From Rising Costs to Subsidy Cuts, Two-Wheeler Story is Missing Spark

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Synopsis

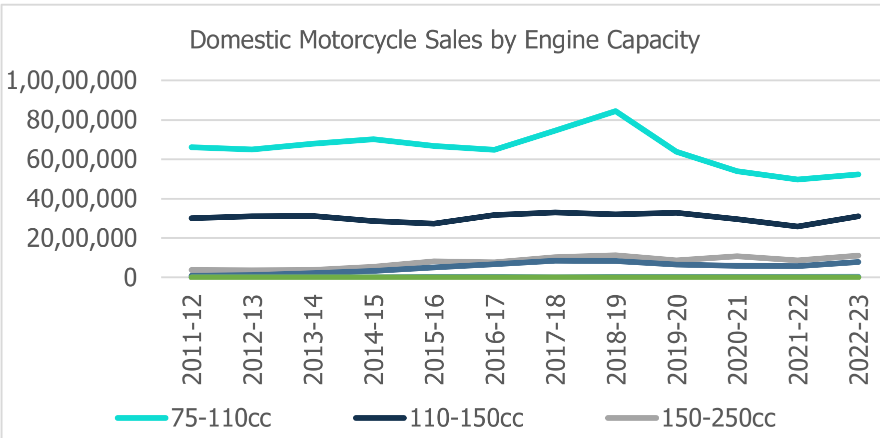
- The core segments of two-wheelers, specifically the 75cc-110cc range in motorcycles and the 75cc-125cc range in scooters, exhibited a sharp sales volume decline from FY19 to FY22, with a slight recovery noted in FY23.
- Motorcycles have witnessed a partial offset of this decline through relatively lower drops or quicker recoveries in the higher engine capacity segments. In contrast, the higher capacity scooter segment also registered a significant decline over this period.
- This decline in sales volumes of the mainstay models can be attributed to an overall higher cost of ownership of two-wheelers, brought about by an increase in the prices, as well as fuel costs and insurance expenses.
- Mainstay models, particularly in motorcycles, typically cater to the price-sensitive market segment, with higher sales in rural areas. These models saw substantial declines in FY21-FY22, followed by a moderate recovery in FY23. The impact of El Nino on the rural economy in FY24 remains uncertain, affecting the prospects of two-wheeler sales rebound during the year.
- Exports volumes of two-wheelers declined by 31% during Q1FY24, which is attributed to the weakening of economic conditions in key markets in Africa and Latin America. These nations are currently facing challenges on account of high inflation, reduced buying power and inadequate foreign exchange reserves.
- Sales of electric two-wheelers also significantly declined in Q1FY24 due to the government withholding FAME subsidies for certain Original Equipment Manufacturers (OEMs). Additionally, a subsidy reduction to Rs. 10,000 per kWh (from Rs. 15,000/kWh) and 15% of the ex-factory price (from 40% earlier) further adds to the uncertainty in two-wheeler sales.
- Domestic two-wheeler volumes recovered by 18.2% in FY23 aided by the low base effect of FY22 (attributed to three continuous years of declining volumes), and strong demand in higher engine capacity segments of motorcycles.
- Owing to the aforementioned factors, the medium-term sales trajectory for two-wheelers is anticipated to be modest, characterised by uncertainties. The absence of definitive growth drivers and an already substantial sales volume base (with 1.63 crore two-wheelers sold domestically in FY23) will constrain high growth rates in the medium term.

Declining Sales in Mainstay Two-wheeler Segments

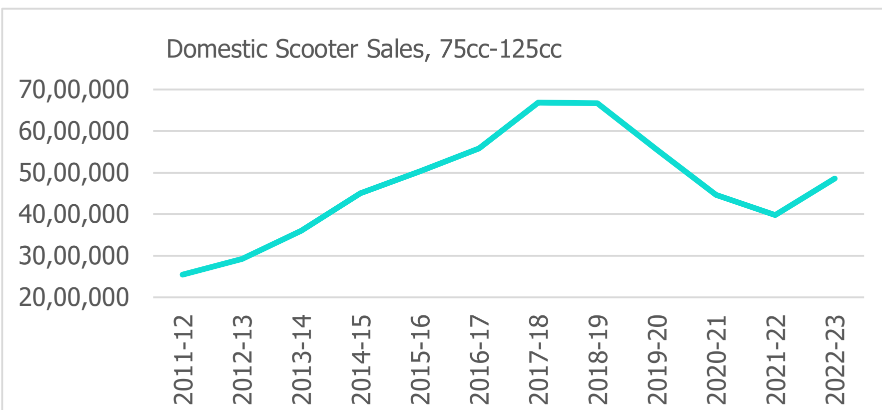
The mainstay segment of motorcycles, specifically the 75cc-110cc category, witnessed a notable contraction in domestic sales volumes over the period spanning FY19 to FY22. However, a modest resurgence was evidenced in FY23. Conversely, segments with higher engine capacities displayed comparatively lower volatility. In FY19, domestic motorcycle volumes reached a pinnacle at 1,35,98,190 units, with the 75cc-110cc segment constituting 62% of the industry's sales volumes. While the share of this pivotal segment has progressively diminished, accounting for 51% in FY23, the industry's overall volumes have not rebounded to their FY19 levels. This dynamic indicates that the incremental volumes generated in the higher capacity (and consequently higher-priced) segments have not successfully counterbalanced the decline experienced in the foundational segment.

In the realm of scooters, a similar trajectory was observed in the primary 75cc-125cc segment, resembling the trends seen in the core motorcycle segment. However, the 125cc-250cc scooter segment experienced a more pronounced volume correction, and sales in the sub-75cc category have consistently remained low.

The downturn in sales within the core segments of both motorcycles and scooters can be attributed to escalated acquisition and operational costs over the past three to four years. In the case of the 125cc-250cc scooter segment, the decline can be partly attributed to the impact of electric scooters cannibalizing sales. Notably, incentives such as road tax exemptions and subsidies under the government's FAME (Faster Adoption for Manufacturing of Electric Vehicles) scheme have catalyzed a surge in electric scooter sales over the preceding four years.



Source: Centre for Monitoring of Indian Economy



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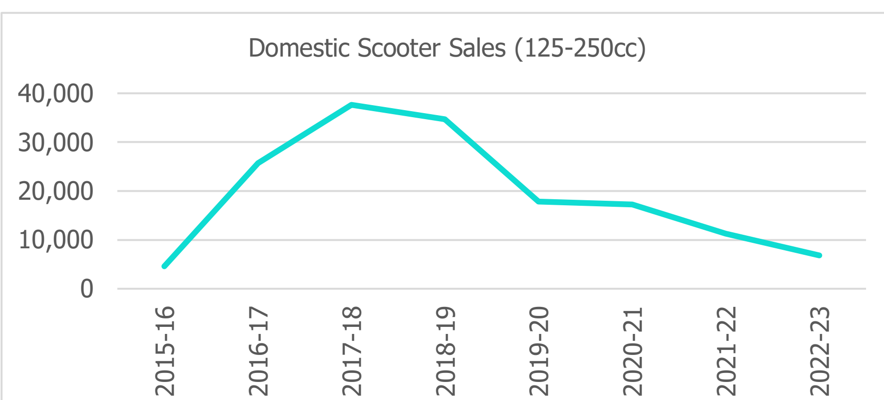


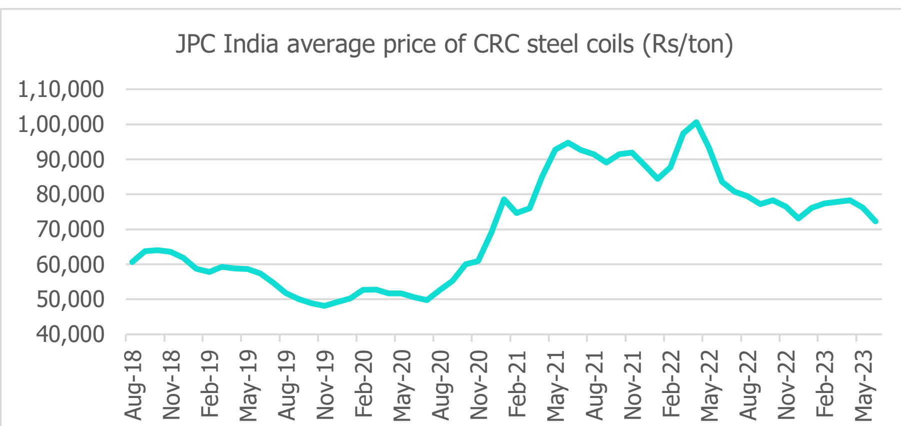
Source: Centre for Monitoring of Indian Economy

Note:

1. Given the wide disparity in volumes of 75cc-125cc scooters, volume trends have been displayed in separate charts.
2. 125cc-250cc scooters had negligible sales volumes prior to FY16.
3. <75cc scooters had displayed low and declining sales volumes till FY15 and virtually no volumes after that. Hence this segment has not been included in the above chart.

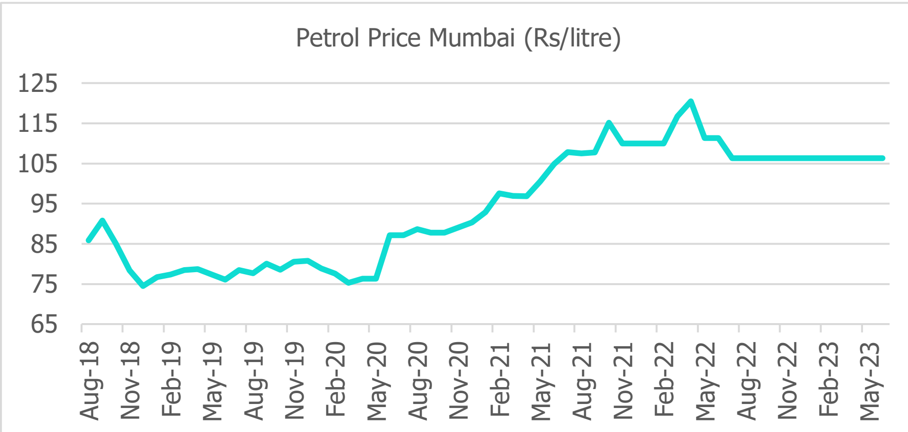
Increased Cost of Ownership of Two-wheelers

During the FY20-FY23 period, the price of two wheelers have increased by at least 35%, driven by commodity price increases as well as government regulations which mandated the incorporation of additional safety features as well as adherence to more stringent emission norms. The transition from BS-IV to BS-VI emission standards was made effective from 1 April 2020. Safety features such as Anti-Lock Braking Systems (ABS, for two-wheelers 125cc and above) and Combined Braking System (CBS, for less than 125cc) became mandatory from exactly a year earlier. CARE Ratings believes that while the revised insurance norms introduced effective from September 1, 2018, (mandating the purchase of five-year third-party insurance policies while purchasing a two-wheeler) had increased overall acquisition costs only marginally, it has also contributed to the rise in the cost of acquisition, and has impacted the sales of the entry-level models of motorcycles and scooters along with the other factors mentioned earlier. The over 50% surge in steel prices during FY21-FY22 had a larger impact on the prices of two-wheelers than the regulation-driven price increases of previous years.



Source: Joint Plant Committee, Ministry of Steel

The overall cost of ownership has gone up significantly also due to the steep rise in petrol prices. Over the five-year period starting from April 2018 till April 2022, petrol prices rose around 46% (from Rs.82.48/litre to Rs.120.5/litre, based on retail prices in Mumbai), before correcting slightly three months later to Rs.106.3/litre, post the downward revision in excise duty by the Centre. Petrol prices have remained largely stable at the same level since then.



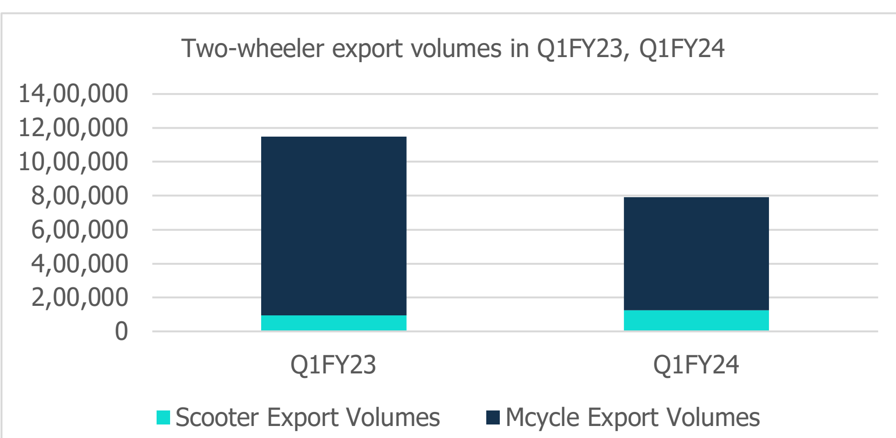
Source: www.mypetrolprice.com

Motorcycle Sales Higher in Rural Areas, Faces Weakening Demand

Lack of public transport and lack of affordability for four-wheelers are the two main factors driving sales of two-wheelers in rural areas. Rural sales of two-wheelers account for a slightly higher proportion of volumes compared with urban, with a preference for motorcycles over scooters. Considering that rural consumers are generally more price sensitive than urban; the mainstay models are naturally bought more by rural consumers. The increase in prices of two-wheelers witnessed in the past four years has led to a weakening in rural demand and deferment of buying decisions, despite four continuous years of normal monsoon over FY20-FY23. Any disruption to agricultural output in FY24 due to the El Nino impact, which reduces the disposable income of the rural populace can further subdue two-wheeler sales in the current year.

Discouraging Quarterly Trend in Two-wheeler Exports

Q1FY24 has witnessed an overall 31% decline in export volumes of two-wheelers, driven by 37% decline in motorcycle sales volumes, which was partly offset by a 30% rise in scooter volumes. India's two-wheeler exports are primarily to developing nations in Africa, Latin America and Asia. Many of these nations are currently facing monetary challenges and have devalued their currencies, making imports more expensive. The decline in motorcycle exports does not exhibit any definitive pattern across the various engine capacities, indicating that the overall demand has weakened from importing countries.



Source: Centre for Monitoring of Indian Economy

Countrywise Exports of Two-wheelers from India over the Past Decade

(In Rs. crore)

Country	FY13 Exports	FY18 Exports	FY23 Exports
Colombia	1,440	1,034	2,454
Nigeria	1,153	950	2,026
Philippines	509	821	1,642
Mexico	188	481	1,571
Nepal	205	1,199	834
Bangladesh	614	1,787	826
Congo, D.R.	12	175	771
Uganda	194	287	755
Guatemala	183	370	716
USA	13	129	639
Rest	2,808	5,670	10,117
Total	**7,320**	**12,903**	**22,351**

Source: Department of Commerce, Ministry of Commerce and Industry

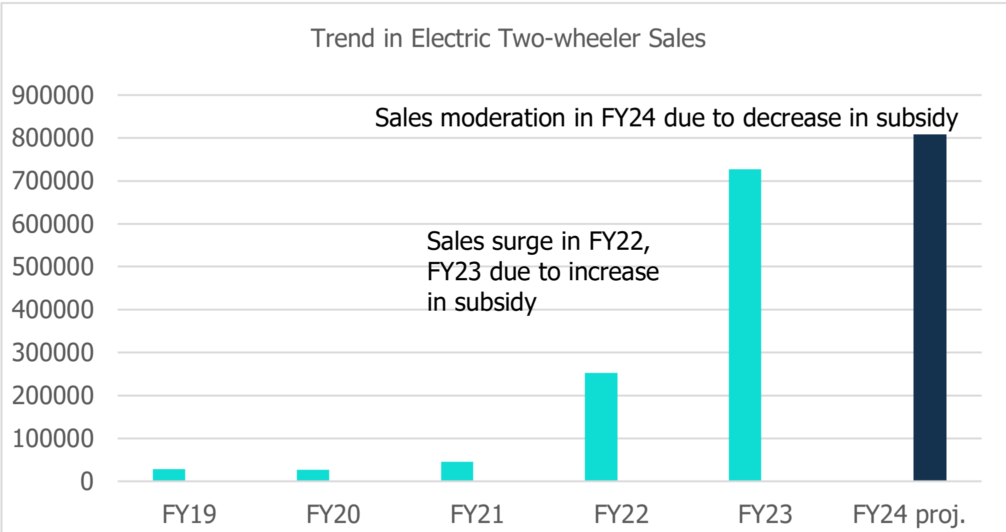
Sharp Reduction in FAME Subsidy Slowing Down Electric Two-wheeler Demand

In order to boost the sales of electric vehicles, the Central Government vide the Ministry of Heavy Industries had introduced the FAME subsidy scheme effective from 1 April 2015 with a small budget of Rs.75 crores. The scheme entailed cash subsidy being credited to dealers of EVs to bring down the acquisition cost for vehicle buyers. The budgetary allocation was increased on an annual basis along with the extension of the scheme, till FY19 when the budget stood at Rs.145 crores. Post this, it was replaced by the FAME II scheme, which entailed a massive increase in budget, to Rs.10,000 crores and was initially applicable for three years (till 31 March 2022), but was extended in June 2021 for another two years, till 31 March 2024. In the same month the Central Government increased the subsidy on two-wheelers from Rs.10,000/kwh to Rs.15,000/kwh with the maximum cap increased from 20% to 40% of the ex-factory price of the vehicle. Apart from the subsidies available under the FAME scheme, various state governments also introduced their own incentives such as a subsidy amount per kwh of battery capacity, and discounts (or complete exemption) on payment of road tax.

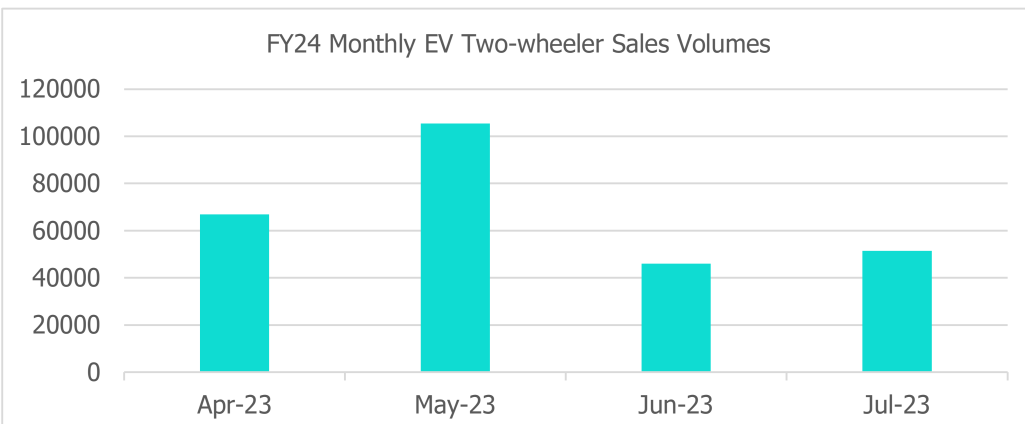
Considering that the subsidy up to Rs.60,000 could be claimed under FAME II from the Central government in addition to the state subsidies and incentives, the on-road price of electric two-wheelers declined to a level where it was comparable with the price of petrol two-wheelers. As a result, demand surged in FY22 and FY23. However, in May 2023, the Ministry of Heavy Industries reduced the subsidy amount to Rs.10,000/kwh, with a cap of up to 20% of the ex-factory price. This action has had an immediate impact on electric two-wheeler sales as was witnessed in the current year's volumes. The government’s action is possibly to nudge the sector towards self-sustainability. Manufacturers of electric two-wheelers will now have to focus on achieving price reduction through R&D and innovation, rather than on government subsidies.

Revisions in FAME II subsidy for two-wheelers

Jun-21	May-23
a) Rs.15,000/kwh b) Cap of up to 40% of ex-factory price c) Ex-factory price up to Rs.1.5 lakhs d) Maximum speed of over 40km/hour and minimum range of 80km	a) Rs.10,000/kwh b) Cap of up to 20% of ex-factory price Other conditions remain the same



Source: Society of Manufacturers of Electric Vehicles
Note: FY24 figures have been prorated based on Apr-July volumes



Source: Society of Manufacturers of Electric Vehicles

Large Volume Base Hinders Meaningful Growth

Sales of two-wheelers peaked in FY19, before declining over the next three years. While the Covid impact was clearly visible in FY20 and FY21, the rise in commodity prices in FY22 constrained rural sales. CARE Ratings is of the opinion that given the challenges explained above and the already high base of 1.9 crores vehicles sold in FY23 (with 1.5 crore vehicles sold domestically in the year), achieving a significant growth rate above this number would be a challenge.

Declining Sales Volumes Post FY19, Recovery in FY23

Year	Domestic Sales		Export Sales		Total Sales
	Motorcycles	Scooters	Motorcycles	Scooters	
FY18	1,26,20,690	67,19,909	24,83,307	3,14,284	2,21,38,190
FY19	1,35,98,190	67,01,430	28,65,851	3,98,316	2,35,63,787
FY20	1,12,13,662	55,65,958	31,35,548	3,69,998	2,02,85,166
FY21	1,00,21,231	44,82,305	30,42,453	2,32,020	1,77,78,009
FY22	89,84,186	41,12,672	40,82,442	3,50,443	1,75,29,743
FY23	1,02,30,502	51,90,018	32,30,981	4,16,935	1,90,68,436

Source: Centre for Monitoring of Indian Economy

Conclusions

CARE Ratings posits that although commodity prices have softened in FY23, the ongoing need for additional technological advancements to adhere to E20 ethanol blending standards (introduced in stages since April 1, 2023) will sustain elevated prices for internal combustion engine (ICE) based two-wheelers. Presently, E20 blended petrol is retailing at around Rs. 60 per litre in select cities as per the government's phased rollout. This seemingly reduces the operating cost for buyers, potentially bolstering sales. However, a substantial track record for E20-compliant vehicles, encompassing fuel efficiency, power, and maintenance costs, is yet to be established. Furthermore, the existing retail price is largely influenced by government subsidies on E20 petrol, which may eventually be withdrawn akin to regular petrol and diesel.

Due to the current high operational and ownership costs of internal combustion-based two-wheelers, buyers had been gravitating towards electric two-wheelers, backed by substantial subsidies from both Central and State governments. Initially, CARE Ratings anticipated that growth in the two-wheeler segment would be driven by electric vehicles, albeit from a smaller base compared to ICE-based vehicles. However, the reduction in FAME subsidy effective from June 1, 2023 has curtailed the previous robust growth in this category.

CARE Ratings believes that the following trends could potentially be witnessed over the next two years:

a) ICE-based two-wheelers could display further recovery in volumes driven by improved cost per km associated with E20 compliant vehicles. However, this would depend on how long the government subsidises ethanol-blended petrol.
b) Mainstay segment volumes would continue to lose ground to higher engine capacity variants.
c) While volumes of electric two-wheelers would pick up given the significantly lower per km running cost (relative to ICE-based vehicles), the offtake would not be to the extent earlier anticipated.

According to Sudarshan Shreenivas, Director, CARE Ratings, "Over the long-term, technological developments leading to a reduction in battery costs which makes electric two-wheelers comparable in price with ICE vehicles (after disregarding subsidies for EVs) would be the key factor driving electric two-wheeler sales. Should the government be successful in the implementation of inter-operability standards for batteries of electric vehicles, it would definitely lead to a spurt in electric two-wheeler sales given the convenience of switching spent batteries with fully charged batteries at charging stations. Additionally, there could be a reduction in retail prices of these vehicles as it would be possible to lease batteries at the time of purchase of an EV, rather than being forced to purchase an EV with a factory-fitted battery".

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