

July 21, 2011

Reco	Previous Reco
Hold	Hold
CMP	Target Price
Rs1,789	Rs 1,840
EPS change FY12E/13E (%)	3/4
Target Price change (%)	3.7
Nifty	5,542
Sensex	18,436

### Price Performance

(%)	1M	3M	6M	12M
Absolute	2	3	1	(8)
Rel. to Nifty	(3)	8	4	(10)

Source: Bloomberg

### Relative Price Chart



Source: Bloomberg

### Stock Details

Sector	Automobiles
Bloomberg	HH@IN
Equity Capital (Rs mn)	399
Face Value(Rs)	2
No of shares o/s (mn)	200
52 Week H/L	2,060/1,378
Market Cap (Rs bn/USD mn)	357/8,019
Daily Avg Volume (No of sh)	129008
Daily Avg Turnover (US\$m)	5.2

### Shareholding Pattern (%)

	Jun-11	Mar-11	Dec-10
Promoters	52.2	52.2	52.2
FII/NRI	33.8	32.9	33.6
Institutions	4.6	5.2	4.6
Private Corp	1.7	1.9	1.7
Public	7.8	7.8	7.9

Source: Capitaline

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- Despite an inline sales (Rs 56.8bn), EBIDTA disappoints at Rs 6.4bn (est-Rs 7.3bn). Lower tax rate at 16.7% (est-20.5%) and higher other inc. leads to inline PAT (Rs 5.6bn, est-Rs 5.7bn)
- Demand outlook remains robust. Capacity will reach 6.4mn units by end FY12. Margin headwinds remain a cause of concern
- Revise our FY12/13 EPS est. upwards by 3%/3.8% to 113.5/131.4 due to lower tax rate. Lower EBITDA margin by 30bps/10 bps on higher cost pressures
- Retain HOLD rating and revise our TP to Rs 1,840 (FY13 PER 14x). Key risks are higher than anticipated cost pressures

### Net Sales – In line with our est.

Net sales at Rs 56.8bn was in line with our est. of Rs 56.9bn. Average selling price for the quarter stood at Rs 37,156 (up 6.7% YoY and flat QoQ).

Product Mix %	Q1FY11	Q2FY11	Q3FY11	Q4FY11	Q1FY12
Motorcycle (Dom)	94.0	93.8	93.5	92.8	93.4
Scooters (Dom)	6.0	6.2	6.5	7.2	6.6
<b>Total (Dom)</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
Exports	2.5	2.7	2.7	2.0	2.6
Domestic	97.5	97.3	97.3	98.0	97.4
<b>Units Sold</b>	<b>1,234,039</b>	<b>1,285,934</b>	<b>1,428,030</b>	<b>1,454,431</b>	<b>1,529,577</b>

Product Mix %	Q1FY11	Q2FY11	Q3FY11	Q4FY11	Q1FY12
<b>Motorcycle (Domestic)</b>					
upto 125cc	93.8	93.5	93.2	92.2	94.1
125 cc to 250 cc	6.2	6.5	6.8	7.8	5.9
<b>Motorcycle (Export)</b>					
upto 125cc	88.0	91.1	88.8	90.0	92.4
125 cc to 250 cc	12.0	8.9	11.2	10.0	7.6

Source: SIAM, Emkay research

### EBIDTA ~12% below est.

EBIDTA at Rs 6.4bn was ~12% below our est. of Rs 7.3bn. EBIDTA margins stood at 11.3% vs our est. of 12.8%. Key disappointment was higher input cost pressures. RM to sales at 74.7% was higher than our est of 72.1%. This was partly offset by lower other expense at Rs 6.3bn (11.1% of sales) vs our est. of Rs 7bn. Company is likely to incur promotional costs on rebranding from next quarter onwards which should increase other expenses going ahead. Staff costs at Rs 1.6bn was in line with our est.

### Financial Snapshot

YE-	Net Sales	EBITDA (Core)	EBITDA (%)	APAT	EPS (Rs)	EPS % chg	RoE (%)	P/E	EV/ EBITDA	P/BV
FY10	157,702	26,620	16.9	22,318	111.8	74.0	61.4	16.0	11.3	10.3
FY11P	193,085	23,476	12.2	21,132	105.8	(5.3)	65.8	16.9	13.0	12.1
FY12E	227,070	25,681	11.3	22,661	113.5	7.2	66.1	15.8	11.8	9.2
FY13E	255,407	30,411	11.9	26,245	131.4	15.8	63.5	13.6	9.7	8.2

Source: Company, Emkay Research

## Quarterly Summary

Rs m n	Q1FY11	Q2FY11	Q3FY11	Q4FY11	Q1FY12	YoY (%)	QoQ (%)
<b>Revenue</b>	<b>42,966</b>	<b>45,520</b>	<b>51,617</b>	<b>53,909</b>	<b>56,833</b>	<b>32.3</b>	<b>5.4</b>
<b>Expenditure</b>	<b>36,941</b>	<b>39,440</b>	<b>45,850</b>	<b>47,381</b>	<b>50,427</b>	<b>36.5</b>	<b>6.4</b>
<i>as % of sales</i>	86.0	86.6	88.8	87.9	88.7		
Consumption of RM	30,594	33,100	38,149	39,269	42,448	38.7	8.1
<i>as % of sales</i>	71.2	72.7	73.9	72.8	74.7		
Employee Cost	1,450	1,498	1,560	1,680	1,645	13.5	(2.1)
<i>as % of sales</i>	3.4	3.3	3.0	3.1	2.9		
Other expenditure	4,897	4,842	6,141	6,432	6,334	29.3	(1.5)
<i>as % of sales</i>	11.4	10.6	11.9	11.9	11.1		
<b>EBITDA</b>	<b>6,025</b>	<b>6,079</b>	<b>5,767</b>	<b>6,528</b>	<b>6,407</b>	<b>6.3</b>	<b>(1.9)</b>
Depreciation	483	608	560	603	627	29.9	4.0
<b>EBIT</b>	<b>5,543</b>	<b>5,472</b>	<b>5,207</b>	<b>5,925</b>	<b>5,780</b>	<b>4.3</b>	<b>(2.5)</b>
Other Income	534	784	620	743	884	65.5	18.9
Interest	(27)	(21)	(52)	81	(32)	19.9	(139)
<b>PBT</b>	<b>6,103</b>	<b>6,276</b>	<b>5,880</b>	<b>6,588</b>	<b>6,696</b>	<b>9.7</b>	<b>1.6</b>
Total Tax	1,187	1,220	790	1,572	1,117	(5.9)	(28.9)
<b>Adjusted PAT</b>	<b>4,917</b>	<b>5,056</b>	<b>5,089</b>	<b>5,016</b>	<b>5,579</b>	<b>13.5</b>	<b>11.2</b>
(Profit)/loss from JV's/Ass/MI							
<b>Adj. PAT after MI</b>	<b>4,917</b>	<b>5,056</b>	<b>5,089</b>	<b>5,016</b>	<b>5,579</b>	<b>13.5</b>	<b>11.2</b>
Extra ordinary items	-	-	(798)	-	-	-	-
<b>Reported PAT</b>	<b>4,917</b>	<b>5,056</b>	<b>4,291</b>	<b>5,016</b>	<b>5,579</b>	<b>13.5</b>	<b>11.2</b>
<b>Reported EPS</b>	<b>24.6</b>	<b>25.3</b>	<b>21.5</b>	<b>25.1</b>	<b>27.9</b>	<b>13.5</b>	<b>11.2</b>

Margins (%)						(bps)	(bps)
EBIDTA	14.0	13.4	11.2	12.1	11.3	(275)	(84)
EBIT	12.9	12.0	10.1	11.0	10.2	(273)	(82)
EBT	14.2	13.8	11.4	12.2	11.8	(242)	(44)
PAT	11.4	11.1	9.9	9.3	9.8	(163)	51
Effective Tax rate	19.4	19.4	13.4	23.9	16.7	(276)	(718)

Per Vehicle Analysis							
Revenue	34,817	35,398	36,145	37,066	37,156	6.7	0.2
RM	24,791	25,740	26,714	26,999	27,751	11.9	2.8
Staff Cost	1,175	1,165	1,092	1,155	1,076	(8.5)	(6.9)
Other exp.	3,968	3,765	4,301	4,422	4,141	4.4	(6.4)
EBITDA	4,883	4,728	4,038	4,489	4,189	(14.2)	(6.7)
PAT	3,984	3,932	3,564	3,449	3,647	(8.5)	5.8

Source: Company, Emkay Research

**APAT at Rs 5.6bn marginally below est.**

APAT at Rs 5.6bn was marginally below our est. of Rs 5.7bn due to higher other income and lower tax rate. Tax rate at 16.7% was lower than our est of 20.5%. Management expects tax rates to be maintained at similar levels for FY12. Higher other income at Rs 884mn vs our est. Rs 650mn was due to liquidation of certain investments to meet interim dividend payment of Rs 17bn and higher yields on current investments.

**Revision in estimates**

We have upgraded our FY12/FY13 est. only due to lower tax rate. We have factored in tax rate of 16.7%/18% for FY12/FY13 as compared to our earlier est of 20.5%/20.5%. But for the lower tax rate, our EPS estimates would have been lower. Our EBITDA margin estimate is revised downwards by 30 bps/10 bps in FY12/FY13 on higher cost pressures.

Rs mn	FY12E			FY13E		
	Earlier	Revised	%Change	Earlier	Revised	%Change
Volumes	6,126,950	6,126,950	-	6,776,308	6,776,308	-
Sales	222,376	227,070	2.1	250,593	255,407	1.9
EBIDTA	25,812	25,681	(0.5)	30,084	30,411	1.1
EBIDTA margins (%)	11.6	11.3		12.0	11.9	
Net Profits	21,998	22,661	3.0	25,279	26,245	3.8
EPS	110.2	113.5	3.0	126.6	131.4	3.8

Source: Emkay Research

**Valuations and View**

At CMP of Rs 1,789, the stock trades at PER of 15.8x/13.6x and EV/EBIDTA of 11.8x/9.7x our FY12/FY13 estimates. We raise our target price to Rs 1,840 implying PER of 16.2x/14x PER and EV/EBIDTA of 12.2/10.1 our FY12/FY13 estimates. We maintain our rating to HOLD with ~3% upside from current levels.

**Key extracts from conference call**

- Maintain target of more than 6.1mn unit sales for FY12. Witnessing double digit growth from across regions (North/South/East/West).
- Dealer inventory remains low at 2-3 weeks that amounts to ~200,000 units.
- Commodity prices have started softening. Hence, expect EBITDA margins to improve from current levels.
- Pricing action: Rs 500-700 on 24<sup>th</sup> of June on select models. Expect this impact to be visible from next quarter.
- Advertisement costs to remain at ~2-2.3% of net sales for FY12. Additionally, expect rebranding costs of ~Rs 1bn in FY12.
- Launched refreshed version of Karizma in this quarter. Expect premium segment to improve with some more refreshments during FY12.
- Capacity expected to reach 6.5mn units by end of FY12. Plans to set up a new plant which should enhance capacity strongly from FY13. Pantnagar production target of 2mn units in FY12
- Capex of ~Rs 8bn – 9bn for FY12. This includes investments for land, plant & machinery for the new plant.
- Cash on books is at Rs 40bn

## Financials

## Income Statement

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
<b>Net Sales</b>	<b>157,702</b>	<b>193,085</b>	<b>227,070</b>	<b>255,407</b>
Growth (%)	27.9	22.4	17.6	12.5
<b>Expenditure</b>	<b>131,082</b>	<b>169,609</b>	<b>201,389</b>	<b>224,996</b>
Materials Consumed	107,484	141,111	167,957	187,961
Employee Cost	5,603	6,189	6,870	7,944
Other Exp	17,995	22,309	26,563	29,091
<b>EBITDA</b>	<b>26,620</b>	<b>23,476</b>	<b>25,681</b>	<b>30,411</b>
Growth (%)	55.7	(11.8)	9.4	18.4
<b>EBITDA margin (%)</b>	<b>16.9</b>	<b>12.2</b>	<b>11.3</b>	<b>11.9</b>
Depreciation	1,915	2,253	2,626	2,884
<b>EBIT</b>	<b>24,705</b>	<b>21,223</b>	<b>23,055</b>	<b>27,527</b>
<b>EBIT margin (%)</b>	<b>15.7</b>	<b>11.0</b>	<b>10.2</b>	<b>10.8</b>
Other Income	3,406	5,058	3,981	4,290
Interest expenses	(206)	(94)	(168)	(190)
<b>PBT</b>	<b>28,317</b>	<b>26,375</b>	<b>27,204</b>	<b>32,006</b>
<b>Tax</b>	<b>5,999</b>	<b>5,243</b>	<b>4,543</b>	<b>5,761</b>
Effective tax rate (%)	21.2	19.9	16.7	18.0
<b>Adjusted PAT</b>	<b>22,318</b>	<b>21,132</b>	<b>22,661</b>	<b>26,245</b>
Growth (%)	74.1	(5.3)	7.2	15.8
<b>Net Margin (%)</b>	<b>14.2</b>	<b>10.9</b>	<b>10.0</b>	<b>10.3</b>
(Profit)/loss from JV's/Ass/MI	-	-	-	-
<b>Adj. PAT After JV's/Ass/MI</b>	<b>22,318</b>	<b>21,132</b>	<b>22,661</b>	<b>26,245</b>
E/O items	-	(798)	-	-
<b>Reported PAT</b>	<b>22,318</b>	<b>20,333</b>	<b>22,661</b>	<b>26,245</b>
Growth (%)	74.1	(5.3)	7.2	15.8

## Balance Sheet

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
Equity share capital	399	399	399	399
Reserves & surplus	34,251	29,161	38,578	43,348
<b>Net worth</b>	<b>34,650</b>	<b>29,561</b>	<b>38,977</b>	<b>43,748</b>
<b>Minority Interest</b>	-	-	-	-
Secured Loans	-	-	-	-
Unsecured Loans	660	327	127	127
<b>Loan Funds</b>	<b>660</b>	<b>327</b>	<b>127</b>	<b>127</b>
Net deferred tax liability	1,528	2,468	2,468	2,468
<b>Total Liabilities</b>	<b>36,838</b>	<b>32,355</b>	<b>41,572</b>	<b>46,343</b>
Gross Block	27,510	30,510	37,510	39,510
Less: Depreciation	10,922	13,175	15,800	18,685
<b>Net block</b>	<b>16,588</b>	<b>17,335</b>	<b>21,709</b>	<b>20,825</b>
Capital work in progress	481	3,050	3,050	3,050
<b>Investment</b>	<b>39,257</b>	<b>51,287</b>	<b>48,287</b>	<b>49,287</b>
<b>Current Assets</b>	<b>28,826</b>	<b>15,046</b>	<b>29,525</b>	<b>38,334</b>
Inventories	4,364	5,249	6,701	7,538
Sundry debtors	1,084	1,306	8,042	9,045
Cash & bank balance	19,072	716	6,154	12,054
Loans & advances	4,058	7,287	8,569	9,639
Other current assets	248	489	59	59
<b>Current lia &amp; Prov</b>	<b>48,314</b>	<b>54,363</b>	<b>61,000</b>	<b>65,154</b>
Current liabilities	38,051	43,553	49,658	52,396
Provisions	10,264	10,811	11,342	12,758
<b>Net current assets</b>	<b>(19,488)</b>	<b>(39,317)</b>	<b>(31,475)</b>	<b>(26,820)</b>
Misc. exp	-	-	-	-
<b>Total Assets</b>	<b>36,838</b>	<b>32,355</b>	<b>41,572</b>	<b>46,342</b>

## Cash Flow

Y/E, Mar (Rs. mn)	FY10	FY11P	FY12E	FY13E
<b>PBT (Ex-Other income)</b>	<b>24,911</b>	<b>21,317</b>	<b>23,223</b>	<b>27,716</b>
Depreciation	1,915	2,253	2,626	2,884
Interest Provided	(206)	(94)	(168)	(190)
Other Non-Cash items	-	6,235	-	-
Chg in working cap	25,971	1,472	(2,404)	1,245
Tax paid	(5,999)	(5,243)	(4,543)	(5,761)
<b>Operating Cashflow</b>	<b>46,592</b>	<b>25,940</b>	<b>18,733</b>	<b>25,895</b>
Capital expenditure	(1,623)	(5,569)	(7,000)	(2,000)
<b>Free Cash Flow</b>	<b>44,969</b>	<b>20,371</b>	<b>11,733</b>	<b>23,895</b>
Other income	3,406	5,058	3,981	4,290
Investments	(5,570)	(12,030)	3,000	(1,000)
<b>Investing Cashflow</b>	<b>(2,164)</b>	<b>(6,972)</b>	<b>6,981</b>	<b>3,290</b>
Equity Capital Raised	-	-	-	-
Loans Taken / (Repaid)	(125)	(333)	(200)	-
Interest Paid	206	94	168	190
Dividend paid (incl tax)	(25,676)	(31,516)	(13,244)	(21,474)
Income from investments	-	-	-	-
Others	-	-	-	-
<b>Financing Cashflow</b>	<b>(25,594)</b>	<b>(31,755)</b>	<b>(13,276)</b>	<b>(21,285)</b>
<b>Net chg in cash</b>	<b>17,212</b>	<b>(18,356)</b>	<b>5,438</b>	<b>5,900</b>
Opening cash position	2,196	19,072	716	6,154
<b>Closing cash position</b>	<b>19,407</b>	<b>716</b>	<b>6,154</b>	<b>12,054</b>

## Key Ratios

Y/E, Mar	FY10	FY11P	FY12E	FY13E
<b>Profitability (%)</b>				
EBITDA Margin	16.9	12.2	11.3	11.9
Net Margin	14.2	10.9	10.0	10.3
ROCE	72.9	76.0	73.1	72.4
ROE	61.4	65.8	66.1	63.5
RoIC	(262.5)	(95.0)	(119.4)	(162.1)
<b>Per Share Data (Rs)</b>				
EPS	111.8	105.8	113.5	131.4
CEPS	121.3	117.1	126.6	145.9
BVPS	173.5	148.0	195.2	219.1
DPS	110.0	135.0	56.7	92.0
<b>Valuations (x)</b>				
PER	16.0	16.9	15.8	13.6
P/CEPS	14.7	15.3	14.1	12.3
P/BV	10.3	12.1	9.2	8.2
EV / Sales	1.9	1.6	1.3	1.2
EV / EBITDA	11.3	13.0	11.8	9.7
Dividend Yield (%)	6.1	7.5	3.2	5.1
<b>Gearing Ratio (x)</b>				
Net Debt/ Equity	(1.7)	(1.7)	(1.4)	(1.4)
Net Debt/EBIDTA	(2.2)	(2.2)	(2.1)	(2.0)
Work Cap Cycle (days)	(75.5)	(69.9)	(56.1)	(51.2)

The difference between the closing cash as per balance sheet and as per cash flow is due to cash credit balances

Note: The balance sheet details for FY11P to FY13E is excluding the recognition of asset and liability pertaining to royalty adjustment of Rs 23bn which shall be nullified over 14 quarters ending June 2014

**Recommendation History: Hero Honda Motors – HH IN**

Date	Reports	Reco	CMP	Target
04/05/2011	<a href="#">Hero Honda Q4FY11 Result Update</a>	Hold	1,600	1,775
08/04/2011	<a href="#">Hero Honda Management Meet Update</a>	Reduce	1,695	1,590
02/02/2011	<a href="#">Hero Honda Q3FY11 Result Update</a>	Reduce	1,523	1,540
16/12/2010	<a href="#">Hero Honda Event Update</a>	Hold	1,679	1,720

**Recent Research Reports**

Date	Reports	Reco	CMP	Target
20/07/2011	<a href="#">Ashok Leyland Q1FY12 Result Update</a>	Accumulate	50	57
19/07/2011	<a href="#">Bajaj Auto Q1FY12 Result Concall Update</a>	Buy	1,417	1,680
14/07/2011	<a href="#">Bajaj Auto Q1FY12 Result Update First Cut</a>	Buy	1,421	1,700
14/07/2011	<a href="#">Motherson Sumi Event Update</a>	Accumulate	231	260

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