



# "Hero MotoCorp Limited Conference Call"

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*Hero MotoCorp Limited*  
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**Moderator:** Ladies and gentlemen, good day and welcome to the Hero MotoCorp Q3 Financial Year 2014 Earnings Conference Call hosted by Motilal Oswal Securities. As a reminder all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during this conference call please signal an operator by pressing \* and then 0 on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Chirag Jain from Motilal Oswal Securities. Thank you and over to you Mr. Jain.

**Chirag Jain:** Good afternoon everyone. On behalf of Motilal Oswal Securities I would like to welcome you all to Q3 FY 2014 post results conference call of Hero MotoCorp Limited. Hero MotoCorp Limited is represented by Mr. Ravi Sud, Senior Vice President and CFO and Mr. Anil Dua, Senior Vice President, Marketing and Sales and Mr. Surender Chhabra, Vice President, Finance. I would request the management for their brief opening remarks on the results and thereafter we can open it up for Q&A session. Over to you Sir.

**Ravi Sud:** Thank you Chirag and welcome to everybody for joining this call for Q3 numbers of Hero MotoCorp Limited. I will give you a brief rundown. As far as volumes are concerned we have done 1.68 million two wheelers compared to 1.57 million in the corresponding quarter last year. As far as turnover is concerned this is 6876 Crores versus 6187 Crores in the corresponding period. I also must state that our volumes are the highest ever in a quarter so is the turnover which is close to 6900 Crores. As far as EBITDA is concerned, for the quarter is 898 Crores and profit after tax is 525 Crores versus 488 Crores showing a growth of around 7.5%. Before we go to the question and answer session there are a few things I would like to clarify. Our turnover has grown by around 11%; our profit after tax has grown by only 7.5%. I think one important factor is that in the current year that is FY 2014 our tax rate has gone up to close to 27% as all of you are aware because the Haridwar plant tax benefit which used to be 100% for five years till FY 2013 has come to a partial end, now we are getting exemption only on 30% of our profit. Last year the tax rate was close to 16 to 16.5% which now has jumped to 27% that is why the increase in tax is not in line with increase in the turnover, however if you look at our profit before tax for the quarter is 717 Crores versus 582 Crores which shows a very, very healthy increase of 23% but most of it has been offset by increase in tax rate.

Now, second important aspect which we have been saying every quarter that with most of our vendors we work with a lag of one quarter and that currency fluctuation in the second quarter the impact of which has come in the third quarter and apart from this, some of the metals which had started showing upward trend in third quarter have also been accounted for in the third quarter leading to erosion of EBITDA of close to 1% point. With these we can start with Q&A.

**Moderator:** Ladies and gentlemen, we will now begin the question and answer session. The first question is from the line of Jay Kale from IDFC Securities, please go ahead.

- Pramod:** Good afternoon sir, this is Pramod here from IDFC. Sir, my first question pertains to other expenditure. There is a dramatic jump in other expenditure from 569 Crores to 740 Crores this quarter, if you can just throw some color as to what is the nature of this jump, whether it is all operational and recurring?
- Surender Chhabra:** Our expenditure, mainly if you see compared to the last two quarters because normally in the first quarter and second quarter they normally have low publicity spend but in the third quarter because of festival period we have certain print media ads as well as on air also, so the spend was slightly more as compared to the previous two quarters.
- Pramod:** Is it like the second half is normally higher, can we expect a similar phenomenon in Q4?
- Surender Chhabra:** Normally it is the third quarter where we have the highest expenditure on publicity because of festival season.
- Pramod:** What would be the impact of loyalty schemes and other incentives what were there in the month of December, has it been very high or is it small marginal impact?
- Anil Dua:** I think there is a very marginal expenditure that we have done on loyalty schemes. It is a very miniscule spend and basically this is I think they had clarified in the course of the quarter, this is part of our customer relationship program where it will be going to our existing customers and saying that those who want to upgrade or want to buy additional bikes they have the incentive to do so under this program, so this was done in the month of December to support a market which is relatively weak.
- Pramod:** So, there are no lumpy one-off or any exceptional hits in the other expenditure, is that clear?
- Anil Dua:** Outbound logistic cost is part of other expenditure though we are recovering from the dealer which sits in the revenue but expense comes out of the head of other expenditures, so there is also an increase because of diesel price increase.
- Pramod:** So the percentage margin as we calculate normally gets a bit depressed because of this methodology?
- Anil Dua:** Sir, your launch pipeline is quite busy going forward with four new launches, so how should one look at the marketing and brand spend as a percentage of revenue as you go forward, is it fair to assume it is going to remain elevated and last quarter result you had talked about some savings which will kick in second half to the tune of around 80 Crores for second half, have they already hit and what is the R&D expenditure for the quarter?
- Ravi Sud:** I think your question needs to be answered in two or three parts. Let me first answer your question about the savings part. As we had shared in our Q4 earnings call that we had initiated a major margin transformation project and in Q2 I had said that in the second half we will start seeing the benefits. I am pleased to inform that we are on the verge of closing the wave 2, each

wave is of four months, we are closing wave 2 by January 31, 2014 and in Q3 there has been the actual accrual of about 45 Crores which has gone in to the bottomline and in the month of January our run rate for month of savings is about 17 Crores per month.

**Pramod:** You said Q2; I think you are referring to Q3?

**Ravi Sud:** Sorry, Q3, I am talking of the quarter.

**Pramod:** Okay and sir my query related to marketing and brand spends considering the launch pipeline?

**Anil Dua:** Pramod, yes we are very aggressive with our launches. We have announced 15 in the month of October and we have shown another five yesterday, I think the important point to note is that out of this 15 launches you would not have seen any big TV campaign against any of them, so fundamentally the way we are looking at these launches it is not that every launch comes with a massive campaign spend. There are different strategies for different brands, many of them are local and actually 11 models out of the 15 that we have launched the only one which is going to go with the new TV campaign is Splendor ismart which has taken the market by storm and is doing very well, overall despite these launches our marketing spends will remain in the region you have known which is in the region of 2 to 2.5% of revenue that is what a normal marketing spend every year is and this year will be no different.

**Pramod:** Sir finally on R&D expenses because you were supposed to start booking them from this quarter?

**Ravi Sud:** As I stated in the Q2 call FY 2013 we have R&D expenditure as a percentage of net revenue was about 0.45%, this year we are expecting it will be around 0.75%.

**Pramod:** Has there been any one-off pertaining to R&D expense which has been booked entirely in Q3 and other expenditure, anything like that or is it more of a recurring head because I am trying to understand whether that is also part of the reason for the jump in other expenditure in a big way?

**Anil Dua:** Yes there was I think some expenditure in relation to the product launches which had taken place during the quarter was booked in R&D.

**Pramod:** Okay, nothing pertaining to H1 which has got booked in this quarter that is what I am trying to clarify?

**Ravi Sud:** Your question is not clear. Can you repeat your question?

**Pramod:** Is there any R&D expenses pertaining to first half which has got booked in Q3 or is it only pertaining to Q3 R&D expenses?

**Ravi Sud:** I have clarified it many times. As you know any payment which you are making toward the development of products to our technology partners, is being treated in the books as Advances. Only when the model come in to commercial production we start charging those to revenue, so if

we have launched a model in the month of say November it will be booked in the month of November, so there is no question of deferring Q2 expenditure relating to R&D to Q3.

**Moderator:** The next question is from the line of Vinay Singh from Morgan Stanley, please go ahead.

**Vinay Singh:** The first question is for Mr. Dua. In the festive season we have seen pretty much, and you guys are also very confident about the retail offtake but then December has been exceptionally weak for all vendors and we have also gained zero operating loyalty schemes. Is environment actually deteriorating that is why you are being pushed in to spending more on advertising and not being able to fully pass on the inflationary pressure and the second question is more on the long term margin profile. We know that Hero is targeting fix line margins but given the inflationary environment and all the loyalty schemes and advertising spend how does that change?

**Anil Dua:** Let me answer your first part and let Ravi answer the long term marginal profile bit. On the first part which is on the festival schemes and loyalty and festival spends and sentiment in the market absolutely right that the sentiment was very good during the two months of festival of October and November. We did some exceptional numbers like we sold 1.2 million in the months of October and November. We sold 1.1 lakh on the single day of Dhanteras, so it was great going. Now December weak sentiment is something which we are used to as the industry is used to year after year, so you will recall that even last year in December we had run some kind of an incentive for the dealers and there was a question that we had probably discussed in a similar call and this time we tried something else, you know with the end customer we ran some kind of a loyalty program under which we might have sold only 15 or 20,000 bikes out of a total sale of about 4 lakh, so really that is a miniscule part which is what I was trying to emphasize in the earlier answer as well and as I said despite all this the marketing spend the advertising spend it is not egregious, it is not outlandish, it is going to remain 2 to 2.5% of the total revenue for the year, so the market sentiment which is very good in October November predictably came down in December because people postponed their purchases to buy the New Year model. In January that lull kind of continues for 15 days after which you start seeing some kind of offtake which we are also seeing right now in the second half of January, so I will say that I am not foreseeing any major spends which can erode margin or which can take marketing spends beyond 2 to 2.5%, so I will say there is no concern on that and let Mr. Sood address the long term margin profile.

**Ravi Sud:** Margin is a function of many, many things. Margin is a function of product mix, your selling price, your realization and your input cost. I think what we have seen in Q3 is the global market or the Indian economy has been very, very slow but we have seen surge in metal prices and as far as Q4 is concerned, we are not expecting any further surprises. Since you are talking of long term as I stated earlier this program which we are running which is a medium to long term type of program which will continue till FY 2017, our aspiration and our confidence today that we should be able to add about 300 basis points net to the EBITDA margin by virtue of these programs because we have booked about 45 Crores on a turnover of around 6900, works out to about 65 basis points, this now has been eroded because of the unexpected foreign currency fluctuations and input cost which have been only partially recovered in the quarter.

- Vinay Singh:** What exactly are long term margin target now?
- Ravi Sud:** If you look at our EBITDA as of now is between 13 to 14; so you add another 300 basis points by FY 2017.
- Vinay Singh:** Sir, anything on price hikes taken like when you say currency fluctuations hit you it is basically weak INR lead inflation that has crept in, so the price hikes taken in October were not enough to offset that and we have seen that Honda has not been taking price hikes, so do you think that the equation is slightly changing that it will be difficult to pass on inflation led pricing action in the coming year?
- Ravi Sud:** As you have noticed in the last six to eight quarters our industry has become extremely competitive and I think all players have taken a price increase in October and November and we understand that Honda has not taken any price increase. Whatever price increases we have taken that have partially covered the costs.
- Moderator:** The next question is from the line of Jamshed from Citigroup, please go ahead.
- Jamshed:** Good afternoon and thanks for the opportunity, just a question on the new launches that you all showcased yesterday, will you all be extending the five year warranty even on these new models?
- Ravi Sud:** Though I must say that specifically model wise calls are taken when the models are launched and therefore it will not be fair for me to right now say that definitely they will all have a five-year warranty but what I can say is that we have committed to the program we have started of five year warranty and as far as possible we do plan to extend five year warranty but still we will take a call closer to the time of launch of each model.
- Jamshed:** Mr. Dua, you indicated in your earlier comments that 11 of the 15 odd brands are kind of localized. Is this a sort of shift in strategy where you all are moving more towards looking at niches or particular segments?
- Anil Dua:** Jamshed I think I don't know what you mean by localized?
- Jamshed:** Fair enough, I mean more region centric.
- Anil Dua:** Let me clarify that. There are 15 models we had announced, 15 new launches we had announced out of which 11 we physically started dispatching to the market and selling to the customers, 4 we are yet to sell. None of these are local in nature; all of them are national in nature but many of them are actually refreshes of current models which in the festival quarter we wanted to refresh our entire range, we also wanted to followup on our philosophy of sale tech and style tech that we shared with you, so we improved our bikes on breaking distance. We included a side stand indicator in these bikes and did a general refresh in terms of colors and stripes and therefore these have not added to our portfolio of models, so almost every brand HF Dawn, HF Deluxe, Splendor pro, Passion Pro have similarly got refreshed and we have started selling these new models in the

market, those therefore are not local models and they are not really adding to our model portfolio. The new models which have come, let me talk specifically about them, these are Splendor ismart, which is a new model which comes with idle stop and start technology which is getting very good response and this is the model which we will support with TV campaign which is yet to start which you will see in this quarter, in Q4 that is a new model and then there are two models which are variants of distinct brands so there is HF Deluxe. We have launched a green bike which comes with aerodynamic guards etc., which we are calling Eco Deluxe, it is a variant. It is a national brand but it is a variant of HF Deluxe and similarly there is one more variant, so really it is not that our model portfolio which was 15 brands have now become 30; 15 brands have probably become 16 and there are variants, there are refreshes which mark this and that is why there is no huge spurt in advertising expenditure but certainly there is a huge spurt in customer interest because there is no news, because our showrooms are looking more attractive with new models and therefore there is far more excitement for a first customer as well as end customer so I hope that clarifies your concern on these 11 launches. There is no shift in strategies. In the past you would have heard me say that every year we bring 7 to 8 new news. This time we brought much more than 7 to 8 new news that is the only difference.

**Jamshed:** Sir if I may add directionally as you will get more aggressive in terms of variants and refreshers and especially more variants does this mean that the dealers will have to absorb more inventory just in terms of number of models?

**Anil Dua:** What happens is that we also keep rationalizing various SKU, so as we bring in new models we also look at our existing portfolio and if there are certain color which are not selling very well, certain SKU which are not selling very well, we cut back on those also so that there is a manageable portfolio of SKU available, having said that yes if a new model is started it certainly adds another line in the dealer inventory but also you will see that we have also been expanding our network, so it is our effort to see that despite more SKU we keep diesel inventory within the norms that we have specified.

**Moderator:** The next question is from the line of Amin Pirani from Deutsche Bank, please go ahead.

**Amin Pirani:** Hi sir, thanks for taking my question, first question I will just go back on the other expenses line. I agree with you that the third quarter is a regular phenomenon when your advertising spend goes up but could you help us with the kind of quantum because this year the increase seems to be quite high especially given that you have also booked cost savings, could you help us with the kind of quantum of how much you spend on specific advertising during this quarter or any in particular branding expenditure?

**Surender Chhabra:** Amin, we should not go from quarter-to-quarter basis because we are giving guidelines that our total spend on the publicity is in the range of 2 to 2.5% annually. It varies from quarter to quarter, first two quarters I have told that we have less expenditure and the third quarter as compared to the first two quarters yes expenditure comparatively is high and we have explained that it was in the print media as well as in the IR also.

**Amin Pirani:** Can you share the number of royalty in the depreciation line, one time royalty that goes to Honda?

**Ravi Sud:** In 2011 when we amortized this payment it used to be about 179 Crores and just to give you a flavor in Q2 it was 215 Crores and in Q3 it is about 197 Crores.

**Amin Pirani:** How are you looking at the demand situation right now, I mean, third quarter was obviously a better quarter for you as well as the industry. What kind of trends are you looking at for the fourth quarter and probably next year?

**Ravi Sud:** Okay so third quarter looks very good overall but clearly October November are the months which are almost 10+ kind of a growth and then December is like a low single digit kind of growth for the industry. January I think the numbers are yet to come, so overall industry, fingers crossed but we feel that we are again talking of single digits in January, so if you look at YTD growth of the industry it is in the region of 5%, we believe it will remain in the region of 5 to 6% for the year as a whole.

**Moderator:** The next question is from the line of Govind Chellappa from Jeffries, please go ahead.

**Govind Chellappa:** Sorry, I am repeating the same question again, your other expenses as a percentage of sales is even compared to your normal seasonality of third quarter is extraordinarily high, I am not comparing with first half or second quarter but compared to third quarter in any year in the past it is by far the highest that you have ever recorded, so if you could just help us understand in this year did you spend higher proportion of your budgeted ad spend in third quarter compared to last year and also if there is any R&D cost that stands out during the third quarter?

**Ravi Sud:** I will explain it to you. As Mr. Chhabra said, let me tell you what are the four major heads in other expenditure, one is the freight, packing, forwarding that has gone up more than in proportion to sale because there have been diesel hikes which have been given to the transporters, second major element is royalty, this is not the royalty which goes as depreciation or amortization, it is royalty on four new products. If you know just to share with you the volumes of four new products in the first nine months are close to 550,000 versus 190,000 in nine months of the previous year, so the amount of royalty which is given as a percentage to Honda. The third element of major cost is NCCD expenditure which is basically for Haridwar, you know there has been litigation with excise authorities, so in 2010 we had taken a call that we will keep on paying this amount under protest because there is issue of interpretation of law, so if the production in Haridwar is high as you know we are producing about 9000 to 9200 bikes per day that element is also there, these are the three major elements which are higher compared to the increase in the turnover.

**Govind Chellappa:** Just on the advertising cost?



**Surender Chhabra:** You will be surprised if I tell you a figure, this is only 1 Crores higher than what it was in the last nine months, the corresponding nine months, I am talking of nine months to nine months. So this is again to allay the fear many of you had voiced on loyalty schemes etc., actually we have had good TV campaign you might have noticed on Splendor and on Maestro with Ranbir, quarter-to-quarter this should explain, there is hardly any difference, so there is no extraordinary spends happening on publicity and as Mr. Sood has explained there are other heads which are accounting for this increase.

**Govind Chellappa:** My second question is on Pleasure, while Maestro has done very well in the recent past which is probably why you are paying such a high royalty in the other expenses Pleasure seems to be quite weak, I think YTD even though scooter market is so strong Pleasure is down, could you just explain what is causing this loss in volumes?

**Anil Dua:** You know Pleasure is doing extremely well fundamentally. There are standalone outlets close to 40 which are viable only by selling Pleasure that we have across the country, so fundamentally the number pressure on Pleasure is because overall the scooter capacity is limited. Maestro is a new model which is also on air and therefore there is massive demand for this model and therefore our scooter mix in terms of production has been loaded towards Maestro. As we go forward our capacity is going up from 60,000 a month which is used to be the last quarter to 75,000 a month from this quarter and therefore that will relax pressure on Pleasure as well as we go forward while we will be able to increase volumes on Maestro. We do plan to come back with a new pleasure shortly which we have already showcased a while back and we will also firm up with a new campaign for that new Pleasure and we are pretty confident that this is the brand which has actually given rebirth to the scooters as a segment and this will come back strong.

**Govind Chellappa:** Just to clarify you are saying that you consciously push Maestro production at the expense of Pleasure even though it looks like after recurring royalty Pleasure makes higher margin than Maestro does.

**Anil Dua:** Our decisions have been market led rather than anything else and market when you launch a new model you need to support it fully, also when it is on air to fully justify the spends that you are making behind marketing of that model you must maximize the availability, so yes it has been a conscious choice to build Maestro as well while we protect Pleasure; Pleasure also because is a relaunch plant very shortly it is in our interest to actually go slow on dispatches of (indiscernible) 31.24.

**Moderator:** The next question is from the line of Nishit Jalan from Nomura Securities, please go ahead.

**Nishit Jalan:** Hello sir, thank you for giving me the opportunity, sir just one question, what was the average price increase that you took in October, your RM to sales have increased by almost 120 basis points sequentially and you got around 70 basis points benefits from cost savings, so does it mean that the cost pressure where around 2% of sales in addition to the price increase taken by you?

- Anil Dua:** Yes.
- Nishit Jalan:** What was the average price increase?
- Anil Dua:** We have taken price increase effective October 3 which was 750 at showroom on an average, so 500 to 1500 rupees if I recall correctly which averages about 750 rupees and you can see that while our volumes are up 7% our turnover is up 11% so that is also reflecting the impact of the price increase.
- Moderator:** The next question is from the line of Joseph George from IIFL, please go ahead.
- Joseph George:** Thank you sir for the opportunity. First question on the pressure on gross margins that you highlighted because of currency etc., would I be right in saying that given that our company has stabilized a bit and we have also seen some easing in global commodity prices would I be right in saying that coming in to the fourth quarter the pressure would have eased a bit?
- Ravi Sud:** To answer your question in two parts number one as far as commodities are concerned I think we were expecting that in Q2 that because of global slowdown and Indian economy also sluggish the commodity prices will not increase but that actually has happened in Q3 and our expectation is that they should stabilize where they are, we don't expect any further increase. As far as currency is concerned, rupee has been looking at 61.5 to 63 which seems to have stabilized and most of the damages was done in Q2 when it went up to 68.9 or 69, so we would expect that Q4 should be smooth.
- Joseph George:** Second question was the four or five models that you showcased yesterday, none of them except maybe the 110 cc scooter addressed high volume segments, so there was a 250 cc motorcycle, then a hybrid scooter and also a diesel concept. When can we expect some new model in the high volume 100 cc motorcycle segments especially in the context of the mention in the 2013 annual report that you have test fired a new 100 cc engine?
- Anil Dua:** If you just go back only a quarter you know when we showcased 15 models and I just spoke about refreshing our entire 100 cc range, Dawn, Deluxe, Splendor Pro, Passion Pro these are all very high volume models and the positive impact of that has been visible in this quarter which has been a record quarter with highest ever volume and turnover, so that is always our first priority and that is why we have done it first. Besides that the new models that we have launched the Splendor ismart which comes with a technology that we have applied patent for I3S is a model which as I just said it has the potential of being a high volume model and we are getting very good response, in fact in the very first quarter we are revising our capacity plans and we are hiking up the capacity of this model as we go forward. A player like us who is number one two-wheeler company has to look at not only high volume models but other models which cater to even smaller segments. The only thing I think different is that we do look that the models should be making a commercial sense and we launch that only in the right market at the right time, so not all the models that you saw yesterday are meant only for India, some of them are meant for

international markets and then to be brought back in to India and also some of them are concepts which maybe launched only after sometime. Xtreme Sports is another model which we showed yesterday which can get good volumes within the premium segment and get a good market share then in the premium segment, so it is a mix of models like it should be from a market leader like us.

**Joseph George:** Sir the savings that you mentioned 45 Crores could you give us some sense on how much of it is in the cogs line that is the raw material line and how much of it is in operating expenses broadly?

**Ravi Sud:** Let me tell you there are three buckets of savings. Number one saving is on account of price rationalization of some of our products and Anil, if you need, he will give you the details. When we took the price increase in October we had differentiated certain prices of scooters, we had increased prices of scooter and some models by more than other products because we thought there was an opportunity, second bucket is on account of material cost which has come through e-sourcing and some of the initiatives like raw material consolidation. Third bucket as of now is our outbound logistics cost. The savings on this account to the tune of around 40 Crores annualized, but since they have not implemented only in the third quarter those savings are small in nature as of now but the overall saving which are accrued to us because of all initiatives are about 45 Crores in Q3.

**Moderator:** The next question is from the line of Chirag Shah from Axis Capital, please go ahead.

**Chirag Shah:** Thanks for the opportunity; sir one question was on the spare parts. In the second quarter you highlighted that the spare part income had inched up slightly and it helped you in the gross margin, so how would be the spare part revenue in this quarter, would it as a percentage of sales be similar to the previous quarter or it has been lower?

**Ravi Sud:** The spare parts are in line with the previous quarter. There is no major change.

**Chirag Shah:** The percentage of sales they are largely similar.

**Ravi Sud:** Yes.

**Chirag Shah:** You highlighted that capacity increase from 60K to 75K in scooters so from when it would be implemented, is it from January itself or by end of March?

**Anil Dua:** We have started from January though the entire 75 will not happen from January but it will start moving up from 60 and over this quarter will come close to 75.

**Chirag Shah:** And beyond 75 if you can share your thoughts, how are you looking at increasing capacity?

**Anil Dua:** We are taking it one bite at a time. We are also launching as we have shown yesterday several scooter models, so we have our plans to increase the capacity further beyond this but currently

since we are just increasing capacity from 60 to 75 it would be premature to talk of further increases.

**Chirag Shah:** Let me put it another way, there is no capacity constraint as such in terms of land or something, you can keep on adding capacity by another 25 to 30,000 in a modular fashion, is it the right way of analyzing, in fact there is no major capacity constraint for which we take time for ramp up?

**Ravi Sud:** As you know our existing capacity is about 6.9 million, so as far as capacity is concerned that is not a constraint, the constraint is only ordering and getting the right equipment for a particular line which takes time, number one, and secondly to ramp up, like today I can say my capacity in scooter is 75, but can I produce 75 in January ? No, we will produce 65 - 67000, February would be 70 and March would be 75, so the time taken to ramp up the capacity.

**Chirag Shah:** Is it possible for you to clarify on the import, the impact of imports in the quarter as a percentage or in absolute amount how much it was which affected your gross margins, if you can roughly indicate how much that impact would be the adverse currency impact which is not recurring in nature at least in the near vicinity?

**Ravi Sud:** Chirag our total imports both direct and indirect, are 12 to 12.5% of our total material cost out of which 5% is direct import and that is mainly in dollars because we are importing alloy wheel from China. On the other end vendors, their major imports are in yen. They are also contributing 7.5%. The yen because of depreciation is helpful but rupees depreciation is not helpful, it is harmful.

**Moderator:** The next question is from the line of Pramod Amte from CIMB, please go ahead.

**Pramod Amte:** Sir, it is quite interesting to see the new concepts which you have unveiled, congrats on that bringing new ideas in to the sector but can you give more color in terms of where the technology for these has come through, how much is in house, how much is joint development and all, one, and second what is your assessment of potential for these products in whichever markets you are planning to launch them?

**Ravi Sud:** I will say ultimately these are all Hero products. We have our own ecosystem as our MD explained yesterday in the press conference of technology partners across the country, across the world, so we have our R&D global arm spreading in to US, Europe and we have our own R&D working here, so it is collaborative team effort between our partners and our R&D and all the five products that you have seen yesterday are a result of that. The one difference I would like to point out that two products that you saw yesterday are built on current platforms the Xtreme Sports is built on Current Xtreme and the scooter that you saw is built on current scooter platform but these three other products that you saw the Leap which is the hybrid scooter, RNT which is the diesel 150 and the 250 cc bike all these three are greenfield platforms developed by us along with the ecosystem of our partners that we spoke of, so that in terms of where these models come from.

In terms of timeline other than the concept RNT the balance four models will all be getting launched in the coming fiscal. Xtreme Sports is in first quarter, the scooter will be in the second quarter and the other two products will also happen in the second half of the coming year. In terms of potential, as we discussed that Xtreme Sports should be helping us increase our share in the premium segment where we have been planning to put a strategy together that is one segment where we have relatively low share and therefore this along with 250 cc should help us get addition volumes as well as a technology imaged above and innovation for us in this segment. The Leap is basically meant for global markets and would be brought back in to India from there, Dash the 110 cc scooter is certainly a high volume potential offering in a growing scooter market which as you know is growing almost 18% and YTD and you are going back 26% against that, so this should help us accelerate the growth further and leverage the capacity increases that we have been talking off.

**Pramod Amte:** Sir, coming to the manpower side you has been making big hires both on the technology front and the cost cutting which is impressive to see, so how have you been able to attract the talent in terms of and how will you be able to retain them both in terms of remuneration and the other factors?

**Ravi Sud:** Thank you very much for the compliment. In the last three years we have attracted a lot of talent in our R&D Centre. We had 171 engineers when we separated in 2011, as of now we got more than 450 plus and we have some expats, three Japanese expats and one Austrian expat. I think the challenge is exciting and providing them a challenging environment and freedom which we are giving and going forward we should be able to retain and attract more talent.

**Pramod Amte:** Is there any thought in terms of considering the challenges to go on ESOP or any of those programs?

**Ravi Sud:** That is a matter which needs to be decided by the Board. I would not like to comment on that.

**Pramod Amte:** Last question with regard to your cost cutting programs, you have already completed Wave 2, so would you like to give color in terms of Wave 3, what products you are addressing, which areas you plan to address there?

**Ravi Sud:** You see what I said earlier was we will have a relook at all our existing models and just to share with you that all 100 cc and 125 cc models we have got in wave 2; wave 3 we will be looking at 150 cc plus model and apart from looking at about 8000 Crores of spend on material cost.

**Moderator:** The next question is from the line of Jamshed Dey from Citigroup, please go ahead.

**Jamshed Dey:** Thank you again. What are your capacity plans and capex plans for the next couple of years that is FY 2015 and FY 2016?

**Ravi Sud:** Jamshed that seems to be a very favorable question every quarter and I would love to answer that once again. We have a capacity of 6.9 million as of now. The Neemrana plant is getting

commissioned by end of March we should be close to 7.65 million, that should happen say effective April 1, 2014 and as far as capex in the current year is concerned we expect about close to 1000 to 1200 Crore because we have certain LCs which we expect to be paid before March 31. Now, beyond 7.65 million capacity we have the Gujarat plant, here we have already started boundary wall construction, that plant ultimately will have a capacity of 1.8 million and expenditure on that is close to 1075 Crores and most of this expenditure should come in FY 2015 of phase I with a capacity of around 900,000. Balance will come in FY 2016 and maybe first quarter of FY 2017. Apart from this we have Global Power Center more so the expenditure of that will come in the present year and maybe some left over if they go to FY 2015. Kukas, where we are starting our new Innovation and R&D Center where the construction work is going to start, that expenditure of around 450 Crores will come in FY 2015.

**Jamshed Dey:** Sir, is it fair to assume with this lump of capex behind you by FY 2015 FY 2016 and the meaningful increase that you are all are targeting in March FY 2017 dividend payout should step up substantially when you look beyond three years?

**Ravi Sud:** We have a very, very consistent type of dividend payout policy. We are between 35 to 45% and you leave aside those special dividends that I say is the privilege and privilege out of the Board of the company. As far as today is concerned I will feel that current dividend ratio of 35 to 45% is a reasonable assumption.

**Moderator:** Next question is from the line of Elizabeth John from Crisil, please go ahead.

**Elizabeth John:** Hello thank you for taking my question. I was actually referring to the new model launches which we have done and you have already highlighted about that, just wanted to have little more understanding about the Leap Model the hybrid scooter where it was mentioned that probably it would be targeting the global market first, something on in terms of mileage and you know in terms of what kind of markets are we looking at in Xsports?

**Anil Dua:** Leap is a very important model for us and I think it also represents the fact that Hero when a couple of years back started on its solo journey it had showcased this as a concept at 2012 auto expo and at that time probably no one would have thought that at this auto expo or even ahead of this auto expo we will be showing it so to say flesh and blood as a preproduction model, very soon to be launched in the global market, so this shows not only our concern for environment and therefore launching of a green hybrid technology but also our progress on how quickly we managed to ramp up our capability of turning around such complex projects from concept to reality. The market that we plan to get in to as we clarified yesterday is the developed western world as a lower hanging fruit we have looked at Africa and South American countries first in our international business but going forward we certainly plan to go across to more continents say Europe, US, etc., where a product like this should have a very good market. As was said yesterday this is a premium product, it had state of the art technology built in to it including a

range extender. Since you asked me about the mileage of this product it is exceptional mileage, I will not get in to specific results but I will reiterate what we shared yesterday that compared to normal electric vehicles which have double digit kilometer range and low double digit kilometers this may be more than 300 kilometer range and therefore it is an exceptionally high performing great value scooter, hybrid scooter which we will be bringing and as we said we will start in the global markets of the west but eventually we do plan to bring it back to India as well.

**Moderator:** The next question is from the line of Dipen Sanghvi from Enam Asset Management Company, please go ahead.

**Dipen Sanghvi:** Hello Sir, my question is specifically, first question is related to Mr. Dua. We keep hearing post festival season there was a lot of slowdown in the industry overall and inventory pile up in the system, so if you can tell me what will be your current inventory, if you can give me absolute number of the number of weeks?

**Anil Dua:** I think we actually had excellent festival and inventories were at a very manageable level but in the month of December the industry had seen slowdown beyond expectation and I think inventory across industry had gone up to about 6 to 7 weeks and our inventories are in line with that figure of six weeks.

**Dipen Sanghvi:** I mean absolute numbers will be around 6, 80, 000.

**Anil Dua:** I did not make a calculation because it is changing by the day and as I said January second half we have seen good spurt from something like 15000 sales a day, the sales have gone up to beyond 20,000 a day and hopefully the trend will continue in to February. The rural numbers are looking very good. The agricultural report is good, agricultural growth is good. I think the demand should come in, so I think the number is a little fluid as we go forward. We have about six weeks of inventory but it seems to be going down as we go forward.

**Dipen Sanghvi:** How would it have affected our receivables as compared to one quarter back and compared to last year same quarter?

**Surender Chhabra:** Receivables I think for the time being are monthly as compared to the previous quarter but because after December mid of 15 January onward I can see the detail is good, receivables are coming under control.

**Dipen Sanghvi:** If you can give me some number of days or absolute amount that will be really helpful?

**Surender Chhabra:** As compared to 10 days of normal receivables we have at this point of time 13 to 14 days of receivables.

**Dipen Sanghvi:** Sir we had initially at the beginning of the year targeted a very high number of exports for FY 2014, I believe we are kind of little lagging behind due to some delays and all, what is the current outlook on FY 2015 exports volumes?

**Anil Dua:** You are right, in terms of exports I feel the last two years have been very tough for the industry especially last year in more than a decade the industry saw some kind of a decline and this year also the year started very sluggishly on exports front but it has started picking up off late for last two quarters. As far as we are concerned we have seen this year as a formative year in which we are planning to consolidate our presence and get in to new markets in a slow and steady manner deliberately seeing the global conditions and also wanting to launch the right products in the right markets and we are currently in more than 15 markets and by the end of this quarter we are likely to be in 20 markets. You will see more countries getting added in the first quarter of next year but certainly next year we have seen as a year of good volume growth substantial high double digit and beyond kind of market growth and this year as a year of really getting in to these markets in a fashion which is in line with the way we do it in India which is bring to the customers what they need, build the infrastructure first in terms of flagship showrooms, workshops, distributive infrastructure supported with advertising, market research, customize products for these markets and then build the business, so this year is marked with those kind of ground work and ground level activities and next year you will see substantial volumes coming from all these markets.

**Moderator:** The next question is from the line of Rajat Chandak from ICICI Prudential, please go ahead.

**Rajat Chandak:** Good evening sir, thanks for the opportunity, sir my question pertains to your 300 basis points margin expansion. What is the risk that the management sees for that margin expansion, could it be higher competition, maybe higher share of exports which maybe lower margins in the initial period for us and second question would be over the next two to three years what would be the company's focus, would it market share production or profitability?

**Ravi Sud:** Okay, I will answer the first part; we have already answered your question. You have given two reasons; those are the risk factors which could rest with 300 basis points increase in EBIDTA margin.

**Anil Dua:** On market share versus profitability I will say for a good business to know that is not a trade off and the way we have always looked at it is if you go for your market share in a healthy way without ignoring fundamental business case behind your business model the bottomline definitely follows. The entire cost focus programs that Ravi has spoken about and the volume focus that I earlier spoke about these 11 models that we have launched and now the global plans that we have the innovation that we are trying to lead which hopefully brings the right kind of preference from the customers we believe that this is a business model which should result in both the market share gain as well as bottomline improvement.

**Moderator:** Yes the last question is from Govind Chellappa from Jeffries, please go ahead.

**Govind Chellappa:** Sir just wanted to clarify your comment on dividend payout. We were under the impression that your dividend payout like last year was recurring dividend payout of 60 to 65% when you have announced the dividend last year you had mentioned that would be the range of payment and I heard now that it will be 35 to 40%.





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*January 30, 2014*

**Ravi Sud:** Let me just clarify. We had a consistent dividend payment policy which varies between 35 to 45% and to take guidance I still maintain that people should work on a dividend payment policy of 35 to 45% leave aside the special dividend there have been years where the Board declared special dividend. The year 2013 was an exceptional year which the Board considered at that point of time. I will not give the guidance that the company dividend policy from 35 to 45% has gone to 60%.

**Moderator:** Thank you very much. I now hand the conference over to Mr. Chirag Jain for his closing comments.

**Chirag Jain:** Thank you all. I would like to thank the management for taking time out and doing this call. On behalf of Motilal Oswal Securities thanks for all the participants for joining in. Have a good day.

**Ravi Sud:** Thank you.

**Moderator:** Thank you very much. Ladies and gentlemen on behalf of Motilal Oswal Securities that concludes this conference. Thank you for joining us and you may now disconnect your lines.