

Automotive



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For automotive companies in Asia, 2009 represents the beginning of an expected shift in emerging countries, particularly China and India, as they begin to exert their respective influence by expanding overseas. This is in stark contrast to the more developed markets in North America, Western Europe and Japan which are deeply troubled with many of the OEMs and associated suppliers either in the process, or on the verge, of restructuring. We are currently at an inflection point in the history of the automotive space that will see a massive shift of ownership and focus from the West to Asia.

The current industry is faced with both a structural and a market problem. With respect to the market problem, vehicle volumes in Western countries are at 30-year lows with a year-over-year decrease in sales of over 30% mainly due to the credit crisis which is preventing otherwise eligible consumers from financing vehicles. Structurally, the Western developed countries are burdened with excess capacity, a long-term inability to generate returns above their cost of capital, and a poor reaction to the realities of global competition and consumer demand. The end result is that a number of the Western OEMs, along with their associated supplier base, are available for purchase due to their necessity to survive or restructure through a formal bankruptcy process.

In Asia, the global downturn has had dramatically different effects on each country within the region. The more developed countries like Japan, Korea, Thailand, and to a lesser extent Australia, have followed Western trends with significant reductions in market demand. The companies present in these countries (like Toyota, Honda, Hyundai, etc. along with their Western transplants) are either taking a “wait-and-see” attitude, or in the case of some troubled Western OEMs, are actually shedding non-performing assets.

In other countries like Malaysia and India, reductions in demand have not been as severe, and both domestic and foreign MNCs are making very targeted investments, typically through facility expansion. If China's growth were excluded, India's growth in the auto sector would be viewed as outstanding. Over the past couple of years a number of Indian auto component manufacturers like Bharat Forge and Amtek Auto made overseas acquisitions to facilitate capacity expansion, access to technology and expanding their global footprint. However, most of these deals were done during peak valuation periods and the downturn has seen several overseas operations of Indian companies record losses. Although the global environment seems to be improving, Indian component manufacturers and OEMs will probably undertake only large strategic transactions of a game changing nature, or small deals that give them access to some new technology. The good news is that domestic sales of passenger cars and two-wheelers in India have picked up and the recently announced budget is likely to help buoy commercial vehicle sales.

China has defied the odds and posted growth in excess of 15%, and in the process has become the leading automotive market in the world by surpassing the US (estimated 2009 assembly volume for China of 10.4 million units versus 9.5 million units in the US). For China, the current global crisis has presented a tremendous opportunity to utilise its financial strength to buy up a number of assets. The Chinese government has articulated a policy calling for consolidation of the automotive industry. Many of the weaker players are in the process of being consolidated with their stronger counterparts. With respect to outbound expansion, the healthier and more capable Chinese companies are looking at purchasing technology, expanding global sales and distribution capabilities, and buying brands to expand their current vehicle portfolio. The China national policy is for Chinese automotive companies to acquire advanced technology from reasonably-sized (under \$500 million revenue) overseas entities rather than making large transactions. Although this is the official view, a number of Chinese companies are actively considering brands like Volvo, Saab, Opel and Hummer, while there are others that are looking at buying selected technology or expanding to countries or regions like Mexico, Brazil and Southeast Asia.

With the events in China and India driving much of the Asian automotive deal activity, some constraining factors exist that may temper with anticipated deals. Firstly, most companies in Asia are not sophisticated deal makers and in particular lack the expertise to buy assets out of a bankruptcy process, lacking the speed and flexibility required to be successful. This is particularly relevant for many Chinese companies looking to acquire overseas assets. Secondly, the entities typically do not have the talent to actively manage a complex global company and they will have to rely on the talent that is acquired in these transactions. One point that everyone agrees on is that the value of Western automotive assets have never been more attractive, and the industry's shift from the West to Asia will be a multi-year process. ■