MANAGEMENT DISCUSSION AND ANALYSIS

(Within the limits set by the Company's competitive position)

Your company is ranked among the worlds' top 20 Tyre Manufacturers and 2018 marks the year where the company begins to consolidate its 4th decade of leadership in the Indian Tyre industry.

The past year was eventful and turbulent in equal measure. The global economy gathered steam and accelerated from 3.2% in 2016 to 3.6% growth in 2017. However, geo-political headwinds, looming trade walls and issues like mass migration continue to be of concern. Further, increasingly shrill protectionist economic and nationalist agendas witnessed in North America and Europe are taking more concrete shape. China's swift response to United States of America over punitive tariff hikes has raised the possibility of a full-blown global trade war which could jeopardize the budding global economic recovery.

India is the proverbial bright spot in the context of this tumultuous backdrop as it continues to remain one of the most favourable economies in the world for growth and investment opportunities.

The discussion below summarises the key issues and challenges that faced your company in the year ended 31st March, 2018.

Market & Industry Overview

The first quarter of 2017-18 saw the impact of demonetisation settling down. In the next quarter, introduction of the landmark Goods and Services Tax (GST) brought in some uncertainties as businesses adjusted to the new regime. However, a good monsoon resulted in a healthy upswing in the agrarian economy and stoked a recovery in rural demand.

Sizeable state spending on infrastructure reaffirmed the government's commitment towards supporting long-term growth and firing up economic activity that was adversely impacted by major policy initiatives.

After registering GDP growth of over 7% for the third year in succession in 2016-17, the Indian economy registered somewhat slower growth, estimated to be 6.5% in 2017-18 on an annualized basis, though growth rates in the last quarter are expected to be around 7.5% per annum.

As expected, the Union Budget 2018 witnessed significant push for rejuvenating the rural economy and improving economic development through better infrastructure and connectivity. This has widened the fiscal deficit for the current fiscal to 3.5% of GDP, instead of the projected 3.2%. The gap was also partly due to lower than anticipated GST collections from the states.

The year also witnessed a slew of measures being undertaken towards the resolution of problems associated with non-performing assets of the banks, further liberalization of Foreign Direct Investment (FDI), thus strengthening the momentum of reforms. With inflation expectations adjusted down, there could be room for further interest rate cuts if inflation durably remains below 4%. However, the clear and ever present danger of hardening fuel and raw material prices could shore up inflationary pressures.

The complex filing procedures of GST and delay in refund of input credits, had its impact on exporters and small and medium enterprises, forcing companies to bring down production and stocks, leading to a decline in manufacturing activity in the short term. However, once these transient factors receded, the economy picked up momentum and is expected to grow at a steady rate in the near to medium term.

The Indian tyre industry is estimated to be approximately ₹60,000 crores in 2017-2018 and the top eleven tyre companies' account for more than 90% of the volume. The industry caters to Original Equipment Manufacturers (OEM), Export and Replacement markets mainly through four vehicle categories namely Commercial Vehicle (CV) including Truck and Buses (T&B), Passenger Vehicles (PV), Two-Wheeler and others including Tractors and Off The Road (OTR).

Of these three distinct markets, Replacement accounts for approximately 60% of the Industry with Institutional/OEM and Exports making up 22% and 18% respectively. While in the Commercial and Farm segments, replacement sales form a major chunk, both Institutional/OEM and Replacement sales play an almost equal role in the Passenger segment.

Traditionally, tyres are classified as Cross-ply (Bias) and Radial based on the technology deployed in their manufacture. In India, the commercial tyre segment continues to be dominated by cross-ply tyres due to road conditions, loading patterns and the high initial cost of Radials. While India's passenger car segment is fully radialized, radialization in the T&B segment has increased from 36% in financial year 2016 and now stands at 40%.

The Indian automotive sector clocked 14% growth in fiscal 2017-18, buoyed by healthy volume growth across segments. This was creditable as it was achieved in the face of market disruptions, teething troubles in GST roll-out and ambitious targets for changeover on emission norms.

By 2020, India's share in the global passenger vehicle market is estimated to touch 8% from 2.40% in 2015. With many players jostling for space in the over-crowded mini car and compact sedan segments, the compact SUV segment emerged as a bright spot. The trend in new purchases showed the growing clout of SUVs and compact SUVs as they powered the overall growth in the passenger vehicles segment which crossed the 3-million sales mark for the second year in a row.

India is now the world's biggest two-wheeler market with annual domestic sales of over 18 million units. Growth in the two-wheeler industry is being powered by Scooters which grew at 20% plus in financial year 2018. The next wave of 'scooterisation' is slated to come from the rural and semi-urban pockets, which have typically been the bedrock of the motorcycle customer base.

The expected stable growth in the passenger vehicle segment coupled with strong performance of the two-wheeler and SUV segments had a cascading effect on the overall tyre demand for personal vehicles.

The domestic tyre sales for financial year 2018 grew on the back of traction in OEM volumes, pick-up in replacement demand and the positive impact of Anti-Dumping Duty (ADD) imposition on Chinese TBR in September 2017.

The government's push towards infrastructure development, restriction on overloading of trucks, road construction and mining activities have given a fresh fillip to demand in the Medium & Heavy Commercial Vehicle [M&HCV] segment which cruised to a strong position during the current fiscal. Commercial vehicle manufacturers have recorded robust 19.94% year on year growth, accruing across both the M&HCV and Light Comercial Vehicle [LCV] sub-segments. The Tipper segment, which is directly linked to the demand for tyres across Earthmoving and Construction equipment categories, grew over 58 per cent over the same period last year as a direct fall-out of increased road construction activity.

A bumper agrarian output riding on two consecutive normal monsoons coupled with increased haulage demand for tractors, as a fall-out of stepped up investments in infrastructure, aided by government support, has given an overall fillip to the demand for Tractors. Consequently, the volumes of the domestic tractor industry scaled record highs with 20% plus volume growth in financial year 2018 on the back of improved sentiment and buoyant demand. This translated into a positive multiplier effect on the demand for Farm and Off-The-Road (OTR) tyres.

Overall, the domestic tyre volume growth is pegged at a strong 8-10 per cent. Of this, the Original Equipment Manufacturer is likely to mirror the overall trend with growth in the region of 8-10 per cent and Replacement demand is expected to post 6-8 per cent growth.

The Anti-Dumping Duty provided a level playing field for domestic tyre companies who had suffered on account of the predatory pricing of Chinese imports and were consequently not running to full capacity.

Given the healthy growth of demand in the industry across segments, capacity addition will continue to dominate the narrative in the industry given the large cash balances, strong accrual position and favourable demand scenario.

The competitive intensity in the industry continues to remain at fever-pitch with expected 'on-streaming' of several greenfield and brownfield capacities by domestic as well as international players. Tyre manufacturers in India have been actively involved in Research & Development and a range of products suited to the Indian market will continue to be launched and aggressively marketed.

Opportunities and Threats

The growth outlook for the auto industry continues to remain strong in financial year 2019. Apart from new vehicles, the pre-owned (used) car market has had relatively steady growth. Shortening ownership cycles of new cars, participation of organized players which is bringing in credibility and consumer confidence and access to financing are factors fuelling the growth and acceptance of the used-car market. As the industry grows and evolves structurally, it is expected to have a positive impact on the tyre sector.

A third consecutive normal monsoon forecast augurs well for the rural economy and more specifically, the Original Equipment & Replacement demand for Farm Tyres and Two Wheelers in the near term.

Unprecedented change and technological disruptions are the order of the day for the Auto industry and the Tyre Industry cannot be unaffected by these. Financial year 2018 started off with a mandatory, nationwide implementation of Bharat Stage (BS)-IV norms which required automakers to comply with cleaner emission norms.

The government's decision to leapfrog to the toughest emission standards of BS-VI from the current BS-IV by 2020, is a game-changer for both Original Equipment Manufacturers and tyre manufacturers who need to demonstrate agility in adapting to a volatile market situation. An over-crowded market, stringent regulations and the increased investment in both cost and technological compliance with the new emission standards is likely to pose a major challenge.

Further, cost of ownership, and therefore fuel economy, continues to be one of the highest priorities in vehicle purchase decisions in India. Therefore, consumers advancing their purchases on the expectation of higher outlay post-2020, would impact Original Equipment & Replacement demand.

In addition, the recent changes in the proposed scrappage policy (coinciding with BS-VI roll-out in April 2020), will significantly reduce the potential population of vehicles eligible for scrappage (20 plus years as opposed to 15 years earlier).

In comparison to developed countries, Natural Rubber dominates the raw material palette of the Indian tyre industry, and in this context, the gap between domestic rubber production and demand will continue to remain a concern area. During financial year 2018, tyre companies had to face a triple whammy of high input costs, namely those of natural rubber, carbon black and crude oil and this may continue to be the case in the foreseeable future too.

Segment wise and Product wise Performance

During fiscal 2017-18, your company achieved a total income of ₹ 15510 crore. Across the board, there was an overall increase in all segments adding up to a 8% increase in total tyre production. In the Heavy Commercial Vehicle segment, the increase was 5% over the previous year while Light Commercial Vehicle tyres increased by around 4%. The Small Commercial Vehicle tyres grew by a marginal 2% in the 4-wheeled segment, while it rose by 3% in the 3-wheeled segment, over the previous year. Passenger & SUV showed a 7% growth. The Farm segment grew at 4%. The Motorcycle and Scooter segments rose by 10% and 13% respectively. The OTR segment grew at 2%.

Exports

India's external sector proved to be resilient to the volatility in the global environment. This was reflected in external debt remaining low and substantial increase in foreign exchange reserves, thereby cushioning against vulnerabilities.

In first half of financial year 2018, export growth decelerated, however in the second half of financial year 2018, the economy witnessed robust signs of revival as the shocks began to fade and the synchronous global economic recovery boosted exports.

Reflecting this trend, tyre exports remained strong for the second straight year, led by revival in demand across product segments. Following a 27.5 per cent growth in financial year 2017, exports volume increased by 10 per cent during financial year 2018.

Overall your company's export turnover stood at ₹1353 crore as compared to the previous year turnover of ₹1316 crore.

Over the past year, we have undertaken several initiatives to stabilize our strong markets and broaden our reach outside India. Most of the exports have been to top 15 destinations which include the US, Europe, Australia, Latin America, Middle East among others. These countries contribute close to 65% of the total exports. We are coming out with market specific products and price-solutions to be able to reach out to the end-consumer across geographies. ASEAN, SAARC and Middle Eastern countries continue to be key destinations and drivers of export growth.

The outlook for the coming years is expected to be favourable, with tyre export volumes projected to grow by about 8-10% compounded annual growth rate (CAGR) during financial years 2019-22 riding on bullish demand prospects (despite strict import regulations in a few countries). There has been increased acceptance of Indian tyres in overseas markets, both in terms of quality and pricing. However, Chinese brands will continue to play their predatory pricing game in all overseas markets and this will remain a key challenge that Indian tyre manufacturers will have to contend with apart from spiralling crude oil prices, geo-political and diplomatic tensions particularly in the Middle East.

Discussion on Financial Performance with respect to Operational Performance

(₹ Crores)

	2017-2018	2016-2017
Revenue from operations	15227	14749
Other Income	283	329
Total Income	15510	15078
Profit before tax	1602	2066
Provision for tax	510	615
Profit after tax	1092	1451

The revenue from operations of the Company for the Current year stood at ₹ 15227 Crore against ₹ 14749 Crore for the previous year ended 31st March, 2017. During the current year ended 31st March, 2018, the Earnings Before Interest and Depreciation (EBIDTA) stood at ₹ 2552 Crore as against ₹ 2921 Crore in the previous year ended 31st March, 2017. After providing for Depreciation and Interest, the Profit Before Tax for the year ended 31st March, 2018 is ₹1602 Crore as compared to ₹ 2066 Crore in the previous year ended 31st March, 2017. After making provision for Income Tax, the Net Profit for the year ended 31 March, 2018 is ₹ 1092 Crore, as compared to ₹ 1451 Crore in the previous year ended 31st March, 2017.

The prices of Natural Rubber and Crude linked derivatives which continued to rise in the last quarter of previous year, remained high during the 1st quarter of 2017-18 and thereafter the prices stabilised to reasonable levels.

Due to introduction of GST, several Central and State Taxes / Levies, is subsumed into a single tax structure. The Company successfully implemented GST across all applicable locations.

Outlook

As global economic activity continues to strengthen, global growth is forecast to grow by 3.9% during 2018. Closer home, a cyclical economic recovery has taken strong hold with growth benefitting from higher public capital spending and recovering private business sentiment. GST promises to deliver positive outcomes as India becomes an integrated and more competitive market.

Industrial growth accelerated sharply during the second quarter of financial year 2018 and jumped to 6.9% from 1.5% in the previous quarter, on account of a stellar turnaround by manufacturing and construction – both of which are the mainstay of economic activity and directly linked with the fortunes of the tyre industry leading to robust growth in demand from the OEM and replacement markets.

A favourable economic outlook, expectation of greater stability in GST, likely recovery in investment levels and ongoing structural reforms, are a harbinger of higher growth (barring any unprecedented global events which could have a dampening effect on GDP growth).

Reflecting this broad-based revival, for financial year 2019, the domestic tyre volume growth is pegged at 8-8.5 per cent as the demand environment continues to be favourable despite the grim input cost scenario.

The auto industry maintains an optimistic view regarding the domestic sales volume growth of both the Commercial and Personal Vehicles in financial year 2019. In fact, certain segments like utility vehicles and scooters are expected to maintain double-digit growth in the coming fiscal.

Tyre companies are therefore expected to reap the benefits of the buoyant growth prospects for Auto OEMs, and consequently, in time, replacement demand will also be robust, given the steady growth in vehicle population that will be due for replacement in the years to come.

Internal Control Systems and their Adequacy

The company has adequate internal control systems in place, commensurate with the size and nature of business. The Company has in place well-documented procedures, covering various financial and operational functions. Company through its own Internal Audit Department carry out periodical Audits at various locations and functions based on the plan as approved by the Audit Committee. Some of the salient features of the internal control systems are:

(i) A robust ERP system connecting all Plants, Sales Offices and Head office.

(ii) Systems and procedures are periodically reviewed to keep pace with the growing size and complexity of company's operations.

(iii) Preparation of annual budget for operations and services and monitoring the same against the actuals at periodic intervals .

(iv) All assets are properly recorded and system put in place to safeguard against any losses or unauthorized use or disposal.

(v) Periodic physical verification of fixed assets and all inventories.

(vi) Observations arising out of the Internal Audit are reviewed at the Audit Committee meeting and follow up action taken.

(vii) Periodic presentations made to the Audit Committee on various operations and financial risks faced by the company and action proposed to mitigate such risks.

Risks and Concerns

In the last quarter of previous year, we have witnessed a sharp price increase in certain crude linked raw-material and this trend of volatility in the raw material prices could continue in future.

Human Resources

Your Company owes its success and dominance in the industry to its Human Resource, their hard work and dedication in overcoming all hurdles, facing the daunting challenges of the market and meeting ever increasing as well as changing expectations of the customers across the length and breadth of the country, as well as overseas.

Your Company continues to constantly give thrust and focus on Human Resource for its prolonged success. From hiring the best possible fit for the organization, developing them to become astute professionals in their respective field and retaining them by offering a unique value.

We hired both, lateral and fresher, candidates with a special focus on campus engagement this year. We acquired some of the top talent from premier engineering and management institutes to build our leadership pipeline. We also attracted talent from other leading organizations with competitive offerings.

While we welcomed new members, focus continued on existing employees, identifying their growth needs and intensively developing them for handling critical positions in near future thus creating a secure and rewarding ambience for existing base to continue giving their best.

Learning and Development department worked tirelessly in designing and delivering training programs that are very need-specific and aids in imparting knowledge seamlessly with a special attention on training effectiveness, measurement and return of investment (ROI).

We also kept our commitment of shaping the future of our plants by imparting team building and collaboration training to our workmen, leadership training for Union leaders and opinion makers.

Cordial and harmonious industrial relations were maintained across all our manufacturing units through various employee/workmen engagement initiatives with parallel improvement of work culture, productivity and quality of life of the workforce.

The total employee strength as on 31st March, 2018 was 15810.

Cautionary Statement

Statements in the Management Discussion and Analysis describing the Company's objectives, expectations or forecast may be forward looking within the meaning of applicable laws and regulations. Actual results may differ materially from those expressed in the statement. Important factors that could influence the Company's operations include global and domestic supply and demand conditions affecting selling prices of finished goods, input availability and prices, changes in government regulations, tax laws, economic developments within the country and other factors such as litigation and industrial relations.