EPRA International Journal of
Multidisciplinary Research (IJMR) Peer Reviewed Journal

THE AUTO INDUSTRY CRISIS IN INDIA

Manisha Choudhury
Associate Professor,
Vijaygarh Jyotish Ray College,
Kolkata

ABSTRACT

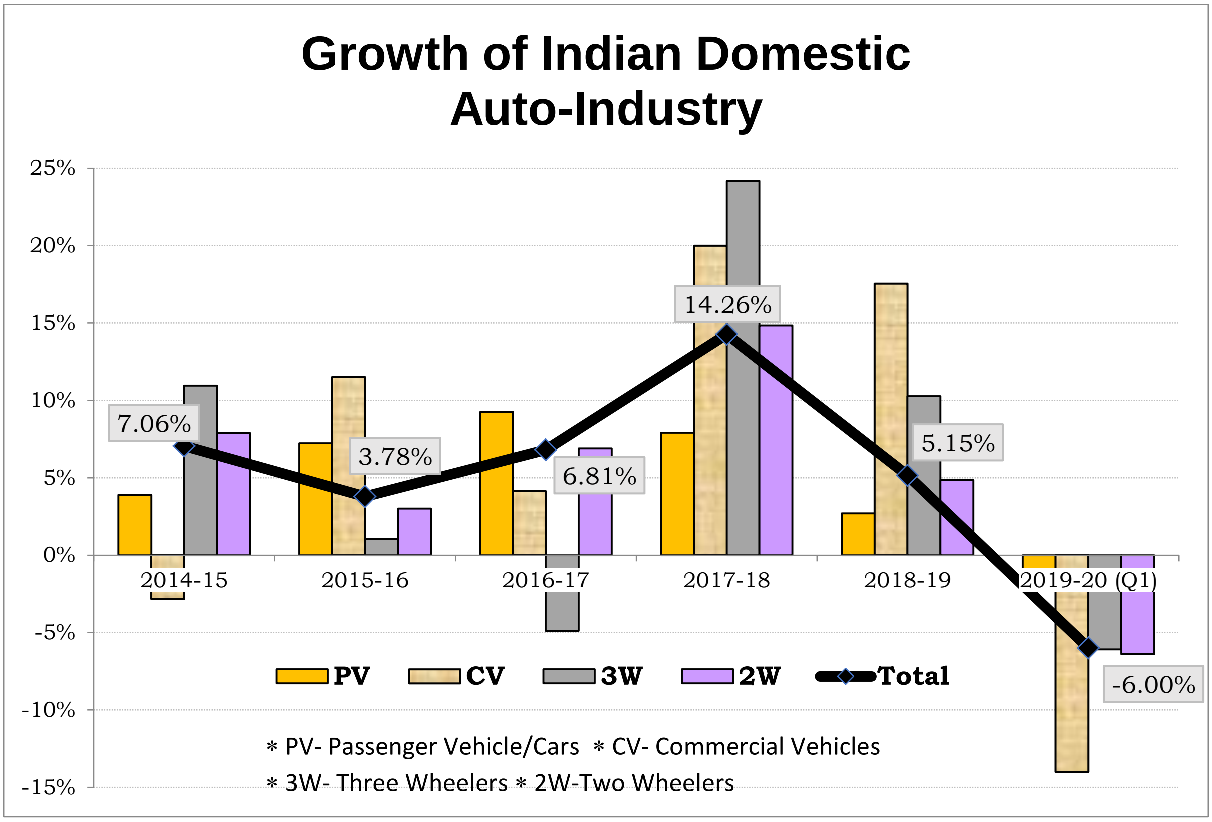
The Indian auto industry currently is faced with its worst crisis in years. The government of India has finally recognised this crisis and has recently come up with a slew of measures to tackle the problem.

The Indian Automotive Industry that is pegged at Rs.4,800 billion contributes 7.5% to India's overall GDP and 49% to the manufacturing GDP and generates about 37 million jobs through manufacturing, services, dealerships and various forward and backward linkages. With a manufacturing volume of 4.5 million units in 2017-18 (without two wheelers) and corresponding sales of 4.02 million units, it is the 4th largest automobile manufacturer in the world. It is the largest two-wheeler market in the world overtaking China with 17.5 million units' sales in 2017. India was the 7th largest manufacturer globally of commercial vehicles in 2018 and the 5th largest manufacturer of passenger vehicles. It made more than 4 million cars in 2018 and was slated to become the 3rd largest passenger vehicle (PV) market by 2020.

INTRODUCTION

The Indian auto industry currently is faced with its worst crisis in years. The government of India has finally recognised this crisis and has recently come up with a slew of measures to tackle the problem.

The Indian Automotive Industry that is pegged at Rs.4,800 billion contributes 7.5% to India's overall GDP and 49% to the manufacturing GDP and generates about 37 million jobs through manufacturing, services, dealerships and various forward and backward linkages. With a manufacturing volume of 4.5 million units in 2017-18 (without two wheelers) and corresponding sales of 4.02 million units, it is the 4th largest automobile manufacturer in the world. It is the largest two-wheeler market in the world overtaking China with 17.5 million units' sales in 2017. India was the 7th largest manufacturer globally of commercial vehicles in 2018 and the 5th largest manufacturer of passenger vehicles. It made more than 4 million cars in 2018 and was slated to become the 3rd largest passenger vehicle (PV) market by 2020.



CURRENT SCENARIO

As per industry data, 26.27 million vehicles were sold in FY18-19 (sales CAGR was 6.71 between FY13-19). 30.92 million Units were manufactured in FY18-19 (Production CAGR was 6.96% between FY13-19). The industry had been on a buoyant growth cycle with a CAGR of 6.71% in FY13-19 and a YOY growth of 9.5% in 2017.

The industry's misfortunes commenced around September-October 2018 when disparate events converged to halt the steady growth it had witnessed over the previous few years.

As per industry reports, India's domestic passenger vehicle sales fell for the ninth straight month in July 2019, amid a deepening crisis in the country's automobile sector that has triggered large-scale job losses.

Sales of passenger vehicles to car dealers fell 30.9% to 200,790 in July, as per the Society of Indian Automobile Manufacturers (SIAM). Commercial vehicles sales fell 25.7% to 56,866 units. Motorcycle and scooters sales fell 16.8% to about 1.51 million units, while passenger car sales fell 36% to 122,956 units. SIAM data also showed that domestic passenger vehicle production was down nearly 17% in the month.

India's S&P BSE auto sector index has fallen 23% this year, with the country's top automaker Maruti Suzuki's market valuation falling 18.3% since the beginning of this year.

The simultaneous decline in car sales with a falling demand for consumer goods is seen as a major sign of an economic slowdown in India. This is at a time when there is a liquidity crunch in the country's shadow banking sector and has impacted the availability of credit in the market.

India's auto sector is cutting thousands of jobs citing slumping sales of cars and motorcycles, with many companies forced to shut down factories for days and axe shifts. The auto component industry body ACMA (that employs five million people) fears that massive job losses to the tune of one million are inevitable if the situation is not addressed immediately.

FACTORS LEADING TO THE CRISIS

The initial decline in sales, that started in September-October 2018, stemmed from a drop in consumer demand that cannot be attributed to a single factor but catalysed from a number of simultaneous or concomitant yet disparate events – a mix of Governmental legislation, regulatory and Activist-court rulings, defaults in the financial sector and the overall macro-economic scenario – all combining together to create an atmosphere of uncertainty and trepidation both in the industry and well as consumers.

In anticipation of buoyant sales during the festival season in 2018, manufacturers had planned their production schedules. A ruling by IRDA to buy increased insurance upfront for 3 to 5 years for various categories of vehicles, a sudden spike in fuel prices, increase in axle loading norms for commercial vehicles (CVs) by around 20 percent were compounded by the IL&FS defaults.

The IL&FS defaults have percolated in various parts of the economy and have severely impacted aggregate demand in many consumption-focused sectors including the auto sector. Also, many NBFCs who were trying to rollover their liabilities at stiff borrowing rates and were forced go slow impacting growth in sectors such as automobile sector and housing finance.

What has followed is a severe crisis of confidence and all-pervading fear psychosis among borrowers, as well as lenders, who have started doubting the solidity of balance sheets of counter parties. This has pushed many other large and highly leveraged corporate houses to the point of default and adding further pressure on an already stretched banking sector over burdened with non-performing loans.

It is in this environment of heightened risk aversion that the auto industry was looking forward to pro-active measures from the policymakers to help resuscitate demand.

Policy Ambiguity

The industry has invested heavily in upgrading their products to comply with BS-6 emission norms that have been made mandatory from April 1, 2020. Because of overzealous policy makers and Activist Courts, Indian manufacturers have been forced to switch from BS-4 to BS-6 in just 3 years, whereas even Europe gave its advanced industry 10 years to make the switch to Euro-VI in 2 stages. This switch will add a substantial 10 to 15 percent to the cost of vehicles, especially in an environment of subdued sales. Similarly, large investments running into a few thousand crores have been made by Oil refiners for lowering sulphur content of fuel before the switch.

Even while the industry was racing against time to be BS-6 ready by April 2020, the NITI Ayog issued several notifications and statements that the industry needs to switch over completely from internal combustion engines to Electric Vehicle (EV) technology – in case of three-wheelers by 2023 and two-wheelers by 2025. This was without due consideration of the fact that India still has a grossly inadequate charging infrastructure; lithium-ion battery manufacturing has just rolled out and is at an infant stage with costs of imported lithium-ion batteries being high and the fact that there is Chinese chokehold on the rare earth metals that go into these batteries.

The geo-economic dangers of being dependent solely on an adversary like China as against scores of crude oil suppliers is something the policymakers still need to think through.

Even the incentives offered for EVs under the FAME India (Faster Adoption and Manufacture of [Hybrid and] Electric Vehicles) Scheme are insignificant: 10 percent for two-wheelers and 3-4 percent for cars over five years do not justify the more than double price difference vis-à-vis a similar-sized IC (internal combustion) engine vehicle. Thus pushing the industry into the EV space looked to be totally out of sync with planning and preparedness both of the government and the industry.

The increase in premiums due to the inclusion of third-party clause in insurance policies as mandated by the courts has not helped either as it has led to the increase in vehicle ownership cost.

The industry has been lobbying with the government for quite some time for a reduction of GST rates on vehicles from 28% to 18% with a view to reduce on-road cost of vehicles and thus stimulate demand. The government has been ambivalent on this demand from the industry - keeping both industry and consumers in a state of suspense regarding its final decision on the matter. The recent roll-out of the new Motor Vehicles Act and the stiff penalties mandated by it, although justifying a much larger objective of on-road safety, could not have come at a worse time for the industry. All this has further aggravated decline in demand for vehicles.

To summarise, the factors that influenced the precipitous fall in auto demand are:

1. Stagnation in the financial system and shortage of credit.
2. Higher cost of interest.
3. Court mandated strictures in respect of homologation from BS-4 to BS-6.
4. Lack of policy clarity for adoption of newer fuel efficient technologies like EV.
5. Uncertainty in respect of GST rate for vehicles.
6. An atmosphere of uncertainty for the industry resulting from a mix of all of the above.
7. A wait and watch policy adopted by consumers who procrastinate purchase in the wake of mixed signals from the government policy makers and courts.
8. Muted/Negative and depressed sentiment both of consumers and lending institutions on account of all the above.

A vicious cycle seems to be in operation where low demand has resulted in a slump in industry sales leading to job losses and a consequent further fall in demand and so on.

The industry is therefore in the immediate need of a balanced, clear and pro-active intervention of policymakers that alone can stem this steep slide. A cash-for-clunkers scheme similar to the Car Allowance Rebate System (CARS) in the US is the need of the hour; that will encourage not only the industry to rapidly move forward to adopt cleaner and greener technologies but also incentivise consumers to trade their old vehicles for more fuel efficient ones. Such a program has the potential to simulate demand and the economy as evidenced in the US.

FUTURE PROSPECT

The Honourable Finance Minister recently met industry representatives and made a slew of pronouncements on 23rd August 2019 with an aim to mitigate the situation. The more significant and relevant measures announced were:

1. BS-4 vehicles purchased till 31st March 2020 will be allowed to remain operational till their entire period of registration. (However it is not yet clear if road-worthy vehicles will continue to be registered after expiry of their registration period.)
2. Upward revision of one time registration fee deferred to June 2020.

3. All vehicles acquired from August 2019 to March 2020 to enjoy additional 15% depreciation taking the total depreciation to 30%.
4. Both IC vehicles and EVs will continue to be registered at the same time. Government's focus will be on setting up infrastructure for development of ancillaries and components including batteries for export.
5. In order to boost demand government will lift the ban on purchase of new vehicles to replace old vehicles by government departments.
6. Government will soon announce and implement a scrappage policy for old or non-roadworthy vehicles after finalising the infrastructure for scrapping old vehicles.

Apart from this, the Finance Minister announced a number of measures that would provide relief to investors and MSMEs and boost the banking sector while improving credit and liquidity in the economy with an aim to improve market and consumer sentiment.

A few days later, the government indicated that it will consider and take up with the state governments if a downward revision of GST for vehicles from 28% to 18% was feasible as demanded by the auto industry. However, the government needs to quickly take a final stand on this to prevent deferment of purchases by the consumers which could further stall the industry's growth.

Apart from this to propel a turnaround the government needs to provide at least partial relief from the current additional cess of Rs 2 per litre that is imposed on petrol and diesel. This will in turn bring down the overall cost of operations for the transport industry and encourage higher movement of commercial vehicles that will result in higher economic activity.

RBI and the banking system needs to further reduce interest rates and increase the availability of channel finance and consumer finance (for sectors like autos) that will help all – manufacturers, dealers/ intermediaries and consumers.

Introducing a measure like the Troubled Asset Relief Program (TARP) will also help. TARP was used successfully by the US Treasury to revive its frozen credit markets and restore economic growth by buying troubled companies' assets and shares.

Given that thousands of jobs have already been lost due to plant closures and dip in sales and millions more risk losing theirs in the immediate foreseeable future in case the decline is not arrested, the government needs to urgently review its timelines for BS-6 and EV implementation. Although the auto majors have their FG inventories in vehicles under reasonable control, the ancillary industry that supplies components to these majors are piled up with unmanageable inventory due to order cancellations and delays (some smaller suppliers have even been forced to close shop). The few months left till March (when BS-6 takes over) is grossly inadequate for these suppliers to get rid of the inventory given the demand situation. Unless sufficient time is given for liquidating their BS-4 component stock, these ancillary units will face huge and unrecoverable financial losses forcing many more to totally shut shop resulting in further and unprecedented job losses. Even if the courts mandate the timeline of 31st March 2020 for BS-6, the government needs to explain the logic to courts and delay the same thus saving the livelihood of millions.

Finally and most importantly, the government must take steps to establish a single, credible and unambiguous channel of communication with the industry as well as the consumers to avoid the kind of double-talk and confusion that was created in the recent past by poorly considered and vague statements that emanated from its various quarters like the Niti Ayog and so on. This will ensure that policy directions are logical, well-thought out and have clarity for its recipients.

List of Abbreviations used in the article, not explicitly explained above:

1. GDP – Gross Domestic Product
2. CAGR – Compound Annual Growth Rate
3. ACMA – The Automotive Component Manufacturer Association
4. S&P BSE – Standard & Poor Bombay Stock Exchange
5. IL&FS – Infrastructure Leasing and Financial Services
6. NBFC – Non Banking Financial Company
7. GST – Goods and Services Tax
8. MSME – Micro Small and Medium Enterprises

BIBLIOGRAPHY

1. *Finance Minister Nirmala Sitharaman announces slew of measures for the auto sector | Moneycontrol.com – August 23, 2019*
2. *With India's economy growing at about 7%, why the auto industry is hurting so badly? | The Economic Times – April 28, 2019*
3. *Govt measures to revive auto sector yet to make impact on ground level: FADA | Hindu Business Line News – September 3, 2019*
4. *Slowdown Blues: India's passenger vehicles sales drop 31% in July; record 9th straight dip | Business Today – August 13, 2019*
5. *Automobile Industry in India, Indian Automobile Industry, Sector, Trends, Statistics -July'19 (India Brand Equity Foundation – IBEF)*
6. *Performance of Auto Industry during 2018-19 | SIAM*
7. *www.fadaindia.org/ presidents-messages-list /527 | FADA – July 2019*
8. *www.fadaindia.org/fada-newsline-list/526-fada-president-applauds-finance-minister-announcement-for-auto-sector | FADA – Aug 2019*
9. *Automobiles-Infographic – May 2019*
10. *Zero Emission Vehicles (ZEVs): Towards a Policy Framework | EV report- NITI AAYOG – Global Mobility Summit, September 7 & 8, 2018*
11. *Passenger vehicle industry: India made four million cars in FY18 | Business Standard News – April 16, 2018*
12. *EVs: NITI-Aayog warns 2-wheeler makers to pull up socks or lose to start-ups | Hindu Business Line News – June 21, 2019*
13. *Niti Aayog's e-mobility plan: only electric vehicles to be sold by 2030 | TechSparks 2019 –June 18, 2019*
14. *India Motor Vehicles Sales Growth 2002 - 2019 | Monthly | % | CEIC Data*
15. *SIAM-car-sales-may-2019-data-show-indias-auto-sector-is-in-dumps | Quartz India – May 2019*
16. *Complete Indian Auto Sales Analysis 2018: CV sales cross one million mark | Auto – The Economic Times – February 12, 2019*
17. *Auto sector crisis: August 2019 turns out to be another gloomy month for major carmakers in India | India Today – September 4, 2019*
18. *Complete Sales Auto Analysis April 2019| auto.economictimes.indiatimes.com – May 4, 2019*
19. *Passenger Vehicle sales continue to slump for 7th straight month | auto.economictimes.indiatimes.com – Jun 3, 2019*
20. *Complete Sales Auto Analysis June 2019| auto.economictimes.indiatimes.com – Jul 2, 2019*
21. *Auto retail sales continue to decline shows registration data, Q1 sales down 6% | auto.economictimes.indiatimes.com – Jul 17, 2019*
22. *Auto sector in slide mode: Sales dip across categories as sentiment stays weak | auto.economictimes.indiatimes.com – Aug 2, 2019*
23. *Tens of thousands losing jobs as India's auto crisis deepens | auto.economictimes.indiatimes.com – Aug 6, 2019*
24. *Complete Sales Analysis August 2019: Auto cos sales further see a downward trend | auto.economictimes.indiatimes.com – Sep 2, 2019*