

# Snarls & crossroads

Risks accelerating for vehicle makers

April 2020



## **Auto sales unlikely to reverse course in a hurry**

The extended nationwide lockdown to contain the Covid-19 pandemic has brought the automobile industry to a standstill. Automobile manufacturers and dealers, who were grappling with weak demand and liquidation of Bharat Stage (BS)-IV inventory ahead of the shift to BS-VI, are now left wringing hands.

The Ministry of Home Affairs in a notification on April 15 allowed resumption of several activities from April 20, albeit by strictly adhering to social distancing norms. This covers manufacturing in industrial units, including automobile factories, under the purview of state/ district administration.

However, operations of automobile dealerships will be difficult until May 3, and some even after. That means, even if manufacturing units start functioning, vehicle sales will not happen until that date.

In addition, the central government has directed state/ district administrations to calibrate the revocation of lockdown after demarcating districts as red (hotspots with high infection) and green (non-infected) zones. This implies that the sales outlets in red zones are likely to remain shut even if the lockdown is lifted after May 3.

Against this backdrop, CRISIL Research has assessed the risk the two-wheeler and passenger vehicle industries face based on a two-factor framework – district-wise automobile sales concentration and the risk of spread of Covid-19.

For the analysis of automobile sales, we considered sales intensity and growth momentum in the districts, and for analysing the Covid-19 spread risk, the present case intensity, and risks to spread. In short, if a district that accounts for high sales of two-wheelers or passenger vehicles is also impacted severely by the pandemic, it poses a higher risk to overall industry sales.

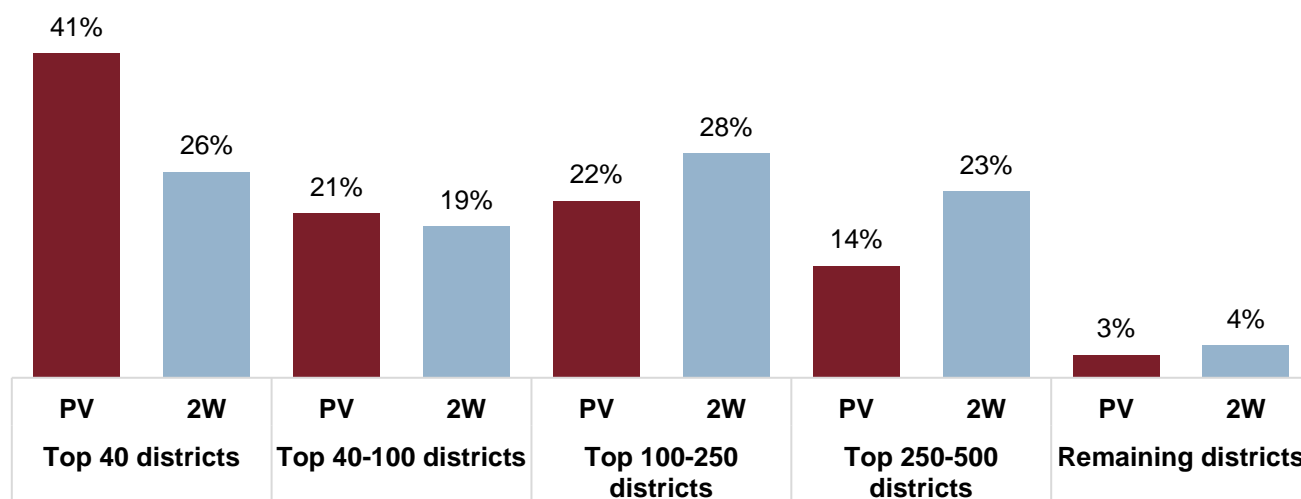
## **Passenger vehicles more vulnerable due to sales concentration**

Two-wheeler and passenger vehicle segments cater to different customer segments. As a result, the geographies they are dependent on for sales also varies.

As per our analysis, top 100 districts account for 62% of passenger vehicle sales in volume terms, with 41% coming from the top 40 districts alone. In comparison, top 100 districts account for only 45% two-wheeler sales and top 40 for 26%.

This shows, sales concentration in the top 100 districts is higher for passenger vehicles compared with two-wheelers.

**Spread of passenger vehicle and two-wheeler sales across districts**



Source: Ministry of Road Transport and Highways, CRISIL Research

**In ‘very high impact’ districts, half of passenger vehicle sales and a third of two-wheeler sales are at risk**

Our analysis of automobile retail sales pattern and spread of Covid-19 across districts in India shows that the level of risk for two-wheeler and passenger vehicles segments is considerably different in ‘very high impact’ districts, or districts where both automobile sales intensity and Covid-19 infection are significantly high.

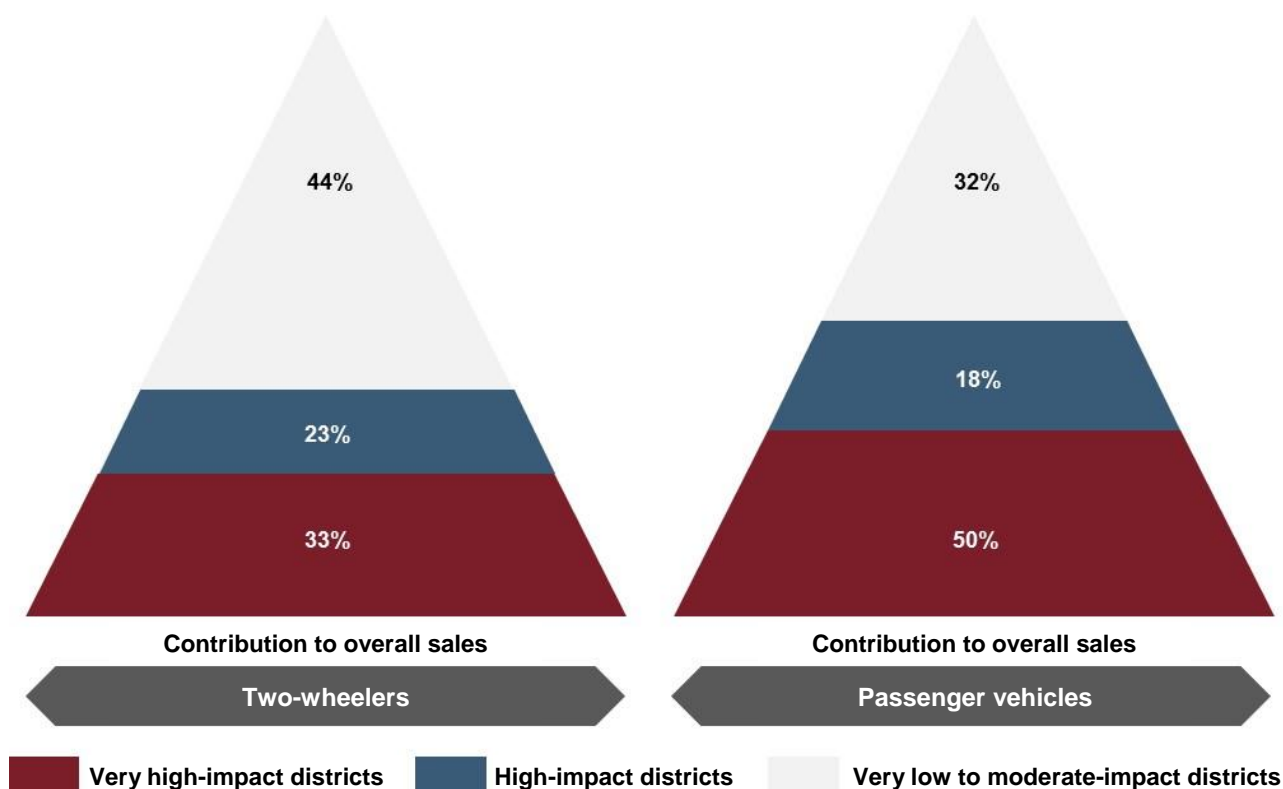
These districts account for 50% of passenger vehicles sales in the country. In case normal business activity does not resume in these districts after the first week of May, half of passenger vehicles sales will be at ‘very high risk’.

That said, these districts account for 33% of two-wheeler sales in the country. If normalcy does not return after the first week of May in these districts, a third of two-wheeler sales will also be at ‘very high risk’.

‘High’ and ‘very high impact’ districts together account for 56% of two-wheeler and 68% of passenger vehicles sales in India.

Even after the lockdown is lifted, sales volume will remain muted as consumers are unlikely to flock to the dealerships. Indeed, consumers may avoid shopping malls/markets due to the fear of infection for an extended period.

**Half of passenger vehicle sales at very high risk**



Source: Ministry of Road Transport and Highways, CRISIL Research

On the brighter side, 44% and 32% of the market for two-wheelers and passenger vehicles, respectively, lies in very low to moderate risk districts, where normalcy is likely to return more quickly, although in a phased manner.

Factors linked to the pandemic such as the impact on consumer incomes and the financing scenario will also have a bearing on demand recovery in these districts.

Consumer incomes would be affected and financiers would be extra-cautious about lending portfolio quality and quantum of exposure to stressed geographies.

Additionally, because of deterioration in asset quality and increase in the cost of funds of non-banking financing companies – despite the reduction in repo rates by the RBI – interest rates for NBFC borrowers are likely to remain firm.

Therefore, automobile manufacturers and new vehicle financiers should tactically target low to moderately impacted districts to minimise the impact of Covid-19 on their sales. Those with sharper focus on these markets will be better positioned to deal with the emerging situation. At the same time, players also need to retune their strategies in high-to-very high impact districts to minimise the impact on overall sales performance.

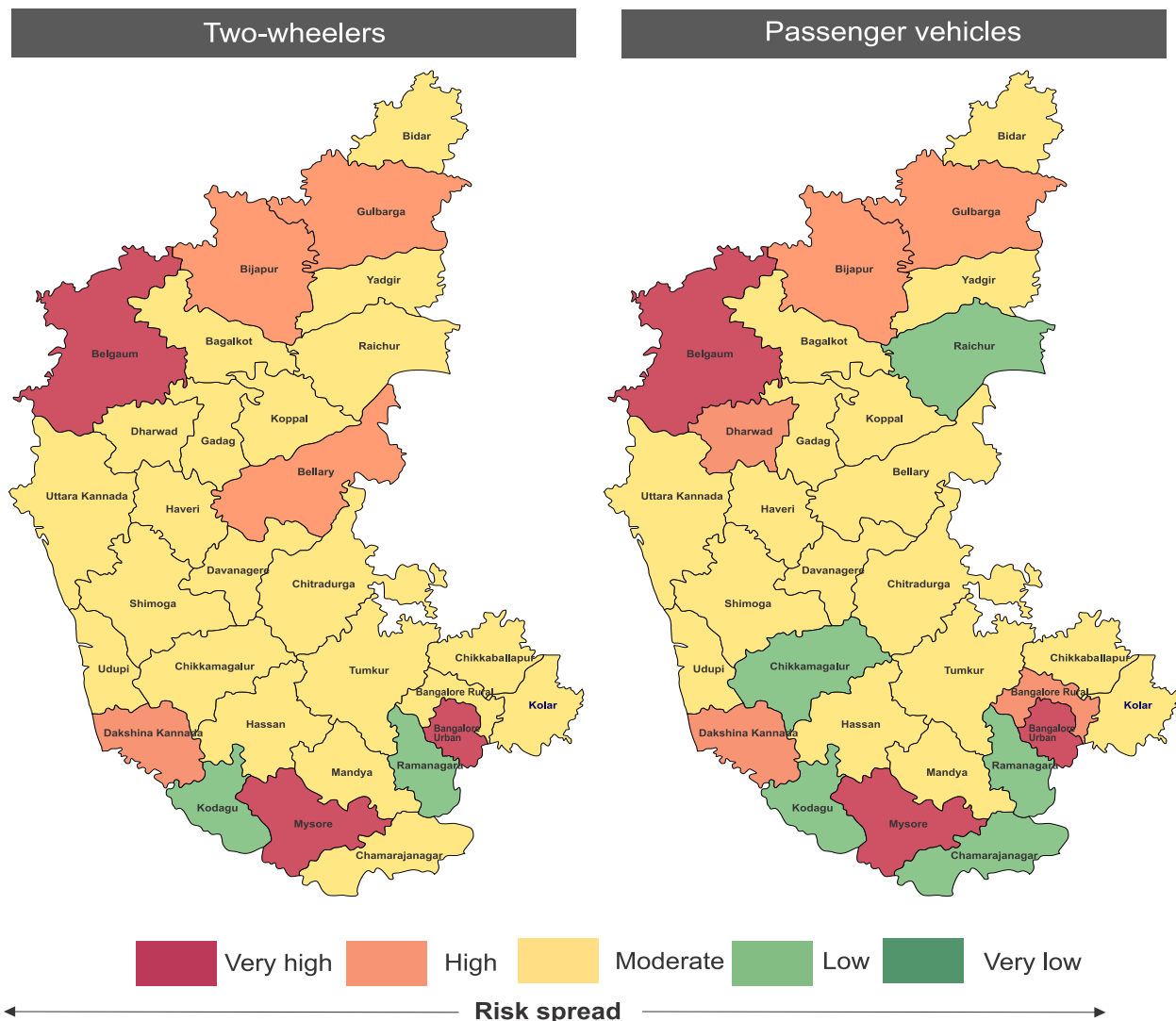
## State-wise differences in risk levels of vehicle segments

In order to understand how various districts fare on Covid-19 risk and automobile sales, we have to look at each state in isolation. The risk situation in Karnataka, for instance, is substantially different from the pan-India scenario.

Our analysis shows that around 60% of two-wheeler sales and 74% of passenger vehicle sales in Karnataka face high to very high risk. As much as 49% of two-wheeler sales and 57% of passenger vehicles sales are estimated to be at very high risk in Karnataka.

Yet, 60% of Karnataka districts show low to moderate risk for both passenger vehicles and two wheelers.

Overall risk assessment of a district though could be different for two-wheelers and passenger vehicles, as the following heat maps show.



Of the 30 districts in Karnataka, 10% fall in the very high and high risk categories each, 53% in moderate, and 7% in low risk category for both passenger vehicles and two-wheelers. The balance 20%, or six districts, fall under different risk categories for two-wheelers and passenger vehicles.

For instance, Ballari is a high-risk district for two-wheelers and a low-risk one for passenger vehicles. Similarly, Raichur, Chikkamagaluru, and Chamarajanagar are moderate-risk districts for two-wheelers and low-risk for passenger vehicles. In other words, the same district may pose different level of risks based on the category of vehicle. The evolving situation makes it imperative for automakers and financiers alike to assess the risks proactively and devise a strategy based on their product portfolio, sales spread across districts and dealership presence.

That would help them identify the districts that could return to normalcy faster and accordingly generate business once the lockdown is lifted.

Our analysis of Karnataka, for instance, reveals that a few districts such as Shimoga, Tumkur and Udupi look attractive for passenger vehicles as these have high sales intensity and low Covid-19 impact.

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