

## Driving in the fast lane

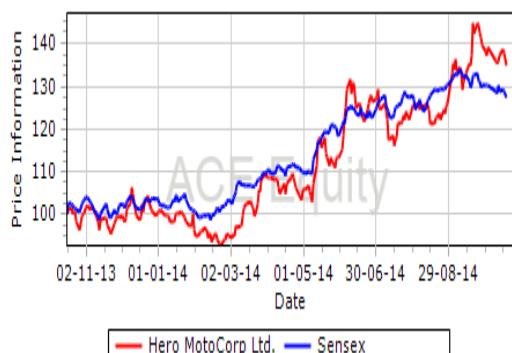
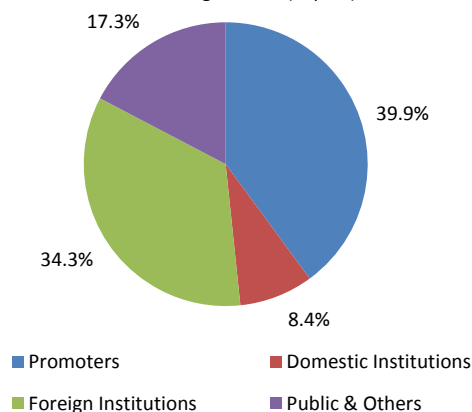
17<sup>th</sup> Oct, 2014

CMP: Rs 2,877  
Target Price: Rs 2,970  
**Recommendation: Neutral**

Stock Info	
BSE Group	A
BSE Code	500182
NSE Symbol	HEROMOTOCO
Bloomberg	HMCL IN
Reuters	HROM.BO
BSE Sensex	26,109
NSE Nifty	7,780

Market Info	
Market Capital	Rs 57,452 cr
Equity Capital	Rs 39.9 cr
Avg Trading Volume	3,95,930
52 Wk High / low	Rs 3,080/1,907
Face Value	Rs 2

Latest Shareholding Pattern (Sep'14)



Hero Motocorp net sales grew by 20.5% YoY to Rs 6,864 cr, on strong volume growth of 19.5%. However, realizations grew by only 0.8%. Volume growth was largely driven by strong motorcycle growth of 20.4%, while scooter segment grew at a slower pace of 13.1%.

EBITDA margins declined by 102 bps to 13.5% on YoY basis as competitive pressures restricted significant price hikes. However, PAT grew by a whopping 58.6% YoY to Rs 763 crs. PAT growth was due to expiry of fixed royalty payment to Honda motors and significant increase in other income.

### Other highlights

- HMCL market share stood at 39.6% in Q2FY15 which is loss of 290 bps sequentially.
- 125cc segment grew by 21.1% which signifies good replacement demand.
- Recently launched Splendor iSmart, variants of Pleasure and Karizma have received encouraging response.
- Company has lined up 10 new launches in coming few months out of which 2 will be in scooter segment while the rest will be in motorcycle segment.
- Expects double digit growth during the festive season.
- Increased product prices by modest Rs 200 per unit in October 2014.

> **OUTLOOK FOR NEXT 2 YEARS:** We remain optimistic on HMCL's domestic business outlook over FY15, due to expected revival of domestic economy. With two new launches (110cc scooter, 250cc premium motorcycle) we expect HMCL to prove its capabilities.

> **FINANCIALS, ESTIMATES & VALUATION:** We estimate Hero Moto's Revenue growth at a 2 year CAGR of 16%, expect EBITDA margins close to 15.5% and expect PAT growth at a 2 year CAGR of 25%.

> **Valuation:** The stock at Rs 2,877 trades at 17.4x our estimated FY16 EPS of Rs 165 per share. We assign a price target of Rs 2,970 at 18x FY16 EPS, and have "Neutral" rating on the stock.

Y/E March, (in Rs crore)	FY13	FY14	FY15E	FY16E
Net Sales	23,583	25,125	28,882	33,813
yoy%	0.9%	6.5%	15.0%	17.1%
Operating EBITDA	3,284	3,540	4,491	5,326
Operating EBITDA %	13.8%	14.0%	15.5%	15.7%
PAT	2,118	2,109	2,781	3,295
yoy%	-10.9%	-0.4%	31.9%	18.5%
EPS	106.1	105.6	139.3	165.0
P/E (x)	27.1	27.2	20.7	17.4

Source: Company data, Aриhant Research

Quarterly P&L in Rs cr	Q2FY15	Q2FY14	yoy%	Q1FY15	qoq%
Volumes (in numbers)	16,92,523	14,16,276	19.5%	17,15,254	-1.3%
Net Realization per unit	40,552	40,221	0.8%	40,807	-0.6%
Net Sales	6,864	5,696	20.5%	6,999	-1.9%
Other Operating Income	52	30		37	
Income from Operations	6,915	5,726	20.8%	7,037	-1.7%
Materials Consumed	4,971	4,096	21.4%	5,111	-2.7%
Employees Cost	285	229		268	
Other Expenditure	725	569		711	
Total Expenditure	5,981	4,894	22.2%	6,090	-1.8%
Operating EBITDA	935	833	12.3%	947	-1.3%
margin	13.5%	14.5%		13.5%	
Core EBITDA	883	803	10.0%	910	-2.9%
margin	12.9%	14.1%		13.0%	
Depreciation and Amortization	75	287	-73.9%	292	-74.3%
Operating EBIT before Other Income & Excp Items	860	546	57.5%	656	31.1%
Other Income	194	115		113	
Interest	4.94	2.96		3	
PBT before Exceptional Items	1,048	658	59.3%	765	37.0%
Exceptional item	0	0		0	
PBT	1,048	658	59.3%	765	37.0%
Tax Expense	285	177		203	
Effective Tax Rate	27.2%	26.9%		26.5%	
Net Profit after Tax	763	481	58.6%	563	35.6%
EPS	38.2	24.1		28.2	

Source: Company data, Arihant Research

## Profit and Loss Account, Year Ending March

Particulars, in Rs crore	FY13	FY14	FY15 E	FY16 E
<b>Net Sales</b>	<b>23,583</b>	<b>25,125</b>	<b>28,882</b>	<b>33,813</b>
YoY%	0.9	6.5	15.0	17.1
Other Operating Income	185	151	144	169
<b>Income from Operations</b>	<b>23,768</b>	<b>25,275</b>	<b>29,027</b>	<b>33,982</b>
Materials Consumed	17,398	18,230	20,507	24,007
Total Expenditure	20,484	21,735	24,536	28,657
<b>Operating EBITDA</b>	<b>3,284</b>	<b>3,540</b>	<b>4,491</b>	<b>5,326</b>
Operating EBITDA margin %	13.9	14.1	15.6	15.8
Depreciation	1,142	1,107	1,159	1,407
Operating EBIT	2,143	2,433	3,332	3,918.9
Other Income	398	446	465	578
Interest	12	12	13	14
<b>PBT</b>	<b>2,529</b>	<b>2,867</b>	<b>3,784</b>	<b>4,483</b>
Tax Expense	411	758	1,003	1,188
<b>Reported Net Profit</b>	<b>2,118</b>	<b>2,109</b>	<b>2,781</b>	<b>3,295</b>
YoY%	(10.9)	(0.4)	31.9	18.5
Effective Tax Rate	16.3	26.4	26.5	26.5
<b>Reported EPS</b>	<b>106</b>	<b>106</b>	<b>139</b>	<b>165</b>

## Balance Sheet, Year Ending March

Particulars, in Rs crore	FY13	FY14	FY15 E	FY16 E
<b>Liabilities + Equity</b>				
(a) Share capital	40	40	40	40
(b) Reserves and surplus	4,966	5,560	6,664	8,161
<b>Shareholders' funds</b>	<b>5,006</b>	<b>5,600</b>	<b>6,704</b>	<b>8,201</b>
Non-current liab & Prov	465	74	74	74
Current liabilities	4,171	4,423	4,865	5,352
<b>Total - Equity and liabilities</b>	<b>9,642</b>	<b>10,097</b>	<b>11,643</b>	<b>13,628</b>
<b>Assets</b>				
Non-current assets				
Fixed assets	3,133	3,097	3,252	3,415
Long Term Inv	651	861	861	861
Loans + Adv + Others	780	583	679	793
Non-current assets	4,564	4,541	4,792	5,069
Current assets				
Cash	181	118	326	727
Other Current Assets	4,897	5,438	6,526	7,831
Sub-total - Current assets	5,078	5,556	6,852	8,559
<b>Total - Assets</b>	<b>9,642</b>	<b>10,097</b>	<b>11,643</b>	<b>13,628</b>

## Cash Flow Statement, Year Ending March

Particulars, in Rs crore	FY13	FY14	FY15 E	FY16 E
Operating Activities				
<b>PBT</b>	<b>2,529</b>	<b>2,867</b>	<b>3,784</b>	<b>4,483</b>
Add Depr + non op exp	1,142	1,107	1,159	1,407
Others	(837)	79	-	-
Total	2,834	4,054	4,943	5,889
Cash Taxes	(613)	(649)	(1,003)	(1,188)
Changes in Working Cap	(331)	(441)	(645)	(819)
<b>Cash Flow from Operations</b>	<b>1,890</b>	<b>2,963</b>	<b>3,295</b>	<b>3,883</b>
Investing Activities				
Change in investments	(133)	(687)	(755)	(1,021)
Capex	(600)	(933)	(655)	(663)
<b>Cash Flow from Investing</b>	<b>(733)</b>	<b>(1,619)</b>	<b>(1,410)</b>	<b>(1,684)</b>
Financing Activities				
<b>Dividends + Taxes paid</b>	<b>(1,044)</b>	<b>(1,403)</b>	<b>(1,677)</b>	<b>(1,797)</b>
Change in Non Curr Liab	(11.9)	(11.8)	-	-
<b>Cash Flow from Financing</b>	<b>(1,056)</b>	<b>(1,415)</b>	<b>(1,677)</b>	<b>(1,797)</b>
Opening Cash	79.8	188.3	117.5	325.6
Changes during year	101.2	(70.8)	208.1	401.8
<b>Closing Cash</b>	<b>181.0</b>	<b>117.5</b>	<b>325.6</b>	<b>727.4</b>

## Ratio Analysis

	FY13	FY14	FY15 E	FY16 E
<b>Profitability</b>				
<b>Operating EBITDA%</b>	<b>13.8</b>	<b>14.0</b>	<b>15.5</b>	<b>15.7</b>
Core EBITDA%	13.1	13.5	15.1	15.3
PAT%	9.0	8.4	9.6	9.7
<b>ROAE%</b>	<b>45.6</b>	<b>39.8</b>	<b>45.2</b>	<b>44.2</b>
Du Pont ROAE breakup				
PAT / Sales	8.9	8.3	9.6	9.7
Sales / Avg Total Assets	2.4	2.6	2.7	2.7
Avg Total Assets / Avg Eqty	2.1	1.9	1.8	1.7
<b>ROE</b>	<b>45.6</b>	<b>39.8</b>	<b>45.2</b>	<b>44.2</b>
Other Ratios				
<b>Current Ratio</b>	<b>1.2</b>	<b>1.3</b>	<b>1.4</b>	<b>1.6</b>
Long Term Debt / Equity	0.09	0.01	0.01	0.01
<b>EPS</b>	<b>106.1</b>	<b>105.6</b>	<b>139.3</b>	<b>165.0</b>
DPS	60.0	65.0	70.0	75.0
<b>Dividend Payout ratio</b>	<b>56.6</b>	<b>61.5</b>	<b>50.3</b>	<b>45.5</b>
<b>P/E</b>	<b>27.1</b>	<b>27.2</b>	<b>20.7</b>	<b>17.4</b>
BVPS	250.7	280.4	335.7	410.7
P/BV	11.5	10.3	8.6	7.0

Source: Company data, Arian Research

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**Stock Rating**

	Absolute Return
Buy	> 20%
Accumulate	12% to 20%
Hold	5% to 12%
Neutral	-5% to 5%
Reduce	< -5%

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