

Ashok Leyland

Sumeet Pillai (sumeetpillai@karvy.com)

Buy

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 upsidess.

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.

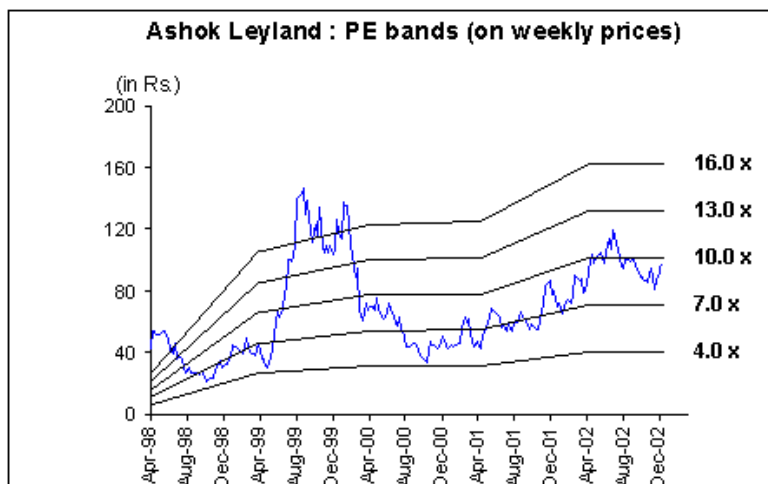
Operational efficiency improvements to continue

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	Sales	Adj. PAT	chg	EPS	PE	ROE	ROCE
March	Rs Mn	Rs Mn	%	Rs	X	%	%
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



Stock Ratings Absolute Returns

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

Karvy Stock Broking Limited

131, Andheri Industrial Estate, Off Veera Desai Road, Andheri (W), Mumbai – 400 053. India.
Voice: (91-22) 695 0204 - 7, 636 7226 /9044.

Disclaimer

The information and views presented in this report are prepared by Karvy Stock Broking Limited. The information contained herein is based on our analysis and up on sources that we consider reliable. We, however, do not vouch for the accuracy or the completeness thereof. This material is for personal information and we are not responsible for any loss incurred based upon it.

The investments discussed or recommended in this report may not be suitable for all investors. Investors must make their own investment decisions based on their specific investment objectives and financial position and using such independent advice, as they believe necessary. While acting upon any information or analysis mentioned in this report, investors may please note that neither Karvy nor any person connected with any associated companies of Karvy accepts any liability arising from the use of this information and views mentioned in this document.

The author, directors and other employees of Karvy and its affiliates may hold long or short positions in the above-mentioned companies from time to time. Every employee of Karvy and its associated companies are required to disclose their individual stock holdings and details of trades, if any, that they undertake. The team rendering corporate analysis and investment recommendations are restricted in purchasing/selling of shares or other securities till such a time this recommendation has either been displayed or has been forwarded to clients of Karvy. All employees are further restricted to place orders only through Karvy Stock Broking Ltd