



BRIC Spotlight Report

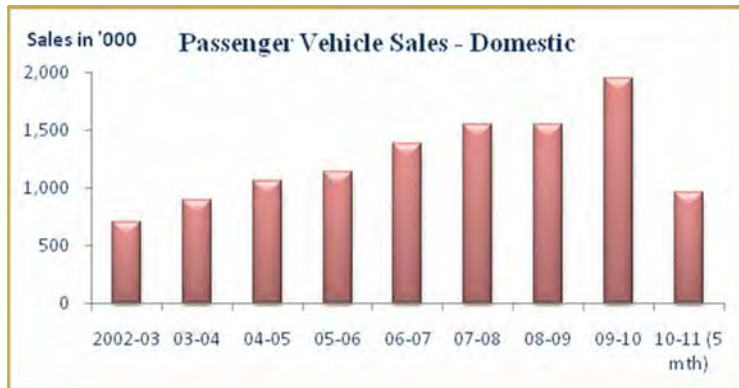
Automobiles Sector in India: Fast Growth

October 2010

Only three decades back, Indian car buyers had just two models to choose from. Both were local reproductions of European models that had disappeared from the western markets soon after World War II. Irrespective of market demand, manufacturing capacity was restricted through government licenses, and buyers had to wait several months after paying cash up front to get delivery. Imports were discouraged through very high duties, which remain high even now, and foreign-made cars were prized possessions of only the most affluent.

Fast Facts

- India is the second fastest growing automobile market in the world after China.
- Passenger vehicle production during the period April 2010 to August 2010 increased by nearly a third from a year ago. For the year ending March 2011, passenger vehicle output is expected to exceed 2.5 million.
- India is emerging as a major production base for small cars, with output expected to reach 3 million units by 2016. The country is building a reputation in designing and manufacturing low cost cars.
- Production of trucks and buses increased by nearly 66% between April 2010 and Aug 2010. An expanding highway network and overall economic growth is pushing up demand.
- India is the second largest market for motorcycles worldwide. Output of over 4.5 million units was registered during April 2010 – Aug 2010, marking growth of over 27%.
- The auto parts industry is also scaling up, as global car manufacturers are increasing their component sourcing from India, due to cost and engineering competencies.
- Competition is intense as most global firms have entered the market.



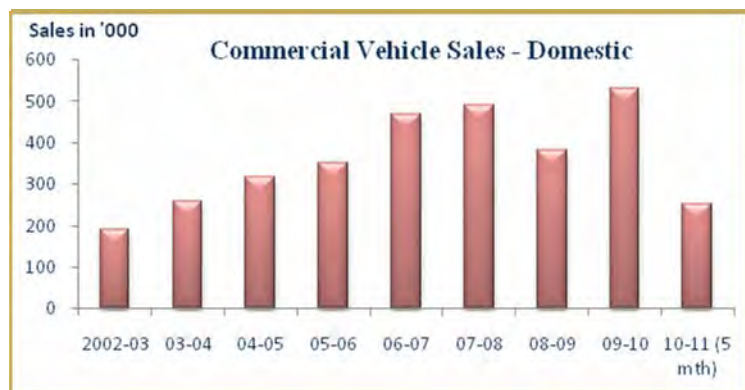
The introduction of a tiny hatchback in 1983 by Maruti Suzuki, jointly promoted by the Indian government and Japanese small car manufacturer Suzuki, was in many ways a defining moment in the development of the Indian automobile industry. Though very small, the Maruti 800, as it was called, was modern and much more reliable than its competitors. After a

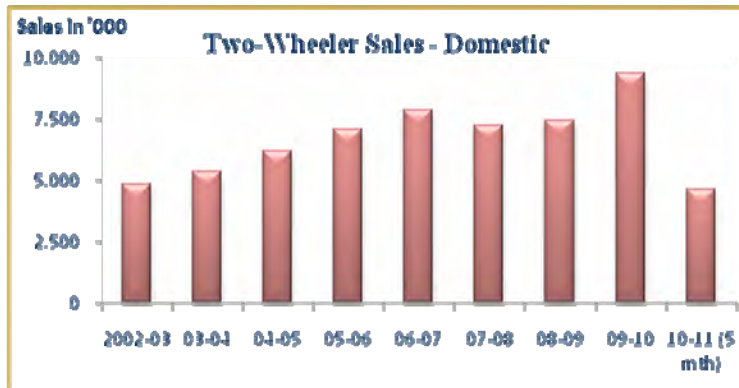
relatively slow start, the car endeared itself to the growing Indian middle class and remained the best seller for the next two decades. Until recently, it was the most inexpensively produced car in the world, and today remains popular in the semi-urban and rural markets of India.

More significantly, Maruti Suzuki introduced more efficient manufacturing practices and developed a number of local component suppliers. This industrial eco-system with vastly improved capabilities eased the entry of several foreign car manufacturers, after industrial licensing was abandoned in the 1990s. The growth of component suppliers also enabled select domestic automobile firms, with no prior experience in car manufacturing, to add passenger vehicles to their product range. Though several foreign manufacturers have struggled to expand their foothold, the growing purchasing power of the middle class continues to attract new entrants to the Indian passenger car market.

This story essentially repeated itself in other segments of the Indian automobile market, including commercial vehicles and motorcycles. These segments too have evolved from duopolistic inertia to vigorous competition. In place of outdated products, buyers now have a surfeit of vehicle models to choose from. The trigger for change has typically been the introduction of foreign technology and competition. However, instead of being overwhelmed, the domestic manufacturers have emerged as market leaders, adapting well through alliances with foreign firms for technology.

Yet, withdrawing restrictive industrial licensing and allowing the entry of foreign firms would not have ensured sustained growth for the Indian automobile industry. For demand growth to endure, the government would also have to enable the development of the country's road network and reduce





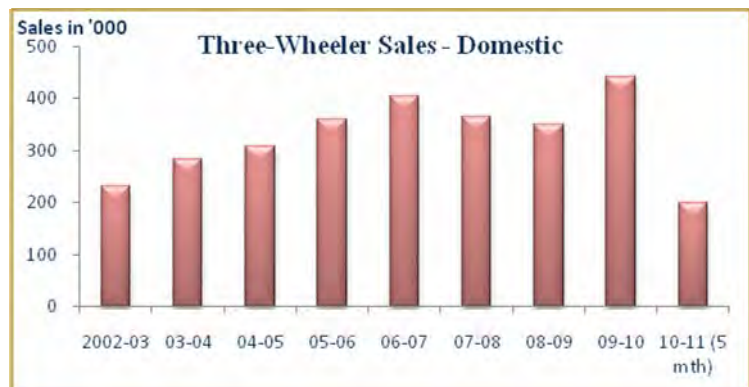
traffic congestion in its cities. Considering the poor state of Indian roads even in the 1990s, this was an arduous task that required large capital investments.

The National Highway Development Program launched in 2000 is similar in concept, though smaller in scale, to the National

Highway System in the U.S. The first leg of the project linked the four big Indian cities of Delhi, Kolkata, Chennai, and Mumbai with a four-lane highway, dubbed the Golden Quadrilateral. The subsequent phases of the program developed the North-South and East-West highway corridors and access roads to major seaports. Since its launch, more than 20,000 miles of highways have been upgraded or are currently being developed under the program. Over the next decade, the government is planning to upgrade another 20,000 miles of highways apart from building more than 10,000 miles of expressways. Most of these projects are being implemented through private sector participation, with the government absorbing part of the costs for segments where toll collections are unlikely to make the project commercially viable.

Most Indian cities have grown without even basic planning of the road network and other infrastructure. As the number of car owners started rising, roads in most cities became clogged and pollution levels increased.

Widening of inner-city roads and construction of elevated roads over busy intersections and level crossings have helped the cities to absorb the significant increase in vehicle population over the last decade. The federal government provides a large part of the financing for such projects, under programs like the National Urban Renewal Mission.



Market Segments

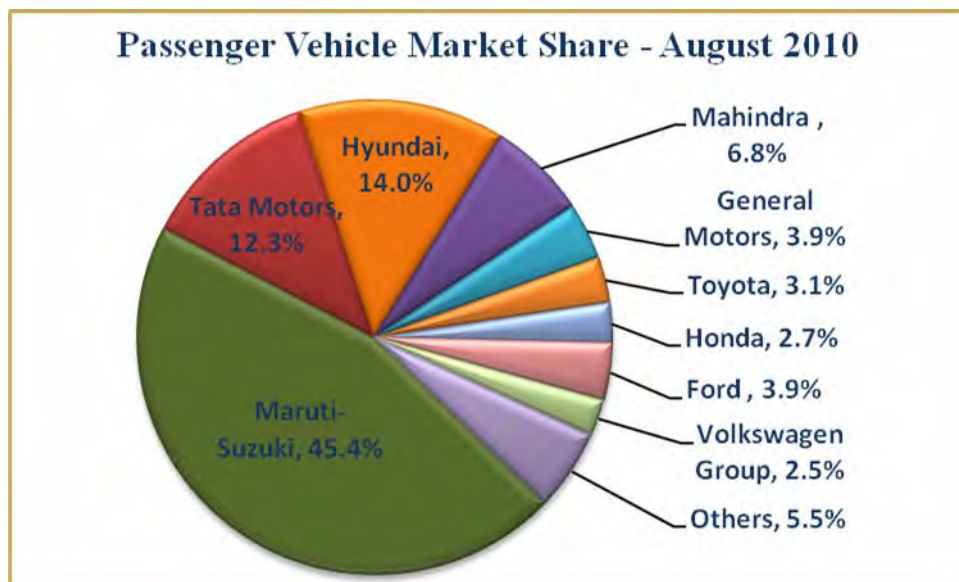
Passenger Vehicles: Middleclass dreams fuel sales growth

Like most other markets, much of the excitement in India is in the passenger vehicle segment. Robust growth in middle class income levels and easier credit availability have sustained

demand growth for passenger cars. Most major global manufacturers are already present in the country, while some of the domestic manufacturers are entering overseas markets.

Despite increased competition, Maruti Suzuki, which is now majority owned by Suzuki Motor Corp, remains the market leader in India with a share of over 45%. Its strength lies in its wide range of small car models, which form the bulk of the Indian car market. Maruti Suzuki also has the largest dealer network and its annual manufacturing capacity is now over 1 million vehicles.

Korean firm Hyundai and domestic major Tata Motors have been in a tight race for the second and third places for a while now. Hyundai is now marginally ahead with a market share of 14% as compared to over 12% for Tata Motors. Small hatchbacks dominate Hyundai's model lineup and the firm has built up a strong brand reputation over the last several years. Tata Motors has a wider product range, from SUV's to the world's cheapest car, the Nano. Tata products are positioned as value-for-money and run predominantly on diesel, which is nearly a third less expensive than gasoline in India because of government subsidies. The firm also jointly owns an assembly line with European carmaker Fiat and markets Fiat cars in India.



Mahindra & Mahindra, another large local manufacturer, derives the bulk of its sales from the SUV segment where it is the market leader. The firm recently bought out European manufacturer Renault in a passenger car joint venture, which has not performed well.

Several global manufacturers have struggled in India, though they have been present in the market for more than a decade. General Motors has seen a revival over the last year, after the firm launched low-priced hatchbacks under the Chevrolet brand. GM also sells small sedans and SUV's, but volumes remain very low. The firm sold half of its Indian operations to Chinese automaker SAIC Group last year, and the joint venture is planning to introduce utility vehicles,

besides passenger cars. Ford has been more successful in the small sedan segment in India. The company has gained market share recently after the launch of a competitively priced small hatchback from its assembly line and engine plant near Chennai, in south India.

Though their product offerings in the Indian market are limited, Japanese manufacturers Toyota and Honda enjoy leadership in their segments. Honda is a clear leader in the mid-sized sedan category, while Toyota sells the most minivans. In a bid to expand their market share, both firms are expected to launch small hatchbacks and sedans shortly.

Among European manufacturers, Skoda Auto, the Czech subsidiary of Volkswagen, has built a relatively good position in the mid-sized sedan market. Volkswagen itself has been a recent entrant in the Indian market and has expanded its product range by launching a small hatchback and a mid-sized sedan. Fiat's record in India has been patchy and it now relies on the Tata Motors dealer network to sell its products. While its venture with Mahindra has not been successful, French automaker Renault has opened a large assembly line, jointly owned by its Japanese associate Nissan. The Renault-Nissan alliance is expected to launch several models in the near future, with Nissan focusing more on the small car segment.

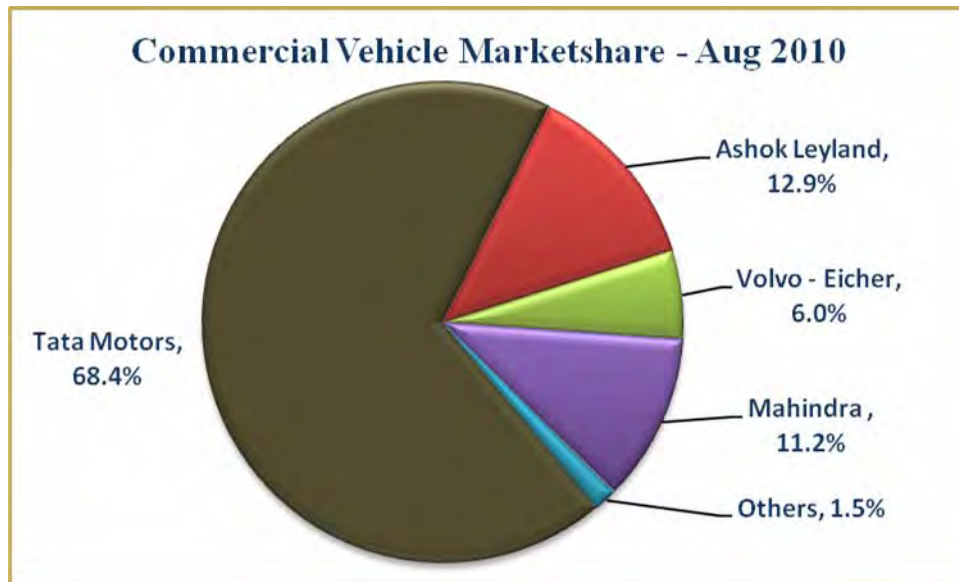
Luxury passenger cars have seen excellent demand growth, especially in recent years. However, the luxury segment now accounts for only about a percent of the total passenger vehicle market. Mercedes Benz and BMW have almost identical market shares while Audi has made rapid gains over the last year. All three manufacturers assemble cars in India from imported kits, which attract high import taxes, and hence product prices are higher than other markets. Jaguar and Land Rover, now owned by Tata Motors, are gradually expanding their dealerships in the country.

Commercial Vehicles: Rapid economic growth boosts demand

The volume of goods to be moved across the country and the demand for commercial vehicles to transport the goods are directly related to the pace of overall economic growth. When the country has a high population density and personal car ownership is low, demand for passenger transport will also rise faster when the economic growth accelerates. In recent years, as the country emerged as the second fastest growing economy in the world, India has seen a substantial increase in demand for trucks, buses, and other commercial vehicles.

Though India has one of the most extensive railway networks in the world, the bulk of the commercial goods movement is by road. The rebuilding of the country's main highways under the National Highway Development Program has made road transport easier and more efficient. Unlike in the past when only single axle trucks were suitable for narrow Indian roads, the new highways can easily accommodate large multi-axle tractor-trailers. Another factor that pushed up demand for trucks is the substantial increase in construction of buildings and infrastructure.

To ease traffic congestion in cities, the bus transit systems have been improved and upgraded across the country. The federal government continues to finance the introduction of modern buses, comfortable enough to encourage commuters to switch from personal vehicles in cities. Increased migration of workers to the cities and industrial zones has also pushed up demand for long distance bus services. As the smaller towns and villages get connected to the highway system and more migrants move out of the villages, demand for commercial transport services will only increase in the future.



For decades, Tata Motors has dominated the commercial vehicles segment and currently controls two-thirds of the market. The firm has the broadest dealer network and the widest product range of all manufacturers, from small goods carriers to large tractor-trailers. Tata Motors has also expanded its overseas presence over the last decade, mostly through acquisitions and joint ventures. The firm currently has a truck manufacturing facility in South Korea and owns a major portion of a bus and coach manufacturer in Spain. Tata Motors is the majority partner in a venture with Brazilian firm Marcopolo to build buses in India. In Thailand, the firm has joined hands with a local company to assemble and market pickup trucks.

Ashok Leyland is a distant second in the segment with a nearly 13% market share of all commercial vehicle sales, including small goods carriers. The firm's large trucks and buses are popular, but it has had limited success in smaller capacity truck models. Ashok Leyland is a market leader in buses and a leading vehicle supplier to the Indian armed forces. The company has recently tied up with Nissan for manufacturing light commercial vehicles and engines.

In the 1990s, several Japanese manufacturers entered the Indian market with light commercial vehicles but had limited success. Among more recent entrants, Volvo has gained market share in the large truck and bus segment and acquired half of a domestic manufacturer of small trucks.

German manufacturer MAN owns half of a joint venture with local firm Force Motors, which manufactures a range of commercial vehicles. American manufacturer Navistar has a joint venture with Mahindra & Mahindra and has recently launched large trucks in India.

Two-wheelers: Rural markets offer further growth opportunity

Like most developing markets, two-wheelers, such as motorcycles and motor scooters, are the most popular mode of personal transport in India. Two-wheelers are more affordable than low cost cars and even used cars. They are also cheaper to run and easier than cars to maneuver and park on narrow roads. Since the average road speeds in India are low, the lower passenger safety of two-wheelers when compared to cars does not inhibit buyers. These factors have made India the second largest two-wheeler market in the world with annual sales of over 10 million units. The increasing income levels in semi-urban and rural areas of the country offers further growth potential for two-wheeler manufacturers.

Hero Honda is the undisputed market leader in the Indian two-wheeler market, with a market share of more than 40%. The firm is particularly strong in the entry-level motorcycle category and its products are positioned as the most fuel-efficient. Honda Motor of Japan holds a 26%

Leading Indian Automobile Firms				
Firm	Products	Foreign Partner	Market Value (in \$ Billions)	Stock Listing
Tata Motors	Passenger and Commercial Vehicles	Fiat	11.6	Mumbai, New York
Bajaj Auto	Two and Three - Wheelers	Renault-Nissan for planned small car	9.2	Mumbai, London (Holding Firm)
Maruti Suzuki	Passenger Vehicles	Suzuki Motor	8.8	Mumbai
Mahindra & Mahindra	Passenger and Commercial Vehicles, Farm Equipment, Two-wheelers	Navistar for Commercial Vehicles	8.7	Mumbai, London
Hero Honda	Two - Wheelers	Honda Motor	7.9	Mumbai
Market value data based on full capitalization as on September 20, 2010				

stake in the firm and provides product technology.

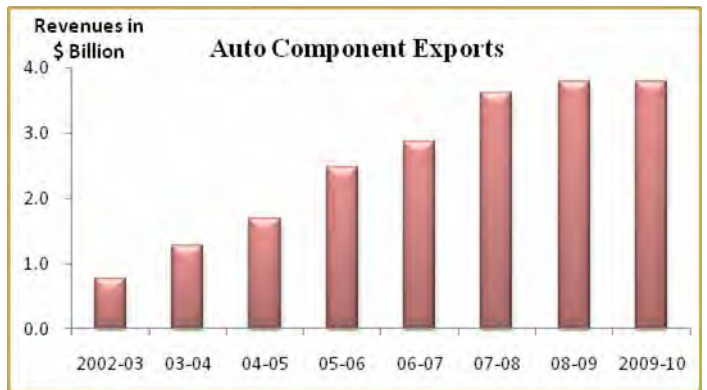
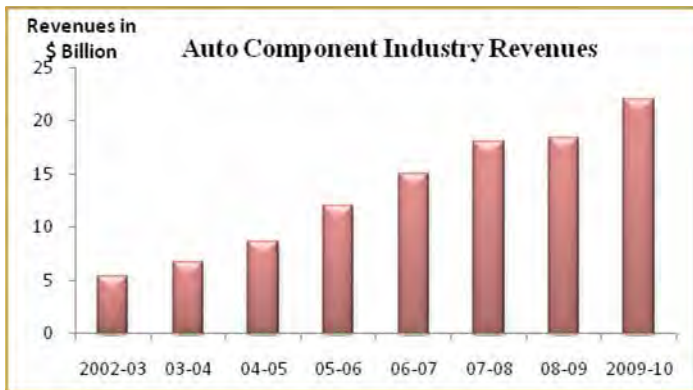
Bajaj Auto is the second largest Indian two-wheeler manufacturer, with a dominant position in higher priced motorcycles. The firm once had a near monopolistic control of the motor scooter

market, but gradually withdrew from the segment as consumers switched to motorcycles. Bajaj Auto is also the market leader in three-wheelers, which are popular as taxis in India. TVS Motor is the third major player in the two-wheeler market.

Honda Motor also has a wholly owned subsidiary in India, for manufacturing motorcycles and motor scooters. It is the market leader in motor scooters and the fourth largest in motorcycles. Honda is followed by fellow Japanese manufacturers Suzuki and Yamaha in the motorcycle segment. Harley Davidson is a recent entrant in the premium motorcycle market where volumes are very low.

Automobile Components: Attractive source for global auto firms

The Indian automobile component industry and allied businesses are among the select success stories in the country’s manufacturing sector, but their achievements are not yet widely acknowledged. The leading Indian component manufacturers have gradually built their design, engineering, and manufacturing competencies over the last couple of decades. The impressive growth of the domestic automobile market has allowed them to scale up their operations. Several of them now export to major global car manufacturers and the leading firms are establishing manufacturing operations in overseas markets.



Though major carmakers bring along their key suppliers when they enter new markets, local component manufacturers are enlisted as suppliers of smaller parts. As the carmakers become more confident in the capabilities of the local parts suppliers, they begin sourcing components from local suppliers even for their global operations. Several global automobile makers have been present in India for several years now and they have been sourcing parts from the network of local suppliers for other markets. Leading global manufacturers including Volkswagen and Fiat have announced their plans to increase component sourcing from India.

Outlook: Export potential adds to domestic demand flourish

Even after the spectacular growth in recent years, the Indian automobile market still has considerable room to grow. Passenger car ownership in India is still very low even when compared to other emerging markets. Despite domestic sales of over 10 million units annually, even two-wheeler ownership is below 100 per 1,000 of the population. It is likely that the

continued rise in average income levels will sustain demand for personal vehicles while overall economic growth will support the demand for commercial vehicles.

Besides the domestic prospects, India also has the opportunity to emerge as a global manufacturing base for select product segments. The big domestic market potential will allow carmakers to build large assembly lines, with sufficient economies of scale. Design, development, and production costs in India are lower than the developed markets. The country is also building a reputation in frugal engineering, or building low-cost products under tight budgets. Together with the growing maturity of domestic auto component suppliers, these factors are making an attractive automobile manufacturing location for the global markets.



In recent years, India has emerged as a leading center for the manufacture of small cars. Hyundai, the biggest exporter from the country, now ships more than 250,000 cars annually from India. Apart from shipments to its parent Suzuki, Maruti Suzuki also manufactures small cars for Nissan, which sells them in Europe. Nissan will also export small cars from its new Indian assembly line. Tata Motors exports its passenger vehicles to Asian and African markets, and is planning to launch electric vehicles in Europe this year. The firm is also planning to launch an electric version of its low-cost car Nano in Europe and the U.S. Mahindra & Mahindra is preparing to introduce its pickup trucks and small SUV models in the U.S. market. Bajaj Auto is designing a low-cost car for the Nissan-Renault alliance, which will market the product globally. Nissan-Renault may also join domestic commercial vehicle manufacturer Ashok Leyland in another small car project.

While the potential is impressive, there are challenges that could pull down future growth of the Indian automobile industry. Since the demand surge for automobiles in recent years is directly linked to overall economic growth and rising personal incomes, industry growth will slow if the economy weakens. Also, any delay in the further development of the highway network could slow down domestic demand growth. It is possible that the government will favor mass transport systems for the large cities, which may restrict the demand for personal vehicles. Most Indian cities will have a combination of metro rail networks and dedicated road corridors for buses and

it is possible that a good number of commuters will opt for public transport. It is also likely that intense competition will erode the profitability of manufacturers, especially in the passenger vehicles segment.

Despite these challenges, the long-term outlook for the automobile industry in India remains bright. In most countries, the automobile industry historically has been one of the sectors leading the economic growth and development. Available indicators suggest that it will be no different in India, which is likely to remain one of the fastest growing economies in the world. 🌐

Data Sources:

- *For automobile sales and export data: Society of Indian Automobile Manufacturers (SIAM)*
- *For auto component revenue and export data: The Automotive Component Manufacturers Association of India (ACMA)*

Thomas White International, Ltd.

One Financial Place
440 South LaSalle Street
Suite 3900
Chicago, Illinois 60605
Email: feedback@thomaswhite.com

Thomas White India Pvt., Ltd.

Suite 300, 3rd Floor
Phoenix Towers
16/1 Museum Road
Bangalore 560001
Tel.: 91-80-40187777

The information contained in this publication does not, in any way, constitute investment advice and should not be considered a recommendation to buy or sell any security discussed herein. It should not be assumed that any investment will be profitable or will equal the performance of any security mentioned herein. Thomas White International, Ltd. may, from time to time, have a position or interest in, or may buy, sell or otherwise transact in, or with respect to, a particular security, issuer or market on our own behalf or on behalf of a client account.

© Thomas White International, Ltd. 2011