

HERO MOTOCORP | Auto & Auto Components

Strong profitability to continue

LKP

Robust quarter, better than expectations

Hero reported strong set of numbers in Q4. Volumes grew by 18.5% yoy while fell by 15% qoq to 1.57 mn units, while topline grew by 39.2% yoy to ₹86.86 bn as realizations witnessed a fantastic expansion of 12% yoy mainly on price hikes taken in Q4, model mix tilting towards big ticket models and low base of last year when BS 6 was playing as a dampener. The demand in Q4 remained strong even after the best quarter of Q3. Input costs to sales remained flattish sequentially at 70.4% despite commodity prices moving up by 5%. This was a big surprise for the street as other auto players were unable to arrest this surge. Due to this impact, EBITDA margins surged to 13.9%, while rising from 10.6% yoy and slightly falling qoq. The company managed the balance of market share and margins well as the cost reduction measures paid off well to mitigate the input cost surge. As depreciation expenses de-grew by 6.6% yoy, PBT rose by 73.6% yoy while PAT growth was at 39.4% yoy to ₹8.65 bn with tax rate at 24%.

Demand drivers remain intact in mid to long term

We witnessed that even after festive season ended, there was no demand deceleration. In the year FY21, Hero won 140 bps market share through a very strong demand for Deluxe, Splendor, Passion Pro and its new launches Xtreme 160 and X-Pulse bikes. The retail demand has also reached pre-Covid levels in the second half of the year. Scooters market share has gone up by 270 bps with strong demand for Pleasure. In the premium bikes segment, the company attained market share of 4% on the back of X-treme 150 R and X-Pulse bikes. Additionally, in exports markets the company has gained market share too, as exports grew by 8% in FY21, mainly in markets like Colombia (market share here grew from 4% to 6% in FY21), Bangladesh and Mexico (where Hero has joined hands with a big distribution partner). With strong volume pick up in H2 of FY21, the annual volume fall is arrested to 10.6%. In FY22, Q1 will be a bit subdued considering an unprecedented sharp second wave of the pandemic. Hero shut its plants for some days in April which may impact production and sales in the short term. Going forward, the intrinsic growth drivers are expected to remain intact with the rural story and monsoons expected to pan out well this year as well. We therefore believe FY22E/23E volumes to record a 15%/10% growth respectively.

Cost reduction initiatives prove to be very effective when input costs are rising

Hero's EBITDA margins in Q4 came robust at 13.9% despite a 5% rise in commodity costs. This was a result of 4% price hike taken by Hero in Q4 and 3% through LEAP program. LEAP cost reduction program yielded 300 bps benefit in Q4 and 200bps in FY21. Model mix tilted in favor of premium segment coupled with lower discounting. The company under the LEAP program is quite aggressive in saving employee costs and other expenses including sales and promotion expenses. These steps shall enable Hero to achieve its margin target of 14-16% in FY22E, despite commodity headwinds. Secondly, premiumisation of bikes with the help of global partner Harley Davidson shall help the product mix to improve further. FY21E margins emerged strong at 13%, while in FY22E/FY23E, we expect them to rise up to 13.8%/14.4% respectively.

Key Financials	FY 20	FY 21	FY 22E	FY 23E
Revenues (Rs bn)	288	308	397	471
EBITDA (%)	13.7	13.0	13.8	14.4
PAT (%)	12.6	9.6	10.3	10.7
EPS (Rs)	181.9	148.4	204.1	253.0
EPS Growth (%)	-12.7%	0.3%	37.5%	24.0%
P/E (x)	15.7	19.2	14.0	11.3
P/B (x)	2.0	1.9	1.7	1.6
EV/EBITDA (x)	12.1	12.5	9.5	7.8
ROCE (%)	21.5%	19.2%	23.6%	27.3%
ROE (%)	20.9%	19.5%	25.0%	28.5%
Dividend Yield (%)	3.4%	3.3%	4.3%	5.3%

Rating	Buy
Current Market Price (₹)	2,860
12 M Price Target (₹)	3,289
Potential upside (%)	15

Stock Data

FV (₹) :	2
Market Cap Full (₹ bn) :	570
Market Cap Free Float (₹ bn) :	378
52-Week High / Low (₹) :	1,933 / 3,629
2-Year High / Low (₹) :	1,475 / 3,629
1 Year Avg. Dly Traded Volume (in lakh)	17
BSE Code / NSE Symbol	50018 / HEROMOTOCO
Bloomberg :	HMCL IN

Shareholding Pattern (%)

	Mar-21	Dec-20	Sep-20	Jun-20
Promoter	34.76	34.76	34.76	34.77
FPIs	37.19	35.89	33.29	32.71
MFs	4.65	5.91	7.47	8.01
Insurance	8.55	8.25	9.29	9.28
Others	14.85	15.19	15.19	15.23

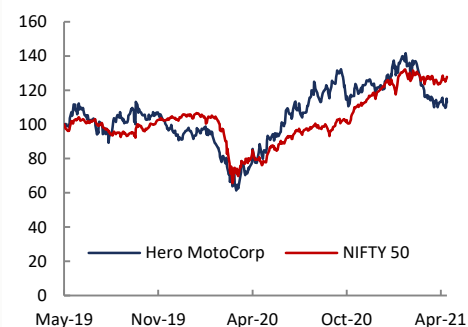
Source: BSE

Price Performance (%)

(%)	1M	3M	6M	1YR
Hero Motocorp	-2.7%	-16.6%	-2.9%	43.0%
Nifty 50	0.03%	-0.7%	20.9%	61.1%

* To date / current date : May 7, 2021

Hero Motocorp vs Nifty 50



Outlook and Valuation

Hero posted robust set of numbers in Q4 FY21. Going forward, we expect a soft Q1, but the growth should come back in Q2 if the second wave comes under control by then. Demand levers post pandemic are intact with rural story remaining strong. Re-migration of construction workers expected to come in to play as well. 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 lower level of inventory, ramping up of production, improving demand, new launches and low base, we expect FY22 to post a solid growth after a strong Q4 FY21. 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. Profitability would improve on price hikes, cost saving programs, capex reduction and operating leverage stemming from improving volumes and product mix. We therefore maintain our BUY rating on the stock with a target price of ₹3,289.

Quarterly Financial Snapshot

(₹ mn)	Q4 FY21	Q3 FY21	% qoq	Q4 FY20	% yoy
Total Net Sales	86,860	97,757	-11.1%	62,384	39.2%
RM Cost	61,173	68,912	-11.2%	43,200	41.6%
Employee Cost	4,884	5,167	-5.5%	4,354	12.2%
Other Expenses	8,691	9,543	-8.9%	8,231	5.6%
EBITDA	12,112	14,136	-14.3%	6,599	83.5%
EBITDA Margins (%)	13.9	14.5	(60 bps)	10.6	330 bps
Other Income	874	2,027	-56.9%	1,695	-48.4%
Depreciation	1,631	1,698	-4.0%	1,747	-6.6%
Interest	62.9	46.5	35.3%	40.6	54.9%
PBT	11,291	14,418	-21.7%	6,506	73.6%
Tax	2,642	3,574	-26.1%	299	784.0%
PAT	8,650	10,844	-20.2%	6,207	39.4%
PAT Margins (%)	10.0	11.1	(110 bps)	9.9	10 bps
Exceptional Items	-	-	N/A	-	N/A
Adjusted PAT	8,650	10,844	-20.2%	6,207	39.4%

Source: Company, LKP Research

Per unit parameters	Q4 FY21	Q3 FY21	Q2 FY21	Q1 FY21	Q4 FY20	Q3 FY20	Q2 FY20	Q1 FY20
Volumes (mn)	1.57	1.85	1.81	0.56	1.32	1.69	1.69	1.84
Net Realization	52,812	52,977	51,620	52,740	47,153	41,311	44,815	43,574
Material Cost/Unit	39,005	37,345	36,700	37,164	32,653	27,513	30,342	30,343
Staff Cost/Unit	3,114	2,800	2,817	6,787	3,291	2,773	2,776	2,538
Other Expn/Unit	5,542	5,172	5,013	6,872	6,222	4,890	5,179	4,410
Total Expn/Unit	47,662	45,317	44,531	50,823	42,166	35,177	38,297	37,290
EBITDA/unit	7,723	7,660	7,089	1,917	4,988	6,135	6,518	6,283
Net profit /unit	5,515	5,877	5,254	1,087	4,692	5,198	5,534	6,822

Source: Company, LKP Research

Income Statement

(₹ mn)	FY 20	FY 21	FY 22E	FY 23E
Total Revenues	2,88,361	3,08,006	3,96,712	4,71,294
Raw Material Cost	1,96,974	2,17,623	2,77,698	3,25,193
Employee Cost	18,417	18,987	23,803	28,278
Other Exp	33,390	31,203	40,465	49,957
EBITDA	39,580	40,192	54,746	67,866
<i>EBITDA Margin(%)</i>	<i>13.7</i>	<i>13.0</i>	<i>13.8</i>	<i>14.4</i>
Other income	7783	5799	5500	5200
Depreciation	8,180	6,769	6,399	6,364
Interest	220	218	225	225
PBT	38,963	39,004	53,623	66,478
<i>PBT Margin(%)</i>	<i>13.5</i>	<i>12.7</i>	<i>13.5</i>	<i>14.1</i>
Exceptional items	6774	0	0	0
Tax	9,404	9,362	12,869	15,955
PAT	29,559	29,642	40,753	50,523
<i>PAT Margins (%)</i>	<i>10.3</i>	<i>9.6</i>	<i>10.3</i>	<i>10.7</i>
Adj PAT	36,333	29,642	40,753	50,523
<i>Adj PAT Margin (%)</i>	<i>12.6</i>	<i>9.6</i>	<i>10.3</i>	<i>10.7</i>

Key Ratios

YE Mar	FY 20	FY 21	FY 22E	FY 23E
Per Share Data (Rs)				
Adj. EPS	181.9	148.4	204.1	253.0
CEPS	222.9	182.3	236.1	284.9
BVPS	707.7	760.9	816.8	886.1
DPS	97.0	95.0	122.4	151.8
Growth Ratios(%)				
Total revenues	-14.3%	6.8%	28.8%	18.8%
EBITDA	-19.7%	1.5%	36.2%	24.0%
PAT	-12.7%	0.3%	37.5%	24.0%
EPS Growth	-12.7%	0.3%	37.5%	24.0%
Valuation Ratios (x)				
PE	15.7	19.2	14.0	11.3
P/CEPS	12.8	15.7	12.1	10.0
P/BV	2.0	1.9	1.7	1.6
EV/Sales	2.0	1.9	1.4	1.2
EV/EBITDA	12.1	12.5	9.5	7.8
Operating Ratios (Days)				
Inventory days	13.0	13.0	13.0	13.0
Receivable Days	15.0	15.0	15.0	15.0
Payables day	42.0	42.0	42.0	42.0
Net Debt/Equity (x)	0.03	0.04	0.02	-0.01
Profitability Ratios (%)				
ROCE	21.5%	19.2%	23.6%	27.3%
ROE	20.9%	19.5%	25.0%	28.5%
Dividend yield	3.4%	3.3%	4.3%	5.3%

Source: Company, LKP Research

Balance Sheet

(₹ mn)	FY 20	FY 21	FY 22E	FY 23E
EQUITY & LIABILITIES				
Equity Share Capital	400	400	400	400
Reserves & Surplus	1,40,965	1,51,585	1,62,751	1,76,594
Total Networkth	1,41,364	1,51,984	1,63,151	1,76,994
Total debt	0	0	0	0
Deferred Tax Liability	5,145	6,799	6,799	6,799
Long term provisions	1,224	1,725	1,725	1,725
Total non current liabilities	6,369	8,524	8,524	8,524
Current Liab & Prov				
Current liabilities	30,222	51,889	54,344	58,105
Other liabilities & Provisions	9,541	9,213	9,213	9,213
Total Equity and Liabilities	1,87,493	2,21,608	2,35,230	2,52,834
ASSETS				
Net block	55,624	52,934	51,535	50,172
Capital WIP	5,748	5,826	8,326	10,826
Intangible assets	3,211	5,490	5,490	5,490
Deferred tax assets	0	0	0	0
Long term investments	35,282	43,081	45,081	47,081
Long term loans and advances	3,774	4,204	4,204	4,204
Other non current assets	969	547	547	547
Total non-current assets	1,04,608	1,12,082	1,15,183	1,18,319
Current Assets				
Current investments	46,945	61,915	64,915	67,915
Cash and Bank	2,419	2,572	5,143	9,931
Inventories	10,920	14,696	16,738	19,601
Sundry Debtors	16,031	24,268	27,172	30,989
Loan, Advances & others	6,571	6,078	6,078	6,078
Other current assets	224	369	369	369
Total Assets	1,87,493	2,21,608	2,35,230	2,52,834

Cash Flow

(₹ mn)	FY 20	FY 21	FY 22E	FY 23E
PAT	36,333	29,642	40,753	50,523
Depreciation	8,180	6,769	6,399	6,364
Interest	220	218	225	225
Income Tax paid	-5,443	-9,759	-12,869	-15,955
Chng in working capital	12,027	10,700	-2,492	-2,919
Cash flow from operations (a)	54,101	41,727	45,764	54,193
Capital expenditure	-13,586	-5,101	-7,500	-7,500
Chng in investments	-16,128	-14,461	-5,000	-5,000
Other investing activities	882	-2,538	0	0
Cash flow from investing (b)	-28,831	-22,099	-12,500	-12,500
Free cash flow (a+b)	25,270	19,628	33,264	41,693
Inc/dec in borrowings	0	0	0	0
Dividend paid (incl. tax)	-23,325	-18,978	-29,587	-36,680
Other financing activities	-220	-218	-225	-225
Cash flow from financing (c)	-24,198	-19,415	-29,812	-36,905
Net chng in cash (a+b+c)	1,072	213	3,452	4,788
Closing cash & cash equivalents	1,478	1,691	5,143	9,931

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