Rubber output cuts set to puncture tyre companies' buoyancy

Local tyre firms, which saw a better June quarter due to a 30% fall in international prices of rubber since May, are in for a jolt as top three global producers of the resource are set to curtail production to boost prices. Thailand, Malaysia and Indonesia, which account for 70% of global rubber production, are cutting output to counter the global demand slowdown and excess production. This is not good news for the Indian tyre industry, which is already reeling under demand slowdown, as prices of domestic rubber are also set to rise in line with the international prices. Companies feel an increase in raw material prices will hurt their profitability in the coming quarters as rubber accounts for 43% of their total raw material costs. International rubber prices have declined over 30% since early May in rupee terms to sub-Rs140/kg, boosting profitability of some domestic companies such as Apollo Tyres, which posted a 78.94% increase in consolidated net profit at Rs138.02 crore for the June quarter. Jaibir Sethi and Anirudha Dutta, analysts with CLSA in a research note dated August 16, said while the soft domestic economic backdrop has raised worries about volumes, this is less critical for Apollo than rubber. "A 5% reduction in our domestic volume estimate implies a 13% reduction in domestic Ebitda and 15% reduction in consolidated earnings per share estimates. This is actually less than the sensitivity to a 5% change in rubber despite being much less volatile than rubber prices." Rajiv Buddharaja, president, All India Tyre Manufacturers Association (ATMA), sees stabilisation in natural rubber prices temporary. "The situation will not be the same. If countries limit he production, rubber prices will again go up. Though some companies have managed to do well in the first quarter, some have suffered due to slowdown. So expected high raw material costs coupled with demand slowdown takes the overall sentiment down for the industry." According to ATMA, the tyre industry witnessed a flattish growth for the first quarter. "Though we have not collated the data yet, we are expecting the growth to be in the range of 2-3% in the first quarter," said Buddharaja. Not just the original equipment makers, the demand from replacement market has also gone down. "We are in a tough situation right now as there is a severe demand squeeze. People are either postponing their purchases of going for cheaper tyres. Plus rupee depreciation is adding to our worries. Any increase in raw material prices will severely hit the industry," said Ajay Sevekari, director, Bridgestone Tyres. "High raw material prices will affect the topline of the companies in the coming quarters," said a senior official from a tyre maker.