

14<sup>th</sup> May 2007

## Reduce

Price

Rs705

Sensex

13796

### Price Performance

(%)	1M	3M	6M	12M
Absolute	10	(3)	(3)	(19)
Rel. to Sensex	5	3	(6)	(27)

Source: Bloomberg

### Stock Details

Sector	Automobiles
Reuters	HROH.BO
Bloomberg	HH@IN
Equity Capital	Rs399m
Face Value	Rs 2
52 Week H/L	Rs898/565
Market Cap	Rs140.7bn
Daily Avg Volume (No of shares)	320483
Daily Avg Turnover (US\$)	5.3mn

### Shareholding Pattern (%)

(31<sup>st</sup> Mar'07)

Promoters	55
FII/NRI	27.9
Institutions	7.3
Private Corp.	1.2
Public	8.7

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# Hero Honda

## High promotional expenses hit margins

Result  
Update

Hero Honda's (HH) Q4FY07 reported results were much lower than expected as profits declined 27% yoy on account of higher-than-estimated hit on margins, due to raw material cost pressures and surge in marketing and promotional expenses. A richer product mix helped the net sales for the quarter grow 17% yoy to Rs26395.8mn (Rs 22558.8mn). Reported margins stand at 10.2%, which is a yoy decline of 592bps, however adjusting the margins for a additional marketing costs due to the world cup to the tune of Rs225mn the margins stand at 11% (our estimates of 11.3%). Reported profits declined 27% yoy to Rs1950mn (Rs 2672mn), however upon the above adjustments, the profits stand at Rs2103mn a drop of 21.3%yoy (our estimates of Rs2143mn). Pressure on margins is likely to continue in the current fiscal as well due to competitive pricing and firm commodity prices. Despite the recouping of market share in the last couple of months we expect the weakness in industry demand to impact the company's sales in the coming months. Trading at a PE of 15.1x and 13.8x its estimated FY08 and FY09 earnings of Rs 46.8 and Rs 51 respectively, we maintain a Reduce.

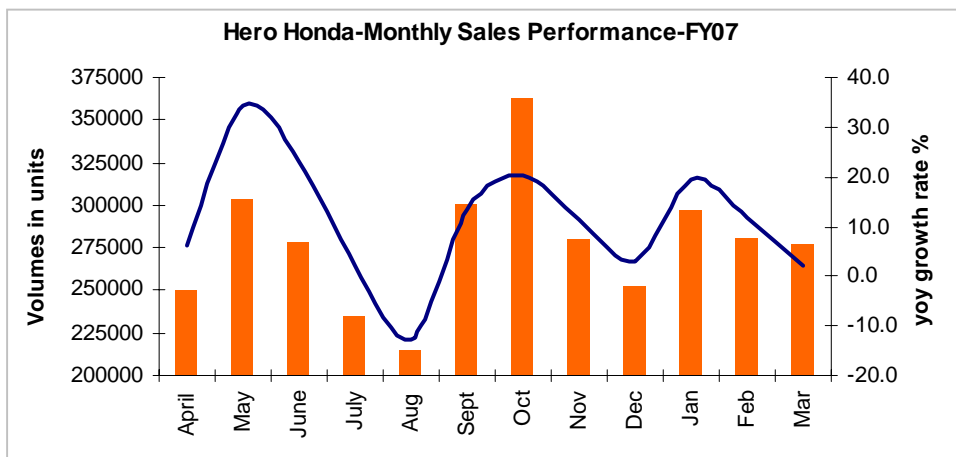
### Result Highlights

- HH registered a good sales growth of 17% yoy to Rs26.4bn on the back of 10.8% yoy volume growth in motorcycles and scooters. The company continued to lose market share in the motorcycle segment during the first 2 months of Q4. It has lost market share by 250bps to 46.5% in Q4FY07, however the months of March07 and April 07 saw the company aggressively inch up its market share to over 50% in motorcycles. For the fiscal the company posted net sales of Rs99bn and held a market share of 45.8% (yoy decline of 235bps) in motorcycles. However, with the industry demand slowing down due to rising interest rates, we expect growth momentum to remain sluggish in the current quarter and pick up only with new product launches and stabilizing of interest rates.
- Adjusted EBITDA margin declined 507bps yoy to 11% due to: i) higher raw material prices – non-ferrous metals (nickel), plastics and rubber ii) Sales of higher end models with alloy wheels which contributed higher to the topline with no additional contribution to the margins iii) new product launches, and iv) higher promotional expenses as well as additional advertisements during the cricket world cup to the tune of Rs225mn. Adjusted EBITDA consequently, declined by 19.8% yoy to Rs2911.6mn (our estimates Rs2910.5mn).
- Adjusted net profit dipped 21.3% yoy to Rs 2103mn (Rs2672mn), due to the decline in EBITDA, a comparatively higher tax charge and modest 3.4% yoy rise in other income at Rs445mn (Rs430mn). For the fiscal the company posted net recurring profits of Rs8.7bn translating into an EPS of Rs 43.7.

### Key Financials: Rs mn

YE-Mar	Net Sales	EBITDA (Core)	EBITDA (%)	APAT	AEPS (Rs)	EV/ EBITDA	P/BV	Div Yld (%)	RoE (%)	P/E
FY05	74217	11645	15.7	8105	40.6	10.5	9.4	2.8	61.6	17.4
FY06	87082	13622	15.6	9713	48.6	8.8	7.0	2.8	55.5	14.5
FY07	99000	11955	12.1	8732	43.7	9.9	5.7	2.4	38.9	16.1
FY08E	107121	12105	11.3	9344	46.8	9.7	4.8	2.8	34.4	15.1
FY09E	116818	13259	11.4	10178	51.0	8.3	4.0	2.8	31.5	13.8

## Monthly sales chart



## Key Financials Rs mn

Particulars	Q4FY07	Q4FY06	% Ch	FY07	FY08E	FY09E
Gross Sales	31353.4	26096.3	20.1	115420.4	124995.5	136310.2
Excise Duty	4957.6	3537.5	40.1	16420.8	17874.4	19492.4
<b>Net Sales</b>	<b>26395.8</b>	<b>22558.8</b>	<b>17.0</b>	<b>98999.6</b>	<b>107121.1</b>	<b>116817.9</b>
Other Income	445.1	430.3	3.4	1898.5	2154.8	2452.0
Total Income	26840.9	22989.1	16.8	100898.1	109275.9	119269.9
Inc/Dec Stock	113	87	29.9	22.4	0.0	0.0
Raw Materials	19177.4	15307.4	25.3	71764.7	78626.9	85627.5
Staff cost	904.5	821.4	10.1	3538.1	3856.4	4263.9
Other Exp	3289.3	2711.1	21.3	11719.0	12533.2	13667.7
Expenditure	23484.2	18926.9	24.1	87044.2	95016.5	103559.0
<b>EBITDA</b>	<b>2911.6</b>	<b>3631.9</b>	<b>-19.8</b>	<b>11955.4</b>	<b>12104.7</b>	<b>13258.8</b>
Gross Profit	3356.7	4062.2	-17.4	13853.9	14259.5	15710.8
Interest	-76.9	-39.3	95.7	-229.9	-220.0	-100.0
Gross Profit	3433.6	4101.5	-16.3	14083.8	14479.5	15810.8
Depreciation	355.1	304.7	16.5	1397.8	1519.2	1675.2
Profit before Tax	3078.5	3796.8	-18.9	12686.0	12960.3	14135.6
Tax	975.5	1124.9	-13.3	3954.1	3615.9	3958.0
Adj Net Profit	2103	2671.9	-21.3	8731.9	9344.4	10177.7
Reported PAT	1950.0	2671.9	-27.0	8578.9	9344.4	10177.7
EPS	10.5	13.4	-21.3	43.7	46.8	51.0
Units Sold	855984	772457	10.8	3336867	3536996	3782250
EBITDA %	11.0	16.1	-507	12.1	11.3	11.4

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