

Heavy Earth Moving Machinery Business - Firm level Analysis (Hitachi Construction Machinery)

A study on analysis of Hitachi Construction Machinery (Japan)

Home Country – Japan , Host country – India (Chapter- Three)



- *Report is prepared by :*

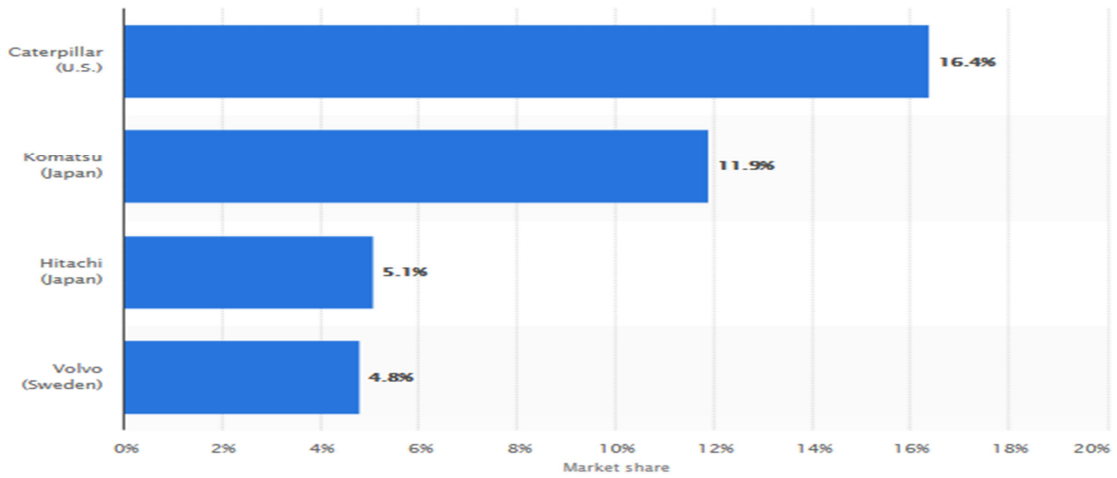
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FIRM LEVEL ANALYSIS:

INTRODUCTION

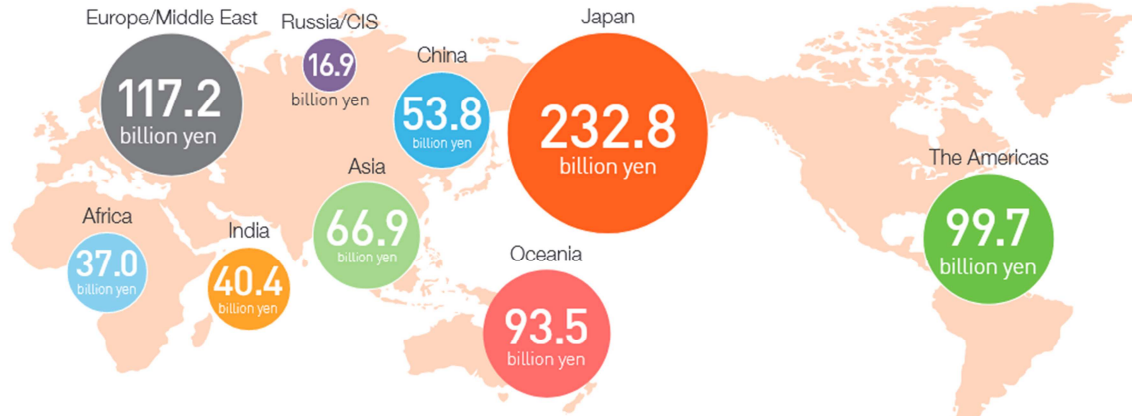
- Hitachi Construction Machinery Co., Ltd. is a Japanese construction equipment company which is into the manufacturing, sales and service of construction machinery, transportation machinery, and other machines and devices.
- It was established in 1970, and was involved in the production of Japan's first mechanical excavator, the company has now become a major construction equipment manufacturer in the world, and it is listed on the Nikkei 225.
- The major operations included are: Manufacturing, Sales and services, Transportation machinery and other machines and devices.
- Hitachi Construction machinery includes subsidiaries: 84 companies and Affiliates 21 companies.
- The proportion of overseas sales has grown from 6% when company was established in 1970 to an anticipated near 80% in FY2016.
- Hitachi Construction Machinery commenced production in nations such as Indonesia, China and India in response to growth in emerging markets.
- Tata Hitachi Construction Machinery Company Private Limited, the leader in construction equipment in India.
- Tata Hitachi is a subsidiary company of Hitachi Construction Machinery Co. Ltd., which holds 60% share and Tata Motors Ltd. holding 40%. There are 3 manufacturing plants in India: Jamshedpur, Dharwad and Kharagpur.
- Tata Hitachi is focused on capitalizing the opportunity in the domestic arena for which the key market segments are excavators, wheeled products, cranes and others.
- Tata Hitachi focuses on value added service offerings too- Full Maintenance Contracts, which complete the offering to customers and enable them to free up precious resources for core activities.
- Numerous key players are operating in the market which include AB Volvo, Caterpillar Inc., Komatsu Ltd., Doosan Heavy Industries & Construction Co. Ltd., Hitachi Construction Machinery Co. Ltd., J.C. Bamford Excavators Limited, Kobe Steel Ltd., Liebherr Group, Atlas Copco AB, and CNH Industrial N.V. They have adopted various growth strategies to capture a larger market share and increase their customer base.

Leading construction equipment manufacturers in 2017, based on global market share



Source: Statista.com

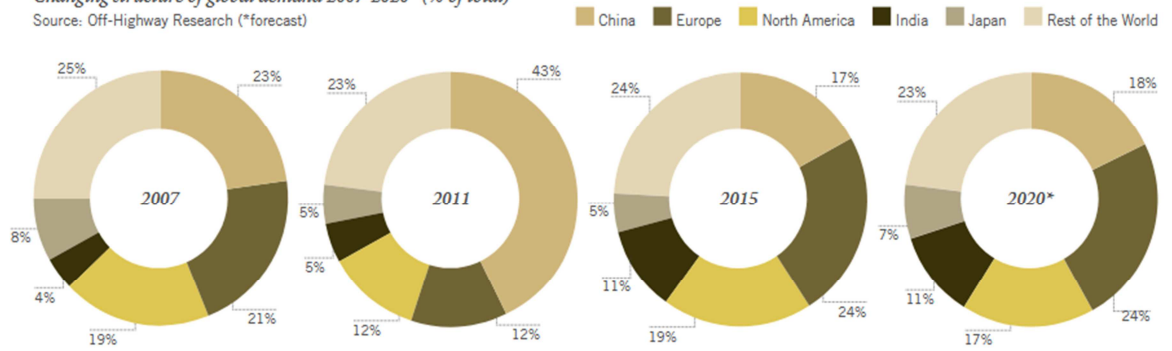
■ Sales and composition ratio by regional segment



Source: Investor Report

Changing structure of global demand 2007-2020* (% of total)

Source: Off-Highway Research (*forecast)



Firm Financials:

2018 REVENUE: \$9,027.27

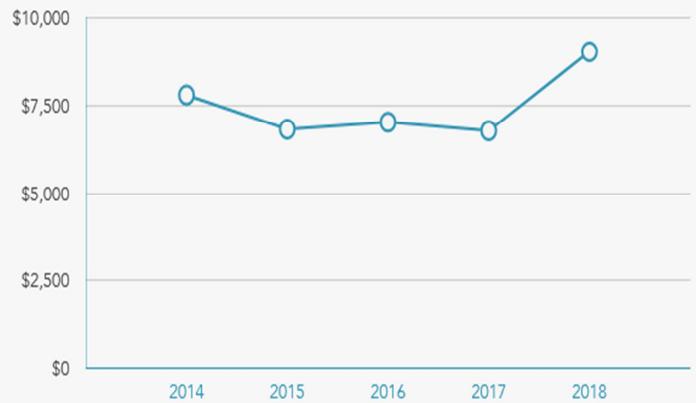
GROSS PROFIT: \$2,483.16

OPERATING INCOME: \$901.05

NET INCOME: \$564.74

DILUTED EPS: \$2.66

In Millions



The following table summarizes the consolidated results for this term ended March 2018.

(Millions of yen ; %)

	FY 2017	FY 2016	Year-on-year change	
	(April 1, 2017- March 31, 2018) (A)	(April 1, 2016- March 31, 2017) (B)	(A)-(B)	(A)/(B)-1 (%)
Revenue	959,153	753,947	205,206	27.2
Adjusted operating income*	93,582	28,265	65,317	231.1
Operating income	95,737	23,622	72,115	305.3
Income before income taxes	95,612	23,859	71,753	300.7
Net income attributable to owners of the parent	60,004	8,022	51,982	648.0

(Rounded off to the nearest million)

The following table summarizes consolidated net revenue by geographic area:

		FY2017 (April 1,2017- March 31, 2018)		FY2016 (April 1,2016- March 31, 2017)		Increase (Decrease)	
		Revenue (Millions of yen) (A)	Proportion (%)	Revenue (Millions of yen) (B)	Proportion (%)	Change (Millions of yen) (A)-(B)	% Change (A)/(B)-1
	North America	136,319	14.2	78,488	10.4	57,831	73.7
	Central and South America	16,081	1.7	6,996	0.9	9,085	129.9
	The Americas	152,400	15.9	85,484	11.3	66,916	78.3
	Europe	104,184	10.9	87,565	11.6	16,619	19.0
	Russia-CIS	27,363	2.9	19,476	2.6	7,887	40.5
	Africa	44,831	4.7	34,051	4.5	10,780	31.7
	Middle East	23,143	2.4	22,741	3.0	402	1.8
	Russia-CIS, Africa, and the Middle East	95,337	9.9	76,268	10.1	19,069	25.0
	Asia	75,418	7.9	62,239	8.3	13,179	21.2
	India	65,077	6.8	48,551	6.4	16,526	34.0
	Oceania	151,903	15.8	96,391	12.8	55,512	57.6
	Asia and Oceania	292,398	30.5	207,181	27.5	85,217	41.1
	China	121,614	12.7	71,463	9.5	50,151	70.2
	Sub-total	765,933	79.9	527,961	70.0	237,972	45.1
	Japan	193,220	20.1	225,986	30.0	(32,766)	(14.5)
	Total	959,153	100.0	753,947	100.0	205,206	27.2

(Rounded off to the nearest million)

The above financial data reveals that Asia and Oceania contributes about 30% of Global revenue in 17-18FY in which there was a increase of about 3%.India as a market contributes about 6.8% to the global revenue in that financial year. The Home country Japan contributes about 20% of the revenue followed by North and South America. The country of focus for Hitachi should be Middle east, Africa and Russia-CIS, where there is a huge growth and market potential but is not a prominent player out there.

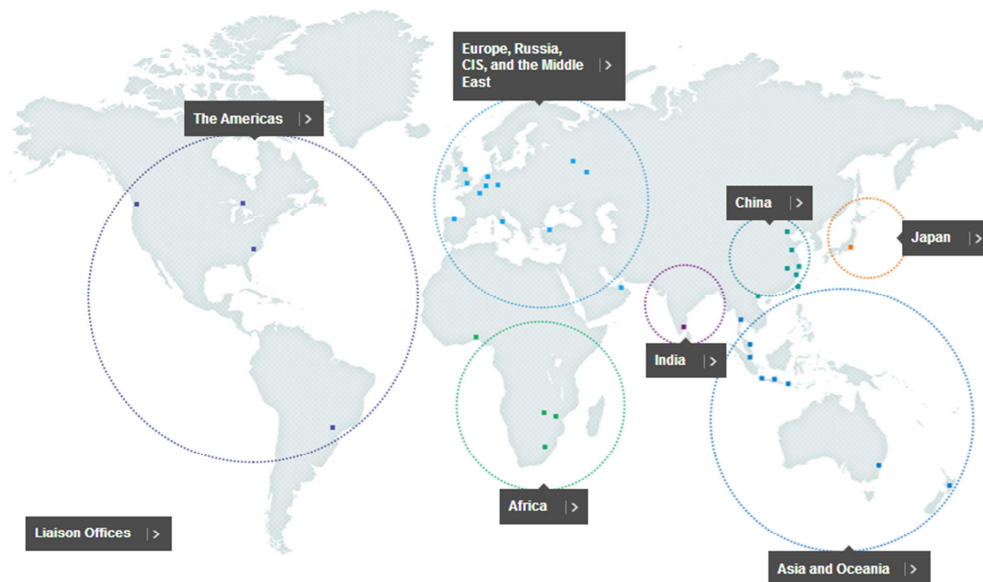
Internationalization Strategy of Hitachi Construction Machinery:

GLOBAL STRATEGY FRAMEWORK:

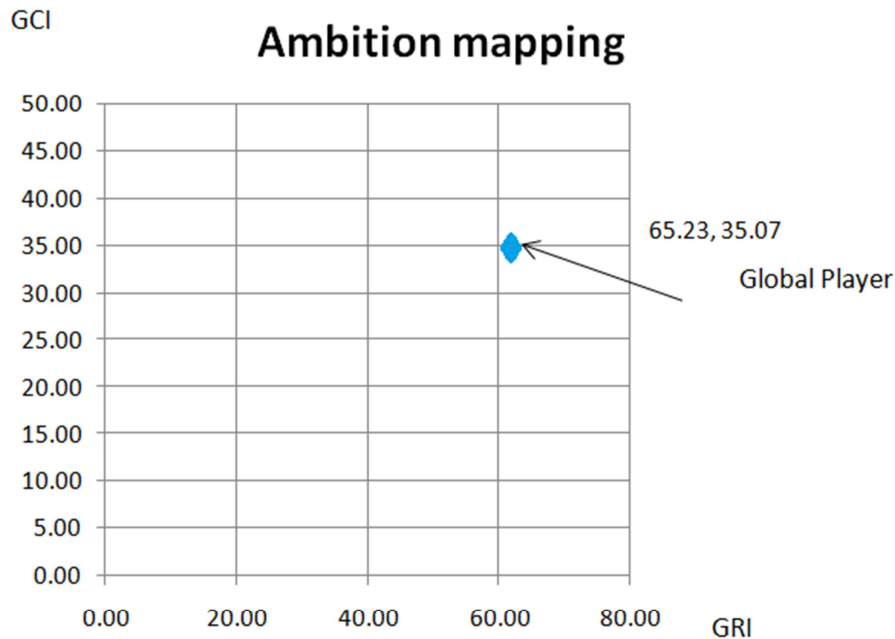


Global Ambition:

Hitachi Construction Machinery has its presence in almost all the continents of the globe:

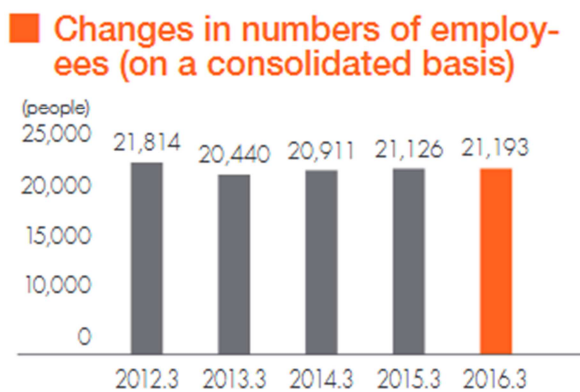


It has about 84 Subsidiaries (Japan: 10 companies, Overseas:74 companies) and 21 Affiliates(Japan:4 companies, Overseas:17 companies)



From the above position of the pointer shows the Global ambition of Hitachi Construction Machinery. The above GCI and GRI index focuses that Hitachi Construction Machinery has global ambition of making its presence felt across all geographies with substantial investment through subsidiary, JV, Global sourcing etc.

Number of Employees Globally:



Global Positioning:

Hitachi Construction Machinery has positioned itself across different countries:

Key Countries: European like Netherlands, France, UK, North America

Emerging Countries: China, Indonesia, India, Brazil, Malaysia

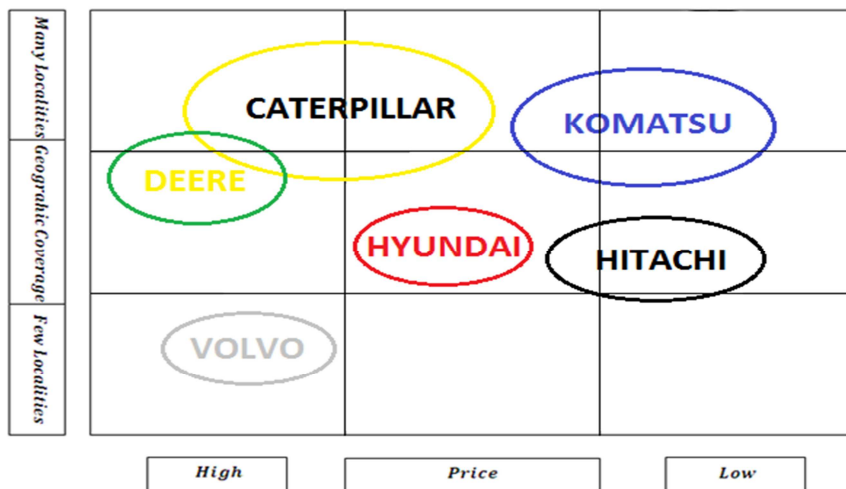
Marketing Countries: Middle East, Nigeria, Senegal, Uganda, SAARC

Platform Countries: Russia, Africa (Zambia)

Sourcing Countries: China, Brazil.

Hitachi Construction Machinery will begin to gradually strengthen its rental business in the North American construction equipment market.

The following graph is a tool for mapping the positioning of TATA Hitachi and its main competitors, according to geographic coverage and products prices. The choices were Komatsu and Caterpillar as the basic players in the industry, John Deere as part of the forest- machinery segment of the industry, Hyundai and Hitachi as the major competitors of the Komatsu in the emerging markets and finally Volvo, for its complete contrary positioning to Komatsu's. Hitachi has low Geographical coverage and price are economical as compared to market leader Caterpillar and Komatsu.



Value Proposition:



In China:

- Expand our dealer network across the entire country
- Models suited to emerging countries, with excellent durability and cost effectiveness, are doing well
- Strengthen productivity, and meet market needs for an increasingly larger model line up

In India:

- Engage in manufacture and sales at our joint venture with the TATA Group*, Tata Hitachi Construction Machinery
- Take full advantage of the TATA Group' network, and secure a strong market position for hydraulic excavators
- Promote the cultivation of other emerging markets, such as in Africa and the Middle East, using India as a strategic base

In Asia and Oceania:

- Strengthen customer support by utilizing Global e-Service, and respond to expanding market demand



In Americas:

- In the Americas, Hitachi Construction Machinery provides world class technology
- The joint venture conducts local production, and Deere & Company*, which has a strong local footing, conducts marketing
- In North America, engage in manufacture and sales at our joint venture with Deere & Company, Deere-Hitachi Construction Machinery Corporation
- In 2011, established a joint venture in Brazil with Deere & Company for full-scale expansion at Central and South America, where the growing demand is expected



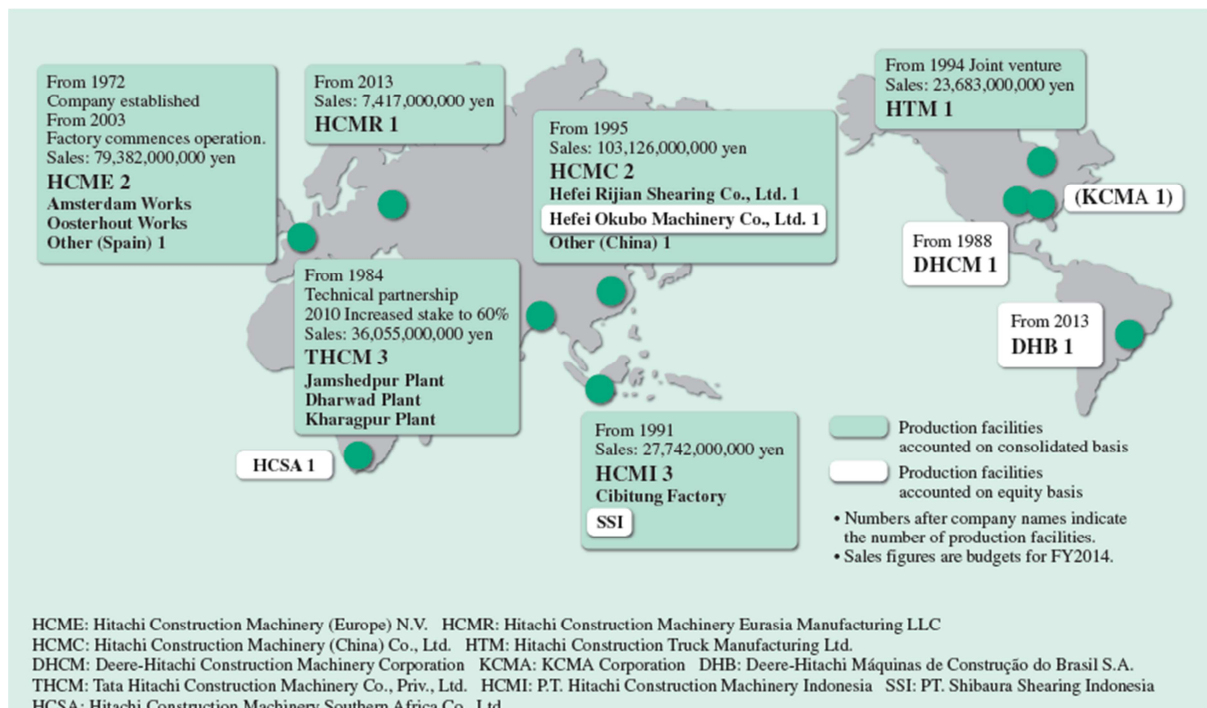
In Russia:

- Launch local manufacturing plant in Russia, the world's largest resource-rich country, and commence production in 2013
- Secure a strong market position for hydraulic excavators

In Africa:

- Capture the growing demand for mining machinery by utilizing the sales and service network covering the whole of Africa

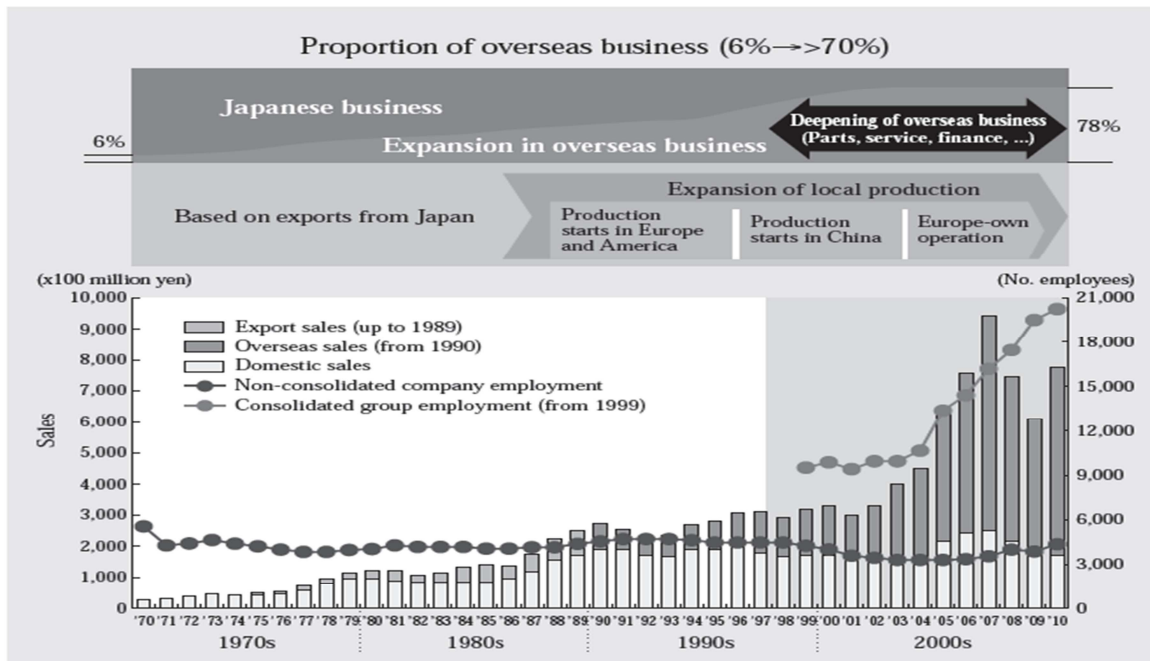
Global Business System:



Hitachi Construction Machinery has been transforming its business from one based on exports from Japan toward expansion of local production. Production in countries such as China and the Republic of Indonesia commenced during the 1990s. The company has increased the proportion of overseas sales year by year to the point where they now account for about 80% of total sales. This was achieved by expanding its network of dealers, particularly in Asia and Oceania, and by establishing its own sales companies in mining regions.

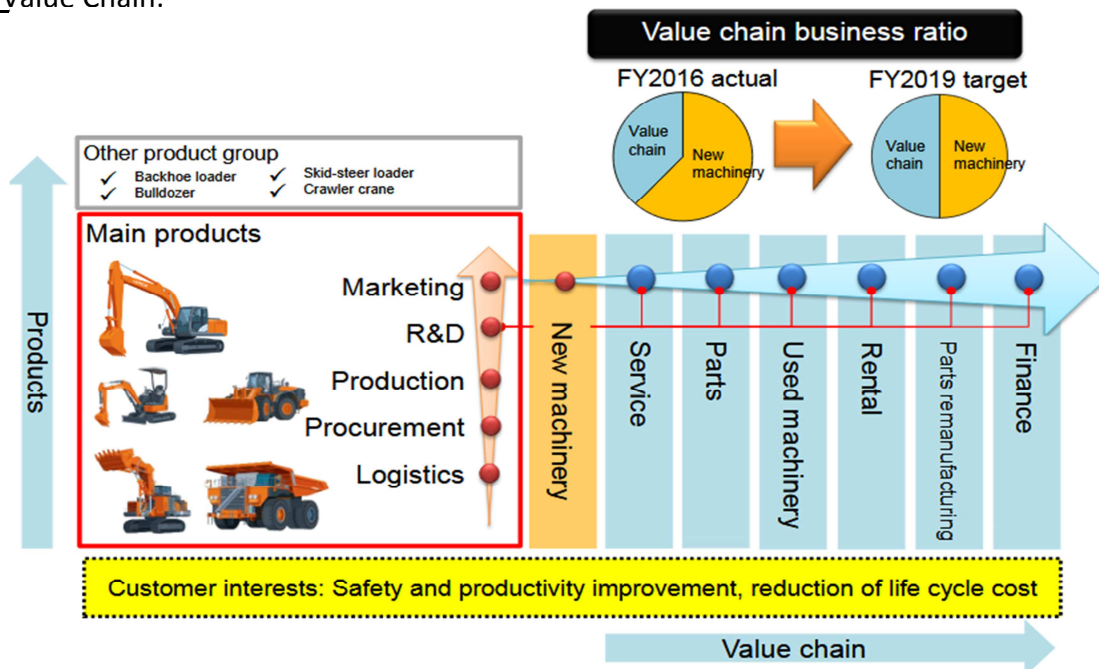
As of 2015, Hitachi Construction Machinery has 17 production facilities in Japan and 19 overseas. Broken down by region, these comprise two sites in North America, one in South America, four in Europe (including Russia), five in China, six in Asia (excluding China), and one in Africa.

In Africa, Hitachi Construction Machinery was the first Japanese company to establish and operate a re-manufacturing factory of hydraulic components for hydraulic excavators. The facility is located in the Republic of Zambia and utilizes know-how from Japan.



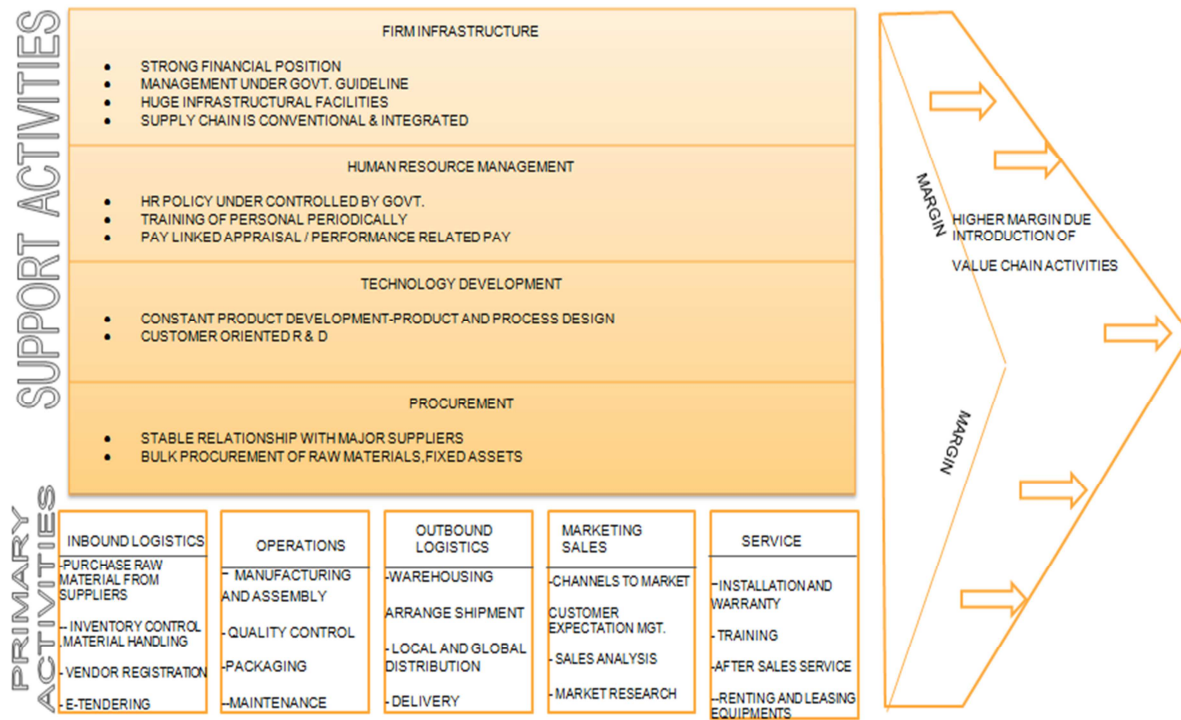
Expansion of Overseas Operations of Hitachi Construction Machinery. Hitachi Construction Machinery seeks to transform itself from a Japanese to a global corporation. Source: Hitachi Construction Machinery website

Global Value Chain:



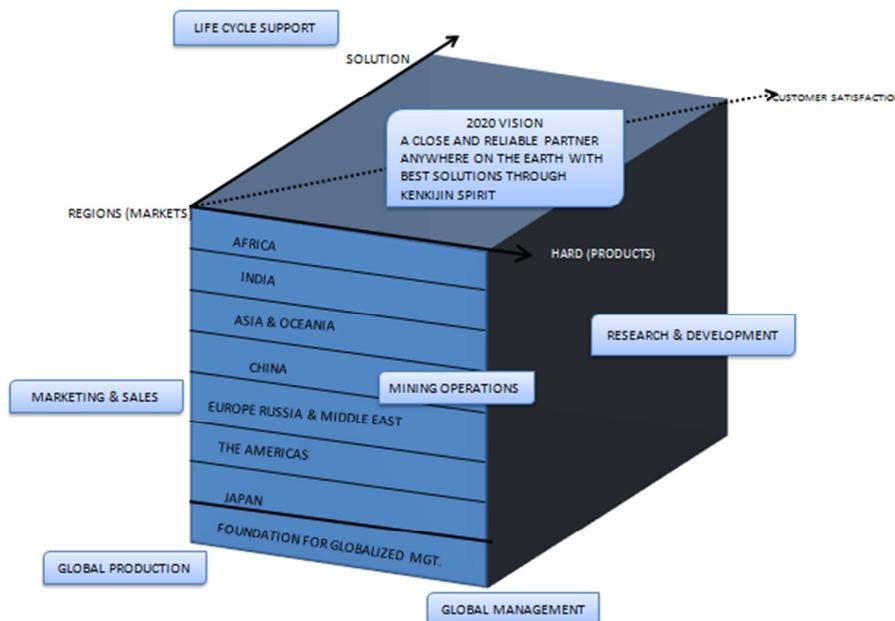
Source: Hitachi Construction Machinery Investors Report

The following illustration shows the general structure of Hitachi Construction Machinery value chain from raw material purchasing to after sales services and support activities.



Hitachi Construction Machinery believes that growth with the value chain, which includes their customers, as well as our sales and service distributors and business associates (suppliers), is essential to increasing corporate value. Hitachi Construction Machinery value chain analysis identifies the company’s “primary activities that create customer value” and its related support activities

GLOBAL ORGANIZATION:



HITACHI Construction Machinery Co., Ltd. was established in October 1970 and since then has contributed to its customers' businesses through two different types of creativity, namely, the development of innovative technologies that satisfy customer needs and the creation of demand by supplying those customers with new value. To respond flexibly to these changes in the business environment and achieve sustainable growth, it is necessary to make progress toward a more global business management base. Looking ahead to 2020, Hitachi Construction Machinery has formulated its 2020 Vision that sets out where it wants to be in a decade's time, expressing its aim to be a "Close and Reliable Partner anywhere on the Earth with Best Solutions. The company's aim is to establish an overwhelming presence for itself in the global market for construction machinery by offering solutions and services that are one step ahead and based on superior technologies cultivated over many years. The Go Together 2013 medium-term management plan was a growth strategy based around the three axes of products, solutions, and regions (markets). The organization created the plan by thinking about the market ten years from now. It seeks to strengthen the following six imperatives of the company's strategy:

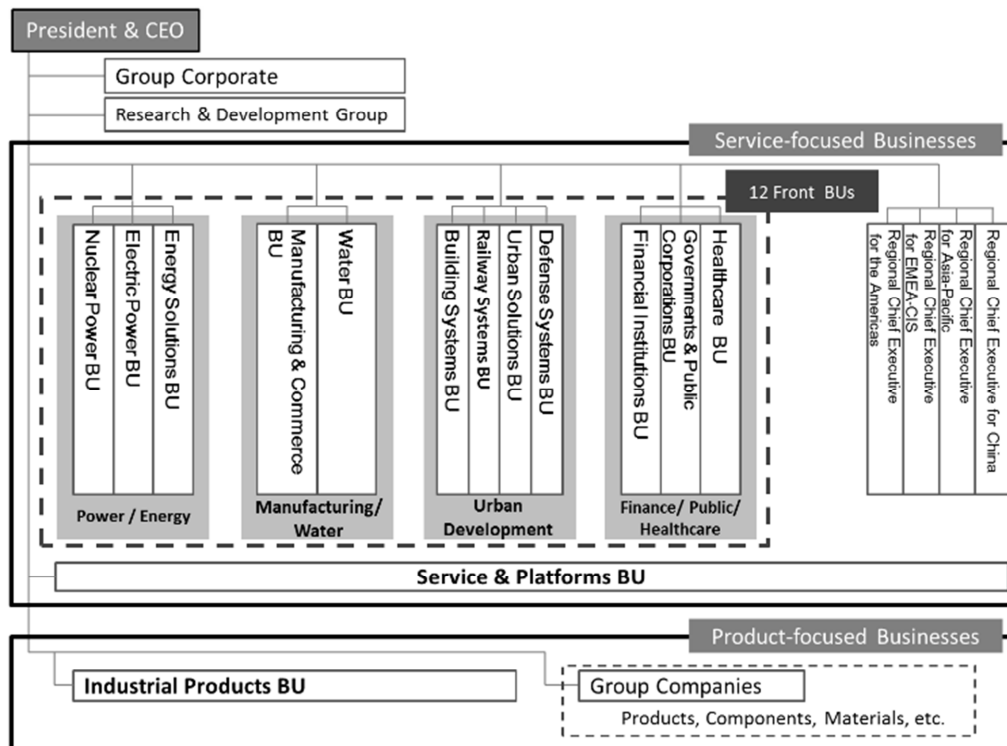
- (1) Research and development
- (2) Life cycle support
- (3) Marketing and sales
- (4) Global production
- (5) Global management
- (6) Mining operation

A "Strategy Planning Division" was set up which included the key players from the various organizations such as development, procurement, production, and sales are gathered here and all the information from each organization, both international and domestic, is analyzed, synergized, and integrated. They move forward by coordinating with one another and by carefully examining what product each area needs, what service should be provided in support of the products, and how all this should be best delivered to sell our products.

Hitachi Construction Machinery has approximately 22,000 staff in total. More than half are local natives in their own country. Since the overseas sales ratio is anticipated to increase even more in the future, the organization considers that localizing the overseas business operations with a native staff would be fundamental to organization's success. To achieve that, a "Succession Plan" was launched to train local staff to become candidates for future executive positions.

To advance localization, a true sense of unity is important. "**Kenkijin Spirit**", which is the organization's standard of values and shared code of conduct among all Hitachi Construction Machinery employees, is fundamental to that unity. All over the world, Hitachi is conducting the training needed to establish this sense of unity and value. **Kenkijin Spirit** is soaking in all over the world and becoming localized, while, at the same time, it is driving the group to advance as one united body.

Hitachi Group's New Business Structure from April 1, 2016



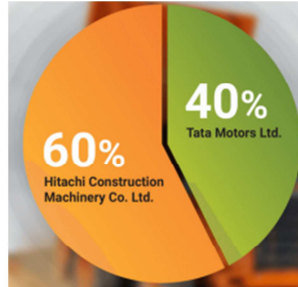
Source: Hitachi website

Hitachi changed its existing product-specific in-house company system making a transition to a new business structure to build a business structure with strengthened front-line functions that will accelerate Collaborative Creation with customers.

Hitachi Construction Machinery Internationalization to India(TATA Hitachi)

- Hitachi opened an office in Mumbai in November 1935 as the Hitachi Group's first overseas base, and in 2015, it will commemorate 80th anniversary of its establishment.
- Tata Hitachi Construction Machinery Company Private Limited, the leader in construction equipment in India.
- The company commenced manufacturing of construction equipment in 1961, as a division of TELCO. In 1984, it entered into a technical collaboration with HCM, Japan for manufacturing state of the art hydraulic excavators.
- Presently, Tata Hitachi is a subsidiary company of Hitachi Construction Machinery Co. Ltd., which holds 60% share and Tata Motors Ltd. holding 40%.
- Tata Hitachi focuses on value added service offerings too- Full Maintenance Contracts, which complete the offering to customers and enable them to free up precious resources for core activities.
- Tata Hitachi is focused on capitalizing the opportunity in the domestic arena for which the key market segments are excavators, wheeled products, cranes and others.

- In terms of overall production, Dharwad plant contributes to about 60 percent, Kharagpur is about 35 percent and Jamshedpur is five percent. Jamshedpur plant mainly supplies components to the other two plants.
- Tata Hitachi has 2 category line up of products-economy and premium. Global manufacturers have launched products in the premium class market but Tata Hitachi have EX Series for the economy market and ZAXIS Series for the premium market.
- Tata Hitachi also has a full – fledged Design and Development set-up for developing indigenous and collaborated equipments
- Tata Hitachi is actively participating in creating the new R&D facilities at Kharagpur with the aim to make the new centre a global R&D hub.



Infrastructure



Mining

- Tata Hitachi also takes pride in its marketing and service network of 230+ touch points – one of the largest distribution networks in the country.
- Tata Hitachi focuses on value added service offerings too- Full Maintenance Contracts, which complete the offering to customers and enable them to free up precious resources for core activities
- Tata Hitachi also provides services like specialized reconditioning and refurbishing services to ensure that the utility of the equipment is extended and life cycle costs are brought down.

VISION OF TATA HITACHI:

“Reliable Solutions for Building a greater tomorrow.”

MISSION OF TATA HITACHI:

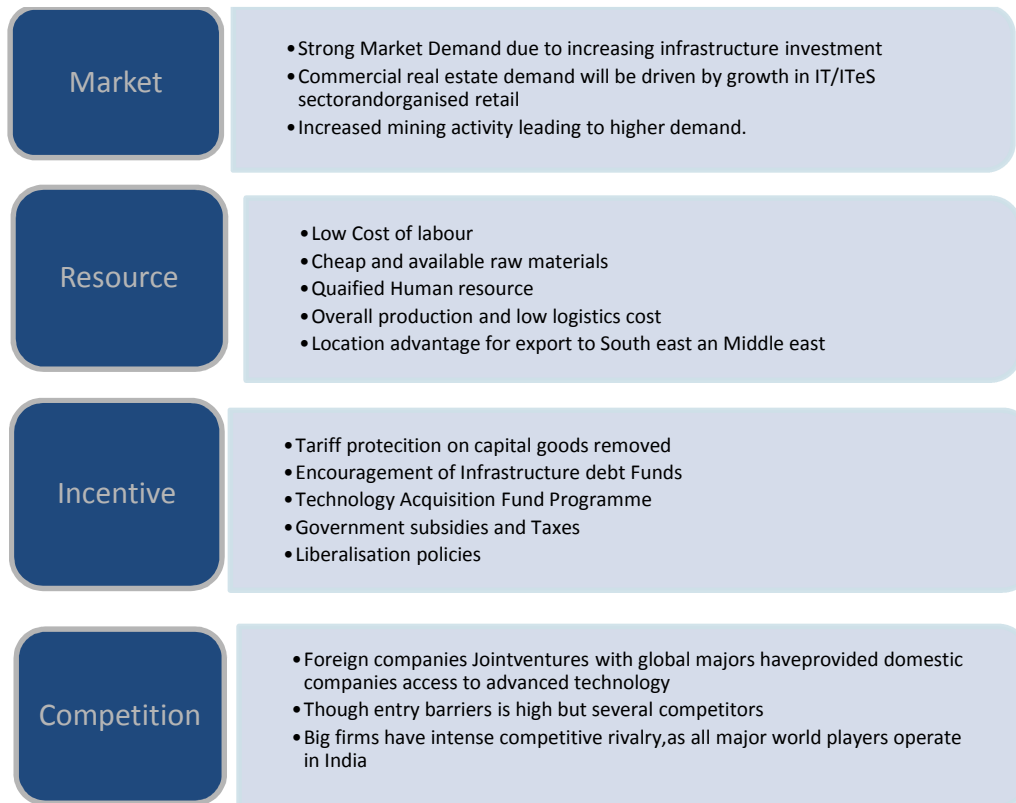
Be the preferred partner for providing reliable solutions for mining and infrastructure sectors. While dominating the domestic market, we will become a global manufacturing and development hub. Our hallmark shall be our motivated people, customer centric culture, superior technologies and strong partnerships, all working safely in unison with environment and society.

India as a market for Tata Hitachi:



India is a high attractive market for TATA Hitachi. There is a huge market potential along with growth opportunity in the construction and mining sector. TATA Hitachi caters to economic as well as premium segments so there is a ample scope of business in India from local infrastructure project to

Market and Investment Opportunities in India:



Host Country Risk Analysis:

Political Risk: Low to medium

- ❖ In India, there is little risk to shareholders in terms of assets freeze, expropriation etc.
- ❖ A major area of concern in India is corruption which engulfs heavy engineering companies easily
- ❖ Also, the employees exposure to risk is very low as the legal system and laws are strict.
- ❖ Labour unrest and strikes are causes of concern which might disrupt the market .

Operational Risk: Low

- ❖ Large number of suppliers available.
- ❖ Infrastructure, transportation and power are causes of concern.

- ❖ Some regulations on local requirements and nationalistic preferences.

Economic Risk: Low to medium

- ❖ High economic growth. The GDP will grow by 7.0% in FY18 which is expected to increase to 7.4% by FY20
- ❖ Fast growing middle class, huge investments in infrastructure project.
- ❖ The current corporate tax rate in India is 30% which has also been subjected to fluctuations
- ❖ Exchange rates fluctuations is on higher side.
- ❖ Inflation high in the country.

Competitive Risk : High

- ❖ High corruption
- ❖ Presence of several Global companies
- ❖ Low switching cost from buyer increases competition

Hitachi's Construction Machinery Entry Strategy in India:

Entry Objective:

Market Development Objectives:

- Size & growth opportunity in terms of rising income & population of the country
- India's growing market is lucrative in terms of Global long-term competitiveness.

Resource Access Objective:

- Extracting key resource such as cheap labour and access to large distribution network for competitiveness

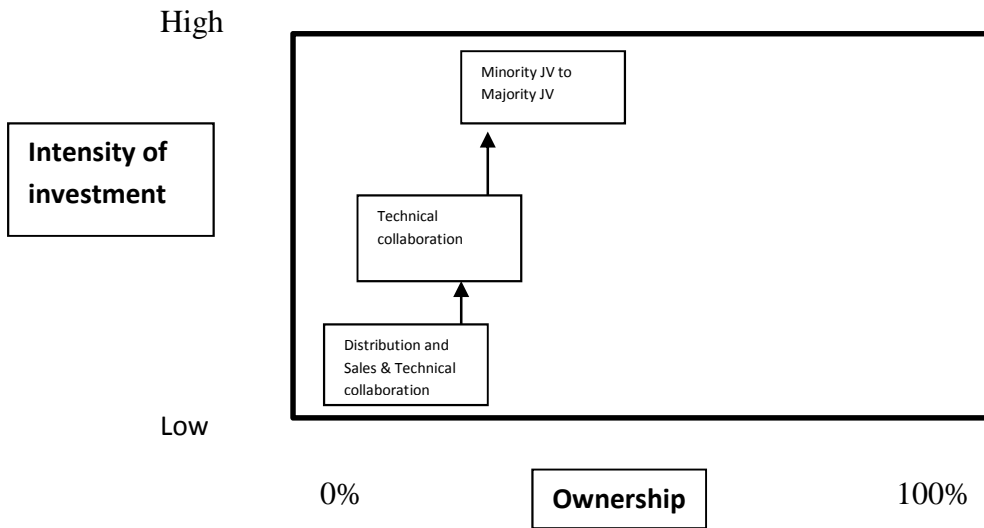
Timing of Entry:

- Hitachi Construction Machinery entered India in 1961 which was a Pre-Mature Phase of the industry .It started as a division of TATA Engineering and Locomotive Company now known as TATA Motors where distribution and sales was the primary objective.

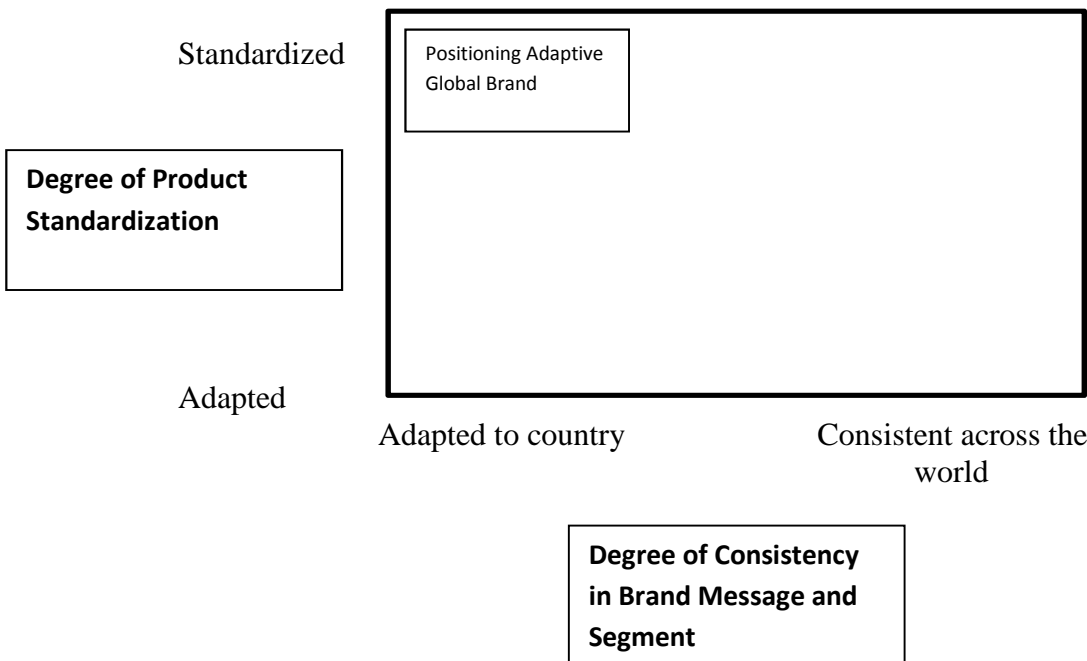
Entry Mode:

Tata Hitachi entered in 1961 as a division of TATA Engineering and launched its 1st 955 Excavator. Then as the market started to grow and new players started to enter Hitachi went into Technical collaboration with TATA in 1984.Later on in 2000 entered into minority JV

with Telco for 80:20 stakes. As the competition grew intense with other global competitors and Hitachi started to invest more the minority JV was transformed to majority 60:40 JV with Hitachi having 60% stakes in 2005.

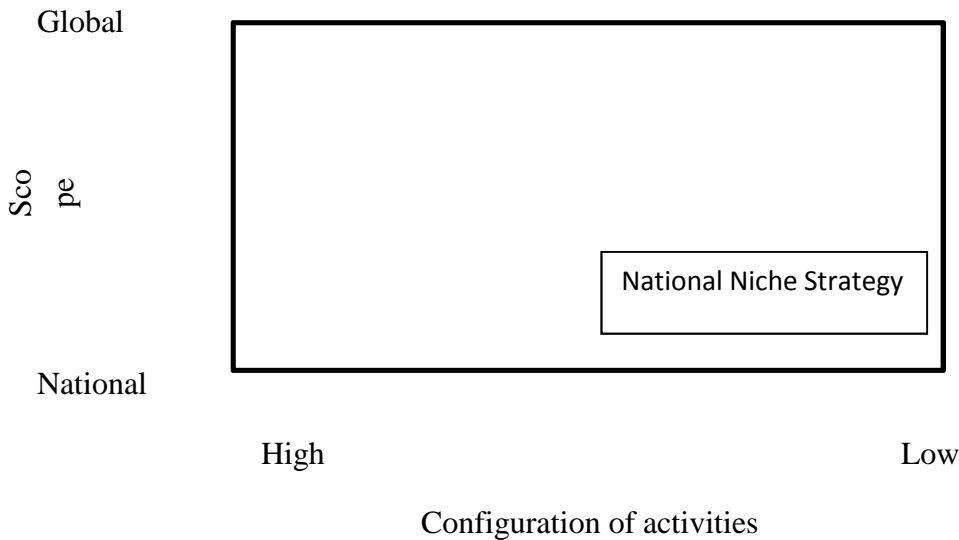


Brand Positioning for Tata Hitachi in India:



Tata Hitachi follows “ Positioning Adaptive Global Brand” in India. Product is standardized which is at par with global offerings but the promotion message is adapted as per the geography in which it is operating as in India it is ”Chalo Desh Banaye”

International Marketing Strategy of TATA Hitachi in India:



TATA Hitachi follows National niche strategy specially on national scale to avoid competition with firm of National High Share like BEML. TATA Hitachi has a market share of about 37% in Indian heavy machinery and mining sector. Also the company have grown by 46 percent in 2016-17 which is better than the industry growth average of around 43 percent.

Way forward:

The construction equipment industry in India had its worst recessionary phase between 2011 and 2014. When growth returned in 2015, Tata Hitachi, a 60:40 joint venture between Hitachi and Tata Motors, decided to restructure its business to make the best of the good times.

Between 2015 and 2017, the company closed down two loss-making overseas subsidiaries: Lebrero SA and Serviplem SA of Spain. In India, the company is closing down its “high cost” Jamshedpur (Jharkhand) facility. Production is consolidated largely at Kharagpur (West Bengal) and Dharwad (Karnataka), both of which are now witnessing a 200-crore capacity expansion drive. The company was back in the black in FY17 after five successive years of losses. The profits only widened in FY18.

The top-line is growing by 15-20 per cent, riding on strong demand from the railways road sector; the Centre’s Bharatmala and Sagarmala projects; the expansion of track-capacity by the railways; the growth in mining; and the State expenditure on irrigation and infrastructure push by urban local bodies.