



INDIA RESEARCH

# Hero Honda Motors

Rs773

NEUTRAL

## RESULT NOTE

Mkt Cap: Rs154bn; US\$3.8bn

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**Result:** Q4FY08

**Comment:** Above expectations

**Last report:** 31 January 2008 (Price Rs677; Recommendation: Neutral)

### Key valuation metrics

Year to March 31 (Rs m)	Net sales	yoy chg (%)	Net profit	EPS (Rs)	yoy chg (%)	PER (x)	EV/E (x)
2006	87,140	17.4	9,713	48.6	19.8	15.9	10.1
2007	99,000	13.6	8,579	43.0	(11.7)	18.0	11.9
2008	103,318	4.4	9,678	48.5	12.8	15.9	10.3
2009E	113,423	9.8	10,418	52.2	7.6	14.8	9.4
2010E	123,728	9.1	11,440	57.3	9.8	13.5	8.2

Hero Honda's Q4FY08 performance was above our expectations mainly due to higher margins. Net sales grew by 5.6% yoy to Rs27.89bn (we saw Rs27.36bn), on the back of 2.1% yoy growth in volumes at 884,075 units. Average realizations grew by 3.5%yoy and 2.8%qoq aided by relatively stronger growth in the executive and premium segment motorcycles. EBITDA margins at 14.8%, higher 460bps yoy & 90bps qoq were above our expectations (13.7%). Consequently EBIDTA grew by 53.3%yoy to Rs4.11bn & net profit was higher by 53.2% yoy at Rs2.99bn. The company declared a dividend of 950% for FY08 (850% in FY07).

We have a muted outlook for the two-wheeler industry and expect the historical double digit growth trajectory to shift downwards to a single digit one due to rising urban penetration levels. Further, interest rates on two-wheelers have risen from 18% to 24% (on a reducing balance basis) over the last few months and financing norms continue to remain very stringent. Even as the growth momentum continues to remain a concern for the industry, leading two-wheeler players have commissioned their new plants in the recent past. As a result we believe the industry would continue to witness increasing competitive intensity accompanied by lack of pricing discipline. Resultant, we maintain our Neutral rating on the stock.

## KEY RESULT HIGHLIGHTS

### □ Net sales grow by 5.6%yoy to Rs27.89bn – marginally higher

Hero Honda's Q4FY08 revenues were marginally higher than our expectations. Net sales grew by 5.6%yoy to Rs27.89bn (our expectations of Rs27.36bn) on the back of 2.1%yoy growth in total volumes at 884,075 units. Average realizations for the quarter grew by 3.5%yoy and 2.8%qoq aided by relatively stronger growth in the executive and premium segment motorcycles.

### □ EBITDA margin at 14.8%, higher 460bps yoy, higher 90bps qoq – above expectations

The company's EBITDA margins were above our expectations primarily due to a better product mix and better control on marketing and advertising spends. Margins were higher by 460bps yoy and by 90bps qoq at 14.8% (we saw 13.7%). Operating profit for the quarter grew by 53.3%yoy to Rs4.11bn.

### □ Net profit higher by 53.2%yoy at Rs2.99bn – above expectations

The company's net profit was higher by 53.2% yoy at Rs2.99bn and was above our expectations of Rs2.7bn. Strong growth in net profit was driven mainly by a very strong growth in operating profit. Other income for the quarter was higher by 24%yoy at Rs551m. The effective tax rate for the quarter was 30.8% against 31.7% in Q4FY07 and Q3FY08.

### □ FY08 net sales up 4.4% at Rs103.3bn, net profit up 12.8% at Rs9.68bn

Hero Honda's FY08 net sales grew by 4.4% to Rs103.3bn with volumes remaining flat at 3.34m units. EBITDA grew by 15.0%yoy to Rs13.49bn with EBITDA margin at 13.1% against 11.8% in FY07. Growth in EBITDA margins despite volumes remaining flat was aided mainly by a improved product mix as well as a tight control on advertising and marketing spends (other expenses remained flat at Rs11.9bn). PAT grew by 12.8% to Rs9.68bn and the company declared a dividend of 950% for FY08 (850% in FY07).

### □ Valuations and view – Maintain Neutral

We have a muted outlook for the two-wheeler industry and expect the historical double digit growth trajectory to shift downwards to a single digit one due to rising urban penetration levels. Further, interest rates on two-wheelers have risen from 18% to 24% (on a reducing balance basis) over the last few months and financing norms continue to remain very stringent. Even as the growth momentum continues to remain a concern for the industry, leading two-wheeler players have commissioned their new plants in the recent past. As a result we believe the industry would continue to witness increasing competitive intensity accompanied by lack of pricing discipline. Resultant, we maintain our Neutral rating on the stock.

#### Quarterly results

Year to 31 March (Rs m)	Q4 FY07	FY07	Q1 FY08	Q2 FY08	Q3 FY08	Q4 FY08	FY08
<b>Sales</b>	<b>26,396</b>	<b>99,000</b>	<b>24,480</b>	<b>23,521</b>	<b>27,431</b>	<b>27,887</b>	<b>103,318</b>
yoy chg	11.6	13.6	3.5	5.5	2.9	5.6	4.4
<b>Operating profit</b>	<b>2,687</b>	<b>11,730</b>	<b>2,635</b>	<b>2,914</b>	<b>3,826</b>	<b>4,118</b>	<b>13,493</b>
yoy chg	(15.8)	(14.0)	(17.4)	2.8	26.7	53.3	15.0
Other income	445	1,899	389	393	521	551	1,854
Interest	(76.9)	(229.9)	(89.5)	(100.8)	(87)	(81)	(358.0)
Depreciation	355	1,398	376	384	408	435	1,603
PBT and extraordinary items	2,854	12,461	2,737	3,023	4,026	4,316	14,103
Extraordinary items	0.0	0.0	0.0	0.0	0.0	0.0	0.0
PBT	2,854	12,461	2,737	3,023	4,026	4,316	14,103
Tax	904	3,882	839	980	1,276	1,329	4,424
<b>PAT</b>	<b>1,950</b>	<b>8,579</b>	<b>1,898</b>	<b>2,043</b>	<b>2,750</b>	<b>2,987</b>	<b>9,678</b>
yoy chg (%)	(18.0)	(11.7)	(20.1)	(5.4)	31.5	53.2	12.8
Cash profit	2,305	9,977	2,274	2,427	3,158	3,422	11,281
OPM (%)	10.2	11.8	10.8	12.4	13.9	14.8	13.1
NPM (%)	7.4	8.7	7.8	8.7	10.0	10.7	9.4
Other income/PBT (%)	15.6	15.2	14.2	13.0	12.9	12.8	13.1
Outstanding shares (m)	199.7	199.7	199.7	199.7	199.7	199.7	199.7
EPS (Rs)	9.8	43.0	9.5	10.2	13.8	15.0	48.5
Cash EPS (Rs)	11.5	50.0	11.4	12.2	15.8	17.1	56.5
PER (x)		18.0					15.9
P/CEPS (x)		15.5					13.7

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