

Update on Auto Components Industry

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Global scenario

The production and demand of the auto component industry is directly proportional to that of the automobiles industry. Although a sizeable portion of auto components production caters to OEMs, the aftermarket or the replacement markets have emerged as crucial sources of revenue for the auto components industry over the past few years. Historically, the automobile OEMs were concentrated in the developed nations and so did the ancillaries. However, in recent years, manufacturing of auto components is gradually gaining traction toward Asian countries such as China, India, and others due to the presence of higher market potential and low-cost manufacturing.

Table 1 depicts the global exports of auto components. Some observations from this table are as follows:

- Gear boxes and drive axles are the two key products that are globally exported.
- The global exports of auto components witnessed a significant downturn in CY2020, over a low base of CY2019. For products like road wheels, steering wheels, steering columns and steering boxes, exports were just 30 to 40% of previous year's levels in CY2020. For other products like gear boxes, exports were better off, but still lower by 1/3rd when compared on a YoY basis in CY2020.
- Some auto components like drive axles, suspension shock absorbers, clutches and bumpers witnessed a decline in global exports in the range of 40 to 50% in CY2020.
- India's share in global exports for each of these products in CY2019 was less than 1.5%, which grew in CY2020 and even doubled for some product categories like road wheels and radiators, however the growth in value terms was negligible.
- Due to the covid-19 related trade restrictions in CY2020, the auto components industry was pushed back by a decade, as exports for all such products were lower than that of CY2011 levels.
- Germany, Japan and USA were the top global exporters for nearly all auto components in CY2020.

Table 1: Category-wise global exports of auto-components

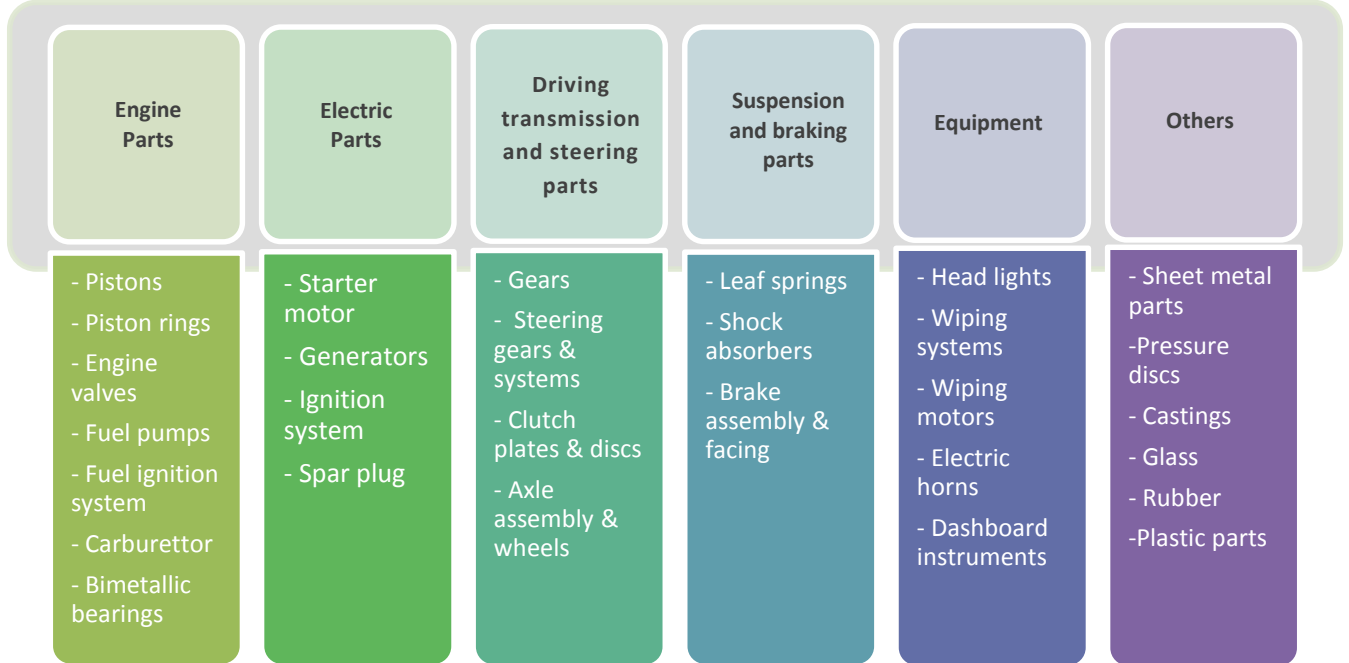
Commodity	CY2011		CY2019		CY2020			Top 3 exporters
	USD bn	USD bn	YoY growth	India's share in global exports	USD bn	YoY growth	India's share in global exports	
Gear boxes	50.6	67.9	-6%	0.6%	44.6	-34%	0.8%	Japan, Germany, USA
Drive axles with differential whether or not provided with other transmission components	20.1	25.3	-6%	1.5%	12.2	-52%	2.8%	Germany, USA, Japan
Steering wheels, steering columns & steering boxes	16.3	21.6	-8%	0.9%	8.6	-60%	1.7%	Germany, USA, Hungary
Road wheels & parts & accessories	17.2	19.3	-8%	0.6%	6.2	-68%	1.4%	Germany, USA, Italy
Suspension shock absorbers	14	19.1	-4%	0.8%	9.5	-50%	1.5%	Germany, USA, Canada
Clutches & parts thereof	8.9	10.8	-6%	0.7%	6.4	-41%	1.1%	Germany, Japan, USA
Bumpers and parts thereof	6	7.8	-2%	1.2%	4.2	-47%	1.7%	Germany, USA, Czechia
Radiators	6.5	6.8	-5%	0.8%	2.9	-57%	1.6%	Germany, USA, Czechia

Source: UN Comtrade Database, EXIM Bank India, CARE Ratings

Indian scenario

The Indian auto component industry, being a critical part of the OEM value chain, has grown at a healthy pace over the past few years. The organised segment of this industry includes OEMs who are engaged in the manufacture of high-value precision instruments, while the unorganized segment comprises of low-valued products catering to after-market services. The industry is highly fragmented with most firms being Indian businesses and relatively lower number of foreign firms and JVs operating in the segment. However, one of the main challenges faced by the indigenous component manufacturers is the low-level of technology adaptation and R&D intensity. The various sub-sectors of the auto component industry in India are engine parts, electrical parts, drive transmission and steering parts, suspension and steering parts, suspension and braking parts, equipment and others. The products that form a part of these sub-sectors are shown in chart 1.

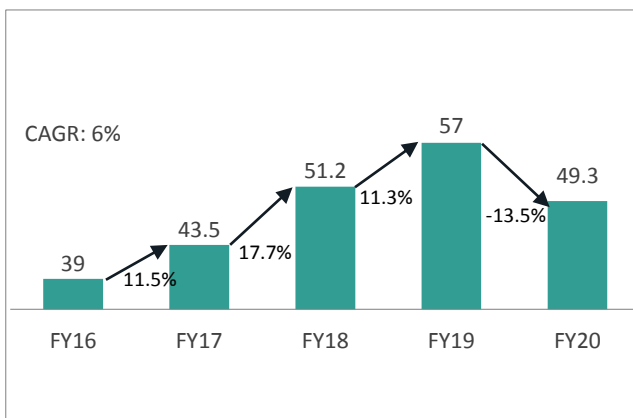
Chart 1: Classification of major Auto-components produced in India



Source: EXIM Bank India, ACMA

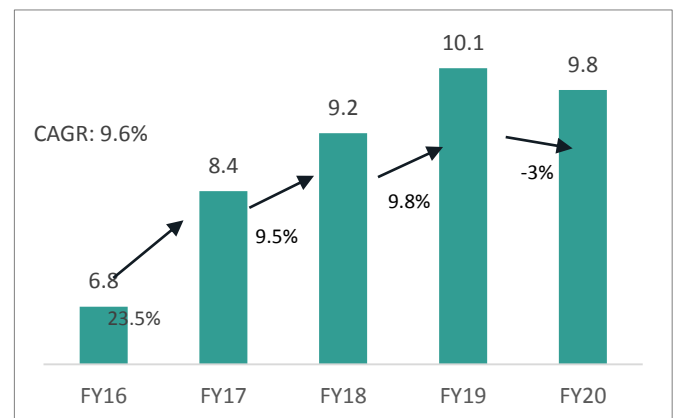
The turnover of the auto components industry grew at a CAGR of 6% from FY16 to FY20. In the same period, sales to domestic aftermarket grew at a faster pace of 9.6% CAGR. Owing to the overall slowdown in the economy and the fall in demand for automobiles, the auto components industry turnover declined 13.5% YoY to USD 49.3 bn in FY20, while the sales to aftermarket declined marginally by 3% YoY to USD 9.8 bn. FY21 further added to the woes of the industry by creating supply side challenges due to multiple nation-wide and localised lockdowns in most part of Q1-FY21.

Chart 2: Indian auto components industry turnover (USD bn)



Source: ACMA, CARE Ratings

Chart 3: Indian auto components after market sales (USD bn)



Source: ACMA, CARE Ratings

In terms of segment-wise share in OEM supplies, the passenger vehicle is the largest segment with 45.3% share, followed by 2-wheelers (19.6% share), M&H CVs (12.4% share), LCVs (11.8% share), tractors (6.5% share), 3-wheelers (3.3% share) and construction equipment (1.1% share). In terms of category of parts supplied to OEMs, engine component is the largest segment (26.1% share), followed by suspension and brakes (15.6% share), body and chassis (14.1% share), drive and transmission (13.2% share), electrical and electronics (12.4% share), interiors (10.8% share), consumables (6.4% share) and cooling (1.4% share).

Trade

Exports

To cater to the growing automobile industry across the globe, increasing number of global OEMs are sourcing their auto components from India. However, despite exporting to nearly 160 nations, India's share in global auto component exports stood at 3.5% or USD 15.1 bn in FY19, which indicates the huge opportunity size for growth in years to come for this industry.

India manufactures several key auto components for customers in the US, Germany, Turkey, Thailand, Turkey, Thailand, UK, Brazil, Mexico, Bangladesh, Italy, U.A.E. and Sri Lanka, among others. Furthermore, the gap between international and national regulations on safety and emissions has narrowed down considerably, bolstered recently by the compulsory implementation of BS-6 emission norms in April 2020. Also, as the need for reducing cost of manufacturing is increasingly being felt among the automobile OEMs in the developed countries, they seek to either set up their operations or source their component requirements from developing nations like India. Indian auto component manufacturers are increasingly gearing themselves to utilize this opportunity. The Indian exports of auto components grew at a CAGR of 6.6% from FY16 to FY20.

Table 2 depicts exports of select auto components from India. Analysis of the same shows that exports of multiple products had fallen in FY20, while in 10M-FY21 it declined for all the products.

Commodity	FY19		FY20		10M-FY21	
	USD mn	YoY growth	USD mn	YoY growth	USD mn	YoY growth
Gear boxes	412	24.6%	419	1.6%	284	-18%
New pneumatic tyres, of rubber used on buses or lorries	288	2.5%	255	-11.6%	152	-29.9%
Mounted brake linings	492	17.2%	493	0.1%	353	-16%
Drive-axles with differential, whether or not provided with other transmission components	378	10.4%	385	1.9%	296	-9.5%
Component Parts For Diesel Engines For Motor Vehicles, N.E	202	4.3%	175	-13.7%	115	-22.4%
Ignition Wiring Sets used In Vehicles	221	8.2%	242	9.5%	147	-28.8%
Steering wheels, steering columns & steering boxes	180	2.1%	194	7.5%	121	-25.3%
Spark ignition engines for motor cars	159	-28.8%	131	-17.5%	73	-32.5%
Road Wheels and Parts & Accessories Thereof	161	20.6%	110	-31.9%	74	-22.3%
Suspension shock absorbers	148	14.8%	149	0.6%	118	-4.2%
Radiators	48	-2.1%	51	6.4%	41	-4%
Clutches & Parts thereof	75	29.6%	74	-0.8%	56	-9.8%
Crank shaft for engines of heading	188	15.9%	157	-16.1%	108	-21.6%

Source: Ministry of Commerce & Industry - GOI, EXIM Bank India, CARE Ratings

Imports

The steady rise in production of automobiles in India over the past few years, has led to a healthy growth in demand for its components. Since India does not produce all varieties of components that automobile OEMs require for manufacturing, they need to be imported. From FY15 to FY19, imports of auto components rose by 1/3rd in value terms (USD 13.6 bn in FY15 and USD 17.7 in FY19), but fell in FY20 as the Indian automobile production declined during this year. The total volume of automobiles (commercial vehicles, passenger vehicles, two and three wheelers) witnessed a negative growth for the first time in 12 years during FY20 of 14.8% YoY. During the same year, auto components imports declined by 13% YoY in value terms.

India has a high dependence on China for its auto components imports with 26% share in FY20. Key items imported were drive transmission and steering parts, cooling systems, suspension and braking parts. Due to covid-19 pandemic, most nations, including India, are now seeking to minimize their reliance on China for imports. The ongoing India-China standoff is expected to hasten this process. However, this is easier said than done, as China offers the advantage of mass manufacturing, availability of subsidies and deployment of power at an economical cost, among others. These factors give the nation a favourable spot in the global exports market. Additionally, China presents a technological competence, which the Indian automotive industry currently lacks by a large extent. Hence, being self-sufficient and reducing imports from China shall take longer than expected, unless the industry receives the required government support.

The recently announced Production Linked Incentive (PLI) scheme for the automotive sector is a step in the right direction to make India 'atmanirbhar'. The automotive sector was allocated the highest amount of Rs. 57,000 crores. It aims at enabling the Indian automotive sector to drive local manufacturing and emerge as a major exporter of vehicles and components, along with reducing component imports. Incentives for other sectors like electronics, specialised steel, etc. would also create a conducive ecosystem for the Indian automotive sector. The incentive of Rs. 18,000 crores for advance chemistry cell battery sector would augment electrification in vehicles. There are expectations of higher investments in R&D, which may help in reducing the royalty payments made by OEMs operating in India. Alongside, it would help create more jobs in the sector and benefit the large number of MSMEs operating in this sector. Further details of PLI scheme are expected to be announced in FY22.

China, which supplied India with 1/4th of its total auto components requirements in FY20, was followed by South Korea (14% share), Germany (11% share), Japan (9% share), USA (7% share). The other nations contributing 3 to 5% share were Thailand, Singapore, Italy, UK and Belgium. Table 3 depicts imports of select auto components by India.

Table 3: Import of select auto-components by India

Commodity	FY19		FY20		10M-FY21	
	USD mn	YoY growth	USD mn	YoY growth	USD mn	YoY growth
Gear boxes	1,077	7.2%	1,019	-5.3%	603	-30.2%
Mounted brake linings	223	18.5%	177	-20.6%	126	-12.7%
Drive-axles with differential, whether or not provided with other transmission components	226	-0.8%	166	-26.7%	106	-23.9%
Component Parts For Diesel Engines For Motor Vehicles, N.E	52	23.9%	73	40.5%	79	42.5%
Ignition Wiring Sets used In Vehicles	103	-4.8%	77	-25.7%	44	-30.8%
Steering wheels, steering columns & steering boxes	262	-4.3%	197	-25%	115	-32.7%
Spark ignition engines for motor cars	436	13.8%	464	6.5%	171	-55.7%
Road Wheels and Parts & Accessories Thereof	180	-6.3%	147	-18.5%	66	-47.3%
Suspension shock absorbers	107	18.2%	78	-26.7%	43	-34.7%
Clutches & Parts thereof	134	6.8%	117	-12.6%	86	-10.7%

Source: Ministry of Commerce & Industry - GOI, EXIM Bank India, CARE Ratings

Challenges

1. Technology upgradation:

The automotive industry faces various disruptions in the areas of emission level, safety, electric mobility, and increasing usage of automotive electronics, all of which are technological intensive. For example, the migration to BS-6 norms poses challenges for the Indian auto component manufacturers due to the technology-intensive nature of the management modules of BS-6. Most of the technology used is imported and the local players do not have a level playing field like the internationally developed alternatives.

To bridge this gap, engaging in JVs with lead firms could play a pivotal role. Several lead firms in India, including both Indian and foreign firms have made efforts towards technology upgradation over the years, including the use of advanced modular platforms, new materials, and platform sharing in India. While there are multiple reasons for indigenous firms to engage in a JV with a lead firm, the key reason remains the access to technology and customer base.

2. High tax:

Some of the auto-components are placed at the highest slab of GST in India. The GST rates for Internal Combustion Engines (ICE) based vehicles and their components are currently at the highest GST rate of 28%. Apart from this, the compensation cess levied on these items is in the range of 1-22%, which makes ICE based vehicles one of the highest taxed manufactured product in India. The auto component industry also faces the challenge of two separate GST rates. While nearly 60% of auto components face a GST rate of 18%, the remaining face 28% GST. The lack of a uniform GST rate for auto components sector creates disincentives for enhancing greater domestic production in some of the sub-segments with higher GST rates.

The GST rate on auto components is higher than the MFN duty of 15% on several auto components. The tariffs are even lower for imports from countries such as China, South Korea and Japan, which benefit from tariff concessions under various free trade agreements, with tariffs for some auto components being as low as 1.8%. Further, the components of Electric Vehicles (EVs), face GST at 18% and 28%, while EVs face a GST of 5%. As such, there is limited indigenisation in EV manufacturing, with about nearly 3/4th of the EV components being imported, including batteries and power electronics. In order to promote indigenization of auto components by attracting investments in key areas such as batteries and domestic power electronics, it is important to streamline the taxes and duties on auto components, etc.

Financials

Analysis of financials of 76 companies in the auto components industry shows that the industry was a downward trend since FY20. After two consecutive years of healthy growth in revenues, FY20 witnessed a decline of 16.9% in net sales. The expenditures, cost of services and raw materials declined along with the income of the industry. Operating profit was lower by 1/5th, while PAT declined by nearly half on a YoY basis in FY20. However, the interest expense grew marginally.

In FY21, Q1 was undoubtedly the worst quarter faced the industry historically, where revenues were just 1/4th of previous year's levels. The expenditures also declined, but was higher than the income generated by the industry, and hence the industry witnessed loss at the operating as well as after-tax level. Q2-FY21 witnessed a recovery and reached nearly same level as last year. Q3-FY21 was a healthy quarter for the industry with growth in all parameters, however, this growth was witnessed on a low base of FY20.

Table 4: Financials of auto components industry (76 companies)

	Net sales		Expenditure		Cost of services & raw materials		Operating profit		Interest		Profit after tax	
	Rs. crore	YoY	Rs. crore	YoY	Rs. crore	YoY	Rs. crore	YoY	Rs. crore	YoY	Rs. crore	YoY
FY18	74,795	8%	66,025	7%	40,470	17%	10,794	11.5%	829	-1%	4,972	9.3%
FY19	86,141	15.2%	75,981	15.1%	49,434	22.1%	12,333	14.3%	1,037	25.1%	5,664	13.9%
FY20	71,562	-16.9%	64,101	-15.6%	39,222	-20.7%	9,884	-19.9%	1,077	3.9%	3,100	-45.3%
Q1-FY21	5,532	-72.3%	6,368	-64%	2,726	-75.7%	-396	-114.6%	248	-8.3%	-1,127	-201%
Q2-FY21	17,754	3.6%	15,804	2.1%	10,062	4.5%	2,381	5%	297	-3.3%	714	-19.7%
Q3-FY21	21,486	29.8%	18,963	27.1%	12,552	38.5%	2,967	41.7%	273	3.6%	1,396	116.1%

Source: ACE Equity, CARE Ratings

Concluding remarks and outlook

FY21 was a year of transition for the Indian auto components industry. The year presented fresh challenges in the form of outbreak of covid-19 and the resultant supply side disruptions, loss in production of automobiles, rise in input costs, trade disruptions, etc. Alongside, the industry also witnessed business growth opportunities for the long term. The announcement of an incentive-based vehicle scrappage policy, though voluntary, is expected to lead to a rise in automobile sales in the country, which has a direct benefit for the auto components industry. Additionally, the government's focus on quick adoption of electric vehicles may create significant potential for auto component manufacturers. The PLI scheme would encourage investments in the industry. The shift from BS-4 to BS-6 norms, which though is at present an impediment for the industry, will place the industry on par with international regulations on safety and emissions in the long term.

According to ACMA, the turnover of the auto components industry fell by 34% YoY to Rs 1.19 lakh crore (USD 15.9 bn) during H1-FY21. The 2nd half of FY21 is expected to see a strong recovery. CARE Ratings expects the industry to decline by 10 to 12% YoY in FY21. However, FY22 is expected to witness a positive growth of 18 to 20%, after two consecutive fiscals of de-growth.

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