

# Suppliers' Profits – Beginning of the end?

*This is Part II of our on-going analysis of supplier profitability and risk evaluation. Read Part I [here](#).*

Going by the widespread downturn in the industry, one would expect that the supplier fraternity would have lost significantly in terms of operating margins.

However, (quite shockingly) the overall operating margin of the industry actually improved in the last four quarters, over the previous four quarters. In the last four quarters, the overall industry (sum of 69 prominent, publicly traded supplier companies) operated at a margin of 9.82%. In the four quarters prior to that, the industry's operating margin was 9.16%.

That is a surprisingly healthy growth of 64-basis points in a time when senior executives, facing a severe downturn, prefer ignoring calls from scribes to avoid answering uncomfortable questions.

But then, a deeper look at the data reveals the deception within.

## **Not many suppliers improved their margins**

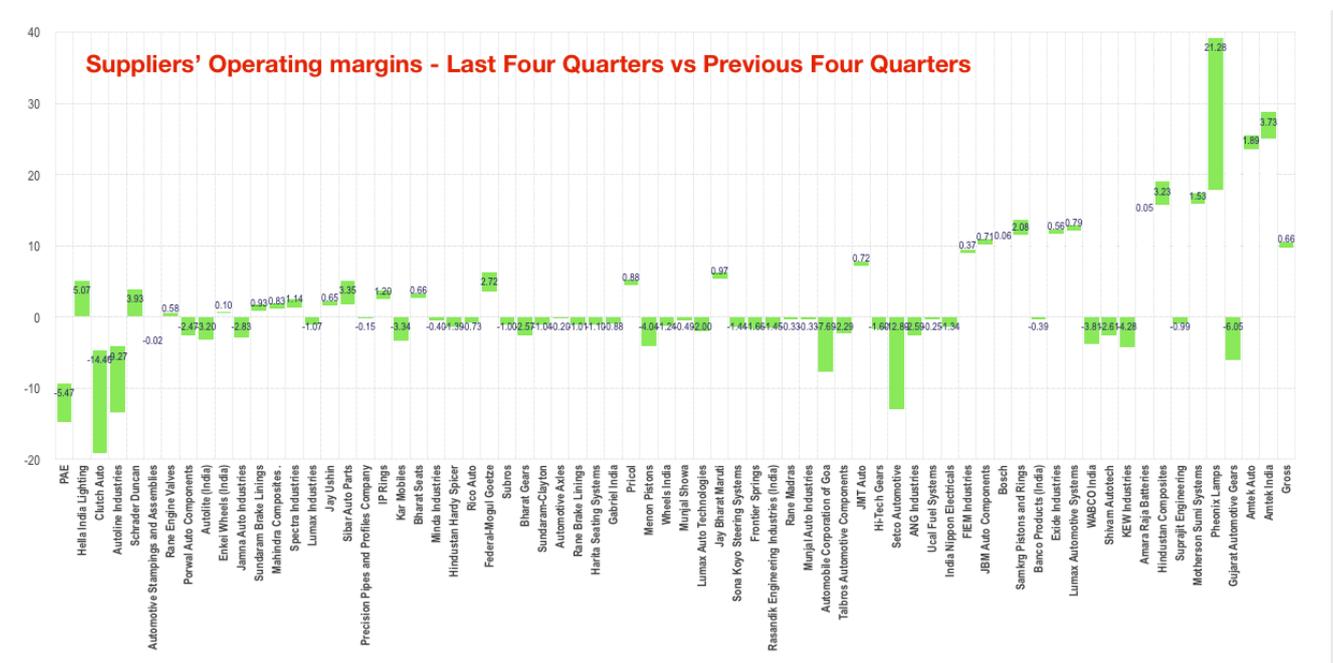
Out of the 69 suppliers under study, only 27 managed to improve their margins. The remaining 42 witnessed erosion in margins as OEMs – under pressure themselves – extracted greater price discounts from suppliers. In many cases, supplier plants were running at below optimum capacity utilisation due to a slowdown in demand. In most cases, suppliers were happy to keep their plants running at the cost of margins, as a closed plant would have incurred even greater

losses.

Apart from that, suppliers also had to deal with a weakening INR, which resulted in commodity prices spiralling out of control. It being a recent phenomenon, suppliers could not convert the weak INR into increased exports during the evaluation period. However, those with a steady international business saw a jump in exports revenue on account of the weak INR.

### Play of data

Deciphering the data, case-by-case, it is apparent that the positive bias of the overall industry profit margin is because of data being skewed by a few cases. **Some** All big suppliers saw a healthy jump in margins and that shifted the average firmly into positive territory.



Most suppliers end up with a decline in margins

Mega suppliers Amtek Group and Motherson Sumi witnessed a large jump in their operating margins. In both cases, the jump was driven by the international business coming through acquisitions. Both Amtek Group companies – Amtek Auto and Amtek India – managed to improve their operating margins

significantly. Amtek India's operating margins in the last four quarters were up 3.73% to 25.04% over the previous four quarters operating margin of 21.31%. Group company Amtek Auto's operating margins were 23.64% in the last four quarters, a 1.89% improvement over last four quarters operating margins of 21.75%.

### **Exports Drive Margins for Mega Suppliers**

In both cases operating margins were driven by the international acquisitions of Neumayer Tekfor and the Kuepper Group. The international business, most of which is in Europe, comes with healthy operating margins, further aided by a weak INR. Amtek may see a further improvement in operating margins as the group's Indian plants become more integrated in their global supply chain. In this financial year, Amtek expects exports / international business to account for 44% of the group's revenues.

Motherson Sumi has a similar story. The company's international acquisitions of Schefenacker (now Visiocorp) and Peguform have provided it with a healthy international business and operating margins improve as a result. In the last four quarters, Motherson Sumi operated at a margin of 15.86%, a 1.53% jump over previous four quarters operating margins of 14.33%.

The two big battery suppliers – Exide and Amara Raja – also managed to improve their margins. Exide's operating margins in the last four quarters were 11.72%, a 56-basis point improvement over previous four quarter operating margins of 11.16%. Amara Raja was a little behind as it improved its margins by five-basis points to 14.26% in the last four quarters.

Mega supplier Bosch also nudged its operating margins up by six-basis points on a very large base. The company has been operating at margins of 10.31% in the last four quarters. For

Bosch to improve its operating margins further, the company would need to shift some more component lines from Europe to India.

### **Better efficiency drives large suppliers**

Amongst the large-sized suppliers, Jay Bharat Maruti and sister concern JBM Auto Components managed to squeeze a lot more margins out of their operations. Jay Bharat Maruti, primarily supplying to Maruti-Suzuki, has been operating at 5.32% margins in the last four quarters, compared to 4.35% margins in the previous four quarters. Sister concern JBM Auto Components, supplying to other OEMs, managed operating margins of 10.21% in the last four quarters, a 71-basis points jump over operating margin in the previous four quarters.

Significant improvements in operating margins were also recorded by Federal-Mogul Goetze, Samkrp Pistons & Rings and Hindustan Composites. Federal-Mogul operated at 3.61% operating margins during the last four quarters, a 2.72% improvement over the previous four quarters. Hindustan Composites managed to improve its operating margins by 3.23%, from 12.55% in the previous four quarters to 15.5% in the last four quarters. Similarly, Samkrp Pistons due to better exports realisation, managed to improve margins. In the last four quarters, the company operated at 11.54% margins, a 2.08% improvement from 9.46% margins over the previous four quarters.

### **Two-Wheeler suppliers make merry**

FIEM Industries, Phoenix lamps, and Pricol benefitted from being key suppliers to the two-wheeler industry, which is relatively stable, unaffected by the slowdown. FIEM operated at margins of 9.01%, 37-basis points improvement from the previous four quarters. Pricol was operating at 4.42% operating margins, 88-basis point improvement from margins of 3.54% during the previous four quarters.

However, the big turnaround was Phoenix Lamps, which is now operating at 17.88% over the last four quarters. In the previous four quarters, the company had negative operating margins of 3.4% implying a 21.28% improvement in margins. Phoenix Lamps is now mostly exports oriented and the company ships to 75 countries.

Both Hella India Lighting and Schrader Duncan improved their margins significantly over the last four quarters. However, they continue to operate at negative losses. Meanwhile, Sibar Auto Parts was able to move into the positive operating margin zone with 1.78% margins in the last four quarters, a 3.35% jump from negative margins of 1.57% in the previous four quarters.

### **Laggards**

For every two suppliers improving their margins, there were three who were operating at lower margins than before. The worst affected were suppliers to the Buses & Medium & Heavy Commercial Vehicles (B&M&HCV) sector. Clutch Auto, Setco Automotive, Autoline Industries and Automobile Corporation of Goa, all major suppliers to the B&M&HCV segment, witnessed sharp declines in their operating margins.

Clutch Auto was the worst hit as the company saw a 14.46% decline in operating margins in the last four quarters. The company operated at negative 4.63% margins during the last four quarters as against 9.83% margins in the previous four quarters. Apart from the slowdown in the B&M&HCV segment, the company was also hit by labour problems and had to shift their manufacturing plant.

Rival Setco Automotive was hit badly as well. The company has been operating at margins of 7.78% over the last four quarters, a 12.89% decline from margins of 20.67% in the previous four quarters. In comparison to Clutch Auto, Setco performs at better margins due to the company's strong

exposure to the exports aftermarket.

Autoline's operating margins declined by 9.27% from 5.13% in the previous four quarters to negative 4.14% in the last four quarters while ACGL's operating margins eroded by 7.69% from previous four quarters to 6.37% in the last four quarters. In the previous four quarters, ACGL was operating at 14.06% operating margins.

Other B&M&HCV suppliers which could not sustain their operating margins included Jamna Auto (down 2.83%), ANG Industries (down 2.59%) and Autolite India (down 3.2%).

While two-wheeler suppliers like Pricol and FIEM improved their margins on the back of higher production, the Hero MotoCorp family supplier group saw erosion in operating margins. Munjal Showa's margins were down 49-basis points, from 5.56% in the previous four quarters to 5.07% in the last four quarters. Similarly, Munjal Auto Industries' operating margins were down by 33-basis points, from 6.6% in the previous four quarters to 6.27% in the last four quarters. Hi-tech gears, another Hero family supplier lost 1.6% in margins and operated at 7.78% operating margins during the last four quarters. The biggest loser in the Hero Group was Shivam Autotech whose margins were down by 2.61%. However, the company is still amongst the top suppliers in terms of margins, operating at 13.25% margins during the last four quarters.

### **The Low becomes lower**

In many cases, the simultaneous slowdown in the commercial vehicles and passenger vehicles segments means that suppliers have been forced to lower their margins even further from the already meagre margins they were operating at. Rico Auto operated at 3.51% in the last four quarters, 71-basis points down from the previous four quarters margin.

Similarly, Gabriel India operated at 4.39% over the last four

quarters, 88-basis points down from the previous four quarters. Similarly, Subros operated at 3.61% margins during the last four quarters, 1.0% down from the 4.61% margins of the previous four quarters.

Rane Brake Linings is another supplier, which sacrificed margins over the last four quarters. The company's margins were down 1.01%, from 4.96% in the previous four quarters to 3.95% in the last four quarters. Similarly, Sundaram-Clayton's operating margins were down 1.04%, from 4.77% in the previous four quarters to 3.73% in the last four quarters.

Lumax Industries was hit even worse as the supplier's operating margins dipped to 1.58% in the last four quarters, from 2.65% in the previous four quarters.

Harita Seating Systems' business was hit in both the passenger vehicles as well as Bus segments. The company operated at 4.31% operating margins during the last four quarters, down 1.1% from 5.41% operating margin in the previous four quarters.

Wheels India lost 1.24% in operating margins and worked at 4.86% margins during the last four quarters. Sona Koyo sacrificed 1.44% in operating margins, from 6.98% over the previous four quarters. Similarly, Rasandik Engineering's margins were down 1.45%; Lumax Auto Technologies' operating margins were down 2.00% and Talbros Automotive Components's margins were down 2.29% over the last four quarters.