



“Hero MotoCorp Limited Q2 FY 2015 Results
Conference Call”

October 17, 2014



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Moderator: Ladies and gentlemen, good day and welcome to the Hero MotoCorp Q2 FY15 earnings conference call hosted by Credit Suisse Securities Private Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing “*” then “0” on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Jatin Chawla from Credit Suisse. Thank you and over to you, Sir!

Jatin Chawla: Thanks a lot, Margaret. Good afternoon, everyone. On behalf of Credit Suisse Securities Private Limited, I welcome you all to the 2Q FY15 Results Conference Call of Hero MotoCorp Limited. I will also take this opportunity to welcome the management team from Hero MotoCorp. From the company side we have Mr. Ravi Sud, Senior Vice President & CFO, Mr. Surender Chhabra, Vice President-Finance and Mr. A. Srinivasu, All India Sales Head. Since the results came out yesterday I guess all of you had enough time to go through them. We can straight away start with the Q&A.

Moderator: Thank you very much. We will now begin the question and answer session. The first question is from the line of Hitesh Goel from Kotak Securities. Please go ahead.

Hitesh Goel: Sir, basically I wanted to understand what has been the cost savings in this current quarter because if I look on a QoQ basis your gross margins have expanded by 70 basis point and on a realization front or a mix front, we are not seeing much change. Can you tell us something about that?

Ravi Sud: I am happy this is the first question and a standard question. I have been saying for last five quarters that we have undertaken a major margin transformation project and I can share some figures with you that as far as H1 is concerned we have added about 95 Crores incremental to the EBITDA and in the quarter 2 it is about 65 Crores so in the first quarter it was 30 Crores and in the second quarter it is about 60 Crores. If I share the overall figures, we have implemented ideas worth about 703 Crores with annualized savings from inception.

Hitesh Goel: Okay. Sir, my second question would be can you just tell us about the scooter capacity, how is it ramping up and can you give us some color on how your capacity will pan out in FY16 I mean almost good?

Ravi Sud: In the last conference call therefore in July we had said we have a capacity of about 75000 and we will take this capacity of 100000 by January. As of now we have been producing about 80000 and even in the month October we are producing 80000 and this capacity will go to 100000 in the beginning of January 2015.



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- Hitesh Goel:** Thank you very much.
- Moderator:** Thank you. The next question is from the line of Kapil Singh from Nomura Financial. Please go ahead.
- Kapil Singh:** Good morning. My first question is related to the festive sales, if you can give us some color as to how it has been progressing, any YoY comparisons compared to last year?
- A. Srinivasu:** Good morning, I am Srinivas here. I head the National Sales function. The festival season was very good and brisk in the first ten days during the Navratra. We clocked a double digit growth during the first ten days. There was some moderation post the Navratra and this is a typical trend that we have seen over the years that normally there is a little bit a lull between the Navratra and Diwali startup and it normally catches up from Poosam Nakshatras, which started yesterday technically and yesterday again we have got back into a double digit growth so we look to closing the festive season with a double digit growth which is good, which we consider reasonably good and the industry also is at around double digit around 10%, 11% growth.
- Kapil Singh:** Sir, on the new launches side, any color you can share?
- A. Srinivasu:** See we have launched two new variants in our Maestro, which is double colored. One body colored, which is red and white and we also launched a mat grey color and both of them have got good response from the market. It is just that we need to scale up on numbers from the supply side and which we would be doing from November onwards.
- Kapil Singh:** Sir what about the upcoming new launches, any color there what should we expect in the next one year?
- Ravi Sud:** As Srini was saying that the scooter market is growing faster than the overall industry, we have two new brand new products which will come in the next one year.
- Kapil Singh:** Thanks.
- Moderator:** Thank you. The next question is from the line of Chirag Shah from Edelweiss. Please go ahead.
- Chirag Shah:** Thanks for the opportunity. Sir, first question on exports, in second quarter we have seen some strong traction on exports, roughly 60,000 units we have done in second quarter. Can you share some light how to look at it going ahead in terms of ramp up and over there so how the trajectory looks? Is the 60,000 kind of quarterly trajectory we should look at or which are the geographies where you have entered, etc?



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Ravi Sud: Let me answer this. As we have said in the last quarter that our target for the current year is about 250000 and as you rightly said this quarter we have done more than 60000 and as far as we are concerned we are on track to achieve our target of 250000. You may see higher numbers in quarter three and quarter four and as far as number of countries are concerned in the last conference call I shared that we were in 19 countries, we are already now in 22 countries. Three new countries have been added. They are Columbia because after July 2013 we had stopped dispatches to Columbia because that was in Hero Honda brand and there was sufficient inventory and we have started shipping our products with Hero brand in the month of August 2014. So that is one country. Then the second country is Iran where the dispatches have also started. So we are now in 22 countries and we are on track to achieve our target.

Chirag Shah: Any more geographies or any more countries to be added in next six months tentatively?

Ravi Sud: We aim to go to 50 countries by 2018 and at this point of time I would not be able to share with you the name of the country which we would enter now.

Chirag Shah: Fair point. Second question was again on scooters. Is there some underutilization of capacity in scooter because demand at the ground level seems to be strong, but your last few months' volumes are not really to that scale because you have highlighted 75,000 units of capacity, but actual numbers seems to be on the lower side?

Ravi Sud: You see the part of scooter capacity is utilized for export. We have got a large orders of about 45000 units. So about 9000 to 10000 units are being dispatched for export out of the total capacity of 75000, but that the orders will be completed by beginning of November, but as far as the capacity is concerned, there is no underutilization and the capacity is being fully utilized.

Chirag Shah: Any thought process of ramping up the capacity beyond 100,000 units because some of your peers are talking of very big numbers on scooters?

Ravi Sud: I shared with you that in the current fiscal our capacity will be 100000 and our plan to increase our capacity to 125000 and 150000 are under consideration and we will do it immediately once we reach 100000.

Chirag Shah: It would happen in the same locations? The new plant...

Ravi Sud: Yes.

Chirag Shah: It would happen in the same locations then one last clarification on the results side. Other expenses have really gone up significantly and so are your staff costs. So while staff costs are understandable, but other expenses really going up significantly for us? So how should one look at that particular number?



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Surender Chhabra: Morning Chirag. I am Chhabra here. In regard to other expenditure I think let me clarify here if we are comparing with the corresponding quarter, you see that the diesel price hike which is coming up on the month-to-month basis and from October onwards we started getting corrected the prices of product marginal increase were taken. This year quarter-to-quarter basis if I said there is no major increase but as per the corresponding quarter is concerned yes you will see major increase because of the diesel affect. That one major head which is there, which has increased my expenditure as compared to the corresponding quarter otherwise there is no major cost increase on Q1 to Q2 basis.

Chirag Shah: The recent price hike announce would actually would be adding to profitability or they would just cover any incremental conversion costs or some cost pressure that we are witnessing?

Surender Chhabra: It is going to only add on marginally to the bottom line and get compensated for the diesel cost in conversion cost.

Chirag Shah: Thank you very much.

Moderator: Thank you. The next question is from the line of Mukesh Saraf from Spark Capital. Please go ahead.

Mukesh Saraf: Sir, first thing is on this margins itself if I look at last couple of quarters, there are two, three items that have affected your margins. One is the vendor hike that you had given the Haridwar plant impact, the diesel impact, and the increase in royalty for those three products that you pay royalty on. So I am just looking at going forward, you have taken a price hike now; we do not expect any further diesel price hike, in fact diesel prices can go down and overall we are expecting commodity costs to more or less stay flat or probably go down slightly. So, is it fair to assume that you will see margin improvement going forward and obviously you have your Leap program where the run rate of benefit is only increasing? So, is it fair to assume that you can see a steep improvement in margins going forward?

Ravi Sud: Yes, you are right. As far as inputs are concerned more or less they are flat or some of them have come down. Leap program is doing very well that was the first question which I answered, whatever we had implemented till September 31, 2014, now we will continue implementing new ideas. However, even if we do not implement anything more in the current year, where we have added 95 Crores till September, the addition will be 225 Crores for FY15. But we will implement additional ideas worth about 300 Crores. My assessment is that we will add about 300 to 325 Crores to the bottomline. In the next two quarters the accruals from leap are going to be much higher than what we have seen in the first two quarters.



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Mukesh Saraf: Especially the net accruals should be higher because we are not going to see any more vendor hikes probably we are not going to see any more of those because of your diesel prices not going up from here on?

Ravi Sud: Hopefully yes.

Mukesh Saraf: Sir, my second question is on the premium side of your vehicles. You had obviously alluded last time that the Xtreme is expected to do quite well and that the premium side itself is expected to do quite well. But are you a bit disappointed with the way your premium segment has done within the motorcycles?

A. Srinivasu: I am Srinivas here. Yes it is a little below expectation because of some delay in launches on the premium side, but nevertheless the new models that we have launched in terms of Xtreme that we have launched and the Karizma, the new Karizma that we have launched that is seeing some good response from the market and going forward we look forward to improving our market share in the segment, but overall if you look at the premium segment the entire segment has not grown excepting for Enfield. So Enfield is actually drawn the segment up otherwise if you see manufacturers most of them has registered a decline in H1, but in H2 I see a revival in the segment and we are also would be launching a new model in the next two months in the premium segment, a different variant of Xtreme so we expect a little better response and higher market share in H2 in premium segment.

Mukesh Saraf: Just one final question, it is actually a continuation from the previous one. In the scooter segment we have seen that domestic scooters obviously for us this quarter has dropped because we have probably allocated the capacity for this order that we have got in the exports. But seeing the domestic scooter market which is obviously growing extremely significant growth we are seeing there, until your new capacity comes up, would you continue to allocate capacity towards exports vis-a-vis domestic because then our market share in the domestic could be under risk?

Ravi Sud: As I said earlier I think we have got a massive one-time order which we are in the process of fulfilling and we are allocating about anything between 9000 and 10000 units for exports and as I said in the beginning of November that order will be fully completed and all the capacity will come back to the domestic.

Mukesh Saraf: So, it is just a one-time order?

Ravi Sud: Yes.

Mukesh Saraf: Great, Sir. Thanks a lot for answering these questions.



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Moderator: Thank you. The next question is from the line of Jamshed Dadabhoy from Citigroup. Please go ahead.

Jamshed Dadabhoy: Two questions, one is could you give us some color in terms of the benefits per bike that you will be getting from the Neemrana plant in terms of the sales tax exemption? And second question relates to what Mr. Srinivasan mentioned in the last quarter in terms of shrinking product cycles leading to higher industry growth. Could you give us some sense in terms of what percent of the Splendor and Passion sales today are replacement versus first time buyers?

Surender Chhabra: Jamshed good morning Chhabra here. Regard to your first question for Rajasthan, let me tell you that Rajasthan production we had started from June onwards and we have ramped up that production from October. The major benefit and the number growth will start coming from this quarter for Rajasthan. As far as the benefit is concerned there is a local benefit on whatever we are going to sell in the state we will have VAT benefit of the state only.

Jamshed Dadabhoy: Do you get an interstate CST benefit also of that 3%, 4%?

Surender Chhabra: Not at all it is only for the local state government benefit which is extended to the company.

Ravi Sud: In a nutshell, Jamshed, it is like that whatever we produce and sell within the state of Rajasthan you get VAT benefit, which is 12.5% to 13.5% and this not an exemption. This is a refund. So which means you charge it, deposit and then get the refund.

Jamshed Dadabhoy Fair enough. Question to ask, Sir, is that is this amount that you will get, is it time bound i.e., for that seven-year period or nine-year period or is it capped at the amount of capex you will all incur?

Surrender Chhabra: It is a time bound not capped.

Jamshed Dadabhoy Okay. It is just for that seven-year period, right?

Ravi Sud: Yes.

Jamshed Dadabhoy Sir, second question on the Splendor Passion replacement versus new sales?

A.Srinivasu: Normally Splendor has a range of products if you look at is and so has Passion, we have a Passion Pro and then we have a Passion Xpro. So if you look at the lower variants of Splendor you will have almost about 70% of the sales coming in from first time buyers and fortunately you have the penetration levels being low across many states in the country. We do see a good response in the first level. But if you look at the higher variants of Splendor like the Super Splendor, the Splendor iSmart, and even the high-end Splendor PRO variant. You find almost



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about 50% of that sales coming in from replacement buyers. We have a good mix of both across the range of splendor and in fact as a brand splendor is growing at about 22% in H1.

Jamshed Dadabhoy Mr. Srinivas, just continuing on this question, you had mentioned last quarter that replacement cycles are shrinking and leading to stronger growth?

A. Srinivasu: One of the reasons yes.

Jamshed Dadabhoy So what is your sense in terms of how much is the replacement cycle coming down from to?

A. Srinivasu: See earlier replacement cycles were typically when I mean replacement cycle I was referring to the ownership cycle the first ownership cycle because normally the life cycle of the motorcycle is still at about 8 to 10 years but the first ownership that is the time and people own it and then replace their product is normally we are in the process of undertaking a big study on that but my guess is it is come down from about five years to about 3.5 – 4 years.

Jamshed Dadabhoy Thank you very much, Sir.

Moderator: Thank you. The next question is from the line of Aryn Pirani from Deutsche Bank. Please go ahead.

Aryn Pirani: Sir, just on your Leap program and you mentioned that you saved something like Rs.95 Crores in the first half, but can you also mention what was the net retention after adjusting for the vendor hikes and the forex?

Ravi Sud: I have been saying that this program will do on standalone basis and this is my standard answer. There could be many factors which will impact the overall margins. These are vendor hikes, transportation hikes, diesel hikes, your inability to pass on the increases to the customer or you may decide to launch a variant or a new product at a lower EBITDA or conversion cost increases, etc., etc. Last year the accrual was 169 Crores this year we are expecting a fresh accruals of about 300 to 325 Crores.

Aryn Pirani: The 100 basis points to 120 basis points you are mentioning on a gross basis, right, assuming anything else is same?

Ravi Sud: Standalone basis. Yes.

Aryn Pirani: So Sir, can you give any guidance say one year down the line or two years down the line where your EBITDA could settle at? Should we assume it should move from 14% to 15% or maybe higher?



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Ravi Sud: If you look at my EBITDA for the quarter it is about 13.5%, there is an anomaly of 1.3% point which I had stated even in the last quarter, that is the anomaly between input and output excise duty. That is something which I cannot control and hopefully Government should correct that anomaly. In other words, we are already close to 15%. So our target is that we should take this EBITDA to about 17% in next three years that was our planning.

Amyr Pirani: Sir, just coming back to demand, obviously you mentioned that festival demand has been in double-digits. But how is your outlook for the remaining of the year? Do you feel demand growth could moderate or you expect that this growth that we have seen in the first half and the festival season could sustain for the next few months also?

A. Srinivasu: The industry grew by at about 16.8% domestic and including global business of all manufacturers it grew through at about 18.5% it will moderate in my view basically because there has been a shift of the festival season when you compare it with last year into H1 and one month shift is there because normally all manufacturers build stock in the month of September for the festival that happens. Otherwise normally we building the stock happen towards the end of September and October if the festival season comes in, in October, November to that extent I expect the moderation but I do expect the industry to continue to grow a double digit even in H2.

Amin Pirani: Thanks, Sir. Thanks for taking my questions.

Moderator: Thank you. The next question is from the line of Pramod Amte from CIMB. Please go ahead.

Pramod Amte: This is with regard to your transport pricing policy. Can you elaborate in the sense how does these pricing to the fleet operators operate when the diesel price goes up and down, when does these trigger?

Surender Chhabra: Pramod as far as the agreement is concerned with the transporters we have long-term agreement on which they have to work with us and there are certain variables which are to be corrected from time to time depending on the market condition, like it gives some diesel hike, this is to be given on every increase we have to pass on to them instead of monthly basis we have added with them with the corrected quarterly basis. On the other hand if the lubricants et cetera get increased these are considered on the six monthly basis otherwise it is in per kilometer rate which is fixed with the transporters to cover-up all over India dispatches.

Pramod Amte: But purely on a diesel, it is a more you are saying monthly basis?

Surender Chhabra: Yes it is only because of diesel hike we have see the pressure come to revise the prices on quarterly basis for the transporters.



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Surender Chhabra: Because you just see diesel prices go up by 0.50 paisa per month I mean in a quarter you can say it is to be Rs.1.50 per liter and hence was so in that I think that as far as diesel is concerned the revision is done every quarter for other parts for lubricants and oil it is done every six months. Otherwise we have very, very long-term contracts.

Pramod Amte: Second is with regard to the competitive scenario. If you look at Honda is now talking about dedicated capacity for scooters. So on a medium-term basis, how do you look at this development? Is it more of easing of competition in the motorcycles or is it the shift towards scooters will happen much aggressively and hence you also have to accordingly plan your capacity in your new plant?

A.Srinivasu: See the structural shift to scooters is about 2% to 3% is what I expect going forward to because the sales being lower we are seeing a high rate of growth in the scooter base. Now that the base effect would catch up from this year onwards and structurally yes there would be a shift but new innovative products can haul that shift even from the motorcycle segment. So in my view the shift would not exceed 2% to 3% every year at best and there can be a reversal depending on the innovative products that come in for example if you have a extremely high fuel efficient bike it could again tilt the shift towards motorcycle. So it is not to be taken for granted that the shift will continue only towards scooters, yes in the immediate mid-term yes there will be a shift but things can change depending on technological innovations too. That is one point and second in terms of capacity see if you look at the capacity of Honda coming up with the new exclusive scooter plant yes probably their expectation is that the scooter demand would be higher but then even after the Bangalore plant is come up not every month that they use the entire capacity it has been sub 4 lakh many months were the capacity is 4.2 a month, it is just that one month they have done 4.2 and even in this month they expect the volumes to be lower than 4. So in my view the shift is 2% then I think we are on track to building capacity to take care of that shift.

Pramod Amte: Sir, where do you expect that to settle in the sense might be two, three years down the line, will it peak out or...

Ravi Sud: It think so, that is why I am saying that there would be product innovations in the motorcycles also and you will find that product innovations and base effect would catch up. It is a 27% this year in my view it should move to 32% - 33% gradually.

Pramod Amte: Just seems like you touched upon the product innovations, you have done so many JVs even with many entities of which one of them seems to be with Magneti Marelli. Can you develop on how this entity will help you? What type of plans you have there going on in terms of meeting the fuel efficiency or also on the emission side?

Ravi Sud: You are talking of Magneti Marelli JV.



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- Pramod Amte:** Yes.
- Ravi Sud:** Magneti Marelli JV is specifically for FI pump. Presently most of our vehicles in India running on carburetor and as we have said maybe in the three to four years, it will become mandatory to use these FI pumps. So, that JV is specifically meant for that. Some of our products even today have been using FI Pumps.
- A. Srinivasu:** We do have FI in for example our Glamour itself which is a 125cc bike and we have it in Karizma variants of Karizma, but having said that also to answer your question for example recently you must be aware that we have enhance the mileage of all our 100cc motorcycle excepting Splendor+ which we are working on and today we have at the top end with this splendor I-smart in terms of mileage hitting 97.2 as per ARA norm so we just 2.8 kilometers away from 100 kilometers to a liter.
- Pramod Amte:** Thanks and all the best.
- Moderator:** Thank you. The next question is from the line of Vinay Singh from Morgan Stanley. Please go ahead.
- Vinay Singh:** My question was could you comment a little bit about the trends that you are seeing in rural versus urban? And secondly also, a little bit about scooter penetration like we know the overall scooter penetration, but what will be the scooter penetration in urban India?
- A. Srinivasu:** I will take the second question first. The scooter penetration in urban India is the penetration is really higher compared to the rural India but if you look at the structure nationally scooter structure at about 27% and urban India it is closer to 40%, basically because of the convenience in the format of usage and speed demographics and things like that. In rural India it is still very low the structure is only at about 12% to 13% and the shift in structure is also very, very minimal there are states virtually where there is no shift at all in the rural market so that is the scooter penetration and structure.
- Vinay Singh:** On that point so in rural India, you mean to say that you are even. Do you expect rural scooter penetration to go up?
- A. Srinivasu:** Marginally because what we are seeing as far I said the shift in rural India towards scooter is very, very low see unless it is a radically different demographic situation which comes in then there could be a little bit of a shift towards scooters but having said that again it depends on product innovation we were a scooter country sometime back its move to motor cycles and there has been a little bit of shift towards scooters but then you would find that there are lot of innovations in the motor cycle segment it could shift back or it could stagnate anything can happen.



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Vinay Singh: So essentially when we say that the scooter penetration can go up from 27% to 32%, 33%; in your view the urban from 40% will go to 50% or so?

A. Srinivasu: Yes 40% to 45% would be my take and vary from market-to-market you might have some urban markets with a high capacity and you might have some urban markets with a little lower than even 40 even and I am saying 40 there are markets which are at 45 and there are markets which are at 25, so it is so radical given the nature of our country, yes in it my view can go up to may be about 45 the shift to be more on the urban than in the rural in my view.

Vinay Singh: The second question on that trends like are you seeing any slowdown in sales in rural?

A. Srinivasu: No in fact see the rains were a little delayed so what we saw was that we in fact saw little bit of a shift on sales in September. The sales were little sluggish in the industry and that is largely on account of late sowing so there are farmers were occupied preoccupied with the sowing activity but then we saw a good revival in the festive season with a double digit growth coming back into the industry so that is the change in pattern in growth. But otherwise there is no slowdown as such in fact if you look at it the industry here is growing at a good 16.8% in H1 it may be partly because a shift in festive season but never say the good growth.

Vinay Singh: Then just lastly like typically we see that whenever the urban economy recovers, the premium bike segment does well. It is also something that you have stated. But with our scooter penetration rate rising in urban and in fact our expectation that it will go up further, do you think this is a different set of consumers that are going to premium bikes and different set is going to scooters so it would not get impacted or is there a risk that in this urban recovery, premium actually does not grow as much? You have niche categories like Eicher growing, but overall premium does not grow because the market migrates to scooters. Any views on that?

A. Srinivasu: There is a little bit of an overlap but by and large the segment is different as scooter side a customer is a little difference from urban customer but then see the customer in the earlier part of his range maybe you would like a premium bike and then when you settles down at 30, 35 years would probably look at a scooter for more of family usage. So it is very difficult to put a point and say that the customers are very distinctly different but having said that there is a little bit of an overlap between these two segments so there could be a little bit of an impact but not much in view. As far as the industry is expanding you may not has much of a problem.

Vinay Singh: Thanks a lot, Sir. Thank you for your inputs.

Moderator: Thank you. The next question is from the line of Jinesh Gandhi from Motilal Oswal Securities Limited. Please go ahead.



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- Jinesh Gandhi:** My question pertains to the price increase, which we have taken. Can you quantify exactly what kind of price increase we have taken?
- Surender Chhabra:** Morning Jinesh, Chhabra here. As far as the price increase is concerned, we had discussed on various straight forms. We had taken in the last week of September once because of the diesel pressure because the first correction we have taken in October 2013 and second now in October 2014. Apart from that we have gone and given some benefit to the metro dealers as the dealer margins so marginally that increase was considered and then some conversion cost because of the diesel hike, as well as the labor cost increase. On an average I can say there is a net at Rs.200 of increase in the effective price and therefore which has come to the company on these account.
- Jinesh Gandhi:** Second question pertains to the scooter capacity you mentioned 100,000 by Jan 2015. So this is excluding addition from Gujarat plant, right?
- Ravi Sud:** Yes of course Gujarat will take another one year to commission.
- Jinesh Gandhi:** When you indicated that you might consider taking capacity to 150,000, this is again excluding Gujarat and AP plant?
- Ravi Sud:** That may include Gujarat that point of time.
- Jinesh Gandhi:** But would not include AP in this at 150,000?
- Ravi Sud:** No AP will be sometime in 201. Gujarat plant will have an ultimate capacity of 1.8 million. In the first phase it would be 1.2 million and then going up to 1.8. So once we reach say over 1.2 million then we will start work on AP plant.
- Jinesh Gandhi:** Of 1.2 million Gujarat, how much would be scooters?
- Ravi Sud:** At this point of time it is very difficult to say but we will increase capacity according to the market need. I am telling the overall capacity of the plant would be 1.8 million.
- Jinesh Gandhi:** Sir, last question pertains to other income during the quarter. We had seen other income of about Rs.194 Crores so this is entirely pertaining to treasury income and is it a sustainable run rate or there were some other?
- Ravi Sud:** Yes, it pertains to the treasury income but it is not sustainable. This is one time booking which we did to pay the interim dividend in August 2014. And there was an extra income of 68 Crore in the quarter.
- Jinesh Gandhi:** Thanks and all the best.



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- Moderator:** Thank you. The next question is from the line of Apurva Kumar from Jefferies. Please go ahead.
- Apurva Kumar:** My questions have been answered. Thank you.
- Moderator:** Thank you. The next question is from the line of Abhishek Gaoshinde from Sunidhi Securities. Please go ahead.
- Abhishek Gaoshinde:** Just one thing that during the quarter, have we paid any royalty to Honda?
- Ravi Sud:** Yes, there was a royalty that is on three products which we still continue to manufacture and sell. These are Passion XPro, Maestro and Ignitor .
- Abhishek Gaoshinde:** How long it will continue, Sir?
- Ravi Sud:** Our agreement with Honda is till June 2017. So long we continue to manufacture these products or June 30, 2017, whichever is earlier.
- Abhishek Gaoshinde:** One more thing that if you can throw some light on the export markets in which you have entered that how that market has been performing and how do you see that that would perform in next 6 to 12 months?
- Ravi Sud:** As I said we are already in 22 countries and in the Q2 our numbers have been much better than what they were in quarter one and for the full year we have a target of over 250000 units and we are well on track as of now.
- Abhishek Gaoshinde:** You are also saying that markets are also doing well. There is no major pressure on that markets in which you have entered that you have mentioned 22 countries?
- Ravi Sud:** No.
- Abhishek Gaoshinde:** Thank you.
- Moderator:** Thank you. The next question is from the line of Nikhil Deshpande from Sharekhan. Please go ahead.
- Nikhil Deshpande:** Good morning Sir. A couple of questions. The depreciation of 75 Crores for the quarter, it includes Neemrana or is the depreciation rate expected to increase in the coming quarters?
- Surender Chhabra:** As far as Neemrana plant is concerned the manufacturing plant has been capitalized in the second half of this Q2 itself. As far as GPC is concerned, the major capitalization will be in the third quarter.



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Nikhil Deshpande: Sir, another question was as we are seeing that for motorcycles, if there is any disruptive technology, it could bring back the share towards motorcycles. For scooters, do you see any new technology coming in which could accelerate the shift towards the scooters?

A.Srinivasu : See I think inherently there are certain disadvantages likely automatic gear versus the manual gear. So scooters will always lag in terms of mileage which is the top most parameter considered for purchase of a two wheeler that is a lag that will always be there towards motorcycle. Yes there can be disruptive technology in terms of features maybe but per se Indian technology I think we have the best technology in the globe the only thing you can have is maybe high-end scooters coming in but that will always be a small volume gain when you come up with high priced high-end technology you will have a range but then the volumes will still come from the base products. Yes there is a possibility that the shift could accelerate a little bit with a lot of high-end scooters coming into the market but I think the opportunities higher on this side where let us say tomorrow one start putting a consistent 100 kilometers plus to a liter you might have customer shifting back because it might make a lot of sense buying a motorcycle in terms of ownership cost.

Nikhil Deshpande: Sir, but is there a space for a geared scooter in the market?

A.Srinivasu: There is a space for geared scooter but it is a very, very small space.

Nikhil Deshpande: That is all from my side. Thank you, Sir.

Moderator: Thank you. The next question is from the line of Yogesh Aggarwal from HSBC Securities. Please go ahead.

Yogesh Aggarwal: I wanted to get your views on the cyclicalities of the industry as such because we have seen in the past during upcycles the industry can even grow 20%, 25%. Now considering the base effect and the industry growth in spite of a weak macro, you think if macro remains good over the next two or three years that kind of cyclicalities is still possible?

Ravi Sud: Very much possible. See we have been varying under high interest rate for quite some time so I think if you look at the finance penetration it has been stagnant for quite some time across the industry if the interest rate really come down it can give us at good growth that we are looking forward to. Answering your question specifically it is very much possible.

Yogesh Aggarwal: You still think that interest rates do matter for two-wheeler buyers that much that it can impact the cyclicalities?

Ravi Sud: To some extent.



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- Yogesh Aggarwal:** Thank you, Sir.
- Moderator:** Thank you. The next question is from the line of Harsh Mehta from Shah Investors. Please go ahead.
- Harsh Mehta:** Sir, are there any specifically new products for the export market you are targeting?
- Ravi Sud :** Each market is different and you have to make your product or modify your existing product to meet the export market. In Africa, two wheelers are used on a Taxi, so you have to modify the seats and similarly for head lights each country has its own norm, so you have to modify the products to meet local regulatory requirements.
- Harsh Mehta:** Sir, I just wanted to get any comments for the export realization. Sir is it higher than the domestic market or is it in the line with the domestic market?
- Surender Chhabra:** As far as margins on that export is concerned, when rupee in the range of 60 to 62, the margins are in line with domestic realizations.
- Harsh Mehta:** Sir, the last question. I had read somewhere that Bharat stage IV norms will be proposing April 1, 2015. So I just wanted to get a sense that with so many JVs around the world, would that JVs help you for a smoother transition from Bharat stage III to Bharat stage IV norms?
- Ravi Sud:** Well, the new norms have been postponed. These new norms were to be effective April 2015.
- Harsh Mehta:** Yes Sir, it is just a proposed thing?
- Ravi Sud :** No, these norms were earlier applicable from April 1, 2015. They have been postponed to April 2016/2017.
- Harsh Mehta:** Thank you very much.
- Moderator:** Thank you. The next question is from the line of Kapil Singh from Nomura. Please go ahead.
- Kapil Singh:** Just a follow-up on this BS IV thing, last time I remember there were some costs involved which impacted all the companies. So is there a similar kind of thing? I mean how much cost increase would take place whenever the emission norms change?
- Surender Chhabra:** I think this last time it was in 2010 when that major change came and we had incurred a cost of Rs.900 at that point of time which we did not pass on to the customers, but this time it is a nominal cost.



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Kapil Singh: Secondly, I wanted to check in terms of segmental growth what is our outlook. If you look at economy, executive, and premium segments; the mix has remained fairly stable in last few years. So, do we expect a change in the next four or five years? How are we planning for that?

A.Srinivasu: See the growth rate might vary but then I do not see a huge shift in the segments. In my view deluxe segment, which is the mid-segment, will continue to be the largest segment. Premium might have a better growth rate. Currently it is Enfield which is actually putting the growth up but I do expect going forward the premium segment will grow at a good pace. Basically because the base is low and then you will find a few of launches going forward in the next two three years in the premium space, but the larger segment dominant segment will continue to be the dealers segment where you will find both the 100cc and 125cc doing well.

Kapil Singh: Sir, finally any more longer term outlook on export side? What are you guys targeting now that we have entered 22 countries? In terms of numbers, where do we see ourselves in next three, four years?

Ravi Sud: We have a plan to ramp up its growth upto 1.2 million by 2020. As I said current year target is 250000. We will keep on increasing progressively as we gain experience in the markets which we are entering and also enter the new markets.

Kapil Singh: Sir, how is our pricing in comparison to other Indian companies like Bajaj Auto, etc?

Surender Chhabra: I may not have the exact information but price is all competitive like in domestic markets.

Kapil Singh: That is helpful. Thank you.

Moderator: Thank you. The next question is from the line of Amrish Mishra from JM Financial. Please go ahead.

Amrish Mishra: Sir just wanted to get a sense on the margin between scooters and motorcycles have you seen is it true that the margins on the scooters are relatively better than what we or the industry enjoys their motorcycles one and second have you seen the gap really narrowing over last may be a year or so when the competition have been more aggressive?

Surender Chhabra: Amrish, as far as the margin of the scooters are concerned, first thing scooters are contributing only 11% to 12% of our total dispatches and in motorcycles where there is a multiple variant wherever scooters we have only one variant or maximum to two variant in Pleasure. Maestro is carrying a 5% royalty to Honda as we know that. On the other hand there is only one model with two variant Pleasure which is there. Margins are I can say if we compare with any particular model in motorcycles like I can say Splendor in the range of based on premium segment are in line with that.



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- Ambrish Mishra:** That is because we pay royalty on the scooters and that is why the margins are take a hit there?
- Surender Chhabra:** It is on the Maestro only, for which we are paying royalty to Honda otherwise Pleasure there is no royalty burden it was only that amortization cost burden which was there till June 30th which is now over so margins had get improved on the Pleasure.
- Ambrish Mishra:** So now the margins on Pleasure would be similar to what we must be enjoying on something like a Splendor or so?
- Surender Chhabra:** Yes.
- Ambrish Mishra:** Thank you Sir and all the best.
- Moderator:** Thank you. The next question is from the line of Sonal Gupta from UBS Securities. Please go ahead.
- Sonal Gupta:** A couple of clarifications. One is on the export side, I mean you said that you got this order and that is reflected in your export number, growth is really coming from the scooter side. We have not really seen much growth on the motorcycle side and you think the order finishes in November. So beyond that, do you have some other orders which will kick in or how does that work?
- Ravi Sud:** Sonal Ravi here. This was a one-time order which came from Sri Lanka and the quantity is about 45000. But in the meantime, as I stated earlier, we have started our shipment in Columbia in the month of August so that is in the range of around 3000 to start with per month and we are going to launch with Hero brand sometime end of November. Similarly Bangladesh where we have entered in end of April, volumes are now close to 4000 a month. These two markets are for the time being. And Angola region is also doing very well where we did about close to 2500 per month and the numbers are good. Sri Lanka is onetime order.
- Sonal Gupta:** Sir, just another thing was on if the diesel price gets cut by Rs.3 to Rs.4 or whatever, you get to retain the benefits or will you get the benefit from the freight side?
- Surender Chhabra:** Sonal, as I told that diesel price there are variable elements which are there to be corrected on quarter-to-quarter basis especially I can say diesel if the diesel price has to go down we have to reduce the prices and that benefit has to come to us.
- Sonal Gupta:** That is good. Sir, just lastly on corporate social responsibility, I mean do you need to provision anything? Are you doing something already or how does that work?



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Ravi Sud: On corporate social responsibility, yes part of the expenditures we are incurring is coming on quarter-to-quarter basis like in case of Prime Minister Relief Fund we had given and that part of corporate social responsibility and a major portion of that will be covered in second half.

Sonal Gupta: Just last question really Sir, just for Mr. Srinivasan. I mean like you are saying the buying cycle is shortening versus ownership cycle is shortening. So I mean how do you see that? So do the customers I mean I guess in the 100cc if you could give the number for your whole 100cc range what is the proportion of first-time buyers. And then I mean do you see them coming back and buying again a 100cc bike after four years or do you think then they become more likely to upgrade to a 125cc or a scooter? How do you see this upgradation really happening or do you think that they will still continue to buy a 100cc?

A. Srinivasu: See the 100cc range across the industry for us it is about 60% first-time buyers and about 40% repeat buyers a year. To that extent 40% of them are actually using our product coming back and buying another 100cc, you might find someone upgrading from HF Deluxe into a Splendor+, or from Splendor+ to a Splendor Pro, or to a Passion Pro that extent we have a range of 100cc across different price point you have iSmart at the top-end of the 100cc. So you will have people to buying 100cc because if for someone, if the cost of ownership has to be low then 100cc is the best solution such a person, where your cost of ownership is really low because it offers great mileage so to that extent I would find that this 3.5 – 4 years would further comedown to 2.5, 3 years going forward in the next two to three years time but the portion of first-time buyers to repeat buyers in 100cc may not change radically you might still have 60% because of low penetration levels across many states in the country, you will have a huge chunk of first-time buyers coming in and that is why the growth will be there and that is the same phenomena for the scooters to even in scooters we have a lot of first-time buyers coming in and buying scooters, especially the base ones when high-end cc scooters come in then maybe you will have upgrades going in there, but yes we are seeing some amount of movement in the 125cc also where you have repeat buyers going in, into 125cc that is another possibility that can happen that from 100cc people who probably economically become a little well off might trade off a little more power towards mileage and might move towards 125cc but then the huge chunk will still remain with the 100cc, 110cc.

Sonal Gupta: Because Sir, we have seen a huge shift I mean not a huge shift, but we have still seen a shift more towards 125cc over the last few years and my thinking would be that especially in urban areas where penetration levels are much higher and income levels are also higher. Would you be seeing more of a shift away from 100cc or are you still seeing 100cc holding up pretty well?

A. Srinivasu: See I still feel 100cc holding up because what is happening is see the shift towards 125cc when I am saying shift the growth of 125cc segment is good and that growth is because of low base effect, both are 125cc products are also doing well and we also have some competition but it is doing well in this segment. But I think even in 100cc now you find a lot of products see the only



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advantage of 125cc is power, better power and acceleration but with technological improvements possible in 100cc, 110cc you might find the 100cc bike power coming very close to that of a 125cc and also delivering great mileage if that happens then you would find the shift a little lower but having said that if you look at purely the growth then yes 125cc will continue to grow very well.

- Sonal Gupta:** No, Sir. What I was saying was that in urban areas, are you seeing a shift away from 100cc or...
- A. Srinivasu:** No it is definitely not urban or rural our 125cc is doing well across markets both in urban and in rural the growth is coming in from both the areas equally. 125cc is not an urban phenomenon as such.
- Sonal Gupta:** Thanks for answering the question.
- Moderator:** Thank you. The next question is from the line of Raghu Nandan from Quant Capital. Please go ahead.
- Raghu Nandan:** Just wanted to understand how is the current direct and indirect Yen exposure as a percentage of revenues? And the recent benign trend in the currency there would you think would help the margins?
- Ravi Sud:** Till June 2014 we had exposure, we had a huge exposure to Yen that is because of the Honda amortization payment of Jap.Yen 45 billion. But it is behind us. However direct imports are only 5% to 5.5% and 90% to 95% of it is in US dollars. Only a few components like EFI Kits come from Japan. That is as far as the direct import is concerned. Indirect export is about 9% about also with 50% in Yen. Indirect means the component which our vendors import and they assemble and give it to us so the 50% of that is in the Yen.
- Raghu Nandan:** Just one clarification, you had mentioned that two new launches over next one year. Just wanted to understand would that include scooter as well?
- Ravi Sud:** No my answer was specifically relating to scooter so I am saying there will be two new scooter launch in next twelve months.
- Raghu Nandan:** Lastly if I can squeeze one more. The 68 Crores of extra income in other income, can you just clarify, Sir? I just missed that.
- Ravi Sud:** We have divested about 700 Crores out of our investments in the month of August to pay the interim dividend and hence we booked the income, so this is that extra income because of the specific divestment done in August.



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Raghu Nandan: Thank you very much, Sir. That is all from my side.

Moderator: Thank you. Ladies and gentlemen due to time constraints that was the last question I would now like to hand the floor over to Mr. Jatin Chawla for closing comments.

Jatin Chawla: Thank you, Margreth. On behalf of Credit Suisse Securities, I would like to thank the senior management team of Hero MotoCorp for taking their time out for this call. I would also like to thank all the participants. Thank you everybody and have a nice day.

Moderator: Thank you. On behalf of Credit Suisse Securities Private Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.