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Rating	Accumulate
Price	Rs2,624
Target Price	Rs2,849
Implied Upside	8.6%
Sensex	28,072
Nifty	8,517

(Prices as on August 04, 2015)

Trading data	
Market Cap. (Rs bn)	524.0
Shares o/s (m)	199.7
3M Avg. Daily value (Rs m)	1424.8
Major shareholders	
Promoters	34.64%
Foreign	38.45%
Domestic Inst.	13.44%
Public & Other	13.47%

(%)	1M	6M	12M
Absolute	1.8	(7.3)	0.9
Relative	1.9	(4.5)	(8.2)
How we differ from Consensus			
EPS (Rs)	PL	Cons.	% Diff.
2016	153.1	146.6	4.5
2017	181.8	171.4	6.1

Price Performance (RIC:HROM.BO,BB:HMCL IN)



Source: Bloomberg

HMCL's results were better than expectations due to the improved operating performance. After two consecutive quarters of disappointing at the EBITDA level, operating performance was much stronger than expected during Q1FY16.

HMCL's results were better than expected as the benefits from input cost reduction and cost control program flowed in. While margin outlook for Q2 also appears good, the normal trend of lower H2 margins should sustain yet again. Demand outlook for two-wheelers in FY16 remains weak, with incremental sales moving to HMCL's competitors. Rural demand remaining subdued is a key concern for HMCL, as is the higher than normal channel inventory. Our residual growth estimate for FY16 is 4.4%.

We factor in higher EBITDA margins in FY16 & FY17, due to which our EPS estimate is increased by 3.7% and 2.2%, respectively. We maintain 'Accumulate' with a price target of Rs2,849 (from Rs2,699 previously). At the current market price, the stock is trading a 17.1x FY16E and 14.4x FY17E EPS.

- Total income declined 1.2% YoY to Rs69.55bn. Volume decline was 4.1% YoY, while realisations grew 2.1% YoY. Other operating income was significantly higher at Rs993m (up 165.2% YoY).
- EBITDA margin was 15.1%, which was better than expected (higher 160bps YoY and higher 280bps QoQ), leading to EBITDA growth of 10.6% YoY (up 25% QoQ). After two successive quarters of YoY EBITDA decline, HMCL recorded decent EBITDA growth during Q1FY16.

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Key financials (Y/e March)	2014	2015	2016E	2017E
Revenues (Rs m)	252,755	275,853	288,166	328,757
Growth (%)	6.3	9.1	4.5	14.1
EBITDA (Rs m)	35,401	35,422	41,643	48,748
PAT (Rs m)	21,091	23,856	30,583	36,305
EPS (Rs)	105.6	119.5	153.1	181.8
Growth (%)	(0.4)	13.1	28.2	18.7
Net DPS (Rs)	65.0	60.0	75.0	95.0

Profitability & Valuation	2014	2015	2016E	2017E
EBITDA margin (%)	14.0	12.8	14.5	14.8
RoE (%)	39.8	39.3	41.8	40.5
RoCE (%)	39.9	39.4	41.8	40.5
EV / sales (x)	2.1	1.9	1.8	1.6
EV / EBITDA (x)	14.8	14.7	12.5	10.7
PE (x)	24.8	22.0	17.1	14.4
P / BV (x)	9.4	8.0	6.5	5.3
Net dividend yield (%)	2.5	2.3	2.9	3.6

Source: Company Data; PL Research

- Gross margins improved 340bps YoY and 100bps QoQ due to a combination of lower commodity prices, increased excise duty in Q4, and the cost reduction program.
- The benefit of further commodity cost reduction during Q1 could be felt in Q2 by HMCL.
- Staff costs / sales ratio was up 70bps YoY (flat QoQ) on commissioning of the new plant at Neemrana and an increase in the R&D staff.
- Other expenditure / sales ratio was higher by 120bps YoY, but lower 170bps QoQ. Normally, HMCL's adspend is on the higher side in H2. After the Q4 results, management had commented that the advertising and publicity spend was likely to be higher in the next two years.
- With the amortised royalty payment ending in Q1FY15, depreciation and amortisation was lower by ~64% in Q1 as well, which resulted in adjusted profit growth of 33.3% YoY to Rs7.5bn, despite a higher effective tax rate.

Conference call highlights

- Gross margin improvement was due to two factors: 50-60bps impact on input cost reduction and 70-80bps impact on excise duty increase.
- Targeted savings from the LEAP program are between Rs1.75-2bn during FY16 (Rs1.69bn in FY14 and Rs3.26bn in FY15).
- Q2FY16 margins should be healthy and may range higher than 15%, while for FY16, HMCL should witness a YoY improvement.
- Channel inventory stands at 5-6 weeks. While this is on the higher side, it should not reduce significantly as September onwards, the ramp-up for the festival season commences.
- New scooter models will be launched within the next two quarters.
- Adspend should be higher in Q3 as the company would sponsor events like the football league, etc.
- Work on the overseas plans is commencing, with the Colombia plant to be inaugurated in early September and the Bangladesh plant to be ready in Apr'16.
- HMCL maintains its vision stands to sell 1.2m units by 2020 (implying a volume growth CAGR of 12.6% over FY15-20). Of the total volumes, the targeted exports are export share is 10%.

Exhibit 1: Q1FY16 Result Overview (Rs m)

Y/e March	Q1FY16	Q1FY15	YoY gr. (%)	Q4FY15	FY16E	FY15	YoY gr. (%)
Net Revenues	69,553	70,368	(1.2)	67,939	288,166	275,853	4.5
Raw Materials	48,105	51,112	(5.9)	47,696	198,599	197,539	0.5
% of Net Sales	69.2	72.6		70.2	68.9	71.6	
Personnel	3,144	2,678	17.4	3,040	13,126	11,729	11.9
% of Net Sales	4.5	3.8		4.5	4.6	4.3	
Manufacturing & Other Exp	7,825	7,107	10.1	8,819	34,798	31,163	11.7
% of Net Sales	11.3	10.1		13.0	12.1	11.3	
Total Expenditure	59,074	60,896	(3.0)	59,555	246,523	240,431	2.5
EBITDA	10,479	9,472	10.6	8,384	41,643	35,422	17.6
EBITDA Margin (%)	15.1	13.5		12.3	14.5	12.8	
Depreciation	1,030	2,915	(64.7)	897	4,267	5,400	(21.0)
EBIT	9,449	6,557	44.1	7,486	37,376	30,022	24.5
Interest Expenses	5	30	(82.2)	8	38	111	(65.4)
Non-operating income	1,019	1,128	(9.6)	929	5,436	4,927	10.3
Extraordinary Expenses	-	-	-	1,550	-	1,550	-
PBT	10,463	7,655	36.7	6,857	42,773	33,288	28.5
Tax-Total	2,959	2,027	46.0	2,092	12,190	9,432	29.2
Tax Rate (%) - Total	28.3	26.5	6.8	30.5	28.5	28.3	0.6
Reported PAT	7,503	5,628	33.3	4,765	30,583	23,856	28.2
Adj. PAT	7,503	5,628	33.3	6,316	30,583	25,407	20.4

Source: Company Data, PL Research

Exhibit 2: Operating Metrics

Y/e March	Q1FY16	Q1FY15	YoY gr. (%)	Q4FY15	FY16E	FY15	YoY gr. (%)
Sales Volume (nos)	1,645,543	1,715,129	(4.1)	1,575,501	6,713,936	6,631,826	1.2
Net Realisation/Vehicle	42,267	41,028	3.0	43,122	42,921	41,595	3.2
Material cost / vehicle	29,234	29,800	(1.9)	30,273	29,580	29,787	(0.7)
Gross Profit / vehicle	13,034	11,228	16.1	12,848	13,340	11,809	13.0
Employee cost /vehicle	1,911	1,561	22.4	1,929	1,955	1,769	10.5
Other expenses / vehicle	4,755	4,144	14.8	5,598	5,183	4,699	10.3
EBITDA/vehicle	6,368	5,523	15.3	5,321	6,202	5,341	16.1
Net Profit/vehicle	4,560	3,281	39.0	4,009	4,555	3,831	18.9

Source: Company Data, PL Research

Income Statement (Rs m)

Y/e March	2014	2015	2016E	2017E
Net Revenue	252,755	275,853	288,166	328,757
Raw Material Expenses	182,299	197,539	198,599	227,875
Gross Profit	70,456	78,314	89,567	100,883
Employee Cost	9,300	11,729	13,126	14,649
Other Expenses	25,755	31,163	34,798	37,486
EBITDA	35,401	35,422	41,643	48,748
Depr. & Amortization	11,074	5,400	4,267	4,379
Net Interest	(653)	(613)	(672)	(860)
Other Income	4,464	6,478	5,436	6,085
Profit before Tax	28,673	36,389	42,773	50,424
Total Tax	7,582	9,432	12,190	14,119
Profit after Tax	21,091	26,957	30,583	36,305
Ex-Od items / Min. Int.	—	—	—	—
Adj. PAT	21,091	23,856	30,583	36,305
Avg. Shares O/S (m)	199.7	199.7	199.7	199.7
EPS (Rs.)	105.6	119.5	153.1	181.8

Balance Sheet Abstract (Rs m)

Y/e March	2014	2015	2016E	2017E
Shareholder's Funds	55,999	65,413	81,018	98,352
Total Debt	—	—	—	—
Other Liabilities	(1,060)	(735)	(735)	(735)
Total Liabilities	54,939	64,678	80,283	97,616
Net Fixed Assets	30,974	36,252	48,485	58,106
Goodwill	—	—	—	—
Investments	40,888	31,541	39,541	49,541
Net Current Assets	(16,922)	(3,116)	(7,743)	(10,031)
<i>Cash & Equivalents</i>	<i>1,175</i>	<i>1,593</i>	<i>3,820</i>	<i>3,309</i>
<i>Other Current Assets</i>	<i>26,877</i>	<i>35,096</i>	<i>29,470</i>	<i>31,870</i>
<i>Current Liabilities</i>	<i>44,974</i>	<i>39,804</i>	<i>41,034</i>	<i>45,210</i>
Other Assets	—	—	—	—
Total Assets	54,939	64,678	80,283	97,616

Cash Flow Abstract (Rs m)

Y/e March	2014	2015	2016E	2017E
C/F from Operations	30,003	19,403	41,743	42,491
C/F from Investing	(15,366)	(1,332)	(24,500)	(24,000)
C/F from Financing	(15,273)	(14,553)	(15,016)	(19,002)
Inc. / Dec. in Cash	(635)	3,518	2,228	(511)
Opening Cash	1,810	1,175	1,593	3,820
Closing Cash	1,175	4,693	3,820	3,309
FCFF	21,552	5,188	25,205	28,461
FCFE	21,552	5,188	25,205	28,461

Quarterly Financials (Rs m)

Y/e March	Q2FY15	Q3FY15	Q4FY15	Q1FY16
Net Revenue	69,153	68,393	67,939	69,553
EBITDA	9,348	8,218	8,384	10,479
<i>% of revenue</i>	<i>13.5</i>	<i>12.0</i>	<i>12.3</i>	<i>15.1</i>
Depr. & Amortization	750	838	897	1,030
Net Interest	49	24	8	5
Other Income	1,935	936	929	1,019
Profit before Tax	10,484	8,292	6,857	10,463
Total Tax	2,851	2,462	2,092	2,959
Profit after Tax	7,634	5,830	4,765	7,503
Adj. PAT	7,634	5,830	6,316	7,503

Key Financial Metrics

Y/e March	2014	2015	2016E	2017E
Growth				
Revenue (%)	6.3	9.1	4.5	14.1
EBITDA (%)	7.8	0.1	17.6	17.1
PAT (%)	(0.4)	13.1	28.2	18.7
EPS (%)	(0.4)	13.1	28.2	18.7
Profitability				
EBITDA Margin (%)	14.0	12.8	14.5	14.8
PAT Margin (%)	8.3	8.6	10.6	11.0
RoCE (%)	39.9	39.4	41.8	40.5
RoE (%)	39.8	39.3	41.8	40.5
Balance Sheet				
Net Debt : Equity	—	—	—	—
Net Wrkng Cap. (days)	(19)	(19)	(29)	(29)
Valuation				
PER (x)	24.8	22.0	17.1	14.4
P / B (x)	9.4	8.0	6.5	5.3
EV / EBITDA (x)	14.8	14.7	12.5	10.7
EV / Sales (x)	2.1	1.9	1.8	1.6
Earnings Quality				
Eff. Tax Rate	26.4	28.3	28.5	28.0
Other Inc / PBT	15.6	14.8	12.7	12.1
Eff. Depr. Rate (%)	14.1	6.0	4.0	3.7
FCFE / PAT	102.2	21.7	82.4	78.4

Source: Company Data, PL Research.

Key Operating Metrics

Y/e March	2014	2015	2016E	2017E
Two-wheeler volume (units)	6,245,960	6,631,826	6,713,936	7,377,832
Realisation per unit (Rs)	40,226	41,241	42,500	44,123
Gross margin per unit (Rs)	11,280	11,809	13,340	13,674
EBITDA per unit (Rs)	5,668	5,341	6,202	6,607
Profit per unit (Rs)	3,377	3,831	4,555	4,921

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