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Future proof plans

Automotive industry summary

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Recent events have clearly demonstrated the extent to which the world is interconnected. The crisis which began in the US banking system has spread through the global economy as a whole – and no region has emerged unscathed. This historic moment provides an unprecedented opportunity for companies, governments and individuals to think more deeply about the sophisticated eco-systems of which we are all a part.

The current crisis has highlighted the need for new institutions, new mechanisms, new strategies and – most critically, perhaps – a different mindset among those leading the world’s most important institutions and companies. Every CEO will have to make tough decisions about what actions are required to ensure his or her company’s short-term survival. Yet none can afford to ignore the need to build a business that is agile enough to respond to new situations as they emerge, durable enough to grow over the long term and responsive to the requirements of all its stakeholders.

Redefining success, the PricewaterhouseCoopers 12th Annual Global CEO Survey, explores how CEOs are reconsidering the fundamentals of business in response to extreme operating conditions and assuming responsibility for issues that were once considered outside the scope of industry. We interviewed 1,124 CEOs around the world between September 10 and December 2, 2008. Our findings show that they are collaborating more extensively to balance the interests of increasingly influential stakeholders. They are also seeking new kinds of information to help them anticipate changes in critical business drivers.

Here, we look specifically at what the 62 CEOs in the automotive industry think, and how they are dealing with a combination of challenges such as mankind has never seen before.

The business environment

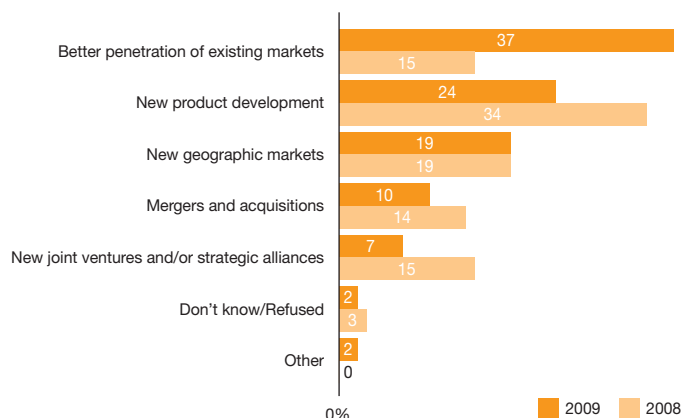
The automotive industry has been deeply affected by the global financial crisis. Some of the problems it faces – lack of credit, declining consumer confidence and falling demand for new vehicles – are familiar. But, together with new pressures such as increasing raw materials costs, rising fuel prices, tighter regulations and the need to satisfy consumer demand for cleaner, greener cars, they have combined to create a ‘perfect storm’ such as the industry has never previously experienced.

A number of big vehicle manufacturers have been forced to seek government assistance – a move that has generated considerable controversy. In November and December 2008, debate raged in the US about the extent to which the federal government should intervene to help the domestic automotive industry. Proponents argued that the economic fallout from allowing the industry to fail would be catastrophic. Critics argued that it operates with an outdated business model, so any government support for the ‘Detroit Three’ would only postpone their inevitable insolvency.

On December 19 2008, then President George W. Bush approved an emergency loan of US\$17.4 billion to General Motors (GM) and Chrysler, to be disbursed in instalments, following further congressional approval. The loans include a number of conditions, some of which give the government broad access to the two companies’ records, including information about transactions. They also give the government power of veto over expenses greater than \$100 million, and stipulate that a viable restructuring plan, including detailed projects out to 2014, must be submitted in February 2009, followed by a written progress report in March 2009.

Figure 1

Automotive CEOs concentrate on existing markets to grow



Q: Which one of these potential opportunities for business growth do you see as the main opportunity to grow your business in the next 12 months?

Base: 2009: 62; 2008: 59

Source: PricewaterhouseCoopers 12th Annual Global CEO Survey 2009

Note: Data for 2009 are based on interviews conducted in the last quarter of 2008
Data for 2008 are based on interviews conducted in the last quarter of 2007

The US is not alone in providing financial aid for its domestic vehicle manufacturers. On the same day that President Bush made his announcement, the Swedish government approved a US\$3.4 billion rescue package for Volvo and Saab. The Canadian government has also approved US\$3.3 billion in loans for any carmakers that request assistance by the end of March 2009. Germany’s carmakers and suppliers have now applied for government support, and some Asian producers may be forced to seek assistance in the future as well.

Meanwhile, many of the industry leaders have announced plans to cut production significantly; indeed, the PricewaterhouseCoopers Automotive Institute predicts that the number of vehicles manufactured globally in 2009 will be just 59.3 million. Most automotive CEOs have also been cutting costs and re-evaluating their business models, as they struggle to balance the immediate demands of survival with the need to develop an approach that is both durable in the longer term and that will position them to take advantage of the economic recovery, when it occurs.

So where do the automotive CEOs we surveyed see the greatest potential for growth? Thirty-seven percent of them believe that the main opportunities for expanding lie in further development of their existing markets. Another 24% are placing their faith in new product development (see figure 1). This represents a reversal of the priorities respondents held last year, when 34% favoured new product development and 15% better penetration of their existing markets. It probably reflects the retrenchment that has been taking place within the industry as a whole over the past few months.

The slowdown in mergers and acquisitions

The financial crisis has also brought mergers and acquisitions in the industry to a virtual halt – in marked contrast with the situation in 2007, when the market boomed, with a global disclosed deal value of US\$57.1 billion. However, some automotive CEOs anticipate more activity in 2009, not least because the need for consolidation in the sector remains a hot topic for discussion.

In an interview with a major European trade paper conducted in December 2008, Fiat CEO Sergio Marchionne predicted that there would eventually be only six major carmakers – and that only one of them would be based in the US. Other industry experts expect to see more deal-making in the components manufacturing arena, as numerous US suppliers try to escape bankruptcy or rationalise their respective sub-sectors. This may explain why 19% of automotive CEOs still plan to complete a merger or acquisition in the next 12 months, although the figure is down from 27% in 2008.

A number of automotive CEOs are also considering more collaborative arrangements. When asked which cross-border activities would play a greater role in the growth of their businesses over the next three years, 40% of those we surveyed favoured joint ventures and strategic alliances over other routes.

Powertrains will need to become greener in response to climate change pressures and scarcity of fossil fuels over the long term

Striking the balance between short- and long-term concerns

Investing for the future

Yet the key challenge currently facing most automotive executives is how to balance the pressing demands of the 'here and now' with the need to create a business that can thrive in future years. The vast majority of automotive CEOs (92%) recognise that innovation is one critical ingredient for long-term survival. But innovation often requires substantial long-term investments, which are difficult to make when a company is struggling for its very existence. It also requires a clear understanding of what customers want. Ninety-five percent of automotive CEOs recognise that information about customers is important or critical, but fifty-eight percent of these respondents say that they would like more information about the preferences of their customers, while 14% say that the information they get is inadequate.

Responding to the threat of climate change

Although the current economic crisis is 'top of mind', climate change is high on the agenda, too. Seventy-three percent of automotive CEOs believe that a new global climate deal to succeed the Kyoto Protocol is important or critical. They also recognise that, like CEOs in other industries, they must play their part to reduce CO₂ emissions. This will entail a significant investment in new technologies, green manufacturing, alternative powertrains and sustainable solutions.

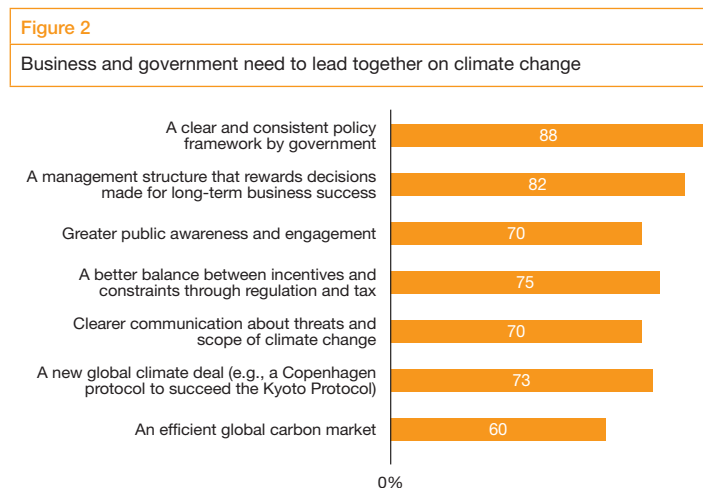
Most consumers are already familiar with hybrid vehicles, which combine a traditional gasoline combustion engine with an electric motor. However, many automotive manufacturers are exploring other options as well. GM has invested a significant amount of money in researching fuel cell technology, for example. It is also developing a plug-in electric car called the Chevy Volt, which has been touted by company executives as a 'game-changer'. The Volt is expected to go into full production in 2010.

Meanwhile, BMW launched the Mini E – the first all-electric car for daily use – at the 2008 Los Angeles Auto Show. Powered by a 150 kW (204 hp) electric motor and high-performance, rechargeable lithium-ion battery, the Mini E will initially be made available in California, New Jersey and New York.

Renault/Nissan CEO Carlos Ghosn is likewise betting on the future potential of pure electric vehicles, while diesel fuel has long been popular in Europe and clean diesel technologies are reducing pollution from nitrogen oxide emissions. Biofuels, particularly those derived from non-food sources, may also hold promise.

However, no one company, industry or government can address the threat of climate change alone. Collaborative global action and a better understanding of the business implications are

essential, as most automotive CEOs realise. Eighty-eight percent want a clear and consistent policy framework to help them respond appropriately to the issues posed by climate change (see figure 2).



Q: How important are the following measures to help you adapt your business to the issues raised by climate change? Automotive companies rating as critical or important.
Base: All respondents who state they are already making changes or plan to make changes to their business in the next 12 months/5 years/beyond 5 years to respond to the challenges posed by climate change: 60

Source: PricewaterhouseCoopers 12th Annual Global CEO Survey 2009

In fact, some governments are already providing other forms of assistance, such as financial support in dealing with pending regulations to curb the production of vehicle emissions. Prior to the recent crisis, the US Department of Energy earmarked US\$25 billion to support advanced technologies, particularly those that increase fuel efficiency. Europe's carmakers are now seeking funds to help them meet the European Union's new CO₂ emission standards.

Cultivating key skills

Yet another area in which automotive CEOs must balance sometimes conflicting short- and long-term demands is the management of human resources. Many vehicle manufacturers and components suppliers will have to make substantial capacity cuts this year. The trend towards flexible manufacturing will also translate into fewer jobs on the assembly line. Not surprisingly, then, 39% of respondents expect to reduce the number of people they employ over the next 12 months.

But though dramatic headcount reductions may be necessary, no company can afford to lose vital talent, particularly the sort of engineering expertise that drives innovation. Fortunately, most automotive CEOs are aware of the danger; 94% of respondents see access to, and retention of, key talent as critical to their companies' long-term success. They are less concerned about

finding new employees with the right skills than with holding onto the employees they already have and cultivating their existing intellectual capital – an attitude that has, perhaps, been shaped by the massive layoffs the industry endured in the first decade of the 21st century.

Managing supply chain risks

Thirty-eight percent of automotive CEOs are also worried about the security of their supply chains – again, an entirely logical response, given the prospect of a global recession and the number of components manufacturers already in serious financial difficulties. Eighty-one percent of respondents think that efficient sourcing and supply chain management is a key source of competitive advantage, and 82% that information about their supply chains is important or critical to their companies' long-term success. However, only 41% of these respondents are completely satisfied with the information they get. Forty-five percent say that they would like to receive more details, while 8% say that the level of information they receive is inadequate for their needs.

Looking forward

The automotive industry must retool its existing business model, which depends heavily on relatively inexpensive and readily available credit. It must simultaneously renew its licence to operate – and recover the trust of its stakeholders. These changes will require automotive CEOs to engage more actively with governments, customers and the general public. But they will also provide the industry with an opportunity to strengthen its reputation and customer service, two critical sources of competitive advantage.

The future viability of the global automotive sector hinges on its ability to secure sources of cash and credit, 'right-size' its operations and deliver a revolutionary fleet of energy-efficient vehicles, while being responsive to the preferences of its customers. Some automotive CEOs remain hopeful, despite these seemingly insurmountable odds. Forty percent of respondents believe that structural changes to their business models will have a positive impact on their companies, enabling them to create durable organisations that can weather the current storm and succeed in the longer term.

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Full findings of the PricewaterhouseCoopers' 12th Annual Global CEO Survey are available at www.pwc.com/ceosurvey from January 28, 2009.

For additional information regarding PricewaterhouseCoopers' automotive sector practice, please visit www.pwc.com/automotive