

Hero MotoCorp

BUY

Entering into interesting phase - BUY

Summary

Hero Motocorp (HMCL) Q3FY22 results were above our expectations on all counts due to better sales and operating margins. In the medium term, Management remains positive on volume growth front due to a) rural economic recovery and b) opening up of distribution network in urban areas. The Company has lined up huge investments and new product launches in EV segment over next few years. To factor in changing business environment, we have revised our volume and PAT estimates downwards by 11.9%/7.6% and 13.3%/8.9% for FY23 and FY24 respectively. At PER of 13.2x FY24E, we see a favorable risk reward ratio. We rate the stock as BUY with revised price target of Rs3,360 (14x FY24E earnings + Rs485 Associate Value).

Result Highlights and Investment Rationale

- Q3FY22 Result Highlights:** During Q3FY22, HMCL sales declined by 19.4% YoY to Rs78.8bn (our Estimates Rs76.7bn), driven by 30% YoY volume decline and 15.2% increase in average realizations. EBITDA margins contracted by 228bps to 12.2% (Our Estimates 11.3%). PAT declined by 36.7% YoY to Rs6.9bn (Our estimates Rs6.5bn).
- Earning Revision:** To factor in soft business environment, we have lowered our volume estimates by 11.9% and 7.6% for FY23 and FY24 respectively. We have revised our PAT estimates downward by 13.3%/8.9% for FY23 and FY24 respectively.
- Attractive Valuation- BUY:** We expect, HMCL to report 13.4% volume CAGR and 25.9% PAT CAGR over FY22-24E. At CMP of Rs2,718 HMCL stock is quoting at PE of 10.9x FY24E, adjusted to associate values. We rate the stock as BUY with price target of Rs3,360 (14x FY24E earnings + Rs485 Associate Value).

TP	Rs 3,360
CMP	Rs 2,718
Potential upside/downside	+24%
Previous Rating	BUY

Price Performance (%)

	-1m	-3m	-12m
Absolute	5.0	1.3	(22.7)
Rel to Sensex	9.9	5.5	(35.5)

V/s Consensus

EPS (Rs)	FY22E	FY23E	FY24E
IDBI Capital	129	173	205
Consensus	153	186	212
% difference	(15.8)	(6.9)	(3.5)

Key Stock Data

Bloomberg/Reuters	HMCL IN / HROM.BO
Sector	Automobile
Shares o/s (mn)	200
Market cap. (Rs mn)	543,159
3-m daily avg Trd value (Rs mn)	101.4
52-week high / low	Rs3,629 / 2,311
Sensex / Nifty	58,153 / 17,375

Shareholding Pattern (%)

Promoters	34.8
FII	29.6
DII	10.2
Public	25.4

Financial snapshot

(Rs mn)

Year	FY20	FY21	FY22E	FY23E	FY24E
Revenue	2,88,361	3,08,006	3,11,463	3,60,680	4,14,222
Change (yoy, %)	(14)	7	1	16	15
EBITDA	39,580	40,192	35,466	47,085	56,066
Change (yoy, %)	(20)	2	(12)	33	19
EBITDA Margin(%)	13.7	13.0	11.4	13.1	13.5
Adj.PAT	29,559	29,642	25,873	34,527	41,031
EPS (Rs)	148	148	129	173	205
Change (yoy, %)	(13)	0	(13)	33	19
PE(x)	18	18	21	16	13
Dividend Yield (%)	4	4	3	3	4
EV/EBITDA (x)	14	13	15	11	9
RoE (%)	22	21	17	21	22
RoCE (%)	23	23	19	24	26

Source: IDBI Capital Research

Earnings Call Highlights:

- The volume in Q3FY22 at 1.29mn units which includes Global business of 61k units which grew by 16%.
- The management expects broader recovery in the economy in FY23 with opening up of sector which was hit hard by pandemic.
- With the commodities price peaked out, the cost pressure to ease and the price hikes will be taken accordingly with strong rebound to be seen in 2W industry.
- HMCL took price hike of Rs1,000 (ex-showroom) in last week of Sept-21 and Rs 500 (ex-showroom) in Jan -22.
- HMCL is currently in progress to launch its EV manufactured at Chittoor (Andhra Pradesh) plant which is expected by Mar 2022.
- In the recent capital raise, HMCL invested Rs 4.2bn in Ather with shareholding of ~35%.
- Further for Ather Energy, the management will continue to evaluate the EV landscape and proper disclosure of HMCL's stake will be made once the capital round is closed.
- With investments and partnerships with Ather & Gorogo JV (battery swapping platform), HMCL's focus is working towards building the entire EV ecosystem.
- On the EV distribution, HMCL will leverage its existing network strength with manufacturing, sourcing and logistics to scale up the business across the nation.
- HMCL's low market share in scooter will be addressed through EV segment which will lead to penetration in the category.
- The rural India which was hit harder by Covid second wave and delayed monsoon last year is seeing to be bottomed out with gradual recovery expected.
- The Retail inventory level currently at 7 to 8 weeks.
- The replacement share now at 20% compared to pre-pandemic level of nearly 30% with rate of buyer seen increasing from Jan 22.

- The retail purchases in the marriage market were seen inching upwards in Feb 22 with uptake seen in the core markets. The company's share in student's category at 8-10%.
- The capital raise of Rs 20bn done by Hero FinCorp will help to reach the AUM of Rs 500bn from current Rs 260bn.
- The current finance penetration level at 58% with Hero FinCorp's share at 35-40%.

Exhibit 1: Quarterly Snapshot

(Rs mn)	Q3FY22	Q3FY21	YoY (%)	Q2FY22	QoQ (%)
Volumes (in units)	1,292,136	1,845,275	(30.0)	1,438,623	(10.2)
Revenue	78,833	97,758	(19.4)	84,534	(6.7)
Expenditure	69,233	83,621	(17.2)	73,870	(6.3)
<i>as % of sales</i>	<i>87.8</i>	<i>85.5</i>	<i>-</i>	<i>87.4</i>	<i>-</i>
Consumption of RM	55,943	68,912	(18.8)	61,104	(8.4)
<i>as % of sales</i>	<i>71.0</i>	<i>70.5</i>	<i>-</i>	<i>72.3</i>	<i>-</i>
Employee Cost	5,180	5,167	0.3	5,054	2.5
<i>as % of sales</i>	<i>6.6</i>	<i>5.3</i>	<i>-</i>	<i>6.0</i>	<i>-</i>
Other expenditure	8,109	9,543	(15.0)	7,712	5.1
<i>as % of sales</i>	<i>10.3</i>	<i>9.8</i>	<i>-</i>	<i>9.1</i>	<i>-</i>
EBITDA	9,600	14,136	(32.1)	10,664	(10.0)
Depreciation	1,644	1,698	(3.2)	1,639	0.3
EBIT	7,956	12,438	(36.0)	9,025	(11.8)
Other Income	1,216	2,027	(40.0)	1,569	(22.5)
Interest	65	47	40.0	65	(0.5)
PBT	9,107	14,418	(36.8)	10,529	(13.5)
Total Tax	2,246	3,574	(37.2)	2,585	(13.1)
Adjusted PAT	6,861	10,845	(36.7)	7,944	(13.6)
Extra ordinary items Loss/(Gain)	-	-	-	-	-
Reported PAT	6,861	10,845	(36.7)	7,944	(13.6)
Adjusted EPS	34.3	54.3	(36.7)	39.8	(13.6)
Margins (%)			YoY (bps)		QoQ (bps)
EBIDTA	12.2	14.5	(228)	12.6	(44)
EBIT	10.1	12.7	(263)	10.7	(58)
EBT	11.6	14.7	(320)	12.5	(90)
PAT	8.7	11.1	(239)	9.4	(69)
Effective Tax rate	24.7	24.8	(13)	24.5	11

Source: Company; IDBI Capital Research

Exhibit 2: Actual vs. Estimates

Rs mn	Actual	IDBI Est	Var %
Revenue	78,833	76,686	2.8
EBITDA	9,600	8,691	10.5
EBITDA Margin (%)	12.2	11.3	88bps
Adj net income	6,861	6,524	5.2

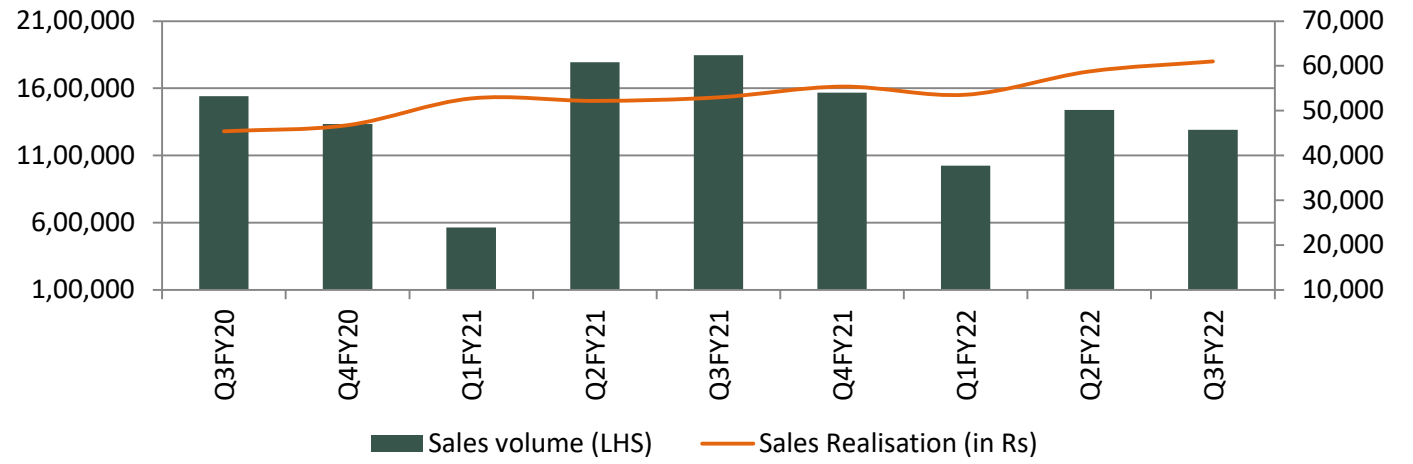
Source: Bloomberg; IDBI Capital Research

Exhibit 3: Change in estimates

(Rs mn)	FY22E			FY23E			FY24E		
	Old	New	% Chg	Old	New	% Chg	Old	New	% Chg
Volumes	5,895,246	5,074,087	(13.9)	6,520,799	5,742,888	(11.9)	7,062,989	6,529,324	(7.6)
Net Sales	3,47,261	3,11,463	(10.3)	3,91,531	3,60,680	(7.9)	4,29,250	4,14,222	(3.5)
EBITDA	44,416	35,466	(20.2)	53,023	47,085	(11.2)	59,172	56,066	(5.2)
EBITDA margin (%)	12.8	11.4	(140)bps	13.5	13.1	(49)bps	13.8	13.5	(25)bps
Net Profit	33,092	25,873	(21.8)	39,829	34,527	(13.3)	45,029	41,031	(8.9)

Source: Company; IDBI Capital Research

Exhibit 4: Quarterly Sales volume and Realisations



Source: Company; IDBI Capital Research

Financial Summary

Profit & Loss Account

(Rs mn)

Year-end: March	FY19	FY20	FY21	FY22E	FY23E	FY24E
Net sales	3,36,505	2,88,361	3,08,006	3,11,463	3,60,680	4,14,222
<i>Change (yoy, %)</i>	4	(14)	7	1	16	15
Operating expenses	(2,87,205)	(2,48,781)	(2,67,814)	(2,75,997)	(3,13,595)	(3,58,156)
EBITDA	49,301	39,580	40,192	35,466	47,085	56,066
<i>Change (yoy, %)</i>	(7)	(20)	2	(12)	33	19
<i>Margin (%)</i>	14.7	13.7	13.0	11.4	13.1	13.5
Depreciation	(6,020)	(8,180)	(6,769)	(6,557)	(6,978)	(7,424)
EBIT	43,281	31,400	33,424	28,908	40,106	48,642
Interest paid	(86)	(220)	(218)	(218)	(218)	(218)
Other income	6,913	7,783	5,799	5,624	6,148	7,024
Pre-tax profit	50,107	38,963	39,004	34,314	46,036	55,448
Tax	(16,259)	(9,404)	(9,362)	(8,441)	(11,509)	(14,416)
<i>Effective tax rate (%)</i>	32.4	24.1	24.0	24.6	25.0	26.0
Minority Interest	-	-	-	-	-	-
Net profit	33,849	29,559	29,642	25,873	34,527	41,031
Exceptional items	-	-	-	-	-	-
Adjusted net profit	33,849	29,559	29,642	25,873	34,527	41,031
<i>Change (yoy, %)</i>	(8)	(13)	0	(13)	33	19
EPS	169	148	148	129	173	205
Dividend per sh	95	97	105	69	92	110
<i>Dividend Payout %</i>	68	79	85	53	53	53

Balance Sheet

(Rs mn)

Year-end: March	FY19	FY20	FY21	FY22E	FY23E	FY24E
Shareholders' funds	1,28,571	1,41,364	1,47,624	1,59,700	1,75,816	1,94,967
Share capital	400	400	400	400	400	400
Reserves & surplus	1,28,172	1,40,965	1,47,225	1,59,301	1,75,416	1,94,568
Total Debt	-	-	-	-	-	-
Other liabilities	(3,028)	827	359	359	359	359
Curr Liab & prov	42,476	40,618	62,473	53,170	60,640	69,248
Current liabilities	40,713	37,929	59,144	49,805	56,742	64,772
Provisions	1,762	2,689	3,328	3,366	3,897	4,476
Total liabilities	39,448	41,445	62,832	53,529	60,999	69,607
Total equity & liabilities	1,68,019	1,82,809	2,10,456	2,13,230	2,36,814	2,64,574
Net fixed assets	51,604	61,782	50,350	51,792	53,814	55,390
Investments	59,686	82,227	1,04,997	1,04,997	1,04,997	1,04,997
Other non-curr assets	-	-	-	-	-	-
Current assets	56,729	38,801	55,110	56,441	78,004	1,04,188
Inventories	10,724	10,920	14,696	15,207	17,367	19,889
Sundry Debtors	28,216	16,031	24,268	19,522	21,619	23,693
Cash and Bank	1,365	2,419	2,572	7,984	23,121	42,349
Loans and advances	850	896	892	902	1,044	1,199
Total assets	1,68,019	1,82,809	2,10,456	2,13,230	2,36,814	2,64,574

Cash Flow Statement

(Rs mn)

Year-end: March	FY19	FY20	FY21	FY22E	FY23E	FY24E
Pre-tax profit	50,107	38,963	39,004	34,314	46,036	55,448
Depreciation	6,020	8,180	6,769	6,557	6,978	7,424
Tax paid	(16,259)	(9,404)	(9,362)	(8,441)	(11,509)	(14,416)
Chg in working capital	(20,270)	17,124	5,699	(5,221)	1,044	3,857
Other operating activities	248	5,337	113	-	-	-
Cash flow from operations (a)	19,847	60,200	42,222	27,209	42,549	52,313
Capital expenditure	(7,173)	(13,066)	4,083	(8,000)	(9,000)	(9,000)
Chg in investments	10,244	(22,540)	(22,770)	-	-	-
Other investing activities	-	-	-	-	-	-
Cash flow from investing (b)	3,071	(35,606)	(18,688)	(8,000)	(9,000)	(9,000)
Equity raised/(repaid)	(93)	(215)	1,900	-	-	-
Debt raised/(repaid)	-	-	-	-	-	-
Dividend (incl. tax)	(22,874)	(23,325)	(25,282)	(13,797)	(18,412)	(21,880)
Chg in minorities	-	-	-	-	-	-
Other financing activities	-	-	-	-	-	-
Cash flow from financing (c)	(22,966)	(23,540)	(23,382)	(13,797)	(18,412)	(21,880)
Net chg in cash (a+b+c)	(49)	1,054	153	5,412	15,138	21,433

Financial Ratios

Year-end: March	FY19	FY20	FY21	FY22E	FY23E	FY24E
Book Value (Rs)	644	708	739	799	880	976
Adj EPS (Rs)	169	148	148	129	173	205
Adj EPS growth (%)	-8	-13	0	-13	33	19
EBITDA margin (%)	15	14	13	11	13	14
Pre-tax margin (%)	14.9	13.5	12.7	11.0	12.8	13.4
Net Debt/Equity (x)	0.0	0.0	0.0	0.0	(0.1)	(0.2)
ROCE (%)	35	23	23	19	24	26
ROE (%)	27	22	21	17	21	22

DuPont Analysis

Asset turnover (x)	2.0	1.6	1.6	1.5	1.6	1.7
Leverage factor (x)	1.3	1.3	1.4	1.4	1.3	1.4
Net margin (%)	10.1	10.3	9.6	8.3	9.6	9.9

Working Capital & Liquidity ratio

Inventory days	12	14	17	18	18	18
Receivable days	31	20	29	23	22	21
Payable days	43	44	71	56	56	57

Valuations

Year-end: March	FY19	FY20	FY21	FY22	FY23E	FY24E
PER (x)	16	18	18	21	16	13
Price/Book value (x)	4.2	3.8	3.7	3.4	3.1	2.8
EV/Net sales (x)	2	2	2	2	1	1
EV/EBITDA (x)	11	14	13	15	11	9
Dividend Yield (%)	3	4	4	3	3	4

Source: Company; IDBI Capital Research



Notes

Dealing

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Key to Ratings Stocks:**BUY:** 15%+; **HOLD:** -5% to 15%; **SELL:** -5% and below.**IDBI Capital Markets & Securities Ltd.****Equity Research Desk**

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