13 December 2002
Research Note

Ashok Leyland

Buy

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Rs 95

Ashok Leyland Limited's stock has under performed both its CV sector peers as well as the broad market in the past six months as investors fretted over the loss in market share to Telco during H1 FY03. We are however, unfazed by this as Telco's market share gains were more of a short-term aberration while the longer term trend clearly remains towards the shift to heavier multi-axle vehicles, which will benefit ALL.

In our opinion, a combination of robust CV sector growth as well as ongoing improvements in its product portfolio will drive earnings while enhanced operational efficiencies and diversified business mix will help safeguard from the inherent volatility of the CV sector.

We are upgrading the stock to a **BUY** from Out Performer with a 12-month price target of Rs128.

CV demand will remain robust in the medium to long-term

Road and highway construction activity
The government's execution of the *Golden Quadrilateral* project and that too in a time-bound manner gives us confidence of the government's abilities to execute the much bigger North-South, East-West (NSEW) corridor project slated for completion in 2007. Also, the government plans to connect ports to the main highways through world-class roads. These projects will help keep CV demand robust.

Creation of a world-class road infrastructure
Creation of a world-class road infrastructure, as a result of these projects, will also help drive the shift towards increasing use of road transport over rail for both passenger as well as freight movement across the country. Specifically, for the goods segment this would mean demand for higher tonnage multi-axle trucks as operating costs for these would be much lower on a per tonne/km basis.

Cheap and easy access to finance
Cheap and easy access to finance for truck operators would be another key demand driver. Apart from the fact that interest rates for truck financing have fallen significantly in the last year or so, NBFCs and banks today have extended their reach in terms of number of towns/villages covered which will also help drive demand.

Passenger segment: Uptick in private operator demand could drive volumes
The passenger segment has stagnated in recent times due to poor financial health of state transport undertakings. However, any pick up in private operator demand as well as a move towards potential privatization of state controlled bus routes (already initiated in Tamil Nadu) could provide additional upsides.

New product launches in traditionally weak segments
ALL has this far been concentrating on the higher (in terms of tonnage) end of the truck segment. However, with the *Ecomet* range, slated for launch some time in December or January, ALL will look at grabbing market share in the lower tonnage segments, which has traditionally been a stronghold of competitors like Telco, Eicher Motors and Swaraj Mazda. ALL's recent launch of the new *W series* HCVs on the proven Hino engine platform will also help it improve its competitive product positioning vis-à-vis Telco.

Revenue model significantly de-risked
In FY02, ALL derived nearly 24% of revenues from outside the commercial vehicle business (including trucks and buses) with engines, spares and defence sales contributing towards this. Furthermore, differing demand dynamics in the truck and bus segments also serves as a hedge against downturns in any particular segment.

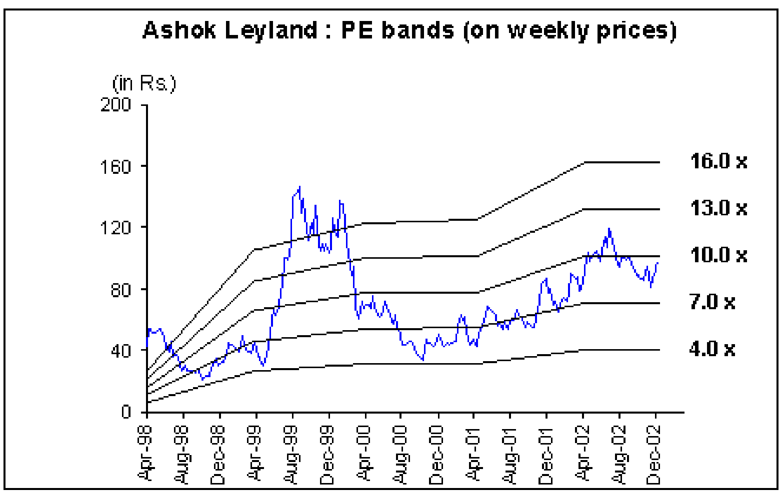
Operational efficiency improvements to continue

Since FY98, ALL has been concentrating on improving its operational and financial parameters. ALL has not only pruned its working capital requirements and reduced capex, it has also introduced huge cost cutting initiatives. We believe such efficiency enhancements will continue though the quantum of these improvements would be much smaller than in the past.

Valuation: Fair value upside of 34%

Our target price of Rs128 is based on 5.5x FY04E EV/EBITDA and 9.5x FY04E EPS. This compares well with the stock's median five year forward EV/EBITDA of 5.5 and median five year forward P/E of 10. We recommend a **Buy** at current levels. We will be following up with a detailed report on ALL very soon.

Year March	Sales Rs Mn	Adj. PAT Rs Mn	chg %	EPS Rs	PE X	ROE %	ROCE %
FY00	23310	785	285	6.6	14.5	7.2	12.8
FY01	23150	917	17	7.7	12.4	8.2	13.7
FY02	23274	922	1	7.8	12.3	8.6	14.1
FY03E	26015	1209	31	10.2	9.4	12.1	17.0
FY04E	28908	1596	32	13.4	7.1	15.3	19.9



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Stock Ratings Absolute Returns

Buy	:	> 25%
Out Performer	:	16 - 25%
Market Performer	:	0 - 15%
Under Performer	:	< 0%

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