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SURVEY  
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HEAT**



SUMETT SAMWHER

### Cool comfort

The air-conditioning sector is entering into the next phase of growth

The domestic air-conditioning industry is all set to look up again after two consecutive years of sluggishness. Backed by improving indicators, the ₹13,000-crore industry is expected to grow at a CAGR of around 13 per cent over the next few years. The overall economic slowdown, coupled with weakening of micro-economic indicators, took its toll on the industry, where the residential segment of the room AC business declined, while the commercial segment of project business struggled to manage a flat growth. The twin impact of shrinking disposable income in the backdrop of uncertain economic climate and increasing prices of products led to a weaker volume off-take in the market. However, things are all likely to change, even as the overall sentiment is on the upswing with a new and stable government in place.

**Thiagarajan:**  
seeing a revival  
in demand



PALASHRANJAN BHAMICK

"The volume in both segments of the industry will recover considerably. While demand on the room AC segment will pick up with buyers providing the much needed support on account of improved sentiment, the project AC business will see a rise in volume in the wake of a much higher level of construction activities," says M. Gopi Krishna, executive vice-president and COO, domestic projects business, Voltas Ltd, who is of the view that the appreciating rupee aggravated the condition in the

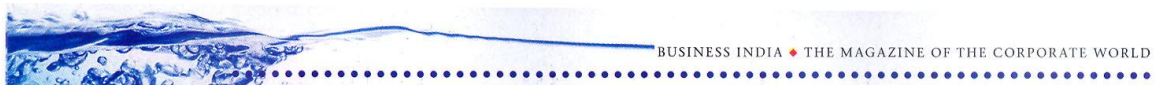
recent past, as this resulted in higher input costs. Despite a weak demand, the manufacturers had no option but to increase prices by 10-15 in the last two years. Domestic manufacturers import more than 50 per cent of their components mainly from China, and hence are exposed to the vagaries of currency fluctuation.

"The market sentiment has improved and this would gradually drive the volume in the market. The room AC market growth to accelerate with increase in penetration, whereas we expect the absorption in new construction space, both residential and commercial, to gain pace in the near future," says Rabindra Nath Nayak, research analyst, institutional equities, SBICAP Securities.

"The subdued economic condition had its bearing on the domestic air-conditioning sector as well. However, now after a couple of years of slowdown, we are gradually seeing a distinct sign of revival in demand. We expect a much better days for the industry going ahead," states B. Thiagarajan, executive director, Blue Star, which has been betting big on the expanding room AC market. The ₹3,000-crore air-conditioning and commercial refrigeration products company, which also forayed into the residential AC segment in 2011, has been witnessing a steady growth in the business for the last three years. In 2009-10, the room AC business contributed to 18 per cent of the company's total sales and the same moved up to around 33 per cent in 2013-14. The company commands a share of about 9 per cent in the ₹7,500-crore room AC market, which saw a sale of some 4.5 million units in 2013-14.

Buoyed by the changing market situation, Blue

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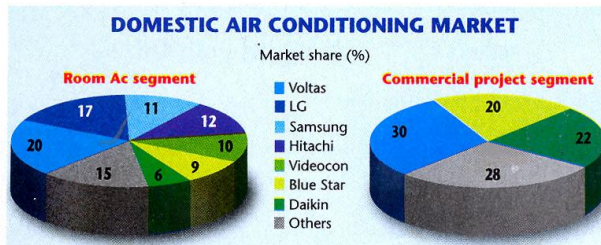
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Star is planning to set up a manufacturing facility for room ACs in south India where it commands a 40 per cent market share. This ₹150-crore manufacturing project with a capacity to produce about 500,000 AC units, will more than double the company's existing capacity of about 400,000 units at Himachal Pradesh. This will also help the company reduce its logistic cost, which amounts to almost 6 per cent of the total cost.

"As a part of our strategy, we are consciously trying to increase our presence in the residential segment of the market. Despite the slowdown, we have been performing better than the industry in the last three years. We would like to maintain this momentum going ahead as well," adds Thiagarajan, who views that the market

have also gone up with changing lifestyle and AC makers cannot sit quietly without catering to this huge market place. Moreover, this will also broaden their market base and help sustain their sales growth," says D. Nirmal Ram, national president, Indian Society of Heating, Refrigerating and Air-Conditioning Engineers.

"In order to achieve the desired growth, we are looking to penetrate more into Tier II and Tier III cities. Currently, we are generating more than 50 per cent of our AC sales from these smaller locations that present huge opportunities," states Pradeep Bakshi, chief operating officer, unitary products business group, Voltas Ltd, which has emerged as number one player in the room AC market with about 20 per cent share. The ₹5,400-crore company has aggressively tried to target a much broader consumer base, with a wide range of products with innovations and newer technologies. Voltas is pushing competitively priced entry-level products for small towns and semi-urban locations with a much stronger distribution network.



penetration at as low as 2-3 per cent speaks volumes about the opportunity for AC manufacturers in the room AC business.

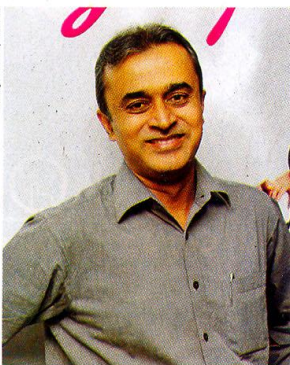
"The new government is likely to take up policy measures that will ensure heightened activities across the construction value chain. Several infrastructure projects are likely to be cleared. Besides, real estate developers are set to launch fresh projects that have been kept on hold. All this will see growing demand for materials and products like ACs," says Pranav Vakil, chairman, Praron Consultancy.

"Over the last few years, the market has undergone a big change. Aspirations of smaller cities

In the last few years, the domestic air-conditioning market has undergone a major transformation with the demand for energy efficient and environmental-friendly AC units on the rise. Guided by regulatory norms, the manufacturers are altering their capacities to come up with a new range of power-saving models in both split and window AC segments. They are also making necessary changes in their production lines to manufacture products conforming to the norms of the Bureau of Energy Efficiency (BEE), which pursues the Star Levelling Programme with an objective to mitigate the greenhouse effect on environment and also to provide the consumers an informed choice about the energy and cost-saving potential of the relevant product.

At present, as per BEE Regulations, room air-conditioners are rated on the basis of their energy efficiency on a scale of 1 to 5 stars. Higher the number of stars, the higher is the energy efficiency of the room air-conditioners and vice-versa. At present, it is mandatory for split air-conditioners to conform to the energy labelling norms. It is pertinent to note that over the years, BEE has upgraded the energy efficiency rating for room air-conditioners in order to make them more energy efficient and environment friendly. With effect from 1 January 2014, the BEE has again mandated the change of star rating for room air-conditioners based on a higher energy efficiency norm. It has raised the energy efficiency standards by about 8 per cent for split air-conditioners for the same rating band.

"The change is intended to help raise



**Nandi: good revival**



**Sachdev: inverter ACs catching up**

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**Krishna:**  
construction  
activities boost  
the sector



**Ram:** big  
change

consumer awareness on saving energy and creating more energy efficient appliances across the spectrum for this industry. The star rating scheme, under the BEE standards and labeling programme is especially relevant in view of the upcoming freeze on hydro-chloroflorocarbons under the Montreal Protocol in 2013 and the effort of getting prepared for future legislations as regards global warming," says Ashish Rakeja, chairman, standards committee, ISHRAE.

In pursuit to come out with more energy-efficient offering, the AC makers are also adding inverter ACs to their product portfolio. Inverter-built systems vary the speed of the compressors and deliver precise cooling, thereby cutting down the power consumption considerably. "With awareness level growing, consumers are asking for products that can ensure a greater level of saving on the energy front. The inverter technology is the latest evolution in the air-conditioning industry. An Inverter is used to control the speed of the compressor motor, so as to continuously regulate the temperature," says C. Subramaniam, Bangalore-based energy consultant and LEED facilitator.

"The market for inverter AC is catching up quite fast and we as a company are also looking at this segment seriously. Going forward, we would like to localise this production to bring down the prices," says Krishan Sachdev, managing director, Carrier Midea India, which is aiming to increase the share of inverter AC in its portfolio to around 10 per cent in the current year from 3 per cent last years.

In India, the inverter AC segment is relatively new and growing rapidly. But, in the mature markets, it is more established segment and, therefore, comprises a larger part of the AC segment. According to estimates, the share of inverter ACs is just 3 per cent in India, while it is about 50 per cent in China and 100 per cent in Japan. Consumption of inverter ACs can entail saving of as high as 25 per cent energy as compared with star rated ACs. Predictably, the price of an inverter AC is steeper than five-star rated products, costing ₹40,000-45,000 for a 1.5-tonne unit. A five-star split air-conditioner of the same size comes for ₹35,000-36,000 in the market place. Meanwhile, BEE is also in the process of introducing the energy labeling programme for inverter ACs.

"These are the consumers who are most likely to make the transition since they do not mind playing a little more to own a product which is better in terms of energy efficiency. In the next few years, the market for inverter ACs will go up to about 30 per cent," says Thiagarajan, who says that the government should bring down the CENVAT to zero per cent for star-rated products.

The ongoing energy levelling programme has kept the manufacturers on their toes recently as they have to upgrade the technologies. Moreover, the rise in input cost has also forced them to hike the prices, even as the demand remained subdued in the recent past. As per experts, such a headwind is a part of any market, which is under transition and they are of the opinion that the market will absorb these events more effectively, going forward.

"In the last couple of years, the prices of ACs went up by 15-20 per cent and that turned out to be a big dampener for the market, which was already struggling. But this year, we have seen things gradually falling in place and we have experienced a sales growth of mid single digit as against de-growth last year," says Nilesh Gupta, managing partner, Vijay Sales.

"This year, we have already seen good revival in all markets except for north where the summer has so far been moderate. The positive sentiment and pent-up demand has further added to the surge in demand. We have lined up a wide range of products," states Kamal Nandi, business head & executive vice-president, Godrej Appliances.

**W**hile the market mantra is energy efficiency, a striking development in the AC market has been demand and supply side shift towards split ACs, as compared to window ACs. Over the years, split AC has surpassed demand for window AC dramatically. Currently, 80 per cent of capacity is utilised for split ACs, as against 20 per cent for window ACs. "The share of window ACs has declined rapidly in the past five-six years. In the next two-three years, window ACs will completely give way to split ACs," states Nayak. In China one mainly sees splits.

All in all, the domestic air-conditioning industry is passing through a transition phase. With a penetration level of just 3.5 per cent, the market presents huge potential in the backdrop of growing economy and changing lifestyle.

On the supply side, domestic manufacturers are altering their strategies where adoption of newer technologies and innovations is in priority in a market, which is intensely competitive in nature. Going forward, the domestic industry will have to scale up their capacity to keep much better control over the value chain.

♦ ARBIND GUPTA