

Above estimate: Structural Growth Drivers Remain Intact

CMP: INR 2,683

Rating: Buy

Target Price: INR 3,414

Stock Info

BSE	500182
NSE	HEROMOTCO
Bloomberg	HMCL IN
Reuters	HROM.BO
Sector	Auto-2&3 wheelers
Face Value (INR)	2
Equity Capital (INR mn)	400
Mkt Cap (INR mn)	539,894
52w H/L (INR)	3,629/2,636
Avg Yearly Vol (in 000')	914

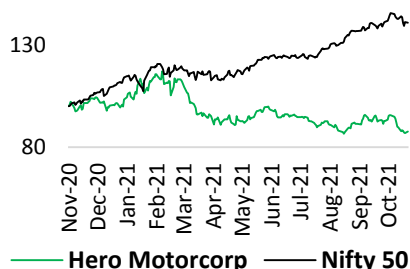
Shareholding Pattern %

(As on September, 2021)

Promoters	34.76
FII	42.23
DII	9.02
Public	10.99

Stock Performance (%)	1m	3m	12m
Hero MotoCorp	-5.35	-2.75	-11.61
Nifty	-0.52	9.65	40.04

Hero MotoCorp Vs Nifty



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- Hero MotoCorp (HMCL) declared results above estimates on all fronts in Q2FY22.
- Standalone revenue from operations grew by 54.1% QoQ/ -9.8% YoY stood at INR 84,534 Mn in Q2 FY22 against our estimate of INR 78,686 Mn.
- EBITDA grew by 107.1%QoQ/-17.1%YoY to INR 10,664 Mn against our estimate of INR 8,630 Mn.
- EBITDA margin expanded by 323bps QoQ/ contracted 112bps YoY to 12.6% Q2FY22 vs our estimate of 11%.
- The Company reported net Profit of INR 7,944 Mn in Q2FY22 against our estimate of INR 6,317 Mn, grew by 117.4% QoQ/-16.7% YoY.
- Basic EPS at INR 39.8 in Q2FY22 as against INR 47.7 in Q2FY21 (Q1FY22 was INR 18.3)
- The total volumes (Motorcycles + Scooters) de-grew by 21% YoY to 14,38,623 units. The blended realization has seen an increase of 14.2% YoY/9.7% QoQ to INR 58,760 unit on account of better product mix.

Business Highlights

- **Global Business:** Annual run rate of 300,000-unit crossed vs 200,000-units for quite a few years. The revised GV strategy doing very well and it will be a key growth driver in the future.
- **Parts Business:** Parts merchandise business has crossed 11,410 mn revenue which is registering 40% YoY growth which accounts for <13% of total revenue. As per the past merchandise performance, it will be going to perform well.

Outlook and valuation

HMCL has witnessed demand recovery during the quarter on account of the festive induced tailwinds and also we are expecting strong demand due to the ongoing marriage sessions.

At CMP of INR 2,683, Hero MotoCorp is trading at PE of 12.6x, to its FY24E EPS of INR 213.4. The company under the LEAP-2 program has been aggressive in cost-saving, operating leverage benefits, and price hikes which would result in margin improvement. Secondly, Hero will benefit from its premium bikes, strong support in the economy, executive motorcycle segments, aggressive product offerings in the premium bikes and scooters segments. The EV segment is likely to do well for growth in the medium term.

We value Hero MotoCorp at PE of 15x to its FY24E EPS estimate of INR 213.4, which yields a target price of INR 3,414. We assign a Buy rating on the stock.

YE March (INR Mn)	Net Sales	EBITDA	PAT	EPS (INR)	EBITDA Margin %	RoE (%)	P/E (x)
FY20	2,88,361	39,580	36,333	181.9	13.7	26.9	14.8
FY21	3,08,006	40,192	29,642	148.4	13.0	20.2	18.1
FY22E	3,57,007	45,845	33,484	167.6	12.8	21.2	16.0
FY23E	4,06,876	53,906	39,209	196.2	13.2	22.6	13.7
FY24E	4,40,091	58,375	42,630	213.4	13.3	22.0	12.6

Source: Arihant Research, Company Filings, Ace Equity, Bloomberg

Conference call Highlights

- **Product Launches:** Recently launched, Xtreme 160, XPulse 200 and it will continue more action in this segment as per the part of the premium strategy. The main focus is premiumization. Glamour Xtec was launched more than 4500 price premium and more than 50% demand in the glamour segment. In the scooter, segment launch Connect in Pleasure Plus XTEC to have the premiumization to a key theme within the segment.
- **EV Launch:** Hero MotoCorp gears up to launch its EV by march'22 to be manufactured at its plant in Chittoor, India. The product is designed in Jaipur, tech in Germany. The plant - aptly called Garden Factory for its eco-friendly and sustainable manufacturing practices will provide an integrated ecosystem for Battery Pack Manufacturing and Testing, Vehicle Assembly, and Vehicle End of Line Testing (EOL).
- **EV& Battery:** As the product is going to launch in March and keep going in every year. The company is in manufacturing and will provide eco-battery it will come from the various provider. EV success: It will require focus on the customer, on cost, on collaboration, and not necessarily on the competition. Commodity Prices, which have been impacting the industry margins so far, are showing some signs of softening as the company move from here. Through an accelerated Leap-II savings program, overheads management, and judicious price increases, the company has been able to improve margins sequentially and expect further recovery moving forward.
- **Festive season:** Overall it was subdued however the 2nd half improved much better because rural over urban this time it lagged due to crop is still in the field but in the Punjab and Rajasthan crop it has reached to Mandi and seen better traction. Post festive: Urban remains on the same level but the rural is rated. Marriage session: Semi-urban and rural positive after the harvest happens rabbi corp.
- **Price increases:** The company took price increase in Apr-July-Sept ~3k price increase in this year and net saving on the cost of material by 110 bps point as margin also improved QoQ basis. Some of the commodities seen to be cooling off, the raw material too, and the management expected to commodity spectrum to be cooling off going forward. In Q2FY22 21st Sept and INR 1000 - July INR 1200 FY21.
- **Inventory:** In the range of 5-6 weeks Inventory level and going forward will maintain the inventory level.
- **Entry level segment:** De-growth level comparatively high. Launched the HF100 to people coming up more on lower price as well. If the financing penetration increase more on an EMI basis so down payment needs to do which is get impacted. Gradually, the consumer realizes the re-sell price also needs to go up, which will take care of the upfront finance penetration also benefit from the price increase. Now people are more focused on not conserving the money but spending on the need they have for mobility.
- **Retail finance:** Increase penetration for the consumer who does not have the banking habits with the launch by HFCL and bullet payment for the farmer.
- **Other operating income:** for the Q2FY22 2230 Mn vs 8870 Mn Q2FY21 for the last quarter 1100Mn. Primarily linked to the production facility.
- **EV scooter strategy:** Customer cost and collaboration: 1) charging basis, 2) Swapping basis convenient range, Cost eliminate, Exiting manufacturing and Distribution location, 3) collaboration, the company will more focus on the collaboration basis.
- **Tech Part of the EV:** Data will control by the company. The co- have 100 mn customer it's a high number of the customer that the hero has. Therefore, that gives an advantage to the Hero MotoCorp.
- **LEAP II:** On the YoY basis the company has saved to 320bps lead as the company continues to work on the LEAP II saving and seeing good traction in coming quarters.

Quarterly result summary

Standalone (INR mn)	2QFY22	1QFY22	2QFY21	YoY (%)	QoQ (%)
Net sales	84,534	54,871	93,673	(9.8)	54.1
- Raw material	61,104	39,796	66,600	(8.3)	53.5
(% of net sales)	72.3	72.5	71.1	119bps	-24bps
Gross Profit	23430.4	15074.6	27073.9	(13.5)	55.4
(% of net sales)	27.7%	27.5%	28.9%	-1bps	0bps
- Staff expenditure	5,054	4,357	5,112	(1.1)	16.0
(% of net sales)	6.0	7.9	5.5	52bps	-196bps
- Other expenditure	7,712	5,570	9,097	(15.2)	38.5
(% of net sales)	9.1	10.2	9.7	-59bps	-103bps
Total expenditure	73,870	49,722	80,809	(8.6)	48.6
EBITDA	10,664	5,148	12,864	(17.1)	107.1
EBITDA Margin (%)	12.6	9.4	13.7	-112bps	323bps
Depreciation	1,639	1,630	1,732	(5.4)	0.5
EBIT	9,025	3,519	11,133	(18.9)	156.5
Interest	65	61	46	40.9	7.4
Other Income	1,569	1,386	1,413	11.0	13.2
PBT	10,529	4,844	12,500	(15.8)	117.4
Tax	2,585	1,189	2,965	(12.8)	117.4
Reported PAT	7,944	3,654	9,534	(16.7)	117.4
Adjusted PAT	7,944	3,654	9,534	(16.7)	117.4
Adjusted EPS (INR)	39.8	18.3	47.7	(16.7)	117.4
Total volumes (Nos)	14,38,623	10,24,489	18,20,278	(21.0)	40.4
Net realisation (INR)	58,760	53,559	51,461	14.2	9.7
EBITDA / vehicle (INR)	7,412	5,025	7,067	4.9	47.5

Other Highlights:

- **Exports business:** 300,000 run rate. Mexico tied up expect to do very well and Bangladesh started recovery and Nigeria modified & customized product and Colombia giving good response on the X plus in the premium segment and soon on the break-even on the EBITDA level. Sri Lanka is there has been no sales due to the ban on import on the ban and expected to resolve in the next 6 months. From the 7-8 countries is the positive market share. Headwinds of Export: EBITDA margin lower than the domestic as launching in Nigeria and some of the other markets it is lower than that but moving forward as scale-up and will add more premium product in the export market. Going forward the EBITDA margin will be higher than the domestic market. There is an opportunity for the gross margin as well.
- **Key Risk:** If there will be a 3rd Covid wave.
- **Motorcycle Vs scooter:** In the 2W motorcycle market 70% and scooter is 30% availability. They come around from exiting scooter customer inquiry and overall EV is >1%. as per the demand perspective, there is not much on the EV. 2W % in Q2FY22 is more than Q1.
- **2W Demand:** The 2W CAGR is going back to the industry level. Fundamental is intact and penetration remains on that level. Going forward in Q4FY22 there will be good demand but for the same level of demand as compared to FY19 still need to wait 2-3 years. The 55% clear departure keeps going up and another 1-2% add in festive session. A lot of financial innovation, the segment of the consumer HFCL very proactive.
- **Capex for EV segment:** Overall is in an investment of 5-7 years' brand building 100,000 mn out of that, 50% of in EV and spending will be based on the requirement.
- **Hero Fincorp:** 35-40% share of financing at a solid level and few bps points changes in QoQ.

Profit & Loss Statement				
YE: Mar (INR mn)	FY21	FY22E	FY23E	FY24E
Net sales	3,08,006	3,57,007	4,06,876	4,40,091
Growth, %	7	16	14	8
RM expenses	-2,17,623	-2,53,832	-2,88,882	-3,12,465
Employee expenses	-18,987	-19,635	-20,751	-22,445
Other expenses	-31,203	-37,695	-43,338	-46,807
EBITDA	40,192	45,845	53,906	58,375
Growth, %	2	14	18	8
Margin, %	13.0	12.8	13.2	13.3
Depreciation	-6,769	-6,940	-7,882	-8,362
EBIT	33,424	38,905	46,023	50,012
Growth, %	6	16	18	9
Margin, %	10.9	10.9	11.3	11.4
Interest paid	-218	-229	-241	-253
Other Income	5,799	6,088	6,636	7,234
Non-recurring Items	0	0	0	0
Pre-tax profit	39,004	44,764	52,419	56,993
Tax provided	-9,362	-11,281	-13,210	-14,363
Profit after tax	29,642	33,484	39,209	42,630
Others (Minorities, Associates)	-	-	-	-
Net Profit	29,642	33,484	39,209	42,630
Growth, %	-18	13	17	9
Net Profit (adjusted)	29,642	33,484	39,209	42,630

Cash Flow				
YE: Mar (INR mn)	FY21	FY22E	FY23E	FY24E
Pre-tax profit	39,004	44,764	52,420	56,995
Depreciation	6,769	6,940	7,882	8,362
Chg in working capital	10,486	1,180	1,639	1,373
Total tax paid	-9,362	-11,281	-13,210	-14,363
CFO	41,316	35,744	42,336	45,386
Capital expenditure	-7,351	-9,824	-10,000	-10,000
Chg in investments	-22,770	-10,500	-11,550	-12,705
Other investing activities	5,799	6,088	6,636	7,234
CFI	-24,322	-14,235	-14,913	-15,471
Free cash flow	11,195	15,421	20,786	22,682
Debt raised/(repaid)	0	0	0	0
Dividend (incl. tax)	-16,364	-21,039	-21,039	-21,039
CCF	-16,582	-21,268	-21,280	-21,292
Net chg in cash	412	241	6,143	8,624
Opening cash balance	2,419	2,725	2,965	9,108
Closing cash balance	2,725	2,965	9,108	17,732

Source: Arihant Research, Company Filings, Ace Equity, Bloomberg

Balance Sheet				
YE: Mar (INR mn)	FY21	FY22E	FY23E	FY24E
Cash & bank	2,725	2,965	9,108	17,732
Marketable securities				
cost	93,902	1,03,293	1,13,622	1,24,984
Debtors	24,268	29,343	33,442	36,172
Inventory	14,696	17,033	19,413	20,998
Loans & advances	892	1,040	1,184	1,280
Other current assets	5,709	6,280	6,908	7,599
Total current assets	48,288	56,662	70,054	83,780
Investments	11,094	12,204	13,424	14,766
Gross fixed assets	1,49,322	1,59,322	1,69,322	1,79,322
Less: Depreciation	-87,841	-94,781	-1,02,664	-1,11,026
Add: Capital WIP	1,779	1,603	1,603	1,603
Net fixed assets	61,480	64,541	66,658	68,296
Total assets	2,16,438	2,38,195	2,65,255	2,93,323
Current liabilities	61,803	66,273	74,754	80,801
Provisions	3,328	8,170	8,579	9,007
Total current liabilities	65,131	74,443	83,332	89,808
Non-current liabilities	-677	-677	-677	-677
Total liabilities	64,454	73,766	82,655	89,131
Paid-up capital	399.6	399.6	399.6	399.6
Reserves & surplus	1,51,585	1,64,029	1,82,200	2,03,793
Shareholders' equity	1,51,984	1,64,429	1,82,600	2,04,192
Total equity & liabilities	2,16,438	2,38,195	2,65,255	2,93,323

Ratios				
YE: Mar	FY21	FY22E	FY23E	FY24E
EPS (INR)	148	168	196	213
PER (x)	18.1	16.0	13.7	12.6
Price/Book (x)	3.5	3.3	2.9	2.6
EV/EBITDA (x)	10.9	9.4	7.7	6.7
EV/Net sales (x)	1.4	1.2	1.0	0.9
RoE (%)	20.2	21.2	22.6	22.0
RoCE (%)	26.9	28.6	30.5	29.7
Fixed Asset turnover (x)	2.1	2.2	2.4	2.5
Dividend Yield (%)	2.6	3.4	3.4	3.4
Receivable (days)	29	30	30	30
Inventory (days)	20	20	20	20
Payable (days)	71	65	65	65
Net D/E ratio (x)	(0.6)	(0.6)	(0.7)	(0.7)

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Stock Rating Scale	Absolute Return
BUY	>20%
ACCUMULATE	12% to 20%
HOLD	5% to 12%
NEUTRAL	-5% to 5%
REDUCE	-5% to -12%
SELL	<-12%

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