

July 22, 2016

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Rating	Accumulate
Price	Rs97
Target Price	Rs112
Implied Upside	15.5%
Sensex	27,803
Nifty	8,541

(Prices as on July 22, 2016)

Trading data

Market Cap. (Rs bn)	275.2
Shares o/s (m)	2,845.9
3M Avg. Daily value (Rs m)	1326.6

Major shareholders

Promoters	50.38%
Foreign	26.33%
Domestic Inst.	9.89%
Public & Other	13.40%

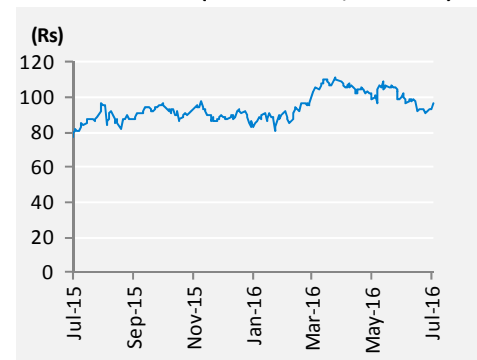
Stock Performance

(%)	1M	6M	12M
Absolute	(3.1)	12.8	18.8
Relative	(7.0)	(0.9)	21.3

How we differ from Consensus

EPS (Rs)	PL	Cons.	% Diff.
2017	5.3	5.3	0.0
2018	5.6	6.4	-13.2

Price Performance (RIC: ASOK.BO, BB: AL IN)



Source: Bloomberg

A favourable product mix and absence of one-off costs as compared to the previous year helped Ashok Leyland (AL) report a healthy operating performance in Q1FY17. While AL's sales growth was 9.7% YoY, EBITDA margin was a healthy 11.2% and adjusted profit was Rs2.4bn (better than expectation of Rs2.2bn).

While volume growth was 10.6% YoY, realisations declined marginally by 0.8% YoY, which led to income growth of 9.7% YoY to Rs42.6bn. M&HCV growth during Q1FY17 was 11.8% YoY, while LCV growth was lower at 6.6% YoY. Management had given an outlook of 15-20% YoY growth during FY17 for M&HCVs; our estimate is at 19.7% YoY for goods M&HCVs and 4.5% YoY for passenger M&HCVs, leading to a total M&HCV growth rate of 16.1% YoY for FY17. Growth for the year is likely to be back-ended.

EBITDA margin was 11.2% (higher 110bps YoY), as EBITDA grew 21.3% YoY to Rs4.76bn. While interest cost reduction was expected in Q1, it was higher than expected. This helped boost adjusted profit (adjusted for exchange gain) to Rs2.4bn, growth of 50% YoY.

While growth in CV demand is expected to continue, with the higher base, the pace will be lower in FY17 (total volume growth estimate is 14.6%). An improving balance sheet position and benefits of operating leverage provide financial stability. Management has passed an enabling resolution for fund-raising post Q4FY16 results, but had also clarified that equity dilution in FY17 is unlikely. We maintain 'Accumulate', with a price target of Rs112, based upon a PE of 20x FY18 EPS. At our price target, AL would trade at an EV/EBITDA of ~11.5x FY18E. At the current price, AL is trading at 18.2x FY17e and 17.3x FY18e earnings.

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Key financials March (Y/e March)	2015	2016	2017E	2018E
Revenues (Rs m)	135,622	188,216	228,422	254,053
Growth (%)	36.4	38.8	21.4	11.2
EBITDA (Rs m)	10,266	21,660	27,126	28,104
PAT (Rs m)	2,440	11,127	15,128	15,927
EPS (Rs)	0.9	3.9	5.3	5.6
Growth (%)	(153.6)	356.1	36.0	5.3
Net DPS (Rs)	0.4	1.0	1.1	1.2

Profitability & Valuation	2015	2016	2017E	2018E
EBITDA margin (%)	7.6	11.5	11.9	11.1
RoE (%)	5.1	20.9	24.8	21.8
RoCE (%)	5.7	15.5	19.3	18.6
EV / sales (x)	2.2	1.5	1.2	1.1
EV / EBITDA (x)	29.4	13.2	10.3	9.9
PE (x)	112.8	24.7	18.2	17.3
P / BV (x)	5.4	5.0	4.1	3.5
Net dividend yield (%)	0.5	1.0	1.1	1.2

Source: Company Data; PL Research

- AL's Q1FY17 vehicle grew 10.6% YoY to 31,165 units. Goods M&HCV sales grew 14.5% YoY and passenger M&HCV sales grew 3.5% YoY, leading to the total M&H CV segment for AL to grow 11.8% YoY, thereby, maintaining a better than industry performance. AL's LCV sales were higher 6.6% YoY (despite the lower base).
- With a decent sales performance, AL posted a 10.6% YoY growth in net sales to Rs41.8bn (flat realisations YoY). Other operating income declined 23% YoY to Rs830m, resulting in total sales growth in Q1 of 9.7% YoY to Rs42.6bn.
- While gross margins were lower YoY by 80bps, they were lower by 220bps QoQ. Gross margin was lower 40bps YoY; some slight increase in commodity costs was largely negated through internal cost reduction, a 1.5% price increase in Apr 2016 and a favourable product mix. Gross profit per vehicle was lower 2% YoY, but higher 8.4% QoQ.
- EBITDA margin was higher-than-expected at 11.2% (up 110bps YoY and lower 140bps QoQ). EBITDA grew 21.3% YoY to Rs4.7bn. EBITDA per vehicle was higher 9.7% YoY and lower 10.7% QoQ.
- Lower OE/sales ratio (by 140bps YoY) was the main reason for AL's YoY EBITDA margin improvement. OE was also lower by 2.1% YoY. This was mainly due to higher export sales related expense of ~Rs800m in Q1FY6, which did not recur this year.
- Interest cost was reined in on YoY and QoQ basis and with a reduction in the absolute debt, it is likely to trend lower ahead. The effective tax rate was as expected at 30%.
- There was exceptional income to the tune of Rs497m (on exchange gain on swap contracts). As a result, reported profit was just Rs2.9m, while the adjusted profit was Rs2.4bn.

Conference call highlights

- Exports were lower during Q1 due to delay in invoicing; exports should pick-up in Q2FY17.
- Industry growth outlook for FY17 is 15-20% on the back of infrastructure demand, replacement demand, banning of old vehicles and pre-buying in H2.
- Capacity utilisation in Q4FY16 was in the range of 70-75%. During FY17, AL should have adequate capacity available in most segments; a few areas may require three shifts though.
- During Q1FY17, a price increase in the range of 1-1.5% was taken; this was followed by another price increase in July on some parts of the portfolio.
- GST is expected to be positive for the industry as the gains for the economy would outweigh other considerations.
- Targeting exports to constitute ~30% of revenues over the next five years.

- Defence constitutes ~4-5% of AL's current revenues. Power solutions constitute ~2-3% of revenues.
- During Q1, AL witnessed commodity rise pressure of 0.2-03% of revenues mainly on account of rise in steel price.
- Inventory stood at ~8,500 units as of Q1FY17-end.

Exhibit 1: Q1FY17 Result Overview (Rs m)

Y/e March	Q1FY17	Q1FY16	YoY gr. (%)	Q4FY16	FY17E	FY16	YoY gr. (%)
Net Revenues	42,588	38,831	9.7	59,553	228,422	188,216	21.4
Raw Materials	29,305	26,572	10.3	42,255	161,436	132,620	21.7
<i>% of Net Sales</i>	<i>68.8</i>	<i>68.4</i>		<i>71.0</i>	<i>70.7</i>	<i>70.5</i>	
Personnel	3,581	3,287	8.9	3,408	15,990	13,987	14.3
<i>% of Net Sales</i>	<i>8.4</i>	<i>8.5</i>		<i>5.7</i>	<i>7.0</i>	<i>7.4</i>	
Manufacturing & Other Exp	4,939	5,047	(2.1)	6,358	23,870	19,949	19.7
<i>% of Net Sales</i>	<i>11.6</i>	<i>13.0</i>		<i>10.7</i>	<i>10.5</i>	<i>10.6</i>	
Total Expenditure	37,826	34,906	8.4	52,022	201,296	166,556	20.9
EBITDA	4,763	3,925	21.3	7,531	27,126	21,660	25.2
<i>EBITDA Margin (%)</i>	<i>11.2</i>	<i>10.1</i>		<i>12.6</i>	<i>11.9</i>	<i>11.5</i>	
Depreciation	1,210	1,138	6.3	1,177	5,094	4,437	14.8
EBIT	3,553	2,787	27.5	6,354	22,032	17,223	27.9
Interest Expenses	338	701	(51.8)	602	1,567	2,735	(42.7)
Non-operating income	443	259	71.1	320	1,302	1,114	16.9
Extraordinary Expenses	-	180	NA	4,209	-	4,326	NA
Extraordinary Income	497	-	NA	417	497	417	19.2
PBT	4,154	2,164	91.9	2,279	22,263	11,692	90.4
Tax-Total	1,246	720	73.2	1,508	6,639	4,474	48.4
<i>Tax Rate (%) - Total</i>	<i>30.0</i>	<i>33.2</i>		<i>66.2</i>	<i>29.8</i>	<i>38.3</i>	
Reported PAT	2,908	1,445	101.2	770	15,625	7,218	116.5
Adj. PAT	2,411	1,607	50.0	4,184	15,178	10,736	41.4

Source: Company Data, PL Research

Exhibit 2: Operating Metrics (Rs m)

Y/e March	Q4FY16	Q4FY15	YoY gr. (%)	Q3FY16	FY16	FY15	YoY gr. (%)
Sales Volume (nos)	31,165	28,182	10.6	43,992	160,996	140,455	14.6
Net Realisation/Vehicle	1,366,546	1,377,876	(0.8)	1,353,720	1,418,803	1,340,044	5.9
Material cost / vehicle	940,322	942,878	(0.3)	960,524	1,002,733	944,214	6.2
Gross Profit / vehicle	426,224	434,998	(2.0)	393,196	416,070	395,829	5.1
Employee cost /vehicle	114,914	116,640	(1.5)	77,469	99,316	99,587	(0.3)
Other expenses / vehicle	158,488	179,085	(11.5)	144,535	148,265	142,032	4.4
EBITDA/vehicle	152,822	139,274	9.7	171,192	168,489	154,211	9.3
Net Profit/vehicle	77,367	57,036	35.6	95,099	94,273	76,439	23.3

Source: Company Data, PL Research

**Income Statement (Rs m)**

Y/e March	2015	2016	2017E	2018E
Net Revenue	135,622	188,216	228,422	254,053
Raw Material Expenses	99,652	132,620	161,436	182,506
Gross Profit	35,970	55,596	66,986	71,547
Employee Cost	11,840	13,987	15,990	17,530
Other Expenses	13,863	19,949	23,870	25,913
EBITDA	10,266	21,660	27,126	28,104
Depr. & Amortization	4,163	4,437	5,094	5,371
Net Interest	3,935	2,735	1,567	1,266
Other Income	2,254	(2,796)	1,798	1,450
Profit before Tax	4,422	11,692	22,263	22,917
Total Tax	1,074	4,474	6,639	6,990
Profit after Tax	3,348	7,218	15,625	15,927
Ex-Od items / Min. Int.	908	(3,909)	497	—
Adj. PAT	2,440	11,127	15,128	15,927
Avg. Shares O/S (m)	2,845.9	2,845.9	2,845.9	2,845.9
EPS (Rs.)	0.9	3.9	5.3	5.6

Cash Flow Abstract (Rs m)

Y/e March	2015	2016	2017E	2018E
C/F from Operations	25,615	15,341	20,933	21,327
C/F from Investing	381	5,337	(10,000)	(14,000)
C/F from Financing	(18,600)	(12,509)	(13,697)	(6,681)
Inc. / Dec. in Cash	7,396	8,168	(2,765)	646
Opening Cash	117	7,513	15,681	12,917
Closing Cash	7,513	15,681	12,917	13,563
FCFF	14,930	13,647	13,401	10,641
FCFE	1,361	6,577	4,401	8,641

Key Financial Metrics

Y/e March	2015	2016	2017E	2018E
Growth				
Revenue (%)	36.4	38.8	21.4	11.2
EBITDA (%)	516.4	111.0	25.2	3.6
PAT (%)	(157.3)	356.1	36.0	5.3
EPS (%)	(153.6)	356.1	36.0	5.3
Profitability				
EBITDA Margin (%)	7.6	11.5	11.9	11.1
PAT Margin (%)	1.8	5.9	6.6	6.3
RoCE (%)	5.7	15.5	19.3	18.6
RoE (%)	5.1	20.9	24.8	21.8

Balance Sheet

Net Debt : Equity	0.5	0.2	0.1	—
Net Wrkng Cap. (days)	(19)	1	1	2

Valuation

PER (x)	112.8	24.7	18.2	17.3
P / B (x)	5.4	5.0	4.1	3.5
EV / EBITDA (x)	29.4	13.2	10.3	9.9
EV / Sales (x)	2.2	1.5	1.2	1.1

Earnings Quality

Eff. Tax Rate	24.3	38.3	29.8	30.5
Other Inc / PBT	36.5	7.1	6.0	6.3
Eff. Depr. Rate (%)	4.9	5.0	5.4	5.1
FCFE / PAT	55.8	59.1	29.1	54.3

Source: Company Data, PL Research.

Balance Sheet Abstract (Rs m)

Y/e March	2015	2016	2017E	2018E
Shareholder's Funds	51,329	55,141	67,103	79,035
Total Debt	34,229	27,160	18,160	16,160
Other Liabilities	4,960	5,356	5,356	5,356
Total Liabilities	90,519	87,656	90,618	100,550
Net Fixed Assets	53,253	51,293	54,199	58,829
Goodwill	503	—	—	—
Investments	26,488	19,179	21,179	25,179
Net Current Assets	10,274	17,184	15,241	16,543
<i>Cash & Equivalents</i>	<i>7,513</i>	<i>15,681</i>	<i>12,917</i>	<i>13,563</i>
<i>Other Current Assets</i>	<i>45,357</i>	<i>47,702</i>	<i>55,730</i>	<i>61,403</i>
<i>Current Liabilities</i>	<i>42,596</i>	<i>46,199</i>	<i>53,406</i>	<i>58,423</i>
Other Assets	—	—	—	—
Total Assets	90,519	87,657	90,618	100,550

Quarterly Financials (Rs m)

Y/e March	Q2FY16	Q3FY16	Q4FY16	Q1FY17
Net Revenue	49,397	40,853	59,553	42,808
EBITDA	5,945	4,297	7,531	4,486
% of revenue	12.0	10.5	12.6	10.5
Depr. & Amortization	1,129	1,087	1,177	1,115
Net Interest	702	666	602	550
Other Income	265	259	320	325
Profit before Tax	4,326	2,738	2,279	3,146
Total Tax	1,458	752	1,508	944
Profit after Tax	2,868	1,986	770	2,202
Adj. PAT	2,915	2,045	4,184	2,202

Key Operating Metrics

Y/e March	2015	2016	2017E	2018E
Passenger M&HCV sales (units)	20,722	25,721	26,870	28,854
Goods M&HCV sales (units)	56,938	84,034	100,600	106,184
Dost volumes (units)	25,223	28,787	32,911	39,414
Other LCV sales (units)	2,033	1,913	614	676
Total volume (units)	104,916	140,455	160,996	175,128
Realisation per vehicle (Rs)	1,268,743	1,322,634	1,401,892	1,432,970
Gross margin per vehicle (Rs)	342,843	395,829	416,070	408,540
EBITDA per vehicle (Rs)	97,853	154,211	168,489	160,475
Profit per vehicle (Rs)	23,254	76,439	93,964	90,946

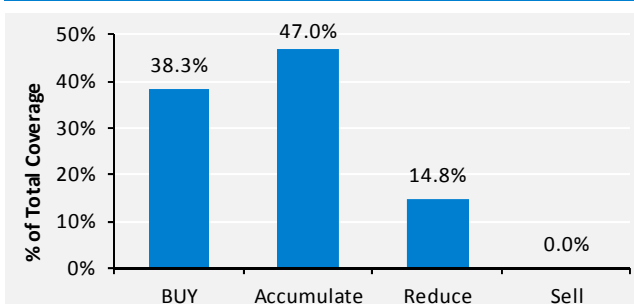
Source: Company Data, PL Research.



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Reduce	: Underperformance to Sensex over 12-months
Sell	: Over 15% underperformance to Sensex over 12-months
Trading Buy	: Over 10% absolute upside in 1-month
Trading Sell	: Over 10% absolute decline in 1-month
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