

Above estimate: Structural Growth Drivers Remain Intact

CMP: INR 2,787

Rating: Buy

Target Price: INR 3,738

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)	556,663
52w H/L (INR)	3,629/2,310
Avg Yearly Vol (in 000')	702

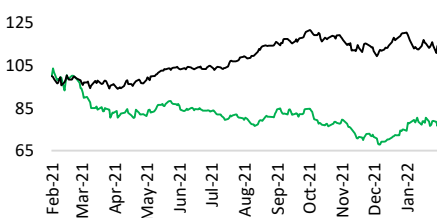
Shareholding Pattern %

(As on Dec, 2021)

Promoters	34.75
FII	43.05
DII	10.22
Public	11.87

Stock Performance (%)	1m	3m	12m
Hero MotoCorp	8.45	1.31	-19.4
Nifty	-5.11	-3.7	13.1

Hero MotoCorp Vs Nifty



— Hero Motorcorp — Nifty 50

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- Hero MotoCorp (HMCL) declared results above estimates on all fronts in Q3FY22.
- Standalone revenue from operations de-grew by 6.7% QoQ/ -19.4% YoY stood at INR 78,833 Mn in Q3FY22 against our estimate of INR 77,440 Mn.
- EBITDA de-grew by 17%QoQ/-37%YoY to INR 9,600 Mn against our estimate of INR 8,900 Mn.
- EBITDA margin contracted by 44bps QoQ/ 228bps YoY to 12.2% Q3FY22 vs our estimate of 11.5%.
- The Company reported a net profit of INR 6,861 Mn in Q3FY22 against our estimate of INR 6,565 Mn, de-grew by 13.6% QoQ/-36.7% YoY.
- Basic EPS at INR 38.8 in Q3FY22 as against INR 54.3 in Q3FY21 (Q2FY22 was INR 39.8)
- The total volumes (Motorcycles + Scooters) de-grew by 30% YoY to 12,92,136 units. The company realizations grew 15%/4% YoY/QoQ led by improved product mix, price hikes, and higher spare parts revenue.

Business Highlights

- **Global Business:** The company's global business consistently doing well, on track to achieve 300K units in FY22E, which is 50% higher than the usual past year's run-rate. Hero Moto Corp QoQ gross margins improved by 132bps due to a combination of mix & cost savings programs. Some bit of recovery is yet to be made, commodity benefits are yet to flow through.

Outlook and valuation

At the CMP of INR 2,787, Hero MotoCorp is trading at a PE of 13.4x, to its FY24E EPS of INR 208. HMCL has reported a performance above our estimates in Q3FY22 backed by a surprise reduction in RMC & higher growth in non-2W business. The company's exports are doing well, while 360-degree efforts on EV will provide an edge. The company under the LEAP 2 program has been aggressive in cost-saving, operating leverage benefits, and price hikes which will result in margin improvement. Secondly, Hero will benefit from its premium bikes, strong support from the economy, executive motorcycle segments, aggressive product offerings in the premium bikes, and scooter segment. The EV segment is likely to do well for growth in the medium term.

We value Hero MotoCorp at PE of 18x to its FY24E EPS estimate of INR 208, which yields a target price of INR 3,738. We maintain our Buy rating on the stock.

YE March (INR Mn)	Net Sales	EBITDA	PAT	EPS (INR)	EBITDA Margin %	RoE (%)	P/E (x)
FY21	308,006	40,192	29,642	148.4	13.0	20.2	18.7
FY22E	319,818	38,887	28,292	141.6	12.2	18.2	19.6
FY23E	347,681	49,272	35,375	177.1	14.2	21.3	15.7
FY24E	389,229	57,919	41,491	207.7	14.9	22.6	13.4

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

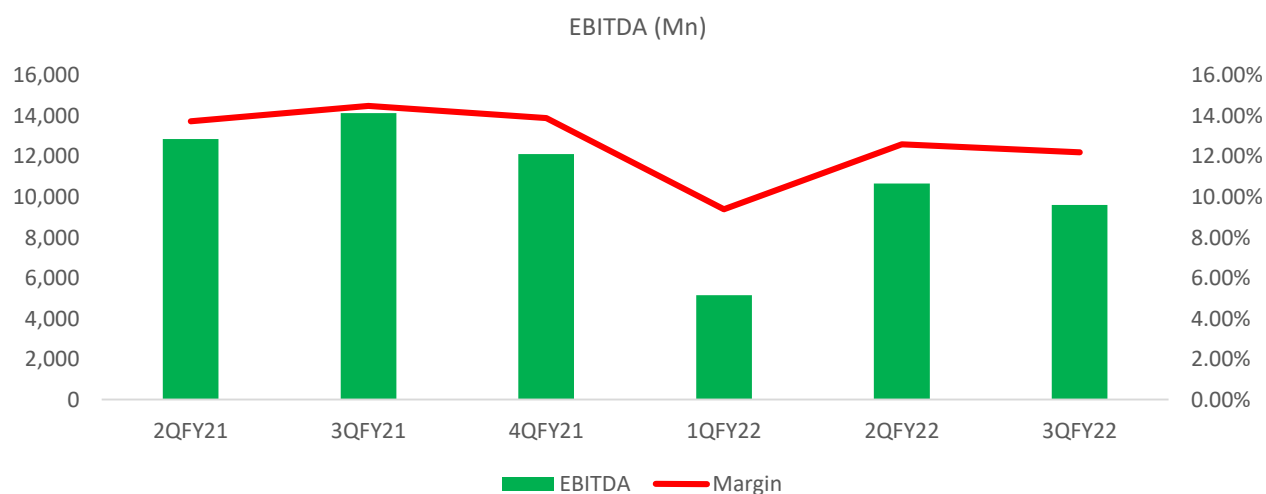
Q3FY22 Conference call Highlights

- **Demand:** Rural demand impacted in the past few quarters due to 2nd wave of Covid, delayed & then extended monsoon impacted sentiments. The company is seeing bottoming out is happening with improvement in consumer confidence, good crop production, the government's focus on rural. Hence, expect good FY23 in rural. Education institutions opening up & upcoming marriage season are going to happen after two years of gap. Entire sectors of the economy are opening up, large expenditure in the union budget announced, private industry to come back, etc. All this will support in sales growth.
- **ICE scooters:** HeroMotoCorp has been losing share. It plans to launch a few models and upgrade existing scooters by doing premiumization. Planning to launch Destini xtec 125cc.
- **Financing:** 58% is the finance penetration. This number was hovering around 40-45% few years back.
- **Inventory:** The current inventory with dealers and sub-dealers are slightly higher at 7-8 weeks. Usually, it's around 6 weeks. The higher inventory is due to soft festive season and marriage season.
- **Non-2W:** The company is also focusing on non-2W product revenues including spare parts. It reported INR 11860Mn revenue from it, which is a growth of 15% YoY. It will continue to grow this business as its giving handsome rewards. The company revenues from non-2W business was INR 100330 Mn in Q3FY21 and INR 11410Mn in Q2FY22. There are big plans to increase it further.
- **Hero FinCorp** Closed capital raise round of INR 20000Mn, which will help it to double the AUM from INR 260000 Mn to 500000mn. The investment is for growth. FinCorp has strong liquidity, delivered positive PAT in Q3FY22.
- **FinCorp** is now fully funded and there won't be any requirement for the next couple of years. May be FinCorp gets listed in the coming years.
- **New launch:** The company will continue to launch products in the premium portfolio, apart from premiumization within existing products and growing global business. Income is coming back, spending too will increase. Consumer confidence which was held back during Covid will come back.
- **LEAP II Programme:** Metals peeking out along with the support from LEAP savings should help margin. Overall, expect strong rebound in 2W industry in FY23 with cost pressures easing out.
- **EV:** The company will launch its own product in March 2022 and will continue to invest in Ather, Gogoro. The company will cover all segments viz. premium, mid & mass.
- **Collaboration:** Forging collaboration and partnering many players in the eco system. The company participates in every capital raise round of Ather Energy and over the period has been increasing shareholding as well. Hero-Ather are exploring collaboration on various things, including charging, global business, front end, etc.
- **EV distribution strategy:** Hero & other incumbents have inherent strength like manufacturing, logistics, sourcing, etc., which will help in terms of reducing cost of acquisition of customers and reducing investments required in EV. Reach of Hero MotoCorp is good and will be using the existing strength of network, logistics, etc. for electric vehicles. In addition, there will be certain exclusive stores as well.
- **Gogoro:** The company has exclusive use of the battery swapping network. The Joint venture will think whether to allow others to use swapping network or not. In Taiwan, people prefer to swap their batteries in commercial and personal usage as people don't want to wait for long hours charging their vehicle batteries. Let's see how swapping behaves in India.
- In the coming 3-5 years, consolidation among EV players has to happen. Number of players will come down. EV penetration for some time will happen only in eScooters. Hero MotoCorp with a low market share in ICE Scooters is sitting in a sweet spot and gives them a chance to build penetration in eScooter segment.
- **FY23: Demand.** GST Collections have been high. Omicron has started to phase out. Opening of colleges and offices would accelerate a growth cycle. Should have a significant positive impact. Expect strong rebound in the 2W sector and cost pressure to ease off in FY23.
- **FY23 outlook:** FY22 was impacted by 2 waves of Covid and input cost. Expect a broad base recovery in FY23E.

Quarterly result summary

Standalone (INR mn)	3QFY22	2QFY22	3QFY21	YoY (%)	QoQ (%)
Net sales	78,833	84,534	97,758	(19.4)	(6.7)
- Raw material	55,943	61,104	68,912	(18.8)	(8.4)
(% of net sales)	71.0	72.3	70.5	47bps	-132bps
Gross Profit	22889.5	23430.4	28845.9	(20.6)	(2.3)
(% of net sales)	29.0%	27.7%	29.5%	0bps	1bps
- Staff expenditure	5,180	5,054	5,167	0.3	2.5
(% of net sales)	6.6	6.0	5.3	129bps	59bps
- Other expenditure	8,109	7,712	9,543	(15.0)	5.1
(% of net sales)	10.3	9.1	9.8	53bps	116bps
Total expenditure	69,233	73,870	83,621	(17.2)	(6.3)
EBITDA	9,600	10,664	14,136	(32.1)	(10.0)
EBITDA Margin (%)	12.2	12.6	14.5	-228bps	-44bps
Depreciation	1,644	1,639	1,698	(3.2)	0.3
EBIT	7,956	9,025	12,438	(36.0)	(11.8)
Interest	65	65	47	40.0	(0.5)
Other Income	1,216	1,569	2,027	(40.0)	(22.5)
PBT	9,107	10,529	14,418	(36.8)	(13.5)
Tax	2,246	2,585	3,574	(37.2)	(13.1)
Reported PAT	6,861	7,944	10,845	(36.7)	(13.6)
Adjusted PAT	6,861	7,944	10,845	(36.7)	(13.6)
Adjusted EPS (INR)	38.8	39.8	54.3	(28.6)	(2.5)
Total volumes (Nos)	12,92,136	14,38,623	18,45,274	(30.0)	(10.2)
Net realisation (INR)	61,010	58,760	52,977	15.2	3.8
EBITDA / vehicle (INR)	7,430	7,412	7,661	(3.0)	0.2

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



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

Margins were 12.2%. There is some recovery yet to be made. Raise prices by INR 1000 ex-showroom in Oct and INR 500 ex-showroom in Jan.

Profit & Loss Statement				
YE: Mar (INR mn)	FY21	FY22E	FY23E	FY24E
Net sales	308,006	319,818	347,681	389,229
Growth, %	7	4	9	12
RM expenses	-217,623	-225,472	-239,900	266,622
Employee expenses	-18,987	-19,829	-21,556	-23,354
Other expenses	-31,203	-35,630	-36,953	-41,335
EBITDA	40,192	38,887	49,272	57,919
Growth, %	2	(3)	27	18
Margin, %	13.0	12.2	14.2	14.9
Depreciation	-6,769	-6,940	-7,882	-8,362
EBIT	33,424	31,948	41,389	49,556
Growth, %	6	(4)	30	20
Margin, %	10.9	10.0	11.9	12.7
Interest paid	-218	-229	-241	-253
Other Income	5,799	5,509	5,398	5,290
Non-recurring Items	0	0	0	0
Pre-tax profit	39,004	37,227	46,547	54,594
Tax provided	-9,362	-8,934	-11,171	-13,103
Profit after tax	29,642	28,292	35,375	41,491
Others (Minorities, Associates)	-	-	-	-
Net Profit	29,642	28,292	35,375	41,491
Growth, %	(18)	(5)	25	17
Net Profit (adjusted)	29,642	28,292	35,375	41,491

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

Balance Sheet				
YE: Mar (INR mn)	FY21	FY22E	FY23E	FY24E
Cash & bank	2,725	1,706	2,791	10,495
Marketable securities cost	93,902	103,293	113,622	124,984
Debtors	24,268	25,410	27,624	30,925
Inventory	14,696	15,259	16,588	18,571
Loans & advances	892	924	983	1,092
Other current assets	5,709	6,280	6,908	7,599
Total current assets	48,288	49,579	54,895	68,682
Investments	11,094	12,204	13,424	14,766
Gross fixed assets	149,322	159,322	169,322	179,322
Less: Depreciation	-87,841	-94,781	-102,664	-111,026
Add: Capital WIP	1,779	1,603	1,603	1,603
Net fixed assets	61,480	64,541	66,658	68,296
Total assets	216,438	231,112	250,095	278,225
Current liabilities	61,803	64,382	68,619	75,866
Provisions	3,328	8,170	8,579	9,007
Total current liabilities	65,131	72,552	77,197	84,874
Non-current liabilities	-677	-677	-677	-677
Total liabilities	64,454	71,875	76,520	84,196
Paid-up capital	399.6	399.6	399.6	399.6
Reserves & surplus	151,585	158,838	173,176	193,629
Shareholders' equity	151,984	159,238	173,575	194,028
Total equity & liabilities	216,438	231,112	250,095	278,225

Cash Flow				
YE: Mar (INR mn)	FY21	FY22E	FY23E	FY24E
Pre-tax profit	39,004	37,227	46,548	54,596
Depreciation	6,769	6,940	7,882	8,362
Chg in working capital	10,486	5,112	415	1,592
Total tax paid	-9,362	-8,934	-11,171	-13,103
CFO	41,316	35,064	38,516	46,409
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	5,509	5,398	5,290
CFI	-24,322	-14,815	-16,151	-17,414
Free cash flow	11,195	14,741	16,967	23,705
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	(1,019)	1,086	7,703
Opening cash balance	2,419	2,725	1,706	2,791
Closing cash balance	2,725	1,706	2,791	10,495

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

Ratios				
YE: Mar	FY21	FY22E	FY23E	FY24E
EPS (INR)	148	142	177	208
PER (x)	18.8	19.7	15.7	13.4
Price/Book (x)	3.7	3.5	3.2	2.9
EV/EBITDA (x)	11.4	11.6	8.9	7.3
EV/Net sales (x)	1.5	1.4	1.3	1.1
RoE (%)	20.2	18.2	21.3	22.6
RoCE (%)	26.9	24.2	28.2	30.0
Fixed Asset turnover (x)	2.1	2.0	2.1	2.2
Dividend Yield (%)	2.5	3.2	3.2	3.2
Receivable (days)	29	29	29	29
Inventory (days)	20	20	20	20
Payable (days)	71	70	70	70
Net D/E ratio (x)	(0.6)	(0.7)	(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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