



Improvement in Margins

9th February, 2017

CMP: Rs 3,262
Target Price: Rs 3,330
Recommendation: NEUTRAL

Stock Info	
BSE Group	A
BSE Code	500182
NSE Symbol	HEROMOTOCO
Bloomberg	HMCL IN
Reuters	HROM.BO
BSE Sensex	28,321
NSE Nifty	8,779

Market Info	
Market Capital	Rs 66,802 cr
Equity Capital	Rs 39.9 cr
Avg Trading Volume	4,11,120
52 Wk High / low	Rs 2,438/3,740
Face Value	Rs 2

Hero Motocorp Ltd. revenue declined by 12.9% to Rs 6,246 cr from Rs 7,174Cr in the corresponding quarter of previous year. During quarter, company has sold 14.73 units, declined of 12.8% on YoY basis and 19.2% 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. Company has received positive initial response from customers for Splendor, iSmart 110.

Due to lower cost of materials, Operating EBITDA margins increased by 131 bps to 16.9% on YoY basis which is higher than our expectation and EBITDA for the quarter stood at Rs 1,080 cr, margins improved due to reduction in other expenses. Q1 profit declined marginally by 3.0% to Rs.772 crore on YoY. Despite of lower volumes company has achieved profits mainly due to control on raw materials & other expenses.

Other highlights

- The introduction of BSIV emission, it has incurred cost of Rs400 to Rs500 per unit. Company has hiked price in month of January by Rs500 to Rs1200 to offset BSIV emission.
- 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.
- Going ahead, Margins are expected to contract due to rise in steel price.
- Company is facing headwinds in export markets like Argentina, Mexico, and Nigeria mainly due to dollar currency crisis. As per management comment, H2 FY17 would be better than H1FY17, mainly growth comes from Scooters as well as Motorcycles.

> **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.

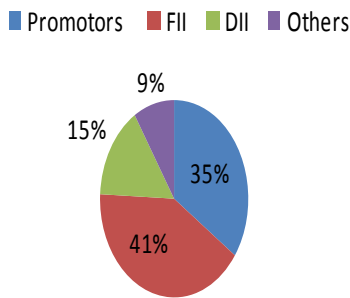
> **Financial, Estimates :** We estimate Hero Moto’s Revenue growth of 10.4% in FY17E and 19.3% in FY18E, expect EBITDA margins close to 16.9% for FY17E and FY18E, expect PAT growth of 17.6% in FY17E and 20% in FY18E.

> **Valuation:** The stock at Rs 3,262 trades at 15x our estimated FY18 EPS of Rs 222 per share. We assign a price target of Rs 3,330 at 15x FY18 EPS, and have “NEUTRAL” rating on the stock.

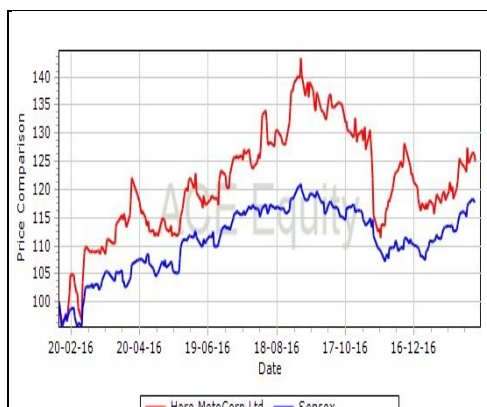
Y/E March, (in Rscore)	FY14	FY15	FY16	FY17E	FY18E
Net Sales	25,125	27,351	28,160	31,086	37,090
yoy%	6.5%	8.9%	3.0%	10.4%	19.3%
Operating EBITDA	3,540	3,542	4,447	5,253	6,268
Operating EBITDA %	14.0%	12.8%	15.5%	16.6%	16.6%
PAT	2,109	2,386	3,132	3,684	4,424
yoy%	-0.4%	13.1%	31.3%	17.6%	20.1%
EPS	105.6	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 Dec 2016



Price Vs Sensex Chart



Quarterly P&L in Rs cr	Q3FY17	Q3FY16	yoy%	Q2FY17	qoq%
Volumes (in numbers)	14,73,548	16,90,354	-12.8%	18,23,498	-19.2%
Net Realization per unit	42,387	42,442	-0.1%	42,059	0.8%
Net Sales	6,246	7,174	-12.9%	7,670	-18.6%
Other Operating Income	119	121		127	
Income from Operations	6,365	7,295	-12.8%	7,796	-18.4%
Materials Consumed	4,128	4,883	-15.5%	5,183	-20.4%
Employees Cost	374	345		357	
Other Expenditure	783	927		887	
Total Expenditure	5,285	6,155	-14.1%	6,427	-17.8%
Operating EBITDA	1,080	1,140	-5.3%	1,369	-21.1%
margin	16.96%	15.6%		17.6%	
Core EBITDA	961	1,019	-5.7%	1,242	-22.6%
margin	15.4%	14.2%		16.2%	
Depreciation and Amortization	125	114	9.6%	119	4.7%
Operating EBIT before Other Income & Excp Items	955	1,026	-6.9%	1,250	-23.6%
Other Income	132	84		152	
Interest	1.52	0.55		1.55	
PBT before Exceptional Items	1,085	1,110	-2.2%	1,400	-22.5%
Exceptional item	0	0		0	
PBT	1,085	1,110	-2.2%	1,400	-22.5%
Tax Expense	313	314		396	
Effective Tax Rate	28.9%	28.3%		28.3%	
Net Profit after Tax	772	796	-3.0%	1,004	-23.1%
EPS	38.7	39.9		50.3	

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	12
Exceptional Item	-	(155)	-	-	-
PBT	2,867	3,329	4,395	5,152	6,175
Tax Expense	758	943	1,262	1,468	1,760
Reported Net Profit	2,109	2,386	3,132	3,684	4,415
YoY%	(0.4)	13.1	31.3	17.6	19.8
Effective Tax Rate	26.4	28.3	28.7	28.5	28.5
Reported EPS	106	119	157	184	221

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	6,175
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	6,425
Cash Taxes	649	1,000	1,262	1,468	1,760
Changes in Working Cap	(441)	(907)	(515)	(373)	(397)
Cash Flow from Operations	2,963	2,250	2,883	3,920	4,268
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	12.0
Cash Flow from Financing	(1,414.9)	(2,231)	(1,730)	(1,905)	(2,121)
Opening Cash	135	66	98	60	81
Changes during year	(69)	32	(38)	20	18
Adj due to amalgamation/unpaid div	51.1	61.3	71.0	80.5	80.5
Closing Cash	118	159	131	161	179

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	11,999
Shareholders' funds	5,600	6,541	7,945	9,732	12,039
Non-current liab & Prov	74	97	347	147	164
Current liabilities	4,423	3,883	4,049	5,099	6,276
Total - Equity and liabilities	10,097	10,522	12,341	14,979	18,479
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	179
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	8,980
Total - Assets	10,097	10,522	12,341	14,979	18,479

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	221.1
DPS	65.0	60.0	72.0	80.0	88.0
Dividend Payout ratio	61.5	50.2	45.9	43.4	39.8
P/E	22	22	18.8	18.1	15.1
BVPS	280.4	327.6	397.9	487.4	602.9
P/BV	8.1	8.1	7.4	6.9	5.5

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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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