

HERO MOTOCORP LIMITED | Auto & Auto Components

Macros remain intact for a recovery in FY23

LKP

Hero reported weak set of numbers in Q4, which were in-line with our expectations of a steep volume decline of 24.2% yoy and 8% qoq to 1.19 mn units. Topline de-grew by 15% yoy and 5.9% to ₹74.2 bn as realizations supported them by growing 12.7% yoy mainly on price hikes taken in Q4 and product mix. The demand in Q4 was weak as Wave#3 of covid impacted for a short while and higher cost of acquisition. Input costs to sales ratio in Q4 was at 69.3%, down from 71% qoq and 70.4% yoy. Other expenses to sales as well as employee costs to sales grew to 13.1% and 6.4% yoy respectively as higher CSR expenses (80-100 bps impact on margins) during the quarter impacted the former. Due to this expense, EBITDA margins dropped to 11.2% down from 13.9% yoy and 12.2% qoq. As depreciation expenses remained flat yoy, and other income grew by 60% yoy, PBT fall was arrested to 29% yoy while PAT fell by 28% as tax rate was at 22%. During the full year, topline fell by 5% while EBITDA margins fell to 11.5% down from 13% in FY21, while PAT declined by 16.6% at ₹24.73bn.

Demand drivers remain intact in mid to long term despite short term blip

Post weak numbers observed in Q4 FY22, demand seems to have started picking up in April as entry level bikes are finding a robust demand amidst marriage season in some parts of the country. The company is gaining strength in the scooters segment as well with increasing market share yoy. In the entry level, HF Deluxe is attracting strong demand taking up the market share to 74% at the end of March. It was 62.5% for full year, while by the end of April it is 68.5%. In the executive segment as well Splendor, Glamour and its new variant(prices at 7-10% higher than their base variants) is performing robustly. 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 expected to pan out well this year as well. Rabi harvest has been bumper and the marriage season is back to total normalcy after a gap of two years. Therefore management expects robust sales till July and beyond that, the theme of underpenetrated markets of country and mobility should continue to play well. On the EV side, Hero will launch an EV scooter in FY22 in partnership with Gogoro and also their own product (capex of ₹4.2 bn o/w ₹1.5 bn was spent in Q4).

Key Financials	FY 21	FY 22	FY 23E	FY 24E
Revenues (₹ bn)	308	292	347	413
EBITDA (%)	13.0	11.5	12.5	13.1
PAT (%)	9.6	8.5	9.2	9.8
EPS (₹)	148.4	123.8	160.3	201.9
EPS growth (%)	0.3%	-16.6%	29.5%	25.9%
P/E (x)	16.8	20.1	15.5	12.3
P/B (x)	1.9	1.8	1.8	1.7
EV/EBITDA (x)	10.9	12.8	10.3	8.4
ROCE (%)	19.2%	14.9%	19.2%	23.1%
ROE (%)	19.5%	15.7%	19.9%	24.1%
Dividend yield (%)	3.8%	3.8%	4.8%	5.7%

Rating	Buy
Current Market Price (₹)	2,418
12 M Price Target (₹)	2,826
Potential upside (%)	17

Stock Data

FV (₹) :	2
Total Market Cap (₹ bn) :	483
Free Float Market Cap (₹ bn) :	323
52-Week High / Low (₹) :	3,090 / 2,147
2-Year High / Low (₹) :	3,629 / 1,933
1 Yr Avg. Dly Traded Volume (in lakh)	7
BSE Code / NSE Symbol	50018 / HEROMOTOCO
Bloomberg :	HMCL IN

Shareholding Pattern

(%)	Mar-22	Dec-21	Sep-21	Jun-21
Promoter	34.75	34.75	34.76	34.76
FPIs	29.22	29.57	32.28	34.97
MFs	8.71	8.43	7.38	6.29
Insurance	13.79	13.83	13.40	12.64
Others	13.53	13.42	12.18	11.34

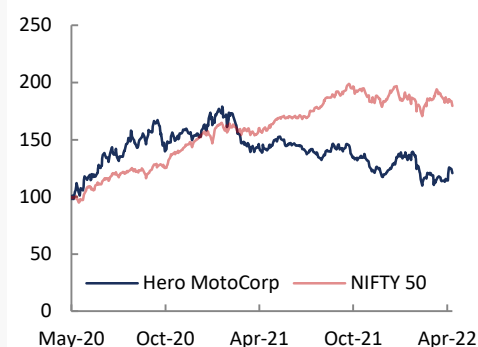
Source: BSE

Price Performance

(%)	1M	3M	6M	1YR
Hero Motocorp	4.6%	-11.2%	-9.7%	-12.9%
Nifty 50	-7.6%	-4.8%	-6.9%	15.0%

* To date / current date : May 04, 2022

Hero Motocorp vs Nifty 50



LEAP-2 and price hikes to arrest decline in margins

Hero's EBITDA margins in Q4 came down to 11.2% on a sharp rise in other expenses. However, the company reported strong gross margin performance on commodity costs softening in Q4. The company took price hikes to the tune of ₹1000 per vehicle in April. The company under the LEAP program is quite aggressive in saving employee costs and other expenses by 300 bps during the quarter. These steps shall help the company to achieve its margin target of 14-15%, despite commodity headwinds. Secondly, premiumisation of bikes with the help of global partner Harley Davidson shall help the product mix to improve further. Price hikes combined with superior product mix and better operating leverage should help margin growth. FY22 margins were at 11.5%, while in FY23E/FY24E, we expect them to rise up to 12.5%/13.1% respectively.

Quarterly Financial Snapshot

YE Mar (₹ mn)	Q4 FY22	Q3 FY21	% qoq	Q4 FY21	% yoy
Total net sales	74,217.3	78,832.7	-5.9%	86,859.7	-14.6%
RM cost	51,424.4	55,943.2	-8.1%	61,172.7	-15.9%
Employee cost	4,763.3	5,180.0	-8.0%	4,884.4	-2.5%
Other expenses	9,753.9	8,109.4	20.3%	8,691.1	12.2%
EBITDA	8,275.7	9,600.1	-13.8%	12,111.5	-31.7%
<i>EBITDA Margins (%)</i>	<i>11.2</i>	<i>12.2</i>	<i>(100 bps)</i>	<i>13.9</i>	<i>(270 bps)</i>
Other income	1,397.6	1,216.3	14.9%	873.8	59.9%
Depreciation	1,584.6	1,644.0	-3.6%	1,631.2	-2.9%
Interest	66.6	65.1	2.3%	62.9	5.9%
PBT	8,022.1	9,107.3	-11.9%	11,291.2	-29.0%
Tax	1,751.6	2,245.6	-22.0%	2,641.5	-33.7%
PAT	6,270.5	6,861.7	-8.6%	8,649.7	-27.5%
<i>PAT margins (%)</i>	<i>8.4</i>	<i>8.7</i>	<i>30 bps</i>	<i>10.0</i>	<i>(160 bps)</i>
Exceptional items	-	-	N/A	-	N/A
Adjusted PAT	6,270.5	6,861.7	-8.6%	8,649.7	-27.5%
<i>APAT margins (%)</i>	<i>8.4</i>	<i>8.7</i>	<i>30 bps</i>	<i>10.0</i>	<i>460 bps</i>

Source: Company, LKP Research

Outlook and Valuation

Hero posted robust weak set of numbers in Q4, which were in line with expectations. However we witnessed strong bounce back in gross margins (30.7% vs 29.6% yoy and 29% qoq) which was a very positive sign. Going forward, we expect strong bounce back in Q1 and thereafter as we believe the pandemic is behind us and normalcy has prevailed. Demand levers post pandemic are intact with rural story remaining strong. Also the radical shift to personal mobility from shared mobility is leading the demand. Due to this till now the first time buyers were increasing, but now the replacement demand is also moving up, 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 solid 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, although in mid to long term. Hero's recent partnership with Taiwan's Gogoro to manufacture Electric Scooters and battery swapping platform shall give Hero the first mover advantage in the EV 2W space. New launch of 2 EVs (one from Gogoro and another made by Hero itself) in FY23 shall provide fillip to the EV strategy of Hero. Profitability would improve on price hikes, cost saving programs like LEAP-2, capex reduction and operating leverage stemming from improving volumes and product mix despite input costs hikes. We therefore maintain our BUY rating on the stock with a target price of ₹2,826. The company has also announced a healthy dividend of ₹95/share (payout ratio of 77%).

All figs in ₹	Q4 FY22	Q3 FY22	Q2 FY22	Q1 FY 22	Q4 FY21	Q3 FY21	Q2 FY21	Q1 FY21
Volumes (mn)	1.19	1.29	1.44	1.02	1.57	1.85	1.81	0.56
Net Realization	62,417	61,018	58,760	53,558	55,384	52,977	51,620	52,740
Material Cost/Unit	43,248	43,301	42,474	38,843	39,005	37,345	36,700	37,164
Staff Cost/Unit	4,006	4,009	3,513	4,252	3,114	2,800	2,817	6,787
Other Expn/Unit	8,203	6,277	5,361	5,436	5,542	5,172	5,013	6,872
Total Expn/Unit	55,457	53,587	51,348	48,532	47,662	45,317	44,531	50,823
EBITDA/unit	6,960	7,431	7,412	5,026	7,723	7,660	7,089	1,917
Net profit /unit	5,274	5,311	5,522	3,568	5,515	5,877	5,254	1,087

Source: Company, LKP Research

Income Statement

(₹ mn)	FY 21	FY 22	FY 23E	FY 24E
Total Revenues	3,08,006	2,92,455	3,47,436	4,12,789
Raw Material Cost	2,17,623	2,08,267	2,45,637	2,90,191
Employee Cost	18,987	19,354	22,236	25,593
Other Exp	31,203	31,145	36,133	42,930
EBITDA	40,192	33,688	43,430	54,075
<i>EBITDA Margin(%)</i>	<i>13.0</i>	<i>11.5</i>	<i>12.5</i>	<i>13.1</i>
Other income	5799	5569	5200	5600
Depreciation	6,769	6,498	6,279	6,564
Interest	218	258	225	67
PBT	39,004	32,501	42,126	53,045
<i>PBT Margin(%)</i>	<i>12.7</i>	<i>11.1</i>	<i>12.1</i>	<i>12.9</i>
Exceptional items	0	0	0	0
Tax	9,362	7,771	10,110	12,731
PAT	29,642	24,730	32,016	40,314
<i>PAT Margins (%)</i>	<i>9.6</i>	<i>8.5</i>	<i>9.2</i>	<i>9.8</i>
Adj PAT	29,642	24,730	32,016	40,314
<i>Adj PAT Margin (%)</i>	<i>9.6</i>	<i>8.5</i>	<i>9.2</i>	<i>9.8</i>

Key Ratios

YE Mar	FY 21	FY 22	FY 23E	FY 24E
Per Share Data (₹)				
Adj. EPS	148.4	123.8	160.3	201.9
CEPS	182.3	156.4	191.8	234.7
BVPS	760.9	790.1	805.0	835.8
DPS	95.0	95.0	120.2	141.3
Growth Ratios (%)				
Total revenues	6.8%	-5.0%	18.8%	18.8%
EBITDA	1.5%	-16.2%	28.9%	24.5%
PAT	0.3%	-16.6%	29.5%	25.9%
EPS Growth	0.3%	-16.6%	29.5%	25.9%
Valuation Ratios (x)				
PE	16.8	20.1	15.5	12.3
P/CEPS	13.6	15.9	13.0	10.6
P/BV	1.9	1.8	1.8	1.7
EV/Sales	1.6	1.7	1.4	1.2
EV/EBITDA	10.9	12.8	10.3	8.4
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%	19.2%	23.1%
ROE	19.5%	15.7%	19.9%	24.1%
Dividend yield	3.8%	3.8%	4.8%	5.7%

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	1,60,391	1,66,559
Total Networth	1,51,984	1,57,829	1,60,791	1,66,959
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	46,642	50,892
Other liabilities & Provisions	9,213	8,378	8,378	8,378
Total Equity and Liabilities	2,21,608	2,17,140	2,24,396	2,34,814
ASSETS				
Net block	52,934	50,943	48,665	47,101
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	1,18,211	1,20,147
Current Assets				
Current investments	61,915	58,377	58,377	58,377
Cash and Bank	2,572	1,751	2,174	3,375
Inventories	14,696	11,227	14,133	17,888
Sundry Debtors	24,268	23,043	24,749	28,273
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	2,24,396	2,34,814

Cash Flow

(₹ mn)	FY 21	FY 22	FY 23E	FY 24E
PAT	29,642	24,730	32,016	40,314
Depreciation	6,769	6,498	6,279	6,564
Interest	218	780	225	67
Income Tax paid	-9,759	-7,688	-10,110	-12,731
Chng in working capital	10,700	-6,825	-318	-3,031
Cash flow from operations (a)	41,727	20,202	38,968	43,914
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	30,468	35,414
Inc/dec in borrowings	0	0	0	0
Dividend paid (incl. tax)	-18,978	-18,981	-29,054	-34,146
Other financing activities	-140	-208	-225	-67
Cash flow from financing (c)	-19,415	-19,389	-29,279	-34,213
Net chng in cash (a+b+c)	213	-706	1,189	1,201
Closing cash & cash equivalents	1,691	985	2,174	3,375

DISCLAIMERS AND DISCLOSURES

LKP Sec. Ltd. (CIN-L67120MH1994PLC080039, www.lkpsec.com) and its affiliates are a full-fledged, brokerage and financing group. LKP was established in 1992 and is one of India's leading brokerage and distribution house. LKP is a corporate trading member of Bombay Stock Exchange Limited (BSE), National Stock Exchange of India Limited (NSE), MCX Stock Exchange Limited (MCX-SX). LKP along with its subsidiaries offers the most comprehensive avenues for investments and is engaged in the businesses including stock broking (Institutional and retail), merchant banking, commodity broking, depository participant, insurance broking and services rendered in connection with distribution of primary market issues and financial products like mutual funds etc.

LKP hereby declares that it has not defaulted with any stock exchange nor its activities were suspended by any stock exchange with whom it is registered in last five years. However, SEBI and Stock Exchanges have conducted the routine inspection and based on their observations have issued advice letters or levied minor penalty on LKP for certain operational deviations in ordinary/routine course of business. LKP has not been debarred from doing business by any Stock Exchange / SEBI or any other authorities; nor has its certificate of registration been cancelled by SEBI at any point of time.

LKP offers research services to clients. The analyst for this report certifies that all of the views expressed in this report accurately reflect his or her personal views about the subject company or companies and its or their securities, and no part of his or her compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this report.

Other disclosures by LKP and its Research Analyst under SEBI (Research Analyst) Regulations, 2014 with reference to the subject company(s) covered in this report:-

Research Analyst or his/her relative's financial interest in the subject company. (NO)

LKP or its associates may have financial interest in the subject company.

LKP or its associates and Research Analyst or his/her relative's does not have any material conflict of interest in the subject company. The research Analyst or research entity (LKP) has not been engaged in market making activity for the subject company.

LKP or its associates may have actual/beneficial ownership of 1% or more securities of the subject company at the end of the month immediately preceding the date of publication of Research Report.

Research Analyst or his/her relatives have actual/beneficial ownership of 1% or more securities of the subject company at the end of the month immediately preceding the date of publication of Research Report: (NO)

LKP or its associates may have received any compensation including for investment banking or merchant banking or brokerage services from the subject company in the past 12 months.

LKP or its associates may have received compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past 12 months.

LKP or its associates may have received any compensation or other benefits from the Subject Company or third party in connection with the research report.

Subject Company may have been client of LKP or its associates during twelve months preceding the date of distribution of the research report and LKP may have co-managed public offering of securities for the subject company in the past twelve months.

Research Analyst has served as officer, director or employee of the subject company: (NO)

LKP and/or its affiliates may seek investment banking or other business from the company or companies that are the subject of this material. Our salespeople, traders, and other professionals may provide oral or written market commentary or trading strategies to our clients that reflect opinions that are contrary to the opinions expressed herein, and our proprietary trading and investing businesses may make investment decisions that may be inconsistent with the recommendations expressed herein.

In reviewing these materials, you should be aware that any or all of the foregoing, among other things, may give rise to real or potential conflicts of interest including but not limited to those stated herein. Additionally, other important information regarding our relationships with the company or companies that are the subject of this material is provided herein. This report is not directed to, or intended for distribution to or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction where such distribution, publication, availability or use would be contrary to law or regulation or which would subject LKP or its group companies to any registration or licensing requirement within such jurisdiction. Specifically, this document does not constitute an offer to or solicitation to any U.S. person for the purchase or sale of any financial instrument or as an official confirmation of any transaction to any U.S. person.

Unless otherwise stated, this message should not be construed as official confirmation of any transaction. No part of this document may be distributed in Canada or used by private customers in United Kingdom.

All trademarks, service marks and logos used in this report are trademarks or registered trademarks of LKP or its Group Companies. The information contained herein is not intended for publication or distribution or circulation in any manner whatsoever and any unauthorized reading, dissemination, distribution or copying of this communication is prohibited unless otherwise expressly authorized. Please ensure that you have read "Risk Disclosure Document for Capital Market and Derivatives Segments" as prescribed by Securities and Exchange Board of India before investing in Indian Securities Market. In so far as this report includes current or historic information, it is believed to be reliable, although its accuracy and completeness cannot be guaranteed.

All material presented in this report, unless specifically indicated otherwise, is under copyright to LKP. None of the material, nor its content, nor any copy of it, may be altered in any way, transmitted to, copied or distributed to any other party, without the prior express written permission of LKP.