Analyst Note

Autofacts®

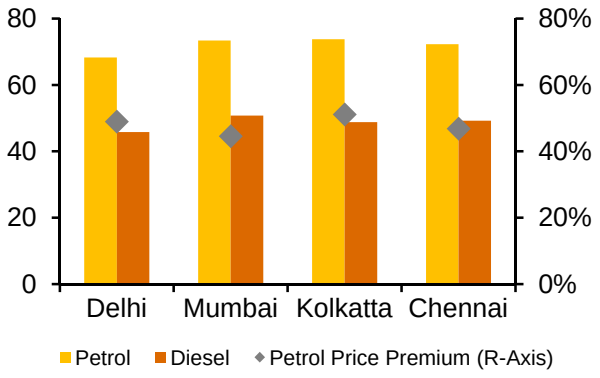
February 2012

India: The Effects of Fuel Subsidies

Policy reform underpins fuel duel

Outside of Europe, India is one of the most prominent markets for diesel powered light vehicles and this eminence is the result of long-standing policy support. But, with pressure to remove fuel price controls mounting, India's automotive sector is approaching a pivotal crossroads.

India: Retail Price of Transportation Fuel
2012YTD (rupees per litre*) *Exchange Rate: $1 = Rs49.06



Policy background

To shield the Indian economy and consumers from the adverse impacts of international oil market volatility, the government regulated consumer prices for four sensitive petroleum products: petrol, diesel, domestic liquid petroleum gas (LPG) and kerosene. Roughly $17 billion in annual fuel subsidies relied on financial support from public sector companies by way of price discounts and government oil bond issuances.

Petrol deregulation gives rise to diesel

Given significant price imbalances and rising global oil prices, the government announced revisions to national fuel policy in mid-2010 beginning with petrol, which was implemented a year later. Deregulation increased the differential between petrol and diesel, thereby shifting consumers further toward diesel powered vehicles. With diesel subsidised by ~9 rupees per litre below cost in late 2011 (resulting in diesel prices roughly two-thirds that of petrol), some manufacturers struggled to meet consumer demand for diesels and others have discontinued petrol engine options on certain models.

Recognizing this market disturbance and the heavy expense of diesel subsidies, the government is debating diesel deregulation/taxation in its forthcoming annual budget. As a result, future automotive investment decisions are being clouded and further complicated by the adoption of LPG and compressed natural gas (CNG) vehicles, evidenced by New Delhi and Mumbai's transport and taxi fleets. Regardless of the ultimate policy action, India's skewed fuel demand patterns will likely be subject to change.

Developing a long-term market view

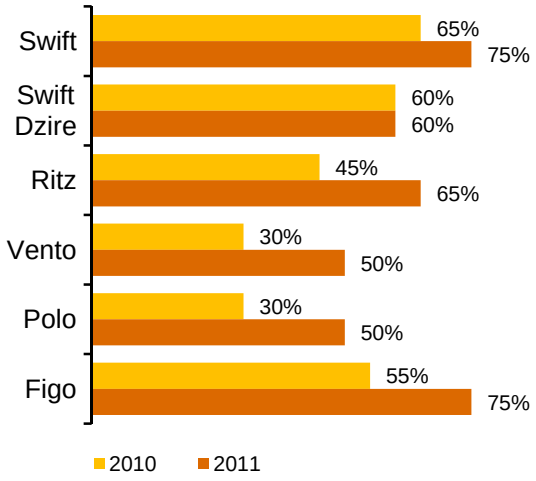
Although the current situation has brought near-term uncertainty to India's automotive operating environment, Autofacts' expectation that India's light vehicle market will increase from 2.8 million in 2011 to 6.5 million by 2018, emphasises the importance of long-term strategic planning. At 2018's forecasted market level, the difference between a diesel penetration level of 50% (an extrapolation of the current trajectory) or 30% (its former level), is 1.3 million units. Such a margin is a powerful lever on investment related to product planning, technology development, supply chain management, export capacity, and/or infrastructure. This dynamic illustrates the profound influence that government policy has on the fundamentals of automotive sector growth.

pwc

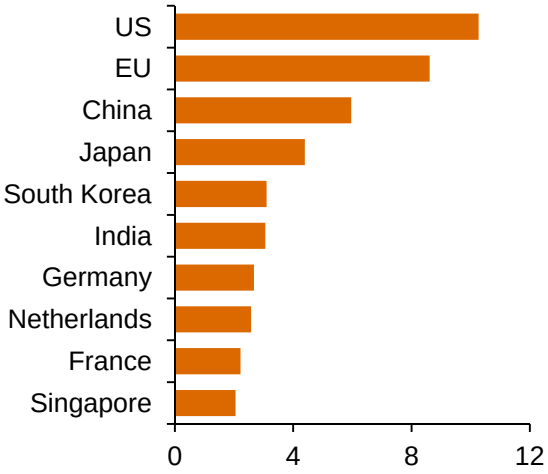
Analyst Note

India spent nearly $16.7 billion on subsidising all petroleum products during FY2011 (Apr 2010 – Mar 2011). Petrol price deregulation was implemented in June 2011, bringing estimated subsidy spending down to ~$11.5 billion for FY2012 (Apr 2011 – Mar 2012), while diesel deregulation has been postponed.

India: Diesel Share of Sales
2010 vs. 2011 (select models)



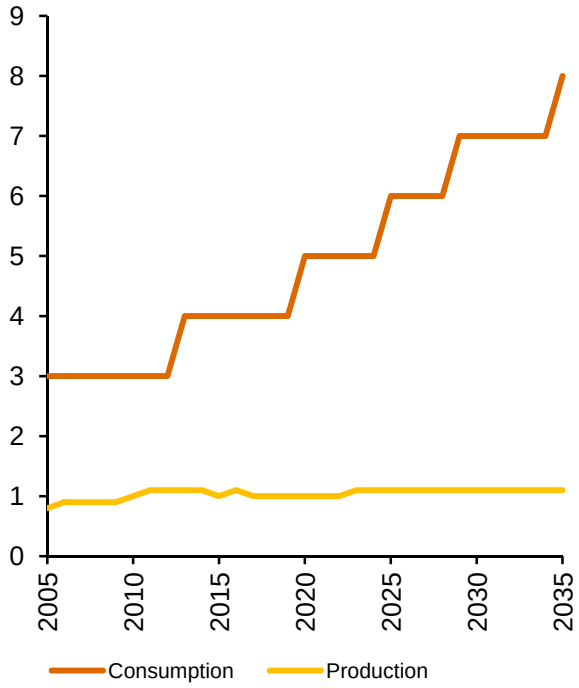
Global: Crude Oil Imports
2011 (millions of barrels per day)



India: Average Fuel Consumption by Vehicle Class
2012 (rupees per litre)

Type of Vehicle	Average Distance covered annually (KM)	Fuel Efficiency (KM/Litre)	Litres/ Vehicle/ Year	Monthly Fuel Cost at price on 7.2.12 in Delhi (rupees)
Two-Wheelers (Petrol)	6,300	73.0	86	5,870
Three-Wheelers (Petrol)	35,000	34.0	1029	70,240
Cars (Petrol & Diesel)	8,000	13.5 (P) 14.0 (D)	593 (P) 571 (D)	40,478 (P) 26,163 (D)
MPV (Diesel)	7,800	8.7	897	41,100
Bus (Diesel)	55,000	4.1	13,415	614,675
Heavy Trucks (Diesel)	55,000	3.6	15,278	700,038
Light Trucks (Diesel)	20,000	4.5	4,415	202,295

India: Oil Consumption & Production Forecast
2005 – 2035(f) (millions of barrels per day)



Source: Autofacts, Industry Estimates, CIA Factbook, Lawrence Berkeley National Laboratory, USA, EIA Energy Outlook 2011

For information regarding our products and services please visit us at www.autofacts.com