

Q3FY2012 Review  
 Sector: Automobiles  
 BSE Sensex: 16,644

## HERO MOTOCORP

 Maintain ACCUMULATE  
 CMP Rs1,901  
 TP Rs2,101

### Volume Growth Continues To Drive Profit

Hero MotoCorp (HMCL) Q3FY12 results were a tad below our estimate with lower than expected realisations. Average realisations at Rs37.9k/unit were up 0.5% sequentially as against our estimate of 1.0% growth. This in tandem with a 1.1% QoQ increase in raw material cost per vehicle impacted margins to the extent of 10bps. Thus, despite a lower than expected tax rate, net profits at Rs6.13bn were 1% lower than our estimate of Rs6.2bn.

**Market leader sets the pace, expands marketshare:** HMCL beat peers Bajaj Auto and TVS Motor with a domestic motorcycle segment volume growth of 10.7% as compared to 7.3% for Bajaj Auto and a 12% decline for TVS Motor. This enabled the company to expand its marketshare by 125bps QoQ to 56.2%. Exports too received a leg-up growing 19.7% to 46k units. Scooter sales continue to do well despite capacity expansion by market leader Honda Motorcycle & Scooters India. Overall volumes were up 11.3% YoY to 1.59mn units, highest ever for the company. The capacity expansion enabled the company produce 560k units in the month of December alone.

**Realisations disappoint, Raw material cost increases:** Average realisations during the quarter were up 0.5% QoQ to Rs37.9k/unit, against our estimate of Rs38.1k/unit. The increase in raw material cost per vehicle at 1.1% QoQ outpaced the growth in realisation, thus adversely impacting margins by 10bps QoQ to 15.6% (PINCe 15.9%). EBITDA per vehicle was flat QoQ at Rs5.9k/unit.

**Lower tax rate:** Depreciation charge for the quarter rose 7.2% sequentially to Rs3.0bn on account of the decline in the rupee vis-a-vis the Japanese yen. Increased contribution from the tax exempt Haridwar facility helped in lowering of tax rate for the quarter by 140bps QoQ to 15.3%. However, despite the benefit of a lower tax rate, the underperformance at the EBITDA level led to a lower net profit of Rs6.13bn.

**Outlook:** HMCL has demonstrated its ability to post a double digit volume growth despite the high base. We have increased our volume estimate for FY12 and FY13 by 2.9% and 1.2% to 6.2mn and 6.9mn units respectively. This has led to an upward revision in our FY12 and FY13 earnings estimate by 5% and 2.2% to Rs119.9 and Rs135.5 respectively. We also introduce FY14 earnings estimate of Rs142.2.

### VALUATIONS AND RECOMMENDATION

The stock is currently trading at 14.0x its FY13E earnings. We see limited upside from the current levels and reiterate an 'ACCUMULATE' rating on the stock with a revised target price of Rs2,101 (earlier Rs2,055) discounting FY13E earnings 15.5x.

KEY FINANCIALS						(Rs mn)
	FY10	FY11	FY12E	FY13E	FY14E	
Net Sales	157,582	192,450	233,898	263,034	292,394	
YoY Gr.(%)	27.9	22.1	21.5	12.5	11.2	
EBITDA	27,705	26,288	36,341	40,797	45,610	
EBITDA margin (%)	17.5	13.5	15.4	15.4	15.5	
Adjusted Net Profit	22,318	19,838	23,936	27,065	28,398	
YoY Gr.(%)	74.1	(11.1)	20.7	13.1	4.9	
KEY RATIOS						
Dil. EPS (Rs)	111.8	99.3	119.9	135.5	142.2	
ROCE (%)	73.4	59.6	61.5	63.9	58.3	
RoE (%)	61.4	61.8	67.1	56.0	45.8	
PER (x)	17.0	19.1	15.9	14.0	13.4	
EV/Net sales (x)	2.0	1.8	1.4	1.2	1.1	
EV/EBDITA (x)	11.6	13.0	9.3	8.0	6.8	

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### QUARTERLY SNAPSHOT (Rs mn)

	Quarter Ended		
	Jun-11	Sep-11	Dec-11
Net Sales	56,833	58,293	60,315
YoY Gr. (%)	32.3	28.1	16.9
EBITDA	8,178	9,187	9,430
EBITDA Mar %	14.4	15.8	15.6
Adj. Net Profit	5,579	6,036	6,130
YoY Gr. (%)	13.5	19.4	26.4

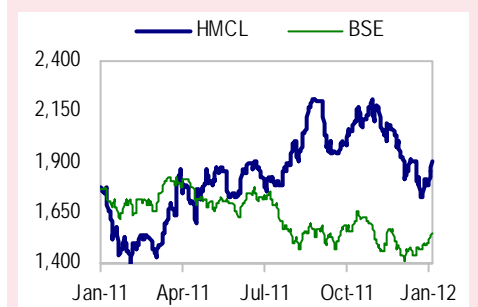
### STOCK DATA

Market Cap	Rs379.6bn
Book Value per share	Rs148
Eq Shares O/S (F.V. Rs2)	200mn
Free Float	47.8%
Avg Traded Val. (6 mnths)	Rs1.23bn
52 w week High/Low	Rs2248/1378
Bloomberg Code	HMCL IN
Reuters Code	HROM.BO

### PERFORMANCE (%)

	1M	3M	12M
Absolute	(0.5)	(6.3)	7.8
Relative	(8.7)	(4.6)	20.1

### RELATIVE PERFORMANCE



**Variance to PINC Estimate**

(Rs mn)	Actual	Estimate	Var (%)	Comments
Net Sales	60,315	60,604	(0.5)	Lower realisations
EBITDA	9,430	9,608	(1.9)	
EBITDA Margin (%)	15.6	15.9	(20)bps	Lower realisation coupled with higher input cost
Adjusted PAT	6,130	6,190	(1.0)	Lower tax rate helps in limiting underperformance

**Financial Table**

(Rs mn)	Dec-11	Dec-10	YoY (%)	Sep-11	QoQ (%)	9MFY12	9MFY11	YoY (%)
<b>Net Sales</b>	<b>60,315</b>	<b>51,617</b>	<b>16.9</b>	<b>58,293</b>	<b>3.5</b>	<b>175,441</b>	<b>140,102</b>	<b>25.2</b>
<b>EBITDA</b>	<b>9,430</b>	<b>5,766</b>	<b>63.5</b>	<b>9,187</b>	<b>2.6</b>	<b>26,795</b>	<b>17,871</b>	<b>49.9</b>
<i>EBITDA Margins %</i>	<i>15.6</i>	<i>11.2</i>	<i>450bps</i>	<i>15.8</i>	<i>(10)bps</i>	<i>15.3</i>	<i>12.8</i>	<i>250bps</i>
Other Income	763	620	23.0	798	(4.4)	2,444	1,938	26.1
Interest	(32)	(52)	(39.1)	(45)	(29.2)	(109)	(100)	9.1
Depreciation	2,987	560	433.7	2,785	7.2	8,169	1,650	395.1
PBT	7,238	5,879	23.1	7,245	(0.1)	21,178	18,258	16.0
Tax	1,108	1,030	7.6	1,208	(8.3)	3,433	3,436	(0.1)
% PBT	15.3	17.5	(220)bps	16.7	(140)bps	16.2	18.8	(260)bps
<b>PAT</b>	<b>6,130</b>	<b>4,849</b>	<b>26.4</b>	<b>6,036</b>	<b>1.6</b>	<b>17,745</b>	<b>14,822</b>	<b>19.7</b>
Exception Item (Net)	-	(559)		-		-	(559)	
<b>Reported PAT</b>	<b>6,130</b>	<b>4,290</b>	<b>42.9</b>	<b>6,036</b>	<b>1.6</b>	<b>17,745</b>	<b>14,263</b>	<b>24.4</b>
<b>Adjusted EPS (Rs)</b>	<b>30.7</b>	<b>24.3</b>	<b>26.4</b>	<b>30.2</b>	<b>1.6</b>	<b>88.9</b>	<b>74.2</b>	<b>19.7</b>

**Vehicle sales**

(units)	Dec-11	Dec-10	YoY (%)	Sep-11	QoQ (%)	9MFY12	9MFY11	YoY (%)
<b>Total 2-Wheelers</b>	<b>1,589,276</b>	<b>1,428,030</b>	<b>11.3</b>	<b>1,544,315</b>	<b>2.9</b>	<b>4,663,168</b>	<b>3,948,013</b>	<b>18.1</b>
Domestic	1,543,212	1,389,551	11.1	1,504,470	2.6	4,538,844	3,844,614	18.1
Exports	46,064	38,479	19.7	39,845	15.6	124,324	103,399	20.2
<b>Motorcycles</b>	<b>1,474,815</b>	<b>1,332,941</b>	<b>10.6</b>	<b>1,436,759</b>	<b>2.6</b>	<b>4,335,367</b>	<b>3,695,779</b>	<b>17.3</b>
Domestic	1,438,160	1,299,110	10.7	1,407,172	2.2	4,238,702	3,604,308	17.6
Exports	36,655	33,831	8.3	29,587	23.9	96,665	91,471	5.7
<b>Scooters</b>	<b>114,461</b>	<b>95,089</b>	<b>20.4</b>	<b>107,556</b>	<b>6.4</b>	<b>327,801</b>	<b>252,234</b>	<b>30.0</b>
Domestic	105,052	90,441	16.2	97,298	8.0	300,142	240,306	24.9
Exports	9,409	4,648	102.4	10,258	(8.3)	27,659	11,928	131.9

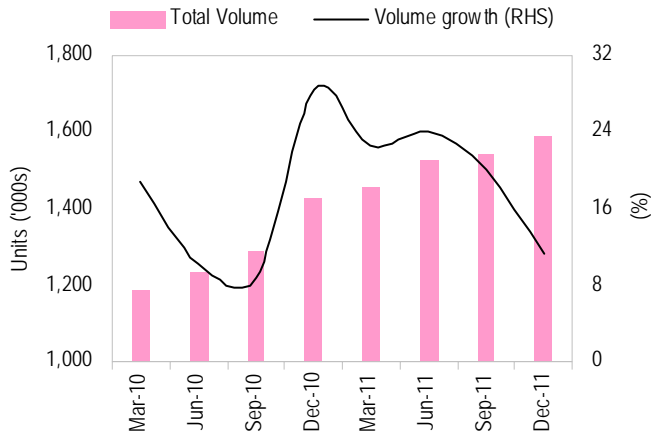
**(%) of Sales**

(%)	Dec-11	Dec-10	YOY (bps)	Sep-11	QoQ (bps)	9MFY12	9MFY11	YOY (bps)
Material Cost	72.9	73.9	(100)	72.5	40	73.3	72.7	60
Staff Cost	3.3	3.0	30	3.1	20	3.1	3.2	(10)
Other Expenses	8.2	11.9	(370)	8.7	(50)	8.3	11.3	(300)
<b>EBITDA Margins</b>	<b>15.6</b>	<b>11.2</b>	<b>450</b>	<b>15.8</b>	<b>(10)</b>	<b>15.3</b>	<b>12.8</b>	<b>250</b>

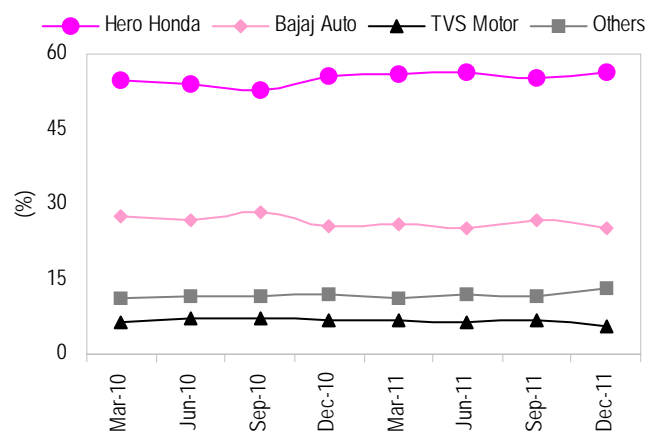
**Per Vehicle**

(Rs)	Dec-11	Dec-10	YoY (%)	Sep-11	QoQ (%)	9MFY12	9MFY11	YoY (%)
Realisations	37,951	36,145	5.0	37,747	0.5	37,623	35,487	6.0
Material cost	27,653	26,714	3.5	27,350	1.1	27,585	25,796	6.9
Staff cost	1,254	1,093	14.7	1,161	8.0	1,165	1,142	2.0
Other Expenses	3,110	4,301	(27.7)	3,286	(5.3)	3,127	4,022	(22.3)
<b>EBITDA</b>	<b>5,933</b>	<b>4,038</b>	<b>47.0</b>	<b>5,949</b>	<b>(0.3)</b>	<b>5,746</b>	<b>4,526</b>	<b>26.9</b>

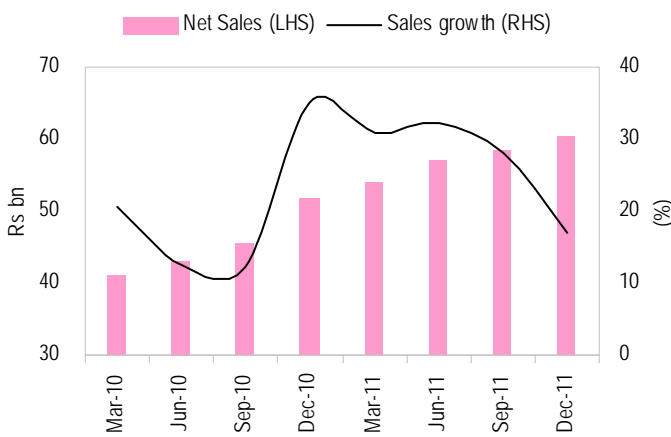
Sales Volume Trend



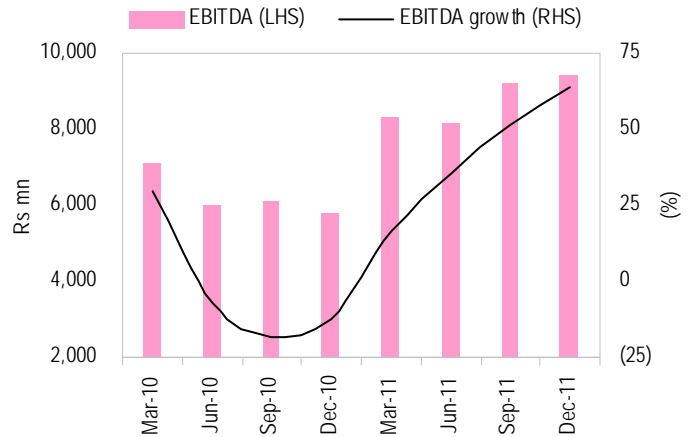
Domestic Motorcycle Marketshare



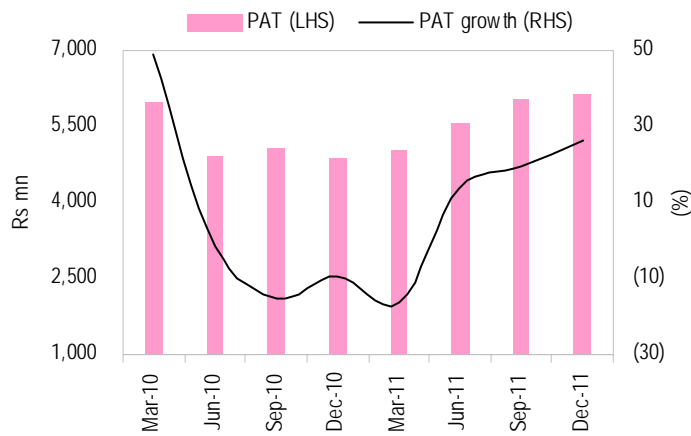
Net Sales



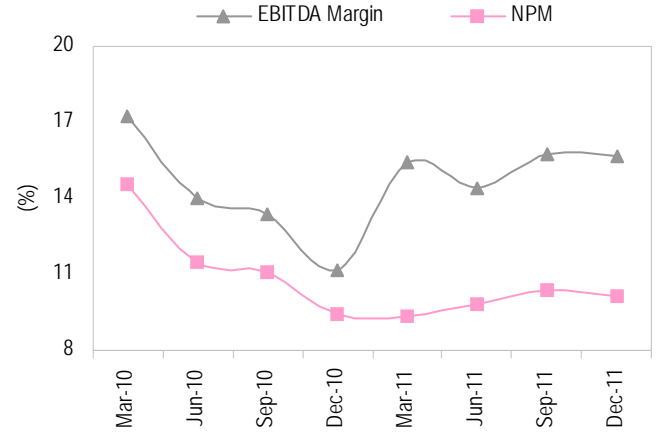
Operating Profits



Net Profits



Profitability Trend



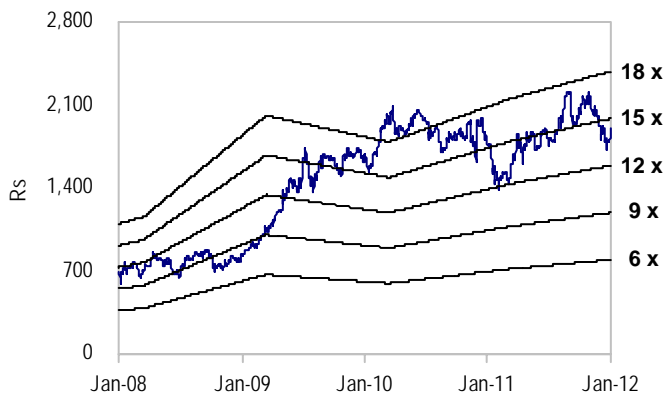
Income Statement	FY10	FY11	FY12E	FY13E	FY14E
Net Sales	157,582	192,450	233,898	263,034	292,394
Growth (%)	27.9	22.1	21.5	12.5	11.2
Operating profit	26,682	24,727	34,713	39,017	43,662
Other operating income	1,023	1,561	1,628	1,781	1,948
EBITDA	27,705	26,288	36,341	40,797	45,610
Growth (%)	56.8	(5.1)	38.2	12.3	11.8
Depreciation	(1,915)	(4,024)	(11,087)	(11,584)	(12,433)
Other income	2,548	2,740	3,431	4,015	4,707
EBIT	28,338	25,004	28,685	33,229	37,884
Interest paid	(21)	(158)	(20)	(20)	(20)
PBT (before E/o items)	28,317	24,846	28,665	33,209	37,864
Tax provision	(5,999)	(5,008)	(4,730)	(6,144)	(9,466)
E/o Income / (loss)	-	(559)	-	-	-
Net profit	22,318	19,279	23,936	27,065	28,398
Adjusted net profit	22,318	19,838	23,936	27,065	28,398
Growth (%)	74.1	(11.1)	20.7	13.1	4.9
Diluted EPS (Rs)	111.8	99.3	119.9	135.5	142.2
Diluted EPS Growth (%)	74.1	(11.1)	20.7	13.1	4.9

Cash Flow Statement	FY10	FY11	FY12E	FY13E	FY14E
Pre-tax profit	28,317	24,287	28,665	33,209	37,864
Depreciation	1,496	3,660	11,087	11,584	12,433
Total tax paid	(5,622)	(4,605)	(4,303)	(5,994)	(9,316)
Chg in working capital	4,975	10,101	2,263	(6,615)	1,196
Other operating activities	-	-	-	-	-
Cash flow from oper. (a)	29,166	33,443	37,712	32,185	42,177
Capital expenditure	(1,623)	(28,645)	(7,723)	(9,420)	(9,920)
Chg in investments	-	-	-	-	-
Other investing activities	-	-	-	-	-
Cash flow from inv. (b)	(1,623)	(28,645)	(7,723)	(9,420)	(9,920)
Free cash flow (a+b)	27,543	4,798	29,989	22,765	32,257
Equity raised/(repaid)	-	-	-	-	-
Debt raised/(repaid)	(125)	14,251	(13,140)	(1,771)	-
Chg in Minorities int.	-	-	-	-	-
Dividend (incl. tax)	(4,973)	(25,376)	(24,369)	(11,682)	(14,018)
Other financing activities	-	-	-	-	-
Cash flow from fin. (c)	(5,097)	(11,124)	(37,509)	(13,453)	(14,018)
Net chg in cash (a+b+c)	22,446	(6,326)	(7,520)	9,311	18,239

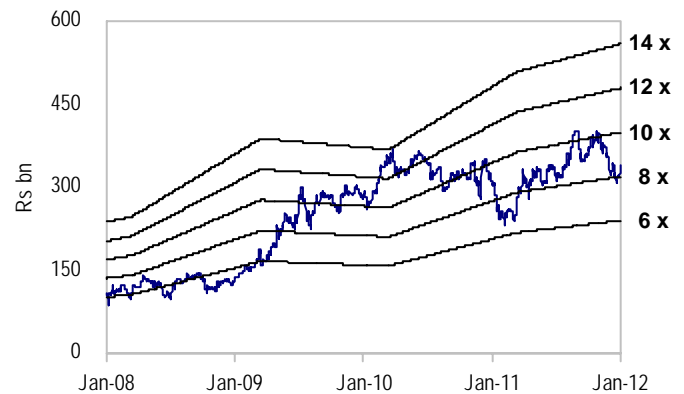
Balance Sheet	FY10	FY11	FY12E	FY13E	FY14E
Equity capital	399	399	399	399	399
Reserves & surplus	34,251	29,161	41,415	54,462	68,842
Shareholders' funds	34,650	29,561	41,814	54,861	69,241
Preference Share Capital	-	-	-	-	-
Total Debt	660	14,912	1,771	-	-
Capital Employed	35,311	44,472	43,586	54,861	69,241
Net fixed assets	17,069	42,054	38,691	36,527	34,014
Cash & Cash Eq.	57,973	51,646	44,126	53,438	71,677
Net other Current Assets	(38,560)	(47,117)	(36,968)	(32,690)	(33,886)
Investments	357	357	357	357	357
Net Deferred Tax Assets	(1,528)	(2,468)	(2,620)	(2,770)	(2,920)
Total assets	35,311	44,472	43,586	54,861	69,241

Key Ratios	FY10	FY11	FY12E	FY13E	FY14E
EBITDA margin (%)	17.5	13.5	15.4	15.4	15.5
Net margin (%)	14.2	10.3	10.2	10.3	9.7
Dividend yield (%)	5.8	5.5	2.6	3.2	3.2
Net debt/Equity (x)	(1.7)	(1.2)	(1.0)	(1.0)	(1.0)
Net Working Capital (days)	(18)	(19)	(19)	(19)	(19)
Asset turnover (x)	2.2	2.0	2.3	2.6	2.6
ROCE (%)	73.4	59.6	61.5	63.9	58.3
RoE (%)	61.4	61.8	67.1	56.0	45.8
EV/Net sales (x)	2.0	1.8	1.4	1.2	1.1
EV/EBITDA (x)	11.6	13.0	9.3	8.0	6.8
PER (x)	17.0	19.1	15.9	14.0	13.4
Price/Book (x)	11.0	12.8	9.1	6.9	5.5

P/E Band



EV/EBITDA



**T E A M**

**EQUITY DESK**

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Rating Objective		
Rating	Large Caps	Mid Caps
	M.Cap > USD1bn	M.Cap <= USD1bn
Return %		
<b>BUY</b>	<b>More than 15</b>	<b>More than 20</b>
<b>Accumulate</b>	<b>5 to 15</b>	<b>10 to 20</b>
<b>Reduce</b>	<b>(-)5 to +5</b>	<b>0 to 10</b>
<b>Sell</b>	<b>Below (-)5</b>	<b>Less than 0</b>



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