

CONSUMER DURABLE INDUSTRY IN INDIA

1. OVERVIEW OF INDIA'S CONSUMER DURABLES MARKET

India's Consumer Market

India's consumer market is riding the crest of the country's economic boom. Driven by a young population with access to disposable incomes and easy finance options, the consumer market has been throwing up staggering figures.

India officially classifies its population in five groups, based on annual household income (based on year 1995-96 indices). These groups are: Lower Income; three subgroups of Middle Income; and Higher Income. However, the rupee income classifications by themselves do not present a realistic picture of market potential for a foreign business enterprise, because of significant differences in purchase power parities of various currencies. In fact, the Indian rupee has a very high purchase power parity compared to its international exchange value. For instance, while the exchange rate of one US dollar is 48.50ⁱ Rupees, the domestic purchasing power of a US dollar in the US is closer to the purchasing power of Rs 6 in India, for equivalent needs and services. As a result, India ranks fifth in the world, on purchase power parity terms, despite being having low per capita national income (US\$ 340 per capita).

Consumer Classes

Even discounting the purchase power parity factor, income classifications do not serve as an effective indicator of ownership and consumption trends in the economy. Accordingly, the National Council for Applied Economic Research (NCAER), India's premier economic research institution, has released an alternative classification system based on consumption indicators, which is more relevant for ascertaining consumption patterns of various classes of goods.

There are five classes of consumer households, ranging from the destitute to the highly affluent, which differ considerably in their consumption behavior and ownership patterns across various categories of goods. These classes exist in urban as well as rural households both, and consumption trends may differ significantly between similar income households in urban and rural areas.

Structure of the Indian Consumer Market

(in millions of households)

<i>Consumer Classes (Annual income Rs)</i>	<i>1996</i>	<i>2001</i>	<i>2007</i>	<i>Change</i>
The rich (Rs.215, 000 and more) ⁱⁱ	1.2	2	6.2	416%
The Consuming Class (Rs. 45-215,000)	32.5	54.6	90.9	179%
The Climbers (Rs. 22-45, 000)	54.1	71.6	74.1	37%
The Aspirants (Rs.16-22, 000)	44	28.1	15.3	-65%
The Destitute (below Rs. 16,000)	33.2	3.4	12.8	-61%
Total	164.8	180.7	199.2	21%

Source: National Council for Applied Economic Research (NCAER)

The target market segments considered for aspiration and lifestyle goods are the 35 million homes representing the consuming classes and the rich, or some 150 million people. It was the roughly 80 million households that comprise the upper aspiring to lower consuming that so excited the global market when they decided to enter the Indian market in the early 1990's.

It was not until 1992, when the Indian market first began to open up post liberalization, that the MNCs started taking a closer look at the purchasing power of the country's middle class. Inevitably, the first thing they saw was the massive volume of this potential market, rather than its cultural idiosyncrasies.

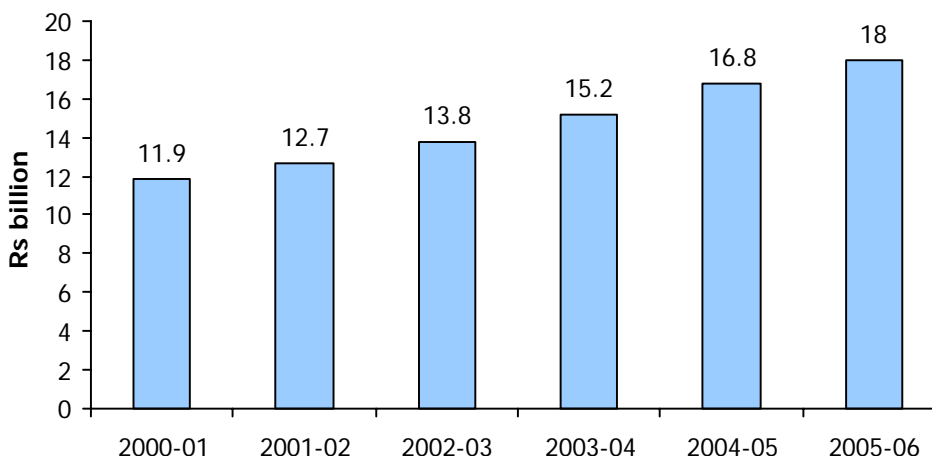
Overview of India's Consumer Durables Market

The Indian consumer durables segment can be segregated into consumer electronics (TVs, VCD players and audio systems etc.) and consumer appliances (also known as white goods) like refrigerators, washing machines, air conditioners (A/Cs), microwave ovens, vacuum cleaners and dishwashers.

Most of the segments in this sector are characterized by intense competition, emergence of new companies (especially MNCs) and introduction of state-of-the-art models, price discounts and exchange schemes. MNCs continue to dominate the Indian consumer durable segment, which is apparent from the fact that these companies command more than 65 per cent market share in the colour television (CTV) segment.

In consonance with the global trend, over the years, demand for consumer durables has increased with rising income levels, double-income families, changing lifestyles, availability of credit, increasing consumer awareness and introduction of new models. Products like air conditioners are no longer perceived as luxury products.

Growth of Consumer Electronics Production in India



Ministry of Information and Technology, Government of India

The biggest attraction for MNCs is the growing Indian middle class. This market is characterised with low penetration levels. MNCs hold an edge over their Indian counterparts in terms of superior technology combined with a steady flow of capital, while domestic companies compete on the basis of their well-acknowledged brands, an extensive distribution network and an insight in local market conditions.

One of the critical factors that influences durable demand is the government spending on infrastructure, especially the rural electrification programme. Given the government's inclination to cut back spending, rural electrification programmes have always lagged behind schedule. This has not favoured durable companies till now. Any incremental

spending in infrastructure and electrification programmes could spur growth of the industry.

The digital revolution is shaking up the consumer durables industry. With the advent of MP3 music files, personal video recorders, game machines, digital cameras, appliances with embedded devices, and a host of other media and services, it is no longer clear who controls which part of home entertainment. This has set off a battle for dominance, and the shakeup is spanning the entire technology spectrum.

Microsoft Corp. is spending billions on entertainment initiatives such as its Xbox video game console. Compaq and HP sell MP3 music players that plug into home-stereo systems. Apple Computer is positioning its new iMac as a digital-entertainment device. Sony is building Vaio computers that focus on integrating multimedia applications. Philips sells stereos that hook into a high-speed Internet connection to play music from the Web. More startups are trying to carve out profitable niches in digital music, video, and home networking. The industry is witnessing a number of strategic alliances, to develop a range of capabilities - electronic hardware, software and entertainment content.

As more consumers grow comfortable with technology, companies need to build simpler devices that offer more entertainment and convenience. These new machines need to work together readily, and should be as easy to set up and use as a telephone or a television. Consumerization of technology could be a major phenomenon over the next 5 to 10 years. This could hasten industry consolidation, as healthy companies gain market share by buying out weaker ones at attractive prices.

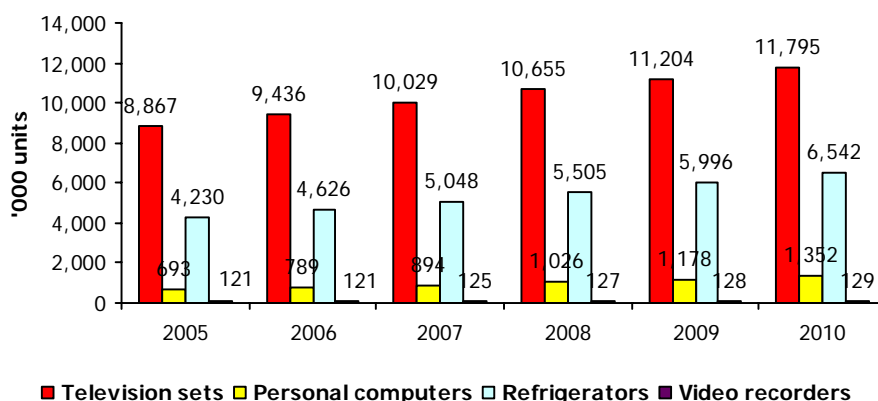
Apart from steady income gains, consumer financing has become a major driver in the consumer durables industry. In the case of more expensive consumer goods, such as refrigerators, washing machines, colour televisions and personal computers, retailers are joining forces with banks and finance companies to market their goods more aggressively. Among department stores, other factors that will support rising sales include a strong emphasis on retail technology, loyalty schemes, private labels and the subletting of floor space in larger stores to smaller retailers selling a variety of products and services, such as music and coffee.

Growth Scenario

Rising disposable income and declining prices of durables have resulted in increased volumes. An increase in disposable income is aided by an increase in the number of both double-income and nuclear families.

The market for consumer durables (including entertainment electronics, communitarian and IT products) is estimated at Rs 32 billion (US \$7.1 billion). The market is expected to grow at 10 to 12 per cent annually and is expected to reach Rs 60 billion (US\$13.3 billion) by 2008. The urban consumer durables market is growing at an annual rate of seven to 10 per cent, the rural durables market is growing at 25 per cent annually. Some high-growth categories within this segment include mobile phones, TVs and music systems.

Sales trend and future projection of consumer electronics segment



Source: Intelligence Unit, The Economist

Consumer durables are expected to grow at 10-15 per cent in 2007-08, driven by the growth in CTV's and air conditioners. Value growth of durables is expected to be higher than historical levels as price declines for most of the products are not expected to be very significant. Though price declines will continue, it will cease to be the primary demand driver. Instead the continuing strength of income demographics will support volume growth.

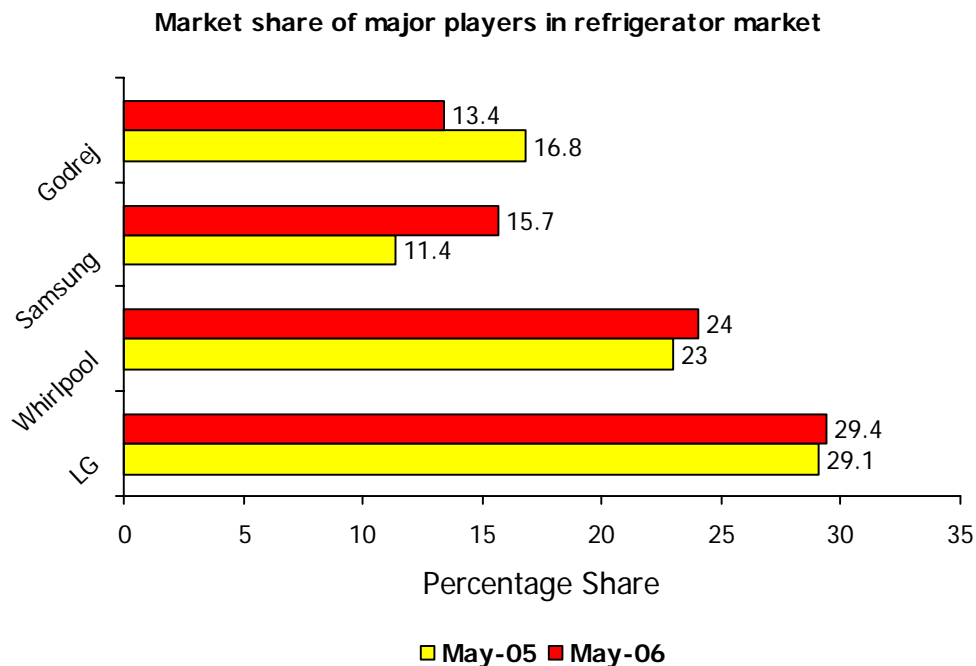
Product Category	2005-06 over 2004-05		2007-08 over 2005-06 (CAGR)	
	%	Growth Driver	%	Growth Driver
Air-Conditioners	15	Reduction in prices	20-22	Decreasing prices and changing lifestyle.
Refrigerators	4-6	Increasing demand resulting in high concentration in urban areas.	5-8	High demand for the frost-free segment together with reduction in prices.
Colour Televisions	3-5	To touch 8.0-8.2 million units, fuelled by increase in disposable income.	5-8	Increasing disposable income and declining prices.
Washing machines	7-9	Low base, increasing demand for fully-automatic segment	8-10	Reduction in prices of fully-automatic machines fuelled by rising disposable income.

Source: CRIS INFAC

2. COMPETITION OVERVIEW

Samsung India

Samsung India commenced its operations in India in December 1995, today enjoys a sales turnover of over US\$ 1 billion in just a decade of operations in the country. Samsung design centres are located in London, Los Angeles, San Francisco, Tokyo, Shanghai and Romen. Samsung India has its headquartered in New Delhi and has a network of 19 Branch Offices located all over the country. The Samsung manufacturing complex housing manufacturing facilities for Colour Televisions, Colour Monitors, Refrigerators and Washing Machines is located at Noida, near Delhi. Samsung 'Made in India' products like Colour Televisions, Colour Monitors and Refrigerators are being exported to Middle East, CIS and SAARC countries from its Noida manufacturing complex. Samsung India currently employs over 1600 employees, with around 18% of its employees working in Research & Development.



Source: ORG-MARG
Outlook Business, 20 August, 2006

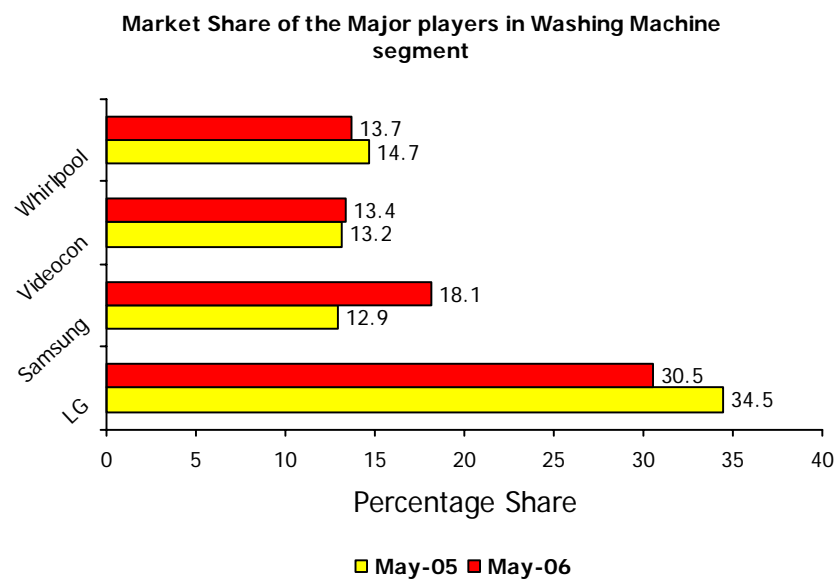
Whirlpool of India

Whirlpool was established in 1911 as first commercial manufacturer of motorized washers to the current market position of being world's number one manufacturer and marketer of major home appliances. The parent company is headquartered at Benton

Harbor, Michigan, USA with a global presence in over 170 countries and manufacturing operation in 13 countries with 11 major brand names such as Whirlpool, KitchenAid, Roper, Estate, Bauknecht, Laden and Ignis. Today, Whirlpool is the most recognized brand in home appliances in India and holds a market share of over 25%. The company owns three state-of-the-art manufacturing facilities at Faridabad, Pondicherry and Pune. In the year ending in March '06, the annual turnover of the company for its Indian enterprise was Rs.1,375 crores. According to IMRB surveys Whirlpool enjoys the status of the single largest refrigerator and second largest washing machine brand in India.

LG India

LG Electronics was established on October 1, 1958 (As a private Company) and in 1959, LGE started manufacturing radios, operating 77 subsidiaries around the world with over 72,000 employees worldwide it is one of the major giants in the consumer durable domain worldwide. The company has as many as 27 R & D centers and 5 design centers. It's global leading products include residential air conditioners, DVD players, CDMA handsets, home theatre systems and optical storage systems.



Source: ORG-MARG
Outlook Business, 20 August, 2006

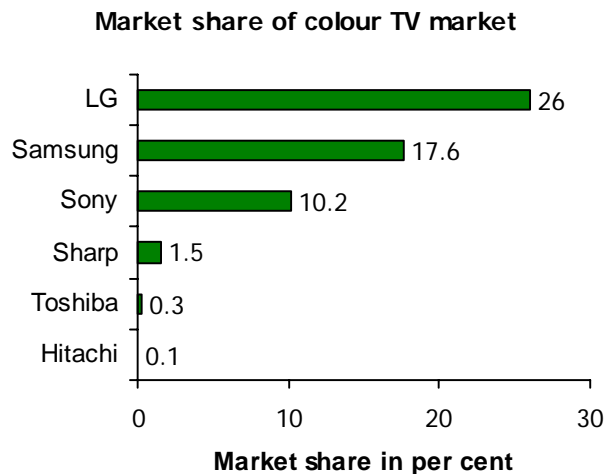
Godrej India

Godrej India was established in 1897, the Company was incorporated with limited liability on March 3, 1932, under the Indian Companies Act, 1913. The Company is one of the largest privately-held diversified industrial corporations in India. The combined Sales during the Fiscal Year ended March 31, 2006, amounted to about Rs. 58,000 million (US\$ 1,270 million). The Company has a network of 38 Company-owned Retail Stores, more than 2,200 Wholesale Dealers, and more than 18,000 Retail Outlets. The

Company has Representative Offices in Sharjah (UAE), Nairobi (Kenya), Colombo (Sri Lanka), Riyadh (Saudi Arabia) and Guangzhou (China-PRC).

Toshiba India

Toshiba India Private Limited (TIPL) is the wholly owned subsidiary of Japanese Electronic giant Toshiba Corporation and was incorporated in India on September 2001. Toshiba had a presence in India since 1985 and was represented in India through their Liaison Office.



Source: ORG_GFK, Dec 2006

Sony India

Sony Corporation, Japan, established its India operations in November 1994. In India, Sony has its distribution network comprising of over 7000 channel partners, 215 Sony World and Sony Exclusive outlets and 21 direct branch locations. The company also has presence across the country with 21 company owned and 172 authorized service centers.

Sharp India Ltd

Sharp India Ltd was incorporated in 1985 as Kalyani Telecommunications and Electronics Pvt Ltd, the company was converted into a public limited company in the same year. The name was changed to Kalyani Sharp India in 1986. The company was entered into a joint venture with Sharp Corporation, Japan - a leading manufacturer of consumer electronic products to manufacture VCRs/VCPs/VTDMs. The company manufactures consumer electronic goods such as TVs, VCRs, VCPs and audio products. The products were sold under the Optonica brand name. Sharp has a production base in 26 countries with 33 plants, and its products are used in 133 countries. The company was accredited with the ISO-9001 certification in the month of February, 2001.

Hitachi India

Hitachi India Ltd (HIL) was established in June 1998 and engaged in marketing and sells a wide range of products ranging from Power and Industrial Systems, Industrial Components & Equipment, Air Conditioning & Refrigeration Equipment to

International Procurement of software, materials and components. Some of HIL's product range includes Semiconductors and Display Components. It also supports the sale of Plasma TVs, LCD TVs, LCD Projectors, Smart Boards and DVD Camcorders.

3. POLICY AND INITIATIVES

Foreign investment up to 100 per cent is possible in the Indian consumer electronics industry to set up units exclusively for exports. It is now possible to import duty-free all components and raw materials, manufacture products and export it.

EHTP (Electronic Hardware Technology Park) is an initiative to provide benefits to companies that are replacing certain imports with local manufacturing. EHTP benefits include export credits, no duties on imported components or capital equipment, business tax incentives, and an expedited import-export process.

The government, in an attempt to encourage manufacture of electronics in India has changed the tariff structure significantly.

Customs duty on Information Technology Agreement (ITA-1) items (217 items) has been abolished from March 2005. All goods required in the manufacture of ITA-1 items are exempt from customs duty.

Customs duty on specified raw materials / inputs used for manufacture of electronic components or optical fibres / cables has been removed. Customs duty on specified capital goods used for manufacture of electronic goods has been abolished.

Excise duty on computers has been removed. Microprocessors, hard disc drives, floppy disc drives and CD ROM drives continue to be exempt from excise duty.

3.1 Intellectual Property Rights

Protection of Intellectual property rights (IPR) is a prime requisite for development of R&D and innovation in the consumer electronics sector. The Government of India has developed a robust IP act to facilitate innovation, growth and development.

Several amendments to the Copyright Act, creation of a new Trademark Act, a new Designs Act and amendments to the Patents Act show India's continued effort to protect IPR.

The country has already made several changes in its IP acts over the years.. Several amendments to the Copyright Act, creation of a new Trademark Act, a new Designs Act and amendments to the Patents Act show India's desire to change and adapt. New acts have also been enacted to cover semiconductors and layout designs which will be of considerable importance to the electronic industry.

In the current WTO regime, India is a party to the "Trade Related Aspects of the Intellectual Properties (TRIPs) Agreement" and has accordingly, amended most of its IPR Acts and Rules to conform to the said Agreement. The Indian Copyright Act 1957 was amended in 1999; the patent Act 1970 was amended in 1999 & 2003 and Trademarks and Merchandise Marks Act 1959 was overtaken by a new Trademark Act 1999. The Industrial Design Act 1911 was effectively replaced by The Design Act 2000, and the Layout Design of Semiconductor integrated Circuit Act 2000 was enacted.

The agreement on TRIPs takes care of the intellectual property rights by enforcing the patent rights, copy rights and related rights, and the protection of industrial designs, trade marks, geographical indications, layout designs of integrated circuits and undisclosed information. Accordingly, the member nations are asked to modify their existing laws. Once these laws come into force, unauthorised use of the patented innovations, trade marks, etc. becomes difficult. Enforcement of the TRIPs agreement makes the production of any product possible either through internal innovation or through formal transfer of technologies.

The consumer electronics and durables sector is expected to continue to benefit from supportive policies and become globally competitive.

3.2 Regulations

3.2.1 Free Trade Agreement

WTO regime which came in force in 2005, results in zero customs duty on imports of all telecom equipment. 217 IT/electronic items were covered under the Information Technology Agreement (ITA) of the WTO for complete customs tariff elimination by 2005.

Out of these 217 items, several items were already at NIL customs duty. In fact, IT/electronics was the first sector in India to face complete customs tariff elimination. The ITA-1 would result in intensifying competition as more imported products will be easily available at lower prices.

3.2.2 Foreign Investment Policy: FDI

Foreign investment up to 100 per cent is allowed in Indian electronics industry set up exclusively for exports. The units set up under these programmes are bonded factories liable to import, free of duty, their entire requirements of capital goods, raw materials and components, spares and consumables, office equipment etc. Deemed export benefits are available to suppliers of these goods from the Domestic Tariff Area (DTA).

A part of the production from such units is permitted to be sold in the DTA depending upon the level of the value addition achieved. The FDI approval for electrical equipment (including computer software and electronics) from January 1991 to March 2004 was US\$ 7.29 billion, which was 9.94 per cent of the total foreign direct investment (FDI) approved. During the same period the FDI inflow for electrical equipment (including computer software and electronics) was US\$ 3.32 billion.

3.2.3 Procedure for approval

Once the investment in equity has been approved, the import of capital goods, components and raw materials or the engagement of foreign technicians for short duration does not require any additional approvals.

Approval of Ministry of Home Affairs is not needed for hiring foreign nationals holding valid employment visa.

Approval for setting up units in Export Processing Zones (EPZs) is given by the Board of Approvals in the Ministry of Commerce.

Approval for setting up export-oriented units (EOUs) outside the zones is given by the Ministry of Industry.

Approvals for setting up Electronic Hardware Technology Park (EHTP) and Software Technology Park (STP) units are cleared by the Inter Ministerial Standing Committee (IMSC) set-up under the Chairmanship of the Secretary, Department of Information Technology.

Proposals involving foreign direct investment not covered under the automatic route are considered by the Foreign Investment Promotion Board (FIPB).

3.2.4 FDI/ Foreign Technology Collaboration Agreement

The government facilitates FDI and investment from Non- Resident Indians (NRIs) including Overseas Corporate Bodies (OCBs), predominantly owned by them, to complement and supplement domestic investment. Foreign technology induction is encouraged through FDI and foreign technology collaboration agreements. FDI and foreign technology collaborations are approved through automatic route by the Reserve Bank of India

4 OPPORTUNITIES AND CHALLENGES

4.1 The Challenges

Heavy taxation in the country is one of the challenges for the players. At its present structure the total tax incidence in India even now stands at around 25-30 per cent, whereas the corresponding tariffs in other Asian countries are between 7 and 17 per cent.

About 65 per cent of Indian population that lives in its villages still remains relevant for some consumer durables companies. This India, at least a large proportion of its constituents, still buys black and white TVs and doesn't know what flat screens are.

Also, foraying into these rural markets has a considerable cost component attached to it. Companies not only have to set up the basic infrastructure in terms of office space, manpower, but also spend on transportation for moving inventory. Even LG and Samsung, which are touted as having the largest distribution network in the country, have a direct presence only in 15,000 to 18,000 of the around 40,000 retail outlets (for consumer durables) in the country.

Poor infrastructure is another reason that seems to have held back the industry. Regular power supply is imperative for any consumer electronics product. But that remains a major hiccup in India.

4.2 And the opportunities...

The rising rate of growth of GDP, rising purchasing power of people with higher propensity to consume with preference for sophisticated brands would provide constant impetus to growth of white goods industry segment.

Penetration of consumer durables would be deeper in rural India if banks and financial institutions come out with liberal incentive schemes for the white goods industry segment, growth in disposable income, improving lifestyles, power availability, low running cost, and rise in temperatures.

While the consumer durables market is facing a slowdown due to saturation in the urban market, rural consumers should be provided with easily payable consumer finance schemes and basic services, after sales services to suit the infrastructure and the existing amenities like electricity, voltage etc.

Currently, rural consumers purchase their durables from the nearest towns, leading to increased expenses due to transportation. Purchase necessarily done only during the harvest, festive and wedding seasons — April to June and October to November in North India and October to February in the South, believed to be months 'good for buying', should be converted to routine regular feature from the seasonal character.

Rural India that accounts for nearly 70% of the total number of households, has a 2% penetration in case of refrigerators and 0.5% for washing machines, offers plenty of scope and opportunities for the white goods industry. The urban consumer durable market for products including TV is growing annually by 7 to 10 % whereas the rural market is zooming ahead at around 25 % annually. According to survey made by industry, the rural market is growing faster than the urban India now. The urban market is a replacement and up gradation market now.

The increasing popularity of easily available consumer loans and the expansion of hire purchase schemes will give a moral boost to the price-sensitive consumers. The attractive schemes of financial institutions and commercial banks are increasingly becoming suitable for the consumer. Consumer goods companies are themselves coming out with attractive financing schemes to consumers through their extensive dealer network. This has a direct bearing on future demand.

The other factor for surging demand for consumer goods is the phenomenal growth of media in India. The flurry of television channels and the rising penetration of cinemas will continue to spread awareness of products in the remotest of markets.

The vigorous marketing efforts being made by the domestic majors will help the industry. The Internet being now used by the market functionaries that will lead to intelligence sales of the products. It will help to sustain the demand boom witnessed recently in this sector. The ability of imports to compete is set to rise. However, the effective duty protection is still quite high at about 35-40 per cent. So, a flood of imports is unlikely and would be rather need based.

Reduction in import duties may significantly lower prices of products such as microwave ovens, whose market size is quite small in India. Otherwise, local manufacturing will continue to stay competitive. At the same time, there will be some positive benefits in the form of reduction in input costs. Washing machines and refrigerators will also benefit from lower input costs.
