

**SELL**

TP: Rs 38 | ▼ 28%

**ASHOK LEYLAND**

Automobiles

26 June 2020

## Weak macros, rich valuations – downgrade to SELL

**AL's Q4FY20 performance was lacklustre despite the boost to blended average realisations from BS-VI price upgrades. Demand remains tepid as operator utilisation continues to languish below 50%. While we assume a 5% GDP revival in FY22, we believe most optimism is in the price. Inter-corporate deposits in group companies are a cause for concern amidst ballooning gross debt over the last three months. We downgrade the stock from REDUCE to SELL with a revised Mar'21 TP of Rs 38 (from Rs 43).**

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**Weak Q4:** AL's topline declined 57% YoY to Rs 38bn due to weak volumes. Average selling price improved 1% YoY, reflective of BS-VI dispatches. EBITDA dropped 81% YoY to Rs 1.8bn, with margins at 4.8%. Adjusting for a one-time write-off of Rs 687mn towards impairment of investments, PAT stood at Rs 114mn, down 98% YoY – this only with a 13-day lockdown in March.

**Key assumptions:** Our channel checks with fleet operators suggest that their current utilisation continues to be at sub-50% levels, which will dent demand. In our view, even the pending scrappage policy will fail to trigger a significant demand push till the economy revives significantly. For FY22, we conservatively assume GDP growth of 5% (against 6.7% estimated by our chief economist), which should aid volume growth of 44% and operating margin expansion to 7.5% for AL. We pencil in EPS of Rs 2.1 for FY22.

**Downgrade to SELL:** Stock has witnessed ~40% rally since Apr'20. Despite strong growth assumptions, current valuations look stretched at 25x FY22E EPS. A steep increase in gross debt over the past three months from ~Rs 30bn to Rs 50bn and inter-corporate deposits within group companies do not augur well. We value the stock at the four-year average P/E multiple of 18x on FY22E (vs. 8x FY22E EBITDA earlier), translating to a revised TP of Rs 38. Cut to SELL.

Ticker/Price	AL IN/Rs 52
Market cap	US\$ 2.0bn
Shares o/s	2,936mn
3M ADV	US\$ 28.1mn
52wk high/low	Rs 91/Rs 34
Promoter/FPI/DII	52%/17%/15%

Source: NSE

## STOCK PERFORMANCE



Source: NSE

## KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20P	FY21E	FY22E
Total revenue (Rs mn)	267,586	294,439	174,675	164,483	240,662
EBITDA (Rs mn)	26,818	30,748	11,737	9,987	17,967
Adj. net profit (Rs mn)	17,177	19,832	3,953	696	6,228
Adj. EPS (Rs)	5.8	6.8	0.8	0.2	2.1
Adj. EPS growth (%)	36.5	15.1	(80.1)	(82.4)	794.6
Adj. ROAE (%)	23.7	23.8	5.4	1.0	8.4
Adj. P/E (x)	9.0	7.7	64.3	221.2	24.7
EV/EBITDA (x)	6.1	5.2	12.9	15.9	9.8

Source: Company, BOBCAPS Research

**BOB Capital Markets Ltd is a wholly owned subsidiary of Bank of Baroda**

Important disclosures, including any required research certifications, are provided at the end of this report.



**FIG 1 – QUARTERLY PERFORMANCE – STANDALONE**

Y/E Mar (Rs mn)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20	FY19	YoY (%)
<b>Net Revenues</b>	<b>38,385</b>	<b>88,459</b>	<b>(56.6)</b>	<b>40,157</b>	<b>(4.4)</b>	<b>136,290</b>	<b>201,833</b>	<b>(32.5)</b>
Raw Materials	27,290	64,292	(57.6)	29,532	(7.6)	96,402	143,157	(32.7)
% of Net Sales	71.1	72.7	-	73.5	-	70.7	70.9	-
Personnel	4,097	5,735	(28.6)	2,728	50.2	12,053	15,104	(20.2)
% of Net Sales	10.7	6.5	-	6.8	-	8.8	7.5	-
Manufacturing & Other Exp	5,168	8,578	(39.7)	5,645	(8.4)	17,928	22,542	(20.5)
% of Net Sales	13.5	9.7	-	14.1	-	13.2	11.2	-
Total Expenditure	36,555	78,605	(53.5)	37,905	(3.6)	126,383	180,802	(30.1)
<b>EBITDA</b>	<b>1,830</b>	<b>9,854</b>	<b>(81.4)</b>	<b>2,252</b>	<b>(18.7)</b>	<b>9,907</b>	<b>21,031</b>	<b>(52.9)</b>
<b>EBITDA Margin (%)</b>	<b>4.8</b>	<b>11.1</b>	<b>-</b>	<b>5.6</b>	<b>-</b>	<b>7.3</b>	<b>10.4</b>	<b>-</b>
Depreciation	1,877	1,598	17.5	1,575	19.2	4,821	4,439	8.6
<b>EBIT</b>	<b>(47)</b>	<b>8,257</b>	<b>(100.6)</b>	<b>677</b>	<b>(107.0)</b>	<b>5,086</b>	<b>16,592</b>	<b>(69.3)</b>
Interest Expenses	331	166	99.3	337	(1.7)	764	481	58.6
Non-operating income	344	91	279.3	223	54.2	889	989	(10.1)
Extraordinary Expenses	687	117	NA	22	NA	871	367	NA
Extraordinary Income	0	0	NA	0	NA	0	(72)	NA
<b>PBT</b>	<b>(721)</b>	<b>8,065</b>	<b>(108.9)</b>	<b>542</b>	<b>(233.1)</b>	<b>4,340</b>	<b>16,661</b>	<b>(74.0)</b>
Tax-Total	(148)	1,535	(109.6)	264	(155.9)	1,372	4,556	(69.9)
Tax Rate (%) - Total	20.5	19.0	7.7	48.8		31.6	27.3	15.6
<b>Reported PAT</b>	<b>(573)</b>	<b>6,530</b>	<b>(108.8)</b>	<b>278</b>	<b>(306.6)</b>	<b>2,968</b>	<b>12,105</b>	<b>(75.5)</b>
<b>Adj. PAT</b>	<b>114</b>	<b>6,647</b>	<b>(98.3)</b>	<b>299</b>	<b>(61.9)</b>	<b>3,839</b>	<b>12,544</b>	<b>(69.4)</b>
<b>PAT Margin</b>	<b>0.3</b>	<b>7.5</b>	<b>-</b>	<b>0.7</b>	<b>-</b>	<b>2.8</b>	<b>6.2</b>	<b>-</b>

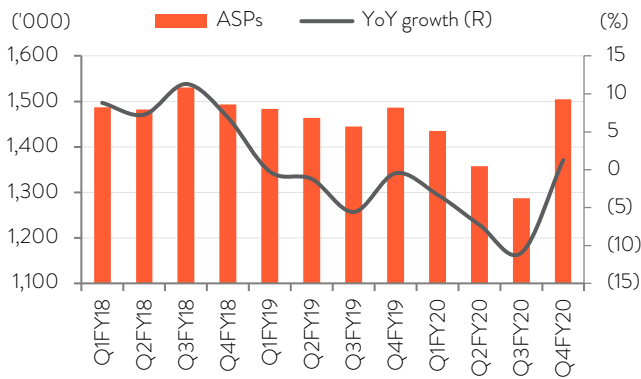
Source: Company, BOBCAPS Research

**FIG 2 – PER UNIT PARAMETERS**

(Rs)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20	FY19	YoY (%)
<b>Sales Volume (nos)</b>	<b>25,507</b>	<b>59,519</b>	<b>(57.1)</b>	<b>31,200</b>	<b>(18.2)</b>	<b>125,253</b>	<b>197,366</b>	<b>(36.5)</b>
Net Realisation/Vehicle	1,504,865	1,486,236	1.3	1,287,067	16.9	1,088,118	1,022,635	6.4
Material Cost/Vehicle	1,069,887	1,080,195	(1.0)	946,548	13.0	769,657	725,335	6.1
Gross Profit/Vehicle	434,979	406,042	7.1	340,519	27.7	318,461	297,300	7.1
Employee Cost/Vehicle	160,630	96,352	66.7	87,433	83.7	96,232	76,529	25.7
Other Expenses/Vehicle	202,623	144,122	40.6	180,923	12.0	143,133	114,212	25.3
EBITDA/Vehicle	71,725	165,567	(56.7)	72,163	(0.6)	79,096	106,559	(25.8)
Net Profit/Vehicle	4,473	111,674	(96.0)	9,590	(53.4)	30,652	63,558	(51.8)

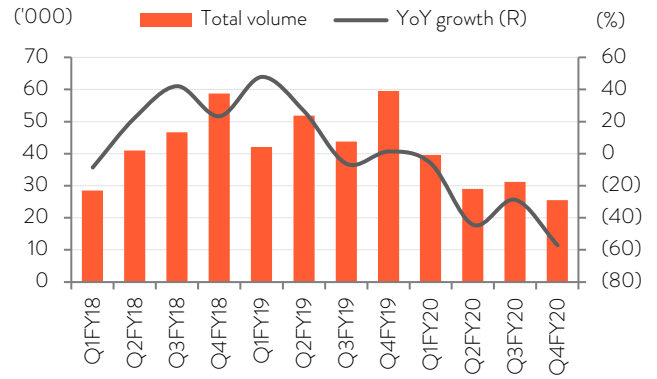
Source: Company, BOBCAPS Research

**FIG 3 – AVERAGE SELLING PRICE (ASP)**



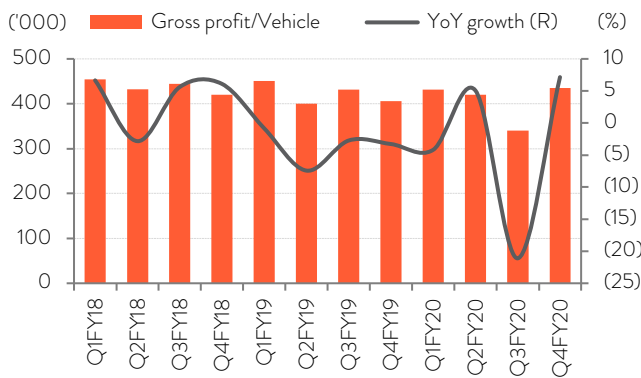
Source: Company, BOBCAPS Research

**FIG 4 – VOLUME GROWTH TREND**



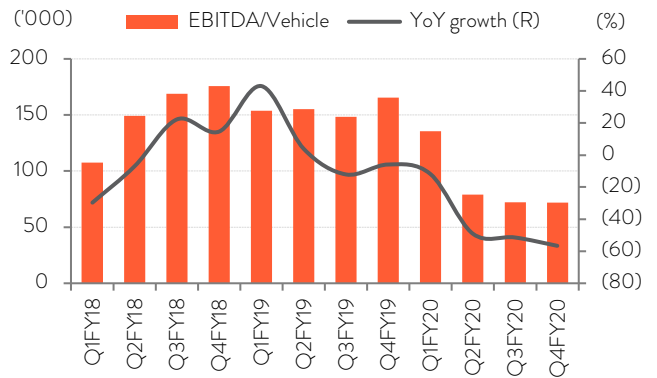
Source: SIAM, ET Autolytics, BOBCAPS Research

**FIG 5 – GROSS PROFIT/VEHICLE**



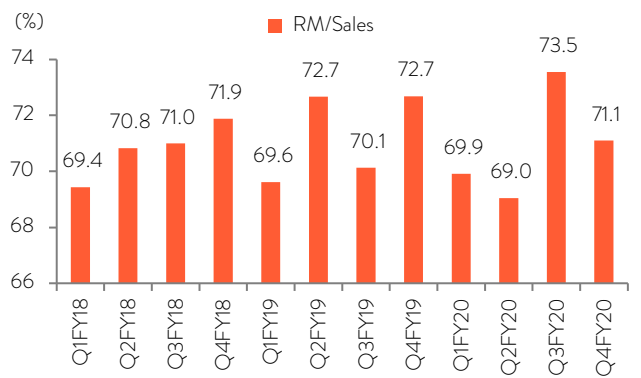
Source: BOBCAPS Research, Company

**FIG 6 – EBITDA/VEHICLE**



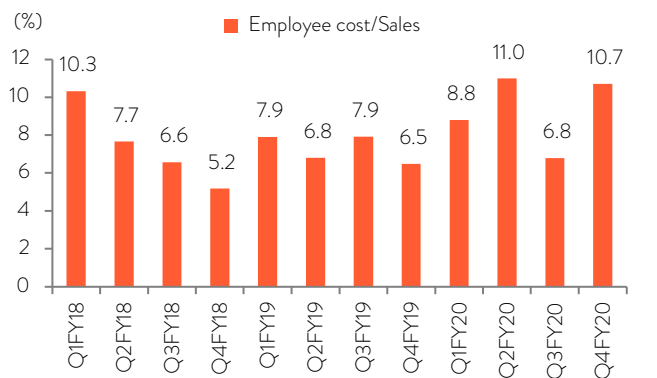
Source: BOBCAPS Research, Company

**FIG 7 – RM COST/SALES TREND**



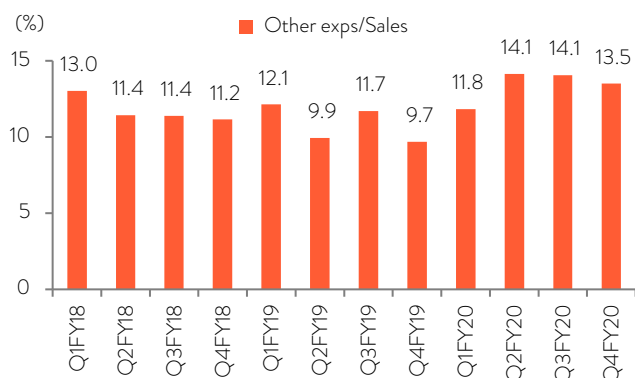
Source: Company, BOBCAPS Research

**FIG 8 – EMPLOYEE COST/SALES TREND**



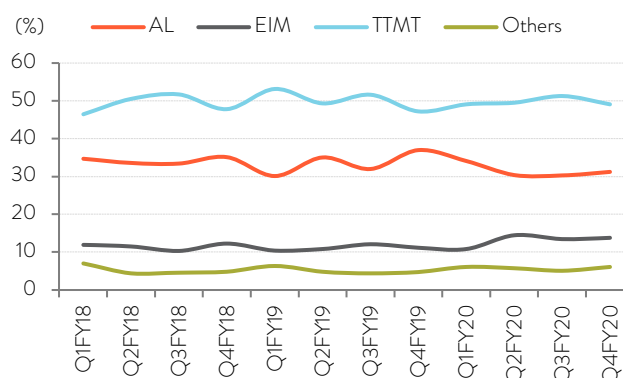
Source: Company, BOBCAPS Research

**FIG 9 – OTHER EXPENSES/SALES TREND**



Source: Company, BOBCAPS Research

**FIG 10 – MHCV MARKET SHARE TRENDS**



Source: SIAM, ET Autolytics, BOBCAPS Research

### Earnings call highlights

- ASP improvement of 1.3% YoY in Q4FY20 was largely due to an increased share of higher tonnage vehicles and BSVI dispatches.
- Additional discounts provided by suppliers supported gross margin improvement.
- AL has successfully transitioned from BS-IV to BS-VI, with no BS-IV inventory at the company and its dealers.
- A new LCV product is slated for launch in Q2FY21 which will broaden the company’s range in the segment and help gain market share.
- AL has expensed close to Rs 1bn in all as impairment charges on its investment in Optare.
- In FY20, the company expensed Rs 12.3bn in capex which was lower than guided earlier. As per management, heavy capex is complete and only maintenance outlays will be incurred in coming years.
- Net debt stands at Rs 40bn currently, against Rs 20bn at the end of FY20.
- AL ended FY20 with negative operating cash flow of Rs 7bn (–Rs 4bn in FY19).

## Valuation methodology

While FY21 will be lacklustre, we conservatively assume GDP growth of 5% in FY22 (against 6.7% estimated by our chief economist), which should aid volume growth of 44% and operating margin expansion to 7.5% for AL. We model for EPS of Rs 2.1, with ROE/ROCE of 8.5%/6.6% in FY22.

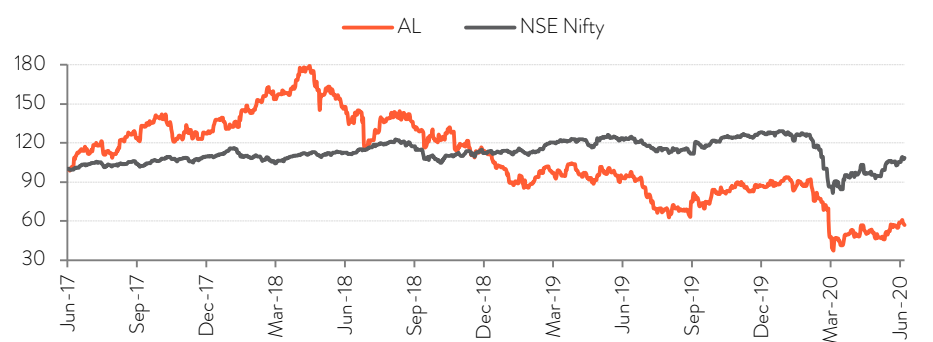
The stock has rallied nearly 40% since Apr'20. Despite strong growth assumptions, current valuations look stretched at 25x FY22E EPS. A steep increase in gross debt over the past three months from ~Rs 30bn to Rs 50bn and inter-corporate deposits within group companies do not augur well. We value the stock at the four-year average P/E multiple of 18x on FY22E (vs. 8x FY22E EBITDA earlier), translating to a revised Mar'21 target price of Rs 38 – downgrade from REDUCE to SELL.

**FIG 11 – KEY VOLUME ASSUMPTIONS**

Particulars	FY20A	FY21E	FY22E
<b>Total volumes</b>	<b>125,255</b>	<b>108,752</b>	<b>156,000</b>
YoY growth (%)	(36.5)	(13.2)	43.4
MHCVs	78,609	66,469	96,000
YoY growth (%)	(45.0)	(15.4)	44.4
LCVs	46,646	42,283	60,000
YoY growth (%)	(14.4)	(9.4)	41.9

Source: Company, BOBCAPS Research

**FIG 12 – RELATIVE STOCK PERFORMANCE**



Source: NSE

## Key risks

- A scrappage scheme with significant government support in the form of large incentives for fleet replacement could lend a short-term boost to CV demand.
- Economic recovery backed by additional fiscal stimulus from the government could drive a faster-than-expected revival in CV volumes.
- Delay in DFC commissioning could defer the potential volume shift from road to rail.

## FINANCIALS

### Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
<b>Total revenue</b>	<b>267,586</b>	<b>294,439</b>	<b>174,675</b>	<b>164,483</b>	<b>240,662</b>
EBITDA	26,818	30,748	11,737	9,987	17,967
Depreciation	5,985	6,210	6,698	7,821	8,648
EBIT	25,331	25,672	6,272	3,175	10,711
Net interest income/(expenses)	(1,473)	(704)	(1,095)	(2,276)	(2,676)
Other income/(expenses)	4,498	1,133	1,233	1,008	1,392
Exceptional items	(129)	57	(1,558)	0	0
EBT	23,729	25,025	3,619	898	8,036
Income taxes	6,681	5,136	1,224	202	1,808
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
<b>Reported net profit</b>	<b>17,048</b>	<b>19,889</b>	<b>2,395</b>	<b>696</b>	<b>6,228</b>
Adjustments	129	(57)	1,558	0	0
<b>Adjusted net profit</b>	<b>17,177</b>	<b>19,832</b>	<b>3,953</b>	<b>696</b>	<b>6,228</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Accounts payables	50,033	51,545	26,242	36,236	39,339
Other current liabilities	22,824	24,977	20,392	21,316	34,973
Provisions	8,201	8,028	8,055	8,055	8,055
Debt funds	12,263	6,324	30,648	50,648	46,648
Other liabilities	4,602	5,549	3,273	3,273	3,273
Equity capital	2,927	2,936	2,936	2,936	2,936
Reserves & surplus	69,528	80,389	69,704	68,865	71,252
Shareholders' fund	72,456	83,324	72,640	71,800	74,188
<b>Total liabilities and equities</b>	<b>170,378</b>	<b>179,747</b>	<b>161,250</b>	<b>191,329</b>	<b>206,476</b>
Cash and cash eq.	10,422	13,736	13,225	24,739	28,180
Accounts receivables	9,448	25,055	11,798	16,674	19,780
Inventories	17,583	26,847	12,380	15,772	18,462
Other current assets	11,630	16,226	17,858	30,975	34,533
Investments	56,067	26,365	27,196	23,196	23,196
Net fixed assets	55,480	56,145	68,036	69,156	72,509
CWIP	4,226	6,576	5,941	6,000	5,000
Intangible assets	0	0	0	0	0
Deferred tax assets, net	(2,985)	(2,497)	(2,648)	(2,648)	(2,648)
Other assets	8,508	11,294	7,464	7,464	7,464
<b>Total assets</b>	<b>170,379</b>	<b>179,747</b>	<b>161,250</b>	<b>191,329</b>	<b>206,476</b>

Source: Company, BOBCAPS Research

**Cash Flows**

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Net income + Depreciation	23,033	26,099	9,093	8,517	14,875
Interest expenses	1,473	704	1,095	2,276	2,676
Non-cash adjustments	(4,498)	(1,133)	(1,233)	(1,008)	(1,392)
Changes in working capital	32,794	(27,814)	(2,215)	(10,466)	7,405
Other operating cash flows	(840)	(487)	0	0	0
<b>Cash flow from operations</b>	<b>51,962</b>	<b>(2,632)</b>	<b>6,739</b>	<b>(681)</b>	<b>23,564</b>
Capital expenditures	(13,924)	(9,225)	(17,954)	(9,000)	(11,000)
Change in investments	(27,278)	29,702	(831)	4,000	0
Other investing cash flows	4,498	1,133	1,233	1,008	1,392
<b>Cash flow from investing</b>	<b>(36,705)</b>	<b>21,610</b>	<b>(17,552)</b>	<b>(3,992)</b>	<b>(9,608)</b>
Equities issued/Others	45	86	0	0	0
Debt raised/repaid	(9,186)	(5,939)	24,325	20,000	(4,000)
Interest expenses	(1,473)	(704)	(1,095)	(2,276)	(2,676)
Dividends paid	(5,495)	(8,598)	(1,536)	(1,536)	(3,840)
Other financing cash flows	2,152	(508)	(11,393)	0	0
<b>Cash flow from financing</b>	<b>(13,956)</b>	<b>(15,663)</b>	<b>10,302</b>	<b>16,188</b>	<b>(10,516)</b>
<b>Changes in cash and cash eq.</b>	<b>1,301</b>	<b>3,315</b>	<b>(511)</b>	<b>11,514</b>	<b>3,441</b>
<b>Closing cash and cash eq.</b>	<b>10,422</b>	<b>13,736</b>	<b>13,225</b>	<b>24,739</b>	<b>28,180</b>

**Per Share**

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20P	FY21E	FY22E
Reported EPS	5.9	6.8	1.3	0.2	2.1
Adjusted EPS	5.8	6.8	0.8	0.2	2.1
Dividend per share	1.9	2.9	0.5	0.5	1.3
Book value per share	24.8	28.4	24.7	24.5	25.3

**Valuations Ratios**

Y/E 31 Mar (x)	FY18A	FY19A	FY20P	FY21E	FY22E
EV/Sales	0.6	0.5	0.9	1.0	0.7
EV/EBITDA	6.1	5.2	12.9	15.9	9.8
Adjusted P/E	9.0	7.7	64.3	221.2	24.7
P/BV	2.1	1.8	2.1	2.1	2.1

**DuPont Analysis**

Y/E 31 Mar (%)	FY18A	FY19A	FY20P	FY21E	FY22E
Tax burden (Net profit/PBT)	72.4	79.2	109.2	77.5	77.5
Interest burden (PBT/EBIT)	93.7	97.5	57.7	28.3	75.0
EBIT margin (EBIT/Revenue)	9.5	8.7	3.6	1.9	4.5
Asset turnover (Revenue/Avg TA)	307.2	319.1	173.2	141.6	192.7
Leverage (Avg TA/Avg Equity)	1.3	1.2	1.3	1.6	1.7
Adjusted ROAE	25.7	25.5	5.1	1.0	8.5

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

**Ratio Analysis**

Y/E 31 Mar	FY18A	FY19A	FY20P	FY21E	FY22E
<b>YoY growth (%)</b>					
Revenue	30.7	10.0	(40.7)	(5.8)	46.3
EBITDA	53.1	14.7	(61.8)	(14.9)	79.9
Adjusted EPS	36.5	15.1	(80.1)	(82.4)	794.6
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	10.0	10.4	6.7	6.1	7.5
EBIT margin	9.5	8.7	3.6	1.9	4.5
Adjusted profit margin	6.4	6.7	2.3	0.4	2.6
Adjusted ROAE	23.7	23.8	5.4	1.0	8.4
ROCE	20.9	22.1	4.1	2.1	6.6
<b>Working capital days (days)</b>					
Receivables	12	21	39	32	28
Inventory	29	28	41	31	26
Payables	80	90	115	98	81
<b>Ratios (x)</b>					
Gross asset turnover	0.3	0.3	0.5	0.6	0.5
Current ratio	0.6	1.0	1.0	1.3	1.2
Net interest coverage ratio	(17.2)	(36.5)	(5.7)	(1.4)	(4.0)
Adjusted debt/equity	0.2	0.1	0.4	0.7	0.6

Source: Company, BOBCAPS Research



## Disclaimer

### Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

**ADD** – Expected return from >+5% to +15%

**REDUCE** – Expected return from -5% to +5%

**SELL** – Expected return <-5%

**Note:** Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

### HISTORICAL RATINGS AND TARGET PRICE: ASHOK LEYLAND (AL IN)



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

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