



“Hero MotoCorp Limited Q1 FY-15 Earnings
Conference Call”

August 05, 2014



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Moderator Ladies and gentlemen good day and welcome to the Hero MotoCorp Q1 FY15 Results Conference call hosted by Nirmal Bang Institutional Equities. As a reminder all participants' 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 entering '*then '0' on your Touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Rahul Arora from Nirmal Bang. Thank you and over to you, sir.

Rahul Arora Good afternoon ladies and gentlemen and thank you for joining on this call for Hero MotoCorp first quarter results. We have from the management Mr. Ravi Sud; Mr. Surender Chhabra and Mr. Srinivas to take us through the results. I would request them to make their opening comments following which we can open it up for the question and answers. Gentlemen, over to you.

Ravi Sud Thank you Rahul. Good afternoon everybody. We just sent the results to the stock exchange about 40 minutes back. I do not know whether all of you had a chance to glance through them but what I would like to do is to give some opening comments on the basic highlights of the results and then we will open it up for question and answers. I have with me Mr. Surender Chhabra; my colleague, from Finance and Mr. Srinivas – All India Sales Head and all three of us will answer the questions.

The main highlights of the results are as follows. In this quarter we have sold 1.715 million two wheelers which is the highest number ever. Similarly our turnover for the quarter has crossed Rs.7,000 crores with the highest ever we have crossed the turnover of Rs. 7,036 crores. In terms of volume growth there has been a growth of 10% compared to the corresponding quarter and in terms of the turnover the turnover has gone up by 14%. As far as EBITDA is concerned EBITDA for the quarter is Rs. 947 crores versus Rs. 915 crores of the corresponding quarter and the profit after tax is Rs. 563 crores versus Rs. 548 crores of the corresponding quarter.

Before I jump to the question and answer there are few highlights which I want to give you once again. Number one, there are four or five factors which have gone either positive or negative during the quarter and I will just like to elaborate them. Number one, all of you know when the excise duty was reduced from 17th February, 2014 from 12% to 8% the anomaly of input excise duty continued at 12% and 10% continued and which still continues even after the budget. Since we produce 40% of our output from our Haridwar plant which is in a tax free zone where there is no excise duty on the output but since the inputs are coming at elevated excise duty there is an additional cost which has come in this quarter for full quarter and the impact of that is about Rs. 94 crores.

Number two is as far as the depreciation is concerned as per schedule 2 the depreciation rates on plant and machinery have been revised and there is an annualized impact of about Rs. 70 crores which will come in the P&L in the current year based on our estimation of capitalization

but the impact for the quarter is about Rs. 15.5 crores. Number three, we book close to Rs. 500 crores of investment income where traditionally our tax rates has varied between 9% to 13% year-on-year but because of the change in definition of long term from 12 months to 36 months and about 50% of our income which gets booked as long term as per the earlier norm will get taxed at higher rate and we expect that our additional tax of anything between Rs. 40 crores to Rs. 50 crores this year.

One positive is that there is an investment allowance of 15% which will be available for all capitalization of P&M which we will do during year. This year we are going to capitalize our Neemrana plant. Actually that has been already capitalized in June and also our global power center. Both could be close to Rs. 800 crores of which 15% extra investment allowance which will work out to about Rs. 122 crores and give us a tax shelter. So these are some of the basic highlights and I think with this we are ready for question answers.

Moderator Thank you. Ladies and gentlemen, we will now begin with the question and answer session. We have the first question from the line of Akshay Saxena from Credit Suisse. Please go ahead.

Jatin This is Jatin. My question is on the excise duty part you mentioned that there is a Rs. 94 crores impact; is this after the price hike that you took and I think you also took a Rs. 200, Rs. 300 price hike towards the end of the previous quarter? So does this account for that or that is separate?

Ravi Sud This is excise duty impact at Haridwar as I said earlier in my opening remarks all inputs to Haridwar plant come at 12% and some engine parts come at 10%. And which becomes the cost because there is no Cenvat available. But as far as excise duty on the final products in other plants is concerned that were reduced from 12 to 8 so which means in order to keep the parity of the prices we had to reduce the prices in line with Gurgaon and Dharuhera plant products. So what has happened is that final price has come down but your input cost has remained at the old level. That impact for bike is about Rs. 1,340 for Haridwar. And you know we produced about 40% of our production from Haridwar so the impact is Rs. 94 crores in quarter.

Jatin But in your final P&L accounts some of it would have been offset by the price hike that you also took, right? So the net impact would have been lesser is that the right way to look at it?

Surendra Chhabra This price hikes of Rs. 200 which period?

Jatin I was talking about the price hike that you took in March?

Surendra Chhabra That was not relating to the excise duty correction That will be independent of excise duty correction because time-to-time whatever price hikes we have taken that was only because of the diesel hikes or other expense increases only.

Jatin So you have not passed this on at all?

- Surendra Chhabra** No, this 4% is the straight hit on our Haridwar plant and that is why you are seeing last if we compare with the previous quarter March quarter where EBITDA margin was 13.76% and this time it is 13.54% while 3% to 7% down only and March quarter because excise duty affect was only for 40 days and this time it is for 90 days. And if you work out based on that you will see the other figures which is coming up is correctly reflected by us.
- Jatin** And in terms of the average realization that also is broadly flattish quarter-on-quarter whereas when we look at the mix it seems to have improved a little bit for you and as you pointed out there was also a price hike that was taken at the end of the quarter. So is this also realization because this is our net realization so the duty impact should not be there. What is the reason for this?
- Ravi Sud** When you are saying Rs. 200 or net realization increase in the overall revenues because last quarter the average realization was 40,600 and now it is about 40,800. So that whatever price increase of Rs.300 we had taken in March, the impact has reflected in realizations.
- Moderator** Thank you. The next question is from the line of Abhijeet Dey from BNP Paribas Mutual Fund. Please go ahead.
- Abhijeet Dey** Just wanted to know the increase in other expenditure on a YOY basis is about 25%. What would account for that?
- Ravi Sud** Well, there are four/five major items which have contributed to this. As Mr. Chhabra earlier stated in other instances one of the major cost is your packing forwarding expenses which has gone up from Rs. 170 crores to Rs. 210 crores. This can be bifurcated in to two parts; one is the volume impact which is about Rs. 18 crores and about Rs. 16 crores is on account of the diesel price hikes. And second is the royalty which we continue to pay to Honda on License-B models which are basically three now and which is related to the numbers and this in the last quarter I mean in June 2013 quarter it was about Rs. 25 crores because of the increase in volumes which has gone up to about Rs. 38 crores.
- Number three, generally ad spent of the company is pegged at about 2% to 2.15% and that you can check from last many, many years except may be one odd years where it would have crossed 2.25% because of certain major events. But this year because of launch of the new models like iSmart and other models, the ad spent in the first quarter is higher than in the previous year's first quarter and there is an increase of about Rs. 25 crores in the first quarter but overall ad spent for the full years will remain within 2% and between 2% to 2.1%. But these are major three items reason of their which are in the major items in other expenses.
- Abhijeet Dey** Sir, the Haridwar our impact which you just explained on excise duty it was also there in the fourth quarter results that is the March quarter results?

- Ravi Sud** Yes, as Mr. Chhabra said this was there because the budget came on 17th of February so it was there for about 40 days. And this time it is there for full quarter. Now and we are comparing June 2013 to June 2014 if we are talking of the corresponding quarter in June 2013 it was not there at all.
- Abhijeet Dey** And in terms of raw material price trends what you are seeing right now, sir?
- Ravi Sud** As far as the price trends is concerned we have not seen any major jump in the commodities. It is only that rupee-dollar which is at 60/62 levels. Diesel hike which is having a cascading effect on the prices. There is no major jump in the raw material cost.
- Moderator** Thank you. The next question is from the line of Sonal Gupta from UBS Securities. Please go ahead.
- Sonal Gupta** One just to so ex of the Haridwar effect we have not seen any impact in raw material costs, right?
- Surender Chhabra** No.
- Sonal Gupta** And sir, there is a jump in terms of the staff cost will that be a normal increase is that how we should look at it?
- Surender Chhabra** As far as the staff cost is concerned there are certain onetime expenditures which comes in the beginning of the year and falls in the subsequent quarter so that is why marginal increase is there. But in the coming quarters I think you can see the average will come up.
- Ravi Sud** To be more specific, the variable part of the salary which we create provision every quarter based on the previous year's actual. This year the variable pay was slightly higher levels and is a one time increase which has come in quarter one. Otherwise it will quarter two, quarter three, quarter four and for the full year you may not see any significant change in the overall percentage of manpower cost to the net revenue.
- Sonal Gupta** Okay so is this sort of a run rate that we can take going forward or you expect it to be lower?
- Ravi Sud** But Sonal, on the other hand if you compare the total expenditure excluding raw material as compared to the previous quarters it is lower in terms of percentage. But I think the raw material cost last quarter March quarter was 18.77% and this quarter it is only 18.14%. So my overall expenditure is lower than the previous quarter but not from the corresponding quarter. And I think you must keep in mind that there are certain items of expense which are related to the period. Like there could be a certain events which is related to this quarter like I can tell you that football world cup that happened in basically in the month of June. So part of the expenditure would have come here which only a onetime cost this has come here.

Sonal Gupta And just last question I had was in terms of demand outlook how are you seeing the demand and how has been the rural demand that really speaking and how are you expecting that and just what is your inventory level at the end of the quarter?

A. Srinivasu Srinivas here National Sales Head.

Ravi Sud Sonal, you are meeting Srinivasu, he is the National Sales Head.

A. Srinivasu The demand is pretty robust Sonal the monsoons are reasonably good across the country excepting a few places where there is some level of deficit. So we do not find a major issue as far as the rural demand is concerned may be in these small pockets there might be a little bit of concerned that the monsoon is not over as yet. We need to see how it pans out. Otherwise we are looking at a double digit growth in the quarter two.

Sonal Gupta And sir, in terms of inventory levels where are you after?

Ravi Sud It is about four weeks inventory and we do not there will be a build up for the festive season in the quarter July to September because the festivity starts from 25th of September and runs across October. So there might be some level of build up in the month of September but otherwise we do not see any major concern as such on inventory.

Moderator Thank you. The next question is from the line of Sahil Kedia from Barclays. Please go ahead.

Sahil Kedia I had two questions. One, can you give us some sense on how demand is actually shaping up in your view and secondly can you also give us an update on the entire cost reduction measures that we have spoken about earlier please?

A.Srinivasu I am Srinivas here. Let me answer the first part of the question which is how the demand shaping up. See primarily the first half of last year was little bit lower in terms of base effects for the entire industry so we do expect the demand in the first half to be little higher than the second half and reasonably there are certain parameters in terms of the overall sentiments, good strong replacement demand, with reducing product lifecycle which will keep the growth story intact till for 3 – 5 years. That is how the demand is shaping up going forward you will find the demand little higher in quarter two because of the shift in festive seasons.

Generally, Q1 is low and Q2/Q3 spend is higher due to festival season. However, this year Q1 is slightly higher compared to previous year due to launch of new models. However, we would be able to cap it between 2 to 2.1%.

Last year you had the festivity in October and November this year it is going to be September, October. So there will be little bit of a shift and the growth will be little stronger in the second quarter across the industry and might moderate a little bit in quarter three and then quarter four should be a normal quarter. So it will expect to good demand keeping the basic growth driver in lined.

Ravi Sud Well, coming to the second part of your question yes, our program of first the margin transformation is in full swing. In the last earning call I had mentioned that our run rate was Rs. 25 crores a month and I can share with you that during the quarter the total accumulation to the bottom-line is about Rs. 97 crores which means already Rs. 32 crores a month and going forward we believe that it should touch about Rs. 50 crores a month by quarter four.

Sahil Kedia And sir, this is primarily coming on lower or more efficient sourcing and so I am just trying to understand where should we start to see this in your numbers?

Ravi Sud Well, since your question is very specific so I will answer it very specific. You see during the quarter there is a accretion of Rs. 97 crores out of which Rs. 66 crores has gone in terms of cost increases to vendors basically on power and fuel and conversion cost. So Rs. 66 crores has gone here so which means the net accretion in the quarter is about Rs. 28 crores to Rs. 29 crores.

Sahil Kedia And normally this should be visible in the raw material cost is that correct?

Ravi Sud Well, not necessarily because what I had explained earlier and I am repeating once again that this is a program which is not only a cost reduction in your sourcing. This is a program which cuts across all functions including feature optimization; including raw material consolidation; e-sourcing; designing; looking at alternate sources; global sourcing, operational expenditure etc. etc. So what we do is we are monitoring all the ideas very scientifically and that is why I am able to give you the figure of Rs. 97 crores accruals during the quarters.

Now other thing may interest you that in the FY14 the total accretion was about Rs.169 crores and we already have implemented which worth Rs. 445 crores annualized savings. So as we keep on increasing this figure of Rs. 447 crores to may be Rs. 500 crores, Rs. 600 crores, Rs.700 crores the accretion will keep on going up.

Sahil Kedia Sir, one housekeeping question. Can you just share what was the payment to Honda that we have amortized in the quarter?

Ravi Sud You know this is in the range of Rs. 190 crores to Rs. 200 crores.

Sahil Kedia Is it possible to give a specific figure sir for the quarter?

Ravi Sud Rs. 201 crores.

Moderator Thank you. The next question is from the line of Govind Chellappa from Jefferies. Please go ahead.

Govind Chellappa I had couple of questions. One, can you tell us a bit about what is happening in the scooter market the gap between you and Honda is expanding again; Honda seems to be doing much better you are. So is that a capacity issue; is that a regional growth issue if you could just

elaborate on that? And my second question is and I have asked this question many times before. I mean what exactly is your dividend policy?

A. Srinivasu

I am Srinivas here. Let me take the first question which is on the scooters. Yes, see Honda basically as the first mover advantage in the scooter market and that is why the volumes are relatively higher. Having said that we have had a decent growth while we have had some capacity gap which I think by the month of September we should be able to catch up in terms of capacity and also the new model launches which are pending would come in because Pleasure New was launched we have a new campaign on air that should give us some adequate numbers and put us in a reasonably good growth pattern. Yes, on scooters may be you are right the gap between us and Honda is little bit wider in the first quarter but I think going forward in the second quarter we would that cap or the market share gap would reduce going forward in the second quarter.

But having said that the overall two wheeler industry actually Honda has lost out in quarter one compared to quarter four and the gap between us and Honda on overall two wheeler is actually widened. They have gone down 2%; we have gone up 2%. So it is a 4% gap in terms of market share. The overall two wheelers this scenario has pretty positive for us. The scooters yes, it is positive for them.

Coming to the second question and since you said you have asked this question many times I will also say I have answered this question many times so I will answer this question once again.

Ravi Sud

Govind, how many shares you have first tell us?

Govind Chellappa

I am very happy that you are paying this dividend just that you always surprise us so I am trying to understand how we cannot be surprised the next time.

Ravi Sud

Let me tell you I can tell you how this dividend policy has evolved over a period of time in this company. If you look at up to 2007-2008 the policy used to be anything between 30% to 40%. 2008 to 2012 policy has been anything between 35% to 50% there have been exceptions. In 2010 and 2011, we had the two special dividends if you exclude that our dividend will fall within 35% to 50%. Between 2013 and 2014 the board has taken a conscious call to increase the dividend payout to between 60% to 70%. And if you look at FY13 it was 66% if I remember. FY14 it was I think 71%.

Govind Chellappa

So that is broadly the number we should be looking at?

Ravi Sud

Well, now see that is I will say a few words of caution because dividend payout will also depend on what the company requirement of funds in the immediate future are how the market is and what type of growth which you expect and what is the type of money if the company needs to keep at any point in time in the company particularly more so for your CAPEX

requirement. So a policy of anything between 50% to 60% will be a prudent policy for you to consider at this point of time. And if there is a surprise that is a bonus.

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

Amin Pirani Sir, just going back to the Haridwar impact on excise duty so would it be fair to say that the impact would have been almost half of Rs. 94 crores in the last quarter?

Ravi Sud Last quarter it was Rs. 32 crores.

Amin Pirani And going forward will this remain to be continued to be an issue or is that resolved now?

Ravi Sud Yes, it will continue to be an issue till the time this anomaly of input and output excise duty is rectified by the government.

Amin Pirani So on a like-to-like basis there would not be any change even next quarter?

Ravi Sud Yes, depending on the numbers we sell from Haridwar, it will continue.

Amin Pirani Of course and if you produce more from Haridwar then it is a bigger problem I guess? And sir, just on the cost savings initiative that you were talking about so sir, this year I think you will have a gain of something like Rs. 400 crores to Rs. 450 crores given the run rate where you are going. But what could be the net accretion for the year if you could give some estimate?

Ravi Sud This is something which I have explained many times and I do not hesitate in explaining it many times. This is an initiative and I always say other things remaining constant, this program has added Rs. 169 crores in FY14 but if your raw material prices go up or your conversion cost goes up or if your diesel prices go up or your transportation is rates go up, then this accrual gets offset. But only thing I can repeat once again is that this is a program and which is running very, very successfully and it is not a short term program we have started it in May 2013 and it will continue for another one year after that it will become part of our life.

Amin Pirani Sir, just to clarify the Rs. 169 crores of Fiscal 14 was the net accretion or was that the gross?

Ravi Sud No, I am saying gross accretion from this program.

Amin Pirani And sir, just lastly have you taken any price increases post March?

Ravi Sud No.

Moderator Thank you. The next question is from the line of Kapil Singh from Nomura. Please go ahead.

- Kapil Singh** Sir, firstly on the investments that we have made if you can throw some light as to what is the investment vision for the full year and whether we can expect some earnings to accrue from Hero Fincorp this year?
- Ravi Sud** If you look at our total investment portfolio the major investment is in Fincorp because last year there was rights issue and once again this year there was a rights issue in the month of June and our stake in the company has now gone up to 48%. Now if you are looking at immediate returns I think the business of Fincorp is in the stage of growth and I can tell you that it is growing very, very fast. Just to share with you some numbers, in the month of June the company touched that magic figure of 10,000 two wheelers and in the month of July, they are at around 12,000. So it is on its growth path.
- And the book size as on March was about 1,100 crores and it is expected that a book size by the end of FY15 should be close to 2,300 crores to 2,400 crores. So my own assessment is that for next couple of years the company will need more and more capital to increase the size of the book. So as far as returns in terms of dividends are concerned the company had declared Rs. 3 dividend even in FY14 but the company will need lot of capital to be preserved for further growth. But in terms of value, if one has to take a perspective of four to five years definitely there is going to be a value for HMC.
- Kapil Singh** And sir, what is the total investment envisioned for this year in Hero Fincorp?
- Ravi Sud** No, whatever investment had to be done now because there was a rights issue we subscribed to the rights issue and we have disclosed in the published figures.
- Surender Chhabra** Kapil you will see that there is a note there that how much investment have been made this year.
- Kapil Singh** So this is the final amount for this year?
- Surender Chhabra** Yes.
- Kapil Singh** And secondly also wanted to check on the tax rate can we assume this around 26.5% of the full year tax rate?
- Surender Chhabra** Kapil, at this point of time it is 26.48% and what Mr. Sud has told you in the beginning that there are certain positive elements and there are certain negative elements in that Finance Bill 2014. Positive is that 32 AC that investment long benefit which is given by the government after a long time again which I think has been on our Neemrana plant on the plant and machinery. The negative effect is on that investments which from fixed income plans which are I think in the Debt Schemes has been considered long term after 36 months not 12 months. So keeping in mind the adjustment of these two because bill is yet to be passed by the president, but we have to take the impact of that Bill, the effective tax rate is 26.48% and more or less I can say will remain same throughout the year.

Kapil Singh And sir, just one final more conceptual question on this excise duty thing. Sir, why is the impact not there for the other plants because the excise duty on imports would be paid at 12% at other plants as well, right so that works out to be slightly higher than?

Ravi Sud Hold on I will explain. You see Haridwar is the only plant where there is no excise duty on the final product. Let us go to now Gurgaon or Dharuhera or Neemrana plant you know you pay Excise at 12% on input but you pay excise duty at 8% on the final product. So which means logically even if the excise duty is at 12% on the inputs, which is about 70% of total price, can be offset against the ED on the final products. However, in case of Haridwar since there is no excise duty on the output, so the elevated ED on inputs becomes cost. However, there could be cases where there is a possibility of accumulation of Cenvat even in Excise Duty Paying Plants because of Service Tax credits on lower value addition.

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

Jamshed Dadabhoy Could you comment a bit in terms of what is going on in the market because this quarter at least we have seen very strong growth in scooters; very strong growth in the 110 to 125 CC segment and in the higher segments but basically in the entry level scooters you have seen only 3.5% to 4% growth. So the bulk of the market we have not seen much growth but very high growth in scooters and in the more premium segments. So could you just explain why this ballooning of growth is happening?

A. Srinivasu Hi, I am Srinivas here. Let me try and take your questions one-by-one. In terms of the overall growth in scooters, you are right it is substantially higher it is almost at about this has gone to 29% and that is largely on account of some new product launches. Coming in you had Yamaha launching Alba you had also Honda launching Activa 125 which probably was actually came in Quarter 1 and then you also had Jupiter which is doing very well. So these three new products have added some numbers in to the overall kitty plus other players also even the basic Activa after the LCD technology our own new Pleasure, so all of them are doing well.

So basically in certain markets there has been a stark shift towards scooter market especially in the Southern and Western market and within these Southern and Western markets certain places like for example Kerala is already hitting (+50%) in terms of scooter volumes and then you have Goa clocking 75% but there are certain pockets where motorcycles are still very, very strong. So that is one reason why you are seeing the scooter volume higher and second most important reason also from why probably Honda which was the largest player in scooter is doing well in quarter one the number went up is it is also the base effect.

See Honda opened up the Bengaluru plant in the month of August meaning it opened in the last week of July the supply had started from August. So they did have a waiting when they actually opened up the quarter so for last year first quarter they were on waiting and that is one reason why the base effect has caught up this year and you are seeing in terms of the percentage

growth we are seeing a big shift in terms of growth pattern. But otherwise I think overall if you look at it if you minus the base effect then you will see it moderating going forward in terms of the overall numbers.

So is the case with the TVS where the base effect is very, very low you can check the quarter one figures of TVS in last year on scooter so this time we are doing well with the Jupiter product and so these are some of the reasons why we are seeing a big growth figure on scooters. The base effect actually remembered. So yes, what is your second question?

Jamshed Dadabhoy

Sir, why is the 125cc 100cc segment why all those segments doing far better than the plain Vanilla 75cc to 110cc segment?

A. Srinivas

Yes, so it is like honestly a customer does not look at cc he looks at products and brands so we classify it from industry and SIAM as cc but having said that see the traction between why a 125cc is doing well or a premium segment is doing well is largely on account of replacement demand. There is a huge chunk of bikes available in the market and it comes up for replacement on a period basis. So we are seeing in the last one year that the life cycle of the product which is the ownership cycle to be rightly put across is reducing from 5 to 6 years to about 3 to 4 years now.

So that is the reason why people are changing bikes more frequently than what they used to do earlier. So this replacement demand is actually triggering the sale of your 125cc and your premium segment and even as you rightly said the non-Vanilla products. The Vanilla products is largely the entry segment buyers who comes in first time buyers as we call them but it is not that even in the entry segment the hardcore entries growing at about 5% but otherwise certain brands in that are doing very well even within that.

Jamshed Dadabhoy

So just following up on the comment on scooters that South is doing very well and Kerala has (+50%) could you give some sense in terms of what the penetration for scooters is in three states basically UP, Bihar, MP and why is that penetration so much lower than the overall country average? Is it just due to a combination of infrastructure and income levels or is there something more to it?

A. Srinivas

Yes, by-and-large the overall two wheeler penetration in the Northern markets have been denoted by as they call it they are Rajasthan, Madhya Pradesh it is only about 11% to 12% whereas you actually look at the Southern markets or the developed markets like Gujarat or Maharashtra or Tamil Nadu the penetration level is close to 30% in terms of our growth. Now scooters has been an old phenomena for us but after the 85-90 after going away it is making a comeback basically because of the various demographic changes that is happening not only in terms of infrastructure in terms of more women riders coming and more nuclear families.

So it is more on demographics and lifestyle patterns is one reason why people do not feel uncomfortable riding a scooter so it is coming back. But then is happening only in a few

centers. Certain centers again the change of demographic is not so stark like typically you take Bihar for example or you take MP; MP certain pockets are doing well but by-and-large if you take UP at some pockets they are still very conservative in terms of what they have and they are very keen that what they drive on is a motorcycle basically because it gives them a macho feel. With this rate of shift while if you look at the overall shift in scooters it is moved out from 23% to 26% in quarter one and it has gained 3% in terms of structure and motorcycles have moved down from 72% to 70% and mopeds they have lost 1%. So it is not a radical shift as such. It is just in some markets it is doing well otherwise the shift is only about 3% towards scooter.

- Jamshed Dadabhoy** Right, I guess my question is that do you expect these three states not just move from say 11%, 12% scooter penetration to about 20%, 25% any time and say the next two to three years because that will be a big delta as far as scooter demand goes because these three states I am guessing will be about 25% to 30% of overall motorcycle demand at this point in time?
- A.Srinivasu** You are talking about the states of MP, Bihar?
- Jamshed Dadabhoy** MP, Bihar, UP?
- A.Srinivasu** See the largest states if you look at it yes, UP I do not see it shifting to 20% may be around 13%, 14% and in Bihar definitely north to 20% may be in MP there might be a shift it might go closer to 20% but in UP and Bihar it will take some time.
- Moderator** Thank you. The next question is from the line of Sudhir Kedia from ASK Investments. Please go ahead.
- Sudhir Kedia** Sir, I wanted to check with this Haridwar excise duty thing. Sir, can you explain to me that what part of your input are based in Haridwar to that extent this excise duty anomaly will not hit you?
- Surendra Chhabra** Let me explain to you. So all parts have to go to Haridwar and they go with a duty of 12% or 10%. So I am repeating unless this can normally be rectified by the government like the output excise duty is 8% so is the import excise duty this impact will continue. Because there is no set off on the input excise duty in Haridwar because there is no excise duty on the final product. So whatever is the duty on the input that becomes your cost. In other plants this input excise duty can be set off against the duty on the final product.
- Sudhir Kedia** So I mean to say that none of your ancillary parts are based in Haridwar and all are coming outside Haridwar in which you have?
- Ravi Sud** No, yes we have some ancillaries but the point is that is why I specify the amount very, very clearly that this amount is about Rs. 1340 net which is the impact of the input which are coming from outside Haridwar.

- Surendra Chhabra** Let me add on because this raw material which are bought by these ancillaries are coming from outside the state and that ancillaries spending 12% excise duty on that which is not our input credit for anyone that is the cost for them. So which is built up in that raw material cost itself because the State of Uttarakhand does not have much of its own resource.
- Moderator** Thank you. The next question is from the line of Jay Kale from CIMB Securities. Please go ahead.
- Pramod Amte** Since you are paid off your last leg of the royalty does it provide any incremental flexibility for you in terms of pricing of the products or in terms of the new launches which you can make in to the market place?
- Ravi Sud** Every quarter Rs. 200 crores gets eliminated so that is the additional money which is available to the company and I think company will use it very, very judiciously whether to launch new products or ad spend it on educating customers or to spend on brand building. I think all those options are available. But the matter of fact is that Rs. 200 crores of expense have gone out of companies P&L account effective 1st July.
- Pramod Amte** So other than this the royalty payment are there any beneficial terms or operational flexibility you get now?
- Ravi Sud** Are you talking in the context of Honda?
- Pramod Amte** Yes in your operations in the sense would you be flexible to launch a new scooters much easily with a much flexible cost structure?
- Ravi Sud** Well Pramod, I think this is an old discussion which we had many times. To develop the two wheeler or to develop a new product takes time. If it is 30 months or 36 months it will take 30 to 36 months whereas we added this flexibility when we were paying this royalty to Honda even in the last 3 years. I think we have refreshed all our models; we have launched many variants; we have launched iSmart and we are also launching some new scooters and also new platforms. This is irrespective of whether you had to pay this payment to Honda or not.
- Pramod Amte** Sir, the reason why I was asking was there will be some efforts or your new product line up seems to be very impressive in the coming months or coming quarters; one. And second, I hear that you are making some rebranding efforts also on the spare side if I am not wrong. So is it just a long term plan or is it coinciding with the royalty going out? That is the question.
- Ravi Sud** If that is your question answer is very simple. I do not think we are waiting for the royalty to be over I mean there have been initiatives which we have taken even when the royalty were being paid and like even if you go back when we were partnering with Honda our ad spent used to be 2% to 2.15% even after separation we have not reduced it rather we have tried to rationalize it and try to build our brand very, very strongly.

- Pramod Amte** And sir, can you give some more clarity in terms of your new product plans with some timeline for the coming quarter and also what type of changes you are trying to bring to the market place with these new products?
- A. Srinivasu** Yes Pramod, I think you have seen in that Auto Expo we have showcased our new products which are coming up in the coming years. I think that will be launched at the right time and these are in the pipelines.
- Moderator** Thank you. The next question is from the line of Hitesh Goel from Kotak Securities. Please go ahead.
- Hitesh Goel** Sir, the royalty amount that you have given Rs. 201 crores this is the total royalty paid to Honda including the new products or this is only the payment that is going out the one time lump-sum payment is going out?
- Ravi Sud** You see there were two types of payments to Honda. One was the lump-sum payment of 45 Billion Japanese Yen which we amortized over 14 quarters and last quarter being the quarter ending June 2014. So that was one part. So this Rs. 201 crores is relating to the part of that lump-sum payment, which was agreed at the time of signing the agreement. Second is License-B. That is relating to four new products out of which three are in production. These are Maestro scooter, Passion Xpro and Ignitor and is relating to the volume.
- Pramod Amte** Okay so this is not the total amount there is some other small amount as well which is basically pertaining to the new products as well?
- Ravi Sud** Yes.
- Pramod Amte** Sir, can you broadly give that number total royalty amount if it is possible?
- Ravi Sud** You can say there is Rs. 201 crores plus another Rs. 40 crores for Licence-B in the quarter.
- Surendra Chhabra** That is in revenue element; expenditure and this is a part of definition to have a different treatment, yes.
- Pramod Amte** Yes I understand that but Rs. 40 crores plus the Rs. 201 crores in the quarter.
- Ravi Sud** You know Rs. 40 crores will be the regular for two-wheelers depending upon volumes and Rs.201 is the last installment.
- Moderator** Thank you. Ladies and gentlemen, we will now close the question queue and take the last question from the line of Amrish Mishra from JM Financials. Please go ahead.
- Amrish Mishra** Just one view that I wanted to have from you guys. We have seen almost everybody really looking at massive capacity expansions. So just wanted to get a sense on how we are looking at

our capacity over let us say next two, two-and-half years though broadly some of these capacities we are already aware just to get a sum up and how do you see the capacity by most of the players coming in to play over next two, three years impacting the pricing environment if at all you think it could?

Ravi Sud

Well, let me first answer your question related to capacity. Before we commence production at Neemrana plant we had a capacity of 6.95 million and we have added another 750,000 with Neemrana where the production has started in the month of June and total capacity now is 7.65 million. As we have also acquired land in Gujarat near Halol and there the capacity of 1.8 million will come in two phases. So you can say 7.65 plus another 1.8 million capacity may be in next 3 years. So that will take us to 9.2 million and as far further capacity is concerned we are scouting for some suitable place for our sixth plant which could have a capacity of anything between 1.5 to 1.8 million. But that will happen sometime in FY17 or FY18 beginning. So that will take our capacity beyond to something like 11 million. Apart from this we have two joint ventures one in Columbia and another in Bangladesh. Now not very significant in capacity but I think if I add both of them it could be close to 450,000 capacity in the next 18 months or so. So as far as any growth in the market is concerned, we will have sufficient capacity. Now your next question is relating to is the capacity being created is it excess? Our assessment is if you look at last two years I think there have been aberration in the growth of two wheeler industries but looking at the current year's first quarter where the industry has grown by around 10% and we believe that the industry will contribute to growth more or less in double digits in next 3 to 5 years, I think building of this capacity is necessary to meet the emerging demand.

Amrish Mishra

Sir, one last what is your outlook and given that we are talking of some recovery even in the urban markets so what is your outlook on the premium motorcycle space over next two or three years especially 150 cc and higher?

A. Srinivasu

I am Srinivas here. See the outlook is quite bullish because we have just came up that the new Extreme and then we have about to launch the new Extreme Sports which we had displayed in Auto Expo and in the first quarter also launched Karizma R and then Karizma ZMR. Now all of these products I mean the Extreme Sports is not yet launched but the other products that we have launched has given us a good growth. In fact in quarter one we have grown almost like 42%. So the products are getting established in the market because it has been done over the first quarter starting from April onwards. So going forward in the next two, three years we have a good decent line up in our portfolio of new product lines. On the (+150cc) and some of the products were also showcased in the Auto Expo which probably definitely you would have seen this. So we do expect that these products would actually do well and we are quite bullish about the (+150cc) segment.

Amrish Mishra

And sir, do you think for the industry as a whole 150cc and higher motorcycles could outpace the growth in 100cc to 125cc is that something which you are looking at for the industry as a whole?

- A. Srinivasu** Yes, see in terms of pure growth rates in certain markets it might because the base is very low. So if probably in a market if it is selling something like 1,000 and close to 2,000 you will see a 100% jump in the overall numbers. But if you are asking me whether volume it will out beat it is a long way off because in India fundamentally biking is motorcycles are used for commuting and not for biking. So it will some time.
- Moderator** Thank you. Ladies and gentlemen, that was the last question. I would now like to hand the floor back to Mr. Rahul Arora for closing comments. Please go ahead.
- Rahul Arora** Just like to thank Mr. Sud, Mr. Chhabra and Mr. Srinivas for taking time out and walking us through the results. Thanks for all the participants for dialing in this afternoon. Thank you so much.
- Moderator** Thank you, gentlemen. Ladies and gentlemen, on behalf of Nirmal Bang Institutional Equities that concludes this conference call. Thank you for joining us and you may now disconnect your lines. Thank you.