

**Investment Idea
Automobiles**

Ashok Leyland Limited

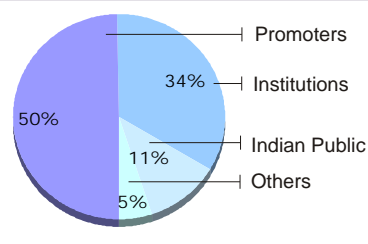
CMP : Rs. 35.0

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Stock Codes

Bloomberg : AL.IN
Reuters : ASOK.BO
BSE Code : 500477
NSE Code : ASHOKLEY
BSE Group : A

**Share Holdings (%)
As on 31st March, 2006.**



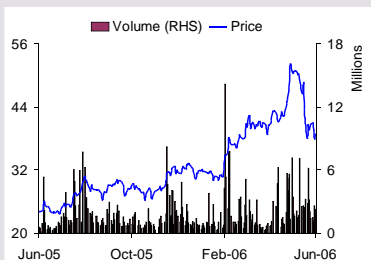
Stock Data

Sensex : 9296.0
Nifty : 2724.0
52 W High Rs. : 53.95
52 W Low Rs. : 22.95
Mkt Cap Rs. Mn : 42755.65
Face Value : Rs 1.00

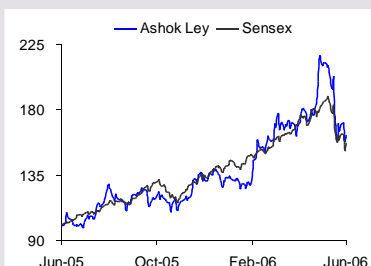
Absolute Returns

%	1M	3M	6M
ALL	-23.25	-2.75	23.45
Sensex	-15.36	-1.36	16.62

Price/Volume



Price Comparison



Ashok Leyland (ALL), the second largest CV manufacturer, has been the technology leader in India's commercial vehicle industry, moulding the country's commercial vehicle profile by introducing technologies and product ideas that have gone on to become industry norms for over five decades. From 18 seater to 82 seater double decker buses, from 7.5 tonne to 49 tonne haulage vehicles from numerous special application vehicles to diesel engines for industrial, marine and genset applications, ALL offers a wide range of products. ALL has six manufacturing plants, 50 dealers operating through 133 outlets, 139 authorized service centers and 293 parts distribution networks. The company has vision to be leader in Heavy duty vehicles in next 5 years.



Summary Arguments:

- Supreme court ruling on disallowance of overloading to led significant demand of CV. The additional demand in MHCV would benefit ALL which is second major player.
- Significant fillip to the road development projects, high focus on infrastructure and rise in allocations for NHDP project to fuel demand for tippers and tractor-trailers where ALL is focused.
- Rising export opportunities specially in CNG bus segment to boost top-line. Breakthrough is expected for CNG buses from Bangladesh and Philippines.
- Cost reduction strategy to make the company more competitive and price hikes to absorb cost pressures.
- 100% capacity utilization and increase in CAPEX to help the company to meet future demands.
- New product launches to bolster market share gains.
- Domestic opportunities in CNG buses especially from STUs could give rise to pleasant surprise ahead. ALL expanded its market share in buses from 40.8% in Mar'05 to 47.7% in Mar'06.

(Rs.Millions) Mar -End	2004	2005	2006	2007E	2008E
Net Sales	33,920.19	41,823.78	52,476.57	61,188.92	69,617.69
EBDITA	4,132.24	4,766.05	5,730.44	7,507.27	8,618.72
EBDITA margins(%)	12.18	11.40	10.92	12.27	12.38
PAT	1,935.80	2,714.10	3,273.20	4,320.54	4,991.19
EPS	1.63	2.28	2.68	3.24	3.75
P/E	21.50	15.34	13.06	10.79	9.34
EV/EBDITA	10.49	8.91	7.75	5.70	4.85
MCAP/SALES	1.23	1.00	0.81	0.76	0.67
ROCE(%)	24.33	21.67	24.09	26.71	26.04
RONW(%)	18.99	23.63	21.80	18.25	17.41

Investment Arguments

Supreme court ruling on overloading curbs to led significant demand for CVs:

Supreme court ruling on disallowing overloading of vehicles would led to increase in demand of commercial vehicles in coming days. This ruling is expected to followed stringently as evident by increase in freight rates. CV demand would expect to arise mainly from user industries like cement, steel, etc. to meet their transportation demands.

This will led to one time significant demand of commercial vehicles in next 8-9 months. The additional demand in M&HCV segment would benefit high tonnage vehicles like trailers and multi-axle vehicles where ALL has been focused over the years.

Road Projects To Boost CV Demand:

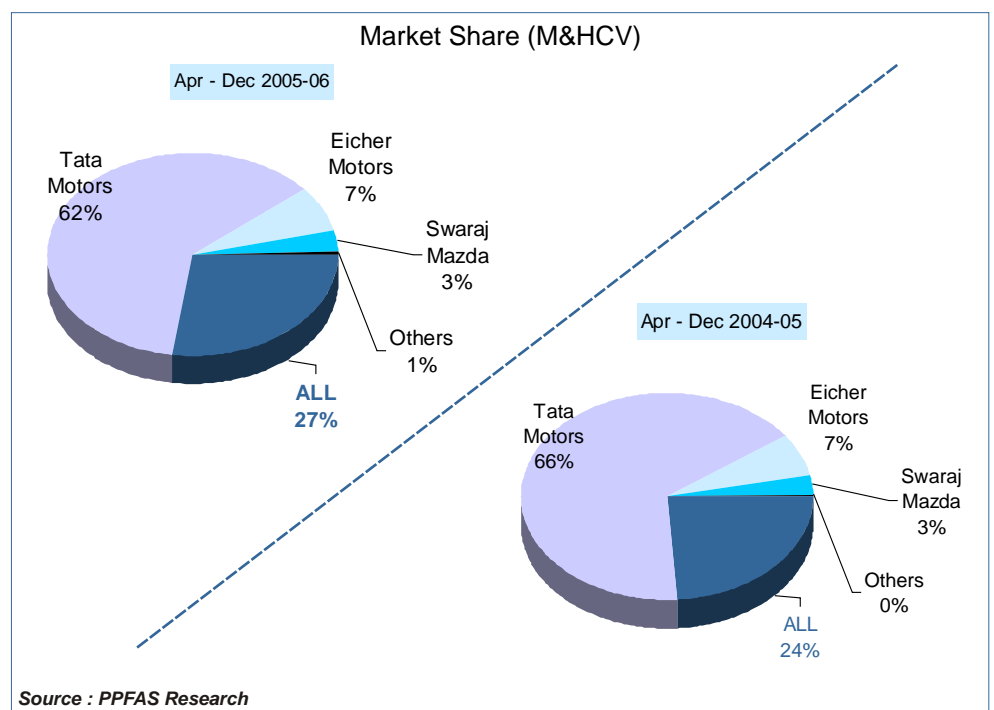
The Union Budget 2006-07 has provided a significant fillip to the roads development, given its higher focus on infrastructure. The rise in allocations for NHDP to the tune of Rs.99.45 bn from Rs. 93.20 bn in 2005-06 and Announcement of six Access Controlled Expressways entailing a total length of 1,000 kms to be implemented on Design, Build, Finance and Operate (DBFO) basis will boost not only this programme but also demand of commercial vehicles. Besides, Demand for CVs is expected to rise as Golden Quadrilateral Project is in its advance stage (84% complete) and NSEW project is around 10% complete. Up to 35% of the target 18,328 km of road development was completed as on 31st December, 2005.

Status of the NHDP as on 31st December, 2005 :

Particulars	Total Length (in kms)	Planned Date of Completion	Completed	Under Implementation	Balance to be Awarded
GQ	5,846	Dec-06	88.0%	12.0%	0.0%
NSEW	7,300	Dec-07	11.0%	34.0%	55.0%
Port connectivity	1,167	Dec-07	33.0%	47.0%	20.0%
Phase III	4,015	Dec-12	0.0%	1.0%	99.0%
Total	18,328		35.0%	20.0%	45.0%

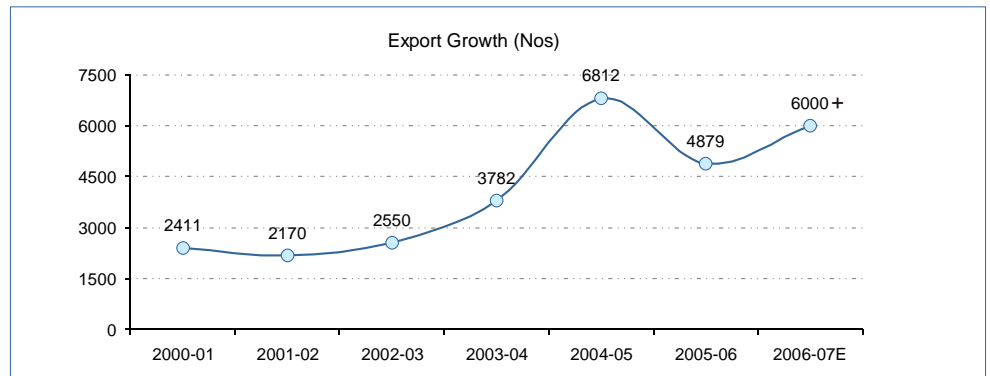
Source : PPFAS Research

ALL is the second largest player in sales of tractor-trailers and is expected to benefit most from the above highway constructions projects.



Rising Export Opportunities:

Excluding last year supplies towards Iraq order, the company expects to sell 6000 plus units in FY07 over 4879 units in FY 06.



The company expects breakthrough in supplies of CNG buses to Bangladesh and Philippines in coming year and is targeting US\$7 mn component exports business to ZF, Germany. ALL exports to over 40 countries, with SAARC, the Middle East and Africa being major markets. It is determined to increase its presence in African markets and wants to focus on emerging markets like Phillipines, Malaysia and Vietnam. ALL also supplies 2000-2500 vehicles per annum to Sri Lanka (its largest export market).

ALL is amongst the leading players in the Middle East. It has 70% market share in the standard bus segment in Dubai. To capitalize on the same, it is setting up an assembly unit in this region with initial capacity of 5000 units per annum. The strategic reason behind setting up assembly unit is primarily to avail tax benefits and other incentives that are available to domestic players. Presently, ALL exports 1000 buses to the middle-east region. The company perceives huge untapped opportunity there. To be closer to its markets and provide local value-addition and service, it has set-up assembly facilities in Sri Lanka, Bangladesh and Egypt. According to management, Middle-East and African markets will be the major drivers for their exports in coming years.

The company perceives Chinese players as a threat after period of three years. ALL is exploring a JV with strategic partner for CVs in order to tap Chinese markets and establish itself as an aggregate supplier of gearboxes, transmissions, engines etc. Being a large supplier to the Indian Army, It plans to reach out to NATO in the medium term as it has a huge cost advantage over competition.

Capex and New Facilities:

ALL had 100% capacity utilization in H1FY06(77,000 units).Due to increasing trend for in-house body-building, company has increased its cabin production to 25,000 units which is mainly required for its 'E-comet' range. Total annual capex for FY06 is Rs.2.4bn. The company spends 1.7-2% of its turnover on R&D.

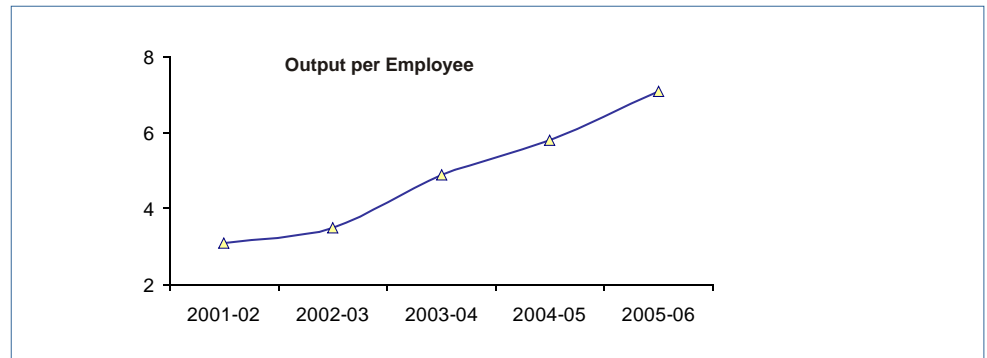
Following initiatives are also being taken:

- Capacity for vehicles to be increased to 1,00,000 units by FY08.
- Capacity for engine/gear box to be raised to 1,00,000 units by FY07.
- Initiatives likes new design office for 400 engineers by the end of H107 would boost product design and engineering.
- Common rail versions of H series engines are under development and would be launched in FY07.
- Introducing modern front axle on all models this year.
- Newgen cab expected to launched by H107.

Cost reduction strategy:

ALL took a price hike of 2% in May'05 to partially meet costs arising out of CMVR regulations followed by another 2.55% hike in Jan'06 and 2.5% hike in April'06. The company aims to bring down its materials cost (as percentage of sales to around 69%) from current levels. A part of saving is expected to come from its e-sourcing strategy, which will become fully operational by H1FY07. The e-sourcing program, when fully implemented, could result in 5% savings in procurement costs. Hike in staff costs of last year have been offset by productivity gains. Also significant cost reduction is expected from shop-floor level employees by introduction of programme known as 'Mission Gemba'.

Productivity Gains



On the other hand, value engineering measures like replacing expensive alloys with ordinary alloys have led to cost savings. Increased in-house manufacturing of engines and gear-boxes and higher localization in axles suppliers have led to cost savings, thus absorbing increase in costs.

New product Launches:

ALL has lined up series of new product launches to augment its product portfolio like mining tippers, CNG BS3, 4921 tractors, rear engine buses on J series, Newgen 4026 J tractors, 44 49 T tractors which would be expected to contribute from H206. It is also expanding its engines in 20HP-500HP range for gensets, industrial and marine applications.

ALL uses the H series engine as the key engine platform for its 16-40T segment. For higher tonnage it uses HINO J- Series engine and the ZF Steering 9 speed gearbox. The expected launch of Newgen range of trucks in Q1FY07, fitted with J-series 260HP engines from Japan's HINO Motors would help it regain market share in the high-end segment. ALL has 85% of its engines on the HINO platform, which is expected to go 100% next year.

Also, ALL is planning to launch its luxury bus - 'Inter Century Luxura' by Q3FY07. According to management, the company is well-positioned to price it competitively against major players like VOLVO and TATA. The new bus meets all latest norms and will help ALL to retain market share (if not gain) in growing Passenger Vehicle Segment. Also In-roads to Defense markets with new application such as TFF, LRV and Water Bowzers and Fully built vehicles with high realisations and margins are on the anvil.

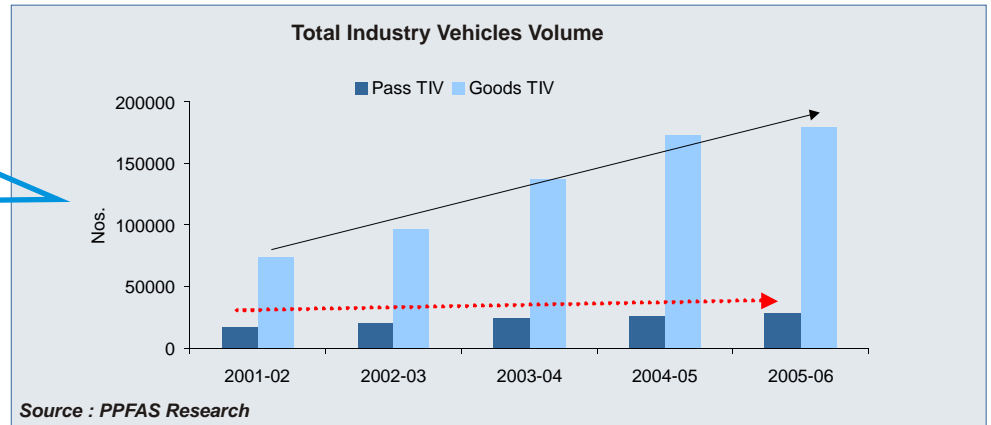
New Launches are:

49T High Power Tractor	4026J Tractor
31T High Power 3126J 8X4 tipper 260HP	1613H Luxliner bus- 12metre 260 HP
16T Semi Fwd Control tipper	4018H Stag CNG bus, H series, 85HP , 28 seater
15T Truck with H series 4 cycle engine	260 HP Megabus
25T High Performance Mining Tipper	12 m Rear Engine Luxury Coach
HMV 6X6 J,260HP for Defense	12m Low- floor buses
3014H Ecomet 1109	ABS Safety system on trucks and MAVs
2516H Ecomet 912	

Domestic opportunities in CNG buses:

The company after bagging BEST order to supply 667 buses, is looking at further opportunities for CNG buses in Gujarat (1,000 plus units), Tamil Nadu (1200 units) and Karnataka (1000 units). In spite of share of State Transport Units in passenger vehicles are sliding down, they are still huge customers given potential for fleet replacement.

The chart reveals stagnant growth in passenger vehicles over the years as compared to goods vehicles. This signifies growing untapped opportunities in Bus segment..



The company has increased its market share in buses from 40.8% in Mar'05 to 47.7% in Mar'06. Increasing judicial activism regarding pollution, emission norms and improved urban road infrastructure could increase domestic opportunities ahead by boosting fleet addition by private transporters as well.

Valuations

The stock is trading presently at 9.34 X EPS FY08E, 4.85 X EV/ EBDITA FY08E and 1.63 X P/B FY08E.

We envisage the following risk factors:

- ALL's product profile is loaded with only MHCVs which makes it vulnerable to cyclical trends in CV
- Its volume growth may get hurt in case of any recurrence of labour problems
- Higher commodity prices and fuel prices could affect the performance
- Increasing competition from new players like MAN, International Truck and M&M pose a risk to the company's market share

Despite these, taking into account several positives such as expected rise in demand of CV with overall boost to highway projects, rising export opportunities, expected growth in bus segment and expansion of 'E-comet' and 'Newgen' range, we estimate that ALL will witness top-line growth of CAGR 15% over 2006-08. The story becomes stronger with Management plans to enter into the LCV business by acquiring businesses abroad. Also technology and market expansion by sale of the IVECO stake can turn out to be a big trigger.

We recommend 'BUY'.

Financials

P & L AC (Rs mn)	2005	2006	2007E	2008E
SALES	48,112.8	60,531.1	70,575.5	80,297.2
EXCISE	6,289.0	8,054.5	9,386.5	10,679.5
NET SALES	41,823.8	52,476.6	61,188.9	69,617.7
RAW MATERIAL COST	30,524.8	39,739.5	-	-
ADJ MATERIAL COST	30,445.4	37,690.0	42,832.2	48,732.4
EMPL COST	3,540.5	4,038.9	5,507.0	6,265.6
OTHERS	3,609.4	5,347.0	5,507.0	6,265.6
TOTAL MFG COST	37,595.3	47,075.9	53,846.2	61,263.6
OPERATING PROFIT	4,228.5	5,400.7	7,342.7	8,354.1
OTHER INCOME	537.6	329.7	164.6	264.6
PBDIT	4,766.1	5,730.4	7,507.3	8,618.7
INTEREST	28.0	164.5	110.1	110.1
PBDT	4,738.1	5,565.9	7,397.2	8,508.6
DEPRECIATION	1,092.1	1,260.1	1,396.4	1,576.4
PBT	3,645.9	4,305.9	6,000.8	6,932.2
EXCEPTIONAL ITEMS	95.8	217.2	-	-
TAX *	836.0	1,249.8	1,680.2	1,941.0
PAT	2,714.1	3,273.2	4,320.5	4,991.2

RATIOS:	2005	2006	2007E	2008E
PBDIT%	11.40	10.92	12.27	12.38
PBT%	8.72	8.21	9.81	9.96
NPM%	6.49	6.24	7.06	7.17
INTEREST COVER	131.30	27.17	55.52	63.98
RONW%	23.63	21.80	18.25	17.41
ROCE%	21.67	24.09	26.71	26.04
INV DAYS	49.58	51.10	51.10	51.10
DEBTOR DAYS	34.80	34.81	34.81	34.81
DEBT/EQUITY	0.77	0.58	0.19	0.15
CREDITOR DAYS	114.93	101.22	109.50	109.50
EPS	2.28	2.68	3.24	3.75
P/E	15.34	13.06	10.79	9.34
PRICE/BV	3.62	2.85	1.97	1.63
BV	9.66	12.29	17.78	21.53
MARKET CAP (Rs Mn)	41625.15	42755.65	46604.25	46603.90
MCAP/SALES	1.00	0.81	0.76	0.67
EV (Rs mn)	42462.39	44419.27	42782.82	41770.31
EV/EBDITA (x)	8.91	7.75	5.70	4.85
EV/Sales (x)	1.02	0.85	0.70	0.60

BALANCE SHEET (Rs Mn)	2005	2006	2007E	2008E
EQUITY	1,189.3	1,221.6	1,331.6	1,331.5
RESERVES	10,489.4	13,794.9	22,347.6	27,338.8
MISC EXP ETC	193.3	-	-	-
ACTUAL RESERVES	10,296.0	13,794.9	22,347.6	27,338.8
NET WORTH	11,485.3	15,016.4	23,679.2	28,670.4
DEBENTURES	1,663.3	1,663.3	-	-
TERM LOANS	971.6	971.6	-	-
SECURED LOANS	2,635.0	2,635.0	2,635.0	2,635.0
UNSECURED LOANS	1,794.6	1,794.6	1,794.6	1,794.6
FCCN	4,374.5	4,342.2	-	-
TOTAL DEBT	8,804.1	8,771.8	4,429.6	4,429.6
DEF. TAX LIABILITY (NET)	1,708.5	-	-	-
TOTAL LIABILITIES	21,997.9	23,788.2	28,108.7	33,099.9
GROSS BLOCK	20,022.5	20,874.1	23,274.1	26,274.1
ACC DEPRECIATION	11,084.0	12,344.1	13,740.5	15,317.0
NET BLOCK	8,938.5	8,530.0	9,533.5	10,957.1
CWIP	851.6	2,400.0	3,000.0	3,000.0
FIXED ASSETS	9,790.0	10,930.0	12,533.5	13,957.1
INVESTMENTS	2,291.9	2,291.9	3,291.9	5,291.9
WORKING CAPITAL				
INVENTORIES	5,680.8	7,346.7	8,566.4	9,746.5
DEBTORS	4,587.7	5,772.4	6,730.8	7,657.9
CASH/BANK	7,966.8	7,108.2	8,251.0	9,263.2
LOANS & ADVANCES	3,337.3	3,673.4	4,283.2	4,873.2
CURRENT ASSETS	21,572.6	23,900.7	27,831.4	31,540.8
LIABILITIES	9,611.9	11,020.1	12,849.7	14,619.7
PROVISIONS	2,044.8	2,314.2	2,698.4	3,070.1
CURRENT LIABILITIES	11,656.7	13,334.3	15,548.1	17,689.9
NET WORKING CAPITAL	9,916.0	10,566.4	12,283.3	13,851.0
TOTAL ASSETS	21,997.9	23,788.2	28,108.7	33,099.9

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