"Hero MotoCorp Limited
Q1 FY2020 Post Results Conference Call

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Moderator: Ladies and gentlemen good day and welcome to the Hero MotoCorp Limited Q1 FY2020 Post Earnings Conference Call hosted by Equirus Securities Private Limited. As the 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. Ashutosh Tiwari from Equirus Securities Private Limited. Thank you and over to you Sir!

Ashutosh Tiwari: Thanks Nirav. Good evening everyone. On behalf of Equirus Securities, I welcome you all to the conference call. Without further ado, I will hand over the call to Umang Khurana, Head Investor Relations for introducing the senior management team from Hero MotoCorp. Over to you, Umang!

Umang Khurana: Thank you, Ashutosh. Thank you for hosting us. Hello everyone! We have with us today Mr. Niranjan Gupta, Chief Financial Officer; Mr. Sanjay Bhan, the Head of Sales and After Sales and Mr. Surender Chhabra, Head of Corporate Finance. We planned the call for an hour.Nirav over to you! Nirav we will begin with Mr. Gupta making opening comments.

Niranjan Gupta: Welcome everyone to Hero MotoCorp's quarterly call. You would have seen our results by now. As far as volumes are concerned, we sold 18.4 lakhs vehicles during the quarter which was lower by 12.5% on a year-on-year basis versus industry which was lower by 10%; however, this included the effect of reduction of inventory by more than 80,000 units and therefore like-for-like we would have been lower by 9% versus the industry's decline of 10%.

Revenue was reported at ₹8,030 Crores. EBITDA margin was 14.4%. This reflects an improvement of 80-basis points sequentially.

Profit before tax included an exceptional item of ₹737 Crores. You would have seen from our notes to our results, that this is on account of the NCCD provision, which we had made over the years and pursuant to a favorable order from the Supreme Court, we have reversed it in this quarter.

Other than this there are a couple of one-off items in PBT. One is higher charge in depreciation amounting to ₹65 Crores. This is on account of accelerated depreciation on assets which will end their useful life by March 31, 2020 on account of BS-VI. The other one off is in other income which is ₹50 Crores and that is the interest provision reversal consequent to NCCD.

The reported PAT is ₹1,257 Crores versus₹909 Crores last year same quarter, which reflects a 38% increase. The underlying PAT after adjusting for these exceptional and one off items is ₹786 Crores for the quarter.

The parts business revenue which we always disclose to you for the quarter was ₹621 Crores versus last year of ₹602 Crores, it reflects 3% growth. Sequentially the Q4 was ₹790 Crores and usually Q4 is always a heavy quarter in terms of the increased parts sales.

With that I hand over for questions.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question and answer session. Ladies and gentlemen, we will wait for a moment while the question queue assembles. The first question is from the line of Kapil Singh from Nomura Securities. Please go ahead.

Kapil Singh: Thanks for the opportunity. Firstly, I wanted to check on the retail sales trend. Could you comment on how the retail sales have panned during the quarter on a YOY basis and how is the trend going to be in July? Looking at the FADA numbers, we can see that retails are down approximately 6% for the quarter is that representative and how is your retail market share?

Sanjay Bhan: Thank you Kapil. Yes, I think the numbers you probably referring to are the FADA has published basis Vahan reporting. So, I think, these numbers are quite consistent with what exactly is happening in the market place, so there is a decline in retail to the extent of about 6% and yes the dispatches overall as per the industry have been down 11.5% so I guess a lot of people have corrected stocks during the quarter. The retails have been slightly better than the dispatches, which is reflected there and you would have also seen the market shares of the players in that report.

Kapil Singh: How is the outlook on retails?

Sanjay Bhan: We did expect the retails to be a little better than negative retail in the first quarter. We had expected some recoveries in the first quarter. This has been a rather soft quarter. May was a very good month, but April and June were not very strong. As things stand, we do expect things to get a little better. There is a lot of expectation building up. We do hope that the season closer to the season things might just start looking better.

Kapil Singh: Secondly, I wanted to check on your market share especially segment wise, we can see some improvement now happening in the economy segment after the heightened competition intensity, but now we are seeing some signs of increased competition in the deluxe segment, so your thoughts on the same and how you are going to handle that?

Sanjay Bhan: Market is a very dynamic situation. Last time around, in fact in several rounds of these earnings calls, we used to get this question about how competition is trying to discount their way in the entry segment and we kept on saying that that is something that we will definitely not do. We will gain back the shares basis our own strategies, which is what we have done and hence we are back with a bang in the entry segment both at a dispatch level as well as in terms of retails, we are doing quite well there now. Yes, there have been a few launches as is known, there is always a first fill attached to the launch, there is the certain amount of stock buildup that also happens in case of a launch. So, you have to brand that and therefore when you look at these there is a slight correction in terms of market share in deluxe segment, as you are pointing out. It is also a function of the amount of stock correction, we have taken. Mr. Gupta just talked to you about 80,000 plus stock correction and majority of that has happened actually in the deluxe segment because that is our key segment and therefore as a consequence it is obviously bound to happen that you may lose a few market share points, but otherwise on retail terms we are pretty strong. Surely competition is intensified. It has always been very intense. It is just that we have been extremely strong and we continue to be so. So, hopefully we will see some further corrections happening as we go along.

Kapil Singh: Thank Sir. Thank you.

Moderator: Thank you. The next question is from the line of Raghunandhan NL from Emkay Global Financial Services. Please go ahead.

Raghunandhan NL: Thank you Sir for the opportunity. Media reports have been indicating about tightening of bank funding to dealers. Can you highlight the initiatives Hero has been taking to support dealers in terms of credit period, corporate guarantee, captive finance, unit support, etc.?

Niranjan Gupta: Yes, in the media a lot of reports have appeared. I presume they are more to do with probably four wheelers. As far as we are concerned, we had also outlined in the last call that we have extended the credit period in order to support the dealers and that is reflected in the higher receivables that we have. Other than that, as far as we are concerned, it is about ensuring that the retail sales grow and therefore all the schemes, promotions or our actions are more towards increasing the throughput and also reducing the inventory, which we have already highlighted that there is another means of ensuring that the stress comes down in the system. So those are the steps that we have taken and we will be continuing.

Raghunandhan NL: Anything you can highlight what have supported the other income in the quarter and also anything you can quantify on the Ind-AS impact? Thank you.

Niranjan Gupta: As I explained the other income in the quarter includes one-off income of 50 Crores. This is on account of the interest provision that we had made linked to the NCCD provision that we talked about. Sorry, what was your other question?

Raghunandhan NL: Ind-AS impact, Ind-AS 116 impact?

Niranjan Gupta: Ind-As 116 impact is negligible. In fact the net impact of all the adjustments is ₹4 Crores for the quarter.

Raghunandhan NL: Sir, 65 Crores was the accelerated depreciation, is that correct?

Niranjan Gupta: Yes.

Raghunandhan NL: Thank you so much. I will come back in the queue for more questions.

Moderator: Thank you. The next question is from the line of Gunjan Prithyani from JP Morgan. Please go ahead.

Gunjan Prithyani: Thanks for taking my questions. Just, a followup on the accelerated depreciation that you mentioned this essentially will be a similar number through the rest of this year or you have just kind of taken the whole adjustment in this quarter?

Niranjan Gupta: For the rest of the year, for the balance three quarters you will see around ₹30 Crores per quarter in terms of the accelerated depreciation against a ₹65 Crores for this quarter. And that ends by March 31, 2020.

Gunjan Prithyani: Then we will move to the normalized depreciation of about 150 Crores or 160 Crores, a quarter, of course we have the new plant commissioning but that should be the level at which it will continue?

Niranjan Gupta: Yes, it will be normalized depreciation subject to the capitalization consequent to Andhra plant.

Gunjan Prithyani: The other thing I wanted to followup was on the market share in scooters. Now we did have couple of launches here which last quarter we had indicated we were doing well on the retail side, but the market share really has not improved at all. In fact, in this quarter it has deteriorated so I am just trying to understand what is happening in this segment, with your new launches now out in the market?

Sanjay Bhan: I think when you look at the scooter market, overall has not been doing well. 75% of the market is 100-110cc and that has been declining at about 23% in the quarter whereas the 25% market which is a 125cc upwards has been growing at about 12%. So this growth has come down from what it was earlier, but still growing. Thankfully, we are now reasonably well covered. We have had two more launches in the 125cc segment with the Maestro 125cc and the Maestro FI 125cc to support Destini. We talked about Destini doing extremely well post launch and continues to do well. It is doing very well in terms of retails. We continue to have approximately about 15% retail market share on Destini and with the support from the two other siblings in the form of Maestro 125 twins we do expect to garner more share in the 125cc.

Niranjan Gupta: I think just to add to what Mr. Bhan has explained the launch Maestro Edge 125cc, which has been done recently in June will not only help us occupy more space, much more space in 125cc, which is actually the growing segment, but is also likely to help the Maestro Edge's equity and therefore help the sales of Maestro Edge 110cc as well. Other than that we have also launched the Pleasure 110, which is a full body refresh and therefore that addresses Pleasure in the 110cc segment as well, so I think as the volumes pickup of the new launches we should see our scooter portfolio getting boosted moving forward?

Gunjan Prithyani: So the market share is essentially reflection of some drag coming from the rundown of the earlier model as well?

Niranjan Gupta: Partly yes.

Gunjan Prithyani: Which we are seeing on the whole sales?

Niranjan Gupta: Yes.

Gunjan Prithyani: Just last question on the gross margin if I look at your sequential the RM has moved up about 60 basis Q on Q, is there any commodity easing that we are seeing at all, what is the reason for this increase and even ASPs have come, so if you can just share some thoughts on this?

Niranjan Gupta: Actually the underlying ASP of two-wheeler has gone up. What you see is the reflection of parts revenue, which is lower in percentage terms for this quarter. So if you see Q1 our parts percentage to revenue is 7.7% and since you are comparing sequentially Q4 was 10%. So if you have to eliminate the impact of parts then you would see that actually two-wheeler realization has gone up by close to around Rs.350 per vehicle sequentially and you would also see that the material cost underlying has come down. Of course, the material cost has an adverse impact of HSRB as well as the CBS rollover, part of the portfolio got rolled over you see the full impact sequentially in this quarter. Moving forward, yes the commodities have remained in a range on a softer note, so as far as margin is concerned amongst the headwinds and tailwinds if I were to identify a tailwind it would be commodity cost.

Gunjan Prithyani: Thank you so much.

Moderator: Thank you. The next question is from the line of Aditya Makharia from HDFC Securities. Please go ahead.

Aditya Makharia: What is our volume growth outlook for the industry for FY2020?

Niranjan Gupta: As things stand currently we do believe that there is going to be an improvement in the sentiment as you get into H2, which will be partially reflected during the festive season, which incidentally starts off on the September 29, 2019, so while some effect will come into Q2, but largely in Q3 and we do hope that some of these changes that we expect in terms of good monsoon, bringing in some cheer into the rural markets, so better participation by the rural is likely to create some positive impact in H2, so going forward versus H1 we do expect a better H2 and there is also this possibility that as we get into Q4 there is this whole piece about BS-VI coming in on April 1, 2020, which is also going to support some numbers in Q4, pre-buying is likely to happen given the overall structure.

Niranjan Gupta: But as a number, just to add, these are really early days to recalibrate and probably we will be recalibrating in outlook number in terms of after seeing how the festive season goes.

Aditya Makharia: Okay, what is our current outlook if I may just ask?

Niranjan Gupta: Right now it is very difficult to put a full year number on it and as we said that the second half we expect better and first half there are various factors, which we believe should play out and once the festive season plays itself out then we can take a call on the full year number.

Aditya Makharia: Sure and just second on the other expenditure there has been a decline on the absolute amount on a YOY basis, so anything to read into that?

Niranjan Gupta: The decline is more to do with certain expenditures which are lower in Q1, which will get elevated in Q2, some of the advertisement phasing on our new launches will be seen in Q2, so it is a more reflection of that rather than any underlying decrease in absolute. There is also an impact of the volume, so you see a lower volume year-on-year basis, so you have lower logistic expenses, which is obviously underlying reduction that happens because of the variable part in the other expenses.

Aditya Makharia: Thank you.

Moderator: Thank you. The next question is from the line of Hitesh Goel from Kotak Securities. Please go ahead.

Hitesh Goel: Thanks for taking my question sir. Basically most of your competitors are talking about a decline in the industry in FY2020 and an outlook for FY2021 also looks little bleak because of the BS-VI changes, which are likely to come in. Are you in a position to quantify the kind of cost increase you may see on your buying because of BS-VI and when will you migrate to BS-VI in terms of the overall portfolio?

Niranjan Gupta: As far as BS-VI is concerned like we said last time as well, you would see the increases whether it is cost or price as the models start getting launched, so as of now we are not in a position to give that number out.

Hitesh Goel: When will you migrate the models to BS-VI sir?

Sanjay Bhan: We are ready with the, as you know, we were the first ones to get the BS-VI certification. Our models are getting readied in time and as far as launch is concerned as we said we will be launching in second half. The exact timing we will decide model by model based on our own transition strategy.

Hitesh Goel: Okay and are you ruling out a decline in the industry in FY2020 because of pre-buy that you expecting or it is a wait and watch currently?

Niranjan Gupta: It is a wait and watch currently. As we have said let us wait for the festive season how it pans out because last year festive season was soft. There have been a few adverse factors impacting two-wheelers so far. There is also a buying postponement, which has been happening. There has been liquidity problem, which seems to be easing out a bit. There is an interest rate cuts, which has been happening, so we will have to see how these positive factors play out and what role do they play moving into festive season. So let us wait and watch.

Hitesh Goel: Sir my final question if I can squeeze in, on the electric side are you launching any product in the next one year because TVS and Bajaj have already announced that they will be launching electric products. Is Hero in a position to tell us about the electric right now?

Niranjan Gupta: So we would not be able to give a timeline to you right now, but what we can say that we are working on multiple fronts as far as electric vehicles are concerned.

Hitesh Goel: All the best. Thank you.

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

Jinesh Gandhi: My question pertains to firstly on inventory you indicated there is reduction by 80,000 how much it would be now, would be what about six, seven weeks or lower than that?

Niranjan Gupta: We indicated last time it was 45 to 50 days, 80k actually translates to around three days roughly, three to four days, so that is the reduction over the 45 to 50 day range that we talked about based on the forecasted sales.

Jinesh Gandhi: Okay and this is where we would be comfortable entering into festive season.

Niranjan Gupta: Well the point is that at this point in time last year we had started building up inventory already, so in a sense that from here on as you build up for the festive one would be comfortable with these levels.

Jinesh Gandhi: Understood. Secondly you mentioned about second have to be better than first half in terms of the expectation, I am presuming would be from retail volume perspective not necessarily from wholesale?

Sanjay Bhan: Yes, so Jinesh I think the reason for us, I think Mr. Gupta mentioned about it that you know this is basis what we currently understand from the customer dynamics point of view because I think best judge of how the industry is going to pan out is not few of us sitting in this room and the rest of you out there, it is the customers who have in some sense indicated in more ways than one that there is a certain amount of genuine intent to buy, it is just that for now they are holding up their purchases. We have reason to believe that there is a whole bunch of customers who have a solid intent to buy, but have deferred their purchase. One clearly seems to be a deferment approach, which at some point in time basically caves in given the overall context in which buying happens and festivals tend to become one of those opportunity areas and periods and spaces wherein a customer eventually decides to go out there and buy.

So I guess that said, it will be very hugely incumbent on a couple of factors. Of course, the factor of rains and the monsoons the way they pan out, how the Kharif crop really comes up and how the prices are there in the rural market, farmers and the upcountry markets to respond, it also depends on the entire NBFC piece how that pans out in terms of liquidity. If these two factors- farm income and liquidity on both sides start working positively for the industry, we do expect a very robust hopefully a good solid recovery getting into second half, that is the reason we are very hopeful and optimistic about, though cautious, yet optimistic about the second half. At this stage it would be too early for us to give up on this second half. I think it is evident. It is not just, as I think in a question earlier was put forth is it entirely on account of the preponement or pre-buying from BS-VI to BS-IV, no not really that, that is one factor, but beyond that also some fundamental demand drivers, if it starts playing up, we do expect some recovery.

Jinesh Gandhi: Got it and with respect to Ind-AS 116 impact you indicated Rs.4 Crores that is negative impact at PBT level right?

Niranjan Gupta: Yes.

Jinesh Gandhi: And any idea how it will split between other expenses, depreciation?

Niranjan Gupta: Sorry I did not understand the question?

Jinesh Gandhi: So there will be some expenses which would have shifted out from other expenses to depreciation?

Niranjan Gupta: That is very marginal. It is an impact of around probably 10 basis points in terms of EBITDA level.

Jinesh Gandhi: Lastly with respect to our capex guidance we maintain the capex guidance, which we have given to the street of ₹1,500 Crores for FY2020 or is there any change?

Niranjan Gupta: Could be a tad lower as we move forward because that was the overall estimate that we had and we will recalibrate this as we move towards second half.

Jinesh Gandhi: Thanks all the best. I will come back in queue.

Moderator: Thank you. The next question is from the line of Ruchit Mehta from SBI Mutual Fund. Please go ahead.

Ruchit Mehta: Just on the BS-VI transition any comments on the potential for E-carb are we rolling that out at this point and you see that as a risk factor especially in the economy segment if competition does launch on that?

Niranjan Gupta: As far as we are concerned, we are going ahead with FI as our lead technology and as far as E-carb is concerned it is more to do with our own strategy that we did not want to the risk the portfolio transition, given that FI is a more robust and tested technology. While E-carb may or may not have a cost opportunity, but could also entail risk to the portfolio. That is the strategy we have chosen and as we move forward we will see how it pans out in terms of cost, in terms of performance, in terms of on-road capability, in terms of its adaptability to OBD2, which is going to come out, so we will see how it pans out. It is not a very easy and simple choice that you choose a technology just based on costs. And also to ensure that we keep working on something our R&D is also working in parallel with E-carb as well, but going in the transition will happen on FI basis.

Sanjay Bhan: I think earlier also we mentioned this in an earlier call, I think one technology that seems to have all the answers to dealing with compliance is FI right and I think this is proven and this is agreed to and largely everyone endorses that. E-Carb is a relatively new animal in that sense. Yes we are aware that there are some people who are working on E-Carb as the primary solution. In our case we obviously would like to take a more secure path because it is about seriously bearing to compliance in E-carb, like Niranjan mentioned, is something that we are working parallelly on, just to keep our options open.

Ruchit Mehta: Just to go back to the electric vehicle question, your competition has talked of launching something this year itself. Is there a risk that we have falling behind on the R&D side are again on this front and we could be launching after competition launches and therefore struggle to create any sort of large first mover advantage or sort of impression in the market that you have the technology and capability of that?

Niranjan Gupta: Not at all. First of all by investing in Ather we are the ones who got the product in the market earlier than everyone else and that generates a lot of learning, a lot of experience first of all and that is why we made the strategic investment in Ather, they launched in Bengaluru, they have expanded to Chennai, so that is answering your question on are we behind or are we ahead. The second thing is in terms of our plan. Our plan, we have our in-house also working on multiple fronts. Also I want to explain that it is not going to be that one launches and then you start picking up thousands or lakhs of volumes. It will be a lot of experimentation. The industry will go through a lot of experiment, lot of experience in this whole journey of EV. It is not going to scale up overnight just by launching, so there will be a lot of trials and errors and experience building that will happen and it will be more about who gets the product right at the right cost and actually right customer preference and convenience will determine the winner. Further, we have also expanded our R&D centre as you know by actually putting a node in Germany TCG, which is our Tech Centre in Germany and there are people there are sourced from experienced manufacturers and they are also working parallelly on E vehicles as we speak.

Ruchit Mehta: Thanks.

Moderator: Thank you. The next question is from the line of Chirag Shah from Edelweiss Financial Services. Please go ahead.

Chirag Shah: Sir two questions. One if you can throw some light on the discounting trend Y-O-Y or Q-O-Q basis and would it be a right statement that with the current gross margin in the current quarter are also separate because of higher retail supporting activity you have received?

Niranjan Gupta: I will answer first and then may be Mr. Bhan can add on to that. So it would not be right to say that the gross margin is impacted because of that. As I said the ASP actually has moved up sequentially if you see reflecting that the price increase that we have taken is actually translating into our numbers, what you see the decline in ASP is the result of the parts revenue mix as a percentage of overall revenue. Having said that Mr. Bhan can comment more on the overall nature of and what is happening in the market on the scheme etc.

Sanjay Bhan: Right now, I do not think there is any (scheme), we have maintained this, we have not been discounting. We would continue to kind of support that agenda. I think it is all about brands at the end of the day. Right now the only thing that seems to be something that really the customers are looking forward to is how do we find ways to break those barriers for them in terms of adoption to the category. I guess that would obviously entail more aggressive penetrative financing options that is something that we work on very regularly. Obviously that is an area which would need further impetus going forward, I guess increasingly there would be a dire need for us to make sure that we are able to get in more customers into the fold and financing would be a good way to do that, I think that is very critical and price increase has been there, already you have seen the price increase in April. We have also increased our prices in the month of July, July 8, or thereabouts so in that sense it is just to take care of some of the costs etc., that are there, but there is no discounting to the customer in the current situation. What we are trying to do is we are trying to be far more robust enabling system for the customer to be able to adopt and come in because one thing is very critical is the availability. In fact availability of finance in urban centers has become a challenge actually because of the NBFC liquidity issue and the footprint of finance in rural markets is the other challenge, so we are trying to tackle both and make sure that customers are able to get to buy the bikes.

Chirag Shah: Sir, why I was asking this is that whatever customer support activity that you would be running and I presume that would be at a reasonably high decibel for the entire industry would either gets accounted in other expenses or in raw material expenses in terms of lowering of ASP and hence raw material ratio turns slightly adverse, but we are seeing either of the two things happening. So that is why I was curious to understand what kind of activities have been and has the intensity of support activity gone down, is that a right statement and that activity has bottomed out from industry perspective?

Sanjay Bhan: When there are these kind of times that we undergoing right now we have to smart about the way we position our strategies in the market. You would have heard about our strategy on "buysurance" for instance, now that might seem to some of us in terms of the promotion, but the fact is that there is very little outgo from outside, in fact there is none. It has been primarily funded. It is almost like a crowd sourced kind of a fund wherein there is a certain third party, which is reassuring that they are able to give the price coverage to our customers and therefore making decision of being able to sell their bikes or two-wheelers at a price, which is perhaps the most attractive. As a consequence of things like that the resale prices in those markets are also obviously going upwards, which is therefore helping the brands further. Now we have to be innovative and that is what we have done exactly.

Therefore, like I said we have not really been running any promotions during the course of this particular quarter except for some local promotion that gets factored in this part of our sales promotion cost, which is very nominal, but there are no discounts and there is nothing like that and we have really no immediate plans because that is not what the customer is really looking at. The customer is trying to find ways how he can be able to reach out and make that decision. I guess to break those barriers would be far more critical. Yes, of course there has been this whole setback about insurance cost increase, etc., etc., but that I think by now customers have really subsumed that, that is part of it. There are some more surprises in store like you would have read registration cost going up etc., which is another pain area, so we are trying to seek ways and find ways to minimize the pain for the customer to be able to eventually buy.

Chirag Shah: One last question on commodity prices, so it seems there has been some benefits in the quarter, is it a right statement and outlook for the ensuing quarters?

Niranjan Gupta: Yes it is, so you are right, there is some benefit in the quarter and one could see probably as I said if you were to count amongst the headwinds and tailwinds then one of the tailwinds one could look at is commodities moving forward. The good thing is as long as they remain even the current level then that helps in terms of stability of margins.

Jay Mehta: That is really helpful. All the best Sir and congrats for a good set of numbers.

Moderator: Thank you. The next question is from the line of Ashwani Kumar is a Fund Manager at Reliance Mutual Fund. Please go ahead.

Ashwani Kumar: My question to Mr. Bhan, Sir are you experiencing this delay or postponement across rural and urban alike which means that people are postponing at both places or is it specific in some certain markets?

Sanjay Bhan: Thanks Ashwani for the question. I think it is a very important question. If you were to ask me frankly the postponement is more significant in case of rural markets, it is not as sharp in case of urban markets because of the available options there, but in case of rural it is a little more pronounced, but it is there in both rural and urban far more sharper in rural than in urban.

Ashwani Kumar: Let us say within rural also let us say if you look at two segments, one is the first-time buyer and another is the upgrade buyer, his replacement in our earlier conversion with you the replacement cycle has been let us say five years or some it may be six, seven and for some it may be three-and-a-half, but do you still standby that this four-and-a-half, five years is the replacement cycle for the two-wheeler buyer for you for Hero MotoCorp for example?

Sanjay Bhan: Honestly, we do not have specific data to kind of validate what I am about to tell you right now more in the current context, but it is bound to happen, Ashwani because when you have people postponing, so it would be a postponement both from somebody who is coming in new and as also by someone who is actually there in the category and he always has that two-wheeler with him right now and maybe he says he can wait 3-4 more month. I do not have segregated data right now, but in any case I think it would be in both categories now. How different would there be, I do not have specific information to share at this stage.

Ashwani Kumar: Sir, what would let us say make the person who is postponing today, change his mind, what has to happen for him who is postponing to come back in the next one or two or three quarters? What is the critical factor?

Sanjay Bhan: Two-wheeler is a considered purchase and it is as emotional as it is rational, so I guess more from a rational point of view, because always in relation for a person to emotionally embrace a brand will stay on, it will not really change significantly, but I think the rational reasons for instance the change in sentiment of the market, the availability of credit, the ease and comfort or interest rate ease up, some impact from a price point of view, there is something, some intervention from the government and we are hoping that the government will in fact have gone and been requesting across there is a reason for the government to look at auto industry, two wheelers in specific, it is a common person's vehicle.

If the government sees that the kind of impact it has on the GDP growth rates and we get some support from those areas I am sure the sentiment will change, I am sure the person who is holding back right now, would want to come happily and buy. I guess it is a mix about the emotional and rational reasons, right now the reasons that he is holding back or she is holding back is only rational, emotionally they are still very connected two wheelers and that is what get thrown back to you when you look at data in terms of the extent of postponement.

Ashwani Kumar: So does mean that your enquiries have not gone down, but the conversion has not one off, is that the right way to look at it?

Sanjay Bhan: Enquiries have been more or less there. It has not been such a dramatic decline. Enquiries are there. People are checking out. People are hoping that they will come back sooner the later and it is also kind of being played back and listen I would rather wait for a few months and see how things pan out, so it is a wait and watch that is what the customer is doing right now and hoping that somethings might given and things might change for better. It could be anybody's guess at this stage and they do not change too much when the customers will still come and buy. I guess if there are other things around in the environment will change, if the rains are good, if the monsoons are good and the crops are healthy and fine, if the liquidity in the market improves, his disposable or her disposable level of income is looking much better, well that is good enough reason for customers to start looking back at industry.

Moderator: Thank you. The next question is from the line of Shyam Sriram from Sundaram Mutual Fund. Please go ahead.

Shyam Sriram: Thanks so much for the opportunity sir. In our annual report we have spoken about business from the secondary network contributing 53% to our overall business, are these sub-dealers that we are talking about and what has changed over the last few years in terms of cultivating this channel if you can just talk about bit of it?

Sanjay Bhan: We have always had a very strong network overall, not just a primary network, but we have had a very robust secondary network, which includes our authorized service centers what we called as ARDs, which operate under dealers and therefore massive footprint we have been talking about at huge footprint that we have across the country, so that has always been very robust and therefore a lot of these people have been significantly contributing to overall growth. I guess their growth right now is inline with overall market sentiment, so hopefully when the market opens up, we will also benefit from that opportunity.

Shyam Sriram: When we talk about dealer inventory that includes the sub-dealers as well right Sir?

Niranjan Gupta: Yes that includes the sub-dealers as well in terms of number of days that really counts for that.

Shyam Sriram: Thanks for that. Sir, in terms of the electric vehicles, we hear that even some customers have started coming to showroom enquiring about electric vehicles, clearly the government seems intend on promoting EVs whether they cutting the GST or hiking registration fees whatever be the way, from your own customer surveys what factors need to be in place for adoption of EVs, more from a customer mindset perspective of course price is one key factor that impacts the purchasing decision, what other factors do you think are required to be in place for adoption of EVs?

Niranjan Gupta: There are multiple factors. The game of EV is not so easy that you put out a product in the market and market will migrate from traditional IC engine to EV. First, there is a price factor, so if you see even the current like-for-like vehicles in the market, are priced at almost 2x compared to their ICE siblings. The second factor, then becomes the convenience of charging. You do not have as many charging stations as fuel stations that you have and therefore building up that infrastructure is another thing. Third, is the time that it takes to charge. Fourth, is how does it feel on acceleration, movement when the battery dies out, battery infrastructure, battery technologies, so there are plethora of factors which will determine the EV transition from a sourcing side, manufacturing side, viability side and the customer side, so I think this is the game of at least, one thing is sure that yes as an industry we are supportive our EV movement, but there will be a transition which will be more slow burn than what one would be expecting and one we will have to learn and put that out and then actually probably it will be more about co-existence of the two technologies rather than one technology giving placed to another one.

Shyam Sriram: We have been adding capacities in Andhra as well, Rs.650 Crores in phase one, are we planning any EV production there, is the line fungible if at all needed at a later point of time?

Niranjan Gupta: Yes, the production can be done there once we are ready with the product.

Shyam Sriram: One last question sorry I missed the part sales absolute numbers that you shared s, spare parts?

Niranjan Gupta: The parts Q1 is ₹621 Crores. Last year Q1 was ₹602 Crores and Q4 FY2019 was ₹790 Crores and just one bit of modification or correction on what Mr. Bhan said is the inventory numbers that we put out is the inventory that we hold and the dealers hold because that is what the account for sales, forecasting, inventory management all the sort of stuff, beyond that it is something that the dealer takes the call.

Shyam Sriram: Beyond that the dealer takes the call as in…

Niranjan Gupta: Dealer take the call on the network, because the network sales are done by the dealers. We do not track that inventory.

Shyam Sriram: Thank you very much.

Moderator: Thank you. The next question is from the line of Pratik Poddar from Reliance Nippon Life Insurance. Please go ahead.

Pratik Poddar: Two questions, one was with regards to your accelerated depreciation, could you ask just about what is the nature of these accelerated depreciation which you are taking this year instead of next, because I would have thought it would have come with BS-VI but you are taking in advance? That is one. Second is if I were to look at monsoons this year there has been a wide disparity between some states in excess and some states in extreme red in fact something like Saurashtra is, it is as deficient as 50%, so just on this variation, are you seeing that in these states which are red as of now, enquiries are very low and workings are low whereas states with the monsoon is healthy, walk-ins are higher? Those are the two questions.

Niranjan Gupta: I will address the BS-VI depreciation question and I will hand over for monsoon to Mr. Bhan. As far as depreciation is concerned, this is of the assets as you migrate from BS-IV to BS-VI there will be certain assets and machines which will be rendered obsolete or it actually reaches the end of life by March 31, 2020. Now one could technically say that okay I could take it after determining March 31, 2020, one could take in FY2021, but being prudent in our accounting and financials and that is why we have taken that accelerated depreciation this year itself.

Pratik Poddar: If I may interfere there are no products development related expenses under these accelerated?

Niranjan Gupta: These are all machines.

Sanjay Bhan: On the monsoon, yes you are absolutely right. Like I said, these are all very strongly linked to with the customer sentiment. I guess you said it yourself. I guess in market where the monsoons are deficient, not as good the problem obviously yes that there is a slightly bit of setback in terms of customers not being as forthcoming and therefore there is a challenge even now. So, going forward if things do not improve then we do expect those markets and those pockets specifically the ones that you mentioned would continue to struggle, but there is also a problem of plenty that we have certain areas which are maroon right now, pretty much under water while there is a sentiment in the market where people are saying “sona baras raha hai,” “gold is raining” but there is also too much of gold that is coming down from the heavens right now.

So I think there are two sides to the story, one of course is the excess in certain areas which is leading to problems currently and creating further depression in the market, because obviously that kind of rain it is very difficult for people to come out and buy, but it is good news for future. There are also markets where there is a certain deficiency, I think the last count end of July 26 or July 27 there was about 90% expectancy of monsoon which is pretty much in the zone that we have been having about six, seven years, 86% to 97% range, so I guess we will be pretty much there, hopefully even if we are close to about 90%, 92%, 93% overall, there would always be some pockets in certain states, which might be a challenge, but like I said we will obviously deal with that as things move.

Pratik Poddar: Sir just one question, there have been comments by the industry to keep the GST rates at 18% next year versus 28% currently, my only question was even if you keep the rates same what makes the industry believe that come next year people would come and buy because the prices are same as what it could be today, so just on that if you could clarify?

Sanjay Bhan: First of all before Niranjan answers that, my point is that I do not think anybody has specifically said that next year I think everybody in the industry saying now, that is the whole point.

Niranjan Gupta: I think I agree with Mr. Bhan when he is saying that we are not saying next year, we are saying this an immediate step which is required and in any case if you look at the customers, customers are building in or planning in their own calculation that this will be the X amount that will go up because of BS-VI and therefore clearly at 28% to 18% is always favorable, because if you pay something 28%, you will pay 10% lower at 18%, so that is simple equation and that is in customer's mind as well. So definitely first that will help boost the sentiment right now in terms of customers coming back, second it helps to insulate the BS-VI impact, third is also that apart from all this, it is just logical and rational, because two-wheelers by no means of imagination can be called either a luxury good or a sin good all of us know that it is a means of basic mobility and basic income enabler for most of the commuting classes who hail from rural and semi-urban areas, so there is a strong rationale to it, we as industry are representing and let us see what happens.

Moderator: The next question is from the line of Basudeb Banerjee from Ambit Capital. Please go ahead.

Basudeb Banerjee: Congrats Sir for decent set of numbers. Few questions, one if I remember last quarter concall you said that Hero Fincorp has been bit cautious in terms of financing in this kind of demand environment, so how has that progressed this quarter and how much is financing mix and how much is from Fincorp this quarter?

Niranjan Gupta: The overall financing of our sales this quarter is 37.3% and Fincorp's share out of this is 47%.

Basudeb Banerjee: In terms of liquidity issues and financing this how are you looking towards that in coming months?

Niranjan Gupta: I think from a two-wheeler financing point of view, I would not say that is a big problem given that we have Fincorp as an associate company and as you can see the share of Fincorp has gone up 42% to 47%, so obviously there are other NBFCs who would have brought down their shares are facing liquidity issues. (Hero) Fincorp has been managing its affairs quite well. In fact, their loan book has grown almost by 40% on a year-on-year basis and that is helping two-wheeler financing. I think what is important is moving forward if the interest rates cuts which are happening at the RBI level and you would have seen today SBI cutting deposit rates, so therefore it is the transmission of these rates by the banks and therefore through the NBFCs that could result in actually lower costs and lower EMIs moving forward, if that helps that could be another positive factor moving forward in second half.

Basudeb Banerjee: Second thing Sir if I see the combination of insurance price hike per vehicle and safety norm led price hike, these two have been the major price hikes over last year and this kind of retail sentiment has happened and now down the line this proposed registration hike of almost Rs.950 per unit plus few states road tax hike of similar quantum plus BS-VI price hike, so incremental price hike looks much, much larger than whatever has happened in past 12 months, so how do you look at customers accepting this and impact on retail demand?

Niranjan Gupta: Impact on demand of the prices whatever has happened, has already reflected in the market and which we have talked about and which you have seen. Also I have to say that it is not just impact of the price, if price was only factor, if rest of the things were doing well liquidity, interest, economic sentiments, rural incomes, then of course if you have higher income you can afford to pay higher price as well, so it is multiple factors and not price alone and these are getting reflected absorbed as cumulative impact into the sale as you see. So moving forward it will be only a sequential impact of BS-VI whatever accounts when you transition to BS-VI and then we will have to see what happens from there on.

Basudeb Banerjee: One small thing sir, as you mentioned mix of spares declined by 230-basis points as a percentage of revenue sequentially despite that I see typically spares margins are much higher than product margin and I see your margin improving where am I missing? Is it purely reflected in the 60-BPS sequential gross margin decline or somewhere else because your other expense on absolute is like lowest in 10 quarters, so how to look at that?

Niranjan Gupta: Yes, it is partly to do with as we said that in Q1 other expenses are lower, partly on account of the logistics cost and partly on account of some of the expenditures or advertisement or the media breakout that will happen in Q2. Other than that there have been some of the commodity benefits as well and Parts if you see on sequential basis as what you are saying 230-basis points down as a percentage, but year-on-year basis it has moved up from 6.8% to 7.7% just to correct that on the Parts revenue.

Sanjay Bhan: Just to add I think Q1 typically on Parts is always the smallest quarter, it starts building post that in any case what is happening in the vehicle sales is also true in terms of what sentiment is in the aftermarket, so I guess as we go on as sentiment keeps improving, things could start looking upward.

Moderator: Thank you. The next question is from the line of Ronak Sarda from Systematix Group. Please go ahead.

Ronak Sarda: Thanks for the opportunity and congrats on decent set of numbers. Sir my question is on the premium model launches Extreme 200, how has been the initial feedback from customers, dealers anything which you can share?

Sanjay Bhan: Ronak thank you very much. First of all thanks for appreciating the performance. Yes the initial excitement has been pretty good I think the response is a little too early to really conclude anything, but yes, the response has been an extremely overwhelming in terms of how customers and dealers have looked at the models. The numbers right now may not seem very significant, because it is only towards the second half of June, towards end of June that we were be able to finally start selling these models, but even this in the short while we have done fairly decent on retails. There is clearly in markets like Kerala for instance there is a serious demand for some of the variants of the XPulse, we are struggling to really apply given the overall ramp up time it takes, but yes I think the response has been extremely encouraging and we are looking forward to really making some impact thorough these models as we go forward in the premium segment.

Ronak Sarda: That is great. Second clarification on financial side, employee expenses if I look there have been growing double-digit despite fall in volume, is this largely to do it Halol ramp up and also some media reports highlighted some voluntary retirement schemes announced by the company, is that significant can you highlight any impact of that?

Niranjan Gupta: As far as the employee expenses are concerned, what you are looking at is on year-on-year basis which is the absolute increase of around 12%, 13%, but that is very normal because if you look at around 3%, 4% is the increase in the manpower, which would be get accounted as you rightly said by the Halol ramp up and also our R&D ramp up because that is where we have been investing to ramp up our R&D and balance around 8%, 9% reflects the annual increases, so it is nothing abnormal, I would say given the ramp up of manufacturing capacities and ramp up of our R&D capability that is pretty much expected. As far as VRS is concerned we do not comment on speculation.

Ronak Sarda: Okay and Sir price hike during the quarter just wanted to understand what will be the prior increase because of CBS and ABS and has that been passed on for the entire range now?

Niranjan Gupta: CBS and ABS price increase had happened way back. I mean, we had started migrating our portfolio from January onwards itself, so that is way back and thereafter recently what we have done is in July we have taken a price hike which is close to around 0.8% to 1% of the pricing, some of it mitigate costs, some of it goes towards increasing dealer margin and some of it will come as a net increase in our ASP.

Ronak Sarda: When you say the two-wheeler motorcycle related ASP increase that is largely driven by the ABS-CBS price hike over the year because the product mix has been slightly inferior as well?

Sanjay Bhan: There was a price increase in the month of April as well, so that is kind of feeding into it.

Ronak Sarda: Thank you and all the best.

Moderator: Thank you very much. The next question is from the line of Sonal Gupta from UBS. Please go ahead.

Sonal Gupta: Good evening. Thanks for taking my question. Sir, I just wanted to understand on just putting two and two together the scooter market clearly has seen a much sharper decline at the same time from your comments like you said that you are seeing more postponement in rural than in urban and given the scooters are more index to urban, I just wanted to understand how are you reading the scooters slowdown really speaking? Is there some sort of major shift happening in the market or what you think is the factor driving a sharp slowdown in urban markets for scooters?

Sanjay Bhan: Well the jury is still out. We have been having this chat for a long time now Sonal. In fact this is probably third time or the fourth earnings call that we got this question on scooters moving back to motorcycles etc., but I think it will be a little premature to conclude or assume that is happening, but yes if you look at the past two years, the contribution of scooter has come down from 34% to roughly about 30%, 30.2% in this quarter, so that gives you some sense in terms of directionally but you know you must also factor in the kind of stock corrections that competition has done in their scooter volumes including us we have also done some corrections in our dispatch volumes, but that said there is a certain evidence, some of the markets where penetration of scooters was not very high, are not really adopting as quickly as one would have imagined or expected, but that is good news for us in any case because that is playing up to our strength in some sense motorcycles where we are extremely strong in, surely we have been there pretty much in scooters and we would obviously have a lot of headroom opportunity in terms of gaining market share and gaining penetration opportunities in some of these markets, but by and large I think motorcycle gaining at cost of scooters does seem like an initial trend. Early to conclude but there are some green shoots there.

Sonal Gupta: Right and just on the cost reduction, given the slowdown do we see that full AP ramp up happening, how much capacity are you adding and what is the plan there?

Niranjan Gupta: We will be commencing our production in AP within this fiscal which is FY2020. The exact production and calibration of that obviously will depend on what we need to supply to the market.

Sonal Gupta: So the phase I is what 6,00,000 units or how much?

Niranjan Gupta: Yes. The capacity would be thereabouts. It could go up to around that level or a little more.

Moderator: Ladies and gentlemen due to time constraints that was the last question. I would now hand the conference to the management for closing comments.

Umang Khurana: Thank you all for dialing in. Have a good rest of the day. Please feel free to call us should you have more questions as well. Bye-bye.

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