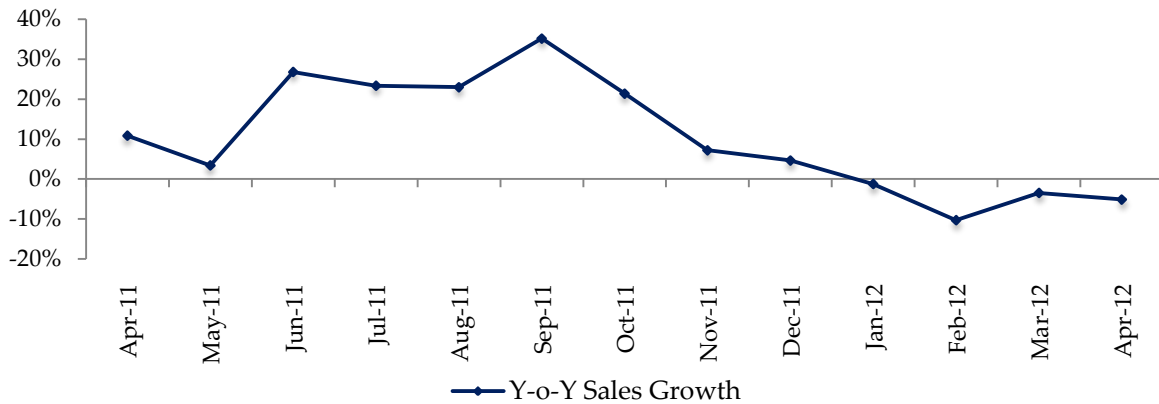


“Tractors growth – low speed yet strong traction”

Tractor industry after witnessing double digit growth in the first three quarters of FY12 observed a drop of around 5 per cent in Q4FY12. . Government measures to curb inflation resulted in decline of food grain and vegetable prices during the last quarter of FY12 which led to lower purchasing power of farmers. Uncertainty in economic scenario resulted in impediment of rural infrastructure development. Combined outcome of both the aforesaid factors resulted in drop in demand for tractors. However, irrespective of dismal performance of the industry, strong fundamentals like low tractor penetration per hectare of land, increasing government spending on agriculture, labour shortage, improving credit scenario, increasing co-operative farming etc. and recent hike in Minimum Support Price (MSP) suggest revival of the industry in H2FY13. Nevertheless, good monsoon will hold the key for the success of the tractor manufacturers.

Chart: Tractor sales growth for FY12



Source: CMIE and CARE Research.

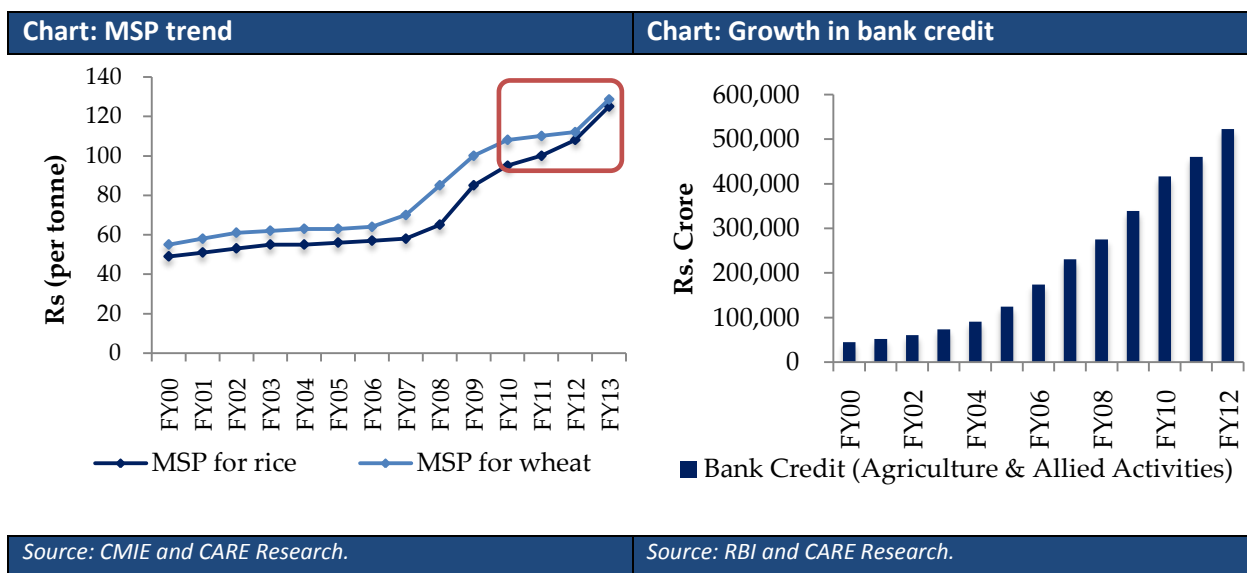
Increased government rural spending will drive tractor growth.

Although agriculture sector contributes less than 15 per cent to the total GDP, it is critical to the economy as it supports around 52 per cent of the total workforce. Agriculture is not only source of livelihood for large section of population but the fact that an average Indian spends half of the total expenditure on food makes it important from the food security point of view. In addition to support the economic growth of around 9 per cent which government was targeting to achieve as per 12th five year plan, CARE research believes agriculture sector needs to grow at 4 per cent per annum. The performance of the agriculture sector thus assumes great significance for the government.

In order to achieve targeted growth government has allocated substantial funds through various schemes and subsidies in rural region, for example increasing farm credit, schemes like Pradhan Mantri Gram Sadak Yojana (PMGSY), Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA), fertilizer subsidies, seed subsidies, irrigation subsidies etc. In Union Budget 2012-13, the agriculture credit was raised to Rs. 575,000 crore from Rs. 475,000 crore allocated in the previous fiscal year. NABARD was being provided with Rs. 10,000 crores for refinancing the Regional Rural Banks (RRBs). Further, government has also initiated drive to modify Kisan Credit Card (KCC) Scheme into a smart card enabling it to be used at ATMs. Collectively these initiatives will lead to increased money supply in the rural system and in turn increase farmer’s liquidity consequently fuels the demand for tractors.

The recent increase in MSP will boost demand for tractors.

MSP is fixed in order to ensure that farmers get remunerative prices, which encourages them to do higher investments in agricultural activities. The Commission for Agricultural Costs and Prices (CACP) takes into account factors such as cost of production, change in prices of inputs, demand and supply, market price trends and cost of living while recommending MSP. During DY07-FY11 period, MSP witnessed sharp rise, however post FY11 the increase in MSP has been moderate as the government was trying to keep food inflation low. The stagnant MSP coupled with increased input prices resulted in impediment in farmer’s purchasing power. In June, 2012 with the slowing down of headline inflation, government increased MSP in the range of 16-53 per cent. This rise in MSP is considered to be encouraging for the farmers as it will boost their income and subsequently push tractor demand.



Fundamentals strong but monsoon holds key to success for OEMs in the short run.

Rainfall is the key determinant of agricultural performance during the “Kharif” season. Adequate rainfall during June to September translates in high yield of Kharif crops and thus improves farmer’s income. For this reason good monsoon is considered as a critical driver for the growth of tractor sales. With the increasing use of tractors for non agricultural purposes in the past 5 years, the strong correlation between monsoon and tractor sales dwindled e.g. in FY10 country witnessed worst monsoon in three decades, conversely tractor sales surged by around 32 per cent. However, considering the current slowdown in economic activities like construction, manufacturing and mining, CARE Research believes healthy growth in agriculture sector will drive tractor demand. Hence tractor sales will be highly dependent on good monsoon. CARE Research believes that the tractor sales will revive in H2FY12 on the back of strong fundamentals however monsoon will play a critical role.

Co-operative farming will be vital to sustain growth in the long run...

Current farm power availability of India is around 1.7 KW/ha which is much lower than that of Korea (7KW/ha), Japan (14 kw/ha and USA (6 kw/ha) which suggests huge potential for the growth for farm mechanization in India. However, small land holdings of Indian farmers make it difficult for them to afford tractors. The net sown area in India currently stands at 141 million ha and with the gradual increase in area put to non-agriculture use the net sown area will decrease in the times to come. Furthermore, with population of country continuously growing will further pull down the per capita land holdings of the country. As per government estimates per capita land holdings which was 0.32 ha in 2001 as against world average of 1.19 ha and it is expected to reduce to 0.23 by 2025.

The 60-70 per cent of the total farmers in India are marginal farmers with less than 1 hectare land holding. The small holdings of the farmers make it futile for the marginal and small farmers to own assets like tractors as benefits of tractors fail to make up for the additional cost burden in absence of proper utilization of the asset. Cooperative farming is a method wherein farmers pool their resources for mutual benefit. With co-operative farming, increased number of marginal and small farmers would be capable of owning tractors which will fuel the demand for tractors going forward.

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