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TYRES: CONTROLLING COSTS CRUCIAL

In view of steep rise in the price of natural rubber, tyre manufacturers want immediate withdrawal of the rubber export subsidy scheme.

The Indian tyre industry is raw-material oriented. Rubber forms nearly 70 per cent of the input costs. Any increase in the price of rubber will force tyre units to raise the prices of tyres. Manufacturers say the increase in tyre prices is lagging behind the increase in input costs. This is because of intense competition. It has resulted in very narrow profit margins for tyre companies.

In respect of cars and two-wheelers, tyres are to be replaced once in a while. But, a minimum of eight truck tyres have to be changed annually due to high wear and tear caused by bad roads. A truck tyre has a life span of 50,000 to 60,000 km compared to a life span of 40,000 to 50,000 km for a car tyre.

The Rs 145-billion Indian tyre industry constitutes about four per cent of the global tyre industry. Three leading companies account for 62 per cent of the sales, and are amongst the 20 large companies in the world. The industry manufactures tyres for almost every application. The companies are known for high-quality products.

The export of tyres from India has been consistently growing at 11 per cent annually and earns Rs 18.5 billion. Indian tyres are exported to 65 countries across six continents.

The Automotive Tyre Manufacturers Association (ATMA) has demanded a ban on exports to check the current bull phase in the market. It said that the supply shortage had hit hard the rubber-based industries, especially tyre industry.

However, such a move has no support as it would hit hard the small and medium rubber farmers. About 85 per cent of the rubber growers are small farmers with no more than two hectares of cultivable land. The traders argued that the Indian tyre industry is getting rubber at Rs 10 less than the international price per kg.

Ready for radialisation?

Radialisation of the Indian tyre industry was pioneered way back in 1977 by J.K. Tyres. Radialisation is gaining popularity particularly in the passenger car segment. Radialisation in the truck and bus segment was introduced only in 1999 again by J.K. Tyres. However, the progress is slow.

Around 650,000 tyres a month are sold in the largest segment of the entire domestic tyre market, i.e., truck and bus tyres. Of this, only 2 to 3 per cent comprises radial tyres. Of course, in the passenger vehicle segment, the level of radialisation is high. The price of radial tyres is 50 to 60 per cent higher than the price of crossply tyres.

The truck and bus radial (TBR) market is an important growth segment for the future. But, the major players are unable to predict when exactly this segment will be ready for radialisation. It may take 5 to 15 years.

The J.K. Industries believes that the share of the radial tyres in the TBR market would go up from 2 to 3 per cent in 2005 to 15 per cent by 2010. However, the market leader Apollo Tyres is not that optimistic.

The Chennai-based MRF thinks that the technology for radial tyres need not come from foreign firms. It feels that we have to develop technology (for radial tyres) on our own.

Major players

Apollo Tyres is one of the fast growing tyre companies in the world and is the 15th largest in the globe. In India, its manufacturing plants are located in Perambra (Kochi) and Kalamassery (leased facility) in Kerala, Ranjangaon near Pune and Limela in Gujarat.

Tyre Production in India

(million tonnes)

Year	Production	
	Automobile tyres	Bicycle tyres
1960-61	1.5	11.2
1970-71	3.8	19.2
1980-81	8.0	27.0
1990-91	20.1	24.8
2000-01	NA	12.7
2003-04	NA	50.4
2004-05	NA	75.7

Source: Economic Survey 2005-06, p.S-32

Apollo Tyres, India's largest tyre maker by volumes, believes in growth with acquisitions. The company is looking at acquisitions in Europe and South East Asia. Early 2006, it acquired Dunlop Tyres International (proprietary) through an all-cash deal worth Rs 2900 million.

Apollo Tyres is all set to invest Rs 5200 million on a Greenfield facility near Chennai to manufacture radial tyres for trucks, buses and cars. The project is expected to generate employment for about 2000 people.

Apollo Tyres wants to import radial tyres for luxury cars like Mercedes Benz, BMW and Vokswagen from the company's manufacturing facility in South Africa. It has decided to completely stop production of these tyres from its manufacturing facility in India in the next few months.

As part of the restructuring, Apollo has replaced the raw material source bases of Dunlop South Africa, with its own bases in China, Russia and Eastern Europe.

The company plans to invest in a new radial tyre plant with an initial investment of Rs 3 billion, going up to Rs 5 billion in the last phase. The new plant will make passenger car, truck, bus and farm equipment tyres.

Apollo International, a subsidiary of the Apollo Tyres Group, will invest Rs 3 billion during 2006 to 2008 for setting up Container Freight Station (CFS) and Inland Container Depot (ICD) at various ports of India. The group is showing interest in Jawaharlal Nehru Port Trust in Navi Mumbai and other locations including Kerala and North India.

The rise in rubber prices has prompted tyre major MRF to set up a small factory in Sri Lanka to procure rubber for retreading products. Rubber prices are reported to be cheaper by a couple of rupees in Sri Lanka.

The tyres qualified for speeds up to 240 kmph are specifically targeted for cars such as Mercedes S Class, Ford Mondeo and Skoda Laura. These tubeless tyres are produced at company's plant in Pondicherry.

J.K. Tyres is expanding the capacity of its Banmore facility near Gwalior in Madhya Pradesh, with an investment of Rs 2 billion in a period of three years, commencing from 2005. The capacity would go up from 2.2 million tyres to 3 million tyres. Besides expansion, the company also intends to set up another plant in the area.

The Madhya Pradesh plant started production in 1991 with a production capacity of 570,000 tyres per annum and a range of tyres and passenger radials in particular.

The state government has granted backward area package, and hence the company has continued to grow despite the increase in the raw material prices.

The J.K. Industries Ltd has undertaken some cost cutting operations which include reduction of overheads, improved working capital management and product re-engineering.

An increase of Rs one per kg in the price of natural rubber results in an additional burden of Rs 350 million annually on the tyre industry.

Unlisted Ruia group has bought majority stakes in tyre companies Falcon Tyres and Dunlop India for Rs 2 billion. The automotive tyre and rubber product manufacturing firms are part of the Dubai-based Jumbo group. Jumbo held 74.5 per cent of Dunlop and 68 per cent of Talcon.

Major problems

Tyre prices are subject to frequent hikes. The prices of rubber have been spiralling in recent years. Also, petroleum, which is used extensively in the manufacture of tyres, is subject to frequent price hikes.

Natural rubber price has been going up steadily. It increased from Rs 30,360 a tonne in 2000-01 to Rs 32,280 a tonne in 2001-02, to Rs 39,170 a tonne in 2002-03. In April 2004, it was Rs 52,350 a tonne.

During a short period of six months (November 2005 to April 2006), natural rubber prices shot up by 36 per cent from Rs 62 to Rs 82 per kg. Rubber price peaked to new high in May 2006 as the benchmark grade RSS-4 pegged at Rs 97 a kg.

It is said that an increase of Rs one per kg in the price of natural rubber results in an additional burden of Rs 350 million annually on the tyre industry. The rubber stocks are alarmingly low. In April 2004, they came down to less than 60 days of consumption.

Tyre manufacturers elsewhere are getting access to cheaper Indian raw materials, and therefore Indian manufacturers are unable to compete on the export front.

The threat of cheap imported tyres from South Asian countries, primarily from China, Taiwan and Korea, is there. These tyres are underpriced by 20 to 30 per cent. This is cutting into the profit margins of dealers.

The industry also suffers from

low productivity of labour. The current regulatory environment does not give management the right to manage, and thus flexibility to reduce costs. A specific timeframe to undertake labour reforms should be adopted.

The import duty on the finished product, that is tyre, is also 15 per cent and under the various trade agreements such as the Bangkok agreement (where South Korea and China are also signatories), it is 12.9 per cent and under the South Asian Free Trade Agreement (SAFTA), it is 7.5 per cent. It is a classical case where the finished product, that is, automobile tyres, suffers from an inverted duty structure. This evidently needs urgent correction.

There is significant difference between sales tax imposed by various states. For instance, in Tamil Nadu, the sales tax on tyres is high at 13.6 per cent (12.6 per cent sales tax plus a resale tax of 1 per cent plus surcharge). But, in the neighbouring Pondicherry it was only 8 per cent. Consequently, there is a difference of Rs 1000 per truck tyre between these two states. In Chennai, around 10,000 truck tyres are sold per month against the potential for 20,000 tyres. Pondicherry is supplying the balance of 10,000 tyres.

One charge against the tyre industry is that it is not investing enough in R&D to offer cheaper options. The R&D spending in the tyre industry is less than Rs 1 billion a year.

Measures needed

In view of steep rise in the price of natural rubber, tyre manufacturers want immediate withdrawal of the rubber export subsidy scheme.

The Rs 3500-5000 a tonne subsidy has led to an export of over 70,000 tonnes of natural rubber in 2003-04 against 13,300 tonnes in 2000-01.

The government proposes to make quality certification compulsory for tyres manufactured and sold in India. This means that tyres with Bureau of Indian Standards (BIS) certification only can be sold and foreign tyres cannot be sold through local outlets. This move would impact imports of cheaper tyres from China as well as companies like Kumho and Hankook.

The government seeks to ensure that manufacturers of pneumatic tyres and tubes cannot sell products that do not conform to the standards specified by the BIS.

The Pneumatic Tyres and Tubes for Automotive Vehicles (Quality Control) Order 2006 could therefore have serious consequences for imported brands. However, tyres and tubes manufactured and dispatched for export purposes will not come under the purview of the order.

There is need for stepping up investment in R&D to a level of Rs 15 billion if manufacturers are serious about developing technology for the TBR market.

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