

HERO MOTOCORP LIMITED | Auto & Auto Components

...on a strong growth trajectory

LKP

Hero reported good set of numbers in Q1, on a steep volume growth of 35.7% yoy and 16.9% qoq to 1.39 mn units. Topline grew by 53% yoy and 13.1% qoq to ₹83.9 bn as realizations supported them by growing 12.7% yoy mainly on price hikes taken in Q1 and product mix. However, the realizations were down qoq by 3% on lower other operating income stemming from withdrawal of incentives at the Neemrana plant and lower spares business. The demand in Q1 witnessed a solid recovery on the back of a robust marriage season in the North, array of XTech launches, low base of last year, impact of pandemic fading off and general positive sentiments. Input costs to sales ratio in Q1 was at 72.8%, up from 69.3% qoq and 72.5% yoy. Other expenses to sales as well as employee costs to sales were reported at 9.6% and 6.4% yoy respectively. EBITDA margins were sequentially maintained at 11.2% despite increase in input costs. As depreciation expenses remained flattish yoy, and other income de-grew by 62% (on MTM losses on investments), PBT grew by just 2% while PAT grew by 7.4% qoq and 71% yoy

Demand drivers remain intact, volumes to witness a surge in the festive season

Post weak numbers observed in Q4 FY22, demand started picking up in April as entry level bikes found robust demand amidst marriage season in some parts of the country. The company is gaining strength through the XTech (Extra Technology) variant launches of Passion, Glamour, Splendor and Deestini models. In the premium bikes segment, the company attained market share of >6% on the back of X-treme 150 R and X-Pulse bikes. Going forward, the intrinsic growth drivers are expected to remain intact with the rural markets bouncing back well and monsoons being in a strong phase except in some eastern states. As the country enters in to festive season, management expects 2W demand to be on a healthy trajectory supported by micro factors such as normal monsoon hereon, crop cycle, opening of all sectors of the economy etc. On the EV side, Hero will launch an EV scooter in the festive season and has forged several partnerships and collaborations on this front including charging infrastructure. These factors, along with the XTech launches done during Q1 and future launches should help the company to post a double digit volume growth in FY23E and increase its market share further. Recovery in chip shortage issue should further assist the cause.

| Key Financials | FY 21 | FY 22 | FY 23E | FY 24E |
|--------------------|-------|--------|--------|--------|
| Revenues (₹ bn) | 308 | 292 | 344 | 394 |
| EBITDA (%) | 13.0 | 11.5 | 12.5 | 13.2 |
| PAT (%) | 9.6 | 8.5 | 8.7 | 9.3 |
| EPS (₹) | 148.4 | 123.8 | 149.7 | 184.3 |
| EPS growth (%) | 0.3% | -16.6% | 20.9% | 23.1% |
| P/E (x) | 18.6 | 22.3 | 18.4 | 15.0 |
| P/B (x) | 1.9 | 1.8 | 1.8 | 1.7 |
| EV/EBITDA (x) | 12.1 | 14.2 | 12.0 | 9.9 |
| ROCE (%) | 19.2% | 14.9% | 18.0% | 21.3% |
| ROE (%) | 19.5% | 15.7% | 18.6% | 22.1% |
| Dividend yield (%) | 3.4% | 3.4% | 4.1% | 4.7% |

| | |
|--------------------------|-------|
| Rating | Buy |
| Current Market Price (₹) | 2,762 |
| 12 M Price Target (₹) | 3,226 |
| Potential upside (%) | 17 |

Stock Data

| | |
|---------------------------------------|--------------------|
| FV (₹) : | 2 |
| Total Market Cap (₹ bn) : | 551 |
| Free Float Market Cap (₹ bn) : | 359 |
| 52-Week High / Low (₹) : | 2,954 / 2,147 |
| 2-Year High / Low (₹) : | 3,629 / 2,147 |
| 1 Yr Avg. Dly Traded Volume (in lakh) | 7 |
| BSE Code / NSE Symbol | 50018 / HEROMOTOCO |
| Bloomberg : | HMCL IN |

Shareholding Pattern

| (%) | Jun-22 | Mar-22 | Dec-21 | Sep-21 |
|-----------|--------|--------|--------|--------|
| Promoter | 34.78 | 34.75 | 34.75 | 34.76 |
| FPIs | 28.84 | 29.22 | 29.57 | 32.28 |
| MFs | 9.74 | 8.71 | 8.43 | 7.38 |
| Insurance | 13.61 | 13.79 | 13.83 | 13.40 |
| Others | 13.03 | 13.53 | 13.42 | 12.18 |

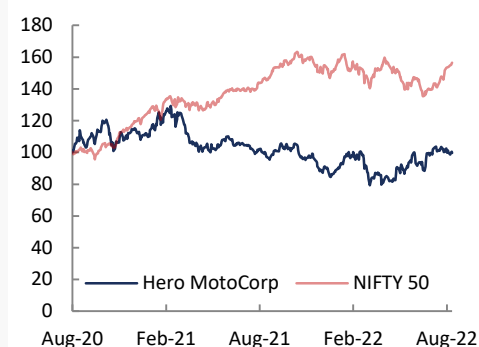
Source: BSE

Price Performance

| (%) | 1M | 3M | 6M | 1YR |
|---------------|-------|-------|------|-------|
| Hero Motocorp | -4.0% | 15.0% | 1.6% | -0.8% |
| Nifty 50 | 10.2% | 12.0% | 1.9% | 8.2% |

* To date / current date : August 12, 2022

Hero Motocorp vs Nifty 50



Margin stability despite challenging cost environment should earn brownie points

Hero's EBITDA margins in Q1 came flat at 11.2% qoq on despite a sharp rise in RM costs on the back of price hikes and cost saving measures under LEAP-2 program. The company took price hikes to the tune of ₹850 per vehicle in April and ₹1200 in June. The company under the LEAP program is quite aggressive in saving employee costs and other expenses. These steps shall enable the company to achieve its margin target of 14-15% in the medium term, as softening of commodities should augur well. Secondly, premiumization of bikes with the help of global partner Harley Davidson shall help the product mix to improve further. The launches of XTech variants which are priced higher by 5-7% than the original models should help the margins further to grow as their volumes grow. Price hikes combined with superior product mix and better operating leverage should help margin growth.

Quarterly Financial Snapshot

| YE Mar (₹ mn) | Q1 FY23 | Q4 FY22 | % QoQ | Q1 FY22 | % YoY |
|-------------------------|-------------|-------------|------------------|------------|----------------|
| Total net sales | 83,925.4 | 74,217.3 | 13.1% | 54,871.0 | 53.0% |
| RM cost | 61,073.8 | 51,424.4 | 18.8% | 39,795.9 | 53.5% |
| Employee cost | 5,381.8 | 4,763.3 | 13.0% | 4,356.7 | 23.5% |
| Other expenses | 8,062.0 | 9,753.9 | -17.3% | 5,569.6 | 44.8% |
| EBITDA | 9,407.8 | 8,275.7 | 13.7% | 5,148.8 | 82.7% |
| <i>EBITDA Margins %</i> | <i>11.2</i> | <i>11.2</i> | <i>0 bps</i> | <i>9.4</i> | <i>180 bps</i> |
| Other income | 529.9 | 1,397.6 | -62.1% | 1,386.0 | -61.8% |
| Depreciation | 1,629.9 | 1,584.6 | 2.9% | 1,629.8 | 0.0% |
| Interest | 69.8 | 66.6 | 4.8% | 60.9 | 14.6% |
| PBT | 8,238.0 | 8,022.1 | 2.7% | 4,844.1 | 70.1% |
| Tax | 1,992.8 | 1,751.6 | 13.8% | 1,189.0 | 67.6% |
| PAT | 6,245.2 | 6,270.5 | -0.4% | 3,655.1 | 70.9% |
| <i>PAT margins %</i> | <i>7.4</i> | <i>8.4</i> | <i>(100 bps)</i> | <i>6.7</i> | <i>70 bps</i> |
| Exceptional items | - | - | - | - | - |
| Adjusted PAT | 6,245.2 | 6,270.5 | -0.4% | 3,655.1 | 70.9% |
| <i>APAT margins %</i> | <i>7.4</i> | <i>8.4</i> | <i>(100 bps)</i> | <i>6.7</i> | <i>70 bps</i> |

Source: Company, LKP Research

Outlook and Valuation

Hero posted good set of numbers in Q1, led by strong volume performance. Along with the volumes, maintenance of margins was the highlight of the quarter given the cost pressures. Going forward, we expect decent volume trajectory with the XTech variants launches in Q1 and new launches coming up. First EV launch in the festive season will further add to the steam. Demand levers post pandemic are intact with rural story remaining strong on good monsoon. Now that the economy has opened up, normalcy has prevailed and demand is coming back on track.

Due to the pandemic, till now the first time buyers were increasing, but now the replacement demand is also moving up (15-18% of volumes), fuelling the overall demand. Financing has also become easier, which is also a driver for a broad based growth. Also, with a better level of inventory (6-7 weeks), ramping up of production, improving demand, new launches and low base, we expect FY23 to post a double digit growth after a weak FY22. HD agreement would provide a fillip to Hero's ambitions to win a respectable position in the premium range of motorcycles in mid to long term. Hero's recent partnership with Taiwan's Gogoro and 35% stake in Aether Energy to manufacture Electric Scooters and battery swapping platform shall give it a good entry in the EV 2W space. Profitability would improve on price hikes, cost saving programs like LEAP-2, operating leverage stemming from improving volumes, cooling off in the input costs and product mix. We therefore maintain our BUY rating on the stock with an increased target price of ₹3,226.

| All figs in ₹ | Q1 FY23 | Q4 FY22 | Q3 FY22 | Q2 FY22 | Q1 FY 22 | Q4 FY21 | Q3 FY21 | Q2 FY21 |
|--------------------|---------|---------|---------|---------|----------|---------|---------|---------|
| Volumes (mn) | 1.39 | 1.19 | 1.29 | 1.44 | 1.02 | 1.57 | 1.85 | 1.81 |
| Net Realization | 60,370 | 62,417 | 61,018 | 58,760 | 53,558 | 55,384 | 52,977 | 51,620 |
| Material Cost/Unit | 43,932 | 43,248 | 43,301 | 42,474 | 38,843 | 39,005 | 37,345 | 36,700 |
| Staff Cost/Unit | 3,871 | 4,006 | 4,009 | 3,513 | 4,252 | 3,114 | 2,800 | 2,817 |
| Other Expn/Unit | 5,799 | 8,203 | 6,277 | 5,361 | 5,436 | 5,542 | 5,172 | 5,013 |
| Total Expn/Unit | 53,602 | 55,457 | 53,587 | 51,348 | 48,532 | 47,662 | 45,317 | 44,531 |
| EBITDA/unit | 6,767 | 6,960 | 7,431 | 7,412 | 5,026 | 7,723 | 7,660 | 7,089 |
| Net profit /unit | 4,492 | 5,274 | 5,311 | 5,522 | 3,568 | 5,515 | 5,877 | 5,254 |

Source: Company, LKP Research

Income Statement

| (₹ mn) | FY 21 | FY 22 | FY 23E | FY 24E |
|--------------------|---------------|---------------|---------------|---------------|
| Total Revenues | 3,08,006 | 2,92,455 | 3,44,102 | 3,93,825 |
| Raw Material Cost | 2,17,623 | 2,08,267 | 2,42,592 | 2,75,677 |
| Employee Cost | 18,987 | 19,354 | 22,023 | 24,417 |
| Other Exp | 31,203 | 31,145 | 36,475 | 41,745 |
| EBITDA | 40,192 | 33,688 | 43,013 | 51,985 |
| EBITDA Margin(%) | 13.0 | 11.5 | 12.5 | 13.2 |
| Other income | 5799 | 5569 | 3500 | 4000 |
| Depreciation | 6,769 | 6,498 | 6,940 | 7,485 |
| Interest | 218 | 258 | 225 | 67 |
| PBT | 39,004 | 32,501 | 39,348 | 48,433 |
| PBT Margin(%) | 12.7 | 11.1 | 11.4 | 12.3 |
| Exceptional items | 0 | 0 | 0 | 0 |
| Tax | 9,362 | 7,771 | 9,444 | 11,624 |
| PAT | 29,642 | 24,730 | 29,905 | 36,809 |
| PAT Margins (%) | 9.6 | 8.5 | 8.7 | 9.3 |
| Adj PAT | 29,642 | 24,730 | 29,905 | 36,809 |
| Adj PAT Margin (%) | 9.6 | 8.5 | 8.7 | 9.3 |

Key Ratios

| YE Mar | FY 21 | FY 22 | FY 23E | FY 24E |
|---------------------------------|-------|--------|--------|--------|
| Per Share Data (₹) | | | | |
| Adj. EPS | 148.4 | 123.8 | 149.7 | 184.3 |
| CEPS | 182.3 | 156.4 | 184.5 | 221.8 |
| BVPS | 760.9 | 790.1 | 804.0 | 832.2 |
| DPS | 95.0 | 95.0 | 112.3 | 129.0 |
| Growth Ratios(%) | | | | |
| Total revenues | 6.8% | -5.0% | 17.7% | 14.5% |
| EBITDA | 1.5% | -16.2% | 27.7% | 20.9% |
| PAT | 0.3% | -16.6% | 20.9% | 23.1% |
| EPS Growth | 0.3% | -16.6% | 20.9% | 23.1% |
| Valuation Ratios (x) | | | | |
| PE | 18.6 | 22.3 | 18.4 | 15.0 |
| P/CEPS | 15.1 | 17.7 | 15.0 | 12.5 |
| P/BV | 1.9 | 1.8 | 1.8 | 1.7 |
| EV/Sales | 1.8 | 1.9 | 1.6 | 1.4 |
| EV/EBITDA | 12.1 | 14.2 | 12.0 | 9.9 |
| Operating Ratios (Days) | | | | |
| Inventory days | 24.6 | 25.0 | 26.0 | 26.0 |
| Receivable Days | 28.8 | 29.0 | 30.0 | 30.0 |
| Payables day | 61.5 | 63.0 | 64.0 | 64.0 |
| Net Debt/Equity (x) | 0.04 | 0.04 | 0.04 | 0.03 |
| Profitability Ratios (%) | | | | |
| ROCE | 19.2% | 14.9% | 18.0% | 21.3% |
| ROE | 19.5% | 15.7% | 18.6% | 22.1% |
| Dividend yield | 3.4% | 3.4% | 4.1% | 4.7% |

Balance Sheet

| (₹ mn) | FY 21 | FY 22 | FY 23E | FY 24E |
|--------------------------------------|-----------------|-----------------|-----------------|-----------------|
| EQUITY & LIABILITIES | | | | |
| Equity Share Capital | 400 | 400 | 400 | 400 |
| Reserves & Surplus | 1,51,585 | 1,57,430 | 1,60,196 | 1,65,828 |
| Total Networth | 1,51,984 | 1,57,829 | 1,60,595 | 1,66,227 |
| Total debt | 0 | 0 | 0 | 0 |
| Deferred Tax Liability | 6,799 | 6,807 | 6,807 | 6,807 |
| Long term provisions | 1,725 | 1,781 | 1,781 | 1,781 |
| Total non current liabilities | 8,524 | 8,587 | 8,587 | 8,587 |
| Current Liab & Prov | | | | |
| Current liabilities | 51,889 | 42,348 | 46,195 | 48,554 |
| Other liabilities & Provisions | 9,213 | 8,378 | 8,378 | 8,378 |
| Total Equity and Liabilities | 2,21,608 | 2,17,140 | 2,23,753 | 2,31,744 |
| ASSETS | | | | |
| Net block | 52,934 | 50,943 | 48,004 | 45,519 |
| Capital WIP | 5,826 | 5,009 | 7,509 | 9,009 |
| Intangible assets | 5,490 | 6,694 | 6,694 | 6,694 |
| Deferred tax assets | 0 | 0 | 0 | 0 |
| Long term investments | 43,081 | 48,147 | 50,147 | 52,147 |
| Long term loans & advances | 4,037 | 3,825 | 3,825 | 3,825 |
| Other non current assets | 715 | 1,372 | 1,372 | 1,372 |
| Total non-current assets | 1,12,083 | 1,15,990 | 1,17,550 | 1,18,565 |
| Current Assets | | | | |
| Current investments | 61,915 | 58,377 | 58,377 | 58,377 |
| Cash and Bank | 2,572 | 1,751 | 2,605 | 4,082 |
| Inventories | 14,696 | 11,227 | 13,957 | 16,994 |
| Sundry Debtors | 24,268 | 23,043 | 24,511 | 26,974 |
| Loan, Advances & others | 6,079 | 6,753 | 6,753 | 6,753 |
| Other current assets | 230 | 229 | 229 | 229 |
| Total Assets | 2,21,608 | 2,17,140 | 2,23,753 | 2,31,744 |

Cash Flow

| (₹ mn) | FY 21 | FY 22 | FY 23E | FY 24E |
|--|----------------|----------------|----------------|----------------|
| PAT | 29,642 | 24,730 | 29,905 | 36,809 |
| Depreciation | 6,769 | 6,498 | 6,940 | 7,485 |
| Interest | 218 | 780 | 225 | 67 |
| Income Tax paid | -9,759 | -7,688 | -9,444 | -11,624 |
| Chng in working capital | 10,700 | -6,825 | -353 | -3,140 |
| Cash flow from operations (a) | 41,727 | 20,202 | 37,483 | 41,221 |
| Capital expenditure | -5,146 | -5,347 | -6,500 | -6,500 |
| Chng in investments | -14,461 | 3,320 | -2,000 | -2,000 |
| Other investing activities | -2,493 | 508 | 0 | 0 |
| Cash flow from investing (b) | -22,099 | -1,519 | -8,500 | -8,500 |
| Free cash flow (a+b) | 19,628 | 18,683 | 28,983 | 32,721 |
| Inc/dec in borrowings | 0 | 0 | 0 | 0 |
| Dividend paid (incl. tax) | -18,978 | -18,981 | -27,138 | -31,178 |
| Other financing activities | -140 | -208 | -225 | -67 |
| Cash flow from financing (c) | -19,415 | -19,389 | -27,363 | -31,244 |
| Net chng in cash (a+b+c) | 213 | -706 | 1,620 | 1,477 |
| Closing cash & cash equivalents | 1,691 | 985 | 2,605 | 4,082 |

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