



Improvement in Margins

8th August, 2016

CMP: Rs 3,440
Target Price: Rs 3,766
Recommendation: HOLD

Stock Info	
BSE Group	A
BSE Code	500182
NSE Symbol	HEROMOTOCO
Bloomberg	HMCL IN
Reuters	HROM.BO
BSE Sensex	25,262
NSE Nifty	7,735

Market Info	
Market Capital	Rs 68,579 cr
Equity Capital	Rs 39.9 cr
Avg Trading Volume	3,98,180
52 Wk High / low	Rs 2,257/3,556
Face Value	Rs 2

Hero Motocorp Ltd. revenue surged by 7.74% to Rs 8,010 cr from Rs 7,435Cr in the corresponding quarter of previous year, it has achieved highest ever quarterly volumes of 17.45 lakhs units rising by 6.05% on YoY basis and 1.40% on Q-o-Q basis. Hero’s strong point is the executive segment in the motorcycle market, but this is also the category that is increasingly being cannibalized by scooters, owing to similar price points. Still, the company’s two recent Products—Maestro Edge and Duet—have helped it overtake TVS Motor Co. Ltd in the last quarter, even as it increases capacity.

Despite higher cost of materials, Operating EBITDA margins increased by 150 bps to 16.6% on YoY basis which is higher than our expectation and EBITDA for the quarter stood at Rs 1,230 cr, margins improved due to reduction in other expenses and robust volume growth in scooters and motorcycles segments during the quarter. Q1 profit surged by 17.7% to Rs.883 crore on YoY. Due to control on other expenses and higher sales volumes helped Hero Motocorp to post higher profit.

Other highlights

- With the above average monsoon so far and the implementation of the 7th pay commission recommendations, we remain optimistic about the remaining months of FY17.
- The growth trajectory has been the 125cc segment where the company now commands well over 50% market share which is contributed by Glamour and Super Splendor.
- In Q1FY17, Glamour grew by 32% and Super Splendor grew by 29% over the corresponding quarter in the previous fiscal.
- Recently launched the all new splendour ismart 110- the first motorcycle to have been completely designed and developed by in-house R&D team at jaipur, and the initial response from customers have been positive.

> **Outlook for next two years:** We remain cautiously optimistic on HMCL’s domestic business outlook over next 2 years, due to expected revival of domestic economy. We have modelled for 6.3% volume growth and 3% price realisation growth in FY17E and 15% volume growth and 3% price realization for FY18E.

> **Financial, Estimates :** We estimate Hero Moto’s Revenue growth of 10.4% in FY17E and 19.3% in FY18E, expect EBITDA margins close to 16.9% for FY17E and FY18E, expect PAT growth of 17.6% in FY17E and 20% inFY18E.

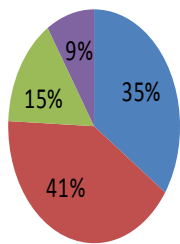
> **Valuation:** The stock at Rs 3,440 trades at 15.5x our estimated FY18 EPS of Rs 222 per share. We assign a price target of Rs 3,766 at 17x FY18 EPS, and have “HOLD” rating on the stock.

Y/E March, (in Rs crore)	FY14	FY15	FY16	FY17E	FY18E
Net Sales	25,125	27,351	28,160	31,086	37,090
yoy%	6.5%	8.9%	3.0%	10.4%	19.3%
Operating EBITDA	3,540	3,542	4,447	5,253	6,268
Operating EBITDA %	14.0%	12.8%	15.5%	16.6%	16.6%
PAT	2,109	2,386	3,132	3,684	4,424
yoy%	-0.4%	13.1%	31.3%	17.6%	20.1%
EPS	105.6	119.5	156.9	184.5	221.5
P/E (x)	21.5	22.1	18.8	18.6	15.5

Source: Company data, Aриhant Research

Share holding Pattern as on Jun 2016

Promoters FII DII Others



Price Vs Sensex Chart



Quarterly P&L in Rs cr	Q1FY17	Q1FY16	yoy%	Q4FY16	qoq%
Volumes (in numbers)	17,45,389	16,45,867	6.0%	17,21,240	1.4%
Net Realization per unit	41,765	41,656	0.3%	42,906	-2.7%
Net Sales	7,290	6,856	6.3%	7,385	-1.3%
Other Operating Income	109	99		127	
Income from Operations	7,399	6,955	6.4%	7,512	-1.5%
Materials Consumed	4,965	4,811	3.2%	4,955	0.2%
Employees Cost	336	314		351	
Other Expenditure	867	782		1,031	
Total Expenditure	6,169	5,907	4.4%	6,336	-2.6%
Operating EBITDA	1,230	1,048	17.4%	1,176	4.6%
margin	16.6%	15.1%		15.7%	
Core EBITDA	1,121	949	18.2%	1,049	6.9%
margin	15.4%	13.8%		14.2%	
Depreciation and Amortization	115	103	11.9%	115	-0.2%
Operating EBIT before Other Income & Excp Items	1,115	945	18.0%	1,060	5.1%
Other Income	120	102		102	
Interest	1.50	0.53		0.53	
PBT before Exceptional Items	1,234	1,046	17.9%	1,162	6.1%
Exceptional item	0	0		0	
PBT	1,234	1,046	17.9%	1,162	6.1%
Tax Expense	351	296		348	
Effective Tax Rate	28.4%	28.3%		30.0%	
Net Profit after Tax	883	750	17.7%	814	8.5%
EPS	44.2	37.6		40.8	

Source: Company data, Arian Research

Profit and Loss Account, Year Ending March

Particulars, in Rs crore	FY14	FY15	FY16	FY17E	FY18E
Net Sales	25,125	27,351	28,160	31,086	37,090
YoY%	6.5	8.9	3.0	10.4	19.3
Other Operating Income	151	235	439	622	742
Income from Operations	25,275	27,585	28,599	31,707	37,832
Materials Consumed	18,230	19,754	19,315	20,983	25,036
Total Expenditure	21,735	24,043	24,152	26,454	31,564
Operating EBITDA	3,540	3,542	4,447	5,253	6,268
Operating EBITDA margin %	14.1	13.0	15.8	16.9	16.9
Depreciation	1,107	540	441	528	601
Operating EBIT	2,433	3,002	4,006	4,726	5,668
Other Income	446	492.7	391	435	519
Interest	12	11.1	2	9	-
Exceptional Item	-	(155)	-	-	-
PBT	2,867	3,329	4,395	5,152	6,187
Tax Expense	758	943	1,262	1,468	1,763
Reported Net Profit	2,109	2,386	3,132	3,684	4,424
YoY%	(0.4)	13.1	31.3	17.6	20.1
Effective Tax Rate	26.4	28.3	28.7	28.5	28.5
Reported EPS	106	119	157	184	222

Cash Flow Statement, Year Ending March

Particulars, in Rs crore	FY14	FY15	FY16	FY17E	FY18E
Operating Activities					
PBT	2,867	3,329	4,395	5,152	6,187
Add Depr + non op exp	1,107	540	441	528	601
Others	79	288	(176)	81	(351)
Total	4,054	4,157	4,660	5,761	6,437
Cash Taxes	649	1,000	1,262	1,468	1,763
Changes in Working Cap	(441)	(907)	(515)	(373)	(397)
Cash Flow from Operations	2,963	2,250	2,883	3,920	4,277
Investing Activities					
Change in investments	2,225	1,738	2,007	2,796	2,991
Capex	608	1,750	817	801	862
Cash Flow from Investing	(1,617.0)	12.1	(1,190.0)	(1,994.7)	(2,129.6)
Financing Activities					
Dividends + Taxes paid	1,403	2,219	1,728	1,896	2,109
Change in Non Curr Liab	11.8	11.1	2.2	8.6	-
Cash Flow from Financing	(1,414.9)	(2,231)	(1,730)	(1,905)	(2,109)
Opening Cash	135	66	98	60	81
Changes during year	(69)	32	(38)	20	38
Adj due to amalgamation/unpaid div	51.1	61.3	71.0	80.5	80.5
Closing Cash	118	159	131	161	199

Balance Sheet, Year Ending March

Particulars, in Rs crore	FY14	FY15	FY16	FY17E	FY18E
Liabilities + Equity					
(a) Share capital	40	40	40	40	40
(b) Reserves and surplus	5,560	6,501	7,905	9,693	12,008
Shareholders' funds	5,600	6,541	7,945	9,732	12,047
Non-current liab & Prov	74	97	347	147	176
Current liabilities	4,423	3,883	4,049	5,099	6,276
Total - Equity and liabilities	10,097	10,522	12,341	14,979	18,500
Assets					
Non-current assets					
Fixed assets	3,097	3,625	4,442	5,536	6,690
Long Term Inv	813	864	1,019	1,142	1,370
Loans + Adv + Others	631	751	944	913	1,439
Non-current assets	4,541	5,240	6,406	7,591	9,499
Current assets					
Cash	118	159	131	161	199
Other Current Assets	5,438	5,123	5,804	7,227	8,801
Sub-total - Current assets	5,556	5,282	5,935	7,388	9,001
Total - Assets	10,097	10,522	12,341	14,979	18,500

Ratio Analysis

	FY14	FY15	FY16	FY17 E	FY18E
Profitability					
Operating EBITDA%	14.1	13.0	15.8	16.9	16.9
Core EBITDA%	13.5	12.1	14.2	14.9	14.9
PAT%	8.4	8.7	11.1	11.9	11.9
ROAE%	39.8	39.3	43.2	41.7	40.6
Du Pont ROAE breakup					
PAT / Sales	8.3	8.6	11.0	11.6	11.7
Sales / Avg Total Assets	2.6	2.7	2.5	2.3	2.3
Avg Total Assets / Avg Eqty	1.9	1.7	1.6	1.5	1.5
ROE	39.8	39.3	43.2	41.7	40.6
Other Ratios					
Current Ratio	1.3	1.4	1.5	1.4	1.4
Long Term Debt / Equity	0.01	0.01	0.04	0.02	0.01
EPS	105.6	119.5	156.9	184.5	221.5
DPS	65.0	60.0	72.0	80.0	88.0
Dividend Payout ratio	61.5	50.2	45.9	43.4	39.7
P/E	22	22	18.8	18.65	15.5
BVPS	280.4	327.6	397.9	487.4	603.3
P/BV	8.1	8.1	7.4	7.1	5.7

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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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