

The Hinterland Millions

India has a population of more than 1.2 billion and nearly 69% (2011 Census) of that live in rural areas. These millions are responsible for billions of dollars of business for Indian vehicle manufacturers. Manufacturers like Tata Motors, Mahindra, Bajaj Auto and Maruti-Suzuki sell a few hundred thousand vehicles to this rural population and make a few billion dollars in revenues.

It's also the kind of revenue, which everyone likes.

You see, the rural market is demanding in terms of lower prices, lower maintenance, lower fuel consumption etc but won't complain about trivial things like NVH levels, gearshift smoothness and quality of air conditioning.

Or safety...

Best thing is, it is a market where you don't need to worry about model cycle changes every 6-7 years. A platform can have a lifecycle easily ~~five times~~ thrice as long as a passenger car and even after that only need some feature addition than a complete retooling.

Even better, the disruptive guys like Ford and Honda ~~turn all snooty at the mention of these products~~ cannot even dream of entering these segments for many more years. The low cost nature, frugal engineering and a made-for-Central-Africa kind of approach just takes the Aces and REs out of reckoning of the MNC skunkworks.

Also, you'd rather die than see the Volkswagen badge on an Indian micro truck.

Which leaves the field wide open for local manufacturers – Tata Motors, Mahindra, Ashok Leyland, Bajaj Auto and Maruti-Suzuki.

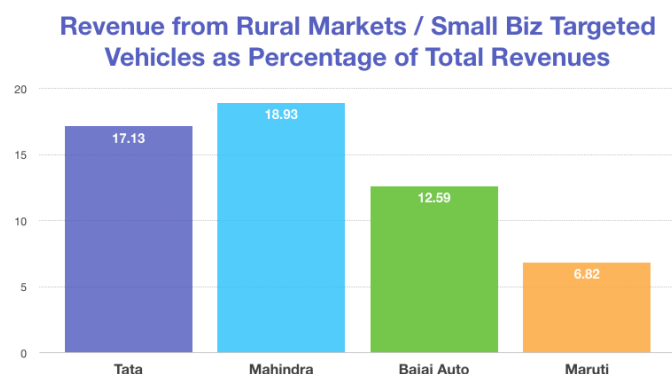
The rural market essentially accounts for two types of vehicles – Goods carriers and Passenger carriers. The Goods carriers are the drivers of business while the Passenger carriers – mostly working as shared cabs – are responsible for the daily commute of the common man in the hinterlands.

How much does the base of the pyramid contribute?

Together, the two accounted for nearly 1.1 million units in CY2013. For the purpose of this analysis, we consider all three-wheelers, all small trucks (below 3.5T) and all Vans (both Hard-top and Soft-top included) as part of this group.

The revenue from these 1.1 million units is significant for the participants. For manufacturers like Mahindra, the revenue share from the rural market targeted vehicles reaches almost 20% of their overall revenues. For others, the share is lower.

EMMAAA did a back-of-a-napkin calculation of revenue share of the non-urban customer in vehicle manufacturer's revenues. However, while looking at the figures one needs to keep in mind that the actual revenue share may be higher as the revenues considered are only from new vehicle sales. Share of earnings from finance or after sales has not been considered.



Analysis - EMMAAA;
Best approximation from market prices, accounting for dealer margins and logistics costs;
Not considering the vehicles share in after sales service revenue

The non-urban customer delivers a significant chunk of revenue to Indian carmakers

Quality of profits

However, these vehicles often bring in the fattest profit margins with the least headache. They require little in terms of product upgradation, advertising, communication or sales promotions. Once established, they are money printing machines on wheels and a dream for the Engineering / R&D departments as they can easily sleep for a few many years before something needs to be tinkered. Even the most aggressive of the participants – Maruti-Suzuki – has been continuing with the Omni platform, with little modifications, for nearly three decades now.

Goods Carrier Segment

Small businesses need small wheels and often the chosen mode of transport is small trucks. For the purpose of this analysis, small trucks include micro-trucks and conventional pick-up trucks.

Micro-trucks are vehicles unique to India though similar in looks and construction to the Kei trucks sold in Japan. However the refinement (or lack of it) and pure utility nature of target usage makes the Indian trucks much cheaper than comparable Kei trucks.

The small truck segment was traditionally dominated by pick-up trucks – mostly traditional Mahindra utility vehicle based pick-ups with platforms dating back to 1960s. Continuous refinement in terms of engines and gearboxes has kept the platforms alive and Mahindra still sells close to 10,000 of these vehicles in a good month. Most of these vehicles are between 2T and 3.5T GVW.



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Sensing an opportunity between the 0.5T GVW three-wheeler goods carriers (incapable) and the 2T pick-ups (expensive), Tata Motors introduced the Ace micro-truck in 2005. Within the first year, the Ace cornered volumes of more than 50,000 units.

Sales have grown spectacularly since then and 2012 saw the Tata micro-truck (along with variants Super Ace and Ace Zip) selling more than 20,000 units every month.

With such a success comes ~~great responsibility~~ a number of misconceptions, legends and myths.

Mythbusters

There are two types of lies – ~~statistics and~~...popular perception and urban legends.

Popular Perception 1: Ace has been growing faster than the overall small truck market

This is true to an extent but only in the two years of the Ace's launch. Tata Motors held a 57% share of the small trucks market in 2005, the first year of the Ace in the market. In 2006, the share had jumped to over 70% as the Ace was quite well received in the market.

However, post that with Mahindra widening its range of utility vehicles offerings, and some price rationalization, the Ace has been continuously losing market share in the small trucks segment. Since 2006, when the Ace held a 70%+ share of the market, its share has continuously dropped to a little less than 54% in 2013.

Looking at it in another way, the Ace has grown slower than the rest of the market in the last seven years.

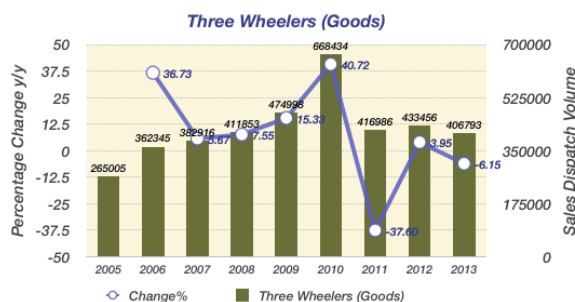
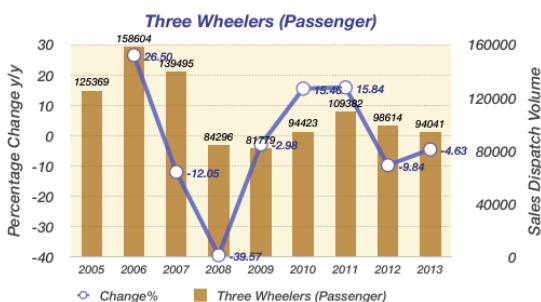
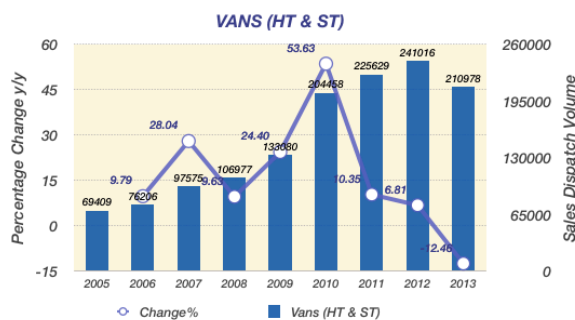
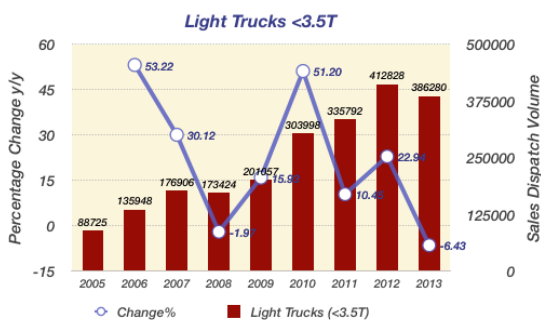
Popular Perception 2: Tata Ace killed the three-wheeler

Yes & No. Since the introduction of the Ace in 2005, the three-wheeler (Goods carriers) market has shrunk by 25%. In overall volumes, this is a loss of about 31,000 units over eight years.

This may still appear significant till we start peeling off layers of the data. Most of this volume loss did not happen due to the introduction of the Ace. During the first year of the Ace's introduction, three-wheelers sales managed to maintain a strong growth trajectory, growing by 26.5% in 2006. A strong decline was seen between 2007-09 with sales hitting the bottom of less than 82,000 units. However, post that strong double-digit growth was again witnessed in 2010 & 2011.

In a nutshell, three wheelers are not clutching their collective hearts and dying in a hurry. Somewhere, in the hinter of the hinterlands, there is a class of people, and a set of businesses, too difficult to classify, which still prefer three-wheelers to micro-trucks.

THE AUTOMOTIVE UNDERBELLY



Passenger Carrier Segment

The passenger carrier segment essentially comprises of soft-top vans and hard-top vans. The hard top Van segment has existed since the mid 1980s when Maruti introduced the Omni in the Indian market. Till 2007, Maruti was the only player in the segment and the Omni was the ubiquitous choice for vans in the cities and smaller towns. The need of shared transport in the smaller towns and the rural areas was being met by three wheelers.

Seeing an opportunity (Again), Tata Motors introduced the Magic, essentially a passenger carrying version of the Ace. With canvas windows, the Magic was as utilitarian as they come. However, sales were brisk and the company was shipping more than 2000 vehicles every month in 2008. Sales crossed 87000 units in 2012 and new competition has come in the form of Mahindra Maxximo & Gio vans.



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Maruti also added to the Omni with the Eco van and met with huge success. Maruti now has two vans and it has been able to push the Eco to passenger transport buyers and the Omni for cargo carrying applications. Omni still does decent numbers because of Maruti's willingness to keep the product alive through heavily customized variants.

With the Eco catering to the urban centers and the Magic to the rural areas, the demarcation between the vans is quite clean.

Is the product answering new questions?

Often the new entrants in the market have barely grown the overall market. In the Van market, the last major increment came in 2010 with the introduction of the Maruti Eco. The

Eeco grew the market (and Maruti sales) by more than 60,000 units.

However, the same effect was not seen with the launch of the Maxximo hardtop van. Most sales have come at the expense of the soft top variant.

Tata's Venture hard top van is another vehicle, which has failed to take off. While the soft top Magic still does brisk numbers, the Venture hasn't taken off yet.

2013: The year when everything shattered

Nearly every automotive segment, barring two-wheelers and a handful of passenger vehicle segments, crashed in 2013. Small trucks, vans and three wheelers sales were also depressed in the year. The pressure on sales of these segments is an accurate indicator of the state of small business in the country.

Such a decline could mean that the rural economy is under pressure so much that cab & fleet operators are not replacing their fleet. A lack of a scrappage scheme or roadworthiness certificate requirements means that operators can keep plying these vehicles till they fall apart.

Another, and even graver, reason for the fall in numbers could be that the rural market is already reaching some kind of saturation and manufacturers are unable to penetrate further.

A lack of new product initiative and / or significant product enhancements to the existing line-up also mean that fleet operators running these vehicles have no incentive to buy new ones.

Small truck sales were down 6.5% in 2013 while Vans were down 12.4% over 2012. Sales of Passenger three wheelers were down 6.1% while those of Goods carriers fell 4.6% over last year. However, Good Carriers sales had already fallen 9.8% in 2012.

Why doesn't Ford Honda Toyota any global carmaker bother?

It's a mix of reasons – global volume planning, product development experience, frugal engineering and lack of dealership network in no particular order.

Product development experience is significant as none of the global carmakers has anything similar to the Ace in their product portfolio. And developing one from scratch may not make sense as their R&D engineers lack the expertise to develop a product at the targeted price. Such a product may only work in India and a few developing markets and volumes may be constrained. With low volumes, the costs go up.

In some ways, it is like asking Lego to develop Ludo.

At an internal meeting of a global carmaker ~~willing to take~~ dreaming of taking on Tata in the Ace market, the engineers of the global engineering centre were dismayed at the wish list from the sales department. One of the items was a Power Take Off (PTO) shaft, allowing the buyer to use the vehicle as an irrigation pump for his fields.

The engineers had never seen such an application and could not imagine one. The vehicle is still 'under development'.

Product design becomes even more complicated when global vehicle manufacturers start rummaging through their parts bins to source some readymade modules for the intended vehicle. ~~Not~~ ~~many~~ Hardly any have a small, two cylinder, low cost, simple design, low maintenance, naturally aspirated, sans space-age material, very high mileage diesel engine sitting on their shelves. Designing one will add a few hundred million dollars to the project cost. Sourcing one from someone like Kubota may complicate things further, making them unmanageable.

Volume planning becomes a serious issue, as India is perhaps the biggest and only market for such vehicles with specifications matching the Ace. With limited volumes on

offer, the platform becomes unviable.

Dealer reach is another big hurdle. Most global carmakers have networks that are limited to the big cities while the major market for these vehicles is in the smaller towns and rural areas. Dealership networks will take time to expand and need volumes.

Which is a rather chicken-and-egg situation.



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