Performance Appraisal of Automobiles Industry in India (A Case Study of Honda Cars India Ltd.)

Nidhi Agarwal
Assistant Professor
Deptt. School of Management
Babu Banarasi Das University, Lucknow

Abstract

On the canvas of the Indian economy, automobile industry occupies a prominent place. This sector has witnessed tremendous growth during the last two decades. Automobile Industry was delicensed in July 1991 with the announcement of the New Industrial Policy. The Indian automobile industry, comprising two-wheelers, three-wheelers, commercial vehicles and passenger vehicles, is the seventh-largest in the world. The study focuses on the performance appraisal of Honda Cars India Ltd. Performance appraisal is the process of determining the operating characteristics of a firm from accounting and financial statements. Honda Cars India Limited is a subsidiary of the Honda Motor Company Limited of Japan, for the production, marketing and export of passenger cars in India. Performance Appraisal of Honda Cars India Ltd. has been studied by efficiency analysis and profitability analysis. Managerial efficiency of the company lies in making optimum utilisation of the assets of the companies. Managerial efficiency ratios are concerned with measuring the efficiency with which asset is managed i.e. the speed and rapidity with which assets are converted into sales. The greater is the rate of turnover or conversion, the more efficient is the utilization or management of the asset. These ratios are usually calculated with reference to sales/cost of goods sold and are expressed in terms of rate or times. Profitability ratios measure the profit earning capacity or the operational efficiency of the company. A lack of profit may arise due to poor sales, lack of control over the expenses. The profitability ratios are the relative measurement which can be determined on the basis of either sales or investment.

Keywords: Automobile Industry, Performance Appraisal, Honda cars India Limited, Efficiency Analysis and Profitability Analysis.

Introduction

Automobile industry is the key driver of any growing economy and plays a pivotal role in country's rapid economic and industrial development. Due to its deep forward and backward linkages with several key segments of the economy; automobile industry has a strong multiplier effect and is capable of being the driver of economic growth. The Indian automobile industry has made rapid strides since delicensing and opening up of the sector in 1991. The passenger car industry was, however, delicensed in 1993. The industry contributes ~22% of India's manufacturing GDP (Gross Domestic Product) and ~7% of India's overall GDP. The Indian automobile industry provides direct employment to 1 million people and indirect employment to 18 million people in the country. The Indian automobile industry, comprising passenger cars, two-wheelers, three-wheelers and commercial vehicles, is the seventh-largest in the world with an annual production of 20.4 million vehicles, of which 2.9 million are exported. Two-wheelers, being the most popular means of personal transport, alone account for about 75% of the total automobile production in India, while passenger vehicles account for nearly 16% of the production. However, owing to their lower sales realisations, two wheelers account for only around 32% of the sales in terms of value while passenger vehicles account for around 62% of the same. Commercial vehicles are categorised into heavy, medium and light. They account for about 5% of the market. Three wheelers are categorised into passenger carriers and goods carriers. Three wheelers account for about 4% of the market in India. The passenger vehicles are further categorised into passenger cars, utility vehicles and multi-purpose vehicles. In the passenger car segment, India is mainly a small car market though mid size and big car sale is continuously rising in recent years.

The major Indian companies present in the automobiles market include Tata Motors, Maruti Suzuki India, Mahindra & Mahindra, Ashok Leyland, Hero MotoCorp and Bajaj Auto. Maruti Suzuki is India’s largest passenger car company, accounting for 45% share of the Indian car market. The largest Indian passenger car manufacturers include Tata Motors, Maruti Suzuki, Mahindra & Mahindra and Hindustan Motors. Presence of foreign players such as Mercedes-Benz, Fiat, General Motors and Toyota is also growing in this segment. Recently, the passenger car segment has also seen the entry of other global majors such as BMW, Audi, Volkswagen and Volvo.

Honda Cars India Limited is a subsidiary of the Honda Motor Company Limited of Japan, for the production, marketing and export of passenger cars in India. The company's product range includes Honda Brio, Honda Jazz, Honda City, Honda Civic, Honda Accord and Honda Amaze which are produced at the Greater Noida facility. During the year 2012-13, the Company has a market share of 2.74% in the overall passenger vehicle segment.

Performance appraisal is the process of determining the operating and financial characteristics of a firm from accounting and financial statements. The goals of such appraisal are to determine the efficiencies or performance of a firm's management as reflected in the financial records and reports. Appraisal of performance of a company can be done through a careful and critical analysis of financial statements. The various tools and techniques of performance appraisal are comparative financial statements, common size financial statements, trend analysis, funds flow analysis, cash flow analysis, cost volume profit analysis and ratio analysis. Ratio analysis has been found the most suitable tool of analysis and has been used in our study for the analysis. The ratios can be classified into four categories: liquidity ratios, managerial efficiency ratios, leverage (long term solvency) ratios and profitability ratios. The study focuses on the performance appraisal of Honda Cars India Ltd. The data used for analysis is a secondary data and has been taken from the annual reports of the companies, published by CMIE (Centre for Monitoring Indian Economy). The data has been collected for a period of 5 years from 2007-08 to 2011-12. Performance Appraisal of Honda Cars India Ltd. has been studied by managerial efficiency analysis and profitability analysis.

Efficiency Analysis of Honda Cars India Ltd. from the Financial Year 2007-08 to 2011-12 (times)

	2008	2009	2010	2011	2012
Inventory Turnover Ratio	7.98	7.34	8.09	5.12	4.91
Debtors' Turnover Ratio	N.A.	83.0	68.24	22.65	17.72
Creditors' Turnover Ratio	7.60	5.16	5.0	3.55	3.01

Inventory turnover ratio of Honda Cars has been declining from the financial year 2008 to 2012 except the year 2010. During the year 2010, the ratio was comparatively high at 8.09 times indicating that the stock of the company is selling quickly**.** During the financial year 2012, Honda Cars has lowest inventory turnover ratio of 4.91 times showing that the stock does not sell quickly and remains lying in the godown for quite a long time. This results in increased storage costs, blocking of funds and losses on account of goods becoming obsolete or unsalable.

Debtors' turnover ratio of Honda Cars is showing a decreasing trend from the financial year 2009 to 2012 which shows the decline in the speed with which the amount is being collected from the debtors The more quickly the debtors pay, the less is the risk from bad debts, and so lower the expense of collection and increase in the liquidity of the company. Debtors' turnover ratio of the company decreases to 22.65 times and 17.72 times in the year 2011 and 2012, which reveals the inefficient credit sales policy of the management.

Creditors' turnover ratio of Honda Cars is showing decreasing trend from the financial year 2008 to 2012 which implies that the company is making delay in the payment to its creditors and thus adversely affects the credit worthiness of the company. Honda Cars has a highest creditors' turnover ratio in 2008 which implies that during the year, creditors of the company have been paid promptly which enhances the credit worthiness of the company. But during the year 2012, the company has the lowest creditors' turnover ratio of 3.012 times which indicates that the creditors are not being paid on the due date by the company which adversely affects the credit reputation of the company.

Profitability Analysis of Honda Cars India Ltd. from the Financial Year 2007-08 to 2011-12 (Percentage)

	2008	2009	2010	2011	2012
Gross Profit Ratio	25.10	13.52	18.58	21.0	5.95
Net Profit Ratio	5.93	(5.64)	(0.86)	(5.40)	(18.98)
Operating Ratio	87.74	103.0	95.72	95.33	120.0
Operating Profit Ratio	12.25	(3.48)	4.27	4.66	(20.12)
Administrative Expenses Ratio	10.73	14.19	11.73	13.23	18.90
Selling and Distribution Expenses Ratio	2.12	2.81	2.58	3.19	7.16
Cost of Goods Sold Ratio	74.89	86.40	81.41	78.90	94.0

Honda Cars has high Gross profit ratio in 2008 which falls in 2009, the ratio rises in 2010 and 2011 but it highly falls in 2012 at 5.95%. The higher gross profit ratio of the company in 2008 indicates the improved efficiency of the company in manufacturing or trading activities which may result from increase in selling price or decrease in cost price or reduction in raw material consumption per unit. But the lowest Gross profit ratio of 5.95% in 2012 implies the decline in the efficiency of the company, decrease in selling price per unit or increase in direct expenses of the company.

Honda Cars has Net profit ratio of 5.93% in 2008 indicating that the company has adequate profitability during the year. But during the financial year 2009 to 2012, Honda Cars have been incurring huge net losses and it even rose to (18.98%) in 2012.

This implies managerial inefficiency and excessive selling and distribution expenses in the company. This also reveals that the company does not efficiently maintain control over its total expenses.

Honda Cars has lower operating ratio of 87.74% in financial year 2008 indicating efficiency and profitability of the company during the year. But the operating ratio of the company have been showing increasing trend from the financial year 2008 to 2012. This shows that the company has been unable to control its operating cost which adversely affects the operating profit of the company.

Honda Cars has a high Operating profit ratio of 12.25% in financial year 2008 indicating high efficiency and profitability of the company. However, during the financial year 2008 to 2012, Operating profit ratio of Honda Cars is showing a decreasing trend, the company even incurs net operating loss in 2009 and 2012. This indicates that the company has been unable to control its cost of goods sold, operating expenses efficiently and is thus reducing the profitability of the company.

From the financial year 2008, administrative expenses ratio of Honda Cars increases to 14.91% in 2009, the ratio even increased to 18.90% in 2012. This implies that during 2009 and 2012, management of the company has not efficiently controlled its administrative expenses, and thus it increases the operating expenses of the company and reduces its profitability. Honda Cars has a lower selling and distribution expenses ratio during the financial year 2008 to 2010, which states that the management of the company have been efficiently controlling its selling and distribution expenses and is thus increasing the profitability of the company. But in 2012, selling and distribution expenses ratio of the company significantly increases to 7.16%. Cost of goods sold ratio of Honda Cars is showing an increasing trend from the financial year 2008 to 2012. This states that the cost of goods sold of the company has not been effectively controlled by the management and thus adversely affects the profitability of the company

Keeping in view the above observations relating to the study, the following measures are suggested which would go on a long way to improve the performance of Indian automobile industry.

1. Inventory is the most crucial asset for a manufacturing organisation. Particularly with reference to inventory turnover ratio, the cost of materials in Indian automobile industry is the major component in production cost and its share is increasing. The managerial efficiency to keep an optimum level of asset lies in maintaining an adequate ratio of assets to turnover.
2. It is suggested that there is a need for Indian automobile industry to adopt producing and selling wide range of products, to adopt better market strategy, by reducing cost and revising selling prices to enhance the value of turnover so as to go ahead in the era of competitions.
3. At present, the profit and loss account of multi-product concern is disclosed in a consolidated form which cannot measure and judge the performance and profitability of each activity. Hence, the profit and loss accounts should be prepared on departmental activity basis by each multi product concern.
4. Honda Cars India Ltd. should also improve its managerial efficiency by effectively controlling its inventory, fixed assets and total assets. The company should also make payment to its creditors quickly as this will increase the creditworthiness of the company.
5. Profitability position of Honda Cars India Ltd. is not sound. Honda Cars should efficiently control its direct material cost, cost of goods sold, administrative expenses and selling and distribution expenses. Honda Cars should also efficiently utilize the assets, proprietors' funds and capital employed in the business.

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