

Rating criteria for the tractor industry

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Executive Summary

The products of India's tractor industry range predominantly from 10 to 50 horse power (HP); they are thus distinct from tractors and farm equipment worldwide. The Indian tractor industry is dominated by domestic players, who are price competitive. Sales are largely driven by bank credit. Factors such as government policy on agriculture, National Bank for Agriculture and Rural Development (NABARD) policies to promote farm mechanisation and bank credit extended towards the agricultural sector (primarily for tractor financing) play an important role in influencing the demand for tractors. The demand to use tractors for haulage activities has also been increasing.

CRISIL's approach to rate tractor manufacturers involves evaluating their business, management, and financial risk profiles. The key parameters include the company's market position and operating efficiency. Market position assessment focuses on the company's product profile, its geographical reach, the demand pattern, and the level of competition. While exploring operating efficiency, a company's cost structure is examined. CRISIL also assesses the financial and management risk parameters to arrive at the final rating.

Scope

While the criteria for the broader category of manufacturing companies¹ also apply to tractor manufacturers, this article² details the industry-specific factors impacting the credit risk profiles of these companies.

Business Risk

Market position

Product profile

There are broadly four product categories within the tractor industry based on power delivered by HP: tractors delivering below 30 HP, those delivering 30-40 HP and 40-50 HP, and those delivering above 50 HP. The bulk volumes are in the 30-to-50 HP range. The growth rate and prospects of each product category are different from others. CRISIL assesses the product profile of the company to estimate its likely growth rates.

Geographical coverage

Assessing the company's geographical reach is vital because each region in the country exhibits its own sales patterns (in terms of volumes) and growth potential depending on the region's product requirement and soil patterns. The company's export initiatives and its success and growth prospects in the export market are also studied.

¹ The detailed criteria is on the CRISIL website under the 'Criteria and Methodology' section—Rating Criteria for Manufacturing and Service Sector Companies and CRISIL's Approach to Financial Ratios.

² To access the previous published document on "Rating Criteria for Tractor Industry" Kindly follow below mentioned link: https://www.crisil.com/content/dam/crisil/criteria_methodology/industrials/archive/CRISIL-Ratings-criteria-tractor-industry_2013.pdf

Level of monsoons

Rainfall levels, both country-wide and region-wise, are vital because they have a direct impact on sales volumes in the tractor industry.

Demand-supply equations

The demand for tractors is influenced by government policies pertaining to duties (mainly excise duties) and changes in diesel prices; other factors include government policy on agriculture, NABARD policies to promote farm mechanisation and bank credit extended towards tractor. CRISIL also evaluates the product categories within which the players have expanded capacities, and their future competitive positions.

Competition

Studying the market segments in which the company is present, its position in each, the inherent competition, and likely changes in the market position helps analyse the company's present and expected competitive status.

Distribution network

The reach of a distribution network, the support it extends to the company, exclusivity of the services it provides, and the credit periods involved are important factors that contribute to healthy sales

Operating efficiency

Location

Proximity to major vendors, ancillaries and important markets lends a competitive edge to players.

Capacity utilisation and flexibility in manufacturing

The flexibility of a company to switch between different product profiles along with optimum capacity utilisation help determine the versatility in operations.

Level of integration

Fully integrated operations ensure sustainability of supplies at various stages of the production chain and provide reasonable control on the cost structure and product quality.

Ancillary and vendor network

The network's strength can be understood from the available capacities, ability to deliver high-quality products on time, and the ability to upgrade/change with the changing basic models.

Raw material

Raw material requirement is examined from the perspective of availability and price movements, to understand the cost structure. CRISIL also assesses the import content and vendors of the company.

Channel inventory levels

This helps assess the actual retail demand and the impact of carrying costs on the manufacturer.

Technology and product development

The company's ability to launch new models/upgrades with varying performance characteristics (for power and fuel efficiency) is an important constituent in the analysis. As most tractor manufacturers do not have foreign collaborations, they tend to outsource the manufacture of both, components and aggregates. A company's product development efforts are calculated to evaluate the new features, market segments addressed, and price-cost issues involved.

Productivity and quality issues

Productivity and labour relations are integral to the business because they determine steady revenue flow and uninterrupted supply. Consistency and improvement in quality are also assessed from both the usability and costing angles.

Financial Risk

In this regard, CRISIL follows the standard criteria used for all manufacturing companies (please refer to the criteria detailed in our publication, '*Rating Criteria for Manufacturing and Services Sector Companies*' and '*CRISIL's Approach to Financial Ratios*').

Management risk

CRISIL follows the standard criteria used for all manufacturing companies in its analysis of management risk for tractor manufacturers (please refer to our detailed criteria document, '*Rating Criteria for Manufacturing and Services Sector companies*').

Conclusion

Thus, in CRISIL's opinion, the key success factors for players in the tractor sector include:

- Presence in high growth segments
- Geographical reach including export initiatives
- Inventory management

Product development and consistency in quality

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