

More cars bring more challenges to the Russian market
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What does the automotive market in Russia look like at present? Growth everywhere. According to the annual 'Global Automotive Financial Review' by PricewaterhouseCoopers, while several mature markets will grow modestly over the next four years, the biggest growth will come from so called "BRIC" countries (Brazil, Russia, India China). BRICs will account for more than 40% of forecast global light vehicle assembly increases and represent 52% of the industry's forecast global capacity expansion. For such reasons nearly all major global automakers are pursuing a BRIC strategy in some form or other as they attempt to gain competitive advantage by tapping the potential of these dynamic emerging markets.

Foreign manufacturers are particularly tempted by Russia's potential. The automotive market is one of the most dynamic sectors of the Russian economy. In dollar terms it has increased in value by around 30% over the last three years and further strong growth is expected. We are witnessing the beginning of an intriguing battle as competition heats up and market participants seek to strengthen their positions. The average annual increase in unit car sales is estimated by PricewaterhouseCoopers at around 7-9% per year, and the total market is rapidly approaching the 2 million units per annum mark.

As far as major foreign players are concerned we see the following picture: growth of local production of foreign brands looks set to increase by some 400% over the next seven years. This growth will be driven by a series of investments in new or expanding production plants by most of the major global manufacturers. Ford, General Motors Renault, BMW and Hyundai are already more or less established here, while new plant is already on the way from Toyota, Volkswagen Fiat, General Motors (this time in St Petersburg) Great Wall, and Cherry. Nissan will also likely be here within 2-3 years.

On the one hand, this rapidly increased competition, will give consumers greater choice, drive costs down and reduce the waiting time necessary to get a new car. On the other hand, however, since so many manufacturers have announced quite

ambitious production plans, it could be that within 5 years time the Russian automotive industry could face another problem – overproduction of cars. Overcapacity is the bane of the automotive industry worldwide and all manufacturers are consequently cautious in their investment plans. And yet the imperative of competing in new markets could drive the major players to repeat the pattern of overinvestment seen repeatedly throughout the world.

Elsewhere in the world the automotive industry is witnessing tremendous pressure to take out excess capacity. Even in America, the automotive capital of the world, we see major players closing plants and laying off significant numbers of workers. The challenge for these major players is to be bold enough to capitalise on the opportunities presented by the Russian market without over committing and ending up with non-performing investments. How to get this balancing act right is one of the toughest questions facing the industry here today. This question is made particularly complex in Russia. The huge size of the country presents complex logistics issues. The poor quality of local manufacturing custom and practice present challenges in securing local component supply. Consumer finance is still in its infancy and needs to grow strongly without losing control and generating a wave of bad debts. Dealership networks delivering quality service still need to be rolled out across Russia, presenting huge recruiting and training challenges. And the whole environment could change significantly depending on future government decisions on customs duties, environmental legislation, environmental taxes, safety legislation etc. Any major manufacturer has to manage all these questions and establish a whole infrastructure for its manufacturing plant – at the same time as playing this balancing act.

In summary a long term increase in demand for quality cars in Russia is set to generate a hectic period of investment activity throughout the automotive infrastructure in Russia. Over the medium term the rewards for the winners will be very, very attractive and the consequences for the losers will be equally painful. However, we can already confidently predict who will be the ultimate winner in this game – the customer.