

## Hero MotoCorp

Reco: Buy

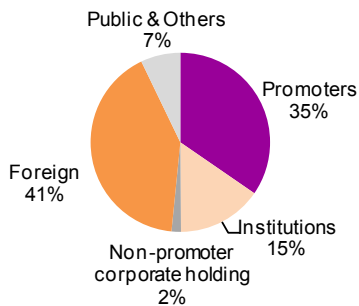
Rural demand accelerating; maintain Buy with a revised PT of Rs4,100

CMP: Rs3,457

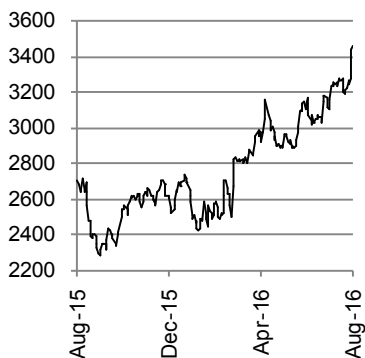
### Company details

|                               |               |
|-------------------------------|---------------|
| Price target:                 | Rs4,100       |
| Market cap:                   | Rs69029 cr    |
| 52-week high/low:             | Rs3,554/2,259 |
| NSE volume:<br>(No of shares) | 3.9 lakh      |
| BSE code:                     | 500182        |
| NSE code:                     | HEROMOTOCO    |
| Sharekhan code:               | HEROMOTOCO    |
| Free float:<br>(No of shares) | 12.7 cr       |

### Shareholding pattern



### Price chart



### Price performance

| (%)                | 1m   | 3m   | 6m   | 12m  |
|--------------------|------|------|------|------|
| Absolute           | 10.7 | 19.0 | 35.1 | 31.0 |
| Relative to Sensex | 6.9  | 6.2  | 17.2 | 29.8 |

### Key points

- Q1FY2017 results in line with estimates:** Hero MotoCorp has posted in-line numbers for Q1FY2017. Revenue grew by 7% YoY to Rs7,399 crore (compared to our estimate of Rs7,695 crore) mainly driven by a 6% YoY volume growth. Realisation per vehicle grew marginally 1% YoY led by price hikes. Operating Profit Margin (OPM) improved by 150BPS YoY to 16.6% (in line with our estimate of 16.7%), led by softer commodity prices and savings under the cost control programme "Leap". Driven by the robust operating performance, net profit grew by 18% YoY to Rs883 crore, coming broadly in line with our estimate of Rs908 crore.
- Rural markets picking up pace; company raises volume forecast:** The rural markets, which form ~40% of the two-wheeler industry volume, have seen a pick-up recently. Rural markets have reported a growth of 7% YoY in FY2017 (April to July 2017) so far as against flat volume growth in FY2016. A normal south-west monsoon after two back-to-back years of drought has led to improvement in the rural sentiment, leading to uptick in two-wheeler demand. The company's management expects two-wheeler demand to gain momentum further and has raised the FY2017 volume growth forecast from 5-6% earlier to ~9-10%. Hero MotoCorp is likely to be the key beneficiary of improved rural demand, as it derives about half of its volumes from the rural areas as against the two-wheeler industry average of 37%. We believe that the company is likely to maintain its leadership position in the two-wheeler space despite increased competition given the higher proportion of its rural-centric volume (where demand is likely to accelerate further).
- Cost control measures, improving demand scenario to offset margin pressures from rising commodity prices:** Hero MotoCorp is likely to incur savings under the cost control programme "Leap", wherein the company has identified raw material, vendor sourcing and designing as the key focus areas. Further, we believe that given the improving two-wheeler demand scenario, the intensity of pricing pressure would reduce, enabling Hero MotoCorp to maintain its margins. We believe that the cost savings, coupled with receding pricing pressures would help the company to offset rising commodity prices. We expect Hero MotoCorp's margins to remain high and expect 15.6% OPM in FY2018 as against 15.4% reported in FY2016. Our OPM assumption is at the higher end of the management's guidance of 14-16%.
- Increase estimates; Maintain Buy with a revised PT of Rs4,100:** We have raised our earnings assumptions for both FY2017 and FY2018 by 4% each, buoyed by the improved demand scenario and the likelihood of stability in margins at higher levels. Hero MotoCorp is among the best play on the rural demand recovery theme. We maintain our Buy rating on the stock with a revised price target (PT) of Rs4,100 (based on 20x FY2018 earnings).

### Results

| Particulars        | Q1FY17  | Q1FY16  | YoY %   | Q4FY16  | Rs cr | QoQ %  |
|--------------------|---------|---------|---------|---------|-------|--------|
| Total income       | 7,398.9 | 6,904.8 | 7.2     | 7,505.2 |       | -1.4   |
| EBIDTA             | 1,230.1 | 1,042.0 | 18.0    | 1,191.9 |       | 3.2    |
| EBIDTA margins (%) | 16.6    | 15.1    | 150 bps | 15.9    |       | 70 bps |
| Depreciation       | 115.2   | 103.0   | 11.9    | 115.5   |       | -0.2   |
| Interest           | 1.5     | 1.2     | 24.0    | 1.2     |       | 24.0   |
| Other income       | 120.4   | 104.4   | 15.3    | 116.8   |       | 3.1    |
| PBT                | 1,233.7 | 1,042.2 | 18.4    | 1,192.0 |       | 3.5    |
| Tax                | 350.6   | 294.7   | 19.0    | 357.4   |       | -1.9   |
| PAT                | 883.1   | 747.5   | 18.1    | 834.7   |       | 5.8    |
| EPS                | 44.2    | 37.4    |         | 41.8    |       |        |

\*Financials as per new Ind AS accounting

## Valuations

| Particulars   | Rs cr    |          |          |          |          |
|---------------|----------|----------|----------|----------|----------|
|               | FY14     | FY15     | FY16     | FY17E    | FY18E    |
| Net sales     | 25,275.5 | 27,585.3 | 28,541.8 | 31,509.4 | 36,829.3 |
| Growth (%)    | 6.3      | 9.1      | 3.5      | 10.4     | 16.9     |
| EBIDTA        | 3,540.1  | 3,542.2  | 4,389.5  | 5,084.8  | 5,736.0  |
| OPM (%)       | 14.0     | 12.8     | 15.4     | 16.1     | 15.6     |
| PAT (Rs cr)   | 2,109.1  | 2,540.7  | 3,074.9  | 3,635.8  | 4,103.7  |
| Growth (%)    | -0.4     | 20.5     | 21.0     | 18.2     | 12.9     |
| FD EPS (Rs)   | 105.6    | 127.2    | 154.0    | 182.1    | 205.5    |
| P/E (x)       | 32.7     | 27.2     | 22.5     | 19.0     | 16.8     |
| P/B (x)       | 12.3     | 10.6     | 8.8      | 7.4      | 6.3      |
| EV/EBIDTA (x) | 18.3     | 18.6     | 14.7     | 12.5     | 10.9     |
| RoE (%)       | 37.7     | 38.8     | 39.3     | 39.0     | 37.2     |
| RoCE (%)      | 51.7     | 53.2     | 55.5     | 54.2     | 51.5     |

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