

Automotive Market Outlook: FY14

An assessment based on industry views and macro data analysis



Prepared for:

An Indian automobile company

2013

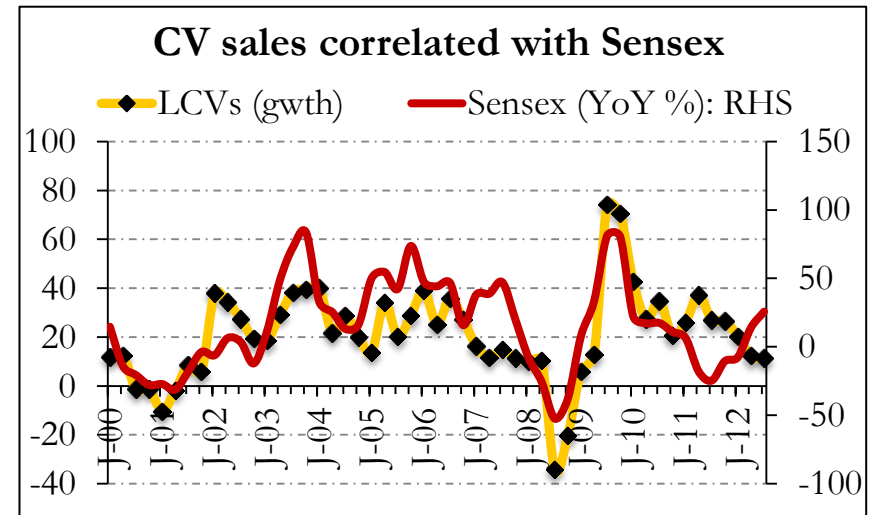
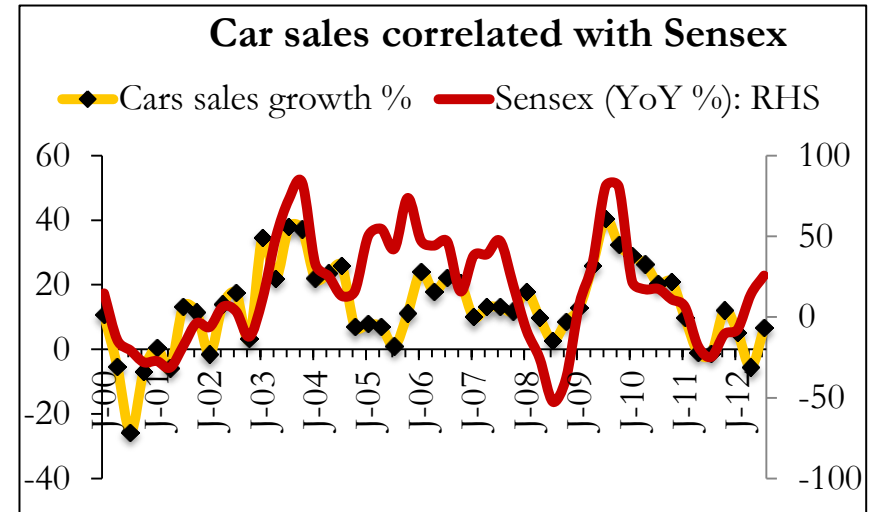
Automotive Market Drivers

Understanding macro relationships

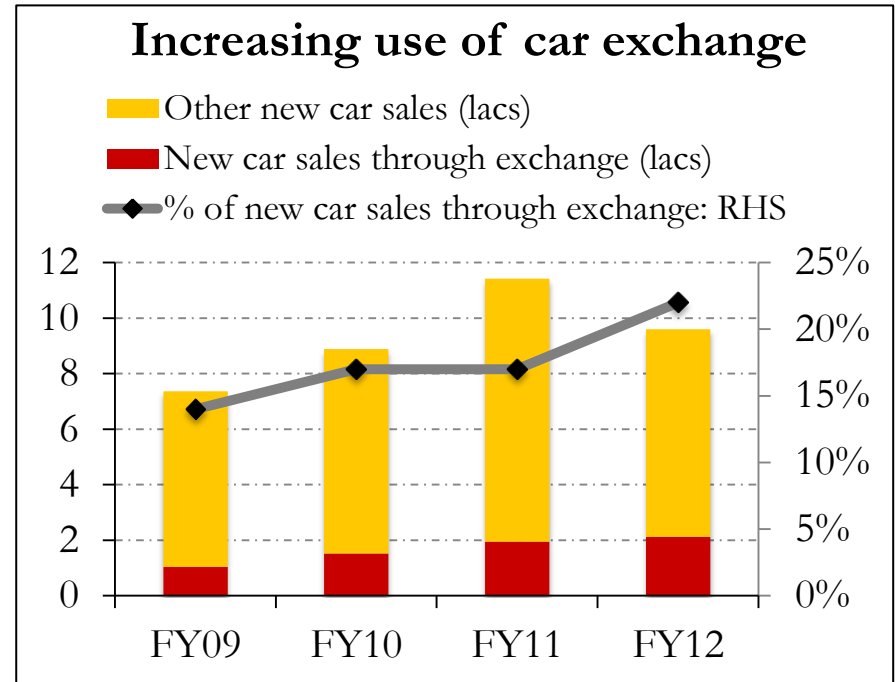
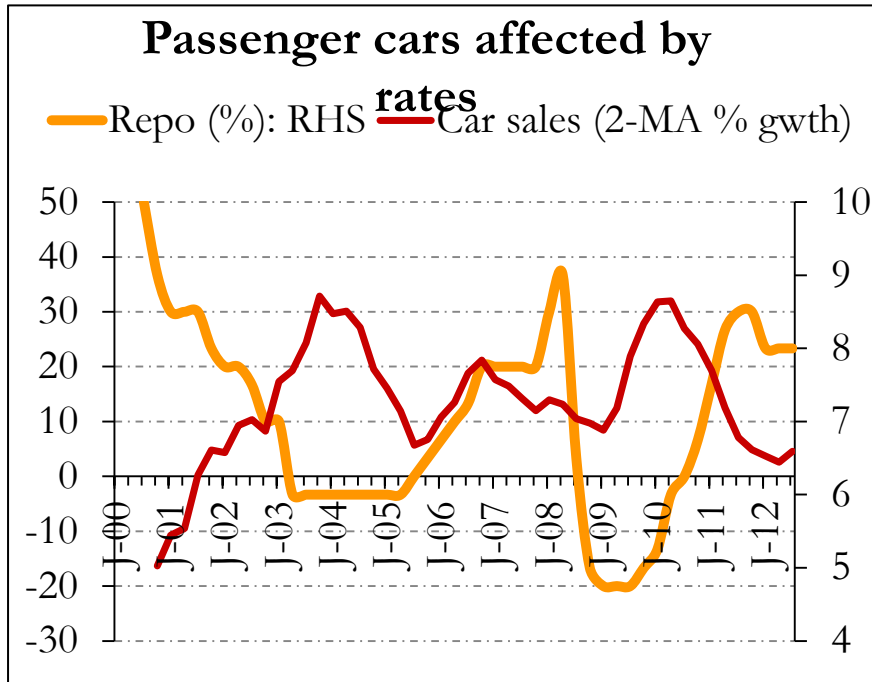


Capital markets drive car and LCV sales

- Passenger cars are driven by the ‘wealth effect’ – notional asset values – and tend to follow stock market movements
- LCVs also show high correlation with the Sensex (>0.6) – both follow vibrant corporate activity
- A strong stock market therefore, implies higher growth in these two segments
- Sensex outlook for FY14 suggests an increase to 22,000-22,500 levels by year end



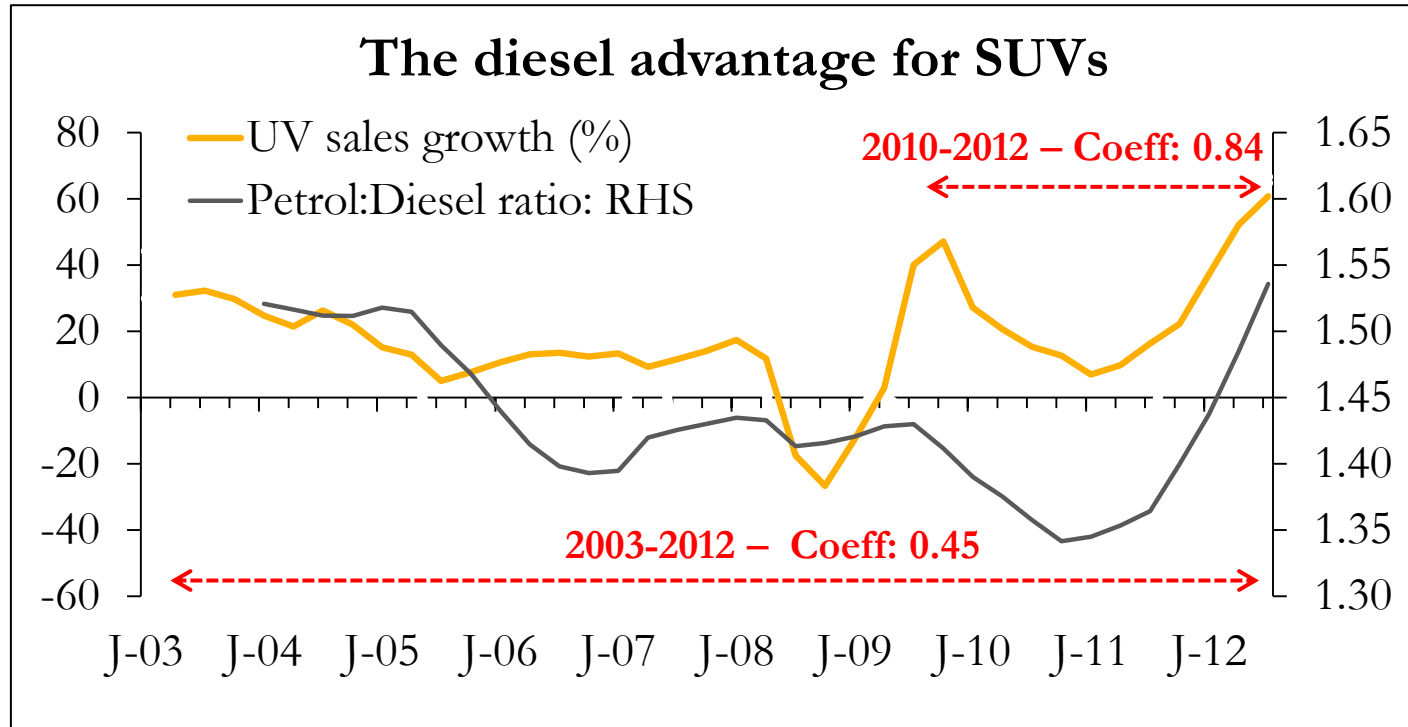
Recent trends: passenger cars



- Car sales significantly affected by rising interest rates as well as dropping consumer sentiment
- An increasing preference for purchasing new cars through old-car exchange – implying up-trading, not addition to HH car ownership

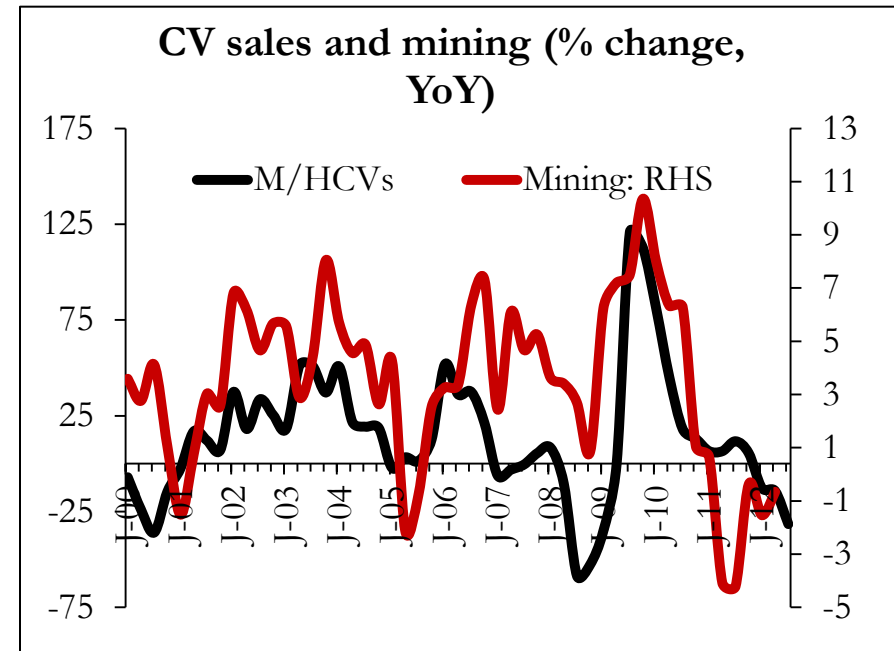
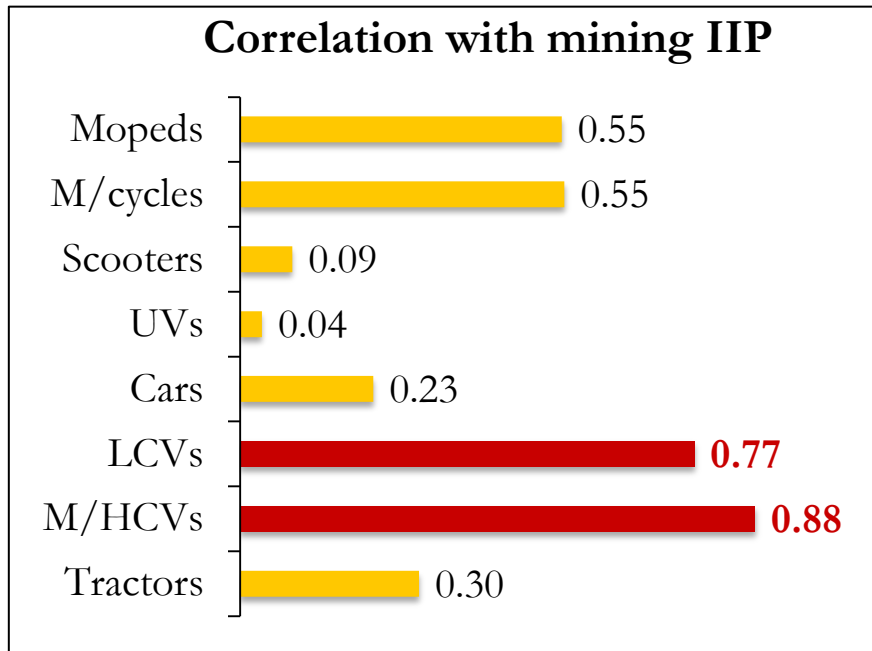
Source: SIAM; RBI; Maruti Suzuki Limited; IMA analysis. Car exchange data pertains to Maruti Suzuki's sales.

Recent trends: UVs



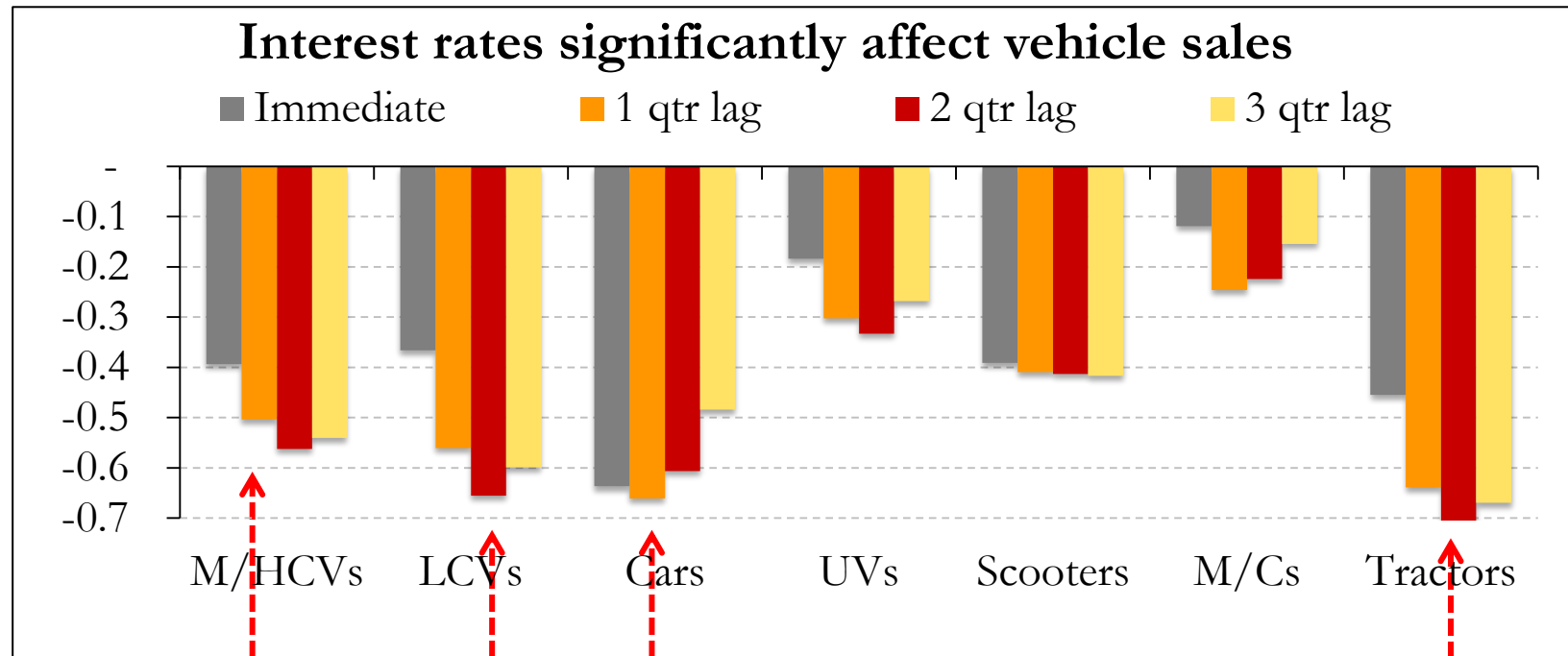
- Since the late 2000s, SUVs have benefitted from the widening petrol-diesel price differential and a slew of new, affordable model launches (correlation coefficient increased from 0.45 to 0.84 from 2003-2012 to 2010-2012)

CV sales are dependent on mining...



- Commercial vehicles exhibit high correlations with the mining sector (coefficients >0.8), reflecting their usage pattern
- Judicial suspensions have led to negative growth in mining, which has impacted CV sales – no immediate improvement likely

...and interest rates

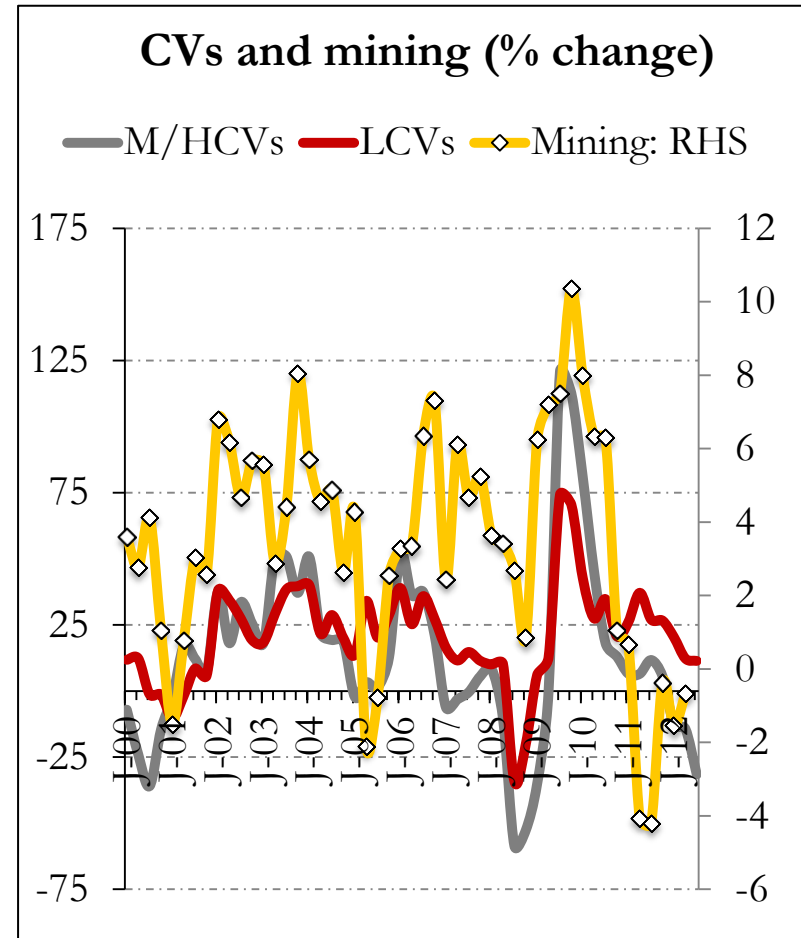


High inverse correlation

- Interest rate movements are significantly and inversely correlated with sales of PCs, CVs and mopeds – average coefficients of >0.6
- However, the impact is not immediate: 2-3 quarter lag in case of CVs and mopeds, and 1 quarter for cars

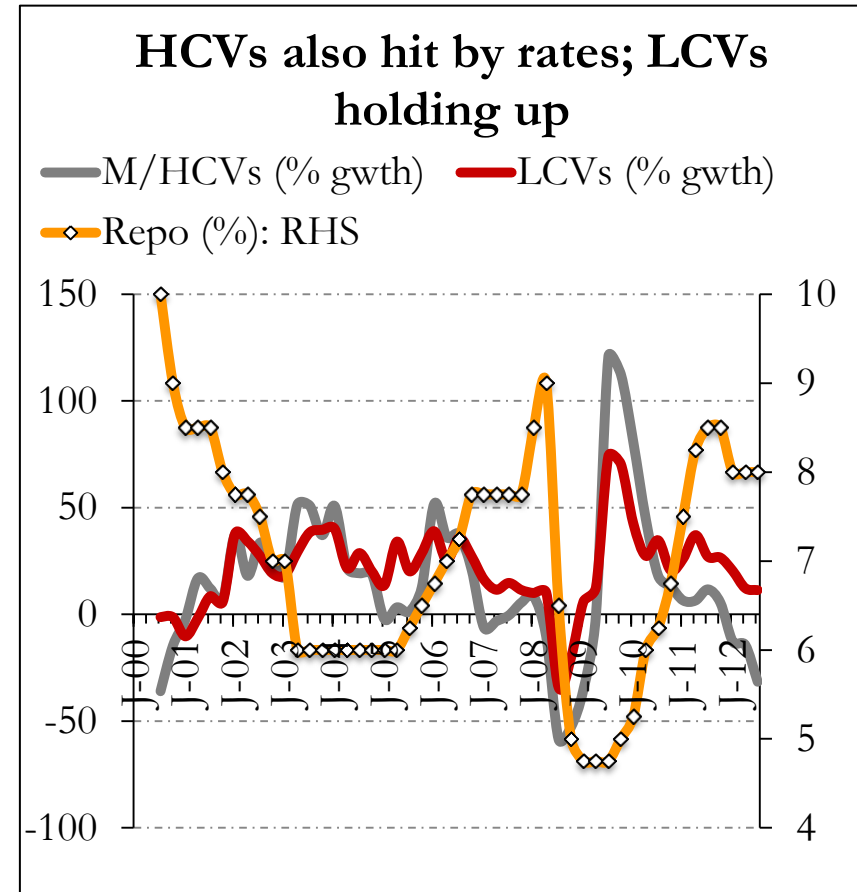
Recent trends: CVs

- MCVs/HCVs have been the worst affected in FY13 with growth turning negative from Q1; reasons include:
 - Restrictions on mineral mining in Karnataka, followed by Goa; large scale suspension of sand mining in North India and elsewhere
 - Slow down in construction and infrastructure projects across the board
- Truck rentals on trunk routes have dipped on account of dropping cargos



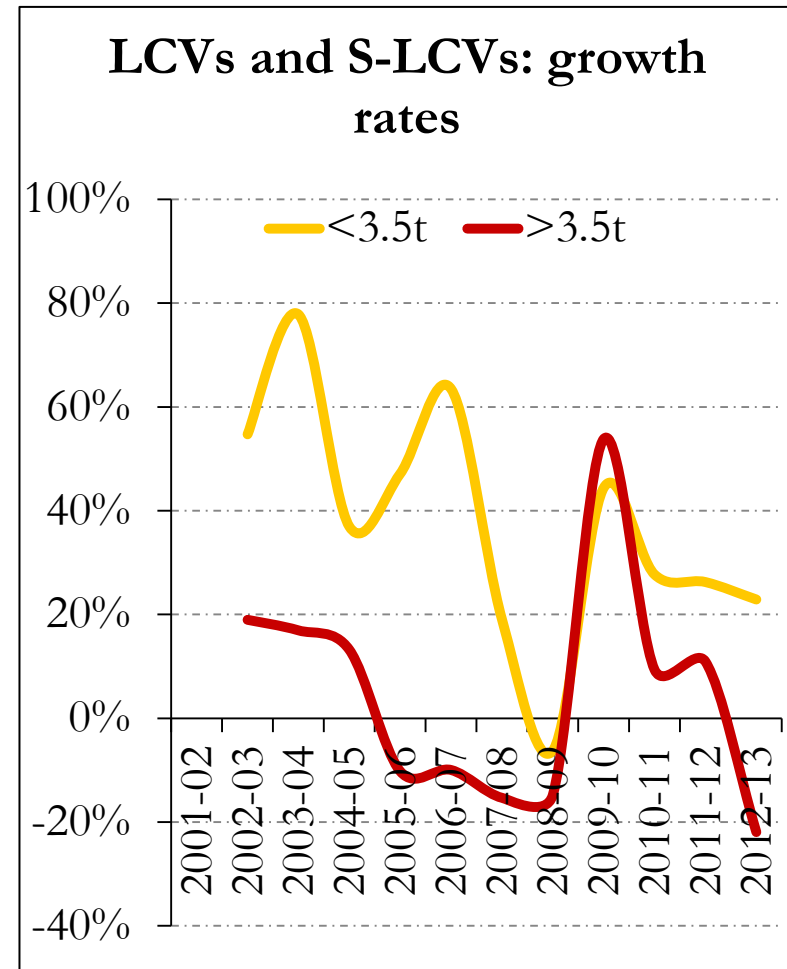
Recent trends: CVs... cont'd

- Higher interest rates have affected all segments of CVs
- LCV growth rates have fallen from the ~30% rates of FY11 and FY12 due to lower GDP and manufacturing sector growth
- Prices of second hand CVs have declined by 15-20%, indicating weak demand



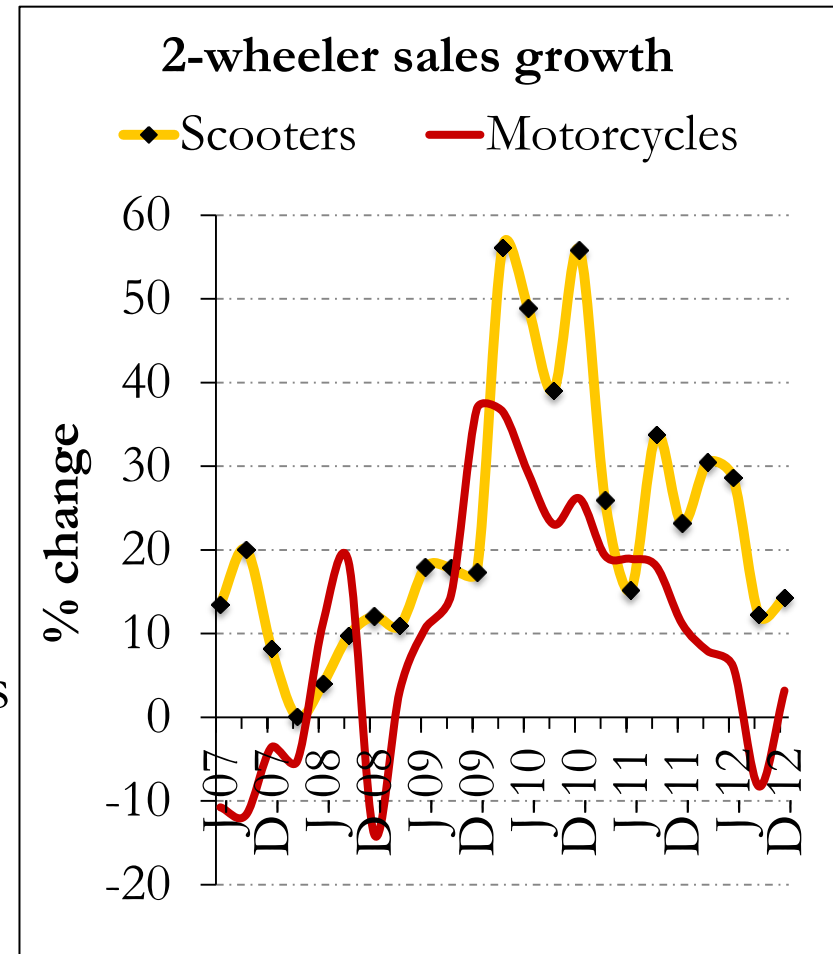
Recent trends: CVs... cont'd

- Construction equipment companies report high levels of under-used equipment – implying re-use of existing equipment instead of new sales
- Introduction of ‘ultra-light’ CVs (1-3 tonnes – Ace, Dost models) has created a new, fast-growing niche which has resulted in overall LCV sales still growing at a healthy rate

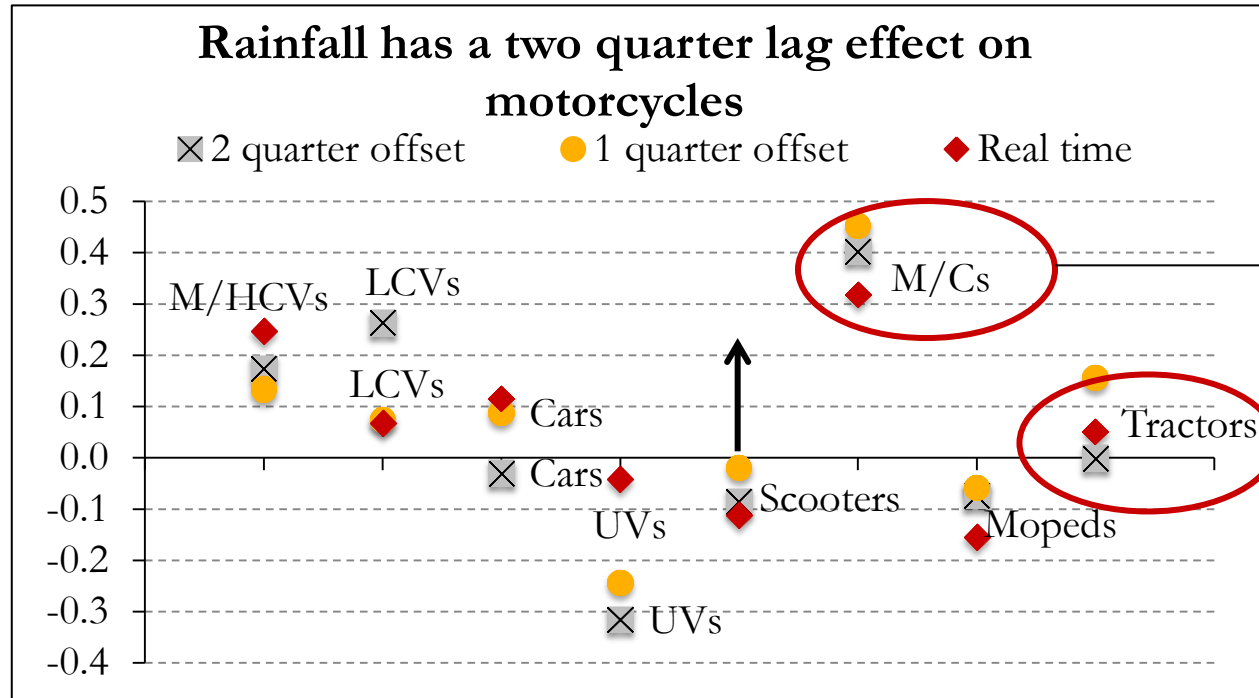


Recent trends: two wheelers

- Scooters have made a comeback since mid-2000s as a repositioned category
 - They are now a discretionary purchase; targeted at younger audiences, including women
 - Gap in fuel efficiency vis-à-vis motorcycles has reduced
- Motorcycles have emerged as the primary mode of transport for HHs that cannot afford cars
 - New model launches have spurred the market, particularly in rural India



Rainfall affects motorcycle sales

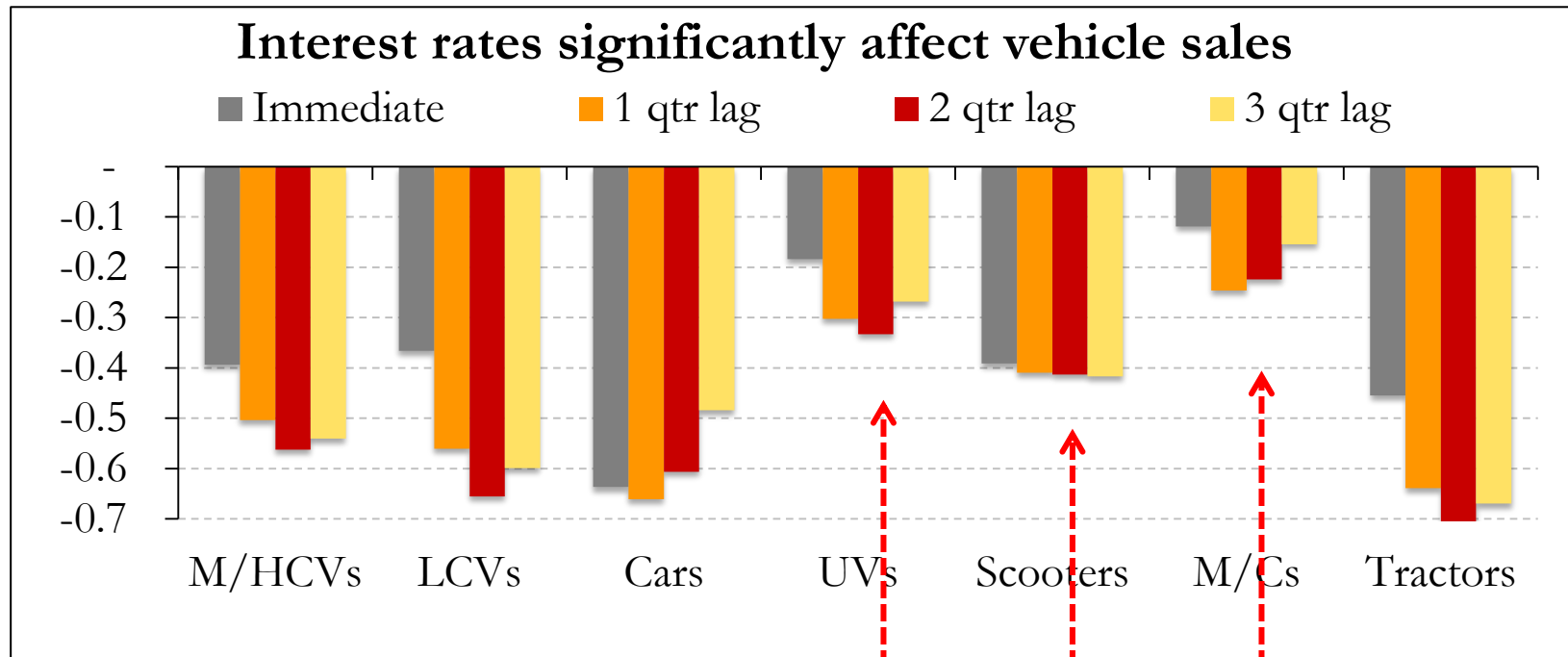


Motorcycle sales show moderate correlation with rainfall with a 1-2 quarter lag

Tractor sales show negligible correlation

- Rainfall correlations are generally low; M/C sales affected with a 1-quarter lag – a result of a higher wealth creation in rural India, which accounts for 60% of sales
- This implies that high rainfall will lift M/C sales one quarter later

But not interest rates

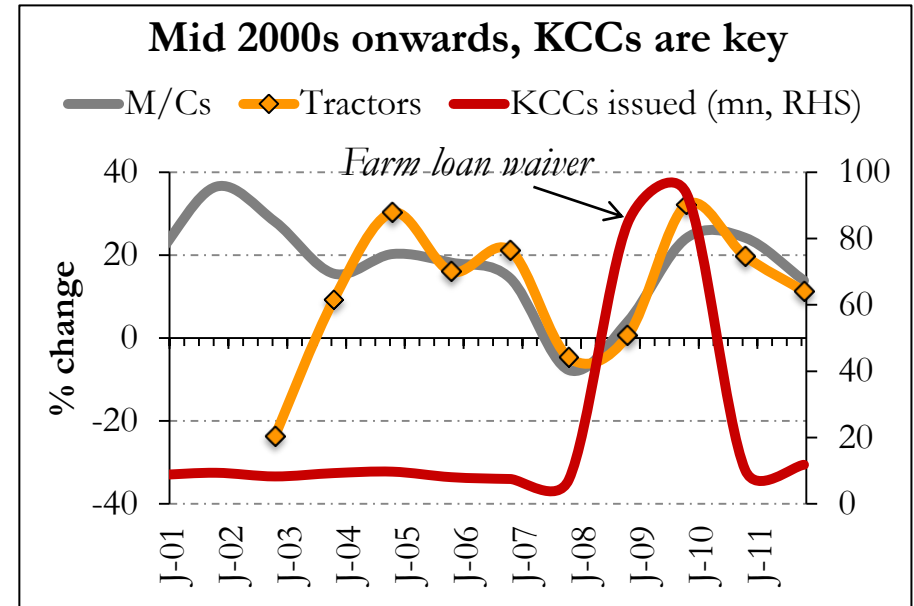
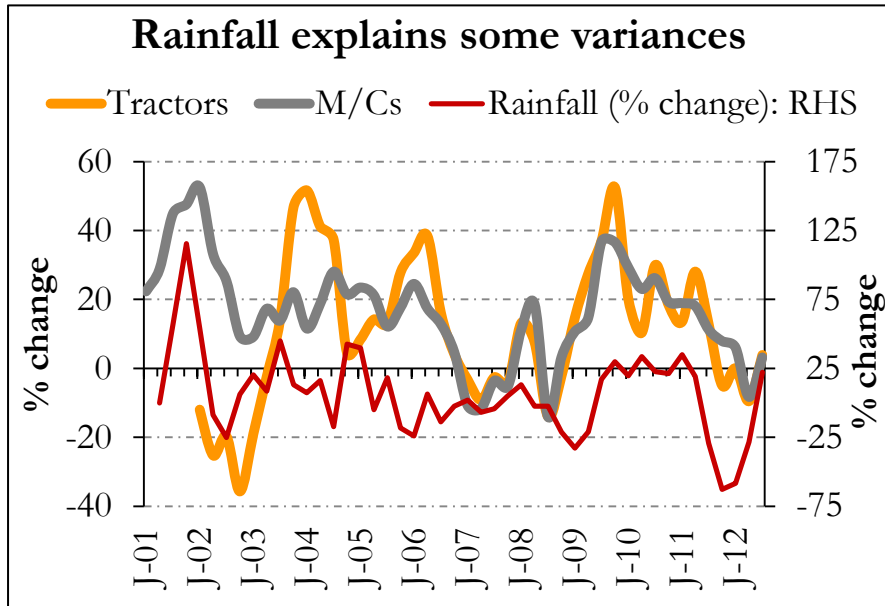


*Low
correlation*

Interest rates do not significantly affect:

- Motorcycles – overall <40% of motorcycles are bought on finance (20% of 60% + 70% of 40%) and they are generally essential purchases
- UVs – discretionary, high value purchases which are not rate dependent

Recent trends: M/Cs and tractors



- Tractor sales in the early 2000s have grown on account of low penetration
- Since the late-2000s, especially post the farm loan waiver, they have increasingly followed credit availability e.g. as measured through Kissan Credit Card (KCC) issuances

The Outlook for FY14



Outlook for key industry drivers

- ↓ Overall economic growth impetus will remain weak at least through H1
- ↓ Mining may restart in a small way; full resumption many months away – demand for M/HCVs likely to remain weak
- ↓ Inflation remains high, though moderating; will continue to dent buyer confidence across vehicle categories and non-essential spares
- ↓ Diesel prices expected to increase – may not impact CVs, but could reduce the attractiveness of UVs if differential with petrol becomes <Rs 10 per litre
- ↓ Urban infrastructure (public transportation) projects under so-called JNNURM II unlikely to become a reality in FY14 – will impact buses and 3-wheelers

↓ *Indicates negative impact on industry growth in FY14*

↑ *Indicates positive impact on industry growth in FY14*

? *Indicates uncertainty regarding the factor's behaviour in FY14*

Source: industry interviews; IMA research and analysis. JNNURM: Jawaharlal Nehru National Urban Renewal Mission.

Outlook for industry drivers... cont'd

- ↑ Interest rates likely to fall, but slowly – positive impact on all four-wheeler categories and CVs
- ↑ Capital flows likely to improve in FY14; Sensex expected to gain 8-10% – can boost car and CVs sales mildly
- ↑ Moderate improvement in infrastructure and construction activity with the formation of the Cabinet Committee on Investment – mild positive impact on CVs
- ↑ Supply-side constraints (labour unrest) amongst vehicle companies largely resolved
- ↑ Pre-election year is likely to see increased MSPs and other rural sops – will benefit motorcycles, tractors and LCVs

↓ *Indicates negative impact on industry growth in FY14*

↑ *Indicates positive impact on industry growth in FY14*

? *Indicates uncertainty regarding the factor's behaviour in FY14*

Source: industry interviews; IMA research and analysis. MSP: Minimum Support Price; NHAI: National Highway Authority of India.

Outlook for industry drivers... cont'd

- ? Increase in NHAI road construction targets for FY14 can spur CV and tractor sales, but implementation remains doubtful
- ? A better monsoon will boost tractor and motorcycle sales, but is an unknown factor
- ? Commodity prices may remain stable due to global factors through H1 but could increase thereafter
- ? Most vehicle manufacturers remain upbeat on new model launches – implying growth opportunities for ancillaries but also capex requirements
- ? FDI in retail will spur investment, leading to higher cargo volumes and demand for CVs; however, given the gestation period, FY14 may not witness a large benefit

↓ Indicates negative impact on industry growth in FY14



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Source: industry interviews; IMA research and analysis. MSP: Minimum Support Price; NHAI: National Highway Authority of India.

Outlook for FY14: passenger cars

Growth

- FY14 growth likely to be moderately higher, **5-7%*** compared to - 4.6%^ based on stock market strengthening and falling rates; fundamental demand for personal transport remaining strong
- Diesel cars will remain attractive until the price differential between petrol and diesel is $> \text{Rs } 10/\text{litre}$

Strategy and issues

- High scope for penetration in tier III and IV towns – major focus area for manufacturers
- New model pipelines intact, but major capex plans postponed
- Cost containment through indigenisation and productivity increases
- Push non-cyclical revenue streams (spares) to counter cyclicity

Outlook for FY14: utility vehicles

Growth

- FY14 growth likely to remain strong at 17-20%*, based the continuing shift towards lifestyle-based shift towards larger, versatile vehicles; new model launches

Strategy and issues

- Manufacturers are bullish and will continue launching new models, with finer market segmentation
- To offset the increasing cost of imports, focus on greater indigenisation
- Diesel price increase can reduce attractiveness of UVs if differential vis-à-vis petrol falls below Rs 10/litre (OMCs have not increased diesel prices in the March 2013 review)

Outlook for FY14: two wheelers

Growth

- FY14 growth likely to improve to 5.0-7.0%* from 3.2%^, based on falling rates; and increasing availability of rural credit
- Substantial scope for further penetration (currently at 35% and 14.3% of households in urban and rural India respectively)
- Growth in scooters to remain higher than M/Cs in urban India
- *Game changers for higher growth*: good monsoon; pre-election sops for rural India (e.g. farm loan waiver; Food Security Bill)

Strategy and issues

- Finer segmentation in the budget segment and new models in the premium segment
- Manufacturers attempting to cut down on discounts while increasing value (e.g. disc brakes in entry level bikes)

Growth

- FY14 growth likely to improve to 5.5-6.5%* from -3.0%^, based on falling rates; increasing availability of credit; and the low base of FY13
- Shift towards farm mechanisation (driven by increasing labour costs) will continue; aided by Government initiatives (e.g. hiring centres)
- *Game changers for higher growth*: faster land consolidation (e.g. Punjab, Rajasthan have introduced laws to boost land leasing); pick up in mining and construction; pre-election rural sops

Strategy and issues

- Rationalisation of HP segments to gather pace (domestic market): down-trading from >50HP to 49HP (due to emission norms) and up-trading from 20 HP to 30HP (due to favourable cost economics)
- Export markets to be led by >50HP tractors; the same capabilities could eventually be leveraged in the domestic market at a later stage

Source: industry interviews; IMA research and analysis. *median projections by industry players; ^pertains to the period April 2012-February 2013.

Outlook for FY14: commercial vehicles

Growth

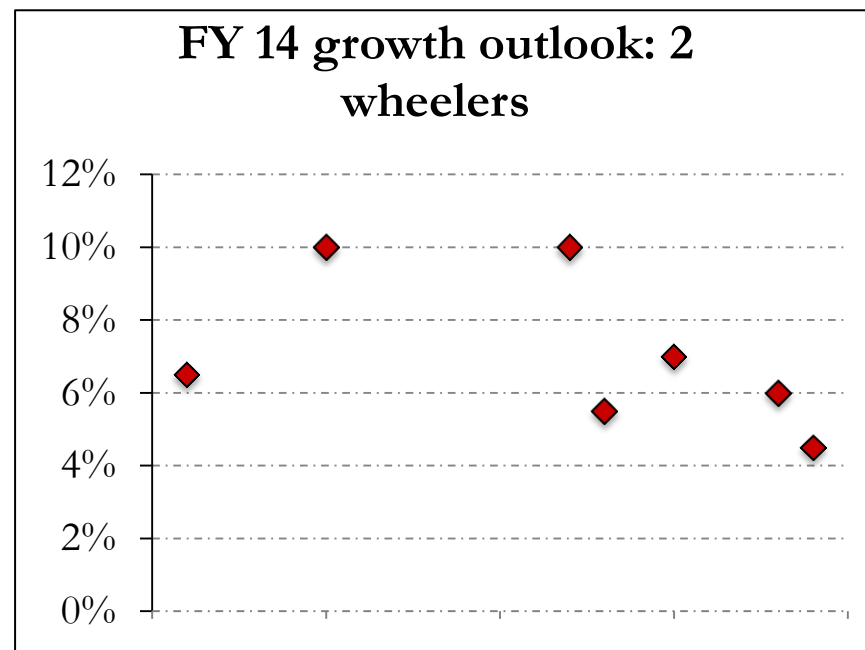
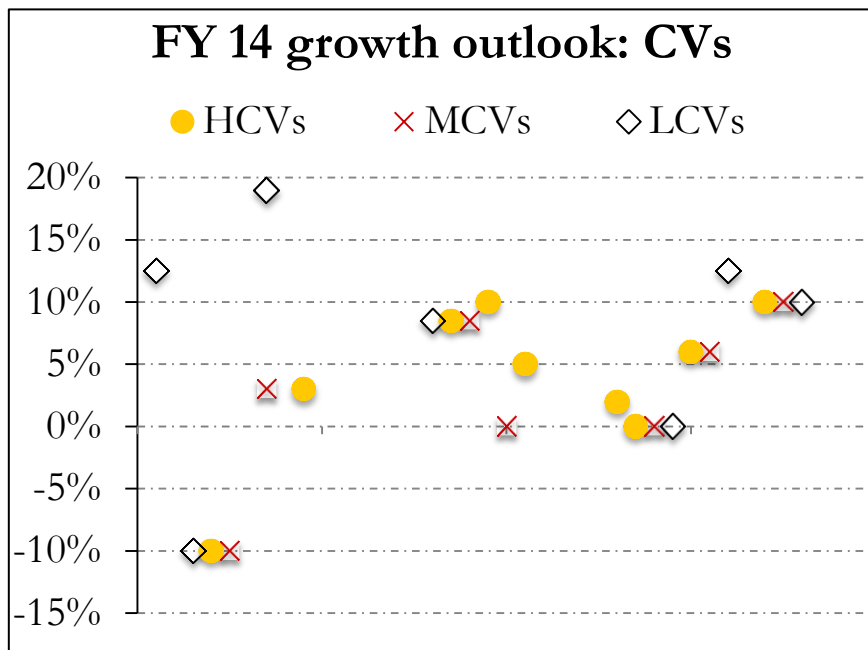
- FY14 growth may improve to 2.0-4.0%* from -22.8%^ for HCVs/MCVs and moderate to 11.0-12.5%* from 14.5%^ for LCVs
- HCV/MCV outlook remains weak on account of the poor outlook for mining and construction; however, further volume decline not expected; LCV outlook is stable with continued growth in the SLCV segment and mild recovery in industrial growth
- *Game changers for higher growth:* pick up in mining (through faster judicial processes) or infrastructure (on account of the CCI) in H2

Strategy and issues

- Focus on increasing sales and service network
- Reinforce transition within SLCV category from 1-2t to 3-3.5t vehicles
- Introduction of heavier-duty and more fuel efficient HCVs to leverage improving road quality and insulate against rising fuel costs

Source: industry interviews; IMA research and analysis. *median projections by industry players; ^pertains to the period April 2012-February 2013.

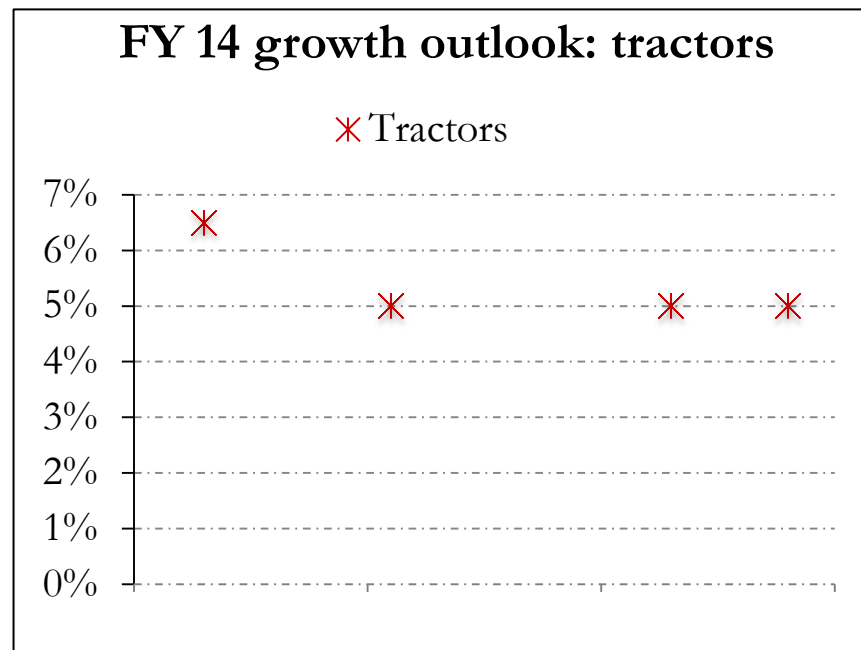
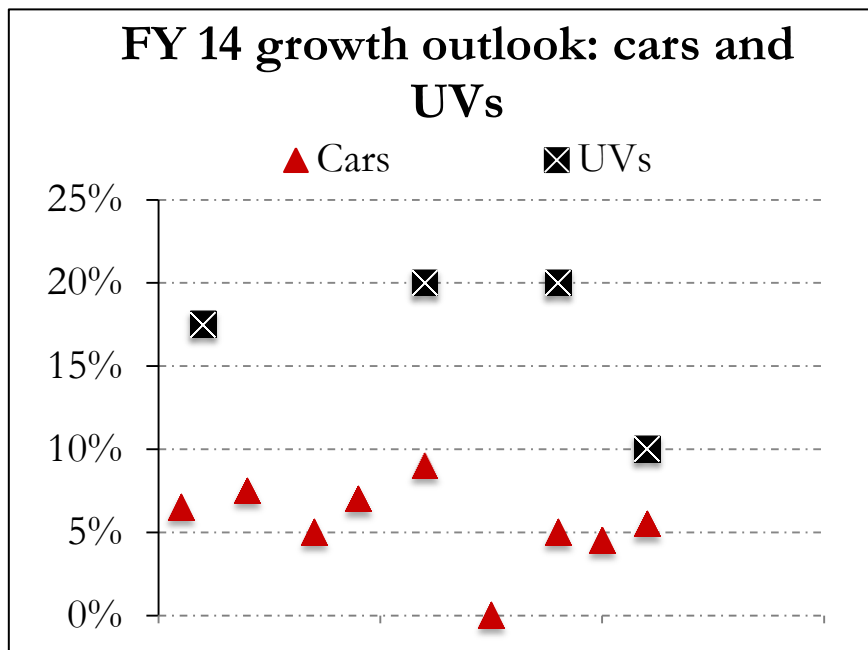
Outlook at a glance: industry views



Forecasts obtained from one-on-one industry interviews:

- HCV and MCV forecasts are both in the range of **0-10%**, except one outlier each; LCV forecasts are higher at **8.5-12.5%**, except two outliers
- 2-wheeler forecasts are in the range of **4.5-7%**, except two outliers at 10%

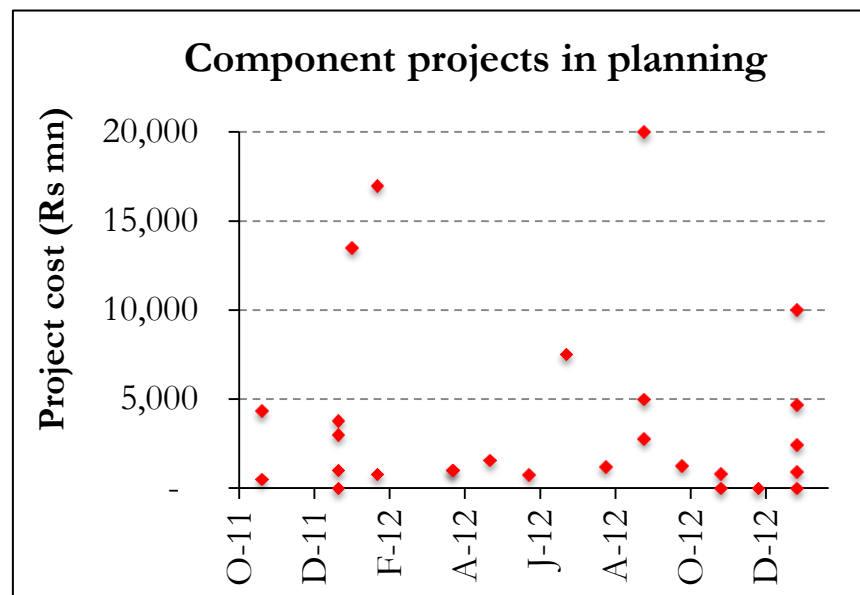
Industry views...cont'd



- Passenger car forecasts are in the range of **5-9%**, except one outlier
- UV forecasts are higher in the range of **17.5-20%**, except one outlier
- Tractor forecasts are in the range of **5-6.5%**

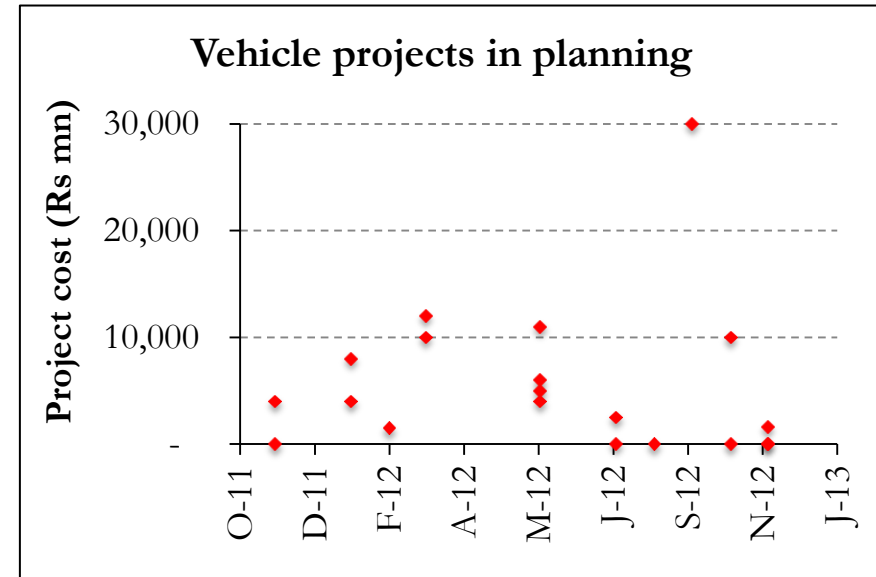
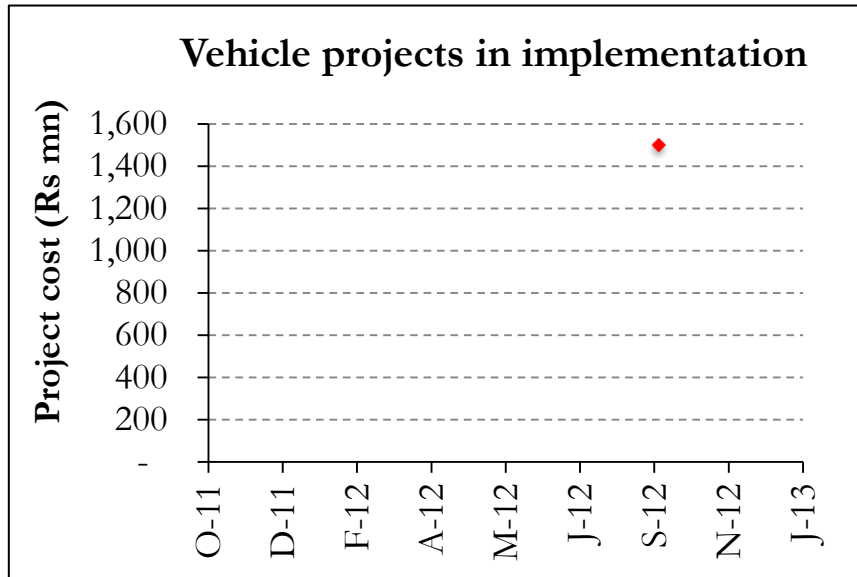
Source: industry interviews; IMA research and analysis. Determination of outlier forecasts is based on IMA's independent research and assessment.

IMA



- Source: IndScan; IMA analysis. Project status as of January 2013. Projects whose capex estimates have not been ascertained are not included.

...even more so for vehicle companies

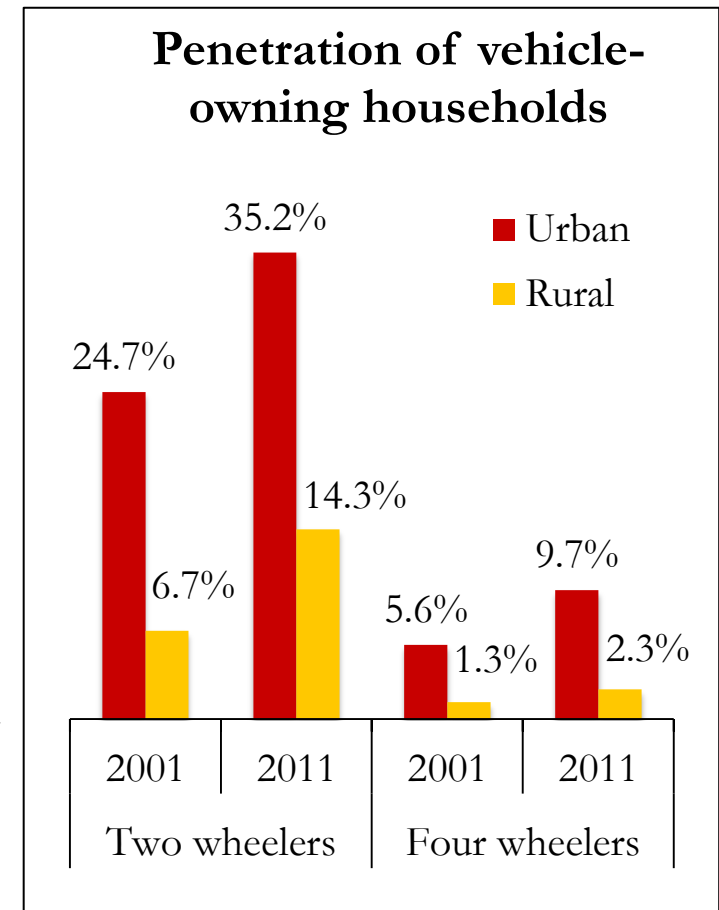


- The status amongst vehicle manufacturers (including engine manufacturers) is even more subdued
- Only one major project is currently under implementation – all others are in ‘planning’ stage

Source: IndScan; IMA analysis. Project status as of January 2013. Projects whose capex estimates have not been ascertained are not included.

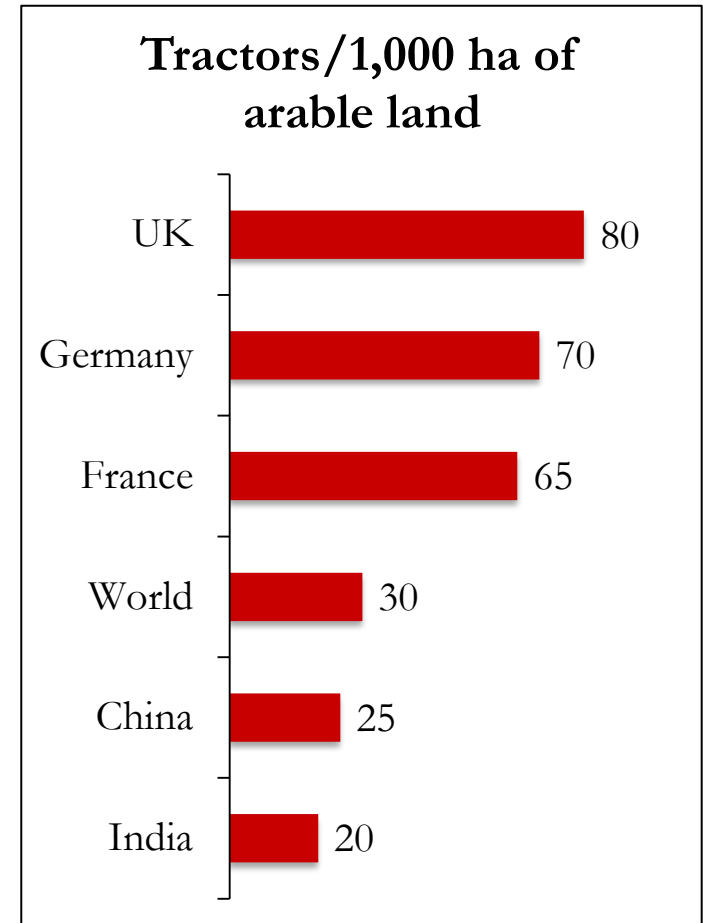
The longer term view

- In 2001, ~25% of urban HHs owned a two wheeler – increased to 35% by 2011
- 6.7% of rural HHs owned one in 2001 – this increased to 14.3% by 2011 i.e. penetration has more than doubled
- 5.6% of urban HHs owned a four wheeler in 2001 and 9.7% by 2011
- In rural India, the penetration increased from 1.3% to 2.3%
- 2-wheeler sales are growing faster in rural India and 4-wheelers in urban India
- The potential for further penetration is still substantial



Opportunity for tractors and CVs too

- Penetration of tractors is 20 per 1000/ha of arable land, compared to 30+ globally
- Average Indian tractor size is 35-39 hp, well below the world average of 70 hp
- Land consolidation and leasing can compensate for small farm sizes; increasing wage rates for manual labour also have a favourable impact
- LCV growth will be driven by intra-city applications – current LCV:HCV ratio at 1:1 in India, against 5:1 in developed countries
- HCVs will benefit from the improving road network and a more sophisticated retail and logistics sector driving higher cargo volumes



Automotive forecast summary

	FY12	FY13 (YTD)	FY14^	Next 5 years^
Commercial vehicles	13.9%	-1.5%	8.7%	7.7%
<i>Medium and heavy vehicles</i>	2.7%	-22.8%	2.9%	7.9%
<i>Passenger carriers</i>	-3.1%	-4.6%*	5.0%	7.5%
<i>Goods carriers</i>	3.7%	-24.1%*	2.5%	8.0%
<i>Light vehicles</i>	24.2%	14.5%	11.6%	7.6%
<i>>3.5 t</i>	10.9%	-21.9%*	2.5%	3.0%
<i><3.5 t</i>	26.3%	22.9%*	12.5%	8.0%
Passenger cars and vans	4.7%	-4.6%	6.0%	5.0%
Utility vehicles	16.7%	54.5%	18.5%	11.0%
Two wheelers	15.7%	3.2%	6.0%	8.5%
Tractors	11.3%	-3.0%	6.0%	7.5%

Source: SIAM; industry interviews; IMA analysis. *YTD figures pertain to the April 2012-February 2013 period except entries marked with * which pertain to the April-December 2012 period; ^Forecasts by IMA based on industry inputs and independent macro analysis.

Thank You

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