INDIAN PASSENGER VEHICLE INDUSTRY

Macro-economic factors + production-disruptions put brakes on sales

DECEMBER 2011

ICRA RATING FEATURE

Summary

The Indian passenger vehicle (PV) industry has experienced a period of strong volume growth in the last five years riding on strong economic growth, rising disposable incomes, favourable demographics and relatively low penetration levels. Frequent introduction of new models by Original Equipment Manufacturers (OEMs), incumbents as well as new entrants, and adequate financing availability also contributed to the growth momentum. As demand and supply tangoed, the industry's volumes grew at 16.3% CAGR during 2007-11, with growth being particularly strong in the last two years (Refer **Table 1**).

However, since the beginning of 2011-12, the industry has been witnessing a slowdown in volume growth marred by rising inflation, hardening interest rates and increasing fuel prices that have combined to dent consumer sentiment. Even the festive season failed to stoke domestic demand despite new model launches, aggressive discounts and promotional schemes offered by OEMs. Apart from macro-economic headwinds dampening demand, events such as production disruption at India's largest PV OEM, Maruti Suzuki, the tsunami in Japan and the recent floods in Thailand also created supply chain stresses, further aggravating the weak performance of the PV industry. The above demand-supply pressures effectively translated into a decline in domestic volumes by 0.5% YoY in 8M FY12. Within segments, the small car and executive car segments have been the worst impacted so far, even as volume growth in the mid-size car segment and utility vehicles (UVs) segment remained in the positive zone. With steady increase in fuel prices since January 2009 (with 63.5% increase till date, diesel is cheaper by ~Rs. 24 per litre, also offers better mileage), there has been a decisive shift in customer preference in favour of diesel-powered cars, reflected in the 24% growth in sales volumes of diesel vehicles in H1 FY12 against a 11% decline in sales volumes of petrol vehicles during the same period. In fact, in segments where both petrol and diesel options are available, diesel vehicle sales far outnumber that of petrol variants by an overwhelming factor of 4:1. However, the preference for diesel vehicles fostered by a distorted fuel price regime could get altered in the event of any increase in excise duty on diesel vehicles that is currently being mulled by the government.

The large incumbents in the domestic PV industry derive strength from their low cost manufacturing capabilities, established vendor base and widespread sales and service network; however, their dominance is being challenged by foreign OEMs that have entered the domestic market in the recent past. Overall, ICRA believes that OEMs may continue to face challenging times at least over the short term as sluggish demand on one hand and increasing competition on the other may restrict earnings growth. While we expect PV volumes (domestic + export) to grow at ~11% CAGR over FY12-16, the growth in FY12 may remain tepid at around 3%.

Table 1: Volumes

	Volumes					YoY Growth (%)				
	FY08	FY09	FY10	FY11	FY12e	FY08	FY09	FY10	FY11	FY12e
Domestic + Export	1,768,283	1,888,432	2,397,478	2,973,900	3,054,600	12.0%	6.8%	27.0%	24.0%	2.7%

Source: SIAM, ICRA's Estimates

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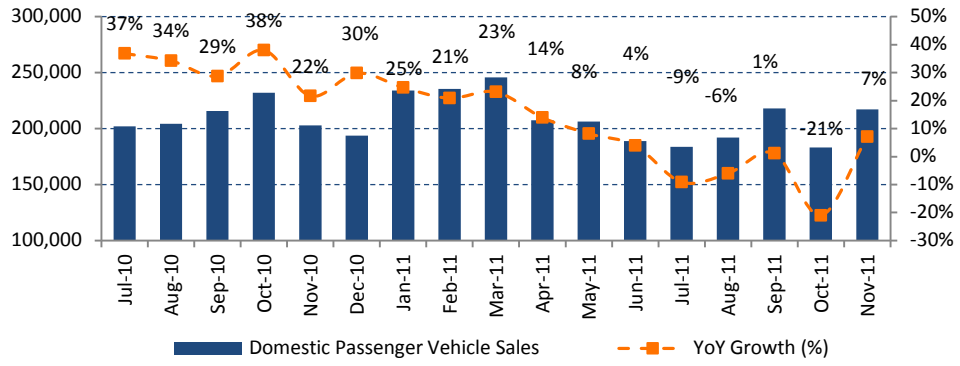
Chart 1: Trend in Domestic PV Sales Volumes and Growth



Source: SIAM, ICRA's Estimates

Table 2: Trend in Market Share in Domestic PV Industry

OEMs	FY08	FY09	FY10	FY11	Q1 FY12	Q2 FY12	YTD FY12
Maruti	45.9%	47.0%	45.2%	45.9%	41.6%	37.5%	38.0%
Hyundai	14.0%	15.9%	16.4%	14.6%	15.5%	14.9%	15.6%
Tata Motors	14.8%	13.9%	13.5%	12.1%	12.6%	12.6%	13.3%
M&M	8.4%	7.8%	8.1%	7.3%	8.9%	10.1%	9.6%
Toyota	3.6%	3.1%	3.3%	3.4%	4.8%	6.4%	5.8%
GM	4.3%	4.0%	4.5%	4.3%	4.4%	4.8%	4.6%
Ford	2.2%	1.8%	1.9%	4.0%	3.5%	3.8%	3.8%
Volkswagen	0.0%	0.1%	0.3%	2.3%	3.3%	3.5%	3.5%
Honda	4.0%	3.4%	3.2%	2.4%	1.3%	2.8%	2.0%
Skoda	0.9%	0.9%	0.9%	0.9%	1.3%	1.0%	1.2%
Nissan	0.0%	0.0%	0.0%	0.5%	0.7%	0.9%	1.0%
Others	2.0%	2.1%	2.6%	2.2%	2.1%	1.8%	1.7%

Source: SIAM, ICRA's Estimates, YTDFY12 corresponds to Apr 11 to Nov 11 time period

Growth enters negative territory

After reporting strong volume growth over the last two fiscal years, the domestic PV industry started witnessing a slowdown since the beginning of FY12. Macro-economic headwinds and depressed consumer sentiments have plagued the domestic PV industry resulting in volume decline of 4.3% YoY in Q2 FY12; that followed a relatively modest volume growth of 8.8% YoY in Q1 FY12. Overall, the domestic PV volumes have declined by 0.5% YoY in 8m FY12.

The monthly volume growth of the domestic PV industry has seen a sharp decline since July 2011; although November month was an exception with regularising of production at Maruti Suzuki. In Sep 2011 YoY sales de-growth was prevented by build-up of dealer inventory prompted by an early festival season (by about ten days) coupled with new model launches and aggressive discounts and promotional schemes offered by OEMs. Retail sales, however, failed to pickup in Oct 2011 with market sentiments running low, resulting in deferment of purchase by dealers. The strike at Maruti Suzuki's plants owing to labour issues also effected production during October.

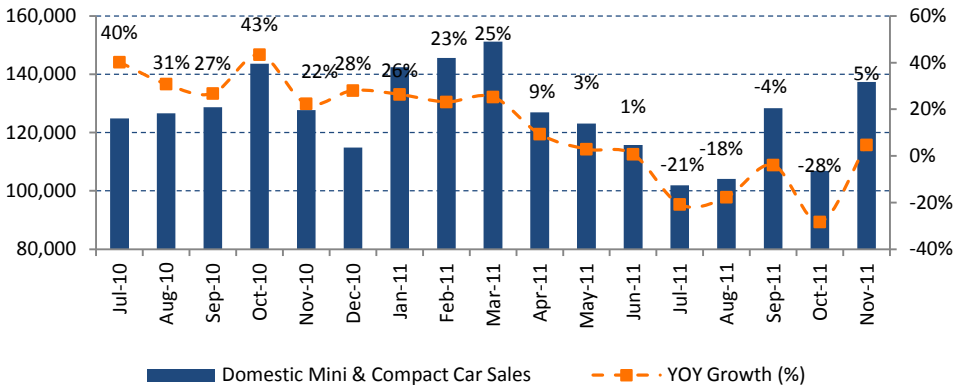
Within the industry, the cars segment de-grew by 3.5%, during 8m FY12, while Utility Vehicles (UVs) and Multi Purpose Vehicles (MPVs) reported a growth of 11.1% and 10.3%, respectively. Amongst segments, the small car segment, which accounts for over 80% of the PV industry's volumes, has been impacted the most, while mid-size segment owing to new product launches has been somewhat insulated from the slowdown so far. The premium & luxury segment of cars, which had reported healthy increase in volumes during Q1 FY12, started showing signs of weakness in Q2 FY12.

Industry leader suffered large market share loss in Q2 FY12

In Q2 FY12, industry volumes were impacted by production disruptions at Maruti Suzuki which led to a sharp decline its domestic market share from 45.9% in FY11 to 37.5% in Q2 FY12. Due to this, a part of the demand shifted to other OEMs like Toyota and Honda which gained market share in the last quarter also facilitated by their new product launches. Also, market participants having diesel models in their portfolio - M&M, Tata Motors and Ford consolidated their market position.

Segment-wise Trends: Small Car Segment

Chart 2: Trend in Domestic Small Car Sales



Source: SIAM, ICRA's Estimates; Note – Small cars include mini + compact segment

Table 3: Trend in Market Share in the Small Car Segment

OEMs	FY10	FY11	Q3 FY11	Q4 FY11	Q1 FY12	Q2 FY12	YTDFY12
Maruti	55.9%	54.0%	57.7%	52.5%	48.6%	47.2%	45.6%
Hyundai	23.8%	20.9%	21.7%	19.8%	21.7%	21.5%	22.0%
Tata Motors	12.1%	10.9%	8.0%	11.7%	13.8%	11.9%	14.3%
Ford	0.7%	5.1%	3.8%	5.8%	4.7%	4.7%	4.7%
GM	5.1%	4.7%	4.6%	4.5%	4.6%	5.9%	5.2%
Volkswagen	0.1%	1.9%	1.7%	2.3%	2.7%	2.7%	2.7%
Nissan	0.0%	0.8%	0.8%	1.3%	1.2%	1.3%	1.3%
Skoda	0.5%	0.7%	0.9%	1.1%	1.3%	1.1%	1.1%
Fiat	1.1%	0.8%	0.6%	0.8%	1.0%	0.8%	0.8%
Honda	0.6%	0.3%	0.2%	0.3%	0.2%	0.5%	0.5%
Toyota	0.0%	0.0%	0.0%	0.0%	0.2%	2.5%	1.7%

Source: SIAM, ICRA's Estimates, YTDFY12 corresponds to Apr 11 to Nov 11 time period

Demand for small cars dries out, market shrinks

The small car space, catering to the most price sensitive customer segment, was amongst the worst performing industry segment in 8m FY12. Successive interest rate hikes and fuel price increases, coupled with pressure on disposable income due to inflationary conditions prevailing in the Indian economy, played on the sentiments of Indian consumers; resulting in a 7.5% YoY decline in small car segment volumes in 8m FY12.

In the recent months, the segment has also been negatively impacted by production disruptions at Maruti Suzuki, maker of every second small car in India. While the segment saw several new car launches during the period including the new Maruti Suzuki *Swift* (launched in mid Aug 2011), labour issues at the company's factories prevented the company from capitalizing on the strong maket response it received for this model. However, with commencement of production at Maruti Suzuki and restocking of its dealers, sale of small cars picked-up during Nov 2011. November month also saw an healthy YoY improvement in small car sales of Tata Motors and GM.

The small car segment, which once used to be a predominantly petrol engine segment, is witnessing rising diesel penetration. Most of the OEMs (except Honda) now have diesel variants in their small car portfolio that co-exist with petrol variants.

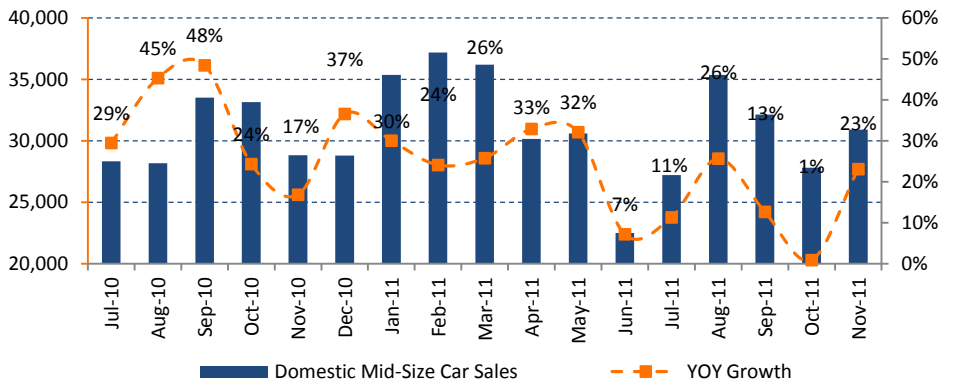
Competitive pressures intensifying on the back of new launches

Competitive intensity in the compact car space continues to increase with recent launches of Hyundai *Eon* (Oct 2011), Honda *Brio* (Sep 2011), Toyota *Liva Diesel* (Sep 2011) and Chevrolet *Beat Diesel* (July 2011). Refurbished versions of Honda *Jazz* and Tata *Indica Vista* were also introduced near the festive season. The pipeline for new hatch back launches remains robust with following new small car models likely to be launched soon - Maruti Suzuki *Cervo*, Chevrolet *Sail*, Ford *Fiesta hatchback*, Volkswagen *UP* and Skoda *Citigo*.

While Maruti Suzuki continues to be the dominant player in the small car segment commanding the largest product portfolio, it lost substantial market share in Q2 FY12. Some correction in the OEM's market share is expected over the next couple of months as it ramps-up production and fulfills pending orders

Segment-wise Trends: Mid-Size Car Segment

Chart 3: Trend in Domestic Mid-Size Car Sales



Source: SIAM, ICRA's Estimates

Table 4: Trend in Market Share in Mid-Size Car Segment

OEMs	FY10	FY11	Q3 FY11	Q4 FY11	Q1 FY12	Q2 FY12	YTD FY12
Maruti	35.9%	35.8%	35.4%	35.7%	36.8%	26.1%	31.1%
Hyundai	11.0%	9.6%	9.1%	6.8%	16.1%	16.8%	16.8%
Toyota	0.0%	2.2%	0.4%	7.1%	15.7%	10.3%	12.9%
Honda	16.3%	12.7%	12.9%	10.6%	7.4%	14.4%	10.2%
Volkswagen	0.1%	5.1%	8.0%	9.1%	9.3%	9.7%	10.1%
Tata Motors	20.5%	24.0%	21.5%	22.6%	4.5%	9.3%	5.0%
Ford	9.6%	4.7%	6.3%	3.1%	4.0%	6.5%	5.9%
M&M	1.9%	2.7%	3.1%	3.0%	4.6%	5.2%	5.0%
Nissan	0.0%	0.0%	0.0%	0.0%	0.0%	0.7%	1.3%
Others	4.7%	3.1%	3.2%	2.0%	1.6%	1.1%	1.7%

Source: SIAM, ICRA's Estimates, YTDFY12 corresponds to Apr 11 to Nov 11 time period

Mid-Size segment outperforms industry on the back of new launches

The mid-size segment remained somehwat insulated from the overall industry slowdown and reported 18.9% YoY growth in 8m FY12. The growth was supported by low base of models like Volkswagen *Vento* (launch date-Jul 2010) and Toyota *Etios* (Dec 2010) apart from healthy demand for the refurbished Hyundai *Verna* (May 2011) and the new Ford *Fiesta* (Jul 2011). The segment has high diesel penetration and shift towards diesel driven vehicles has also contributed to the growth in this segment. Growth in the mid-size car space is expected to remain buoyant with upcoming launches of Skoda *Rapid*, Volkswagen *UP Saloon*, the new Maruti *Swift Dzire* and ramp up in sales volumes of Nissan *Sunny* (launched in Sep 2011).

Amongst the larger selling models in this segment – Honda *City* and Maruti *Swift Dzire* – while the former is witnessing a demand pickup after price cuts, the latter saw a shift in its production from Maruti Suzuki's Manesar plant (where production was impacted to the extent of almost 50% in September) to the Gurgaon plant (where production was largely normal in Q2 FY12). While, the strike in October, which impacted production at Maruti's both locations crippled the production of Dzire and SX4, the situation improved in Nov 2011.

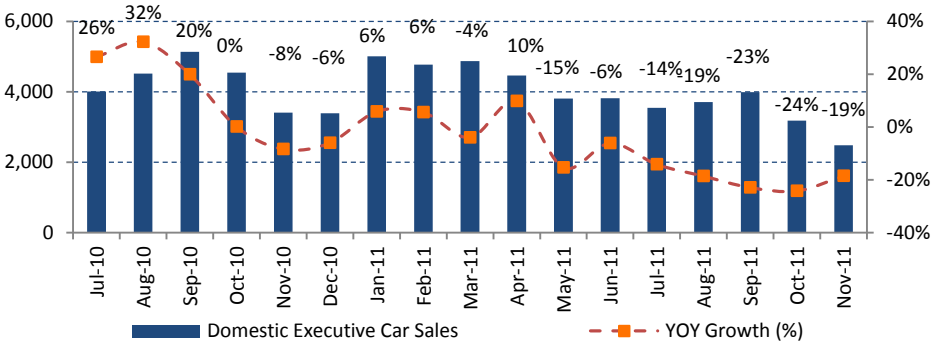
The penetration of diesel variant in the mid-size segment is expected to rise even further. Most of the larger selling models (except Honda *City*) in this space have a diesel option - Toyota introduced the *Etios diesel* in Sep 2011 and Nissan launched the diesel version of *Sunny* recently in Dec 2011

Market share changes hands

Tata Motors, Honda and Ford were the market share gainers in Q2 FY12 at the expense of Maruti Suzuki. Despite intensifying competition in the mid-size car space, it remains an attractive segment for OEMs. Rising disposable income of aspirational middle class Indians has resulted in uptrading from a 'small' to a 'big' car. Further, profit margins in this segment are higher when compared to the mini+compact segment. Strategy of coming out with a hatchback version of a small car has also helped OEMs to keep their incremental investments low .

Segment-wise Trends: Executive Car Segment

Chart 4: Trend in Executive Car Sales



Source: SIAM, ICRA's Estimates

Data post Sep-11 excludes sale numbers of BMW and Mercedes; Nov-11 data excludes sale volumes of Audi

Table 5: Trend in Market Share in Executive Car Segment

OEMs	FY10	FY11	Q3 FY11	Q4 FY11	Q1 FY12	Q2 FY12	YTD FY12
GM	12.5%	22.1%	27.2%	22.1%	27.3%	24.0%	26.1%
Toyota	21.0%	20.5%	23.5%	21.0%	15.1%	26.1%	20.4%
Skoda	16.9%	12.7%	10.5%	12.0%	14.6%	11.1%	12.8%
Fiat	24.0%	17.3%	10.7%	16.8%	16.6%	3.8%	9.5%
Volkswagen	5.3%	6.2%	6.2%	4.5%	2.7%	7.6%	6.5%
Mercedes	3.6%	5.3%	4.3%	6.8%	6.3%	6.3%	5.0%
Honda	12.9%	9.6%	10.2%	9.6%	5.1%	6.0%	6.0%
BMW	3.3%	4.6%	5.6%	4.4%	4.9%	4.3%	4.4%
Audi	0.6%	1.5%	1.9%	1.9%	3.9%	5.7%	4.5%
Renault	0.0%	0.0%	0.0%	0.0%	2.4%	4.3%	3.4%
Maruti	0.0%	0.3%	0.0%	0.9%	1.0%	0.5%	1.2%
HM	0.0%	0.0%	0.0%	0.0%	0.2%	0.1%	0.2%

Source: SIAM, ICRA's Estimates, YTDFY12 corresponds to Apr 11 to Nov 11 time period

Deceleration in Executive Car sales continues

The domestic executive car segment continued to witness flagging sales in 8m FY12, posting a de-growth 14.2% on YoY basis. Although there was a MoM increase in sales during the last quarter,there appeared to be a decline in numbers in Oct 2011 partly due to non-availability of monthly sales data of BMW and Mercedes-Benz for the month, as these OEMs have stopped sharing monthly sales numbers with SIAM.

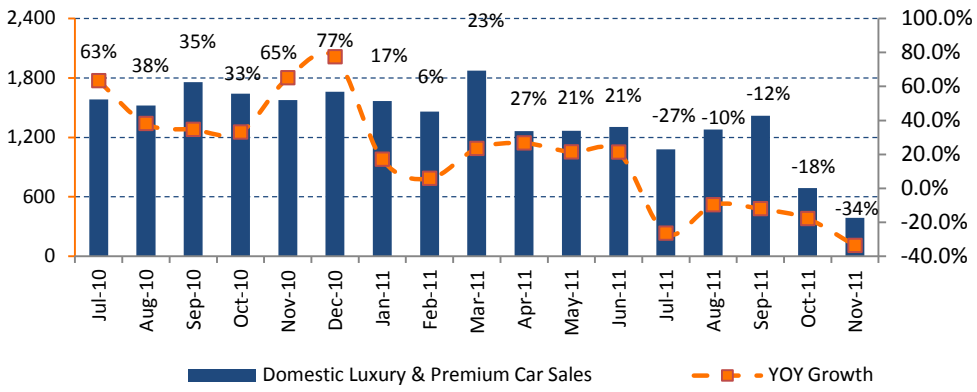
Although the OEMs introduced several refurbished models in this segment – Toyota *Corolla facelift* (June 2011), Volkswagen *Jetta* (Aug 2011) and Skoda *Laura vRS* (Aug 2011), the overall perfromance of the segment remained subdued. Going forward, refurbished versions of Honda *Civic* and Fiat *Linea* are expected during mid FY13.

Toyota regains market position; Fiat sees significant market share loss

In the executive segment, Toyota gained market share in Q2 FY12 post the launch of the new *Corolla Altis* and resumption of regular supplies from Japan. During Q1FY12, the company's production was hampered due to unavailability of imported parts subsequent to the earth quake in Japan. General Motors, with its Chevrolet *Cruze* sedan remains a close competitor to Toyota in this segment. The segment has also seen new model launches in the recent past - Renault *Fluence* and Maruti Suzuki *Kizashi* being the two. Fiat's *Linea* (that was launched in Jan 2009) and is amongst the lower priced offerings in this segment and has witnessed dwindling sales over the last few months resulting in sharp market share loss and making the OEM rethink its vehicle distribution network strategy.

Segment-wise Trends: Luxury and Premium Car Segment

Chart 5: Trend in Luxury and Premium Car Sales



Source: SIAM, ICRA's Estimates

Data post Sep-11 excludes sale numbers of BMW and Mercedes; Nov-11 data excludes sale volumes of Audi

Table 6: Trend in Market Share in Luxury and Premium Car Segment

OEMs	FY10	FY11	Q3 FY11	Q4 FY11	Q1 FY12	Q2 FY12	YTD FY12
Skoda	23.9%	22.2%	19.4%	21.2%	27.1%	15.3%	21.7%
BMW	14.3%	20.1%	25.4%	21.6%	22.9%	23.9%	23.7%
Volkswagen	5.7%	3.9%	1.3%	0.4%	15.3%	7.5%	11.9%
Audi	12.7%	17.4%	18.0%	21.4%	6.4%	14.8%	11.1%
Mercedes	14.6%	17.8%	19.3%	18.5%	17.5%	25.3%	18.0%
Honda	20.9%	13.5%	13.2%	12.9%	7.8%	9.3%	10.1%
Hyundai	3.3%	1.5%	1.2%	1.3%	1.5%	0.8%	1.0%
Toyota	3.0%	2.3%	1.2%	1.9%	1.0%	2.2%	1.6%
Nissan	1.6%	1.3%	1.1%	0.9%	0.4%	0.8%	0.9%

Source: SIAM, ICRA's Estimates, YTDFY12 corresponds to Apr 11 to Nov 11 time period

Growth momentum in Luxury and Premium Cars changes gears

The luxury and premium car segment which was unaffected by macroeconomic headwinds till Q1 FY12 started showing signs of weakness since July 2011. Weak business environment seems to have caught up with the upper-end consumer segment as well. In Q2 FY12, the segment saw an industry wide drop in numbers barring select OEMs like Audi. Agressive discounts by dealers and low interest rates offered by financing arms of luxury carmakers failed to revive the slackening demand in the festive season.

High import duty on Completely-Built-Units (CBUs), and increase in cutoms duty (from 10% to 30%) on pre-assembled engine and transmission parts has forced many luxury car makers to set-up assembly facilities in India. OEMs are willing to undertake these investments given the strong demand potential of premium and luxury car market in India over the long term. Widening consumer base has also prompted the entry of high-end brands such as Maserati, Ferrari, Bentley, Rolls Royce, Porsche, Lamborghini in the domestic market.

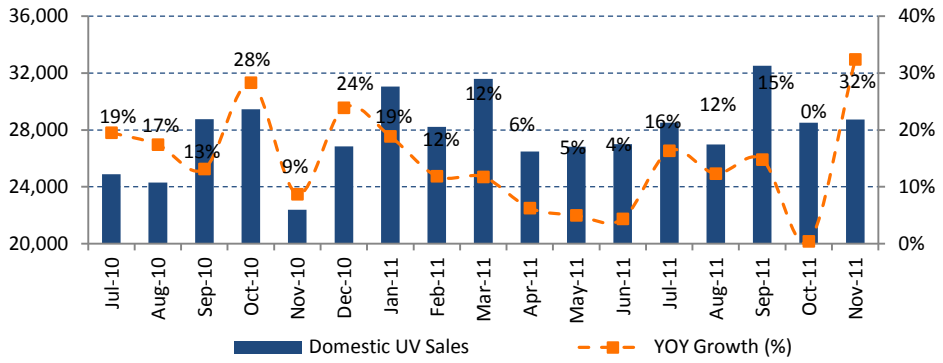
European OEMs continue to dominate the segment

Following entry of new players, competition in the luxury and premium car segment has already picked up. However, as of now, the premium and luxury segment of the domestic car market continues to be dominated by European OEMs – Skoda, BMW, and Mercedes.

In Q2 FY12, sales of Skoda *Superb* saw a sharp decline, partly due to deferment of purchase by customers in wait of the new *Superb*. This, along with strong marketing efforts by Audi and Mercedes, allowed them to gain market share in Q2 FY12

Segment-wise Trends: Utility Vehicle Segment

Chart 6: Trend in Utility Vehicle Sales



Source: SIAM, ICRA's Estimates

Data post Sep-11 excludes sale numbers of BMW and Mercedes; Nov-11 data excludes sale volumes of Audi

Table 7: Trend in Market Share in Utility Vehicle Segment

OEMs	FY10	FY11	Q3 FY11	Q4 FY11	Q1 FY12	Q2 FY12	YTD FY12
M&M	55.2%	52.6%	54.3%	52.0%	56.9%	54.0%	55.9%
Toyota	19.7%	20.0%	19.2%	19.1%	16.8%	19.3%	17.7%
Tata Motors	13.0%	13.7%	13.3%	15.2%	11.5%	11.2%	11.8%
GM	6.0%	6.2%	6.5%	5.6%	7.3%	6.5%	6.8%
Maruti	1.4%	1.7%	1.1%	1.1%	1.9%	2.7%	1.9%
BMW	0.2%	0.2%	0.2%	0.5%	1.1%	1.4%	1.1%
Force Motors	2.2%	2.7%	2.7%	3.0%	1.0%	1.1%	1.2%
Ford India	1.0%	1.0%	0.8%	1.1%	0.8%	0.9%	0.8%
Others	1.3%	1.9%	1.9%	2.5%	2.7%	2.9%	2.8%

Source: SIAM, ICRA's Estimates, YTDFY12 corresponds to Apr 11 to Nov 11 time period

UV sales pick up speed in Q2 FY12

Domestic UV segment has been one of the most resilient PV segments, registering a YoY growth of 14.5% in Q2 FY12. While growth in Q1 FY12 was lower (5.2%) partly due to shortage of component supplies from Japan, the situation improved during the last quarter, in which volumes were also supported by an early festival season. While sales in October were subdued due to inventory clearing by dealers and maintenance shutdown at M&M, wholesale numbers shot-up in November. Lower MoM sale in Oct 2011 and Nov 2011 was due to exclusion of sales numbers of Mercedes, BMW and Audi from SIAM data.

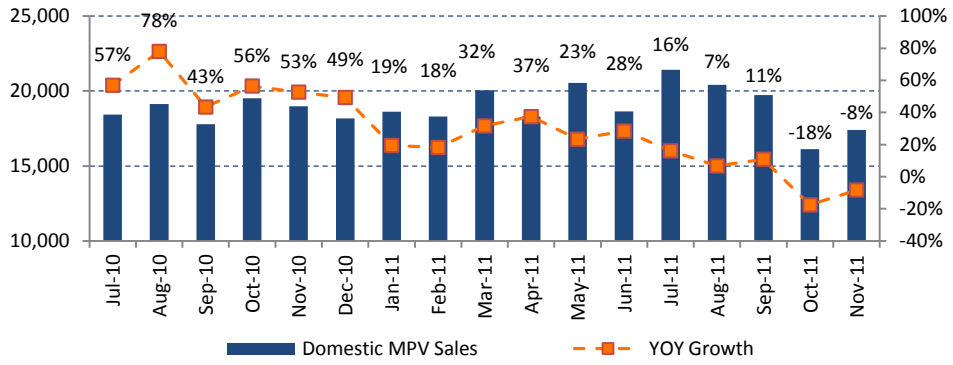
The domestic UV segment is characterized by a wide price range and a more dispersed customer base across income segments. Also the segment primarily operates largely on diesel, which supports demand in the current scenario. Accordingly, demand in this segment has been more stable. Entry level vehicles continue to do well with burgeoning demand from Tier-II and Tier-III cities along with demand from the people-mover segment in metros. Private ownership of models like M&M *Xylo* and Toyota *Innova* is also on the rise. Further, unlike the premium and luxury cars, the upper-end of the UV segment (price >Rs. 15 lakhs) continued to see strong growth (26.1% in Q2 FY12).

M&M continues to dominate the UV segment; some market share decline expected with launches by competition

While M&M's *XUV 500* (launch Oct 2011) garnered overwhelming market response, demand for *Force One* (Aug 2011) launched by Force Motors remained staid. The UV segment has a long pipeline of new model launches and refurbishments over the next 12 months - Tata *Safari Merlin*, Toyota *Avanza*, Maruti Suzuki *RIII*, Renault *Duster*, M&M *Korando*, Audi *Q3* and BMW *X3*. Further, a new compact UV segment is expected to emerge with the launch of the Ford *Ecosport* and M&M's *mini Xylo* in early 2012. With these launches, the UV segment is expected to get further fragmented based on new price points.

Segment-wise Trends: Multi Passenger Vehicle Segment

Chart 7: Trend in Multi-Passenger Vehicle Sales



Source: SIAM, ICRA's Estimates

Table 8: Trend in Market Share in Multi-Passenger Vehicle Segment

OEMs	FY10	FY11	Q3 FY11	Q4 FY11	Q1 FY12	Q2 FY12	YTD FY12
Maruti	67.4%	75.2%	77.0%	73.5%	70.9%	61.1%	64.2%
Tata Motors	32.6%	24.2%	22.8%	24.7%	21.9%	26.3%	25.1%
M&M	0.0%	0.4%	0.0%	1.6%	7.0%	12.5%	10.6%
Force Motors	0.0%	0.1%	0.2%	0.2%	0.1%	0.1%	0.1%

Source: SIAM, ICRA's Estimates, YTDFY12 corresponds to Apr 11 to Nov 11 time period

MPV sales witness growth moderation in Q2 FY12 due to production disruptions at Maruti Suzuki

The multi passenger vehicle (MPV) segment of the domestic PV industry recorded moderation in growth rate to 11.2% in Q2 FY12 (29.2% in Q1 FY12) in light of supply constraints of Maruti Suzuki *Eeco*, the largest selling model in the segment. Other players, constituting less than 30% of the market, posted healthy volumes growth with M&M experiencing healthy ramp-up in volumes of *Maxximo* (launched in April 2011). The growth turned negative in October, largely contributed by production disruption at Maruti Suzuki. Tata Motors also reported a contraction in demand in the MPV segment.

The MPV segment, pioneered by Tata *Ace Magic,* has met with huge success catering to the latent demand for last mile connectivity to public transportation hubs in cities and towns. The people mover section has also seen a trend in increasing preference towards smaller and less expensive MUVs like *Eeco*. However, private consumption of these models is limited and most of the demand is generated from the taxi segment.

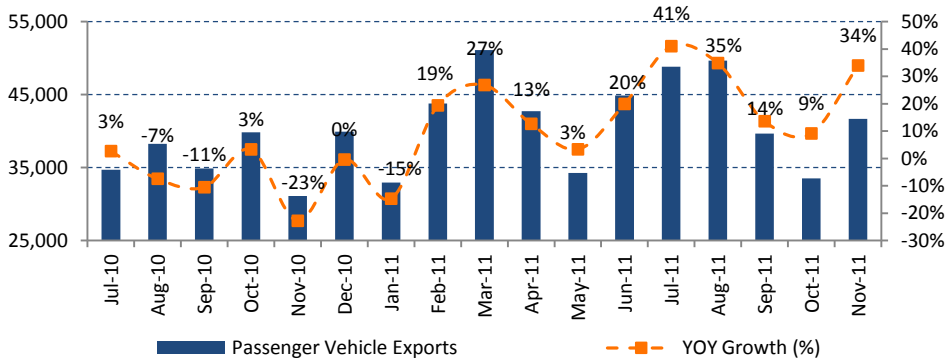
Market share of Maruti Suzuki expected to pickup; segment to see entry of new players

Notwithstanding the decline in market share, Maruti Suzuki continues to lead the pack with *Eeco* as the largest selling model. Also, the OEM is likely to regain its lost market share once regular supplies commence fully by end of Q3 FY12.

With sound demand potential, the MPV segment is expected to attract new OEMs. Chevrolet is expected to launch a budget MPV *CN-100* in July 2012 and Force Motors is expected to launch a new MPV in late 2012.

Segment-wise Trends: Exports Segment

Chart 8: Trend in Export Volumes



Source: SIAM, ICRA's Estimates

Table 9: Trend in Market Share in the Exports Segment

	FY10	FY11	Q3 FY11	Q4 FY11	Q1 FY12	Q2 FY12	YTD FY12
Hyundai	64.0%	51.2%	46.5%	43.9%	48.6%	50.9%	49.8%
Maruti	33.1%	30.4%	28.1%	24.2%	25.3%	21.6%	22.0%
Nissan	0.0%	12.5%	19.2%	26.6%	18.4%	19.8%	20.2%
Ford	0.3%	2.7%	3.5%	3.2%	4.4%	5.2%	5.1%
Tata Motors	1.5%	1.8%	1.7%	0.9%	1.8%	1.3%	1.5%
M&M	0.7%	1.0%	0.7%	0.8%	0.9%	0.8%	0.8%
Others	0.4%	0.4%	0.3%	0.2%	0.6%	0.4%	0.5%

SIAM, ICRA's Estimates, YTDFY12 corresponds to Apr 11 to Nov 11 time period

Low base and geographical diversification efforts by OEMs enable healthy growth in the exports segment

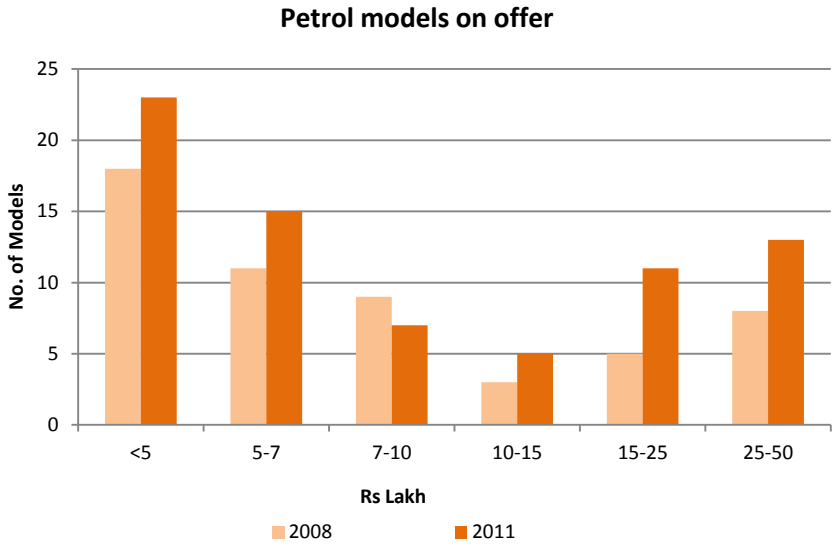
India's PV exports reported healthy 29.9% YoY volume growth in Q2 FY12. Apart from the low base of Ford *Figo* and Nissan *Micra*, export volumes were supported by greater focus of Hyundai towards the export market, given the weak demand situation on the domestic front. However, Maruti Suzuki, the second largest car exporter from India, saw dwindling of its export numbers in Q2 FY12 and Oct 2011 because of production disruption at its Manesar factory where A-Star is produced. Fluctuations in YoY export volumes have largely mirrored the domestic/export sales mix adopted by Hyundai. The OEM had diverted production towards the domestic market in Oct 2011 in lieu of the festive season, but resumed focus on overseas sale in Nov 2011

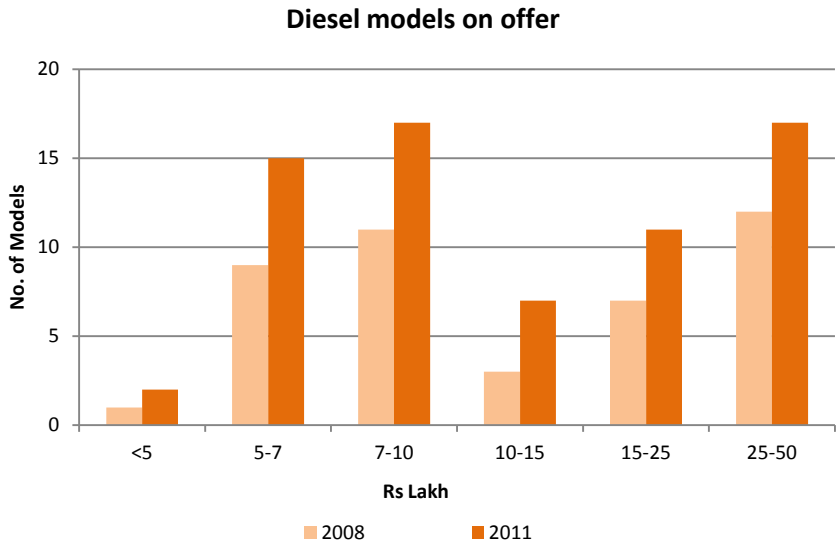
While sales to Europe have remained subdued, much of the export growth has been on account of OEMs exploring new markets. The demand outlook in Europe (India's largest car export destination) is expected to remain weak post discontinuation of scrappage incentive schemes, besides macro-economic weakness plaguing many European nations. This has prompted OEMs like Maruti Suzuki and Hyundai to diversify geographically by adding new non-European markets. Also, Nissan, which was earlier exporting *Micra* mainly to Europe, is expected to start exports to West Asian and African countries.

More OEMs expected to jump on the export bandwagon

Although competition from other exporting nations like Thailand, China, Mexico, Argentina and Brazil is high, competition amongst exporters from India is limited, given the few market participants. This is expected to change with multinational OEMs exploring opportunities to develop India as their global low cost manufacturing hub.

Model clutter highest in entry level and premium car segments; growing preference for diesel-powered vehicles in the domestic market





Source: ICRA Research

Base model ex-showroom Delhi prices considered

The current distribution of petrol-based PV models across various price points shows that vehicle clutter in the lower and upper price bands is the highest with the middle price band being the leanest. The hatchback and mid-size car segments, which together account for over 90% of the PV demand in India, have attracted the maximum attention from OEMs who offer multiple models at close price points. Most of the players in the entry level PV segment have set-up full-fledged manufacturing setup in India and rely on domestic component sourcing to control costs. On the other hand, most of the models on offer in the upper-end of the price bracket are imported either in Semi-Knocked-Down (SKD) form or as Completely-Built-Units (CBUs). Since overall investment required for import/partial assembly is limited, foreign OEMs have flooded the luxury and premium car and UV segments with their global model range. This is reflected in the fact that out of a total of 162 PV models on offer in the domestic market at present, 61 vehicles have a price tag of over Rs 50.0 lakh.

Price-wise distribution of models in the diesel space is somewhat less symmetrical owing to the spread of UVs across multiple price points which remain diesel-powered predominantly. Also, considering that diesel variants are typically priced about Rs 1 lakh higher than the petrol variants, the chart above showing diesel model distribution is skewed towards the right as compared to that of petrol. While the number of options available to Indian customers has increased at a rapid pace over the last three years, the trend has been more marked in diesel. This is in line with the increasing preference for diesel-powered vehicles in India, given the widening price differential between diesel and petrol.

Distribution Network – OEMs' attention rising towards network expansion

Dealerships, being the face of OEMs, play a very crucial role in automotive value chain in terms of delivering differentiated customer experience throughout the vehicle ownership cycle. While historically, involvement of dealerships was restricted to sale of vehicles and their servicing, operationally they have evolved as a one-stop-shop offering services such as vehicle financing, insurance, road side assistance and pre-owned vehicle purchase. Needless to say, OEMs undergo a considerable due diligence while appointing new dealers, looking into myriads of factors like demand potential in the town/city, number of existing dealerships, location of the dealership, financial muscle of the dealer to invest in infrastructure and raise working capital etc. While expanding distribution network is critical for OEMs to increase sales volumes, they are also faced with the conflicting objective of ensuring dealer viability since increasing concentration in a given territory curtails the catchment area of a dealer.

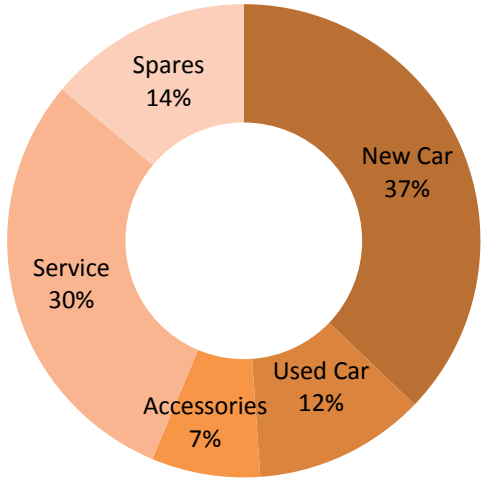
With dealership density in metros and Tier-I cities nearing saturation, much of the future growth is expected to come from Tier-II and Tier-III cities. In place of operating full-fledged dealerships in these cities, OEMs have resorted to opening extension counters that act as satellites to main dealers in cities. The larger players in the domestic market – Maruti Suzuki, Tata Motors and Hyundai – currently have over 50% of their outlets in semi-urban and rural locations, and thereby have a natural head start on this aspect. Nevertheless, network expansion plans of new entrants too remain aggressive with their eye on Tier-II and Tier-III cities. Retail outlets of luxury car makers are also on the rise with new brands like Aston Martin, Ferrari, Maserati and Bugatti making their presence felt in metros and existing players like Mercedes, BMW and Audi expanding to Tier-I cities.

Table10: OEM-wise retail Outlets

	Cities covered	Existing Network	Expansion plans
Maruti	643	970	2000(2015)
Hyundai	290	336	340 (2011 end)
Tata Motors	194	254	300 Nano specific outlets, 100 outlets for UVs
GM	NA	242	300 (2012)
Honda	77	125	150(2012)
Toyota	NA	152	NA
Ford	100	170	NA
Volkswagen	57	71	NA
Nissan	30	32	100 (2013)
M&M	161	180	NA
Mercedes	28	59	65 (2012)
BMW	NA	22	40 (2012)
Audi	NA	13	25 (2012)

Source: Company Releases, Media Articles, ICRA Research

Segment-wise profit contribution of a dealer



Source: ICRA Research

While demand for new dealers is high, heavy overhead costs and pricing pressures from OEMs has stalled the influx of many new entrepreneurs in the dealership business. Supply-demand gap has resulted in churn in dealership networks, with few instances of dealer poaching by relatively new entrants. In a bid to keep the network franchisees interested and ensure dealer viability, margins offered by foreign OEMs to their dealers is relatively higher, given the low initial volumes. Also, absence of service load and spare sales (contributing over 40% to gross margins of a typical dealer) in the initial start-up period, has prompted new OEMs to shore up dealer profitability by other ways like providing working capital support.

Trimming down new product development costs becomes an imperative

The design, engineering and development cost of building a new PV model in developed markets, having no carry-over components and built from scratch, starts at around USD 1 billion. This is not surprising since an automobile is a complex machinery bringing together thousands of both functional as well as safety-critical parts that must function reliably as a system over an extended period of over 10 years while meeting the extant safety and emission norms. These investments are generally spread over a time horizon of 2-4 years (*depending on the manufacturer and model*), representing the duration between conceptualization and mass production. The development cycle of a new PV model involves multiple phases including market survey, feasibility study, design, engineering, development and validation of individual parts, assemblies and fully-built vehicles. The process involves three broad cost elements viz., cost of manpower, cost of tooling and cost of plant & machinery (*listed in increasing order of cost burden*). While the scope of reducing expenses varies across cost heads, PV OEMs are increasingly showing the proclivity to focus on all three to maximize benefits. The various levers accessible to OEMs to improve product development efficiency are given in **Table 2**.

Table 11: Avenues for PV OEMs to reduce new model development costs

Cost reduction measures taken by PV OEMs during new product development	Examples in Indian context
Deploying common platforms to produce more than one vehicle out of largely the same development investment	**Maruti Suzuki** - (a) *Swift* and *Swift Dzire;* (b) *Alto, WagonR* **Tata Motors** - *Indica*, *Indigo* **Nissan** - *Micra, Sunny* **Toyota Kirloskar** - *Liva, Etios*
Use a common engine and other parts across a broad range of models	Same diesel engine deployed in: – Maruti Suzuki *Swift*, Tata Indica *Vista*, Fiat *Grande Punto* – Maruti Suzuki *SX4*, Tata Indigo *Manza*, Fiat *Linea*
Build and launch global platforms across a much wider spectrum of the world market	– Global launch of the Suzuki *Swift* in Japan, Europe and India – Toyota *Etios* and *Liva*, launched first in the Indian market, now planned to be exported to South Africa – Nissan *Micra* available in multiple geographies including India, China, Japan, Australia, Canada, USA, Latin America
Design outsourcing to low cost destinations	Following companies have design and research centres in India: General Motors, Hyundai, Ford, Honda, Suzuki
Increasing use of digital prototypes to cut down product development cycle time	Used by most PV OEMs in India with a varying degree

Source: ICRA Research

While reducing product development costs is a focus area across global OEMs, it is ought to be more so in the Indian context given the sharp rise in competitive intensity in the PV industry over the last two years. The growing competitive intensity has persuaded OEMs to increase the rate at which they introduce new models in the domestic market and upgrade existing ones (while leveraging the same platforms). This has necessitated OEMs and component manufacturers to incur reasonably large capital investments on a recurring basis towards new product development. The strong volume growth recorded by the PV industry in the past had allowed the market to assimilate the flurry of new model launches, while giving reasonable returns to OEMs (barring few exceptions). However, since the frequency of new model launches in the PV market has been particularly high over the last two years, it remains to be seen to what extent OEMs can protect their profitability in the current environment of sluggish demand. In ICRA's view, the likelihood of OEMs' profitability erosion seems high over the short term given the large supply push having happened at a time when demand environment in the PV market is not conducive. That said, the present demand-supply mismatch may be considered to be incidental since the new models launched in the recent past were conceptualized several years in advance assuming the trend in strong growth of the PV industry to be sustained at the time of launch. Thus, although new product

development plans of OEMs are influenced more by medium to long term growth prospects of a market or segment, their ability to improve efficiency of development expenditure remains a critical control variable which could allow them to mitigate the adverse impact of cyclical dips on profitability. Creditably, Indian OEMs like Tata Motors and M&M have demonstrated their ability to engineer new products at significantly lower costs as compared to their global counterparts. In ICRA's view, a cut-to-bone product development approach encompassing themes of platform sharing (engine level and vehicle level), design outsourcing to low cost destinations, increasing the use of digital prototyping and adopting reverse engineering techniques to cut down the time spent on iterations during design, development and testing is expected to occupy centre stage in the times to come.

Automotive Manufacturing Clusters in India – New ones in the making

The benefits available to the automotive industry arising from agglomeration of manufacturing facilities in concentrated spatial hubs are undeniable. These benefits, the outcome of commonalities and complementarities in the clusters of interconnected companies, include improvement in supply chain management, greater investment economies and lower logistics costs all combining to generate improved productivity and competitiveness for companies constituting the cluster. India's automotive industry is concentrated across three major regions – the National Capital Region (NCR) and Uttaranchal, with OEMs such as *Maruti Suzuki, Honda Siel, Hero MotoCorp* and *Bajaj Auto*; the Chennai-Hosur-Bangalore region, with OEMs such *as Hyundai, Toyota, Ford, Ashok Leyland* and *TVS*; and the Pune-Nashik-Aurangabad region, with OEMs such as *Tata Motors, Bajaj Auto, Mahindra & Mahindra* and *Volkswagen*. Each of the above hubs contributes over 30% to the total automotive revenues, indicating existence of a well-balanced eco-system of automobile companies dotting these regions. In addition, there are two other relatively smaller hubs located in and around Pithampur in Central India and Jamshedpur-Kolkata in Eastern India, whose contribution to automotive industry revenues remains moderate.

Table 12: Automotive hubs in India and key OEMs present

	North	South	West	East	Central
Key Regions:-	**NCR and Uttaranchal**	**Chennai-Hosur-Bangalore**	**Pune-Nashik-Aurangabad**	**Jamshedpur-Kolkata**	**Pithampur**
PV	Maruti Suzuki, Tata Motors, Honda, Sonalika	Hyundai, Ford, Toyota, Hindustan Motors, Mahindra Reva, **Renault-Nissan**, **BMW**	General Motors, M&M, Fiat, Tata Motors, Skoda, **Audi**, **Volkswagen**, **Mercedes Benz**	Hindustan Motors	
2W	Honda, Suzuki, LML, Yamaha, **Hero MotoCorp**, **Bajaj Auto**, **TVS**	Royal Enfield, TVS	Bajaj, Mahindra Two Wheelers		Mahindra Two Wheelers
CV	SML Isuzu, **Tata Motors**, **Ashok Leyland**	Volvo, Ashok Leyland, Tata Motors, **Scania**, **Daimler Trucks, ALL-Nissan**	Force, AMW, **Mahindra Navistar**	Hindustan Motors, Tata Motors	Volvo-Eicher, Hindustan Motors, Force, MAN Force
3W	**M&M**	TVS	Piaggio, Bajaj Auto, Atul Auto		
Tractors	ITL, New Holland, TAFE, Escorts	Same-Deutz Fahr, TAFE	John Deere, M&M		TAFE

Source: ICRA's Research; Company names indicated in **Blue font** *represent greenfield investments made over last five years*

Typically, to set-up an integrated car manufacturing facility encompassing press shop, weld shop, paint shop, machine shop and assembly shop with 200,000 vehicle manufacturing capacity, an investment outlay of around Rs. 4,000 Crore is required. Due to such large investment involved, choosing an appropriate manufacturing location is a vital decision element for any OEM as it could influence the **payback period**[1]. Factors which generally go into such decision making for OEMs include ease and price of land

[1] *The payback period for a PV OEM making such investments could be in the range of 7-10 years depending on the capacity utilization, profitability and fiscal incentives offered by the state.*

available, strength of infrastructure facilities (including road, rail, port connectivity; power availability), availability of manpower, existence of an established vendor base, besides extent of fiscal incentives offered by the state in terms of excise and income tax holiday. Over the last five years, the bulk of the greenfield investments by PV OEMs in India have occurred in the Southern and Western regions with the five PV OEMs viz., Renault Nissan, BMW, Audi, Volkswagen and Mercedes Benz incurring an aggregate capex of around Rs. 9,000 Crore within existing clusters in Tamil Nadu and Maharashtra (Refer **Table 1**).

While cluster-based growth has its merits, the existing clusters are bound to hit a ceiling over time in terms of their ability to make available to the industry factors of production (including land and labour) in adequate measure. Already, there are signs of new automotive clusters emerging in India. Since the year 2007, Uttaranchal has emerged as an alternate manufacturing hub in North India becoming home to various 2W and CV manufacturers. Gujarat too, which already had names such as *General Motors* (at Halol) and *Asia Motor Works* (at Bhuj), has added *Tata Motors* (at Sanand) over the last one year, besides evincing interest from other players such as *Ford, Peugeot* and *Maruti Suzuki* for greenfield investments. Although not necessarily a trigger in itself, the fact that automotive demand is increasingly tending towards becoming pan-India (*as opposed to being largely concentrated in urban centers in the past*), is an added enabler to the process of geographical dispersion of automobile clusters. From an OEM's standpoint, having a presence in multiple clusters allows it to partially hedge its risks from possible loss in production due to external events such as labour strike, social agitations or natural calamities that may inflict a particular region. Overall, ICRA expects India's progress towards becoming a global automotive hub to encourage the emergence of new automotive clusters, due to eventual capacity constraints in existing ones; however, the ability of state governments to create investor-friendly environment will be a necessary condition for the above trend to sustain.

Free Trade Agreements – Changing dynamics of auto component sourcing

India has entered into Free Trade Agreements (FTAs), Preferential Trade Agreements (PTAs), Regional Trade Agreements (RTAs) and Comprehensive Economic Partnership Agreements (CEPAs) with several nations to expand the trade of goods and services with its partner nations and encourage investments. Some of the key regions/ countries with whom India has signed such agreements include ASEAN, Thailand, Singapore, Japan and South Korea, with more such engagements in the offing including the ones currently being negotiated with the European Union (EU) and China. In fact, India has signed the second highest number of trade treaties with other nations (after Singapore) in a bid to gain broader market access for its goods and services and to seek fresh investments. The theoretical underpinnings advocating trade agreements between nations are based on expected benefits in the form of increase in trade volumes, achievement of economies of scale and other improvements over the long run for consumers and producers alike. Invariably, however, the government's efforts towards signing of FTAs is accompanied by scepticism shown by institutions and industry groups with regard to possible loss of domestic industry's competitiveness, rise in unemployment and dumping of products by exporting countries. While these concerns are not completely unfounded, there are generally adequate safeguard provisions for vulnerable product categories, besides negative lists to mitigate the potential adverse impact of these agreements on the domestic industry.

Amongst India's existing FTAs with various nations, the ones with Thailand, South Korea and Japan are likely to have a greater impact on the component sourcing decisions of PV OEMs in India, given the more advanced automotive industry in these counties. For OEMs, these FTAs open up opportunities to go for global sourcing of parts and reduce component costs while avoiding fresh local investments (in case same-design component is already being manufactured overseas); but for component manufacturers, FTAs create formidable pricing challenge due to lowering or elimination of customs duty which gets further accentuated due to higher operating costs in India in the wake of infrastructure inefficiencies, higher cost of power, higher effective taxes and inflexible labour laws. India continues to be a net importer of auto components with its trade deficit for automotive components having expanded to USD 5.0 billion in 2010-11 from USD 210 million in 2004-05. This is attributable to faster growth of imports and to some extent erosion of the traditional advantage of low cost of production enjoyed by Indian companies against competition from other low cost countries like China, Malaysia, Thailand and South Africa, which has got accelerated by phased lowering of import duties by India. In fact, imports of auto parts (*such as tyres, batteries, wheels, chassis components, engine valves etc*) from China have ballooned at a brisk rate over the last several years (even without an FTA) with their increasing pervasiveness in the domestic replacement market as well as greater acceptance by domestic OEMs in the CV and 2W segments. The trade deficit could widen further if the proposal to cut down the duties currently being levied on import of Completely-Built-Units (CBUs) from EU gets agreed upon as part of ongoing negotiations for the India-EU FTA. Even FTAs

between other nations (where India is not a party) could have significant implications for the growth of the Indian industry. For instance, the proposed FTA between Korea and the European Union (EU) has prompted Hyundai Motor India Limited to suggest that the company may look to shift part of its production meant for export to the EU from India to Korea – implying lower new capacity creation in India. In ICRA's view, while FTAs may bring down the cost of select components for PV OEMs, their domestic supplier base gets exposed to risks related to possible loss of business from OEMs and lower incremental growth opportunities.

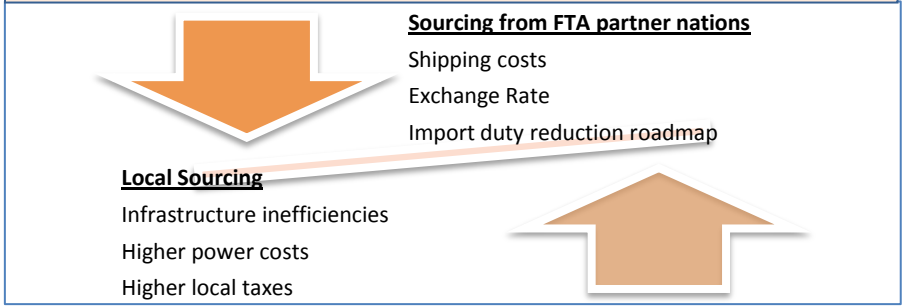
Existing scenario	Implications
PV OEMs already source select components from a single location (Thailand/ India/ Japan etc) in cases where: (a) The component has high design complexity such as integrated hub-bearings, toe-correct suspension bushes, various electronic sensors (b) Manufacture of the component requires high tooling investments which may not be viable to replicate across multiple locations	FTAs may further support this process and contrary to the intended objective of encouraging investments in India, may rather maintain status quo and discourage technology transfer
Developed nations are persuading India to accept and implement global technical standards, UNECE 1958 and 1998 (termed WP-29 which is concerned with harmonization of vehicle standards in safety, emissions, anti-theft etc)	India's non-adherence to these standards has acted as a non-tariff barrier so far. India's eventual compliance may increase competitive advantage of European OEMs/ suppliers vis-à-vis Indian players

Existing Import Duty Structure

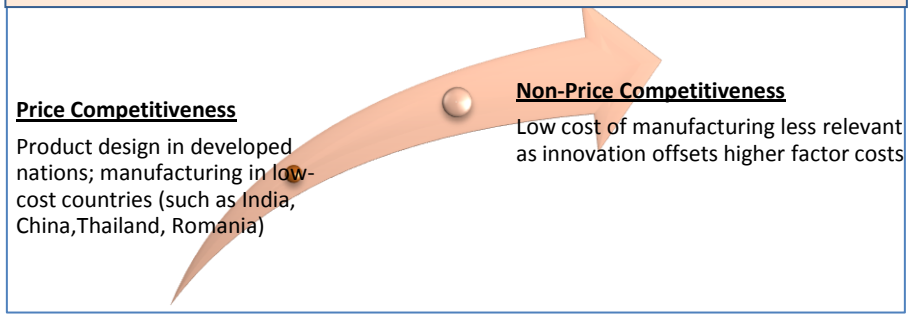
	Motor Vehicles	Auto Parts/ Assemblies
India	110%	7.5-30%
Thailand	80%	30%
ASEAN	30-80%	0-30%
EU (for India & ASEAN)	6.5%	0%
EU (for others)	10-22%	3-4.5%

Source: ICRA's Research, IHS Global Insight

Key cost considerations for OEMs in sourcing decisions



India must endeavour to enhance its non-price competitiveness in automotive sector as increasing global free trade could dismantle the traditional price competitive plank



In this context, the Indian auto industry must realign its priorities towards building and optimizing capacities, focusing on continuous improvement, absorbing advanced technologies, adopting latest manufacturing processes and building R&D competencies. Only then, the Indian auto industry could shift its comparative advantage from being a low cost manufacturing location (which is facing challenge from other low cost nations) to becoming a centre of product and process innovation, and in the process achieve sustainable growth riding on non-price competitiveness.

Supply Chain – Force majeure events causing supply-side stress

The current flood situation in Thailand is a second reminder this year of the susceptibility of world supply chains to natural calamities, close on heels of the earthquake and tsunami that hit Japan in March 2011. As if demand-side stress was not enough, these force majeure events have made matters worse for the Indian PV industry, particularly for Japanese OEMs like Toyota Kirloskar and Honda Siel who had launched new models recently, some of whose components were being imported from Japan/ Thailand. Honda Siel had recently returned to full production after the catastrophe in Japan had forced its plant to shut down. Now with floods in Thailand, Honda Siel has stopped taking bookings for some of its models due to unavailability of parts. Toyota Kirloskar too has started to have production issues owing to the floods. The production at Tata Motor's plant at Thailand which makes pick-up truck *Xenon* in partnership with a local company has also got disrupted due to floods.

Thailand had become a hub for Japanese PV OEMs in the 1980s and 1990s, partly due to yen appreciation during that period which hampered export competitiveness of Japanese OEMs influencing them to invest outside of Japan towards building production facilities in consumer markets. Today, as a measure of Thailand's importance to the global automotive supply chain, the flooding there has forced Toyota globally to reduce output in factories in Indonesia, Japan, Malaysia, North America, Pakistan, the Philippines, South Africa and Vietnam. Honda, the OEM most affected by Thai floods, has also slowed production at factories in several countries. Although foreign companies affected by floods are not expected to leave Thailand en masse given its well-developed ecosystem of manufacturing industry and relatively lower cost of manufacturing, PV OEMs may try to balance their future expansion so that they do not have supply chain dependence on a single market. However, such decision making may not be easy with multiple forces pulling in different directions – on one hand, there is the consideration of reducing supply chain dependence on select markets; on the other, there is the conflicting objective of pushing up scale economies which inevitably requires investment congregation. This apart, OEMs may also need to re-evaluate the 'just-in-time' and lean manufacturing principles whose associated risks show-up during such acts of nature. In ICRA's view, in case OEMs that have suffered damage due to flooding in Thailand do eventually decide to augment their supply chain and develop alternate suppliers in new locations, countries such as India, Indonesia and **Vietnam**[2] could be strong contenders for these fresh investments by virtue of their large market size and low cost characteristics.

Move towards greater content localization

Table 13: Indigenized content in small-car launches

	% Localisation
Ford Figo	85
Honda Brio	80
Nissan Micra	85
Toyota Liva	70
Volkswagen Polo	70

Source: Media Articles

Over the years, many of the international OEMs in India have had a volatile earnings profile in India due to low economies of scale, high import content and exposure to foreign currency fluctuations. Now, with most OEMs targeting the highly competitive small-car segment, thrust on localisation of key components forms an integral part of international OEMs' strategy to reduce costs. More particularly in the small car segment, where competitive pressures are relatively higher compared to other segments. Typically, localization levels are low during the launch phase and increase gradually depending on the success of the model and volume ramp-up. While localisation appears to be a straightforward route in achieving cost competitiveness, it is only meaningful at large volumes since it involves large investments in capacity building. Besides cost advantage arising from lower duties and logistics costs, localization also helps in reducing earnings fluctuation on account of currency volatility. In terms of technological positioning, although the Indian auto component manufacturers may lack design know-how in certain product categories, their overall capability in manufacturing auto components, with consistent quality and reliability is now well acknowledged by global OEMs. This is evident from the trend of increased localisation levels in most new models (Refer **Table**). Additionally, most global auto players are setting up capacities to locally develop and manufacture engines & transmissions in India with vendor development forming a key part of their strategy, something which was amiss earlier.

[2] *Both Indonesia and Vietnam had attracted more foreign direct investment than Thailand in 2010 and may attract more investment going forward. Indonesia has a large population and its domestic demand too is quite strong. The two countries account for more than half of the ~600 million people in the countries that comprise the ASEAN region.*

Trends in JV/Technology Alliances

Table 14: JVs in the Automotive Space in India

JVs	Segment	Status
M&M-Renault	Passenger Cars	Called off due to disagreements on product designing & customization plans
TML-Fiat	Passenger Cars	After a dismal performance, Fiat is planning to open exclusive dealers
Bajaj-Renault	Passenger Cars	No development on the small car front so far
Hero-Daimler	CVs	Called-off in the initial stage itself
Force-MAN	CVs	MAN aims to go solo in India
Bajaj-Kawasaki	Two Wheelers	Strategy related issues
TVS-Suzuki	Two Wheelers	Strategy related issues

Source: ICRA Research

Table 15: JVs in the Auto Component Space in India

JVs	Segment
Motherson Group-Kyungshin	Wiring Harness
JBM Auto-Magnetto Automotive	Sheet Metal Parts
Rico-Continental	Braking Systems
Sona Koyo-JTEKT Japan	Steering Systems
Gabriel-Magnetti Marelli	Dampers
Hero Group-Kiriu Corporation	Casings – Brake drums & discs

Source: ICRA Research

In line with some of the other developing markets, the regulatory environment in India till 2000 required foreign OEMs to partner with local companies to enter the Indian automobile sector. However, with Government lifting the regulatory restrictions and allowing 100% FDI, most of the OEMs over the last decade have opted to directly enter the Indian market. Despite a free market environment, some of the OEMs have still pursued the JV route and formed alliances with local players. Such JVs were forged with the strategy to leverage on the product and technological capabilities of the foreign OEMs and the strengths of local player in terms of their understanding of the domestic market. The performance of JVs in the OEMs space has been a mixed bag as some of them have parted ways and others have restructured their business plans. Disagreements on product customization, localization strategies and issues related to dealership & service network have been some of the key factors that have impacted the success of these JVs. In contrast, foreign OEMs have preferred bringing in their global auto component suppliers in the Indian market, through tie-ups/JVs with local companies. As a result, JVs in the auto components space have become a prominent trend in the industry as majority of the domestic vendors now have JVs with international suppliers, servicing the foreign OEMs.

Additionally, OEMs have also resorted to technology/platform sharing alliances to fill gaps in their product portfolios. Some of the OEMs are also sharing manufacturing facilities. Maruti Suzuki's technology sourcing for diesel engine from Fiat, Renault-Nissan (production sharing) and GM-SAIC (plans to introduce platforms from SAIC's portfolio) are some of the examples of recent collaborations in the Indian automotive space. With increasing competitive pressures and reducing customer ownership cycle, OEMs need to regularly launch new models and upgrade existing ones to remain competitive. In response to such a scenario, such alliances are likely to gain momentum as OEMs aim at rationalizing their investments and maximizing reach through technology, manufacturing and distribution. However, at the same time, consolidation in the form of entire companies being acquired as has been seen globally in unlikely in the Indian context.

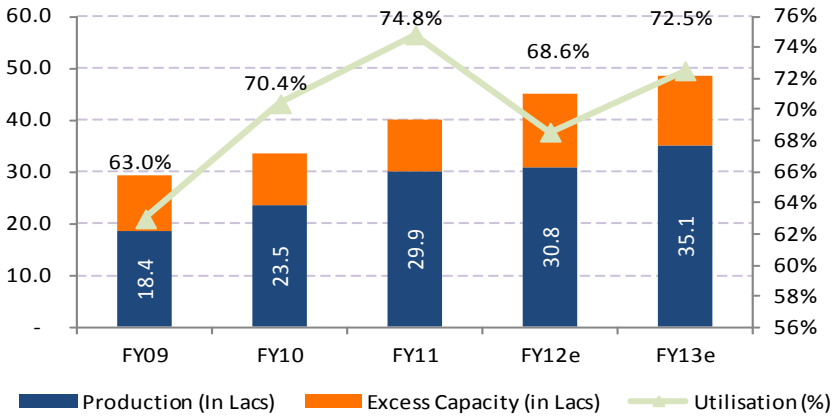
Capacity Expansion & Investment Plans

Table 16: Recently Greenfield project announcements

OEMs	Expansion Plans
Maruti Suzuki	New Greenfield manufacturing site in Gujarat
Peugeot Citroen	Has identified Gujarat for setting up a manufacturing facility; Capacity/Investment – 170,000 units/$ 1billion
Ford	Planning to put up its second integrated vehicle & engine manufacturing facility in India Capacity/Investment - $ 1billion

Source: ICRA Research

Chart: Trend in Capacity Utilization in the PV segment



The strong growth prospects and favourable demand drivers have attracted most of the international OEMs to emerging markets. Although China remains a favourite destination given the sheer size and rapid growth that the market has witnessed, India too has become a centre of attraction for most OEMs. As a result, most of the new entrants have set up base in India and capacity creation has been at the core of each OEM's strategy for the Indian market. Over the past 3-4 years, many of the existing OEMs have expanded capacities and new entrants have set up Greenfield projects. At the end of March 2011, India had a capacity to manufacture ~4.0 million vehicles which is expected to be scaled up to 4.8 million units by 2012-13. While incumbents such as Maruti Suzuki, Tata Motors (capacity at Sanand) and M&M (at Pune) have added capacities, over 50% of the capacity expansion has come in from new entrants such as VW (Pune), Renault Nissan (Tamil Nadu) etc. Recently, Peugeot Citroen and Ford have also finalized their plans of setting up Greenfield manufacturing sites in Gujarat, which is gradually emerging as a new automotive hub. Although the manufacturing facilities are largely flexible, majority of capacity expansion in India has been done keeping in mind opportunities in the small car segment and exports potential. In the near term, capacity utilization levels are likely to drop given the slowdown in the industry and impact of recently added capacities. However, we expect utilization levels to inch upwards to 70%+ levels from FY13 onwards. The utilization levels may however differ across OEMs as demand for certain models/platforms could be significantly different from other models in the market. Such a scenario is common during the launch phase for new models or during changing trends such as the spike in the demand for diesel cars in India at present.

Emerging markets are more distinct than common….

Over the past decade, Brazil, Russia, China and India (commonly referred as BRICS) have emerged as the bellwether of the global automotive demand. Led by China, the BRIC countries together contributed nearly 30% to the global automotive demand in 2009 compared to just over 20% in 2007. Favourable macro-economic indicators, growing middle class population, rising disposable income levels and last but not the least extremely low penetration levels have propelled automotive demand in these markets. As a result of their growing importance in the global automotive landscape and stagnating demand in developed markets, virtually all the multinational OEMs and auto component suppliers now have presence in emerging markets. Besides strong domestic demand, emerging markets also offer opportunities for OEMs to source auto components, set-up global R&D back offices and manufacturing footprint in these markets.

In contrast to China, India has clearly emerged as a manufacturing hub for low-cost small cars owing to its scale and significant competencies in the small car space. It also benefits from lower development cost and an improving auto component manufacturing base. The trend in favour of higher fuel efficiency and smaller cars in developed

markets also augurs well for India. For foreign OEMs, India has also been at the forefront when it comes to outsourcing capabilities particularly in the R&D space owing to its vast skilled manpower base and expertise in the IT domain. Many of the foreign OEMs have chosen India as a destination for their global R&D centres. The table below illustrates the key distinctions among BRIC countries from the perspective of the PV industry.

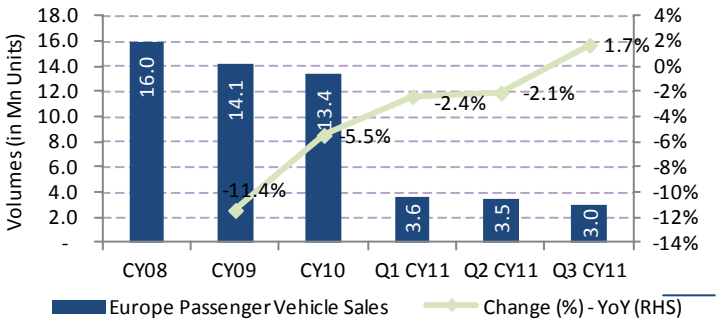
Table 17: Comparison between Emerging markets

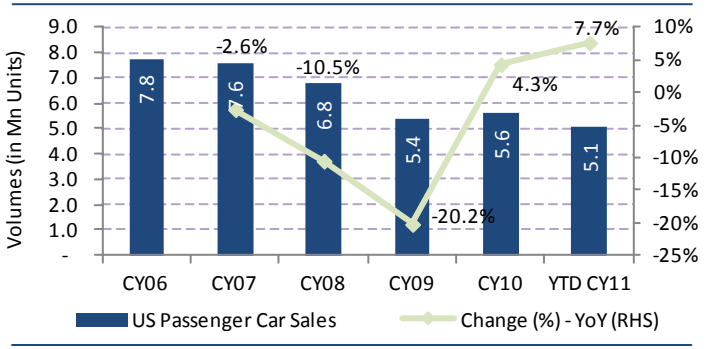
	Brazil	Russia	India	China
Passenger Car Production*	2.82 million	1.21 million	2.81 million	13.89 million
Vehicle Penetration	158	188	13	56
Industry Structure	In terms of market segmentation, Brazil is similar to India; hatchbacks account for over 60% of volumes	Consumer preference in Russia largely mirrors that of developed markets, particularly US; market is dominated by SUVs and sedans	Unlike other emerging markets, India is predominantly a small car market 70% of the market is dominated by hatchbacks	Unlike India, Chinese market is dominated by sedans, accounting for over 60% of volumes
Ownership Structure	Is predominantly dominated by foreign OEMs, which control over 80% of the market; US and European OEMs have been the front runners	Post the meltdown, there has been a significant shift in market share; share of imported vehicles have dropped substantially and market is now well spread out between local OEMs, foreign OEMs and imports	Indian market is dominated by foreign OEMs; Front runners dominate the market with top 3 players accounting for over 70% of the volumes; Suzuki dominates the market with over 45% share However, new entrants are now threatening the incumbents with aggressive launches	Due to ownership constraints, foreign OEMs are present in the Chinese market through JVs with local companies Nearly ~50% of the market is dominated by foreign JVs Market share is relatively fragmented among players
Regulatory Environment	Considered to be one of most matured markets among other emerging markets	Deregulation happened somewhere in the late 90s; offlate there has been increase in duties on imported cars	With 100% FDI, entry barriers for setting up operations in India are low State Govt. also offer additional incentives	China has relatively stringent regulatory environment; JV route and local sourcing conditions prevail
Exports Potential	Despite competitive manufacturing capabilities, most of automotive production is dedicated to domestic demand; Less than 20% of production is exported and majority is to nearby Latin American countries	Exports potential from Russia is currently negligible given the limited capabilities in auto component supplier base and manufacturing; Most foreign OEMs are relatively new entrants in Russia	Exports contribute 15% to the overall industry size Emerged as a small car manufacturing hub Competitive manufacturing skills, favourable government policies, attractive domestic market and improving vendor base are together supporting exports potential	Despite massive domestic market, which has allowed OEMs to achieve economies of scales, exports still account for a small portion of total production; Robust domestic demand has kept OEMs busy meeting local demand
Auto Components Industry & Localisation	With foreign OEMs being present for decades, Brazil has relatively higher level of localization	Localisation levels are relatively low in Russia; majority of operations are in SKD/CKD form; components are mostly imported Most OEMs have no R&D presence	Auto component industry has gradually evolved and developed capabilities in various areas India is also serving as an R&D outsourcing destination for OEMs	With competitive costs base and technology absorption, it has developed a large auto part exports base Most OEMs have established strong localization capabilities

*Source: ICRA Research; Industry Data * Source: International organization of Motor Vehicle Manufacturers (2010)*

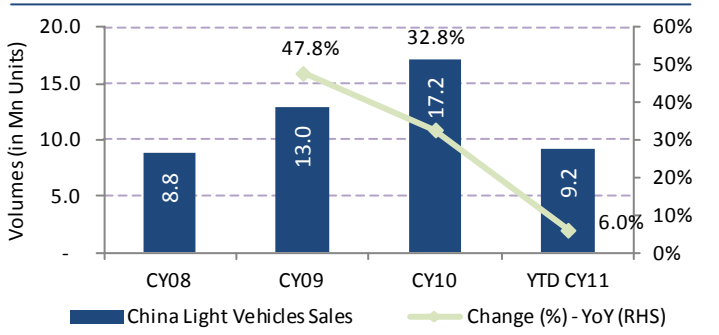
Global Passenger Vehicle Sales Trend

Trend in Passenger Vehicle Sales in Europe





Source: Wards Auto, ICRA Estimates



Mixed trends are emerging across markets; while U.S. and emerging markets are growing; macro-economic headwinds in Europe are weighing on demand

European markets continue to witness stagnating demand: The demand for passenger vehicles in European regions continues stagnate amid steadily weakening macro-economic outlook and impact of scrappage schemes which fueled demand post the downturn. With the exception of Germany which has posted a growth of 10% till YTD, most of the major European markets (UK, France, Italy and Spain) continue to witness a declining trend in sales. Unlike US, where OEMs considerably rationalized excess capacity after the financial crisis, European OEMs, particularly in Western Europe face problem of overcapacity. Given the uncertain macro-economic scenario, consumers are likely to postpone their purchases for some time to come, resulting in a weak demand in the near term.

Recovery underway in the US on back of low base: In contrast to the European markets the demand for passenger vehicles in the US has been steadily recovering after contracting sharply post the meltdown. Much of the growth is attributable to the low-base effect. During the current year, the demand for passenger vehicles has grown by 7.7% between January-October 2011. While persistently high unemployment rate and reduced economic growth forecasts weigh on the outlook, the market is likely to still remain in the growth in the near term.

Emerging markets are also losing steam: The demand for passenger vehicles has also considerably slowed down in emerging markets. China, the largest market (by volumes) and the key contributor the global auto demand is also witnessing moderation in growth in the current year In Russia too, after the meltdown when market shrunk by almost 50%, the recovery has been gradual. Increasing inflationary pressures and rising interest rates (as a result of monetary tightening) besides high-base have been the root cause for slowing sales.

Table: Impact on Global Auto OEMs

	Key Issues
US OEMs	Significant capacity elimination, funding support by the Govt. and improvement in demand has considerably improved the earning generating ability of US based OEMs; however shifting trends towards smaller vehicles require OEMs to consistently invest in new platforms and driveline technologies
European OEMs	OEMs with higher dependence on European markets are more vulnerable to stagnating demand environment in Europe; Rising commodity prices and overcapacity problem, especially in Western Europe continue to impact earnings profile of OEMs
Japanese OEMs	Japanese OEMs are recovering from the earthquake and subsequent production disruption and bottlenecks in supply chain; further strengthening of Yen against the US$ has been hurting exports earnings of OEMs exporting to the US

Source: ICRA Research

MARUTI SUZUKI INDIA LIMITED – Performance Overview in Q2 FY12

Labour troubles and unfavourable currency mar EBITDA and PAT in Q2 FY12

(Standalone)	Q2 FY11	Q2 FY12	Q1 FY12
Operating Income	**9,147.3**	**7,831.6**	**8,529.3**
Growth (%) *- YoY*	*27.0%*	*-14.4%*	*2.6%*
OPBDIT	**959.3**	**494.2**	**814.4**
Less: Depreciation	238.2	266.4	242.5
Less: Interest Charges	9.7	10.9	5.8
Other Income	135.0	117.7	180.1
Exceptional Gain/Loss	0.0	0.0	0.0
PBT	846.4	334.6	746.2
Less: Tax	248.1	94.2	197.0
PAT (Concern Share)	**598.2**	**240.4**	**549.2**
OPBDIT/OI (%)	**10.5%**	**6.3%**	**9.5%**
PAT/OI (%)	**6.5%**	**3.1%**	**6.4%**

Source: Company Data, ICRA Estimates

	Q2 FY11	Q2 FY12	Change (%)	Q1 FY12
Mini	139,765	112,848	-19.3%	122,052
Compact	64,395	44,864	-30.3%	55,651
Super Compact	25,489	20,288	-20.4%	25,095
Mid Size	5,873	4,392	-25.2%	5,517
Executive	0	54		117
Utility Vehicles	818	2,344	186.6%	1,502
MPVs	41596	37,616	-9.6%	40,749
Exports	35,718	29,901	-16.3%	30,843

Revenue Growth – In Q2 FY12, the revenues of Maruti Suzuki India Limited (MSIL) at 7,831.6 Crore reported a sharp decline of 14.4% YoY, impacted by production disruption at its Manesar plant during the September month, besides sluggish demand conditions that impacted the PV industry as a whole. The demand-supply double whammy translated into a volume decline of 19.6% YoY and 10.4% QoQ for MSIL in Q2 FY12. The decline is expected to be even more precipitous in Q3 FY12 in the wake of the labour strike which continued into October and disrupted production not only at the Manesar plant but also the Gurgaon plant of MSIL. However, we expect MSIL's revenue growth to remain healthy over the medium term, even as some market share loss seems inevitable, by virtue of its strong product portfolio, expansive distribution network and economies of scale, apart from favourable fundamental demand drivers for the PV industry.

Profitability – In Q2 FY12, MSIL reported OPBDIT of Rs. 494.2 Crore on a standalone basis, a decline of 48.5% YoY and decline of 39.3% QoQ. The decline was on account of lower revenues and unfavourable JPY movement resulting in MTM losses on royalty and commodity hedges. We expect MSIL's OPBDIT growth to remain negative in Q3 FY12 consequent to the deleterious impact of the labour strike that got resolved only by end-October 2011, relatively slower production ramp-up post the period of strike, elevated discount levels and price compensation scheduled to be offered to the vendors in Q3 FY12 (related to imported components) due to JPY appreciation in Q2 FY12 (*MSIL's indirect imports through vendors account for 14% of its net sales*). Although MSIL's OPM is expected to increase post Q3 FY12 as concerns surrounding production disruption and commodity inflation recede, the company's margin recovery to 2010-11 levels may remain restricted due to rising competition and challenging demand environment.

ICRA Ratings

Long Term	Not Rated
Short Term	Not Rated
Outlook	Not Rated

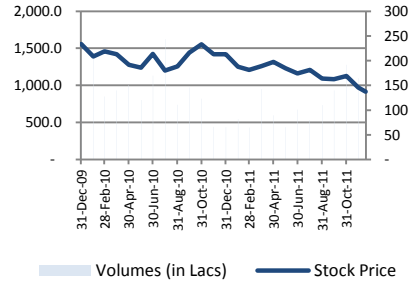
Shareholding Pattern (%)

Suzuki Motor, Japan	54.2%
FIIs	19.2%
DIIs	17.7%
Others	8.9%

Price Performance (%)

	3M	12M
MSIL	-18.7%	-33.7%
BSE Auto	-10.9%	-22.1%
BSE Sensex	-11.1%	-24.4%

Stock Movement



(Standalone)	Q3 FY10	Q4 FY10	Q1 FY11	Q2 FY11	Q3 FY11	Q4 FY11	Q1 FY12
Operating Income	7,522.0	8,485.8	8,231.5	9,147.3	9494.5	10,092.2	8,529.3
Growth (%) - YoY	*62.2%*	*31.0%*	*26.8%*	*27.0%*	*26.2%*	*18.9%*	*2.6%*
OPBDIT	1,133.9	1,107.7	792.5	960.3	901.8	1,009.7	814.4
PAT	687.5	656.6	465.4	598.2	565.2	659.9	549.2
OPBDIT/OI (%)	15.1%	13.1%	9.6%	10.5%	9.5%	10.0%	9.5%
PAT/OI (%)	9.1%	7.7%	5.7%	6.5%	6.0%	6.5%	6.4%

Source: Company Data, ICRA Estimates; Amounts in Rs. Crore

Bloomberg Code MSIL

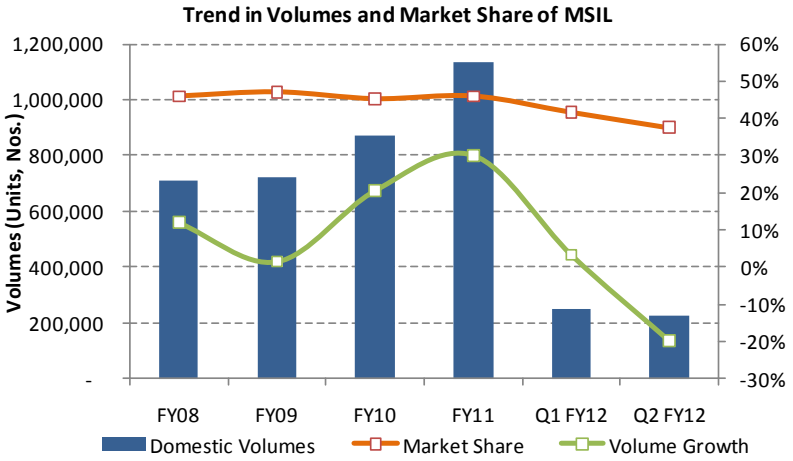
Market Capitalisation Rs.26,468 Cr

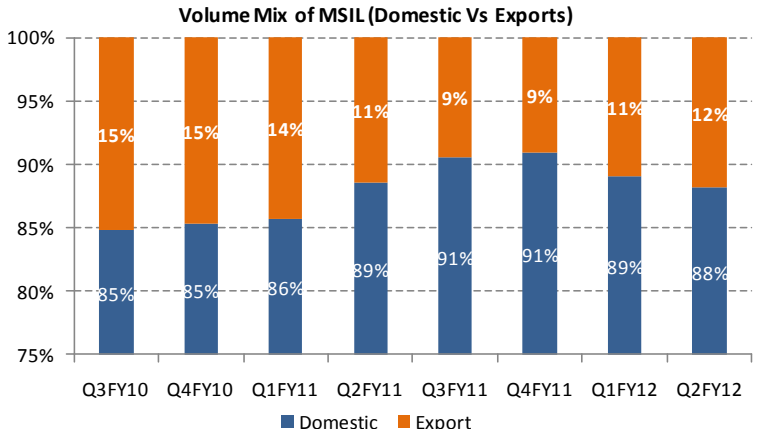
Valuations

	FY12e	FY13e
Price/Earnings	13.8	10.7
Price/Sales	0.7	0.6

Source: Bloomberg Consensus Estimates

MARUTI SUZUKI INDIA LIMITED – Operating Performance Overview





MSIL has displayed the highest rate of new product instructions vis-à-vis competition due to its larger scale in the domestic PV market

	FY08	FY09	FY10	FY11	FY12 YTD
MARUTI SUZUKI	SX4 Swift Dzire	A-Star	Ritz New Zen Estilo Upgraded SX4 Eeco	New WagonR CNG Variants- *SX4, Eeco, WagonR, Alto, Estilo* Alto K10 Kizashi	New Swift
TATA MOTORS	Indigo CS	Indica Vista Nano	Indigo Manza	Aria	
HYUNDAI	i10	i20		New i10	
FIAT		Linea	Grande Punto		
M&M		Xylo			Bolero Refresh XUV 500
VOLKSWAGEN	Passat	Jetta	Polo	Vento	
NISSAN	Teana			Micra	
TOYOTA			Fortuner	Etios	Liva
HONDA			Jazz		Brio
FORD			Figo		New Fiesta
GENERAL MOTORS			Cruz Beat		

Source: ICRA Research

Domestic Market Share

MSIL's market share slid below 40% in Q2 FY12 for the first time in its recent operating history due to disruption in its factory output caused by labour strike. Although the labour strike is over now, the market share related challenges for MSIL are unlikely to abate, given the slew of new product launches by all PV OEMs in India particularly in the small car segment, which has been MSIL's forte in the past. In our view, MSIL's ability to sustain its leadership position in the domestic PV market would hinge on its ability to maintain a high new product introduction frequency, manage its supply and distribution chain effectively and be ahead of the curve in terms of capacity expansion, especially with regard to diesel vehicles which are increasingly finding greater favour with consumers.

Exports Performance

MSIL's exports volumes had more than doubled in FY10 over the previous year aided by strong growth in exports to Europe where scrappage incentives were on offer to customers. However, subsequent to discontinuation of scrappage incentives in Europe, MSIL's exports growth has fizzled out since then with overall volumes declining by 6% in FY11 and by 20% in H1 FY12. With this, the share of Europe in MSIL's export revenues has declined from 80% in FY10 to 50% in FY11 to ~30% in H1 FY12. As per the company, it has recently expanded its reach to around 100 countries and intends to further increase its efforts towards diversification into additional markets to tap the small car demand potential.

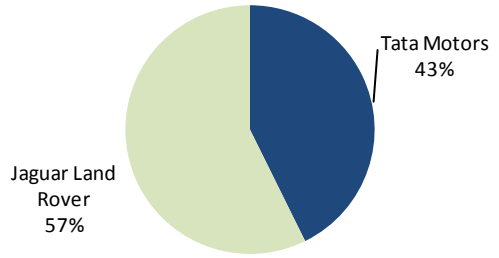
TATA MOTORS LIMITED - Performance Overview in Q2 FY12

Standalone operations face headwinds; but Jaguar Land Rover continues to support consolidated performance

Table 18: Tata Motors' Consolidated Key Financial Indicators

	Q2 FY11	Q2 FY12	Q1 FY12
Operating Income	**28,519.2**	**36,197.5**	**33,572.5**
Growth (%) *- YoY*		*26.9%*	*24.1%*
OPBDIT	**4,001.6**	**4,503.9**	**4,235.8**
Less: Depreciation	1,094.9	1,330.8	1,143.2
Less: Interest Charges	531.3	525.1	765.9
Other Income	19.5	60.8	76.1
Exceptional Gain/(Loss)	127.6	(439.0)	(57.0)
PBT	2,522.7	2,269.9	2,345.8
Less: Tax	(313.1)	(363.0)	(351.9)
PAT (Concern Share)	**2,223.0**	**1,877.3**	**1,993.9**
OPBDIT/OI (%)	**14.0%**	**12.4%**	**12.6%**
PAT/OI (%)	**7.8%**	**5.2%**	**6.0%**

Source: Company Data, ICRA Estimates



Tata Motors includes Tata Daewoo & Fiat Traded Vehicles

Revenue Growth –

During Q2FY12, Tata Motors reported a consolidated operating income of Rs. 36,197 crore (up 26.9% on YoY basis) and an OPBDIT of Rs. 4,504 crore (up 12.6%). The company's performance on YoY basis was fairly stable despite the weakness in the Indian operations, which was compensated by the strong operating performance in JLR during the quarter. The weakness in company's Indian operations was largely on account of the sharp contraction in the passenger vehicle business, which de-grew by 21% over the previous year owing to slowing passenger vehicle sales in India and rising competitive pressures. Despite rising interest rates and relatively flat freight rate, the CV segment managed to report a growth led by strong growth in the LCV segment.

Profitability –

In terms of the profitability, the company's OPBDIT margins at 12.4% during the quarter were 160 bps lower on YoY basis and almost flat on QoQ basis. The trend in margins largely reflects the contraction in profitability in the standalone operations which has been supported by relatively stable margin profile in JLR.

Other Highlights -

- Capital expenditure during H1FY12 stood at Rs. 6,610 crore, which included GBP 709 million in JLR and Rs. 1,160 crore in the Indian operations
- Company's consolidated debt levels increased to Rs. 43,973 crore from Rs. 32,791 crore (March 2011) on account of increase in working capital borrowings and the $500 million ECB
  On net automotive debt level, company's leverage stood at 0.7x with cash & cash equivalents of Rs. 18,125 crore

Table 19: Tata Motors' Consolidated Kev Financial Indicators

	Q2 FY10	Q3 FY10	Q1 FY11	Q2 FY11	Q3 FY11	Q1 FY12
Operating Income	21,088.5	25,974.2	27,055.6	28,519.2	31,685.2	33,572.5
Growth (%) - YoY	*-8.2%*	*46.7%*	*64.2%*	*9.8%*	*22.0%*	*24.1%*
OPBDIT	1,505.9	2,971.8	3,855.4	4,001.6	4,488.6	4,235.8
PAT	(2.2)	650.3	1,988.7	2,223.0	2,424.4	1,993.9
OPBDIT/OI (%)	7.1%	11.4%	14.2%	14.0%	14.2%	12.6%
PAT/OI (%)	N.A	2.5%	7.4%	7.8%	7.7%	6.0%

Source: Company Data, ICRA Estimates; Amounts in Rs. Crore

ICRA Ratings

Long Term	[ICRA]AA-
Short Term	[ICRA]A1+
Outlook	Stable

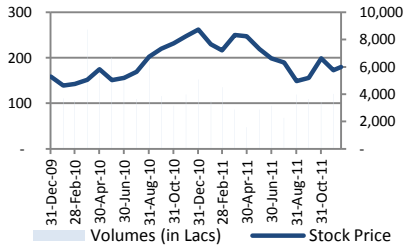
Shareholding Pattern (%)

Promoters	35.1%
FIIs	21.9%
DIIs	15.4%
Others	27.6%

Price Performance (%)

	3M	12M
Tata Motors	8.5%	-33.0%
BSE Auto	-10.9%	-22.1%
BSE Sensex	-11.1%	-24.4%

Stock Movement



Bloomberg Code TTMT
Market Capitalisation Rs.51,287 Cr
Valuations

	FY12e	FY13e
Price/Earnings	6.4	5.9
Price/Sales	0.4	0.3

Source: Bloomberg Consensus Estimates

Table 20: Tata Motors' Standalone Key Financial Indicators

In Rs. Crore	Q2 FY11	Q2 FY12	Q1 FY12
Operating Income	**11,248.9**	**12,953.8**	**11,897.9**
Growth (%) - YoY		*15.2%*	*14.2%*
OPBDIT	**1,094.7**	**872.9**	**966.6**
Less: Depreciation	331.6	386.9	365.1
Less: Interest Charges	307.2	212.1	253.2
Other Income	77.5	56.8	115.5
Exceptional Gain/Loss	3.8	(294.2)	2.4
PBT	537.2	36.5	466.3
Less: Tax	(104.5)	65.5	65.0
PAT (Concern Share)	**432.7**	**102.0**	**401.3**
OPBDIT/OI (%)	**9.7%**	**6.7%**	**8.1%**
PAT/OI (%)	**3.8%**	**0.8%**	**3.4%**

Source: Company Data, ICRA Estimates

Table 21: Trend in Tata Motors' volumes across segments

	Q2 FY11	Q2 FY12	Change (%)	Q1 FY12
Commercial Vehicles	**110,603**	**130,216**	**17.7%**	**113,186**
M&HCVs	48,106	50,716	5.4%	45,570
LCVs	62,497	79,410	27.1%	67,616
Passenger Vehicles	**82,591**	**65,082**	**-21.2%**	**69,529**
Micro	22,624	7,402	-67.3%	21,979
Compact	38,697	39,061	0.5%	31,593
Mid Size	9,211	5,202	-43.5%	3,735
Executive	2,214	1,117	-49.5%	1,115
Premium	67	194	189.6%	126
Utility Vehicles	9,556	10,126	6.0%	9,433
MPVs	52	1,980	3707.7%	1,548
Exports	**14,451**	**16,192**	**12.0%**	**14,891**

Source: Company Data

Weak passenger vehicle business and cost-based headwinds impacts operating performance; MTM on forex liabilities were add to the woes

Performance Update

Tata Motors operating income grew by 15.2% during the quarter driven largely by improvement in realization (higher shares of CV and pricing action (1%)) as volumes grew marginally by 1.8% at standalone level. While volumes in the CV segment grew by 17.7% driven by 27.1% growth in LCVs and 5.4% growth in M&HCVs, the passenger vehicles segment posted a stark underperformance to the underlying industry average by reporting a 21.2% drop in volumes. Aggressive launches in the compact and mid-size segment by new entrants and industry-wide factors such as increased interest rates and fuel prices have impacted the company's market position. As a result, Tata Motors' market share in the passenger car segment dropped to XX% in Q2FY12, while in the UV segment it stood at XX% (FY11 – XX%).

Despite a favourable product mix, operating margins of standalone operations contracted by 300 bps on YoY basis on back of lower volumes and higher marketing spends in the passenger vehicle segment and overall cost pressures, including commodity costs. The drop in EBITDA combined with exchange loss (Rs. 294 crore) on revaluation of forex liabilities resulted in a sharp drop in PBT to Rs. 36.5 crore compared to Rs. 537.2 crore in Q2FY11

In line with our view, the M&HCV segment has so far been resilient to the macroeconomic headwinds; however, given the weakening IIP growth numbers and slowdown in capital investments, we expect the outlook on the CV segment to be weaker for H2FY12. This coupled with Tata Motors' weakening market position in the passenger car segment is likely to result in subdued performance in the near term given the intensifying competitive pressures.

Key Takeaways from Q2FY12 Call

- Tata Motors' market position in the passenger car segment has been weakening due to aggressive product launches by new entrants and subsequent rise in competitive landscape particularly in the hatchback segment
- Recognizing the need to improve its market position in the passenger vehicle segment, Tata Motors has revamped its entire product offerings across segments over the past two years; with a relatively young portfolio in place, the company aims to effectively leverage on attributes such as fuel efficiency and focused distribution and marketing strategies.
- It aims to aggressively expand its sales and service network with focus on rural markets and tier II/III cities; it has put in place a programme to enhance customer satisfaction at dealer's end and also strengthen financing availability

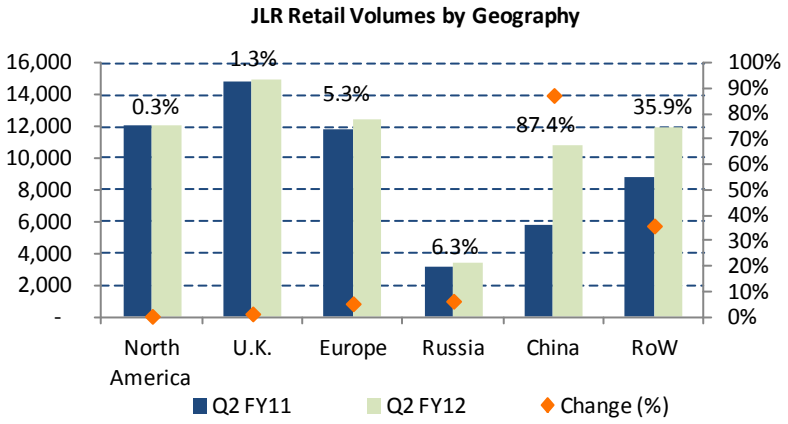
Jaguar Land Rover: Business Overview

In GBP Million	Q2 FY11	Q2 FY12	Q1 FY12
Operating Income	**2,232**	**2,915**	**2,703**
Growth (%) - YoY		*30.6%*	*20.0%*
OPBDIT	**346**	**401**	**354**
Less: Depreciation	94	113	93
Less: Interest Charges	(1)	35	24
Other Income	18	23	12
Exceptional Gain/Loss	(11)	(60)	3
PBT	260	216	251
Less: Tax	(21)	(44)	32
PAT (Concern Share)	**239**	**172**	**220**
OPBDIT/OI (%)	**15.5%**	**13.7%**	**13.1%**
PAT/OI (%)	**10.7%**	**5.9%**	**8.1%**

Source: Company Data, ICRA Estimates

	Q2 FY11	Q2 FY12	Change (%)	Q1 FY12
Wholesales Volumes	**55,134**	**68,000**	**23.3%**	**62,090**
Jaguar	14,325	13,306	-7.1%	11,343
Land Rover	40,809	54,694	34.0%	50,747
Retail Volumes	**56,420**	**65,682**	**16.4%**	**63,276**
Jaguar	14,118	13,233	-6.3%	12,557
Land Rover	42,302	52,449	24.0%	50,719

Source: Company Data



Strong operating performance continues as robust demand from emerging markets compensates for the weak macro outlook in matured markets

Performance Update

Driven by strong volumes growth and favourable product & geographic mix, JLR continued to report strong operating performance in Q2 FY12. The company's revenues grew up 31% on back of 23% increase in wholesale volumes. The growth was predominantly led by strong Land Rover volumes (up 34%) riding on back of Evoque launch and strong demand from China. Jaguar volumes shrunk by 7% on back of weaker sales in the US and UK. With increasing share of emerging markets and Range Rover & Range Rover Sport, the company's geographic and product mix continues remain favourable. Among geographies, while growth in matured markets such as North America and the UK were fairly subdued, strong growth in emerging markets, particularly China continues to support performance. China now accounts for almost 17% of company's overall volumes, contributing 55% to the incremental volumes during the quarter.

In line with strong volume growth, JLR reported an EBITDA of GBP 401 million in Q2FY12, reflecting a growth of 16% YoY. Despite strong volume growth, EBITDA margins dropped by 180 bps on YoY basis largely due to unfavorable forex movement and losses on commodity hedges. As a result of MTM losses of GBP 94 million on derivative contracts (non-cash) and higher tax provisioning (i.e. in national sales companies), JLR's PAT dropped to GBP 172 million in comparison to GBP 239 million during the same quarter in the previous year.

Key Takeaways from Q2FY12 Call

- New product introductions and strong demand from emerging markets continue to support robust operating performance; Further ramp up in *Evoque* volumes and launch in other markets adds to visibility in the near term, particularly in view of uncertain macro-economic environment in Europe
- Availability of engines have improved; however efforts going on to improve supplies
- In line with its strategy to manufacture engine in-house, JLR will investment of GBP 355 million in an engine manufacturing facility in the UK; at present, the company sources engines from Ford and over the next three years would replace it with captive engines
- JLR's gross debt stood at GBP 1.56 billion compared to GBP 1.40 as on March 2011; with cash & liquid investments of GBP 1.34 billion, the company's liquidity continues to remain strong

MAHINDRA & MAHINDRA LIMITED - Performance Overview in Q2 FY12

Table 22: M&M's Standalone Key Financial Indicators

In Rs. Crore	Q2 FY11	Q2 FY12	Q1 FY12
Operating Income	**5,434.4**	**7,360.6**	**6,733.5**
Growth (%) - YoY	*19.2%*	*35.4%*	*30.5%*
OPBDIT	**895.0**	**874.0**	**897.3**
Less: Depreciation	97.0	125.7	109.9
Less: Interest Charges	(9.1)	4.9	(2.0)
Other Income	199.8	231.5	24.9
Exceptional Gain/Loss	-	-	-
PBT	1,006.8	974.9	814.3
Less: Tax	248.3	237.6	209.5
PAT (Concern Share)	**758.5**	**737.4**	**604.9**
OPBDIT/OI (%)	**16.5%**	**11.9%**	**13.3%**
PAT/OI (%)	**14.0%**	**10.0%**	**9.0%**

Source: Company Data, ICRA Estimates

Table 23: Trend in M&M's volumes across segments

	Q2 FY11	Q2 FY12	Change (%)	Q1 FY12
UVs	42,131	48,635	15.4%	45,636
MPVs	0	7,679	-	4,073
LCVs	29,334	39,568	34.9%	33,038
3W	17,103	20,088	17.5%	15,221
M&HCVs	37	584	1478.4%	494
Cars (Super Compact)	3,403	4,900	44.0%	3,807
Tractors	42,473	54,585	28.5%	57500

Source: SIAM, Company Data

Strong revenue growth led by improved volumes; however, rising cost pressures and forex loss impact operating profits, though they continue to remain healthy

Performance Update

M&M reported a strong YoY growth of 35.4% in revenues to Rs. 7,360.1 crore facilitated by ~36% growth in both automotive (volume growth of 31%) and farm equipment (FES – volume growth of 26%) segments. However, the operating leverage benefits were shadowed by raw material cost pressures (automotive segment margin declined by 572 bps YoY and FES margin declined by 178 bps) largely on commodity inflation, especially steel and rubber, and weak product mix (higher share of low margin products). This, combined with a loss of Rs. 32 crore on account of the depreciation of the Rupee against the US$ and the consequent revaluation of its ECBs (repayable largely in 2016), has resulted in a 459 bps YoY decline in operating margin to 11.9%. However, the lower operating profit was marginally off-set by ~16% increase in other income (dividend income from subsidiaries/ JVs), resulting in PAT margin at 10.0% in Q2 FY12 (14.0% in Q2 FY11).

With increasing contribution from the Chakan plant (which resides under M&M's wholly-owned subsidiary, Mahindra Vehicles Manufacturers Limited - MVML), M&M and MVML combined performance is a better indicator of M&M's business performance, which reported a YoY revenue growth of 33.9% to reach Rs. 8,298.8 crore and a 3.2% growth in PAT to reach Rs. 761.5 crore, despite the forex loss of Rs. 32 crore in the quarter. Excluding the same, the combined entity reported a PAT of Rs. 783.1 crore in Q2 FY12, culminating to a YoY growth of 6.0%.

Table 24: M&M's Standalone Key Financial Indicators

	Q2 FY10	Q3 FY10	Q4 FY10	Q1 FY11	Q2 FY11	Q3 FY11	Q4 FY11	Q1 FY12
Operating Income	4,557.8	4,497.1	5,304.6	5,160.1	5,434.1	6,121.1	6,778.2	6,733.5
Growth (%) - YoY	*35.9%*	*56.0%*	*45.5%*	*21.6%*	*19.2%*	*36.1%*	*27.8%*	*30.5%*
OPBDIT	831.2	669.5	845.6	775.6	895.0	923.8	861.9	897.3
PAT	702.9	413.7	570.3	562.4	758.5	734.7	606.5	604.9
OPBDIT/OI (%)	18.2%	14.9%	15.9%	15.0%	16.5%	15.1%	12.7%	13.3%
PAT/OI (%)	15.4%	9.2%	10.8%	10.9%	14.0%	12.0%	8.9%	9.0%

Source: Company Data, ICRA Estimates; Amounts in Rs. Crore

ICRA Ratings

Long Term	[ICRA]AA+
Short Term	[ICRA]A1+
Outlook	Stable

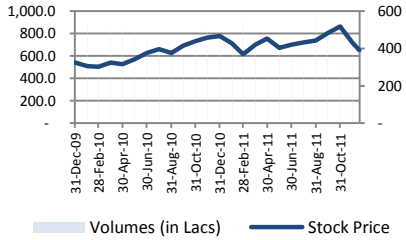
Shareholding Pattern (%)

Promoters	25.2%
FIIs	26.4%
DIIs	20.6%
Others	27.8%

Price Performance (%)

	3M	12M
M&M	-17.6%	-10.1%
BSE Auto	-10.9%	-22.1%
BSE Sensex	-11.1%	-24.4%

Stock Movement



Bloomberg Code MM
Market Capitalisation Rs.39,899 Cr
Valuations

	FY12e	FY13e
Price/Earnings	12.6	10.6
Price/Sales	0.9	0.8

Source: Bloomberg Consensus Estimates

Table 25: M&M's Consolidated Key Financial Indicators

In Rs. Crore	Q2 FY11	Q2 FY12	Q1 FY12
Operating Income	**9,410.3**	**15,250.4**	**14,256.0**
Growth (%) - YoY		*62.1%*	*66.2%*
PAT (Concern Share)	**700.9**	**682.0**	**662.3**
PAT/OI (%)	**7.4%**	**4.5%**	**4.6%**

Source: Company Data, ICRA Estimates

Note: Figures of Q2 FY12 are not strictly comparable with Q2 FY11 as the previous year did not include a) the revenues and results of Ssangyong Motor Company Limited and its subsidiaries (SYMC) and b) share in profit of Satyam Computer Services Limited

Table 26: SYMC's Key Financial Indicators

In US$ million	Q3 CY10	Q3 CY11	Q2 CY11
Operating Income	**440.7**	**689.3**	**672.7**
Growth (%) - YoY	*139.8%*	*56.4%*	*48.1%*
EBITDA	**7.0**	**(3.1)**	**0.8**
Net Income	**58.2**	**(32.7)**	**(32.2)**
EBITDA/OI (%)	**1.6%**	**(0.4%)**	**0.1%**
Net Income/OI (%)	**13.2%**	**(4.7%)**	**(4.8%)**

Source: Bloomberg, ICRA Estimates

Note: Financial year ending December

Reduction in VAT incentives, weak operating performance of Ssangyong and cost headwinds result in weak consolidated profile

Performance Update

During Q2 FY12, M&M reported a consolidated operating income of Rs. 15,250.4 crore (up 62.1% on YoY basis) and a PAT of Rs. 682.0 crore (a decline of 2.7%). While the revenue growth has been driven by the Automotive and FES segments, the margin has been largely impacted on account of input cost pressures and lower VAT incentives (though the management has not quantified the loss of benefits on VAT). The weak performance of SYMC has further added to the woes.

On SYMC's performance

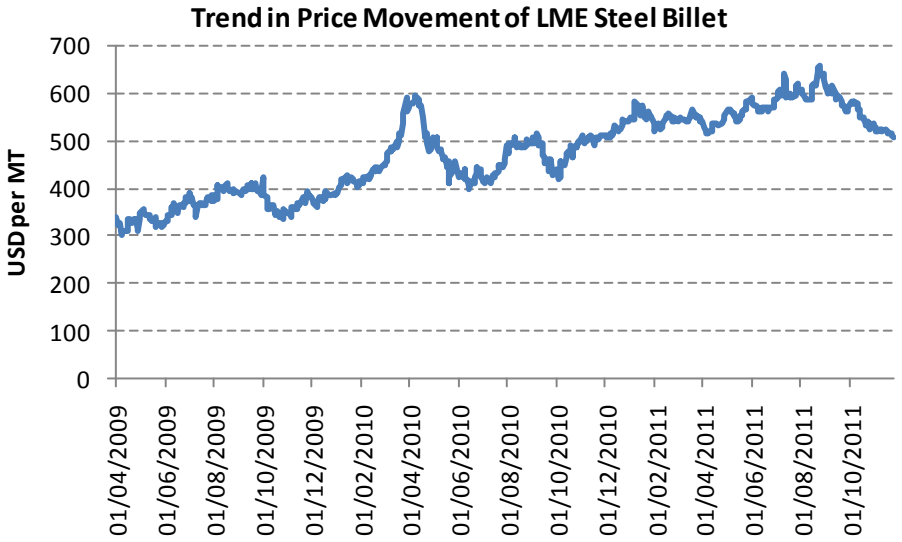
Despite the sharp increase in volumes (30,367 units for Q3 CY11, a YoY growth of 45.9%) and 56.4% YoY growth in revenues, SYMC's margins continue to remain weak on account of costs associated with the turnaround of operations. Further, during Q3 CY10, SYMC was under court receivership, which resulted in some extraordinary profits on account of sale of assets, resulting in significantly high net income. However, as per M&M management, SYMC's financial results are almost in line with the business plan they had chalked out when M&M acquired the company. SYMC would still take a few quarters to turn positive at PAT level because this company was in dire trouble at the time it was acquired and thus M&M's first focus has been to improve volumes, and having achieved so, it would now focus on improving the operating performance of the company with primary focus on reducing material cost.

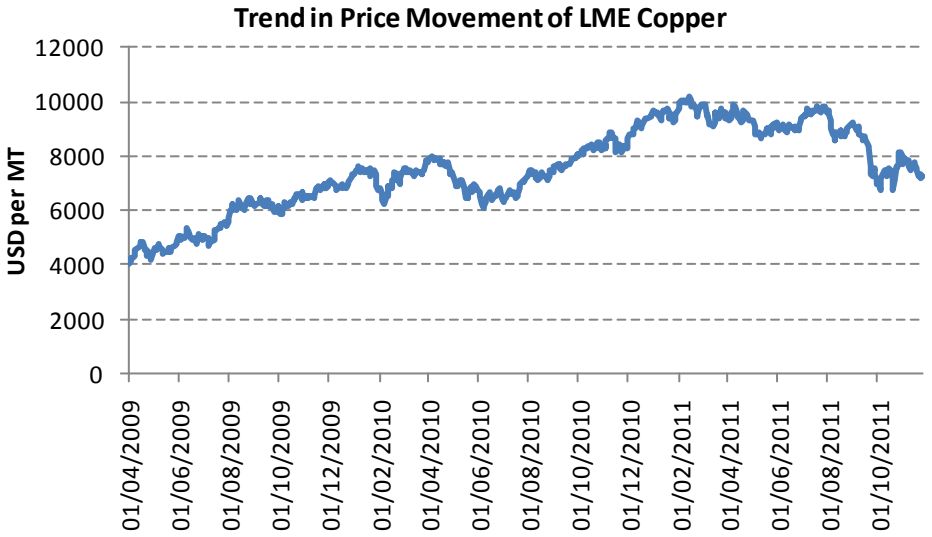
Key developments: During September 2011, M&M launched the 'XUV 500', its first global SUV platform which is priced at Rs. 10.8 lakh (ex-showroom Delhi) and Rs. 12.88 lakh for the W8 All Wheel Drive model. The product has been well received by the customers, with an order booking of more than 8,000 vehicles in just 10 days and five cities. The company has stopped taking any further bookings and will restart bookings sometime later. M&M has produced about 1,200 units in October, expected to produce close to 2,000 units in November, 2,500 in December, and is planning to ramp up the same to 3,000 units from January 2012 onwards, and reach 5,000 by June 2012. M&M has sold 1,000+ units in October and expects sale of 2,000 units in November.

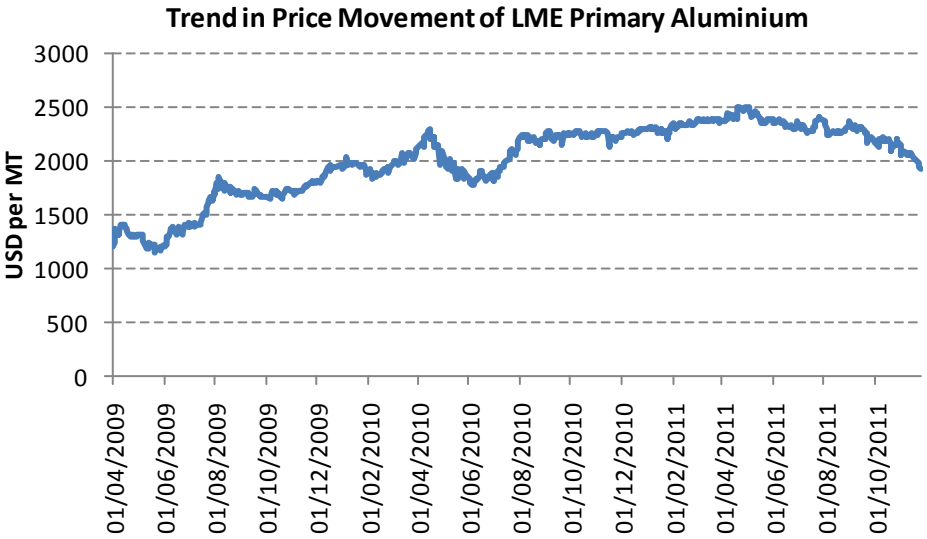
Key Takeaways from Q2 FY12 Call

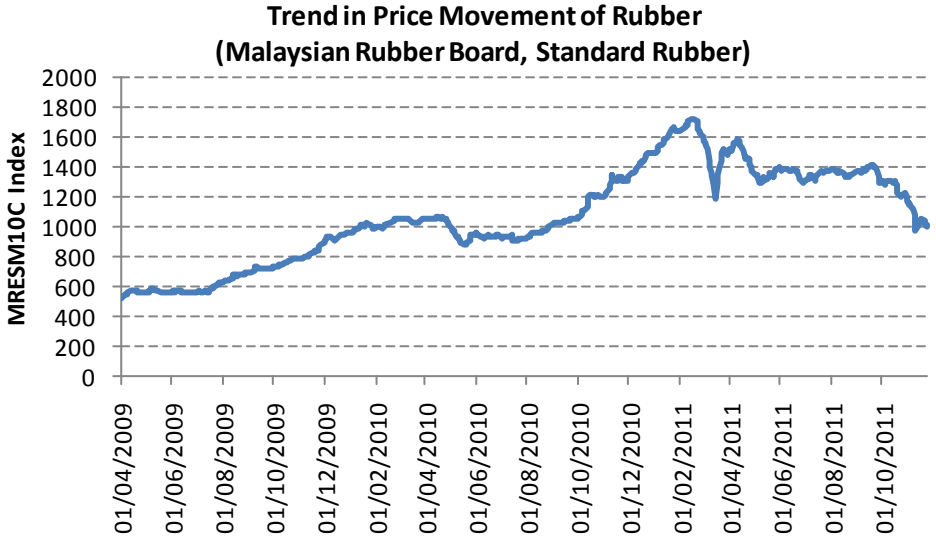
- While in the Tractor business, M&M's volume increase has kept pace with the industry in Q2 FY12, in the Automotive business, M&M has out stepped the industry by a huge margin in terms of market share increase in various segments that it operates in
- The tractor industry growth in the current fiscal has been more than 20%, higher than what was anticipated at the beginning of the year. The 24% growth in October has come as a surprise, expected to moderate in the next five months; however, the overall growth for the year still ending at 17-18%
- The increase in commodity prices has been less than what M&M had anticipated at the beginning of the year, and the management does not expect the trend to continue during the rest of the year, though it would be still higher than the Q2, FY12 levels. Thus, they do not expect the commodity prices to be a huge additional pressure on M&M's profitability
- M&M has taken a price increase of about 1.5% - ~Rs, 6,000 in H1, FY12 in the Tractor business – one price increase in Mahindra brand (in June) and one in Swaraj brand (in July) and 2-3% price increase in the automotive sector. However, even if M&M is able to pass on 100% increase in raw material prices to the customers, there is an impact of ~2-2.5% on operating profits on account of the numerator-denominator effect
- The company has lost ~2,500 units/month of UV volumes in the quarter on engine capacity constraints (engines that go into one line for Xylo, all lines of Bolero and pick-ups), with constraints likely to ease by February 2012
- The increase in inventory levels as on September-end is on account of stocking done for the forthcoming festivals of Dussehra and Diwali
- New emission norms have emerged in the tractor industry in October for all tractors above 50 hp, which will see the revenue effect from Q3 FY12 onwards as the prices would increase with the new emission norms
- M&M will keep pressing hard with the Government against imposition of diesel tax on vehicles as this would significantly impact diesel vehicle demand. However, the saving for M&M is that it does not have any petrol offerings in the UV segment – so concerns would arise if the demand for the UV segment itself slumps, but as long as UV demand continues, there is no shift from diesel to petrol that can happen in UV
- While the Amendment in VAT rules by the Maharashtra Government has impacted margins in Q2 FY12, M&M is in constant dialogue with the Government to resolve the issue

Annexure-1: Trend in Commodity Price Movement









Source: Bloomberg

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