

CMP: INR 2,589

Rating: Buy

Target Price: INR 3,437

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)	399.6
Mkt Cap (INR mn)	528,389
52w H/L (INR)	2,906/2,148
Avg Yearly Vol (in 000')	622

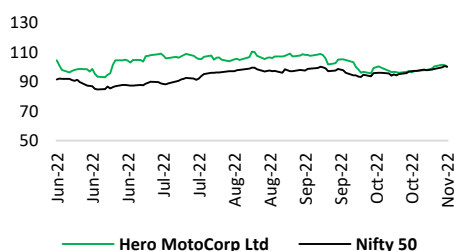
Shareholding Pattern %

(As on June, 2022)

Promoters	34.78
FII	42.92
DII	11.50
Public	10.80

Stock Performance (%)	1m	3m	12m
Hero MotoCorp	4.7	-5.6	0.1
Nifty	6.8	3.8	1.2

Hero MotoCorp Vs Nifty



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Revenue significant improvement on a sequential basis: Standalone revenue stood at INR 90,754 Mn, against our estimate of INR 87,070 Mn registering 8.1% QoQ/7.4% YoY. The company, reinforced the focus on both revenues as well as profitability. The total volumes (Motorcycles + Scooters) grew by 2.7% QoQ/-0.7% YoY to 1,428,168 units. Realizations grew 8.1% YoY/5.3% QoQ led by improved product mix, price hikes, and higher spare parts revenue. The company EBITDA per Vehicle increased by 7.4% QoQ/-1.9% YoY of INR 7,270 against INR 6,767 in Q1FY23.

Maintained its EBITDA Margin on QoQ: EBITDA stood at INR 10,383 Mn, against our estimate of INR 10,575 Mn, Registering a growth of 10.4%QoQ/-2.6%YoY. On the margins front, EBITDA margin expanded by 23 bps QoQ/ -117bps YoY to 11.4%, against our estimate of 12.1%. Reinforcing the focus on both revenues as well as profitability.

Focus on the Premiumisation: Recent festive season: ~32 days. Hero was close to understanding the trends and sentiments of consumers and dealers. The trend is moving towards premiumization. The company has prioritized the xTech range of vehicles. (Premium variants of Destiny, Passion, Glamour). Rural, in July and August, was a little soft. However, Sept onwards it picked up. The company witnessed pent-up demand. However, in the last 6 days (Dussehra to Diwali), volumes picked up and grew 20% YoY (consumer retails) compared to the last festive period.

Outlook and valuation

At the CMP of INR 2,589, Hero MotoCorp is trading at a PE of 12.7x, its FY24E EPS of INR 203. HMCL has maintained its EBITDA Margin on a sequential basis, however, the overall decent set of numbers in Q2FY23. Recent festive season, the 125cc segment has seen good growth as customers have grown from 100cc to 125cc. Super splendor 125cc has also done well, along with Glamour xTech. Rural, in July and August, was a little soft. However, Sept onwards it picked up and we believe it will do well going forward. Going forward, HMCL has lined up multiple product launches in different cities with entry-mid vehicles that would add ~20% to the market size. **We maintain our Buy rating on the stock and value it SOTP valuation for a revised target price of INR 3,437 per share (earlier target price; INR 3,405 per share).**

Exhibit 1: Financial Performance

YE March	Net Sales	EBITDA	PAT	EPS (INR)	EBITDA Margin %	RoE (%)	P/E (x)
(INR Mn)							
FY22	292,455	33,688	24,730	123.8	11.52	16.0	20.9
FY23E	340,576	40,783	29,243	146.4	11.97	18.1	17.7
FY24E	381,017	47,945	34,358	172.0	12.58	20.1	15.1
FY25E	428,940	56,589	40,599	203.2	13.19	21.8	12.7

Source: Arihant Research, Company Filings

Q2FY23 Conference call Highlights

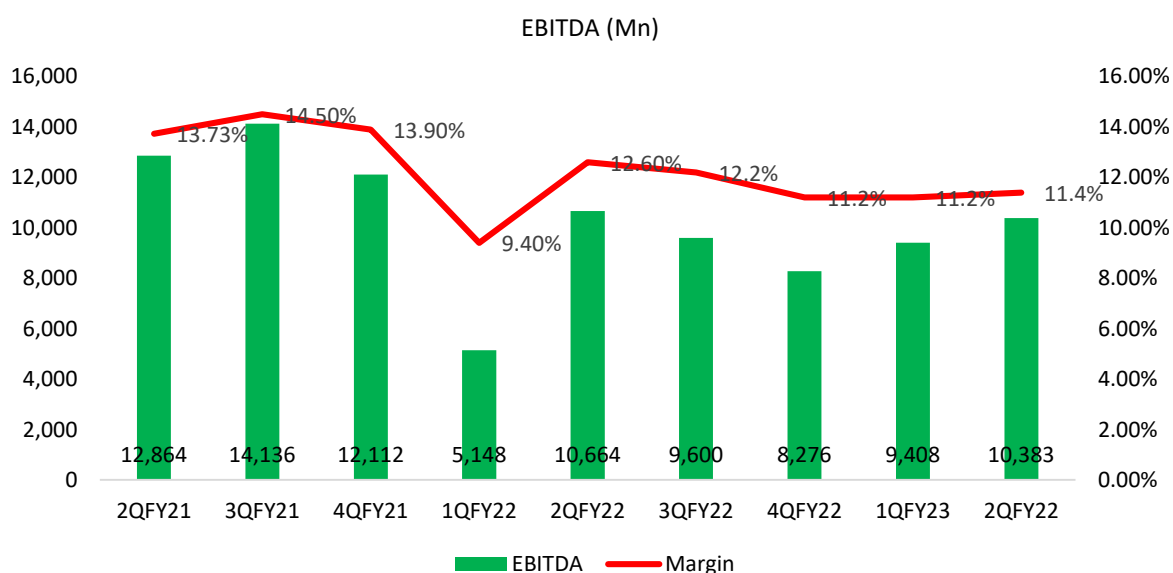
- **Gogoro:** The results include one off MTM loss on account of Gogoro investment of INR 44 crores. Pilots going on in this front. Would further expand the network for EVs.
- The company delivered highest ever first half gross profit per vehicle at rupees 17,140 unit of vehicles sold.
- **Recent festive season:** ~32 days. Hero was close to understanding the trends and sentiments of consumers and dealers. The trend is moving towards premiumization. Management has prioritized the xTech range of vehicles. (Premium variants of Destiny, Passion, Glamour). Rural, in July and August, was a little soft. However, Sept onwards it picked up. The company witnessed pent-up demand. However, in the last 6 days (Dussehra to Diwali), volumes picked up and grew 20% YoY (consumer retails) compared to the last festive period.
- **Pipeline:** The company is building a strong pipeline of premium products as well and will be able to see exciting model launches in this segment every year. This will help HeroMotoCorp build market share in the premium segment and boost profitability over medium term.
- The company has been focusing on growing PAM business in the last few quarters and glad to report that parts business revenue for H1FY23 was at 2,300 cr registering a growth of 45%.
- Parts business revenue now accounts for 13.7% of revenue and the company aim to increase it to 15% beyond that those prospects in the parts which is a traditional business. Aim to grow accessories and merchandise, which has got huge opportunities over the next few quarters. In order to address the affordability in the entry segment
- **Finance:** The company finance penetration has now gone up to 60% plus. And again this builds a strong underlying platform to translate the desire and need of people into real demand.
- **EV:** The company will be starting test sites soon. The deliveries will begin as planned and from initial three cities, plan to get to 10 plus cities by March. Plan to cover both the mid and affordable segment as well. Vida is priced at the premium segment levels. Plans to open test drive soon. Would release booking numbers in subsequent months.
- **Macroeconomic factor:** India clearly is relatively much better placed with strong consumption base, favorable demographic profile, a significant headroom for per capita consumption relative to other countries. The recent resurgence of spending across categories during the festive season is reflective of return of consumer confidence and augurs well for the industry growth moving forward.
- **Inventory levels:** Lowest post-festive. ~4-6 weeks range. Around 4 weeks.
- 125cc segment has seen good growth as customers have grown from 100cc to 125cc. Super splendour 125cc has done well during the festive season, along with Glamour xTech. The company has run various ad campaigns as well. Seen strong double-digit growth. It expects to launch more products in the segment.
- **Hero Fincorp:** It is doing well. GNPA is at 6.5%, targeting 5% over the next few quarters. AUM grew in double digits. Q2 PAT of ~INR 60cr.
- Model mix has been favourable in Q2. Splendour and xTech have done well. Customers are wanting to upgrade.
- **Festive retails:** 20% growth augurs well for the next leg of growth. This builds a strong base going forward. On-ground demand remains strong. Management. remains optimistic on demand going forward, on the back of strong rains, rural and marriage season in H2. Management believes volumes have come back to ~95% pre-covid festival period.
- **Parts revenue:** Q2FY23 INR 1,244cr, Q1FY23 INR 1,061cr and Q2FY22 INR 1,141cr.
- **Demand scenario:** Rural was recovering, although slower. Rains came in and further impacted offtake. However, from Dussehra to Diwali, rural sales bounced back strong. Urban has continued to perform strong. Overall, they are close to their pre-covid days.
- **RM Cost:** Cost in the quarter has come down YoY and QoQ. Going forward, it is seeing metals cooling off and expects some benefits. However, headwinds from forex on the back of currency depreciation are expected to impact earnings partially. 30-40bps drop on the back of commodity costs. A large bulk of this would come in subsequent quarters.
- **Other expenses:** On the back of high marketing expenses and some bit of spend phasing. Management. has given a range of 10.1% for FY23.
- **Margins:** Hero is working on premiumization. It expects this would aid margin expansion in the near term.
- **Next 2 years:** it plans to launch models in the premium segment. Including products co-developed with Harley Davidson.
- **Price absorption:** Looking at the recent festive season retails, the industry has absorbed the price increases positively. Overall, it had raised prices by 5-6% in the last few quarters. Going forward, it would further raise prices, in line with the inflation rate.
- **Market share trend:** 34.8% in Oct'22; 38.5% in Nov'22. Continue to be extremely strong in entry, deluxe, splendour passion and others. For the 125cc, it is on the way to recovering lost market share through the glamour passion xtech series. For Premiums, it plans to build a portfolio and launch products in the near term.
- **Ather:** Minor dilution in the stake. Gone down by ~2% to ~27%. Raised funds from GIC INR 400cr at a valuation of INR 6,000cr. Plans for Ather don't change and continue to do extremely well.
- Seen a good revival in passion and glamour along with xtech range of the same models. Mgmt. believes this segment is coming back. Whatever the company lost in Passion, it managed to gain in Splendor +
- Credit period without interest to dealers stands at 15 days. Post that, interest is chargeable.
- 32% of the EV market is for premium EV two-wheelers. Hero is playing in a significant portion of market. Further launches in different cities with entry-mid vehicles would add ~20% to the market size.
- **OBD Phase 2:** Impact is not significant. Marginal from a cost point of view.
- HFCL 35%, share of financing.
- Other Operating revenues Q2FY23 INR 231cr Q1FY22 INR 181cr.

Exhibit 2: Quarterly result summary Q2FY23

Standalone (INR mn)	2QFY23	1QFY23	2QFY22	YoY (%)	QoQ (%)
Net sales	90,754	83,925	84,534	7.4	8.1
- Raw material	65,301	61,074	61,104	6.9	6.9
(% of net sales)	72.0	72.8	72.3	-33bps	-82bps
Gross Profit	25452.1	22851.6	23430.4	8.6	11.4
(% of net sales)	28.0%	27.2%	27.7%	0bps	1bps
- Staff expenditure	5,490	5,382	5,054	8.6	2.0
(% of net sales)	6.0	6.4	6.0	7bps	-36bps
- Other expenditure	9,579	8,062	7,712	44.8	18.8
(% of net sales)	10.6	9.6	9.1	143bps	95bps
Total expenditure	80,371	74,518	73,870	8.8	7.9
EBITDA	10,383	9,408	10,664	(2.6)	10.4
EBITDA Margin (%)	11.4	11.2	12.6	-117bps	23bps
Depreciation	1,634	1,630	1,639	(0.3)	0.2
EBIT	8,749	7,778	9,025	(3.1)	12.5
Interest	33	70	65	(49.4)	(52.6)
Other Income	921	530	1,569	(41.3)	73.7
PBT	9,637	8,238	10,529	(8.5)	17.0
Tax	2,476	1,993	2,585	(4.2)	24.2
Reported PAT	7,161	6,245	7,944	(9.9)	14.7
Adjusted PAT	7,161	6,245	7,944	(9.9)	14.7
Adjusted EPS (INR)	35.8	31.3	39.8	(9.9)	14.7
Total volumes (Nos)	1,428,168	1,390,193	1,438,623	(0.7)	2.7
Net realisation (INR)	63,545	60,370	58,760	8.1	5.3
EBITDA / vehicle (INR)	7,270	6,767	7,412	(1.9)	7.4

Source: Arihant Research, Company Filings

Exhibit 3: Hero is working on premiumization. It expects this would aid margin expansion in the near term.



Source: Arihant Research, Company Filings

Exhibit 4:SOTP valuation

SOTP Valuation	Amount (INR)
FY25E Core EPS (INR/share, A)	203
P/E Multiple assigned (x, B)	14
Value of Base Business (C =A*B)	2,845
Ather Energy (P/sales 4x) Per share Value (D)	108
Hero Fincorp (P/sales 2x) Per share Value (E)	484
D+E=F	592
Target Price (F+C)	3,437
CMP INR	2,589
Potential Upside (%)	33%

Source: Aриhant Research

Financial Performance

Profit & Loss Statement				
YE: Mar (INR mn)	FY22	FY23E	FY24E	FY25E
Net sales	292,455	340,576	381,017	428,940
Growth, %	(5)	16	12	13
RM expenses	-208,267	-242,490	-269,760	-301,116
Employee expenses	-19,354	-21,116	-22,861	-25,736
Other expenses	-31,145	-36,187	-40,451	-45,499
EBITDA	33,688	40,783	47,945	56,589
Growth, %	(16)	21	18	18
Margin, %	11.5	12.0	12.6	13.2
Depreciation	-6,498	-7,659	-8,139	-8,619
EBIT	27,190	33,124	39,806	47,970
Growth, %	(19)	22	20	21
Margin, %	9.3	9.7	10.4	11.2
Interest paid	-258	-271	-284	-299
Other Income	5,569	5,625	5,687	5,749
Pre-tax profit	32,501	38,478	45,208	53,420
Tax provided	-7,771	-9,235	-10,850	-12,821
Profit after tax	24,730	29,243	34,358	40,599
Others (Minorities, Associates)	-	-	-	-
Net Profit	24,730	29,243	34,358	40,599
Growth, %	(17)	18	17	18
Net Profit (adjusted)	24,730	29,243	34,358	40,599

Balance Sheet				
YE: Mar (INR mn)	FY22	FY23E	FY24E	FY25E
Cash & bank	1,751	2,196	3,787	11,187
Marketable securities cost	94,320	93,632	101,924	110,950
Debtors	23,043	26,834	30,021	33,797
Inventory	11,227	13,074	14,626	16,466
Loans & advances	402	469	521	582
Other current assets	6,525	7,177	7,895	8,684
Total current assets	42,947	49,749	56,849	70,715
Investments	12,204	13,424	14,766	16,243
Gross fixed assets	154,669	164,669	174,669	184,669
Less: Depreciation	-94,339	-101,998	-110,137	-118,756
Add: Capital WIP	873	1,603	1,603	1,603
Net fixed assets	60,330	62,671	64,532	65,913
Total assets	213,479	226,793	245,388	271,138
Current liabilities	53,038	59,147	65,414	72,585
Provisions	3,385	3,554	3,732	3,918
Total current liabilities	56,423	62,701	69,145	76,504
Non-current liabilities	-772	-772	-772	-772
Total liabilities	55,650	61,928	68,373	75,731
Paid-up capital	399.6	399.6	399.6	399.6
Reserves & surplus	157,430	164,465	176,615	195,007
Shareholders' equity	157,829	164,865	177,015	195,407
Total equity & liabilities	213,479	226,793	245,388	271,138

Source: Aриhant Research, Company Filings

Cash Flow				
YE: Mar (INR mn)	FY22	FY23E	FY24E	FY25E
Pre-tax profit	32,501	38,478	45,208	53,420
Depreciation	6,498	7,659	8,139	8,619
Chg in working capital	-1,682	-2,737	935	893
Total tax paid	-7,979	-9,235	-10,850	-12,821
CFO	21,528	28,811	38,030	44,660
Capital expenditure	-6,042	-10,729	-10,000	-10,000
Chg in investments	-1,526	-533	-9,635	-10,502
Other investing activities	5,569	5,625	5,688	5,748
CFI	-2,000	-5,637	-13,947	-14,754
Free cash flow	13,959	17,549	18,395	24,158
Debt raised/(repaid)	0	0	0	0
Dividend (incl. tax)	-22,208	-22,208	-22,208	-22,208
CFF	-22,466	-22,479	-22,492	-22,506
Net chg in cash	(2,938)	695	1,591	7,400
Opening cash balance	4,438	1,751	2,196	3,787
Closing cash balance	1,751	2,196	3,787	11,187

Ratios				
YE: Mar	FY22	FY23E	FY24E	FY25E
EPS (INR)	124	146	172.0	203.2
PER (x)	20.9	17.7	15.1	12.7
Price/Book (x)	3.3	3.1	2.9	2.6
EV/EBITDA (x)	12.5	10.3	8.6	7.0
EV/Net sales (x)	1.4	1.2	1.1	0.9
RoE (%)	16.0	18.1	20.1	21.8
RoCE (%)	21.2	24.1	26.7	29.0
Fixed Asset turnover (x)	1.9	2.1	2.2	2.3
Dividend Yield (%)	3.7	3.7	3.7	3.7
Receivable (days)	29	29	29	29
Inventory (days)	16	16	16	16
Payable (days)	60	60	60	60
Net D/E ratio (x)	(0.6)	(0.6)	(0.6)	(0.6)

Source: Arian Research, Company Filings

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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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