

SELL

TP: Rs 80 | ▼ 40%

ASHOK LEYLAND

| Automobiles

| 13 August 2021

Margin stress ahead; maintain SELL

- Q1 revenue and gross margin beat our estimates but lower operating efficiency crimped profitability
- Channel checks suggest an 8-10% QoQ rise in steel price, muting gross margin in the near term
- Maintain SELL with a Mar'22 TP of Rs 80

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Lower volumes drive weak Q1: AL's Q1FY22 revenue declined 58% QoQ to Rs 29.5bn (Rs 27.5bn est.), with volumes down 59% QoQ. Despite an above-expected gross margin performance (+280bps QoQ), lower operating efficiencies and poor capacity utilisation in Q1 led to an EBITDA loss of Rs 1.4bn (-4.7% EBITDA margin vs. +3.2% expected). AL reported a net loss of Rs 2.8bn.

Margin stress ahead: Our channel checks suggest that steelmakers have taken an average price hike of Rs 4,000-5,000/t (8-10%) QoQ in Q1FY22. Tyre costs are also expected to rise by 3-4% QoQ in Q2. To mitigate this cost increase, AL will have to take a price hike in the range of 4-5% QoQ which looks difficult in the current environment. Clearly, gross margin pressures will continue in the near term until steel prices cool off.

Modest earnings outlook: We expect FY23 EBITDA per vehicle to improve by 7% over Q4FY21, assuming similar sales volume per quarter, lower discounts and pass-along of steel costs. Assuming steady other income but higher depreciation and interest costs, PAT margin is likely to be significantly lower than in FY18-FY19. Depreciation was high in FY19 and FY20 (due to the introduction of BSVI from FY21), and we believe the increased adoption of EVs, especially in the bus segment, would keep depreciation elevated, thus weighing on PAT.

Maintain SELL: We maintain our FY22/23 estimates and introduce FY24 forecasts, expecting AL to report a revenue CAGR of 29% during FY21-FY24, with ROE/ROCE of 18%/15% by end-FY24 (vs. peaks of 26%/21% in FY18). Our Mar'22 TP stands unchanged at Rs 80 and comprises (1) Rs 70 for AL (valued at 20x FY23E EPS, in line with its long-term average) and (2) a value of Rs 10 for the stake in Hinduja Leyland Finance (in line with consensus) s

The latest investment by Dana implies a ~US\$ 1.8bn valuation for Switch which is subsidiary of AL. Since this is a strategic investment, it may not lead to immediate value discovery. We currently do not assign a value to Switch but note that it does carry upside potential if AL is successful in the global e-mobility segment.

Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	AL IN/Rs 134
Market cap	US\$ 5.3bn
Free float	49%
3M ADV	US\$ 30.9mn
52wk high/low	Rs 143/Rs 52
Promoter/FPI/DII	52%/17%/15%

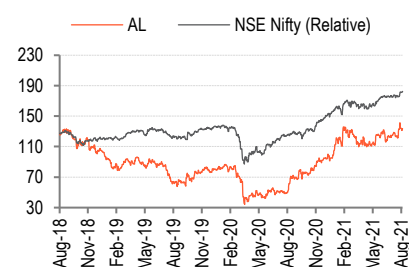
Source: NSE | Price as of 12 Aug 2021

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	153,014	231,600	293,848
EBITDA (Rs mn)	5,351	15,001	23,159
Adj. net profit (Rs mn)	(3,016)	3,644	10,247
Adj. EPS (Rs)	(1.1)	1.2	3.5
Consensus EPS (Rs)	(1.1)	2.1	5.9
Adj. ROAE (%)	(4.3)	5.3	14.0
Adj. P/E (x)	(125.0)	107.6	38.3
EV/EBITDA (x)	74.4	27.8	18.2
Adj. EPS growth (%)			181.2

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Fig 1 – Quarterly performance

(Rs mn)	Q1FY22	Q1FY21	YoY (%)	Q4FY21	QoQ (%)	FY21	FY20	YoY (%)
Volume (nos)	17,987	3,814	371.6	44,060	(59.2)	100,728	125,255	(19.6)
Avg. Realisation per Vehicle (Rs)	1,640,624	1,706,529	(3.9)	1,588,854	3.3	1,736,203	1,380,406	25.8
Total Income (A)	29,510	6,509	353.4	70,005	(57.8)	174,884	172,903	1.1
Operating Expenses:								
Raw Materials Consumed	21,873	4,175	424.0	53,834	(59.4)	132,043	121,449	8.7
Employee Expenses	4,243	3,542	19.8	4,016	5.7	15,310	17,520	(12.6)
Other Expenses	4,795	2,125	125.7	6,813	(29.6)	19,376	22,620	(14.3)
Total Expenditure (B)	30,911	9,841	214.1	64,663	(52.2)	166,729	161,588	3.2
EBITDA (A-B)	(1,401)	(3,332)	NA	5,342	NA	8,155	11,315	(27.9)
Other Income	134	256	(47.7)	380	(64.7)	1,234	1,355	(9)
Depreciation	1,835	1,637	12.1	2,185	(16.0)	7,717	7,000	10
EBIT	(3,102)	(4,713)	NA	3,537	NA	1,672	5,669	(70.5)
Finance Costs	707	769	(8.0)	771	(8.2)	3,182	1,089	192
PBT before Excep Items	(3,809)	(5,481)	NA	2,766	NA	(1,511)	4,581	NA
Exceptional Items	17	17		(374)		(781)	525	NA
PBT after Excep Items	(3,826)	(5,498)	NA	3,139	NA	(2,291)	5,106	NA
Tax Expense	(1,003)	(1,610)	NA	728	NA	(266)	812	NA
Reported PAT	(2,823)	(3,888)	NA	2,412	NA	(2,025)	4,294	NA
Adjusted PAT	(2,806)	(3,871)	NA	2,038	NA	(1,245)	3,769	NA

Source: Company, BOBCAPS Research

Fig 2 – Key parameters

(%)	Q1FY22	Q1FY21	YoY (bps)	Q4FY21	QoQ (bps)	FY21	FY20	YoY (bps)
Gross margin	25.9	35.9	(998)	23.1	278	24.5	29.8	(526)
EBITDA margin	(4.7)	(51.2)	4,645	7.6	(1,238)	4.7	6.5	(188)
EBIT margin	(10.5)	(72.4)	6,190	5.1	(1,556)	1.0	3.3	(232)
PBT margin	(12.9)	(84.2)	7,131	4.0	(1,686)	(0.9)	2.6	(351)
Tax rate	26.2	29.3	(306)	23.2	304	11.6	15.9	(430)
Adj PAT margin	(9.5)	(59.5)	4,997	2.9	(1,242)	(0.7)	2.2	(289)

Source: Company, BOBCAPS Research

Valuation methodology

We maintain our FY22/23 estimates and introduce FY24 forecasts, expecting AL to report a revenue CAGR of 29% during FY21-FY24, with ROE/ROCE of 18%/15% by end-FY24 (vs. peaks of 26%/21% in FY18). Our Mar'22 TP stands unchanged at Rs 80 and comprises (1) Rs 70 for AL (valued at 20x FY23E EPS, in line with its long-term average) and (2) a value of Rs 10 for the stake in Hinduja Leyland Finance (in line with consensus).

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Fig 3 – Key assumptions

Parameter (Rs mn)	FY21	FY22E	FY23E	FY24E
M&HCV volumes (nos)	51,820	79,200	102,960	112,226
LCV volumes (nos)	48,908	66,000	75,900	83,490
Total volume sold (Nos)	100,728	145,200	178,860	195,716
Revenue per vehicle (Rs)	1,519,086	1,595,040	1,642,892	1,692,178
Revenues	153,015	231,600	293,848	331,187
EBITDA	5,351	15,001	23,159	27,507
OPM (%)	3.5	6.5	7.9	8.3
Adj. PAT	(3,016)	3,644	10,247	13,999
EPS (Rs)	(1.1)	1.2	3.5	4.8

Source: Company, BOBCAPS Research

Fig 4 – Valuation summary

Business	Value (Rs/sh)	Comments
Standalone Business	70	20x FY23E EPS
Hinduja Leyland Finance	10	Consensus value
Total	80	

Source: BOBCAPS Research

Key risks

Key upside risks to our estimates are:

- above-expected sales volume,
- sharp fall in raw material prices,
- increase in market share, and
- assignment of meaningful value to subsidiaries.

Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Ashok Leyland	AL IN	5.3	134	80	SELL
Bajaj Auto	BJAUT IN	14.7	3,769	3,200	SELL
Hero MotoCorp	HMCL IN	7.5	2,783	2,900	HOLD
Mahindra & Mahindra	MM IN	13.0	776	630	SELL
Maruti Suzuki	MSIL IN	28.5	7,012	8,000	HOLD
TVS Motor	TVSL IN	3.5	552	480	SELL
VST Tillers Tractors	VSTT IN	0.2	1,909	2,300	HOLD

Source: BOBCAPS Research, NSE | Price as of 12 Aug 2021

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Total revenue	178,847	153,014	231,600	293,848	331,187
EBITDA	11,736	5,351	15,001	23,159	27,507
Depreciation	6,698	7,477	8,256	8,483	9,166
EBIT	6,272	(931)	7,973	15,964	19,749
Net interest inc./(exp.)	(1,095)	(3,068)	(3,270)	(2,742)	(1,686)
Other inc./(exp.)	1,233	1,195	1,227	1,287	1,407
Exceptional items	(1,558)	(121)	0	0	0
EBT	3,619	(4,119)	4,702	13,221	18,063
Income taxes	1,224	(983)	1,058	2,975	4,064
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
Reported net profit	2,395	(3,136)	3,644	10,247	13,999
Adjustments	1,558	121	0	0	0
Adjusted net profit	3,953	(3,016)	3,644	10,247	13,999

Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Accounts payables	26,239	51,647	49,666	62,586	74,144
Other current liabilities	18,227	14,859	35,769	42,111	44,111
Provisions	8,055	6,545	6,545	6,545	6,545
Debt funds	32,814	37,163	37,163	25,162	13,162
Other liabilities	3,273	2,805	2,805	2,805	2,805
Equity capital	2,936	2,936	2,936	2,936	2,936
Reserves & surplus	69,704	66,837	65,400	70,058	77,909
Shareholders' fund	72,640	69,772	68,336	72,993	80,844
Total liab. and equities	161,248	182,792	200,283	212,202	221,611
Cash and cash eq.	13,225	8,436	5,636	7,465	5,026
Accounts receivables	11,798	28,160	28,553	30,592	34,480
Inventories	12,380	21,423	22,208	24,152	27,221
Other current assets	17,855	16,397	32,266	33,357	35,914
Investments	27,196	30,687	30,687	33,687	36,687
Net fixed assets	68,036	70,504	73,466	75,983	75,318
CWIP	5,941	3,719	4,000	3,500	3,500
Intangible assets	0	0	0	0	0
Deferred tax assets, net	(2,648)	(1,708)	(1,708)	(1,708)	(1,708)
Other assets	7,464	5,174	5,174	5,174	5,174
Total assets	161,247	182,792	200,283	212,202	221,611

Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Cash flow from operations	4,104	6,650	15,824	28,888	24,115
Capital expenditures	(17,954)	(7,722)	(11,500)	(10,500)	(8,500)
Change in investments	(831)	(3,491)	0	(3,000)	(3,000)
Other investing cash flows	1,233	1,195	1,227	1,287	1,407
Cash flow from investing	(17,552)	(10,018)	(10,273)	(12,213)	(10,093)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	26,490	4,349	0	(12,000)	(12,000)
Interest expenses	(1,095)	(3,068)	(3,270)	(2,742)	(1,686)
Dividends paid	(12,702)	(1,761)	(5,081)	(5,589)	(6,148)
Other financing cash flows	244	(940)	0	0	0
Cash flow from financing	12,937	(1,421)	(8,351)	(20,331)	(19,834)
Chg in cash & cash eq.	(511)	(4,789)	(2,799)	(3,656)	(5,812)
Closing cash & cash eq.	13,225	8,436	5,636	7,465	7,465

Per Share

Y/E 31 Mar (Rs)	FY20A	FY21A	FY22E	FY23E	FY24E
Reported EPS	1.3	(1.0)	1.2	3.5	4.8
Adjusted EPS	0.8	(1.1)	1.2	3.5	4.8
Dividend per share	4.3	0.6	1.7	1.9	2.1
Book value per share	24.7	23.8	23.3	24.9	27.5

Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21A	FY22E	FY23E	FY24E
EV/Sales	2.2	2.6	1.8	1.4	1.2
EV/EBITDA	33.2	74.4	27.8	18.2	14.8
Adjusted P/E	163.8	(125.0)	107.6	38.3	28.0
P/BV	5.4	5.6	5.7	5.4	4.9

DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21A	FY22E	FY23E	FY24E
Tax burden (Net profit/PBT)	109.2	73.2	77.5	77.5	77.5
Interest burden (PBT/EBIT)	57.7	442.6	59.0	82.8	91.5
EBIT margin (EBIT/Revenue)	3.5	(0.6)	3.4	5.4	6.0
Asset turnover (Rev./Avg TA)	175.4	140.1	212.4	280.8	334.9
Leverage (Avg TA/Avg Equity)	1.3	1.5	1.6	1.5	1.3
Adjusted ROAE	5.1	(4.2)	5.3	14.5	18.2

Ratio Analysis

Y/E 31 Mar	FY20A	FY21A	FY22E	FY23E	FY24E
YoY growth (%)					
Revenue	(39.3)	(14.4)	51.4	26.9	12.7
EBITDA	(61.8)	(54.4)	180.3	54.4	18.8
Adjusted EPS	(80.0)			181.2	36.6
Profitability & Return ratios (%)					
EBITDA margin	6.6	3.5	6.5	7.9	8.3
EBIT margin	3.5	(0.6)	3.4	5.4	6.0
Adjusted profit margin	2.2	(2.0)	1.6	3.5	4.2
Adjusted ROAE	5.4	(4.3)	5.3	14.0	17.3
ROCE	4.1	(0.6)	5.7	11.8	15.5
Working capital days (days)					
Receivables	38	48	45	37	36
Inventory	40	40	34	29	28
Payables	115	125	105	93	100
Ratios (x)					
Gross asset turnover	0.5	0.7	0.5	0.4	0.4
Current ratio	1.1	1.0	1.0	0.9	0.8
Net interest coverage ratio	(5.7)	0.3	(2.4)	(5.8)	(11.7)
Adjusted debt/equity	0.5	0.5	0.5	0.3	0.2

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Disclaimer

Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

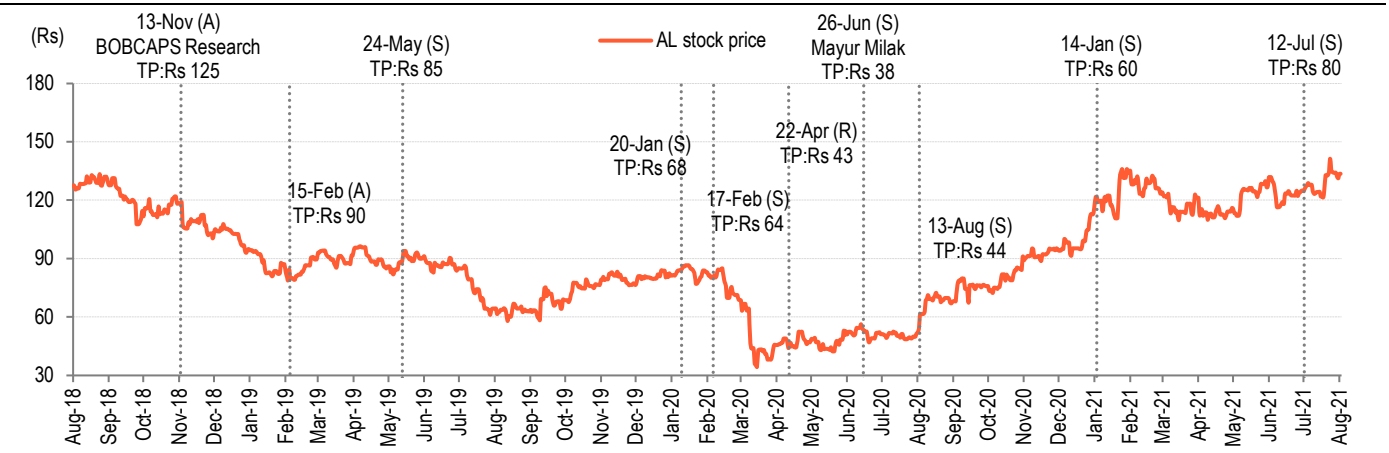
HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

Ratings and Target Price (3-year history): ASHOK LEYLAND (AL IN)



B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

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