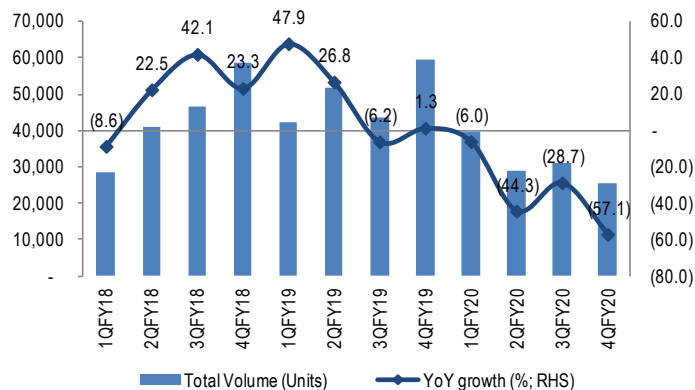
Key takeaways from the conference-call:

- Demand outlook:** In FY20, total M&HCV industry volume declined by ~40%. In 4QFY20, industry volume declined by 57% YoY. Industry was already facing slowdown due to weak economy and BS-VI transition. Covid-19 added to the industry woes. Domestic demand scenario continues to remain weak on account of weak underlying economic growth. However, within M&HCVs, segments like tippers are showing good improvement in demand. The management expects that there will be pent-up demand in the next 60-90 days, which will start showing results in 2QFY21. The management expects 3QFY21 to be much better as the economy will move towards normalcy. Demand for Passenger Bus will take some time to pickup as people shift away from public transportation due to covid-19. Industry has represented with state governments to buy more buses as social distancing is expected to put pressure on existing capacity of public transport. The management stated that AL is very well positioned in ITD and LCVs market as it has gained market share over the last few years. AL will be focusing on increasing the addressable market by filling production gap and the launch of Phoenix will further boost its market position and help to further gain market share. Overall, the management believes that the CV industry has bottomed out and will see gradual recovery going forward. AL is also targeting export growth over the next 5 years to achieve its vision to be among the top 10 CV players globally. AL is using this slowdown as an opportunity to implement some structural measures, including cost reduction, focus on productivity and cash flows and new product development, which the management believes will make the company more resilient.

- **Volume & market share:** M&HCV industry volume declined by ~42% in FY20, while the company's volume declined by ~46%. AL's FY20 market share in the M&HCV segment declined by 200bps to 31.8% due to 400bps decline in market share of M&HCV trucks mainly on account of inventory management due to BS-VI transition. Its market share in Bus increased by 380bps to 45.1% in FY20. It also gained market share in ICV and LCVs. Going forward, with the launch of the AVTR platform, AL is focusing on value selling as TCO will be lower for customers and also AL's cost of components will reduce significantly. Management is confident of gaining market share on the back of the AVTR platform without resorting to higher discount.
- **ICDs:** AL placed ICDs worth Rs5,000mn with the group companies of its Parent – Hinduja group. The management stated that these ICDs are short term in nature and part of efficient treasury management operations as yields will be higher than short bank deposits (yield ranges 9.5-10.5%). Management stated that it has raised additional liquidity to sail through tough market environment on account of Covid19 and parking it in short term ICDs will help generate 3-4% incremental returns. These ICDs can be withdrawn anytime by giving some days prior notice. Management clarified that no further ICDs were placed.
- **Impairments:** AL charged an impairment of over ~Rs654mn towards its investment in Optare. All the investments made in Optare will be impaired. However, AL will also continue to invest in Optare as it believes that the company has strong future oriented technologies and good product portfolio which will be valuable for AL in future. Optare has been focusing on electric buses and has received orders from across London, Dubai and NewZealand. AL is working towards improving its efficiencies to turn it around.
- **Margins & cost reduction program:** AL's gross margin improved by 160bps YoY and 240bps QoQ to 28.9% on account of better product mix, lower discounts, benign commodity costs and cost reduction efforts. Discounts were lower as company didn't have pressure to sell at higher discounts due to BS-VI inventory management. But, higher employee costs affected EBITDA margin. The management stated that the company achieved cost saving of ~Rs5,400mn in FY20 on account of efficient cost management across all the functions. Last quarter, it had guided for further cost savings target of about Rs6,000-6,500mn in FY21. The management reaffirmed that its cost savings program 'K54' is sustainable and will structurally bring down the breakeven point for AL. Its cash burn when factories were shut due to Covid-19 lockdown stood at Rs1500mn-1700mn per month.
- **New platforms:** AL's new LCV platform 'Phoenix' will be launched within the next 3 months. All the products on this platform are ready and AL is just waiting for the right time to launch them. The management is very confident of improving its position in the LCV market along with market share gains on the back of the Phoenix platform. AL launched its modular platform 'AVTR' during 1QFY21 and is receiving good initial traction. AVTR will allow customers to customize the products as per their requirements and is an attractive value proposition for customers. It will come with right as well as left hand drive and hence can be exported. The AVTR platform will reduce manufacturing complexity, lower inventory and new product development costs and improve productivity, making operations more efficient.
- **Exports:** The company is redrawing its exports strategy and has much larger product portfolio to offer to its customers globally. AL is strengthening its dealerships in the Middle-east, Africa and SAARC regions. The management believes that the AVTR platform will give AL an edge globally with its potential to switch between right-hand-drive and left-hand-drive and provide flexibility to export the products globally without incurring any major cost to switchover to left-hand-drive. The management stated that to achieve its vision to be among the top 10 CV players globally, it will focus on the exports markets. It will be a 5 year strategy.
- **Inventory levels:** AL ended the year with zero BS-IV inventory.
- **Discounts:** Discounts were lower during the quarter as AL's BS-IV inventory was at comfortable level. During the last six months, there has been high industry wide discounting mainly due to higher BS-IV inventory. However, AL did not resort to high discounting as its BS-IV inventory was at comfortable level, which also led to some impact on its market share.
- **Capex:** FY20 capex outflow stood at Rs12,270mn. Most of its capex towards modular business program, phoenix project and BS-VI has come to an end and going forward only maintenance capex will be required. In 3QFY20, the management had guided for capex of ~Rs4,000-5,000mn in FY21, mainly towards maintenance.
- **Debt:** Gross/net debt as on 31st March stood at ~Rs31bn/~Rs20.05bn. AL raised additional debt during 1QFY21 and its current net debt stands at ~Rs40bn. Its current net debt/equity stands at ~0.4x-0.45x.
- **Hinduja Leyland Finance:** Hinduja Leyland Finance is doing extremely good and has comfortable liquidity arrangements. Some of its customers have opted for moratorium, but are not very significant, according to the management.

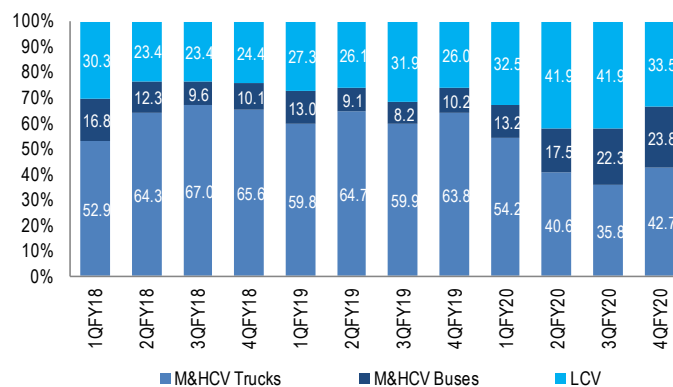
Story in Charts

Exhibit 4: Total Volume & YoY growth (%)



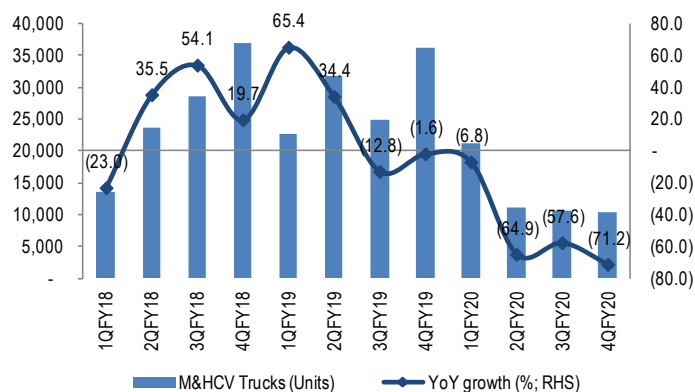
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 5: Segment mix (%)



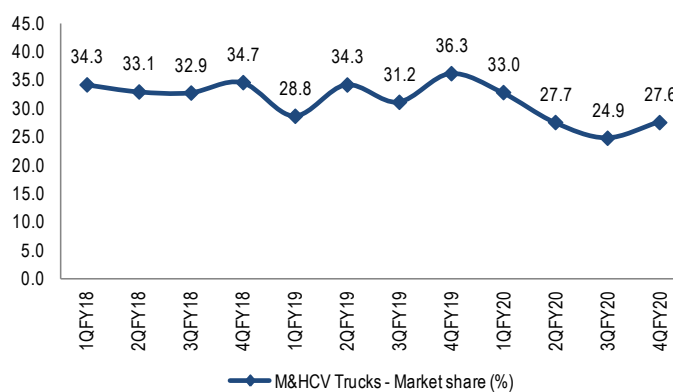
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: M&HCV Trucks - Domestic volume & YoY growth (%)



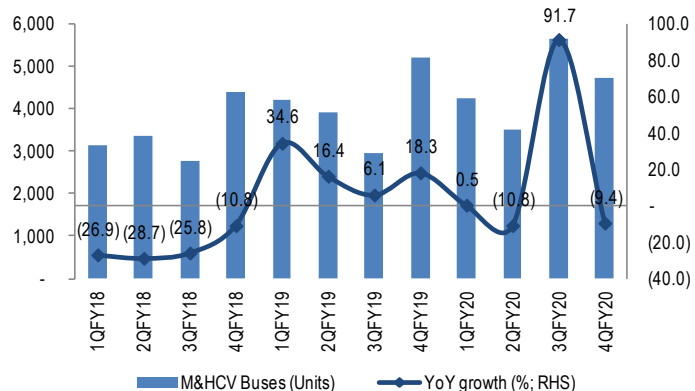
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: M&HCV Trucks - Domestic market share (%)



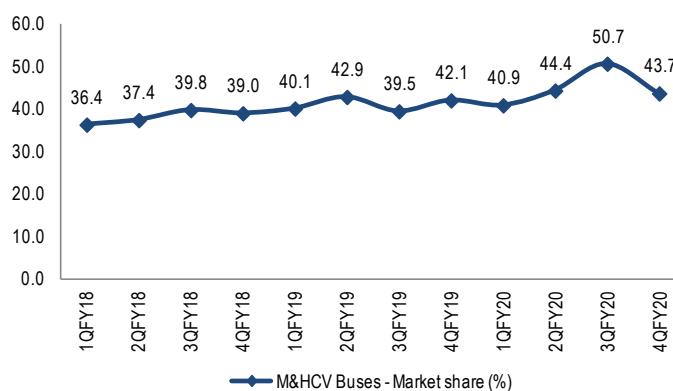
Source: CRISIL, Nirmal Bang Institutional Equities Research

Exhibit 8: M&HCV Buses - Domestic volume & YoY growth (%)

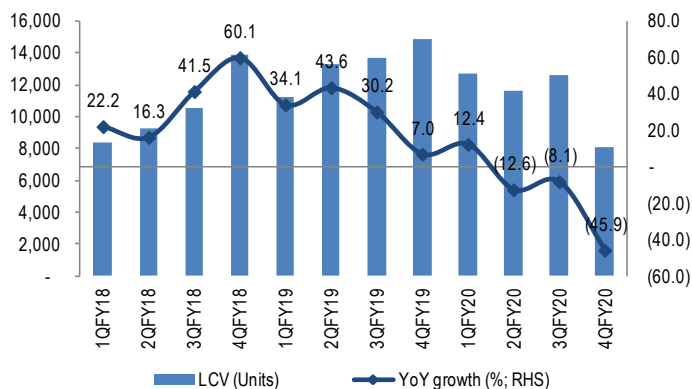


Source: CRISIL, Nirmal Bang Institutional Equities Research

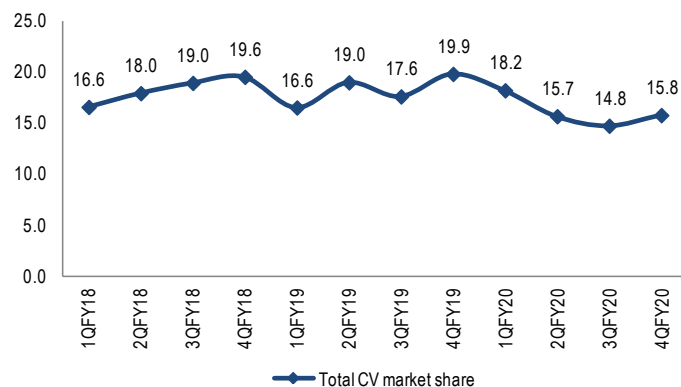
Exhibit 9: M&HCV Buses - Domestic market share (%)



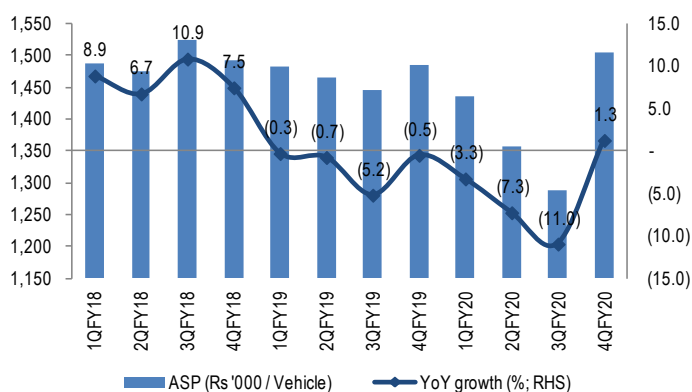
Source: CRISIL, Nirmal Bang Institutional Equities Research

Exhibit 10: LCV - Domestic volume & YoY growth (%)


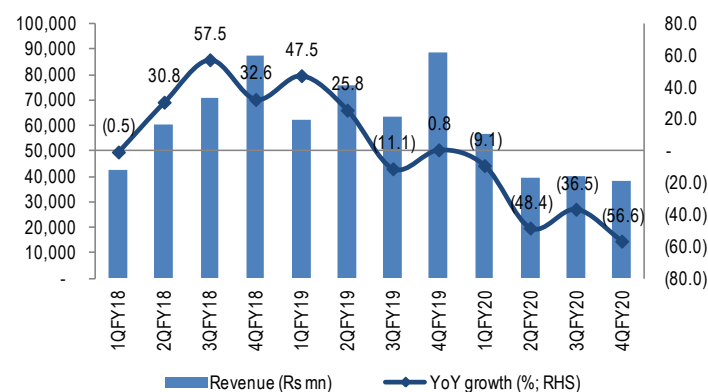
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 11: LCV - Domestic market share (%)


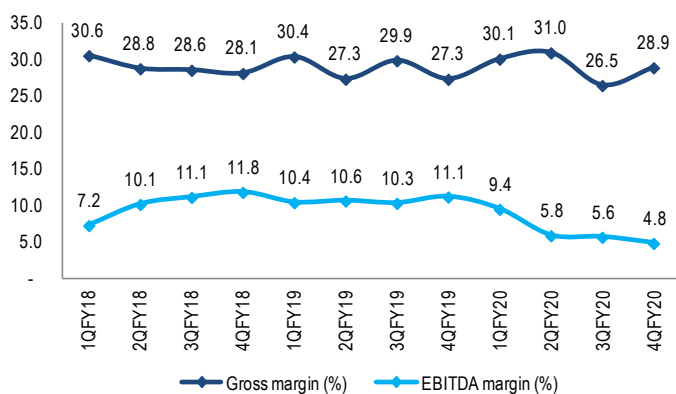
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 12: Avg selling price (ASP) & YoY growth (%)


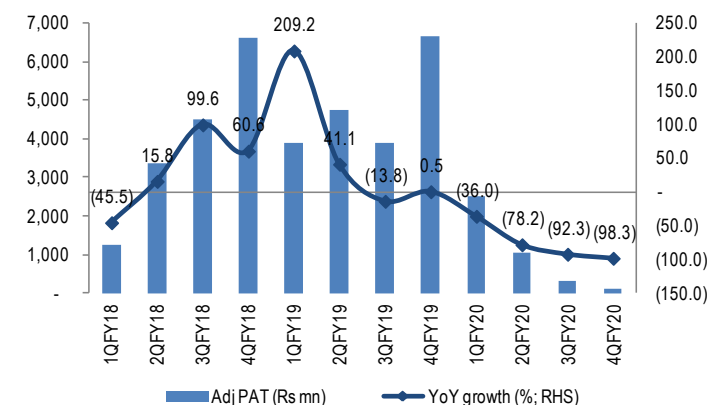
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 13: Revenue & YoY growth (%)


Source: CRISIL, Nirmal Bang Institutional Equities Research

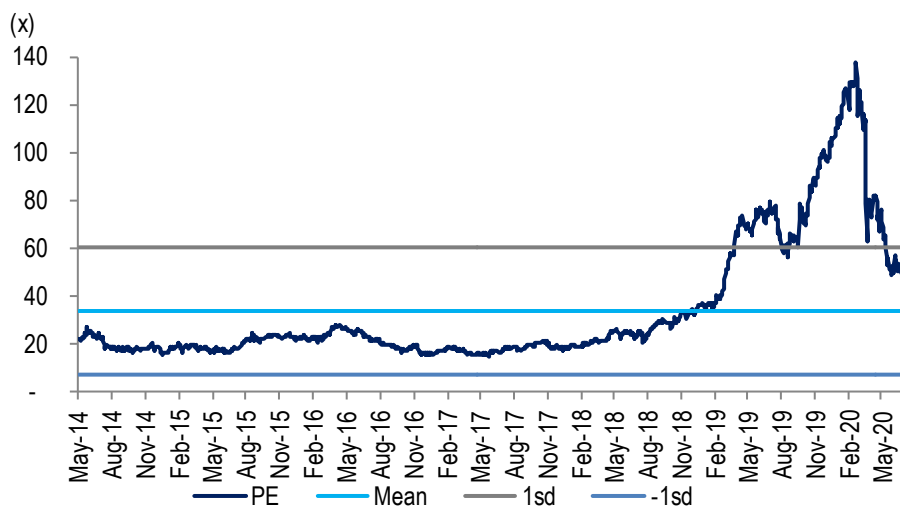
Exhibit 14: Gross margin & EBITDA margin trend


Source: CRISIL, Nirmal Bang Institutional Equities Research

Exhibit 15: Adj PAT & YoY growth (%)


Source: CRISIL, Nirmal Bang Institutional Equities Research

Exhibit 16: P/E chart



Source: Bloomberg, Nirmal Bang Institutional Equities Research

Financials

Exhibit 17: Income statement

Y/E March (Rsmn)	FY18	FY19	FY20	FY21E	FY22E
Net Sales	262,479	290,550	174,675	160,933	215,321
% Growth	31.1	10.7	(39.9)	(7.9)	33.8
Raw material	186,213	206,796	123,692	115,067	150,725
Staff costs	18,119	20,988	16,151	14,484	17,656
Other expenses	30,757	31,409	23,096	21,565	27,992
Total expenses	235,089	259,192	162,938	151,116	196,373
EBITDA	27,390	31,357	11,737	9,817	18,948
% Growth	24.4	14.5	(62.6)	(16.4)	93.0
EBITDA margin (%)	10.4	10.8	6.7	6.1	8.8
Other income	1,898	1,099	1,233	1,339	1,680
Interest costs	1,312	704	1,095	1,703	1,715
Depreciation	5,546	6,210	6,698	7,568	7,764
Profit before tax (before exceptional items)	22,429	25,543	5,177	1,885	11,149
Exceptional items	122	575	1,558	-	-
Tax	6,681	5,136	1,224	377	2,230
Adj PAT	15,748	20,407	3,953	1,508	8,919
% Growth	35.1	29.6	(80.6)	(61.9)	491.4
Adj PAT margin (%)	6.0	7.0	2.3	0.9	4.1
EPS (Rs)	5.4	7.0	1.3	0.5	3.0
% Growth	35.1	29.6	(80.6)	(61.9)	491.4
DPS (Rs)	2.4	3.1	0.5	0.2	0.9
Payout (incl. div. tax) (%)	52.3	52.8	70.5	44.8	34.1

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 19: Balance sheet

Y/E March (Rsmn)	FY18	FY19	FY20	FY21E	FY22E
Share capital	2,927	2,936	2,936	2,936	2,936
Reserves	68,721	80,389	69,704	70,505	76,237
Net worth	71,648	83,324	72,640	73,440	79,173
Total debt	5,157	3,984	31,053	37,053	31,553
Net deferred tax liability	2,984	2,497	2,648	2,648	2,648
Capital employed	79,789	89,806	106,341	113,141	113,374
Gross block	63,121	75,926	94,524	99,524	107,524
Depreciation	13,378	19,791	26,489	34,056	41,821
Net block	49,742	56,135	68,036	65,468	65,703
Capital work-in-progress	4,012	6,576	5,941	5,941	5,941
Investments	58,026	26,365	27,196	32,196	37,196
Inventories	17,099	26,847	12,380	13,227	17,698
Debtors	9,805	25,055	11,804	10,875	17,698
Cash	10,044	13,736	13,225	16,537	15,823
Loans & advances & Other current assets	17,132	27,520	25,314	26,552	27,072
Total current assets	54,080	93,158	62,723	67,192	78,290
Creditors	46,586	50,179	26,239	22,046	32,446
Other current liabilities & provisions	39,486	42,249	31,316	35,611	41,312
Total current liabilities	86,072	92,428	57,555	57,656	73,757
Net current assets	(31,992)	729	5,168	9,536	4,533
Application of funds	79,789	89,806	106,341	113,141	113,374

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 18: Cash flow

Y/E March (Rsmn)	FY18	FY19	FY20	FY21E	FY22E
OP/(loss) before tax	21,844	25,147	5,039	2,249	11,184
Depreciation & amortization	5,546	6,210	6,698	7,568	7,764
Other income	1,898	1,099	1,233	1,339	1,680
(Inc.)/dec. in working capital	28,341	(29,030)	(4,950)	(1,056)	4,289
Direct taxes paid	(4,966)	(5,623)	(1,073)	(377)	(2,230)
Other/extra-ordinary Items	1,671	359	(13,170)	(121)	(544)
Cash flow from operations (after E/O)	54,333	(1,837)	(6,223)	9,602	22,143
Capital expenditure (-)	(7,534)	(15,167)	(17,964)	(5,000)	(8,000)
Net cash after capex	46,799	(17,003)	(24,187)	4,602	14,143
Other investing activities	(29,238)	31,661	(831)	(5,000)	(5,000)
Dividends paid (-)	(7,113)	(9,098)	(1,468)	(587)	(2,642)
Inc./(dec.) in total borrowings	(9,605)	(1,877)	25,975	4,297	(7,215)
Others	81	8	-	-	-
Cash from financial activities	(16,637)	(10,966)	24,507	3,710	(9,857)
Opening cash balance	9,120	10,044	13,736	13,225	16,537
Closing cash balance	10,044	13,736	13,225	16,537	15,823
Change in cash balance	924	3,692	(511)	3,312	(714)

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 20: Key ratios

Y/E March	FY18	FY19	FY20	FY21E	FY22E
Per share (Rs)					
EPS	5.4	7.0	1.3	0.5	3.0
EPS Growth (%)	35.1	29.6	(80.6)	(61.9)	491.4
Cash EPS	7.3	9.1	3.6	3.1	5.7
Book value per share	24.5	28.4	24.7	25.0	27.0
DPS	2.4	3.1	0.5	0.2	0.9
Payout (incl. div. tax) %	52.3	52.8	70.5	44.8	34.1
Valuation (x)					
P/E	9.7	7.5	38.6	101.3	17.1
Cash P/E	7.2	5.7	14.3	16.8	9.2
EV/EBITDA	3.3	3.7	12.2	14.4	6.9
EV/Sales	0.3	0.4	0.8	0.9	0.6
P/BV	2.1	1.8	2.1	2.1	1.9
Dividend yield (%)	4.7	6.0	1.0	0.4	1.7
Return ratios (%)					
RoCE	29.8	29.2	5.9	3.2	11.3
RoE	22.0	24.5	5.4	2.1	11.3
Profitability ratios (%)					
EBITDA margin	10.4	10.8	6.7	6.1	8.8
PAT margin	6.0	7.0	2.3	0.9	4.1
Turnover ratios					
Debtors (days)	14	31	25	25	30
Inventory (days)	24	34	26	30	30
Creditors (days)	65	63	55	50	55
Asset turnover (x)	3	3	2	1	2
Leverage Ratio					
Debt/equity (x)	0.1	0.0	0.4	0.5	0.4

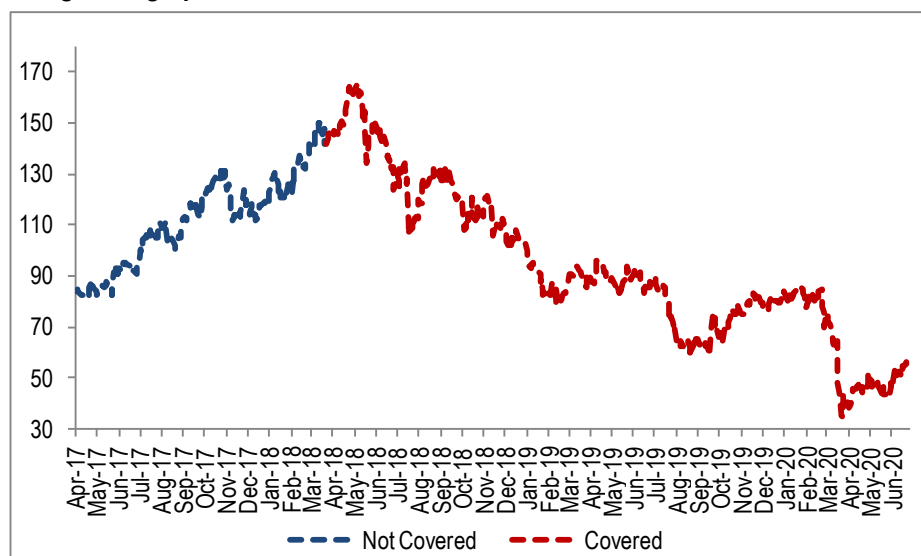
Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
23 March 2018	Buy	142	167
23 May 2018	Buy	141	165
19 July 2018	Buy	111	129
18 September 2018	Buy	127	152
15 February 2019	Buy	84	152
2 August 2019	Buy	69	80
23 September 2019	Buy	75	80
13 November 2019	Buy	79	92
18 February 2020	Buy	82	98
30 March 2020	Buy	43	56
29 June 2020	Acc	52	52

* Coverage shifted to Anish Rankawat wef 2 August 2019

Rating track graph



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Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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