

October 01, 2021

Hero MotoCorp Limited: Rating Reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Issuer Rating	-	-	[ICRA]AAA(Stable); Reaffirmed
Non-convertible Debenture Programme	15.00	15.00	[ICRA]AAA(Stable); Reaffirmed
Fund-based and Non-fund Based Limits	990.0	840.0	[ICRA]AAA(Stable)/[ICRA]A1+; Reaffirmed
Unallocated	110.0	260.0	[ICRA]AAA(Stable); Reaffirmed
Total	1,115.00	1,115.00	

*Instrument details are provided in Annexure-1

Rationale

The reaffirmation of ratings of Hero MotoCorp Limited (HMCL) factors in its strong business profile, as evidenced by its market leadership in the domestic two-wheeler (2W) industry (market share of 37%¹ and 52% in the overall 2W and motorcycle segments, respectively), its robust product portfolio, established brands and well entrenched dealership network. The rating also continues to favourably factor in its strong financial profile, demonstrated by robust return and credit metrics and superior liquidity position.

The benefits of HMCL's strong business profile played out to an extent during the pandemic struck FY2021. While Q1 FY2021 had been significantly impacted by the widespread impact of the pandemic across the country, HMCL was able to report faster-than-expected recovery, thereafter, resulting in better than the industry's aggregate performance. Against ~13% YoY decline in domestic volumes posted by the industry, HMCL reported a better performance, with a lower ~10% decline in volumes in FY2021. In exports as well, the company clocked a 6% YoY growth (albeit on a low base), while the industry exports contracted by 7%. While the negative operating leverage from the first quarter led to moderation in profitability in FY2021, ICRA notes the several cost containment initiatives taken by the company led to improvement in operating margins—from 11% in H1 FY2021 to 14% in H2 FY2021—despite escalating commodity prices. Even as the resurgence of Covid cases in Q1 FY2022 led to extended localised lockdowns and broke the demand recovery momentum for the industry, improving pace of the vaccination program, preference for personal mobility solutions (to adhere to social distancing norms), possibility of healthy rural cash flows and robust exports are expected to augur well for HMCL, and help it record a moderate growth in revenues in the current fiscal.

The rating continues to factor in the strong financial profile of the company, evidenced by its healthy profitability (average OPBDITA and core ROCE of ~15% and ~80%, respectively, over the past five years) and cash accruals, negative net debt position and robust liquidity profile (cash balances and liquid investments of ~Rs. 8,450 crore as on March 31, 2021). Over the years, HMCL's management has followed a prudent approach for growth. As a result, despite facing muted demand over the past two years and undertaking significant capex (towards setting up greenfield manufacturing units and investments towards a BS-VI compliant portfolio), the dependence on external borrowings has remained negligible. It is expected to remain so in the medium term as well.

¹ Market share for FY2021 as derived from SIAM data.

ICRA notes that HMCL's performance remains exposed to challenges such as increasing regulatory interventions (emission norms, safety norms) and fierce competition in the domestic 2W market. Additionally, the overall large revenue dependence on the domestic market (96%) and limited presence in the premium motorcycles and scooter segment, exposes it to adverse demand trends in the domestic/rural markets. A structural shift in preference for electric vehicles (EVs) (as opposed to conventional 2Ws) also remain a medium-to-long term challenge. However, HMCL's proven ability to adapt to the changing customer requirements and multipronged strategies to enhance presence in the aforementioned segments, mitigate the above risks to some extent. HMCL plans to address the risk posed by the EVs by launching its own EV product (expected next year), as well as strategic investment in Ather Energy and partnership with Gogoro, a Taiwanese developer of swappable e2W battery platform. In addition, its investments in Hero Fincorp Limited, for supporting 2W financing, evidence its focus on developing a favourable financing eco-system and are likely to aid it in its growth plans.

The Stable outlook on the long-term rating reflects ICRA's expectation that HMCL is likely to maintain its leadership position in the Indian 2W industry, aided by its strong product portfolio, established brands, extensive dealership network and regular investments in new model launches and R&D for future technologies. The same is likely to help HMCL successfully navigate the uncertainties caused by the pandemic or any other exogenous shocks, while maintaining a strong credit profile.

Key rating drivers and their description

Credit strengths

Market leader in the Indian 2W market with wide dealer network and strong rural connect - HMCL reported annual global sales of 5.8 million units and 1.9 million units in FY2021 and 5M FY2022, respectively, and maintained its market leadership in the Indian 2W market with a ~37% market share. Among the 2W segments, HMCL is a market leader in the domestic motorcycle segment with a ~52% share (in FY2021). It is also among the top four OEMs in the scooter segment, with a market share of ~10%. With new product launches in motorcycles, especially in the premium as well as scooter segments, HMCL is likely to maintain its leadership position in the Indian 2W industry. Its strong brand equity, well-entrenched distribution network and wide product offerings are likely to continue to aid in the same. HMCL has more than 9,000 customer touch points worldwide, with a deep-rooted rural presence in India, making it one of the strongest sales networks among all 2W manufacturers in the country.

Strong product portfolio with established brands - The company had four brands in the top 10 motorcycles sold in India and all its three models in the top 10 scooters sold in India for FY2021, the highest among any other 2W OEM. HMCL's strong brands include Splendor, HF Deluxe and Passion, which drive nearly 70% of its total volumes in the entry level sub-segment. A healthy dominance in the largest sub-segment of 2Ws, supported by healthy and increasing presence in other sub-segments as well as product categories (scooters), ensures healthy revenue visibility for the company.

Robust financial risk profile - HMCL's strong financial profile is evidenced by a conservative capital structure (TD/TNW of Nil and TOL/TNW of 0.5x as on March 31, 2021) and a negative net debt position at a consolidated level (zero debt on standalone basis). Despite contraction in operating profits and revenues in FY2021, the core RoCE of the business, on a consolidated level, stood at around 58% during the last fiscal, driven by high asset utilisation and minimal debt. Additionally, the company has sizeable amount of cash and investments worth ~Rs. 8,450 crore as of March 31, 2021 (including FMPs).

Credit challenges

Relatively low share in export markets; remains susceptible to vagaries of rural demand sentiment - The company is largely dependent on the domestic market, which accounted for 97% of total volumes dispatched in FY2021. While it has presence in over 40 overseas markets, HMCL's share in total 2W exports remained muted at 6% in FY2021. Nevertheless, the company

entered several distribution agreements in FY2021—in Mexico, Nicaragua, Honduras, and several African markets—to expand its exports. A better domestic-export mix could provide a cushion in case of slowdown in domestic demand.

HMCL has a high dependence on products in the entry and executive sub-segments of motorcycles, which primarily attract an income-sensitive rural and semi-urban clientele. While HMCL has launched several new products in the premium motorcycle and scooter segments to attract urban customers over the past few years and gained market share in FY2021, its market share in these segments remains modest till date. The impact of tie-up with Harley Davidson (in FY2021) for distribution and development of new premium products, to further enhance HMCL's premium segment presence, will also be ascertainable only over the medium term. The ability of the company to gain further market shares in these segments would remain critical for it to reduce its susceptibility to downturn in demand for the entry and executive level segments.

Increasing competition in domestic 2W market; structural transition to EVs over medium to long term - The Indian 2W industry is highly competitive with regular new product launches and refreshes by OEMs to gain market share. Aided by successful migration to BS-VI technology for its product portfolio and revamped 125cc scooters and new motorcycles in the premium segment, HMCL intends to improve its market share across segments and sub-segments. Consequently, consistent investment in R&D and introduction of newer models will remain crucial for HMCL to maintain its leadership position in the Indian 2W market.

As a market leader in conventional 2Ws, HMCL remains exposed to risk of a structural shift in customer preferences towards EVs over the medium to long-term. HMCL has adopted a three-pronged strategy to capitalise on the opportunities presented in this space—strategic investment in Ather Energy Private Limited (which has developed premium e2Ws), in-house R&D efforts (to develop mass market e2Ws) and collaboration with the Taiwan-based Gogoro to venture into battery swapping infrastructure. However, all these ventures are in very nascent stages and their success remains to be seen.

Liquidity position: Superior

HMCL's liquidity is **superior**, as reflected by strong cash and investments of nearly ~Rs. 8,450 crore as on March 31, 2021, (including FMPs, quoted debentures/bonds, etc.) and unutilised working capital bank limits of over Rs. 800 crore. Healthy accruals from the business, coupled with negligible debt obligations and favourable working capital cycle, have enabled the company to maintain a superior liquidity profile, despite large capex undertaken in the last few years. For FY2022 as well, the entire planned investments are expected to be funded through internal accruals. Despite near term demand uncertainties, ICRA expects the company to continue maintaining its superior liquidity profile.

Rating sensitivities

Positive factors – Not applicable

Negative factors – A sharp and sustained contraction in profitability metrics or significant erosion in market share on a sustained basis amid increasing competition, or any sizeable debt-funded inorganic/organic growth plans leading to material deterioration in credit metrics, or any sizeable cash outflow in the form of dividends or buybacks that sharply depletes the currently robust liquidity, could be triggers for a downward rating review.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Two-wheeler Manufacturers Rating approach- Consolidation
Parent/Group Support	Not applicable
Consolidation/Standalone	The ratings are based on the consolidated financial statements of the company. As on March 31, 2021, the company had four subsidiaries, two step-down subsidiaries and two associate companies, which are enlisted in Annexure-2.

About the company

HMCL is engaged in manufacturing and marketing of motorcycles and scooters and is the largest 2W manufacturer in the world. In India, it currently commands a market share of 37% (FY2021). The company has eight manufacturing facilities with an annual production capacity of 9.5 million units. Of the same, six plants are in India—one each at Dharuhera and Gurgaon (both in Haryana), Haridwar (Uttaranchal), Neemrana (Rajasthan), Halol (Gujarat) and Chittoor (Andhra Pradesh)—and two overseas—at Columbia and Bangladesh. Additionally, the company has also set up an R&D centre at Jaipur (India) and Germany and a Global Parts Center in Neemrana (Rajasthan). Backed by a large product portfolio across various price segments, HMCL is a market leader in the domestic motorcycle industry with a share of ~52% (FY2021). It is also present in the domestic scooter market, albeit its market share remains modest at ~10% (FY2021).

HMCL had commenced operations as Hero Honda, a joint venture company (both promoters holding 26% equity) between Hero Cycles Limited and Honda Motor Company (HMC), Japan, in January 1984. In January 2011, HMC agreed to transfer its entire shareholding of 26% to the Hero Group, thus bringing an end to the partnership. The company is listed on BSE and NSE. The B.M. Munjal family, led by Mr. Pawan Kant Munjal, holds ~34% stake in HMCL.

Key financial indicators (audited)

	FY2020	FY2021	Q1FY2022
Operating Income (Rs. crore)	29,254.0	30,959.2	5,502.8
PAT (Rs. crore)	3,624.8	2,982.6	256.5
OPBDIT/OI (%)	14.0%	13.3%	9.4%
PAT/OI (%)	12.4%	9.6%	4.7%
Total Outside Liabilities/Tangible Net Worth (times)	0.4	0.5	-
Total Debt/OPBDIT (times)	0.1	0.1	-
Interest Coverage (times)	87.7	88.4	38.6

Source: Company Annual Reports/ Limited Quarterly results; ICRA Research

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation

Status of non-cooperation with previous CRA: Not Applicable

Any other information: None

Rating history for past three years

Sl. No.	Instrument	Current Rating (FY2022)				Chronology of Rating History for the past 3 years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2021	Date & Rating in FY2020	Date & Rating in FY2019	
					1-Oct-21 28-Jul-21	31-Jul-20	19-Aug-19 21-Jun-19	3-May-18	
1	Issuer Rating	Long term	-	-	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	
2	Non-convertible Debenture Programme	Long term	15.0	*	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	
3	Fund-based and Non-fund Based Limits	Long term/ Short term	840.0	-	[ICRA]AAA (Stable)/ [ICRA]A1+	[ICRA]AAA (Stable)/ [ICRA]A1+	[ICRA]AAA (Stable)/ [ICRA]A1+	[ICRA]AAA (Stable)/ [ICRA]A1+	
4	Unallocated	Long term	260.0	-	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	

*The company has not issued any NCDs

Complexity level of the rated instruments

Instrument	Complexity Indicator
Issuer Rating	NA
Long Term-Bonds/NCD/LTD	NA
Long Term/Short Term - Fund Based and Non-Fund Based Limits	Simple
Long-Term-Unallocated	NA

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments, is available on ICRA's website: www.icra.in

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Issuer rating	-	-	-	-	[ICRA]AAA(Stable)
NA	Non-convertible Debenture Programme*	-	-	-	15.00	[ICRA]AAA(Stable)
NA	Fund-based and Non-fund Based Limits	NA	NA	NA	840.0	[ICRA]AAA(Stable)/ [ICRA]A1+
NA	Unallocated	NA	NA	NA	260.0	[ICRA]AAA(Stable)

Source: HMCL. * The company has not issued any NCD as on date.

Annexure-2: List of entities considered for consolidated analysis

Company Name	HMCL Ownership	Consolidation Approach
HMCL	Rated Entity	Full consolidation
HMCL Americas Inc.	100.0%	Full Consolidation
HMCL Netherlands B.V.	100.0%	Full Consolidation
Hero Tech Center Germany GmbH	100.0%	Full Consolidation
HMCL Colombia S.A.S (through HMCL Netherlands B.V)	68.0%	Full Consolidation
HMC MM Auto Limited	60.0%	Full Consolidation
HMCL Niloy Bangladesh Limited (through HMCL Netherlands B.V)	55.0%	Full Consolidation
Hero FinCorp Limited	41.2%	Equity Method
Ather Energy Private Limited	34.8%	Equity Method

Source: HMCL annual report FY2021

ANALYST CONTACTS

Shamsher Dewan
+91 124 4545 300
shamsherd@icraindia.com

Srikumar Krishnamurthy
+91 44 45964318
ksrikumar@icraindia.com

Rohan Kanwar Gupta
91 124 4545808
rohan.kanwar@icraindia.com

Ritu Goswami
91 124 4545826
ritu.goswami@icraindia.com

RELATIONSHIP CONTACT

L. Shivakumar
+91 22 6114 3406
shivakumar@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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ICRA Limited



Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001

Tel: +91 11 23357940-45



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