

CMP: ₹ 148

Target: ₹ 185 (25%)

Target Period: 12 months

BUY

November 12, 2022

Volume growth, margin expansion to boost earnings

About the stock: Ashok Leyland (ALL) is a pure-play CV manufacturer domestically, with H1FY23 market share pegged at 17.5%. The company is present in M&HCV trucks and buses as well as LCV goods segments. It also has a formidable presence in the e-mobility (electric buses) domain through Switch Mobility.

- FY22 product mix – LCV goods 42%, trucks 52%, buses 6%

Q2FY23 Results: ALL reported a steady performance in Q2FY23.

- Standalone operating income for Q2FY23 was up 14.4% QoQ to ₹ 8,266 crore, amid 14.2% sequential growth in volumes to 45,295 units
- EBITDA came in at ₹ 537 crore with margins at 6.5%, up 210 bps QoQ. Gross margin expanded ~131 bps QoQ and was further supported by other expense, which declined ~96 bps QoQ
- Consequent PAT for the quarter came in at ₹ 199 crore

What should investors do? ALL's share price has grown at ~5.4% CAGR in the past five years (from ~₹ 112 in November 2017), outperforming the Nifty Auto index

- We retain **BUY** rating driven by cyclical recovery underway in domestic CV space and gross margin expansion on anvil amid decline in key RM prices

Target Price and Valuation: We value ALL at a revised SOTP based target price of ₹ 185 (15x core FY24E EV/EBITDA, 2.0x P/BV for investments; earlier TP ₹ 180)

Key triggers for future price performance:

- Healthy volume growth in the offering driven by government's thrust on infrastructure spending and pickup in core industrial activity with buses segment to benefit from reopening of workplaces, schools and colleges
- Blended ASPs to rise amid exports push, improved product mix & intent to increase market share aided by new launches with superior tech offering
- We build 25% volume & 33% net sales CAGR over FY22-24E; margins seen rising to 8.5% levels by FY24E on the back of operating leverage benefits and normalised input cost. Return ratios are seen ~20% levels by FY24E
- Focus on electrification & new mobility services with intent to launch E-LCV (i.e. Dost and Bada Dost) sometime in mid-2023 for B2B segment

Alternate Stock Idea: Besides ALL, in our auto OEM coverage we like M&M.

- Focused on prudent capital allocation, UV differentiation & EV proactiveness
- BUY with target price of ₹ 1,590



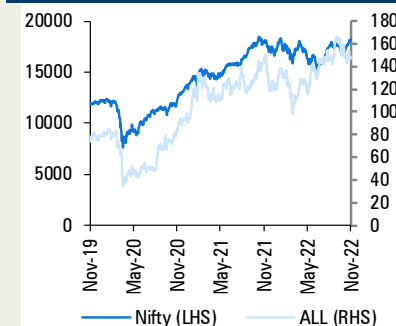
Particulars

Particular	₹ crore
Market Capitalization	43,321.1
Total Debt (FY22)	3,507.1
Cash & Inv. (FY22)	2,345.0
EV (₹ Crore)	44,483.3
52 week H/L (₹)	169 / 93
Equity capital (₹ crore)	293.6
Face value (₹)	1.0

Shareholding pattern

	Dec-21	Mar-22	Jun-22	Sep-22
Promoter	51.5	51.5	51.5	51.5
FII	15.1	13.5	15.0	17.6
DII	20.7	21.9	21.7	19.5
Other	12.8	13.1	11.7	11.4

Price Chart



Recent event & key risks

- Posted steady Q2FY23 results.
- Key Risk:** (i) Slower than expected margin recovery, (ii) aggressive discounting in market place to win market share

Research Analyst

Shashank Kanodia, CFA
shashank.kanodia@icicisecurities.com

Raghvendra Goyal
raghvendra.goyal@icicisecurities.com

Key Financial Summary

Key Financials	FY19	FY20	FY21	FY22	5 year CAGR (FY17-22)	FY23E	FY24E	2 year CAGR (FY22-24E)
Net Sales	29,055.0	17,467.5	15,301.5	21,688.3	1.6%	31,644.3	38,274.1	32.8%
EBITDA	3,135.7	1,173.6	535.1	994.5	-14.7%	2,087.7	3,261.2	81.1%
EBITDA Margins (%)	10.8	6.7	3.5	4.6		6.6	8.5	
Net Profit	1,983.2	239.5	(313.7)	541.9	-15.0%	785.3	1,697.2	77.0%
EPS (₹)	6.8	0.8	(1.1)	1.8		2.7	5.8	
P/E	21.9	181.4	NM	80.2		55.3	25.6	
RoNW (%)	24.3	4.7	(4.4)	0.2		10.0	20.0	
RoCE (%)	25.7	4.5	(1.9)	2.1		11.5	20.9	

Source: Company, ICICI Direct Research

Key takeaways of recent quarter & conference call highlights

Q2FY23 Results:

- Standalone operating income came in at ₹ 8,266 crore up 14.4% QoQ. Total volumes for the quarter were at 45,295 units, up 14.2% sequentially
- ASPs for the quarter came in at ₹ 18.2 lakh/unit, flat QoQ
- M&HCV volumes in the total sales volume mix (~61.5% in Q2FY23 vs. ~63% in Q1FY23). The company gained market share in the truck segment
- EBITDA for the quarter came in at ₹ 537 crore with corresponding margins at 6.5%, up 210 bps QoQ. Gross margin expanded ~131 bps QoQ and was further supported by other expense, which declined ~96 bps QoQ
- Consequent reported PAT was at ₹ 199 crore

Q2FY23 Earnings Conference Call highlights

- The management said Q2FY23 remained strong for the company with second consecutive quarter with 30%+ market share in the truck segment with market share in this space increasing to 32.2% up ~10% YoY vs. ~31.1% in Q1FY23. ALL sustained market share amid new launches
- The company's truck volumes rose much higher than industry truck volume growth, whereas LCV was slightly affected by semiconductor shortages
- During the quarter, working capital increased by ₹ 650 crore due to increase in size of operations while net debt increased by ~₹ 400 crore to ₹ 2,677 crore vs. ~₹ 2,281 in Q1FY23
- Management indicated Crisil expects M&HCV industry to grow 22-23%, bus to grow 103-105% and LCV to grow 18-20% in FY23E. Crisil expect the bus portfolio to outperform over the mid to long term amid low base
- Capex during Q2FY23 was at ₹ 103 crore vs. ~₹ 218 crore in H1FY23. For full year, capex reduced from ₹ 750 crore to ₹ 600 crore. Above capex guidance does not include capex requirement of Switch Mobility. Switch capex requirement was ~\$200-250 million for FY23-24E
- The company continues to provide support to Switch Mobility and is actively looking for the right partner. However, ALL will not infuse further equity in Switch Mobility
- The management intends to target EV version of "Dost" & "Bada Dost" in CY23E amid demand from courier companies and need of last mile mobility. However, it expects this to be largely driven by B2B demand
- The company has taken ~1.8-1.9% hike during Q1FY23 followed by ~1% price hike in Q2FY23. Further, ALL has taken ~1.5% hike in November 2022. Discounts were largely stable QoQ

Steel price rose ~₹ 4-5/kg for Q1FY23 and were down by ~₹ 10/kg in Q2FY23. The company expects benefits of RM price decline to start accruing from Q3FY23

Spares revenue was at ~7-8% of topline

Rise in employee expense was largely due to booking of bonus for employees, salary hikes as well as wage settlement arrears for workers

The company is actively engaging in the defence sector tenders for trucks and expects healthy uptick in order from Q3FY23

The company witnessed a revival in demand from fleet aggregators & witnessed increase in fleet utilisation levels and improvement of free cash flow in the hands of fleet operators amid reduced operating cost

Peer comparison

Exhibit 1: Peer Comparison (4-W)

Company	CMP	TP	Rating	Mcap	Total lakh volumes			EBITDA margin (%)			RoCE (%)			EV/EBITDA (x)		
	₹	₹		₹ crore	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
Ashok Leyland (ASHLEY)	148	185	Buy	43,321	1.3	1.7	2.0	4.6	6.6	8.5	2.1	11.5	20.9	44.7	21.4	13.4
Tata Motors (TATMOT)	423	465	Hold	1,61,967	7.3	9.6	10.7	12.2	10.3	12.7	4.8	4.4	11.9	7.0	7.4	4.9
M&M (MAHMAH)	1,296	1,590	Buy	1,61,119	4.7	6.5	7.2	12.3	11.5	12.7	9.3	11.4	13.9	22.2	17.8	14.0

Source: Company, ICICI Direct Research; Note – volume data above is for Tata Motors' India business and M&M's automotive business only

We believe ALL would be an outsized beneficiary of the ongoing CV revival domestically given its presence across industry segments. Blended realisations are set to improve amid exports focus and improved mix. Riding on operating leverage gains, margins and RoCE are set to expand to 8.5%, 21% by FY24E, respectively.

Exhibit 2: Variance Analysis

	Q2FY23	Q2FY23E	Q2FY22	YoY (%)	Q1FY22	QoQ (%)	Comments
Total Operating Income	8,266.0	8,330.8	4,457.9	85.4	7,222.9	14.4	Topline came in marginally below our estimates tracking lower than anticipated ASPs
Raw Material Expenses	6,446.6	6,574.0	3,418.5	88.6	5,728.1	12.5	Savings were realised in RM costs, which, for the quarter, were down 130 bps QoQ at 78% of sales
Employee Expenses	527.1	458.2	400.3	31.7	445.4	18.3	Employee costs were higher at 6.4% of sales primarily tracking salary hikes and wage settlement with workers
Other expenses	755.0	749.8	504.3	49.7	729.1	3.5	
EBITDA	537.3	548.8	134.7	298.9	320.3	67.8	EBITDA was broadly in line with our estimates with margins for the quarter coming in at 6.5%
EBITDA Margin (%)	6.5	6.6	3.0	348 bps	4.4	207 bps	
Other Income	20.0	27.2	20.9	-4.5	25.6	-22.0	
Depreciation	176.8	202.3	184.3	-4.1	182.4	-3.1	Depreciation was lower than our estimates
Interest	77.1	67.7	87.1	-11.5	68.9	11.8	
Tax	112.4	77.1	-32.5	-445.9	39.6	183.9	Tax rate for the quarter was at 36.1% of PBT
Reported PAT	199.3	228.9	-83.0	340.1	68.0	NM	
EPS	0.7	0.8	-0.3	340.1	0.2	NM	PAT came in lower than our estimates tracking higher depreciation charge as well as higher effective tax rate
Key Metrics							
ASPs (₹ lakh/unit)	18.2	18.4	16.2	12.8	18.2	0.2	ASPs were broadly flat QoQ at ₹ 18.2 lakh/unit amidst 150 bps lower share of M&HCV volumes in the product mix amid price hikes undertaken by the company

Source: Company, ICICI Direct Research

Exhibit 3: Change in estimates

(₹ Crore)	FY23E			FY24E			Comments
	Old	New	% Change	Old	New	% Change	
Revenue	29,340	31,644	7.9	35,309	38,274	8.4	Upgrade in our volume and ASP estimates leads to upward revision in topline estimates. We expect topline at the company to grow at a CAGR of 32.8% CAGR over FY22-24E
EBITDA	1,636	2,088	27.6	2,833	3,261	15.1	
EBITDA Margin (%)	5.6	6.6	102 bps	8.0	8.5	50 bps	Upgrade margin estimates tracking pricing discipline talk by all industry participants as well as decline in key commodity prices resulting in expansion in gross margins
PAT	502	785	56.5	1,401	1,697	21.1	
EPS (₹)	1.7	2.7	56.5	4.8	5.8	21.1	Upward revision in sales and margin estimates leads to sharp double digit upgrade in our earning estimates, going forward, for FY23E, FY24E

Source: ICICI Direct Research

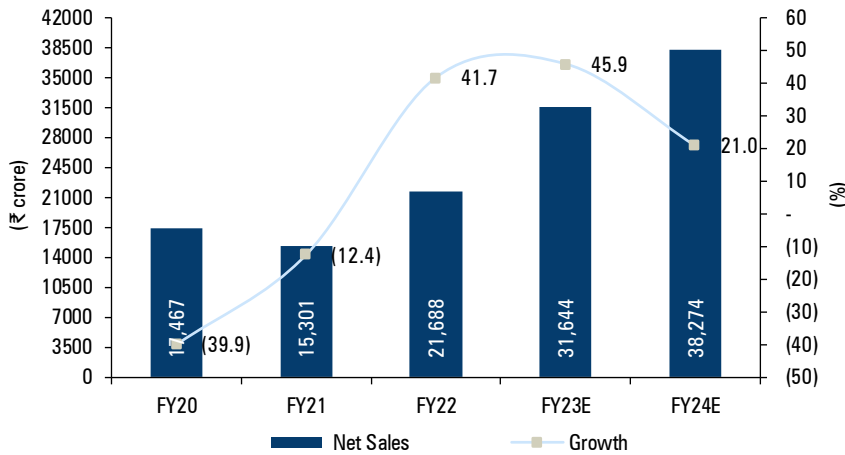
Exhibit 4: Assumptions

	FY19	FY20	FY21	Current			Earlier		Comments
				FY22	FY23E	FY24E	FY23E	FY24E	
M&HCV Passenger volumes	19,871	23,323	5,629	7,799	14,635	17,562	12,527	15,012	Upgrade our volume estimates tracking upbeat volume prints till date in FY23E and upbeat management commentary on demand prospects. We expect total volumes at the company to grow at a CAGR of 24.8% over FY22-24E led by 31.6% volume CAGR growth in the M&HCV domain and steady 15.1% CAGR growth in the LCV space. Also upgrade our ASP estimates tracking management commentary on price hikes and greater export push
M&HCV Goods volumes	122,987	55,231	46,178	66,086	91,876	110,359	87,185	104,623	
Total M&HCV Sales Volume	142,858	78,554	51,807	73,885	106,511	127,921	99,712	119,635	
LCV volumes	54,508	46,646	48,908	54,441	64,926	72,094	59,890	65,879	
Total Sales Volume	197,366	125,200	100,715	128,326	171,437	200,016	159,602	185,515	
YoY Growth (%)		-37%	-20%	27%	34%	17%			
ASPs (₹ lakh/unit)	14.4	12.8	15.2	16.9	18.4	19.1	18.2	19.0	

Source: ICICI Direct Research

Financial story in charts

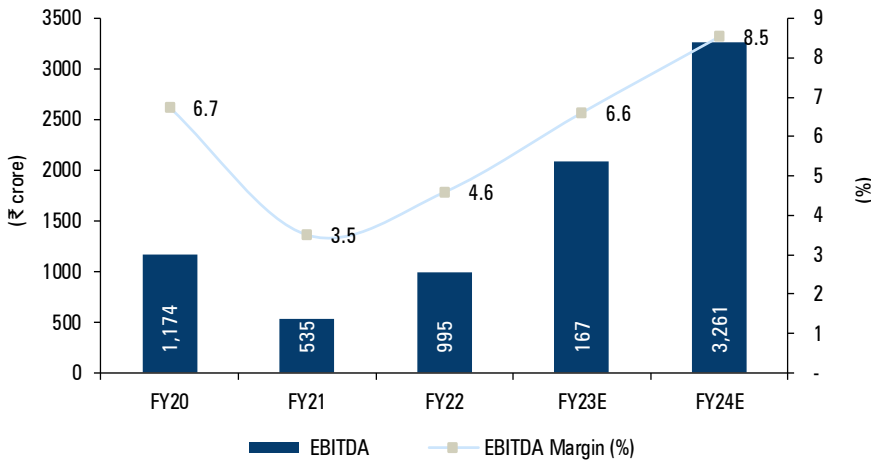
Exhibit 5: Topline trend



We expect sales to grow at a CAGR of 32.8% over FY22-24E backed by 24.8% volume CAGR in the aforesaid period, led by M&HCV segment

Source: Company, ICICI Direct Research

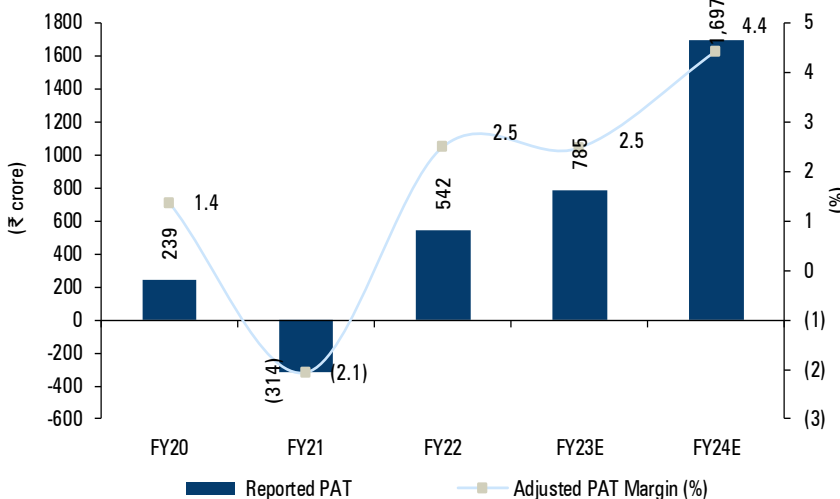
Exhibit 6: Trend in margins



We expect ALL margins to be at 8.5% by FY24E, riding on substantial operating leverage gains and cost control measures

Source: Company, ICICI Direct Research

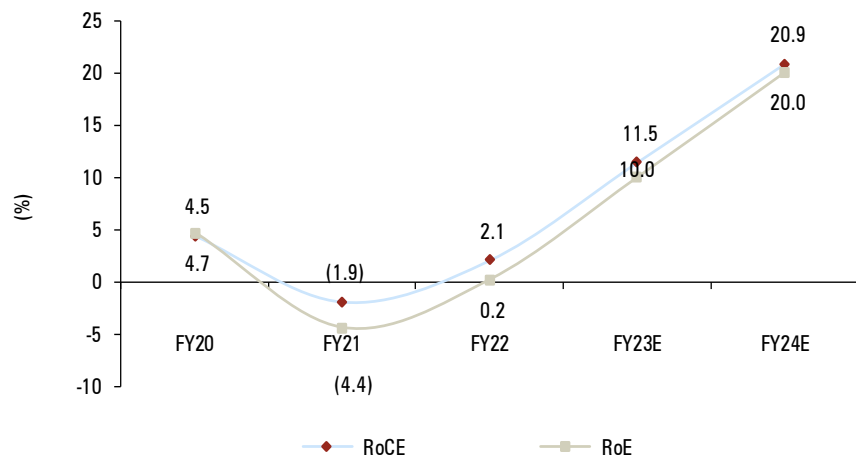
Exhibit 7: Trend in profitability



PAT is expected to reach ₹ 1,697 crore in FY24E

Source: Company, ICICI Direct Research

Exhibit 8: Trend in return ratios



The company is positioned to post healthy double digit return ratios in FY24E

Source: Company, ICICI Direct Research

Exhibit 9: SOTP-based valuation

SOTP	
Target EV/EBITDA (x)	15.0
EBITDA (₹ crore; FY24E)	3,261
Enterprise Value (₹ Crore)	48,918
Net Debt (₹ crore; FY24E)	517
Target Market cap Core business (₹crore)	48,401
Value/Share (A)	165
Strategic Investments FY24E (₹ crore)	3,922
P/BV(x)	2.0
Total Value/Share post applying 20% Holdco. Discount (B)	20
Price target (₹, A+B)	185

Source: Company, ICICI Direct Research

Exhibit 10: Valuation Summary

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY18	26,356	31.7	5.9	36.6	25.2	13.6	24.0	25.6
FY19	29,055	10.2	6.8	15.1	21.9	13.6	24.3	25.7
FY20	17,467	(39.9)	0.8	(87.9)	NM	38.6	4.7	4.5
FY21	15,301	(12.4)	(1.1)	NA	NM	86.4	(4.4)	(1.9)
FY22	21,688	41.7	1.8	NM	NM	44.7	0.2	2.1
FY23E	31,644	45.9	2.7	NM	55.3	21.4	10.0	11.5
FY24E	38,274	21.0	5.8	116.1	25.6	13.4	20.0	20.9

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 11: Profit and loss statement				
	₹ crore			
(Year-end March)	FY21	FY22	FY23E	FY24E
Total operating Income	15,301.5	21,688.3	31,644.3	38,274.1
Growth (%)	-12.4	41.7	45.9	21.0
Raw Material Expenses	11,403.4	16,761.1	24,618.1	29,295.4
Employee Expenses	1,583.9	1,694.6	1,961.3	2,196.3
Other Expenses	1,779.1	2,238.1	2,977.2	3,521.2
Total Operating Expenditure	14,766.4	20,693.8	29,556.6	35,012.9
EBITDA	535.1	994.5	2087.7	3261.2
Growth (%)	-54.4	85.9	109.9	56.2
Depreciation	747.7	752.8	791.1	842.0
Interest	306.8	301.1	296.3	250.7
Other Income	119.5	76.1	90.3	100.6
PBT	-399.9	16.8	1090.5	2269.0
Exceptional chages	12.1	-510.8	-21.2	0.0
Total Tax	-98.2	-14.2	326.5	571.8
PAT	-313.7	541.9	785.3	1697.2
Growth (%)	-231.0	-272.7	44.9	116.1
EPS (₹)	-1.1	1.8	2.7	5.8

Source: Company, ICICI Direct Research

Exhibit 12: Cash flow statement				
	₹ crore			
(Year-end March)	FY21	FY22	FY23E	FY24E
Profit after Tax	-313.7	541.9	785.3	1,697.2
Add: Depreciation	747.7	752.8	791.1	842.0
(Inc)/dec in Current Assets	-2,495.2	-511.2	-1,596.9	-1,455.4
Inc/(dec) in CL and Provisions	2,031.6	1,787.7	1,225.6	1,559.3
CF from operating activities	277.2	2872.2	1501.4	2893.9
(Inc)/dec in Investments	-349.1	-1,750.9	500.0	-300.0
(Inc)/dec in Fixed Assets	-681.5	-249.7	-600.0	-550.0
Others	86.3	57.3	-156.5	-146.0
CF from investing activities	-944.3	-1943.3	-256.5	-996.0
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0
Inc/(dec) in loan funds	447.4	-221.7	-500.0	-500.0
Dividend paid & dividend tax	-176.1	-293.6	-425.6	-924.7
Others	-103.7	-189.8	-296.3	-250.7
CF from financing activities	167.6	-705.0	-1222.0	-1675.4
Net Cash flow	-499.4	223.9	22.9	222.5
Opening Cash	1,322.4	823.0	1,046.9	1,069.8
Closing Cash	823.0	1046.9	1069.8	1292.3

Source: Company, ICICI Direct Research

Exhibit 13: Balance Sheet				
	₹ crore			
(Year-end March)	FY21	FY22	FY23E	FY24E
Liabilities				
Equity Capital	293.6	293.6	293.6	293.6
Reserve and Surplus	6,683.7	7,043.4	7,403.0	8,175.5
Total Shareholders funds	6977.2	7336.9	7696.5	8469.1
Total Debt	3,728.8	3,507.1	3,007.1	2,507.1
Deferred Tax Liability	170.8	144.4	144.4	144.4
Other non-current liabilities	280.5	254.4	254.4	254.4
Total Liabilities	11346.9	11443.0	11302.6	11575.2
Assets				
Gross Block	8,706.7	9,134.0	9,828.2	10,428.2
Less: Acc Depreciation	3,107.5	3,860.3	4,651.4	5,493.4
Net Block	5599.2	5273.7	5176.9	4934.8
Capital WIP	371.9	194.3	100.0	50.0
Total Fixed Assets	5,971.0	5,468.0	5,276.9	4,984.8
Investments	3,068.7	3,521.6	3,721.6	3,921.6
Inventory	2,142.3	2,075.2	2,600.9	3,145.8
Debtors	2,816.0	3,111.0	3,901.4	4,718.7
Loans and Advances	20.6	0.0	0.0	0.0
Other current assets	1686.7	1990.6	2271.5	2364.7
Cash	823.0	1046.9	1069.8	1292.3
Total Current Assets	7,488.6	8,223.7	9,843.6	11,521.5
Creditors	5,164.7	6,875.2	7,802.7	8,913.1
Provisions	465.0	470.3	533.7	609.6
Other current Liabilities	1,473.5	1,545.3	1,780.0	2,153.0
Total Current Liabilities	7,103.1	8,890.8	10,116.4	11,675.7
Net Current Assets	385.5	-667.1	-272.8	-154.2
Application of Funds	11346.9	11443.0	11302.6	11575.2

Source: Company, ICICI Direct Research

Exhibit 14: Key ratios				
(Year-end March)	FY21	FY22	FY23E	FY24E
Per share data (₹)				
EPS	-1.1	1.8	2.7	5.8
Cash EPS	1.5	4.4	5.4	8.7
BV	23.8	25.0	26.2	28.9
DPS	0.6	1.0	1.5	3.2
Cash Per Share	2.8	3.6	3.6	4.4
Operating Ratios (%)				
EBITDA Margin	3.5	4.6	6.6	8.5
PBT / Net sales	-2.6	0.1	3.4	5.9
PAT Margin	-2.1	2.5	0.9	2.4
Inventory days	51.1	34.9	30.0	30.0
Debtor days	67.2	52.4	45.0	45.0
Creditor days	123.2	115.7	90.0	85.0
Return Ratios (%)				
RoE	-4.4	0.2	10.0	20.0
RoCE	-1.9	2.1	11.5	20.9
RoIC	-2.1	2.7	13.6	25.4
Valuation Ratios (x)				
P/E	-138.5	80.2	55.3	25.6
EV / EBITDA	86.4	44.7	21.4	13.4
EV / Net Sales	3.0	2.1	1.4	1.1
Market Cap / Sales	2.8	2.0	1.4	1.1
Price to Book Value	6.2	5.9	5.6	5.1
Solvency Ratios				
Debt/Equity	0.5	0.5	0.4	0.3
Current Ratio	1.1	0.9	0.9	0.9
Quick Ratio	0.7	0.6	0.7	0.7

Source: Company, ICICI Direct Research

Exhibit 15: ICICI Direct coverage universe (Auto & Auto Ancillary)

Sector / Company	CMP	TP	Rating	M Cap	EPS (₹)			P/E (x)			EV/EBITDA (x)			RoCE (%)			RoE (%)		
	(₹)	(₹)		(₹ Cr)	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
Apollo Tyre (APOTYR)	290	335	Buy	18,404	10.1	16.5	25.0	28.8	17.5	11.6	8.9	6.9	5.2	6.3	9.4	13.0	5.4	8.4	11.7
Ashok Leyland (ASHLEY)	148	185	Buy	43,321	1.8	2.7	5.8	80.2	55.3	25.6	44.7	21.4	13.4	2.1	11.5	20.9	0.2	10.0	20.0
Bajaj Auto (BAAUTO)	3,731	3,910	Hold	1,07,958	173.4	200.2	232.2	21.5	18.6	16.1	16.5	13.6	11.6	18.4	24.7	28.0	17.6	22.6	25.4
Balkrishna Ind. (BALIND)	1,888	2,550	Buy	36,498	73.0	65.3	98.3	25.9	28.9	19.2	19.3	20.2	13.3	15.9	13.1	19.7	20.4	16.0	20.4
Bharat Forge (BHAFOR)	880	900	Buy	40,970	23.1	19.8	28.3	38.0	44.5	31.1	21.9	21.3	16.7	9.6	9.2	12.2	15.2	12.7	16.1
Eicher Motors (EICMOT)	3,519	4,310	Buy	96,174	61.3	101.4	124.6	57.4	34.7	28.2	40.4	24.4	19.7	13.3	20.5	21.6	13.3	19.2	20.4
Escorts Kubota (ESCORT)	1,981	2,330	Buy	26,133	58.0	47.8	72.5	34.1	41.5	27.3	22.4	25.7	18.4	10.4	7.8	10.0	9.7	8.4	10.4
Hero Moto (HERHON)	2,665	2,910	Hold	53,220	123.8	138.0	178.2	21.5	19.3	15.0	13.3	11.3	8.9	16.3	19.4	23.9	15.7	16.8	20.6
M&M (MAHMAH)	1,300	1,590	Buy	1,61,616	41.4	48.7	60.6	31.4	26.7	21.4	22.2	17.8	14.1	9.3	11.4	13.9	13.1	13.5	14.9
Maruti Suzuki (MARUTI)	9,109	11,200	Buy	2,75,165	124.7	234.9	350.2	73.1	38.8	26.0	40.9	22.0	15.6	5.1	12.5	16.7	7.0	12.0	16.0
Uno Minda (MININD)	560	650	Buy	32,018	6.2	10.4	14.4	90.0	54.0	38.9	36.8	28.0	21.8	10.2	13.5	16.9	10.3	14.9	17.4
Tata Motors (TATMOT)	423	465	Hold	1,61,967	-29.9	-22.3	8.2	-14.2	-18.9	51.6	7.0	7.4	4.9	4.8	4.4	11.9	-23.5	-21.3	7.2

Source: Company, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



Pankaj Pandey

Head – Research

pankaj.pandey@icicisecurities.com

ICICI Direct Research Desk,
ICICI Securities Limited,
1st Floor, Akruiti Trade Centre,
Road No 7, MIDC,
Andheri (East)
Mumbai – 400 093
research@icicidirect.com

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