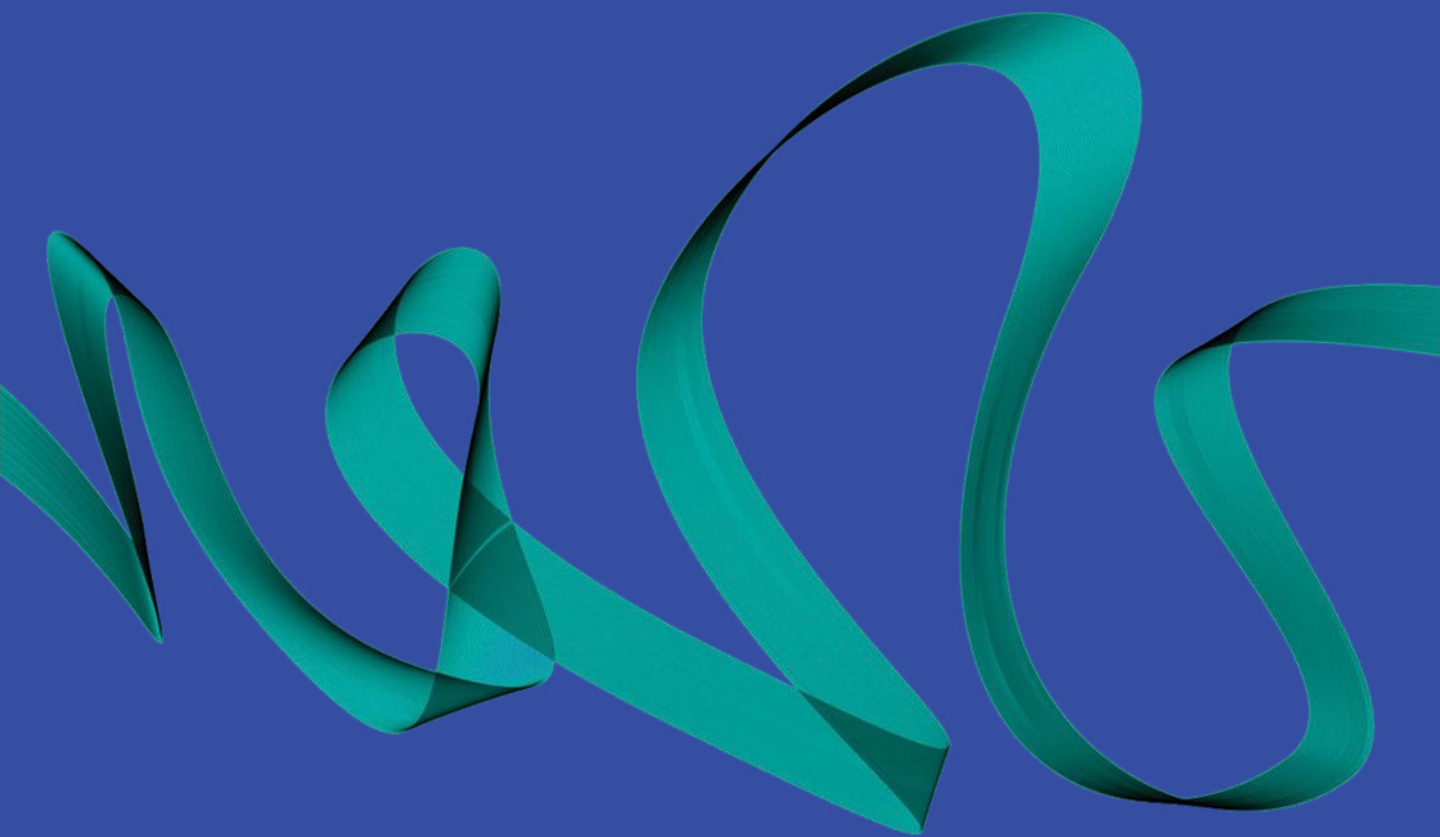




India's Hatchback Market

The Big Business of Small Cars



Ipsos Business Consulting

Build · Compete · Grow

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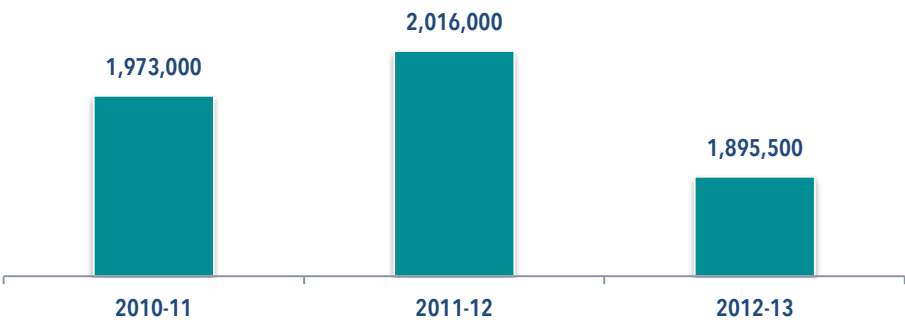
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Market overview

India's automobile industry is one of the largest recipients of foreign direct investment within the country and accounts for about 8 per cent of the economy. The industry is not only gaining ground as a global production hub, world-leading brands are increasingly setting up local operations to tap India's lucrative domestic market. This has seen more activity across the entire consumer market as global luxury automobile brands target the country's burgeoning upper-middle class and high net worth individuals, while major international carmakers are entering the highly competitive small car segment.

The industry is not immune to global dynamics, however, and growth within the auto sector and the overall economy has been sluggish for the past few years. As a result, this year's sales are expected to grow at a lower rate than the 5 per cent achieved in 2011-12.

Figure 1: Annual domestic sales of passenger vehicles, 2011-13 (number of vehicles)



Source: SIAM, Ipsos Business Consulting

Several factors have contributed to the slowdown including higher fuel prices, excise duty hikes and economic turmoil. Utility vehicles are the auto sector's the greatest hope, however, the recent 3-per-cent rise in excise duty for sports utility vehicles (SUVs) may dampen the segment's performance.

India is expected to become the world's third largest automobile market by 2030, behind the US and China, according to industry forecasts. This confidence is based on drivers including low vehicle ownership within India, anticipated high levels of economic growth, substantial government investments in infrastructure and an increasingly upwardly mobile middle class.

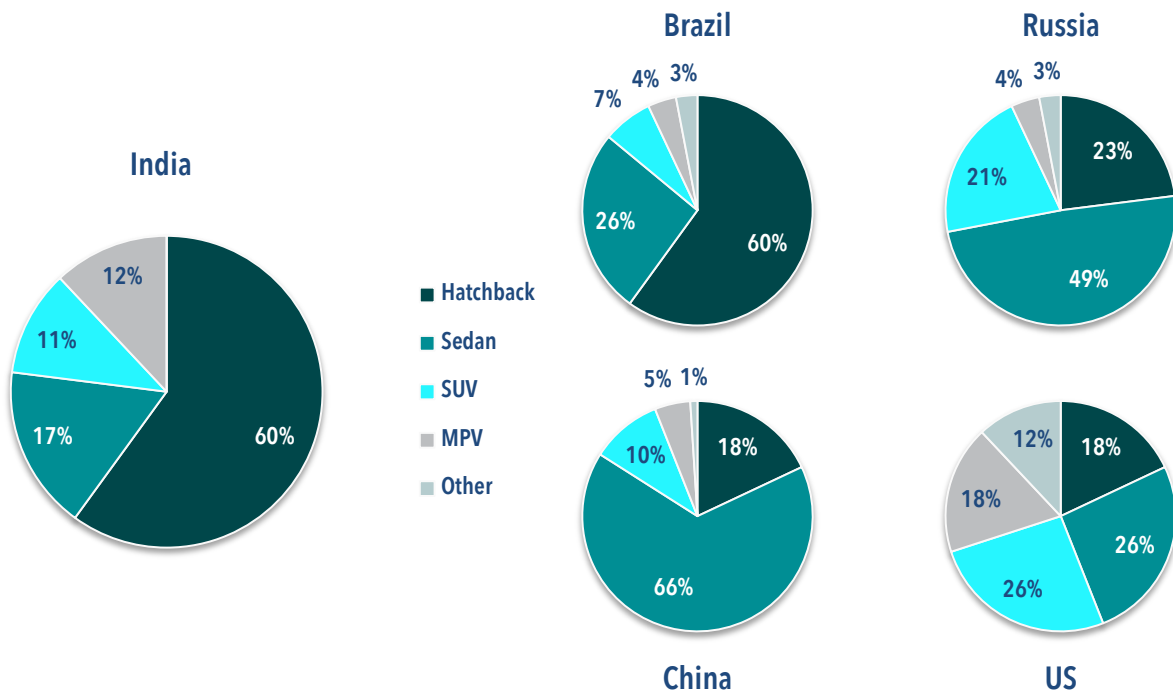
Comparison with international markets

Indian consumers are value-centric. Many carmakers, as a result, have focused their activity within the economical hatchback segment. This contrasts with a preference for bigger, more luxurious cars in developed countries. India's luxury car market currently has a 3-per-cent market share and therefor exhibits strong growth potential.

Car production in Brazil, Russia, India and China grew with CAGR of 7.3 per cent, 1.9 per cent, 17.6 per cent and 39.3 per cent respectively from 2001-10. Weak macro-economic conditions in Brazil and India resulted in slower car sales in 2012. While China

still enjoyed attractive macro-economic conditions, sales were crimped by government measures such as high import tariffs on automotive parts and assembled vehicles.

Figure 2: Market share of passenger vehicles in BRICS nations by category, 2011



Source: OICA, Ipsos Business Consulting

The US car market is dominated by large cars including SUVs, multi-purpose vehicles (MPVs) and pickups. Smaller cars, such as hatchbacks, are more popular in developing countries such as India and Brazil, whereas consumers in Russia and China prefer sedans.

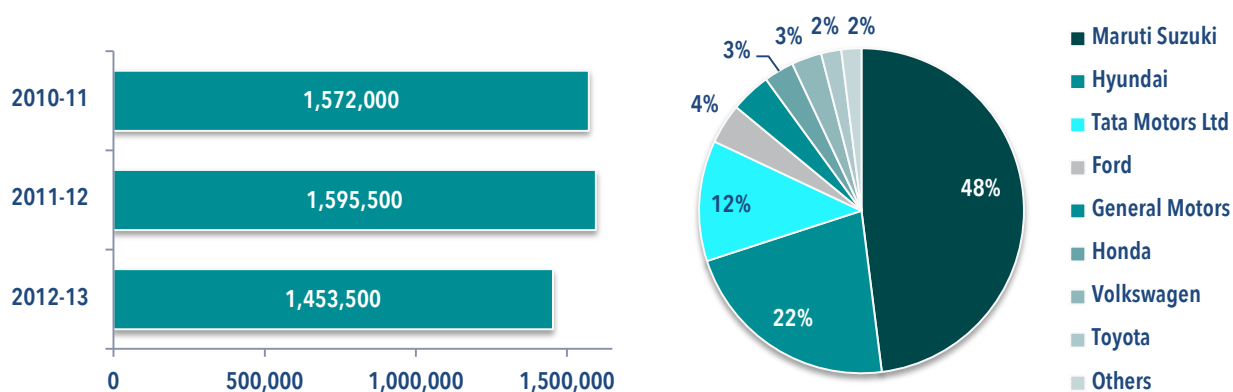
The top four players namely Suzuki, Hyundai, Tata Motors and Mahindra & Mahindra constitute 80 per cent of the passenger car sales in India thereby making it a highly consolidated market. However, increasing competition across vehicle segment is expected to lower the concentration levels such that five or more players will make up for 80 per cent of the market in the upcoming years.

Sales trends

Hatchbacks have been the bestselling cars in India since they were introduced in the early 1980s. The image of small compact cars is changing from that of the ideal vehicle for budget conscious middle-class consumers to something that is increasingly popular with wealthier buyers, thanks to the introduction of more stylish customised models.

However, the segment has seen overall sales decline over the past few years as more consumers opt for sedans and utility vehicles. The hatchback segment grew by only 1.5 per cent in 2011-12 compared with 5 per cent for India's passenger car market. A lack of new hatchback models has done nothing to help the segment's lacklustre performance, a point illustrated at Auto Expo 2012 where only one small car was launched compared with four at the previous year's event.

Figure 3: Annual hatchback sales and market share by brand (April 2012-February 2013)



Source: SIAM, Ipsos Business Consulting

Maruti continues to lead the hatchback segment with a 48-per-cent market share, about 800,000 vehicles last year, despite the company facing major internal and external issues related to production and labour management. While other major players such as Hyundai and Tata lead in terms of innovation and vehicle performance, they still lag far behind in terms of sales.

International car giants including General Motors, Honda, Toyota and Volkswagen have entered the market but have yet to gain a foothold or compete effectively against the dominant local brands in hatchback segment.

Historical trends

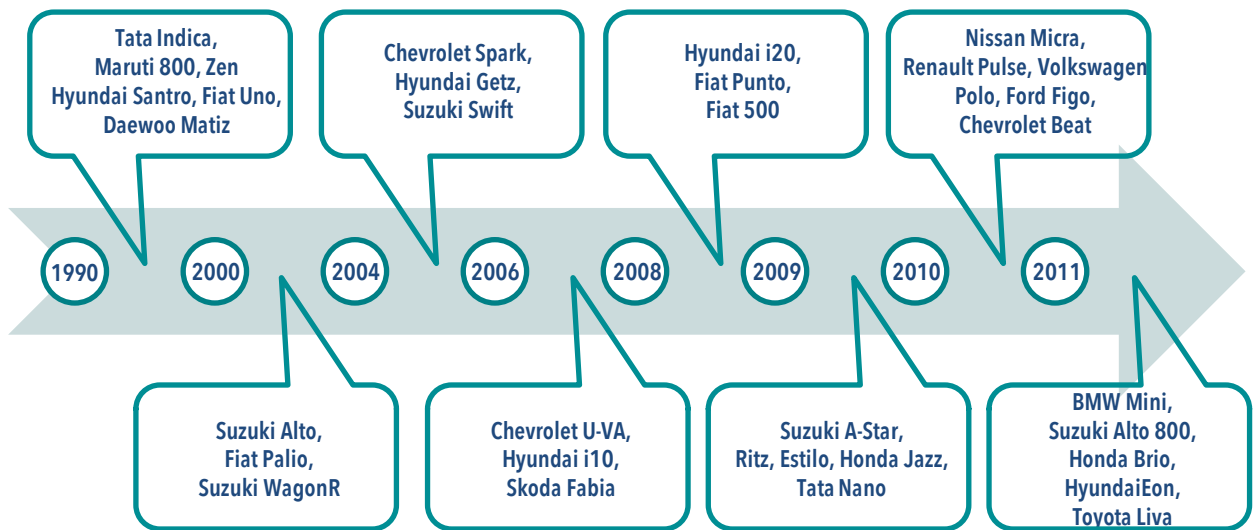
Maruti took hold of the hatchback market in the 1980s when it introduced the Maruti 800, a customised car aimed at India's mass market which dislodged Hindustan Motor's Ambassador from pole position. Within a matter of a few years, Maruti Suzuki was manufacturing and selling 100,000 cars a year in a country where the entire auto market had previously only chalked up combined annual sales of 35,000-40,000 units over the previous decade.

Hyundai Motors India in 1998 became the first carmaker to seriously challenge Maruti's dominance by launching the Santro, which was a runaway success and became the segment's no.1 seller within the year it was launched. Maruti introduced the WagonR in response, but the car did not enter the market for two years due to the production cycle.

Tata Motors announced India's first totally homegrown passenger car, the Indica, in the same year. Its rugged look was an instant hit. Other compact cars, such as Daewoo Mates, Fiat Uno and Fiat Palio, failed to gain traction in the market and were eventually phased out.

This enabled four models – Maruti Suzuki 800 and Alto, Tata Indica and Hyundai Santro – to practically own the hatchback segment until the recent entry of foreign players.

Figure 4: Development of India's hatchback segment



Source: Ipsos Business Consulting

Major international automakers such as Chevrolet, Nissan, Volkswagen, Ford and Renault started introducing compact car models in 2010 in order to tap the segment's long-term potential.

Market segmentation

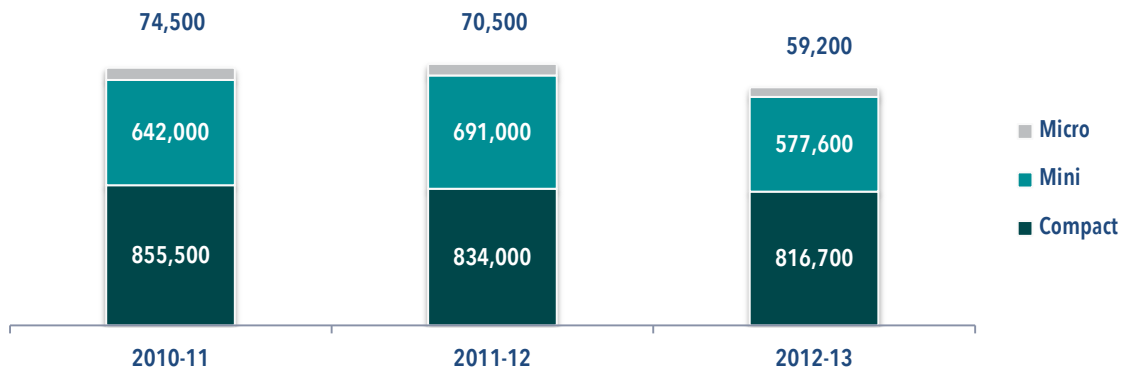
India's hatchback market can be broadly divided into three segments: micro, mini and compact.

Tata Nano is currently the only micro car in the market. Costing less than 200,000 rupees, the model was marketed as "the world's cheapest car". While it has performed well in India, it failed to gain traction in foreign markets.

The mini segment includes a mix of classic models such as the Maruti Suzuki Alto and Hyundai's Santro Xing, as well as newer cars like the Hyundai Eon. Basic models are shipped without air conditioners and central locking. They are typically priced from 100,000-200,000 rupees.

Tata launched India's first compact car with the Indica in 1998. Maruti Suzuki entered the segment with the Swift in 2005. Since then compact cars have become one of the auto industry's most competitive and fastest growing segments.

Figure 5: Annual sales by hatchback sub-segments (number of vehicles)



Source: SIAM, Ipsos Business Consulting

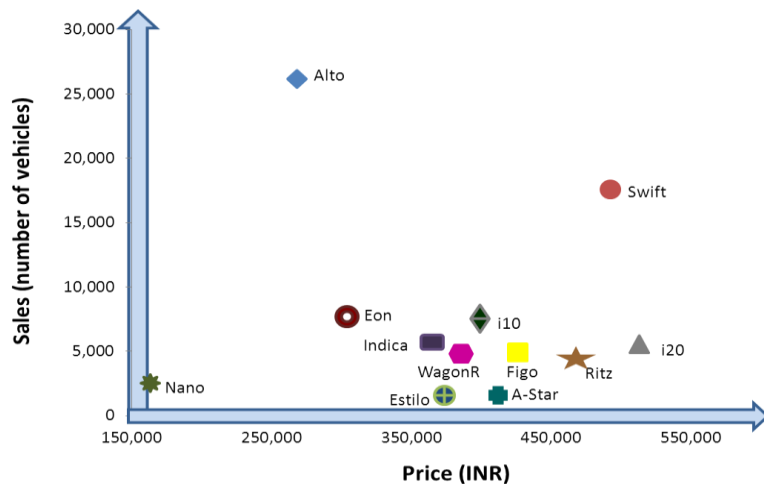
Mini models dominated the market for most of the past decade. Sales of compact cars now lead the hatchback segment and 12 brands are producing models.

Market dynamics

Competition has intensified within the hatchback sector and consumers have had a much greater choice of models ever since international carmakers became more active within India's auto market.

While Indian consumers are very cost-focused, carmakers cannot compete on price alone. If they could, Tata Nano would have been the bestselling car in India, a position currently enjoyed by the Maruti Alto.

Figure 6: Sales (December 2012) vs price positioning of key hatchback models



Source: SIAM, Ipsos Business Consulting

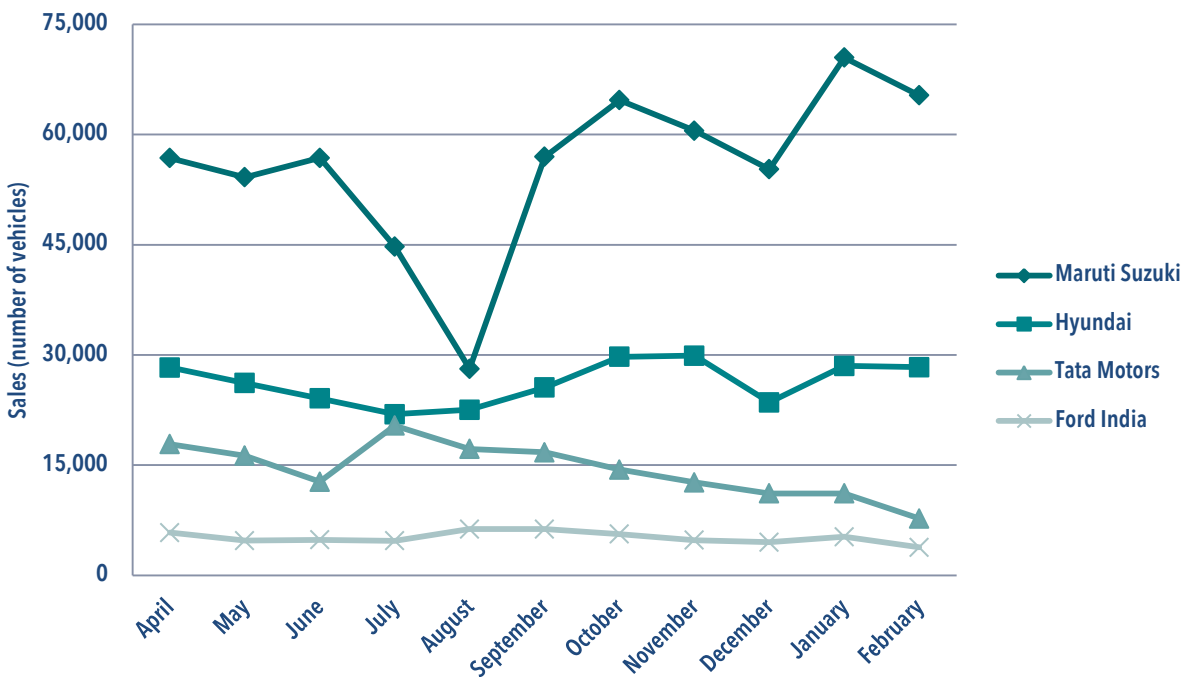
Certain non-price based factors influence the buying decisions of Indian consumers. In fact, Indian car buyers appear more value-driven than price-driven. Alto and Swift are the bestselling models despite commanding relatively high prices. This is due to their combination of contemporary design, fuel efficiency, after-sales service, build quality and price which outstrips the offering of other players in the hatchback segment.

Competitive landscape

India's hatchback market comprises 12 automakers with three brands – Maruti Suzuki, Hyundai and Tata – accounting for 80% of the market by volume. Foreign brands account for less than 3 per cent of the market.

The Hyundai Eon was one of the most notable launches in 2011. Priced below 300,000 rupees it is looking to succeed the iconic Maruti 800 which Maruti Suzuki started phasing out in 2010. It was seen as a challenger to the highly popular Alto which sells more than 20,000 cars a month.

Figure 7: Monthly sales for Indian car manufacturers, 2012-13



Source: SIAM, Ipsos Business Consulting

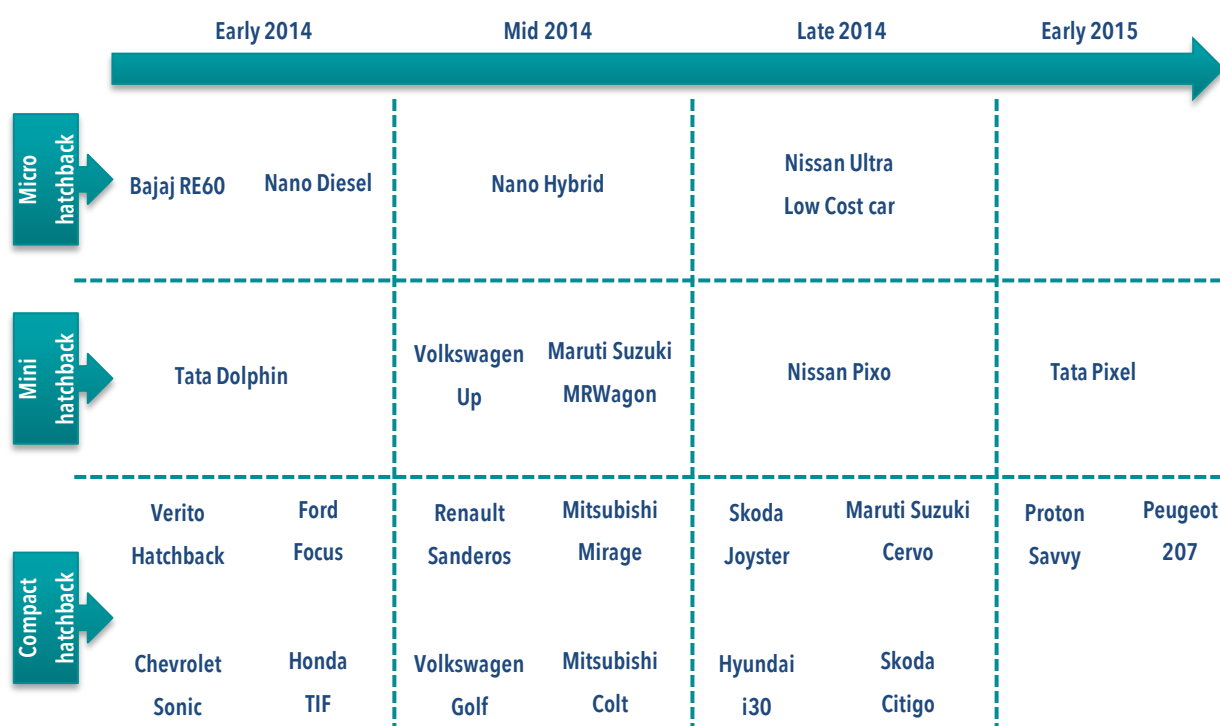
Maruti Suzuki suffered a sharp drop in sales during August 2012 when stock of the Swift ran dry. However, other carmakers could not take advantage of the situation as the Swift was so popular buyers simply waited for new supply to reach the market, which led to sudden growth from September.

Fiat, one of the oldest players in the market, finished the year with the lowest sales figures as competing hatchbacks from other automakers were seen as being of better quality and coming with higher levels of after sales support.

Looking forward

India is emerging as one of the most attractive automobile markets in the world. According to the Department of Heavy Industries' Auto Mission Plan 2006-16, the auto industry should top US\$145bn before the end of fiscal 2016. However, it is likely the target will now be missed by as much as 20 per cent due to current sluggish growth rates. Nevertheless, the market still provides a huge opportunity for domestic and international players with CAGR forecast at 8 per cent for 2013-20.

Figure 8: Expected launches by sub-segments



Source: Ipsos Business Consulting

The disposable income of Indian consumers, especially younger people, is set to increase as the country's economy continues to grow. This, along with infrastructure improvement, will also play a vital role in the automobile market's development.

As hatchbacks are no longer seen as just a basic means of affordable transport, one should expect to see more luxurious and powerful models being launched. With global carmakers such as Volkswagen, Fiat, Tata and Toyota fighting for dominance, the competition is only going to increase in coming years.

The compact hatchback segment is expected to drive the market for the foreseeable future with higher-end models competing directly with entry-level sedans. With 85 per cent of all Indian cars paid for by instalments, consumers are looking at price differently as they have a wider range of more competitive financing plans available to them. This will affect the future growth of different segments as buyers opt for more expensive models which they previously could not have afforded.

Mini and micro hatchbacks are expected to penetrate secondary and tertiary markets in India and directly compete with the motorbike and scooter segment.

The government's 2002 auto policy allowed unrestricted 100-per-cent foreign ownership within the car making segment. The government also established special economic zones which have led to the emergence of automotive hubs in and around cities such as Chennai, Gurgaon and Pune.

Both local and foreign OEMs have heavily invested in manufacturing and R&D within India's hatchback segment over the last decade. Many foreign players are now doing in-house development, manufacturing and exporting small cars from India. As a part its National Automotive Testing and Research and Development Infrastructure Project, the International Centre for Automotive Technology was set up in Manesar to provide research and development and other support services for automotive design, testing and validation. Global component manufacturers such as Bosch, Valeo, Caterpillar, General Motors, Ford and Cummins have also set up research and development facilities in India.

While the country's auto sector is still vulnerable to global dynamics and domestic economic headwinds, the groundswell in activity within all aspects of the industry and the increasing presence of foreign automakers and equipment manufacturers point towards a healthy but increasingly competitive future for car makers in India.

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