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VOL. 01/24

SECTOR REPORT

2 November 2017

Two & Three Wheelers: Robust performance

Diwali came early for the Indian automobile industry. Official industry sales data for September 2017 showed all vehicle segments put together have closed in on the 2.5 million mark. In fact, all segments – passenger vehicles, commercial vehicles, three-wheelers and two-wheelers– have posted robust growth. What the September 2017 sales numbers indicate is that demand has bounced back, particularly from rural India. A combination of new vehicle launches, a bountiful monsoon in most parts of the country translating into demand for PVs, small CVs and two-wheelers, as well as a boost in consumer demand from the nine-day Navratri festival and Dussehra, which is seen as an auspicious day to buy vehicles, have helped automakers post robust numbers.

In September, overall two-wheeler industry registered 10% rise to 22,92,707 units on a y-o-y basis. On a m-o-m basis, sales were higher by 7.8%. Motorcycle sales were 10% higher on yoy basis at 14,87,581 units. Sales were 11.1% higher over the month. Sales of scooters were 12% higher at 719,796 units. Sales were 1.8% higher over the month. Mopeds sales rose 7% at 85,330 units. Moped sales were 2.9% higher on mom basis.

In the domestic market, 2W volumes rose 9% at 20,41,024 units in Sept17. Motorcycles sales were 7% higher while scooter sales rose 13%. Mopeds sales rose 8%. Overall three-wheeler sales rose 23% to 97,083 units in Sept17 and sales were higher by 16.4% on mom basis.

In Sept 2017, the two wheelers segment also posted robust growth, with Hero Motocorp, TVS Motors and Eicher Motors (RE) posting double-digit growth. TVS Motors was the star performer with 22.2% growth.

Clearly post BS-IV enforcement, two-wheeler sales are witnessing new permutations and combinations and it will be a while before the market settles down.

2-W sales in FY17 were racing until demonetization hampered its sales growth. Overall, the Indian two-wheeler industry closed FY2017 with a growth of 5% to 19,928,784 units. Scooter, motorcycle and mopeds grew 12%, 2% and 23% respectively.

Overall three wheeler sales industry closed FY2017 with a drop of 17% to 785,108 units. While passenger carrier sales

dropped 20%, goods carrier sales rose 20%.

The domestic two-wheeler industry has been gradually picking up after the major fall it experienced since the cash crunch and weak demand sentiment that ensued post the discontinuation of higher denomination currency notes in November 2016, the industry closed March 2017 with a sales growth of 0.3%. For the month of March, 2017, the scooters segment reported a healthy YoY growth of 8.1% in its monthly volumes, and motorcycles segment reported de-growth of 3.3%.

Two Wheeler Segment Mix:

The polarization trend in the Indian two wheeler market is gaining strength as customers stick to market leader and top brands. The smaller companies are on constant decline. It could be due to the downturn, where normally consumers prefer to stick to market leaders and impose higher confidence in their products.

Led by new launches, the scooter segment grew at a faster clip of 8% YoY in FY 17 and 12% in FY 16 period against a 3% drop in m/c segment in FY 17 and nil in FY 16. The faster volume growth of the scooter segment led to an improvement in its share of the two-wheeler market during this period. The main drivers for this growth are (a) growing acceptability of gearless scooters, particularly by women, (b) rising urbanization and increasing proportion of working women and (d) new launches. From a share of just 17% in FY11, scooters accounted for 32% of the 17.58 million two-wheelers sold in the domestic market last year. The share of motorcycles has been on a decline.

With just one percentage point gap with entry-level bikes segment, automatic scooters are set to overtake the largest volume segment in the two-wheeler market that now controls only 36% of the pie, sooner than later. The time is not far off when automatic scooters will dominate the two-wheeler industry, say industry observers. The optimism comes from the fact that led with a 63% of the overall market pie in scooters space, Honda Motorcycle & Scooter India (HMSI) has been leading the market growth for many years by a wide margin for many years now.

Scooters had only 19% of the market in fiscal 2012, when

110cc bikes had 47%, which jumped to 32% for scooter but declined to 37% for bikes in fiscal 2017 and in April 2017 further narrowed to just 1%. This means that in flat six years, led by Honda, the contribution of automatic scooters zoomed to 35% in April 2017, while 110-cc bikes share declined from 49% to 36% in the same period.

Scooters have been able to offer better mileage in recent years. This, along with enhanced road networks, has helped volumes grow. Factors such as growth in the population of working women as well as a scooter's unisex appeal, light weight and automatic transmission have also contributed to the growth. In many families, scooters are usually bought by males but are now increasingly being used by women.

India was once primarily a scooter market and geared scooters ruled the market till the mid-1990s. Bajaj Auto was a dominant player. However, the entry of global players and introduction of newer motorcycles shifted demand away from scooters. Motorcycles surpassed scooters gradually. Gearless scooters from Honda brought interest back among buyers. However, Bajaj exited the segment. Today, it is the only major player that does not make scooters.

One of the biggest factors working in scooter's favour is its ability to cater to male as well as female riders, the so called Unisex appeal. On the other hand, motorcycles have traditionally been popular among male riders. Notably, scooters have significantly broadened the women customer base.

With better road infrastructure and more women joining the work-force, the primary requirement of riders has now shifted from just looking at mileage and price available in the 110cc motorcycles to the more zappy and unisex automatic scooters. Within 6 years, the contribution of automatic scooters to the domestic industry has also zoomed to 35% while the contribution of the 110cc motorcycle market has declined from 49% to 36% over the same period. In fact, Honda's market share in automatic scooters is now pegged at its highest 63%.

Automatic scooter sales are currently being driven by the rising number of women professionals opting for scooters. In addition, scooterisation that was till now mainly an urban phenomenon is slowly penetrating rural areas as well, hitherto a motorcycle stronghold. Two-wheeler marketers say this trend will continue with improvement in rural road infrastructure and more women and elderly customers joining the two-wheeler customer pool, and scooters will drive ahead due to their multi-usage edge.

Market Overview

Hero MotoCorp set a new benchmark for the two wheeler industry by reaching 720,739 units during September 2017, as against 674,739 units in the corresponding month last year, in the meantime registering a healthy growth of 6.8% YoY. Hero MotoCorp's monthly sales have been rising since March, after four straight months of decline since

demonetization in November. Going forward, one can expect good monsoon to provide a kicker as rural income is bound to improve with it.

Hero MotoCorp plans to launch three new scooter models by next fiscal as part of strategy to enhance its leadership position as erstwhile partner Honda challenges its number one spot. The company plans to launch a new 125 cc scooter in the fourth quarter of the ongoing fiscal, while two more new models will hit the market in 2018-19. Besides, the company is working to enhance its product portfolio in the premium motorcycle segment, with plans to launch a completely new 200cc sports bike by the end of this fiscal. The three new upcoming models will further augment Hero's existing portfolio of three scooters - Maestro Edge and Duet (both 110cc) and the Pleasure (100cc).

The company has phased out different models and variants as part of its plans to realign product portfolio to focus on premium bikes and scooters for future growth. The company has discontinued Ignitor, Hunk and HF Dawn models while it has already stopped selling of variants such as Maestro scooter, Passion Xpro, Splendor Pro Classic and Karizma R motorcycles in the recent months. In-line with this strategic approach, the company has already introduced four new versions of existing models — Glamour, Maestro Edge, Duet and Pleasure.

Following the demonetisation initiative of the government in November, Hero immediately installed and activated POS machines at its retail outlets and also rolled out several other effective initiatives to enable cashless transactions, including innovative and consumer friendly financing schemes. With improvement in the currency situation and in the consumer sentiment, Hero's volumes are gradually picking up.

The company is eyeing 1 crore unit sales by 2017-18.

HMCL plans to enter new markets globally, including Mexico and Nigeria, as it eyes 1 crore unit sales by 2017-18. The company aims at getting 10% of annual sales from export markets, at around 1 million units, by 2017.

Hero MotoCorp has lined up 35 new launches over the period of next three years.

The company had earlier announced plans to increase its footprint to 50 countries with 20 manufacturing facilities and assembly plants and sell 100 million two-wheelers cumulatively by 2020. By then, it hopes to achieve a turnover of Rs 60,000 crore from around Rs 24,000 crore now.

Bajaj Auto's, the world's third largest motorcycle manufacturer, posted total sales growth of 11.4%YoY at 369,678 units, led 7% growth in motorcycles to 247,418 units and also by a 31.9% YoY rise in 3 wheeler rates to 59,074 units. Exports registered robust growth by 21.3% YoY to 1,46,973.

The management has guided for export volume of 140-150k

units in Sept'17 and 1.7mn units for FY18 on back of stabilization witnessed in its key export markets like Philippines, Bangladesh, Egypt and LATAM. This implies a monthly run-rate of ~148k export units for the remaining part of FY18.

BAL remains optimistic about export sales and aims to achieve 800,000 units by H1FY18. The company's efforts in diversifying revenues from its export market has been fruitful as it has reduced dependence on geographies like Sri Lanka and Nigeria with incremental volume coming from Turkey, Iran & South-East Asia. The management has given guidance of achieving sales of 16 lakh units for FY18 in terms of export sales.

FY17 motorcycle volumes declined 5% YoY (18% YoY drop in exports and 4% YoY growth in domestic volumes) at 3.66 million units.

For the current year, Bajaj is focused on increasing its share in the value segment with launch of V15. Bajaj has been able to enhance its position in the entry level segment through models like new CT and Platina. The company hopes to improve its market share to close to 50% in premium segment. It is also focusing on increasing its market share in the mid-end motorcycle category (more than 110cc and less than 150cc).

Allotment of more 3W permits in Maharashtra or other states may provide the much needed fillip to its 3W business.

TVS Motors' September 2017 saw a double-digit growth of 17.2% in sales at 359,850 units as

compared to 293,257 units sold during the month of September 2016. Sale of two wheelers grew by 22.1%, driven by stellar jump of 43.3% in scooters at 121,601 units.

Also, mopeds (6.9% YoY to 85,330 units) and 3 wheelers (54.9% to 8,996 units) displayed a solid recovery trend.

Two wheeler exports continued to do well with 30.5% growth at 43,694 units against 33,475 units in September 2016.

The company is now expected to soon roll out the BMW G 310 R, an entry-level naked street motorcycle powered by a single-cylinder, 313cc engine, built under TVS Motor Company's alliance with Germany's BMW Motorrad.

TVS Motor Company expects its domestic sales of two-wheelers to grow by 10% in the coming fiscal.

TVS Motor is aiming to corner a fifth of India's two-wheeler market over the next three years, as it banks on products including the new Apache and Victor motorcycles to drive demand. The company is also seeking to break into a double-digit operating margin in the same period. TVS is aiming to produce 3.6 million to 4.2 million units a year by 2018-19.

HMSI recorded sales of 569,888 units in Sept 17. It managed additional volumes of only 30,484 units over its September 2016 sales (539,404 units). The company's YoY growth stands at 5.65%, the lowest among all the OEMs in September 2017. Nevertheless, considering the total monthly sales of 601,998 units (including exports),

September has now become the second month in a row when HMSI has reportedly breached the 600,000-unit mark.

The company last launched a new 110cc Scooter - Honda Cliq at Rs 42,499 (Ex-Delhi).

Over 61% of HMSI's total sales including exports come from the scooter segment. Honda Activa has been company's top seeking scooter for a while now and sensing the need of one more product the company has introduced Cliq to its existing line-up of five automatic scooters (excluding Honda Navi). The overall design of the scooter will attract both male and female buyers.

The company is targeting 20% growth to touch six million units in FY 17-18.

The company closed FY17 with all-time high sales of 5,008,103 units. Honda's total automatic scooter sales crossed 3 million mark for the first time ever to reach at 3,351,604 units with 16% growth compared to 2,892,480 units in FY'15-16. Despite exports de-growing by 6% in FY17, Honda's exports grew by 41%, increasing from 200,114 units in FY'15-16 to 283,153 units in FY'16-17.

For the month of September 2017, Eicher Motors recorded a positive growth, of 22% and selling a total of 70,431 units, as compared 57,842 units sold in to September 2016 is. Out of 70,431 units sold in September 2017, 69,393 units were sold in the country while the company exported 1,038 units. The company's sales for the period of April-September 2017 was 3, 78,304 units, which itself is a growth of 23% over the same period last year.

The Chennai based motorcycle manufacturer earlier had announced the opening of its second direct distribution subsidiary outside India. The company started direct operations in Brazil, the fourth biggest two wheeler market in the world.

FY17 RE volumes were up 31% YoY to the extent of 6,66,490 units as against 5,08,154 units in financial year ended March 2016. The company has cleared out all BS III stocks while deliveries of BS IV compliant vehicles immediately commenced from 1st April 2017.

Royal Enfield operates in the niche market; they don't operate in 125 cc or 150 cc segment, which appeals to some set of customers mostly from urban areas. These urban customers were not affected much by demonetisation. Moreover, Royal Enfield has packaged Classic 350 very well by capturing aspiration of the customers as well as their commuting needs. On the other hand, mass segment motorcycles have a large rural customer base due to which the sales got affected.

Company is focusing to launch one new product in this financial year and one in the next.

Scooters:

Nearly one in every three two-wheelers sold in the country is a scooter. After being written off in the late 1990s when Bajaj Auto dumped the Humara Bajaj tagline and exited the scooter

business, scooters have come back into reckoning led by Honda Motorcycle & Scooter India (HMSI). In the past decade, the scooter's presence in the two-wheeler pie has more than doubled from 13% (2005-05) to 32% (FY 16-17) while the share of motorcycles has declined from 82% to 65%. In volume, scooters have grown a whopping 450% in the decade from 9.09 lakh in 2005-06 to 58.98 lakh in 2015-16. Motorcycles, on the other hand, have grown only 80%.

In Sept 17, total domestic scooter sales increased by 13% to 686,478 units over Sept 2016. Hero Motocorp's sales rose 5% to 88,524 units. HMSI scooter sales rose 9% to 386,456 during the month. TVS Motor sales rose 50% to 118,174 units.

Globally, scooters constitute ~55% of the two-wheeler market (ex China and Africa). Excluding India, the share of scooters is at ~79%.

On a longer term perspective, scooter industry volumes are expected to grow at ~20% CAGR over FY14-20, twice the growth rate for motorcycles. Overall two wheeler industry volumes are likely to grow at 12% CAGR during this period. The share of scooters are expected to increase to 37% by 2020, with annual sales of 10.7m units (equal to the current market size of the domestic motorcycle industry).

HMCL and TVSL are prepared for the transition, while BAL is also considering are entry.

To support international operations, HMCL has already set up assembly operations in Sri Lanka and Kenya. It has plans to build 20 assembly facilities (including India) to expand the company's presence to 50 countries by the end of the decade.

While the share of scooters is likely to increase, the dominance of motorcycles will continue, driven by increasing penetration in rural markets. Motorcycles fare better in rural areas, where road infrastructure is relatively poor, are more suitable for longer distance travel, and offer higher mileage (an important factor for cost conscious customers).

In a recent latest report, it says that two-wheeler sales will continue to be driven by scooters and their share in the industry will jump to around 40% by 2019-20.

But scooters are growing at the expense of lower executive bikes. Over the past five years, the share of scooters has risen from around 20% to over 30% while the share of lower executive bikes (under Rs 50,000, same as scooters) has shrunk from 35% to 25% now.

Three Wheeler

The three-wheeler industry's total volumes grew 23% to 97,083 over the year but grew 16.4% over the month in Sept 2017, led by 24% rise in the passenger segment. Sales of the goods carrier (GC) segment rose 16% at 11,275 units. Exports rose 29% to 35,223 units. Domestic sales were higher by 19% at 61,860 units in Sept 2017.

Bajaj Auto's total 3W sales rose by 32% yoy while growing 16% mom to 59,074 units in Sept 2017. In the domestic markets they increased by 37% yoy, while in the exports

markets sales grew by 25% yoy.

The company has given a guidance of average 20,000-21,000 3w unit sales each month from July to December 2017 versus an average of 17,000-18,000/unit. The increase in 3 w sales is expected on account of with the removal of new permit restrictions in Maharashtra clubbed with the release of new permits in Delhi along with the requirement of mandatory conversion of two-stroke vehicles to four-stroke ones in Bengaluru.

The company expects to launch an electric 3W within the next year and said that it will require minimum cost.

TVS Motor's 3W sales continued to witness recovery from recent average of ~5k units. Total sales increased 54.9% to 5,808 units. 3W exports increased by 55% yoy, while domestic 3W volume improved by 54% yoy.

M&M's total 3W sales rose marginally to 6219 units in Sept 2017 mainly due to 2% rise in passenger carrier segment.

Piaggio passenger carrier vehicles sales decreased by almost 3% to 11,919 units in Sept 2017. Goods carrier sales rose 23% at 5,575 units.

Atul Auto sold 4,799 vehicles in the month of September 2017 as compared to 4,666 vehicles in the month of September 2016, showing an up move of 2.9%. The company expects growth to pick up further in coming months, led by the launch of the 0.35t petrol/CNG passenger 3W models in export and domestic markets. With further capacity addition and new petrol product launch, Atul can efficiently tap export markets along with urban markets in India and, thereby, continue the strong growth momentum.

Vehicles like three-wheelers and e-rickshaws provide last-mile connectivity at affordable rates and therefore there is a potential for sales to grow. India, the world's largest three-wheeler market, is believed to be at an inflexion point. The removal of permit system in states such as Maharashtra, coupled with shared mobility providers such as Ola aggressively expanding three-wheeler transportation to provide last mile connectivity for city commuters, is opening up new opportunities Maharashtra accounts for almost 10% of the overall three-wheeler market annually. The national capital, New Delhi, is likely to release fresh permits that can quickly add about 30,000 to 40,000 units per annum in a short time. Seeing the rise of Ola and Uber, the Maharashtra government has expressed a desire to bring in the black-and-yellow autorickshaws and cabs under an app-based business model of its own.

Outlook:

The automobile sector, one of the major beneficiaries due to reduced taxation in all vehicle categories other than hybrids, is witnessing an uptick in demand. In the run up to the festive season which begins in end-September, consumer demand is likely to boost. The robust pick up is expected to remain sustained given the strong consumer demand and

on par monsoon which should support the rural spends.

Retail demand on the ground has shown recovery in the last month due to normalization of GST-related anxiety. Further, pre-festive demand beginning with Ganesh Chaturthi in Maharashtra followed by Navratri and Diwali should drive volumes. Factors such as good monsoon and increase in MSPs have lifted sentiment in rural/semi-urban areas. Pre-festive demand is evident in states like Maharashtra and Gujarat. Pre-festive inventory building is driving wholesale demand.

The domestic two-wheeler volumes is expected to grow by 8-10% during FY18.

Pent up demand consequent to the deferment of purchases during the third and fourth quarter of FY17 augurs well for demand revival on the rural front. Urban sentiments are expected to draw support from staggered pay revision for state government employees and pensioners as well as muted CPI inflation. Expected improved demand from rural segment is on the basis of improved farm sentiments following two seasons of good crop, forecasts of normal monsoons and benefits from rural employment guarantee schemes trickling in.

Favorable budgetary allocations towards rural development, increased focus on creation of irrigation infrastructure in the latest budget will also support the demand to some extent.

The effect of new GST rates almost neutral for Two-Wheeler sector and would marginally increase for Three Wheelers as it didn't attract additional NCCD earlier. The GST rate for the sector will be 28% plus cess. Overall, tax incidence is maintained by government with levy of 3% Cess over and above highest slab of 28%. Under GST, most of the two-wheelers will attract a tax rate of 28%, lower than total tax incidence of around 30% at present. The 3% cess on motorcycles with engine capacity more than 350 cc will have a marginal negative impact. Companies had announced price cuts to pass on the benefits to customers which will help in further boosting demand.

Over the medium term, the two-wheeler industry is expected to reach a volume CAGR of 8-9% and a size of 22-23 million units (domestic + exports) by FY2019. The expectation draws

on the various structural positives associated with the domestic two-wheeler industry, including favourable demographic profile, moderate two-wheeler penetration levels (vis-a-vis several other emerging markets), under-developed public transport system, growing urbanization, strong replacement demand and moderate share of financed purchases. With new capacity coming on-stream from 3QFY18, one can expect sales growth to stabilise in the range of 15% in long run.

While scooters are expected to continue to lead the growth, revival in the motorcycle segment is also expected going forward as rural demand revives. The 32% market share of scooters is set to expand further as scooters are expected to post a growth of 15-20% during FY18.

The three-wheeler market is likely to cross the major milestone of 1 million units in production in the next couple of years, with domestic market crossing its previous peak of 5.5 lakh units per annum to about 6-7 lakh units. Passenger carrying three-wheelers will be crossing a critical half a million mark in the domestic market by 2019-2020. With shared mobility providers such as Ola and Uber expected to add almost half a million vehicles to their platform in the coming three years, industry players expect demand to surge.

GST for the two wheelers is in favour for the mass markets. Various manufacturers have released their updated prices after the implementation of GST, which indicates a marginal drop in prices which is expected to gradually result in a better industry growth.

The various structural positives associated with the domestic 2W industry are favorable demographic profile, moderate 2W penetration levels (in relation to several other emerging markets), under developed public transport system, growing urbanization, strong replacement demand and moderate share of financed purchases remain intact; as also the large opportunity available to grow presence in overseas markets, mainly Africa and Latin America.

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