

Hero Motocorp Limited

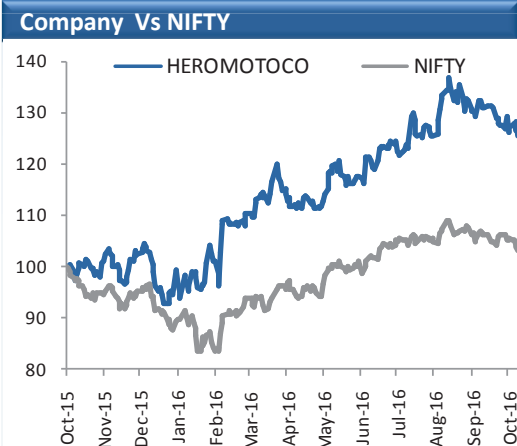
7-Nov-16

Result Update	
CMP	3283
Target Price	3830
Previous Target Price	3179
Upside	17%
Change from Previous	20%

Market Data	
BSE Code	500182
NSE Symbol	HEROMOTOCO
52wk Range H/L	3740/2375
Mkt Capital (Rs Cr)	65,558
Av. Volume	35025
Nifty	8434

Stock Performance			
	1Month	1Year	YTD
Absolute	-5.9	27.1	21.8
Rel.to Nifty	-2.4	22.4	15.7

Share Holding Pattern-%			
	2QFY17	1QFY17	4QFY16
Promoter	34.6	34.6	34.6
Public	65.4	65.4	65.4
Others	--	--	--
Total	100.0	100.0	100.0



Naveen Kumar Dubey
naveen.dubey@narnolia.com

The company has reported better set of numbers for 2QFY17, with a growth of 14% in topline, which was led by 15.8% volume growth. The important factors which led to volume growth were- high demand from rural areas and festivals during the quarter. We expect rural demand to remain positive in near future on account of better monsoon during the current fiscal. Seventh pay commission will drive urban and semi-urban demand for premium segment bikes. Hero is working on strengthening its international business which will be expected to lead better exports going forward. New launches in the premium segment will increase Hero's presence in this segment. It will further improve realisation and will also lead to higher margins.

2QFY17 Results Update

>>Revenue grew 14% YoY to Rs.7796 crore in 2QFY17, which was led by volume growth of 15.8%YoY.

>>Realisation declined by 90bps YoY due to higher sales of entry-level bikes in the rural areas.

>>Gross margin improved by 170 bps YoY to 33.5% driven by cost cutting initiative LEAP and lower commodity price benefit.

>>EBITDA margin expanded by 160 bps by lower advertising and promotional expenses.

>>PAT margin improved by 160 bps due to higher other income during the quarter.

Outlook and Valuation

Going ahead the management is expecting double digit growth for the full year on account of festivals, marriage season, seventh pay commission to lead urban and semi-urban demand and new launches in coming quarters. It has a healthy dividend payout of 54%, which provides cushion to the investors to invest in the company for long term. **Earlier we recommended 'BUY' on this stock at a target price of Rs.3179, but considering company's current development and future growth aspects, we maintain 'BUY' on this stock and revise our target from Rs.3179 to Rs.3830, an upside of 20%.**

	Rs. In crore				
Financials	2QFY17	1QFY17	2QFY16	QoQ	YoY
Sales	7796	7399	6837	5.4%	14.0%
EBITDA	1369	1230	1083	11.3%	26.3%
Net Profit	1004	883	772	13.7%	30.1%
EBITDA%	17.6%	16.6%	15.8%		
PAT %	12.9%	11.9%	11.3%		

(Source: Company/Eastwind)

Investment Argument

- >> Rural demand will be key trigger for Hero Motocorp because approx. 60% of the volumes comes from rural areas. Monsoon in the current fiscal have been good and hence we expect it to improve rural demand.
- >> Seventh pay commission will improve the living standard of the government employees and this may drive urban and semi-urban demand for premium segment bikes going forward.
- >> Hero Motocorp is a debt free and cash rich company. It has a healthy dividend payout of 54%, which provides cushion to the investors to invest in the company for long term.
- >>HMCL has increased its R&D expenditure to develop technologically advanced in house products. R&D team will focus on premium products where Hero has minimal presence and this segment has huge growth potential. Hero has only 6% market share in this segment.

Management Highlight

Chittoor Plant

- >> The two-wheeler giant will commence production of 5 lakh units (per annum) in the first phase by December 2018 with an investment of Rs 800 crore.(Chittoor Plant, Andhra Pradesh). It will add another 5 lakh units to its production capacity in the second phase by December 2020, and an additional 8 lakh units in the third phase by December 2023 with an investment of Rs 800 crore for both the phases. HMCL will provide employment to 1,500 people in the first phase and another 3,500 in the subsequent phases.
- >> Company is also setting up Ancillary units, which are expected to commence production in the first phase by December 2019 with an investment of Rs 400 crore. Another Rs 600 crore each would be invested for the next two phases by December 2021 and 2024, respectively.
- >> Capex guidance for FY17: Rs 1100 to 1300 crore (out of the total capex, R&D will be around Rs.150 crore and maintenance capex will be Rs. 250-350 crore).
- >> EBITDA margin guidance above 15% in FY17.
- >> Target of Rs.275 crore benefit from cost cutting program LEAP.
- >> Other income for FY17 would be higher by 8-9 percent on an average.
- >> The tax benefit for plants in Rajasthan and Gujarat will last for 7 years; and the benefit is restricted to the extent of investment
- >> Scooters to continue outpace motorcycle growth going forward in FY17.
- >> Normal dealer inventory 5 to 6 weeks and during the festive season it goes up to 7 weeks.
- >> Effective tax rate for FY17 will be slightly higher than FY16
- >> Advertising and Promotion expenses stood 2.2% of total sales for 1HFY17.

Plant Details

Plant Location	Capacity
Haridwar	3060000
Gurgaon	2340000
Dharuhera	2340000
Neemrana	450000
Halol	1800000

- >>Gujarat Plant- capacity expansion will include an initial capacity of 1.2 million (mn) units (phase 1: 0.75 mn units by Q1FY17; phase 2: 0.45 mn units by FY17 end) & a final addition of 0.6 mn (phase 3) by FY18 beginning.
- >>The Haridwar operations currently contribute towards 38% of HMCL's volumes. Once the excise benefits expire in FY18 end, there will be a 100 bps impact on the EBITDA margins.

Financials Snap Shot

	INCOME STATEMENT			
	FY14	FY15	FY16	FY17
Revenue (Net of Excise D	25,275	27,538	28,614	31,181
Other Income	444	492	389	531
Total Revenue	25,720	28,030	29,003	31,712
COGS	18,230	19,715	19,313	20,683
GPM	28%	28%	33%	34%
Other Expenses	2,576	3,147	3,575	3,688
EBITDA	3,539	3,497	4,382	5,353
EBITDA Margin (%)	14%	13%	15%	17%
Depreciation	1,107	540	447	571
EBIT	2,432	2,956	3,935	4,781
Interest	12	12	12	6
PBT	2,864	3,437	4,312	5,306
Tax	758	943	1,262	1,548
Tax Rate (%)	26%	27%	29%	29%
Reported PAT	2,103	2,365	3,094	3,758
Dividend Paid	1,519	1,402	1,682	2,043
No. of Shares	20	20	20	20

Source: Eastwind/Company

	BALANCE SHEET			
	FY14	FY15	FY16	FY17
Share Capital	40	40	40	40
Reserves	5,583	6,500	7,913	9,627
Net Worth	5,623	6,540	7,953	9,667
Long term Debt	24	12	146	146
Short term Debt	-	88	84	92
Deferred Tax	-	-	228	228
Total Capital Employed	5,647	6,552	8,099	9,813
Net Fixed Assets	3,102	3,671	4,689	5,270
Capital WIP	855	719	653	653
Debtors	921	1,372	1,282	1,397
Cash & Bank Balances	120	216	179	1,090
Trade payables	2,291	2,855	2,792	3,042
Total Provisions	1,594	801	884	959
Net Current Assets	1,135	1,481	1,999	3,044
Total Assets	10,122	10,654	12,672	14,711

Source: Eastwind/Company

	RATIOS			
	FY14	FY15	FY16	FY17
EPS	105	118	155	188
Book Value	282	328	398	484
DPS	76	70	84	102
Payout (incl. Div. Tax.)	72%	59%	54%	54%
Valuation(x)				
P/E	22	22	19	18
Price / Book Value	8	8	7	7
Dividend Yield (%)	3%	3%	3%	3%
Profitability Ratios				
RoE	37%	36%	39%	39%
RoCE	43%	45%	49%	49%
Turnover Ratios				
Asset Turnover (x)	2	3	2	2
Debtors (No. of Days)	13	18	16	16
Inventory (No. of Days)	13	16	14	14
Creditors (No. of Days)	33	38	36	36
Net Debt/Equity (x)	0.0	0.0	0.0	0.0

Source: Eastwind/Company

	FY14	FY15	FY16	FY17
OP/(Loss) before Tax	2864	3329	4312	5306
Depreciation	1107	540	447	571
Direct Taxes Paid	(649)	(1000)	(1104)	(1548)
Operating profit before w	3557	3586	4508	5830
CF from Op. Activity	2963	2250	3796	4476
	(9)	1354	26973	(47)
Capital expenditure on fix	(941)	(1156)	(1708)	(1151)
CF from Inv. Activity	(1618)	12	(2286)	(1523)
Repayment of Long Term Borrowings				
Interest Paid	(12)	(11)	(11)	(6)
Divd Paid (incl Tax)	(1403)	(2219)	(1682)	(2043)
CF from Fin. Activity	(1414)	(2231)	(1561)	(2042)
Inc/(Dec) in Cash	(69)	32	(50)	910
Add: Opening Balance	135	66	155	179
Closing Balance	69	98	104	1090

Source: Eastwind/Company