THE AUTO SECTOR: OUTLOOK AND PROSPECTS

In conversation with AK Taneja, Managing Director and Chief Executive Officer, Shriram Pistons and SG Murali, Advisor, TVS Motors

In 2018, the automotive industry entered what everyone now agrees is a structural slowdown. Initially, it appeared as if the downturn was being driven by short-term factors such as a jump in insurance premiums, but as it accelerated, it became apparent that other factors were at play. These included a credit squeeze, tightening emission norms and a waning of consumer sentiment. Today, the entire sector is under immense stress, which has spread to allied and peripheral industries, too. Given its substantial linkages with the rest of the economy, the automotive industry is in many ways a barometer of the wider industrial system. What does the future hold for this industry? We invited AK Taneja, Managing Director and Chief Executive Officer, Shriram Pistons and SG Murali, Advisor to TVS Motors, to share their assessment of current industry trends and the forward view.

THE PERFECT STORM

Sales continue to decline across all segments…

The Indian auto industry is undergoing a prolonged phase of turbulence. Overall sales are on a downward trend, with passenger vehicle (PV) shipments falling 18% in April-November 2019 and those of commercial vehicles (CV) by a steeper 22%. Even the resilient two-wheeler segment saw a 13% decline in this period. Several factors – regulatory, economic and customer-driven – have all converged to create a perfect storm for the auto sector.

Safety and environmental norms, and mandatory insurance have impacted cost structures and overall demand

- **Regulatory changes:** A number of regulatory changes have pushed up cost structures for auto companies and pulled down demand. New safety norms require the installation of anti-lock/combined braking systems, driver-side airbags, speed warnings, rear parking sensors and seat-belt reminders. Added to that, mandatory upfront payments for insurance – for a minimum of three years for four-wheelers and five years for-two wheelers – have increased on-road prices. Illustratively, the price of 2-wheelers has jumped 21% on average in the last 2 years. The new Bharat Stage VI (BS-VI) emissions standards and CAFE norms are expected to push up retail prices by a further 5-15%. The shift to BS-VI has also caused buyers to hold back in anticipation of steep discounts on unsold stock, and a dip in the resale value of older cars. Plainly, in a low-income (USD 2,000 per capita), high-volume (4 million PVs a year) market like India, reduced affordability will impact demand. In the CV segment, a new rule allowing a 25% increase in load-carrying capacity has negatively impacted demand.

Policy changes have been broadly deflationary

- **Policy reforms:** The government's broader policy thrust over the past few years, though well-intentioned, has been largely deflationary. Important 'course-correcting' steps such as demonetisation, the rollout of the GST, the Insolvency and Bankruptcy Code, and the RBI's recognition of NPAs, have all exerted a downward pull on spending. The liquidity crisis in banks and NBFCs have had a huge strain, with a ripple effect on companies, investors and the public. Given that most vehicles are purchased on finance, this has hit the auto industry particularly hard.

The Auto Sector Shifts Gears: From Turbulence to Hope

In conversation with Ajay Seth, Chief Financial Officer, Maruti Suzuki; SG Murali, Mentor and Advisor, TVS Motor Company and Soumitra Bhattacharya, Managing Director, Bosch Limited and Regional President, Bosch Group

The automotive sector is not only a vital cog in India's manufacturing sector but also a key barometer of general economic health and a significant employment multiplier. It accounts for 7% of GDP, 50% of manufacturing GDP, employs 32 million people either directly or indirectly, and has strong inter-linkages with many other industries. Direct employment by auto OEMs, component manufacturers, dealers and transporters creates indirect employment, such as for after-sales service, drivers, mechanics and insurers. Regularly monitoring the health of the auto sector is thus key to understanding India's broader macro-economy. The sector was in troubled waters even before Covid halted production and sales, but more recently, it has seen a sharp V-shaped recovery. Industry veterans from three prominent companies – Maruti Suzuki, TVS Motor Company and Bosch – shared valuable insights on the 'rebound journey' of their own industry segments. They also provided an assessment of the sustainability of the current upsurge and offered perspectives on government policy, taxation and the way forward on electric vehicles.

A crisis predating Covid…

A myriad of issues had raised prices and dented sales well ahead of Covid

The auto industry was grappling with a host of issues even before Covid hit. These included complex regulations such as CAFÉ and RDE; the change in emission norms from BS-IV to BS-VI; rising fuel prices; rising insurance premiums for PVs and stricter insurance norms for 2Ws; higher road taxes; and cost increases due to the compulsory fitment of safety features such as ABS in 2Ws. On net, these factors led to ~40% and ~25% increases in 2W and entry-level car prices, respectively, over the last few years. Slow job creation, slowing income growth and liquidity issues on account of the NBFC crisis all impacted affordability.

…and signs of recovery…

Sales have recovered faster than expected in recent months on account of several factors…

With the economy on a recovery path, auto sales are now on an upward trajectory. In the near-term, sales are being driven by pent-up demand, easier credit conditions and the positive after-effects of last year's monsoon, which is spurring rural demand, especially for 2-wheelers. Further, there is strong demand from first-time buyers, who are purchasing vehicles for reasons of personal hygiene and safety in the aftermath of Covid. (The lack of an effective mass-transit system in most parts of India is an additional growth factor.) Positive sentiment arising from the ongoing vaccination drive will support growth, and there are expectations that the government will soon exclude 2Ws from the 28% 'sin-good' GST tax bracket. On the downside, rising commodity costs over the last six months have been a cause of concern for the industry.

…but the road to 'normalcy' will be long

…but it will take a few years to regain the peaks seen in FY18-19

Each segment of the auto industry is projecting a very different path back to 'normalcy', which is broadly defined as the peak sales levels seen in FY18-19. Light (LCV) and heavy (HCV) commercial vehicle sales, at 0.41 and 0.16 million, respectively in FY20-21, are a long way from their FY18-19 peaks of 0.67 and 0.48 million. However, 2Ws at 17 million and PVs at 3 million are much closer to their highs of 25 million and 4 million.

INDIAN AGRICULTURE OF TOMORROW: E-CHOUPAL 4.0

In conversation with S Sivakumar, Head (Agri and IT Businesses), ITC

In June 2000, ITC launched e-Choupal, a web-based, market-integration model that sought to enhance farm efficiency and enable better price discovery. Over time, the initiative grew from strength to strength and helped enable a transformative shift in the farm sector. S Sivakumar, who heads the company's Agri and IT businesses, shed light on how e-Choupal heralded a new era for Indian agriculture.

A GAMUT OF CHALLENGES…

Low returns, poor productivity, high consumer prices, and mixed quality

Twenty years ago, India's farm sector was a complete shambles. Farmer prices were staggeringly low, productivity was poor, and foreign consumers would complain that Indian produce was not only expensive but also of inconsistent quality. Many of these issues arose from the *mandi* mechanism, a system under which farmers could not sell directly to buyers, but only through auctions. The entire process was facilitated by mandi agents, who would charge farmers a commission on the selling price. Agricultural transactions could only occur in a mandi, and the system was plagued with corrupt practices and hefty commissions. This multi-tiered system pushed up consumer prices, and also suppressed farmer income.

…AND HOW ITC UNLOCKED BOUNDLESS OPPORTUNITIES

e-Choupal: A disruptor like nothing before it

ITC's decision to enter the agri-business space breathed new life into the system. Early on, the firm conducted a thorough situation analysis of the sector. It realised that India's agricultural value chain required a complete overhaul – which led it to create e-Choupal, a web-based market-integration model. Today, the initiative covers more than 4 million farmers in over 35,000 villages. Three versions of the model have been implemented, and the fourth is about to be launched. Essentially, a handful of factors explain why e-Choupal succeeded where others may not have:

Generation 1: Navigating operational roadblocks…

Overcoming key obstacles. The infrastructural challenges were significant: ITC needed to set up computer terminals in villages, and even had to 'regularise' power supplies in many places. A major task was to convince the state governments to institutionalise the setting-up of Internet kiosks, which made for faster and smoother price discovery. Additionally, processes were created to procure directly from farmers, thus avoiding major price distortions. Since the states relied heavily on cesses collected from mandis, they were fairly sceptical about this shift. It took much convincing for them to see that the new system *could* help farmers take more informed decisions about what to produce and the price at which to sell. Farmer empowerment, in fact, lay at the very roots of 'e-Choupal 1.0'.

…and mobilising market intermediaries

Leveraging intermediaries. Weak rural infrastructure meant that intermediaries had to played a vital role, especially in e-Choupal's early days. They enabled such activities as cash handling, goods aggregation, crop quality assessment, and farmer creditworthiness analysis, all at a