Grant Thornton

Sales

Manufacturing

Exports

Auto Track

Q1 FY22

Contents

Foreword

The time is opportune to accelerate the change processes by reviewing and adapting strategies and investment plans as consumer mobility demands are changing, forcing the industry to rethink its sales models and explore new concepts.

Most automotive original equipment manufacturers (OEMs) already have electric vehicle programmes in place or are underway. The country is riding high on the support extended by the government through the Faster Adoption and Manufacturing of Hybrid and Electric Vehicle (FAME) scheme and interest shown by the private players. Also, with significant shifts in the automotive retail and distribution model, the industry is witnessing changes in the business of vehicle sales.

On the contrary, the high cost of ownership due to fuel price hikes would have limited impact except for the more vulnerable categories such as two-wheelers. The global semi-conductor shortage would have a limited incremental impact on Indian OEMs as the timing of its worst effects during Q1 FY22 coincides with weak demand. Indian automakers' margins are likely to improve in FY22 on favourable operating leverage, while price increases may offset higher input prices.

We see a strong commitment among policymakers and industry leaders, although, with the ongoing transformations, the financial resources may be limited over the next few years. Meanwhile, the OEMs are undertaking this unique chance of bold actions to change their overall strategies with the shift in the vehicle distribution model.

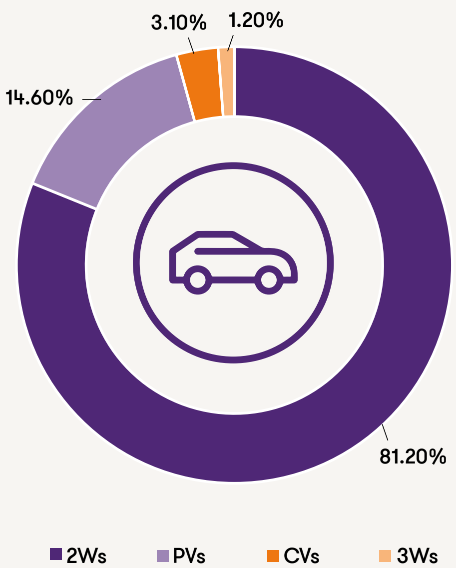
Saket Mehra
Partner and Automotive Sector Leader
Grant Thornton Bharat

Industry overview

The automobile industry is one of the prime movers of the manufacturing sector and the 'Make in India' initiative. It aims to increase exports of vehicles by five times by 2026. The industry has the potential to generate up to USD 300 billion in revenue and around 65 million additional jobs by 2026.

Small and mid-size cars dominate in the passenger car sales category. Two-wheelers (2Ws) and passenger cars accounted for 81.2% and 14.6% market share, respectively, accounting for a combined sale of over 17.8 million vehicles in FY21.

Segment-wise domestic market share in FY21 (%)



Overall, the automobile exports reached **4.12 million** vehicles in FY21

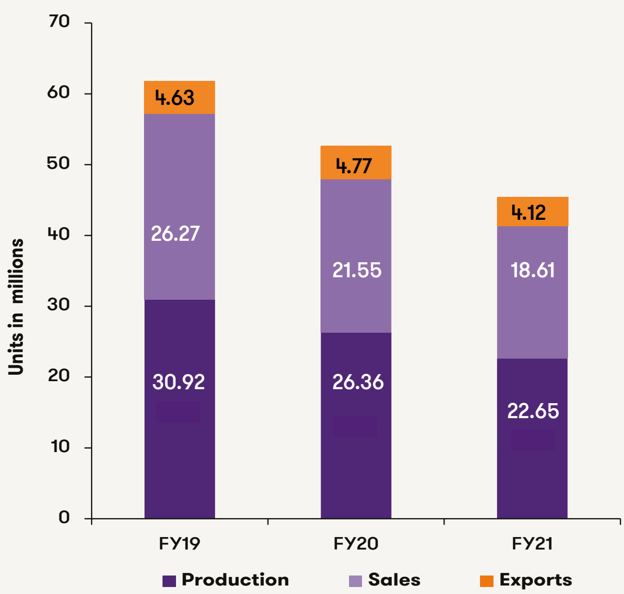
Two-wheelers made up **79.38%** of the total exports

Followed by passenger vehicles at **9.79%**

Three-wheelers at **9.51%**

Commercial vehicles at **1.21%**

Production, sales and exports



Export incentives

- Under the Merchandise Export Incentive Scheme (MEIS), automobile manufacturers get a benefit of 2% on vehicle exports.
- In terms of bilateral foreign trade agreements, about 20 tariff headings have been considered as 'sensitive items' to be maintained in the negative list of India in most of the trade agreements.

Additional capacity

- The cumulative FDI equity inflow in the automobile industry is USD 25,848.13 million from April 2000 to March 2021. This constitutes 4.88% of the total FDI inflow received across sectors.
- The industry is expected to attract USD 8-10 billion in local and foreign investments by 2023.

Major dampeners

Semiconductor shortage

Prolonged semiconductor shortage for over six months has put pressure on automotive supply chains and continues to decelerate the production levels.

Fuel economy standards in flux

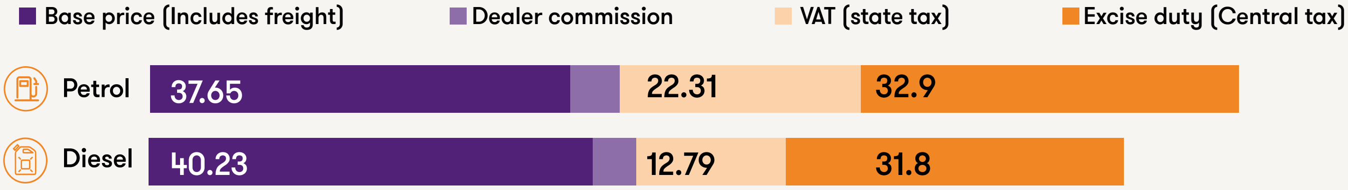
Petrol and diesel prices have increased about 20% in the last year. The rise in prices has impacted consumer sentiments and made logistics and supply chains expensive for automobile OEMs.

The price of petrol has surpassed the INR 100 per litre mark in numerous states and union territories including Maharashtra, Rajasthan, Madhya Pradesh, Andhra Pradesh, Telangana, Karnataka and Ladakh. Since 4 May 2021, petrol prices surged 40 times and in July itself the prices were increased 10 times (as of 17 July 2021).

High taxes

While international crude oil prices determine the cost of fuels in India, it is major factor contributing to the rise in petrol and diesel prices. The main reason for this hike is central and state government taxes. More than half of fuel prices are made up of taxes.

Price build up in Delhi (INR/litre)



Source: Indian Oil. (As on 16 June 2021)

Shift to electric vehicles: The future is bright

Opportunities

- Electric vehicle market in India would present opportunities worth USD 206 billion by 2030.
- It is estimated that the EV market in India is likely to grow at a CAGR of 36% until 2026. Also, the EV battery market is likely to expand at a CAGR of 30% in the same period.
- A cumulative investment of over USD 180 billion is required in vehicle production and charging infrastructure.
- OEMs have placed big bets on all-electric fleets and batteries.
- This transition is likely to save Indian crude oil imports worth INR 1,07,566 crore.

Challenges

High costs: With the increase in research and development activities and market competitiveness, EV price will be rationalised considering the price sensitivity of consumers.

Higher dependence on imports: Reliance on imports of battery as well as other components is also one of the factors adding to the cost of EVs in India.

Insufficient charging infrastructure: Establishing the charging infrastructure is necessary for large-scale EV adoption. It is an enormous but essential undertaking for widespread adoption.

Range anxiety (kms/charge): With compatible charging stations along EV route, this challenge will be taken care of.

Grid challenges: Increasing methods of power generation are necessary to meet the expected growth in electricity demand once EVs become mainstream.

Growth drivers

- Federal subsidies
- Favourable policies with deeper discounts for Indian-made electric two-wheelers
- Boost for localised ACC battery storage production through the PLI scheme

Impact of COVID-19 second wave

The sudden and severe onset of the second wave of the COVID-19 pandemic in the country has derailed the recovery momentum of automobile OEMs and auto ancillaries to quite an extent. While most of the segments would continue to report growth on a y-o-y basis, given the favourable base, the growth estimates stand revised downwards given the sharper and longer-than-expected impact of the second wave.

Segment growth	Passenger vehicles	Two-wheelers	Commercial vehicles
Expected earlier	16-18%	22-25%	27-30%
Now	10-12%	17-20%	21-24%

- The second wave has seen deeper and wider penetration including rural hinterlands.
- Near-term supply disruptions in the sector.
- Collapsed sales of new vehicles as auto plants and many dealers were forced to close.
- Impact on disposable income and rising vehicle costs (including fuel cost).
- The prolonged impact is likely to be on account of the effect on various demand drivers.
- An elongated recovery cycle or possibility of a third wave offers further downside risks.

Impact of lockdowns on sales

- Drop in new orders as per OEMs
- Piling up of inventories/stocks
- Second thoughts by consumer wherein pre-bookings were held
- Global semiconductor shortage

Quarterly domestic sales analysis

(In units) *

Category	April		May			June			April-June	
	2020	2021	2020	2021	y-o-y % change	2020	2021	y-o-y % change	2020-21	2021-22
PVs	-	261,633	33,546	88,045	162.46	105,617	231,633	119.31	153,734	646,272
2Ws	-	995,097	279,682	352,717	26.11	1,014,827	1,055,777	4.04	1,294,509	2,403,591
3Ws	23	13,728	2,437	1,251	(48.67)	10,300	9,397	(8.77)	12,760	24,376
CVs	-	-	-	-		-	-		31,636	105,800
Total	**23**	**1,270,458**	**315,638***	**442,013**	**40.04**	**1,130,744**	**1,296,807**	**14.69**	**1,492,639**	**3,180,039**

Note:
According to data released by the industry body Society of Indian Automobile Manufacturers (SIAM).
Does not include volumes of Tata Motors.

*Less 27 quadricycles in May 2020

April 2021

In April 2021, the total passenger vehicle sales reached 2,61,633, and automobile production (including quadricycle) was 1.88 million. The automobile sales in April 2021 reflect the various disruptions caused due to the pandemic, while Y-o-Y comparison was irrelevant as April 2020 witnessed nil sales due to nationwide lockdown.

The factory dispatches of 2Ws, 3Ws, PVs, MHCVs, and LCVs declined by 10-58% sequentially.

May 2021

The second wave of the pandemic had a drastic effect on the automobile industry, consequently, it witnessed a massive drop in sales in May 2021. As many as 88,045 PVs got sold as compared to 33,546 units a year-ago period. However, the production and retail sales numbers are not comparable as the previous year's months were impacted due to nationwide lockdowns imposed in the country due to the pandemic. Many OEMs had shut their manufacturing plants to divert oxygen from industrial use for medical purposes.

So, as compared to May 2019, sales in the month of May 2021, for PVs stood at 88,045 units (- 61.2%), for 2Ws at 3,52,717 units (- 79.6%) and for 3Ws at 1,251 units (- 97.6%).

In April and May, owing to the alarming rise in the number of COVID-19 cases and subsequent lockdowns, vehicle sales plummeted. The situation in Q1 FY22 was exacerbated with supply chain disruptions that are expected to persist over the coming months as well.

June 2021

With the relaxation of norms after the second wave of COVID-19 announced by the government, the overall domestic vehicle sales rose by nearly 15%.

The PV sales increased by 119.31% to 2,31,633 units from 1,05,617 units in the year-ago period. Domestic 2Ws sales witnessed a 4.03% increase with 10,55,777 units.

Q1 FY22 units

Category	Production		Domestic sales		Exports	
	2020	2021	2020	2021	2020	2021
April	15,741	1,875,698	23	1,270,458	57,332	520,289
May	339,488	806,755	315,638	442,013	129,093	435,471
June	1,094,554	1,693,639	1,130,744	1,296,807	246,190	447,319

Note: According to data released by industry body SIAM

India's auto demand to recover despite the COVID-19 second wave

A resilient buyer sentiment would support a swift rebound in sales after the easing of restrictions. The industry expects to drive double-digit growth in FY22 from a low base, although sales volume is likely to remain below the peak in FY19. The rise in domestic sales in June 2021 is seen to be primarily driven by the pent-up demand.

There remains no doubt that with the launch of new products in the market, consumers will have some excitement as the industry SUV segment has a significant buyer interest. Thus, the consumer sentiments need to be induced at the entry-level hatchback segment, other sub-segments, and the luxury segment as the numbers have been quite slow since the beginning of FY22.

Coverage

Shift in automotive retail and distribution

Changes in automotive retail

With an OEM in India's luxury vehicle space making a radical shift in its retail structure; having introduced an agency (direct-to-customer) sales model by owning of stock of the new vehicles, India sees an enhanced buying experience. Agency models in which dealers would sell vehicles and services on behalf and at the risk of the OEM and receive service fees could act as a bridge from dealer-entrepreneurs to a direct-sales model.

Digitalisation as enabler of new business models

The Indian automobile industry witnessed major OEMs establishing and enhancing their online retail channels to a marked extent in FY20. On the other hand, customers had positive experiences in using the digital modes for evaluating their purchase of vehicles. The retailers focused on remote communication channels or at-home services to accommodate social-distancing measures and reduce dependency on in-person dealer visits for customer experience.

India has displayed an increased adoption of technology and digitalisation, and online has essentially emerged as the preferred purchase channel for most customers.

275
dealerships closed down in FY20.

Debt on dealers increased to the range of **20% to 40%** in FY21.

15% to 20%
job losses in 2021.

Revenue from after-sales and services declined by up to **7%** in FY21.

Source:
Federation of Automobile Dealers Association (FADA)

	Pre-pandemic	Post-pandemic
Research on information majorly online ready		
Configuration increase in online share		
Trade-in increased use of external platforms		
Test drive VR/AR online booking		
Negotiation transparency in prices		
Closing digitally signed, online purchases		
Delivery at home		
Use OTA, mobility offerings		

Amid a significant uptick in technology adoption, Sandeep Aggarwal, Founder and CEO, Droom Technology, believes that "the Indian automobile industry is now shifting online in a more rapid manner post-COVID-19. We have observed that the online transition of buying and selling automobiles can deliver a wide range of options for customers with home test drives and exceptional delivery facilities while cutting down on the capital required to run a physical retail showroom. It is estimated that by 2025, 6% to 7% of the total automobile market will shift towards online marketplaces which are right now less than 1%. By 2030, it is projected that online automobile sales will overtake physical showroom-based buying."

Accelerated trends: New structures, formats and technologies in automotive retail

With digitalisation and changes in ownership models, OEMs achieve a direct interface to their customers whereas dealerships lose their exclusive role as intermediaries.

Direct sales by OEMs could support financially weakened dealerships in terms of stock financing.

With an increasingly complex model line-up and lower sales volumes, central test-drive locations could lower the costs of retail.

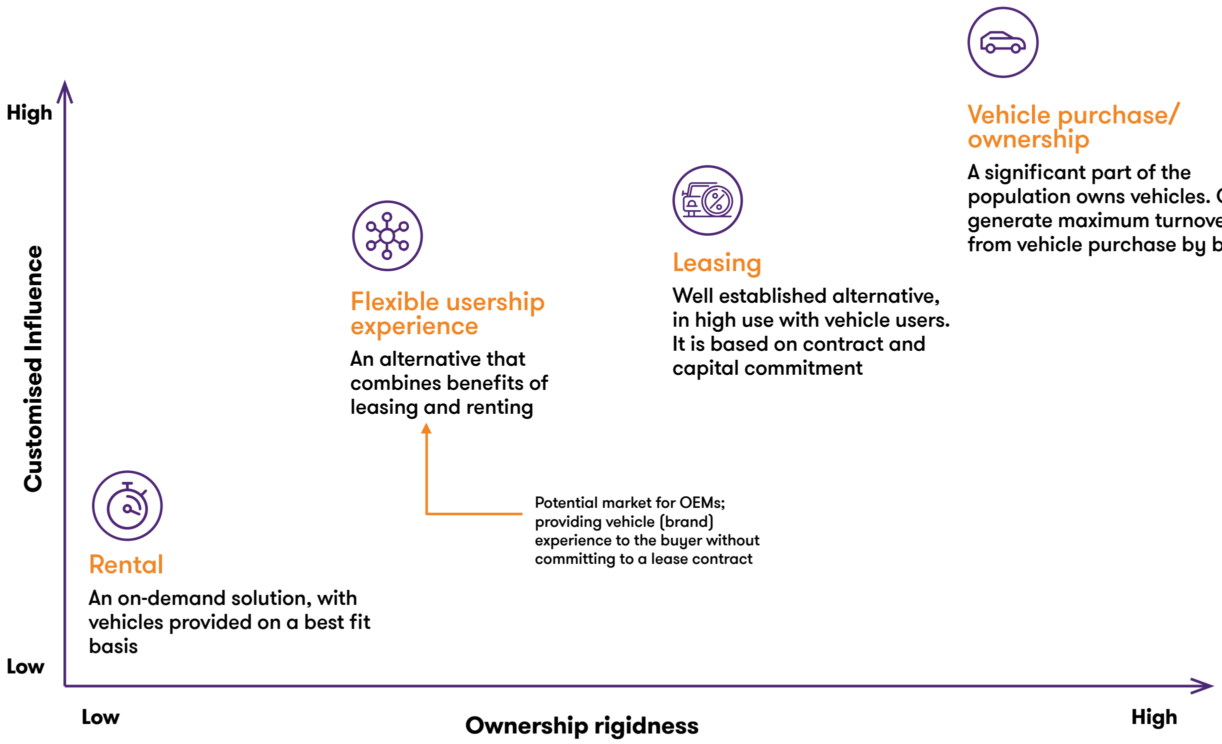
Technology to enhance the customer experience with product visualisation and communication technology, and virtual and augmented reality.

Increased relevance of centralised customer data and a direct customer interface.

Vehicle subscriptions on the rise

The industry is witnessing a revolution that is radically reshaping its marketing, distribution and selling techniques. Business transformation is becoming pertinent for auto companies in India to stay relevant to the customers and ensure that they are future-proofing their business models.

Thus, to extend the brand value and to showcase their renewed interest in building strong, lasting relationships with the customers, OEMs have executed new and transformed concepts for the sustainability of the automotive business. Vehicle subscription service schemes are seen as a thriving trend in the distribution model. These schemes are being offered with a high degree of flexibility and are getting fostered by automotive OEMs, rental companies, and disruptors.



Key features

Service provider	Customer centricity	First party data	Better revenue predictability
Consumer	Vehicle choice	Contract flexibility	Convenience

With a variety of customer needs, a more fluid form between renting and leasing offers a better fit for many. Overall, the consumer-segment requirements would be actual drivers of the service requirements and in turn, would help determine the best cost and operating structure for the specific distribution format and customer-value proposition.

According to Jyoti Malhotra, Managing Director, Volvo Car India,

'Volvo is a very customer-centric company and we deliver on customer aspirations. Over the period, customer preferences have changed and there has emerged a section of customers who aspire to possess a high-end luxury car without owning it. Volvo's subscription model is aimed at this section of consumers who can now enjoy the Scandinavian luxury of Volvo Cars as per their preferred duration and pay only for that duration. At present, we are offering our high-end luxury cars under this program in Delhi and Haryana, keeping the scope open for other markets in the future.'

Car subscriptions bridge the gap between leasing and rental. They offer high flexibility and reduce risk, commitment, and rigidity inherent in car ownership. This has proven particularly attractive in times of economic uncertainties and primarily targets a younger, up-and-coming clientele. However, subscription models must be well marketed and positioned, as the increased flexibility leads to additional complex processes, demanding a higher price point than traditional leasing offers.

With his vast experience in the automobile industry, Giriraj Dhingra, head of Dhingra Motors Pvt. Ltd. and leading Tata Motors passenger car dealers adds that,

'A subscription-based model in auto industry requires a completely new operating business model to be sustainable and profitable as the asset would still be owned by the company. The upcoming times are of e-mobility and the industry needs to be mindful of the buying behaviour of consumers very effectively. Customers should know the subscription polices well and evaluate the cost before preferring ownership to usership. Overall, in the Indian scenario, these models have room to grow, and industry needs to overcome the imminent challenges to ensure continued customer loyalty as well as revenue gains.'

Regulatory updates

I. Extension of FAME II scheme till 31 March 2024 - move to further drive adoption of electric vehicles

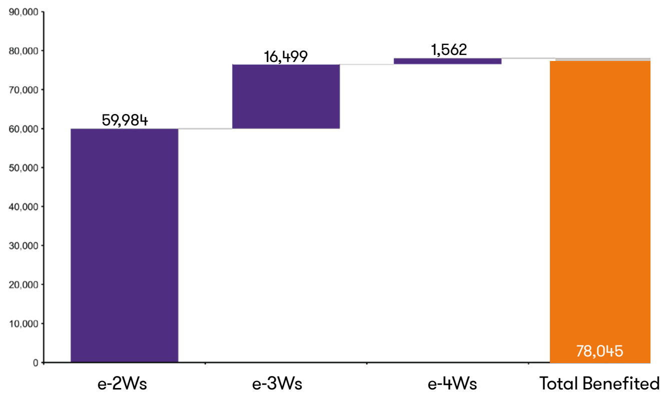
The Union government extended the ambitious Faster Adoption and Manufacturing of Hybrid and Electric Vehicles (FAME) scheme to promote electric mobility by two years till 31 March 2024.

Scheme

- Supports the electrification of public and shared transport and help create charging infrastructure.
- Signals the government's intent to reduce vehicular emissions and dependence on fossil fuel.

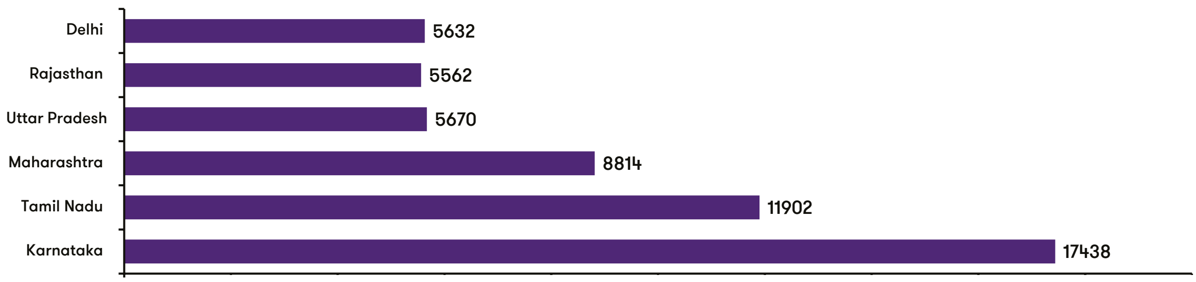
The cap on maximum available subsidy was raised from 20% of the price of the vehicle to 40%, increasing the incentive to INR 15,000 per kWh compared to INR 10,000 per kWh earlier.

Vehicles benefitted under FAME scheme



Leading states to avail benefits under the scheme

State wise registrations



Budgetary allocation of **INR 10,000 crore** is for three years to **31 March 2022**

Scheme's first phase began: **1 April 2015** (extended till 31 March 2019)

Second phase (Fame-2) began: **1 April 2019** (It was to end on 31 March 2022)

However, the scheme has utilised only **5%**, or **INR 492 crore** of the INR 10,000 crore allocated under its second phase spent till March 2021

Some critics blame the lack of supply-side policy instruments such as Zero Emission Vehicle (ZEV) sales requirements or ICE phase-out targets to hasten EV adoption, while others have indicated the limited availability of EV models for average consumers.

Future scenario

- With the total expenditure for both phases of the FAME programme at INR 818 crore till March 2021, the budget sought for 2021-22, 2022-23 and 2023-24 is INR 1,893 crore, INR 3,775 crore and INR 3,514 crore respectively, bringing the total to INR 9,182 crore.
- Significant acceleration is required to reach both the programme targets and national targets of 30% EV sales by 2030.
- The industry is prepared for a major transformation and see EVs occupying a major space.

II. India adopting global standards for scrapping vehicles

Announced in the 2021-22 Union Budget, the new vehicle scrapping policy provides for

Fitness tests*

PVs- in **20 years**

CVs- in **15 years**

*Failure to obtain fitness certificate will result in end of life of vehicle

Rebate on road tax by state governments*

PV – **up to 25%**** CV- **up to 15%** **

* From 1 October 2021 against scrapping certificate for old vehicles

** For a period of eight years for CVs and 15 years for PVs from the date of registration

Policy benefits

- 5% discount from OEMs on new vehicle
- Waiver in registration fee
- Incentives for encouraging scrappage
- Corroboration with 'Make in India'
- Support in revival of the auto CV segment
- Steel and electronics industry to utilise scrap emanating from vehicle
- Increase in the country's automobile industry turnover
- Improvement in fuel efficiency
- Reduction in pollution levels
- Significantly lowered carbon emissions
- Adoption of better technology on Indian roads
- Safer roads

Future scenario

The scrappage needs formal and scientific collection.

Dismantling and processing activities for end-of-life products.

Guidance to the recycling centres to expand the technological know-how for segregation and recycling.

Scrapping of old vehicles will be promoted with assorted incentives including road tax rebate, scrap value, discount and waiver of registration fee on purchase of new vehicles.

Recent announcements

28 June 2021

Ministry of Road Transport and Highways (MoRTH) issued a draft notification dated 28 June 2021, notifying mass emission standards for E 12 (blend of 12% ethanol in gasoline) and E 15 fuels, thereby facilitating their use as automotive fuels.

25 June 2021

Ministry of Heavy Industry and Public Enterprises (MoHIPE) issued Gazette Notification for FAME-II Scheme.

09 June 2021

Production Linked Incentive (PLI) scheme, 'National Programme on Advanced Chemistry Cell (ACC) Battery Storage' for implementation of giga-scale ACC manufacturing facilities in India.

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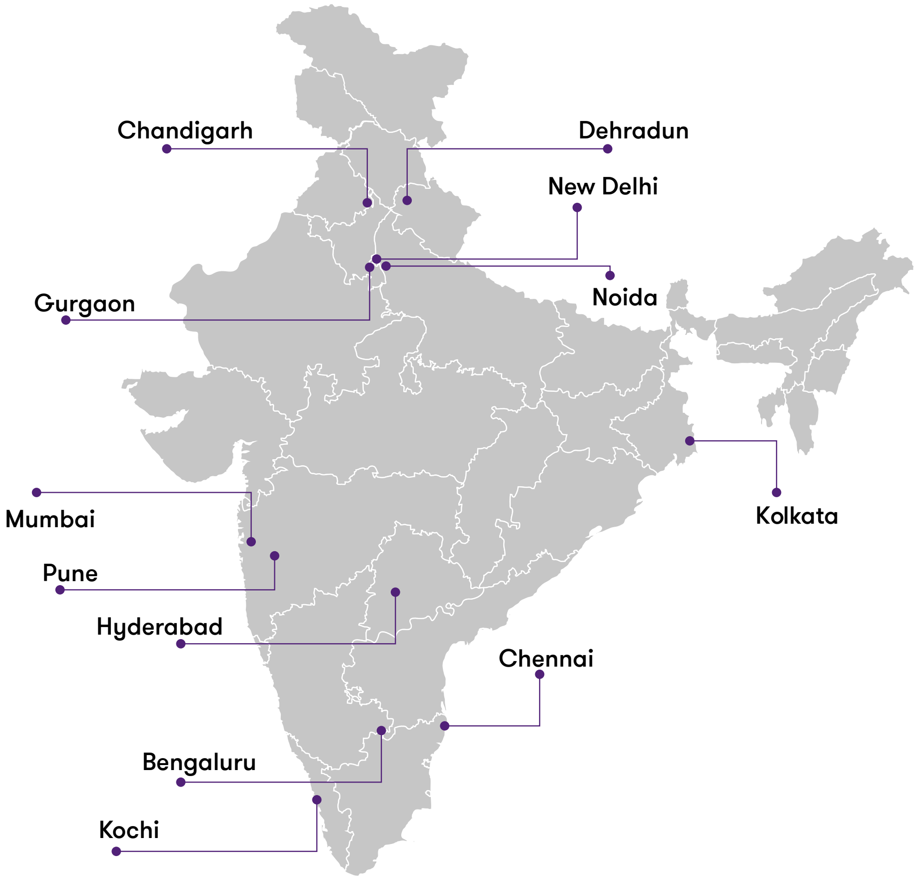

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