

Fall 2009

China Emerges as a Leading Automotive Nation

Impact of Today's Automotive Market Conditions

Following a prolonged period of historically low sales and bankruptcy restructurings of two of the Big Three U.S. auto companies, the automotive industry experienced a temporary revival in the summer of 2009 as a direct result of the government's "cash for clunkers" incentive program. However, by September, the discontinuing of the program, along with rising unemployment and continued depressed consumer confidence, led U.S. auto sales to post a dramatic drop with subsequent signs of recovery in October. As a result of the lingering market uncertainty, automotive suppliers and original equipment manufacturers (OEMs) are acutely focused on financial liquidity and sustainable market positions. Additionally, competing foreign economies, particularly China, have emerged as commanding markets in the automotive sector.

New Car Sales

Total September 2009 auto sales were down 23 percent from a year ago and fell by 40 percent from a 15-month high in August 2009, which had been the first year-over-year increase since October 2007. The October 2009 results continued the turbulent trend in auto sales by posting an 11 percent increase over September 2009 and remained flat

from October 2008. The annualized pace of sales in October was 10.46 million units, up from 9.22 million compared with the prior month but down from October 2008's pace of 10.82 million. General Motors Company (GM) posted a year-over-year increase of 4.7 percent in October, its first annualized gain since January 2008. GM also announced it was discontinuing its Saturn brand after it failed to complete a deal with Penske Automotive Group, Inc., a Michigan-based automotive retailer. Renault SA, a France-based manufacturer, would not commit to producing the Saturn brand for Penske when GM ceases production in 2011. Chrysler Group LLC (Chrysler) posted a year-over-year decline for October 2009 of 30 percent, while Ford Motor Company's (Ford) strong 3.3 percent increase raised its market share to a level 2.5 percent higher than at the same point last year. Toyota Motor Corp. (Toyota) and Honda Motor Co. (Honda) sales in October were flat on a year-over-year basis. In the U.S. luxury car segment, Porsche Cars North America reported year-over-year increases of 15 percent while BMW AG posted a decline of 19.1 percent.¹

Overall, analysts attribute the choppy sales trend to the residual effects of the 'clunkers' program, which had drawn national attention and directed

deal-seeking buyers to the showrooms from late July through August. The consumer rush combined with manufacturers' yearlong focus on cutting production led to inventory shortfalls that resulted in an industry-wide loss of 300,000 car sales in September, as estimated by GM Sales Chief Mark LaNeve.¹ Consequently, major automakers will continue their plans to increase production in the hopes that September's dismal performance was an aberration in the industry's gradual recovery trend. Ford announced it is increasing third quarter production by 2 percent, all of which will be used to manufacture more of its fuel-efficient Ford Focus and Ford Escape models. Toyota began increasing production of the Corolla Sedan, the best-selling model in the 'clunkers' program, and has recalled more than 3,000 employees to its plant in Alabama. Moreover, both Chrysler and Honda are adding overtime at most of their factories. However, with employment and consumption remaining weak and the continued structural overcapacity in the industry, many analysts remain skeptical about when the U.S. auto sector can regain a steady financial position.²

¹ *The Wall Street Journal*, "US Auto Sales Suffer Sept Rollercoaster As Incentives Fade," October 1, 2009.

² CNNMoney.com, "Auto Sales fall as Clunkers rush ends;" *MSNBC.com*, "Clunkers Prompt Ford to boost production," August 13, 2009.

China's Surge

For the first time, the automotive market in China surpassed the United States in monthly sales in January 2009. China secured the claim as the world's new market leader by selling 8.3 million units through the nine months ended August 2009, an increase of 29 percent, as compared to 7.1 million or a decline of 27.9 percent for the United States for the comparable period. Many traditional manufacturers have benefited from this growth as evidenced by GM's sales in China being up 49.6 percent on an annual basis through August and GM plans to double its sales in China to two million over the next five years. Volkswagen AG (VW) also experienced impressive sales growth in China with its subsidiary, Volkswagen Group China, recording over 1 million units in sales in the Chinese mainland and Hong Kong through September, which surpasses its sales in the region from all of 2008. This makes China VW's largest market outside of Germany and has convinced the German-based manufacturer to invest US\$5.8 billion for additional expansion in China. The luxury car segment has also experienced strong growth in China. German-based manufacturer Daimler AG said its Mercedes-Benz (China), Ltd. division sold 44,300 units in the period January through September 2009, which is a 52 percent increase compared to the same time period last year and more than its total sales for all of 2008. Mercedes-Benz (China) sales in 2008 were 44 percent higher than the previous year.³

Analysts attribute the staggering growth in China's car sales to a thriving economy that has allowed for a sustained investment in the auto industry combined with intensified consumer demand for autos as a symbol of personal wealth. In the face of the economic recession that has reached global proportions leading to an anticipated negative GDP growth in 2009 for the United States, Japan, and much of Europe, analysts expect China to surpass its 8 percent GDP

growth target. Moreover, towards the end of 2008, China introduced a two-year stimulus plan proportionate to US\$588 billion and targeted 45 percent of those funds towards infrastructure improvements. In addition to infrastructure improvements, the stimulus plan also earmarks approximately US\$1.5 billion to a plan intended to boost the local automotive market called the Auto Industry Revitalization Plan (AIRP). The AIRP has three main goals: (1) consolidate the manufacturers while increasing production, (2) promote consumption, and (3) stimulate energy saving innovations. The government specifically stated its desire to reduce the top 14 auto makers to 10 and increase production capacity by 10 percent annually in each of the next three years. The plan aims to expand auto consumption outside of major cities by offering a subsidy for rural residents to buy new autos. Additionally, the Chinese government is offering a reduction of 50 percent in the sales tax on cars with a 1.6 liter engine or smaller, which will help spur both consumer demand and energy saving initiatives.⁴

With government incentives and increased wealth attributing to affordability of vehicles, China's 1.3 billion populace is further inspired by the symbolic social status that has accompanied the transformation of car ownership from public to private consumption. This increase in consumer demand is the primary reason why the economic forecasting company, Global Insight, has listed the Asian markets as having the largest growth potential in the global auto industry with China representing more than half of that expected growth.⁵

Changing Industry Dynamics

Industry analysts believe that the rapid growth in China's auto market has begun to ripple through the global auto industry and may drastically change its entire foundation. Automotive companies worldwide, in an effort to strengthen their market position and to capitalize on the changing dynamics,

have been increasing investments in China where the national auto policy requires local partners to hold at least 50 percent of ventures. GM has emerged from bankruptcy protection and is attempting to pare its operations in Latin America, Europe, and North America by selling off some of its most recognizable brands (Saab, Oldsmobile, Hummer, and Pontiac) and announced plans to establish its global operation base in Shanghai. GM already has two joint ventures in China and is expected to create a commercial-vehicle venture with China FAW Group by the end of the year. Many industry experts believe that GM will begin importing cars to the United States from China in 2011 and has already announced plans to export its micro-minivans from its Chinese plants to South America, the Middle East, and North America. VW, already the market share leader in China through two joint ventures with China-based manufacturers, announced that it will manufacture two new SUV models in its plants in eastern and western China, and additionally, they are joining forces with BYD Company Ltd., a China-based manufacturer of rechargeable batteries, to develop lithium-ion battery powered autos. Furthermore, Toyota announced in July 2009 its plan to introduce a new generation of a fuel-efficient Prius to the Chinese market in 2010.⁶

Auto suppliers are also poised to benefit from the boom in China. In July 2009, auto parts supplier ArvinMeritor Inc. agreed to supply components of power transmission and braking systems to Yutong Group Co., a China-based producer of buses and chassis.⁷ In June 2008, Lear Corp, a Michigan-based seats and electronic systems manufacturer, announced the acquisition of automotive fabric manufacturer China New Trend Group Co Ltd.⁷ Visteon Corporation,

³ *Cbsnews.com*, "China's 2009 Auto Sales Forecast to Hit 12.6M," September 25, 2009; *Forbes*, "Could China Make VW Number One?" September 15, 2009; *The Wall Street Journal*, "Mercedes-Benz | Jan-Sep China Sales Up 52% At 44,300 Units," October 12, 2009.

⁴ *Reuters Online*, "Myths around China's Revitalization Plan," March 26, 2009.

⁵ *Associated Press*, "China's July Auto Sales up 64 percent," August 7, 2009; *GLG*, "China's Next Revolution: Transforming the Global Automotive Industry," June 18, 2009.

⁶ *MSNBC.com*, "Toyota to sell New Prius in China Next Year," August 13, 2009; *GLG*, "China's Next Revolution: Transforming the Global Automotive Industry," June 18, 2009.

⁷ *Capital IQ*, October 31, 2009.

a Michigan-based supplier of automotive systems to manufacturers, is currently reorganizing under Chapter 11 and has been in partnership with Shanghai Automotive Industry Corporation, a components manufacturer also specializing in the production of commercial vehicles, which over the past 10 years has established itself as a leading automotive component supplier in China. This new joint venture, Yanfeng Visteon Automotive Trim Systems Co., Ltd., has a substantial business relationship with UK-based software developer Delcam plc in an effort to enhance its mould-making operations.⁸ In June 2009, Illinois-based Tenneco Inc., a manufacturer of emission control systems, announced the formation of a joint venture with Beijing Hainachuan Automotive Parts Co., Ltd., an international components provider, to manufacture and distribute emission control exhaust systems to the Chinese automakers. Tenneco has leveraged its partnership capabilities to form six joint ventures in China and has greatly

enhanced its market position.⁹

Industry experts believe that there are numerous opportunities for technology and fuel-efficient focused U.S. auto suppliers to enter the China market. As indicated by the representative few numbers of joint ventures and new deals described previously, many U.S. based auto suppliers are using the growth in Chinese auto production to capitalize on long-term growth plans by using their current business in China as a foothold to advance their Asian operations.¹⁰ Chinese auto manufacturers are also seeking growth opportunities abroad. Geely Automobile Holdings Ltd., a full-service provider of sedans and components, followed its successful 2006 acquisition of UK-based Maganese Bronze Holdings plc, a special-use car manufacturer, with the acquisition of Australian-based Drivetrain Systems International Pty Ltd. in March 2009 to bolster its gearbox production capabilities.¹¹ Also in March 2009, one of China's biggest diesel engine producers, Weichai Power Co. Ltd., bought

France-based Moteurs Baudouin S.A., a manufacturer of diesel propelled motor systems.¹¹

Industry veterans advise auto companies looking to transact in China to fully comprehend the intricacies of the venture. It is crucial that all partners are in alignment on objectives, conflict resolution, and strategy, to ensure long-term success. With cultural and technological differences between eastern and western companies, the postacquisition integration period will require strong diligence.¹²

⁸ *Eworksglobal.com*, "Yangfeng Visteon Increases Investment in Delcam Software," January 16, 2009.

⁹ *Tenneco Inc. press release*, June 5, 2009.

¹⁰ *Tenneco Inc. press release*, June 5, 2009; *Delcam press release*, January 16, 2009; *Thomson Financial*, June 13, 2008.

¹¹ *Washington Post*, "As Detroit Crumbles, China Emerges as Auto Epicenter," May 18, 2009.

¹² *GLG*, "China's Next Revolution: Transforming the Global Automotive Industry," June 18, 2009.

Select Automotive Transactions in Q3 2009

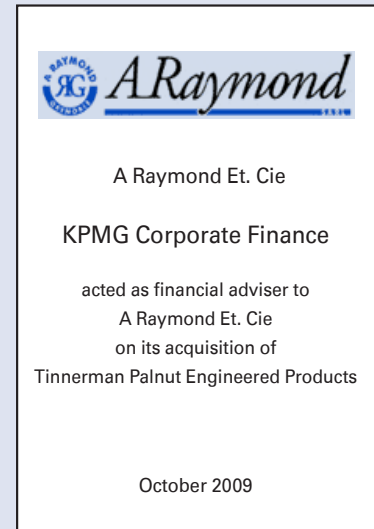
- Private equity firm **Madison Capital Partners** announced the acquisition of **SPX Filtran LLC** from **SPX Corporation** (NYSE: SPW) for an undisclosed amount. Illinois-based Filtran provides filters and transmission products through its manufacturing facilities in the United States, Germany, and China. The acquisition will provide Filtran with additional growth opportunities and signifies SPX's intention to shift its focus away from the automotive industry. (Source: *Madison Capital Partners press release*, October 2, 2009)
- Brake materials manufacturer **Akebono Brake Industry Co. Ltd.** (TSE: 7238) definitively agreed to acquire the North American brakes operations of **Robert Bosch GmbH** for approximately US\$10 million in cash. This transaction represents the beginning of Bosch's restructuring efforts and will provide Japan-based Akebono with manufacturing facilities in Tennessee and South Carolina to complement its existing North American operations. (Source: *Akebono Brake Industry Co. Ltd. press release*, September 24, 2009)
- Battery manufacturer **GP Batteries International Ltd.** (SGX: G08) agreed to acquire a 40 percent stake in **Plug-In Conversions Corporation** (PICC) for approximately US\$0.25 million. California-based Plug-In provides kits that convert hybrid cars to plug-in hybrid electric vehicles (PHEVs) with a specified focus on converting Toyota Prius models. This transaction will significantly expand PICC's market reach and will substantiate GP Batteries' offerings in the growing PHEVs market. (Source: *Plug-In Conversions Corporation press release*, September 11, 2009)
- Cold gas container producer **iSi Automotive GmbH** announced the acquisition of European Airbag Activities from **Delphi Corp.** (OTCPK: DPHI) for an undisclosed amount. European Airbag Activities provides airbags to contracted clients including **SEAT Pagine Gialle S.p.A.**, **Audi AG**, and **Daimler AG**. The acquisition solidifies iSi's market position as a supplier of full-range airbags and will also provide it with a modern research and development facility in Germany. (Source: *iSi Automotive GmbH press release*, August 31, 2009)
- Alternator remanufacturer **Motorcar Parts of America, Inc.** (NASDAQ: MPAA) definitively agreed to acquire certain assets of **Reliance Automotive, Inc.** for an undisclosed amount. Connecticut-based Reliance supplies automotive electronic components and will provide Motorcar with additional revenue streams and retail customers throughout North America. (Source: *Motorcar Parts of America, Inc. press release*, August 19, 2009)
- Steering systems and components manufacturer **JTEKT Corporation** (TSE: 6473) definitively agreed to acquire the assets of Needle Roller Bearing Business from **Timken Co.** (NYSE: TKR) for approximately US\$330 million in cash. This transaction implies a valuation of 0.5x revenue. The Needle Roller division produces a range of specialized engine bearings and has provided a strong revenue stream for Ohio-based Timken. This cross-border transaction will enhance JTEKT's production capabilities and expand its customer base in the industrial sector aftermarket. (Source: *JTEKT Corporation press release*, July 29, 2009)

Deal Spotlight

The Company: A Raymond Et. Cie (the Company) is a family-owned global designer, manufacturer, and distributor of metal and plastic fastener solutions for industrial and automotive customers.

The Situation: Tinnerman Palnut Engineered Products, Inc. (Tinnerman), a designer and producer of highly engineered fastener systems, was adversely affected by the broad downturn in the automotive industry and the restrained lending environment. As a result, Tinnerman entered into a restructuring agreement with its lenders who initiated a sale process intended to maximize creditor recoveries.

The Transaction: KPMG Corporate Finance was engaged by A Raymond Et. Cie to assist the Company in analyzing, structuring, and negotiating a transaction to purchase substantially all of the assets of Tinnerman Palnut Engineered Products. KPMG Corporate Finance leveraged its full suite of advisory services, cross-functional team of professionals from France, Canada, and the United States, and its in-depth knowledge of the U.S. bankruptcy code to prepare a transaction analysis for in-court and out-of-court acquisition options that formed the basis of the acquisition strategy and ultimately brought the transaction to signing in 90 days.



KPMG Corporate Finance

KPMG Corporate Finance provides a full suite of investment banking, advisory, and real estate services to its domestic and international clients. KPMG Corporate Finance's Industrial Markets team has significant automotive knowledge and experience with a focus on OEM, auto supplier, and auto dealer market segments. We leverage this deep industry experience across our diverse product offerings to advise clients on mergers and acquisitions, sales and divestitures, buy-outs, financings, debt restructurings, equity recapitalizations, infrastructure project finance, and

other advisory initiatives. Additionally, KPMG Corporate Finance's Special Situations Advisory Group (SSAG) serves as intermediaries to alternative sources of debt and equity capital focused on lending and investing during restrictive credit markets. We develop and implement debt restructuring strategies to de-leverage companies' balance sheets and to raise cash quickly through an accelerated M&A process.

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We welcome the opportunity to meet with you, learn more about your company's objectives, and discuss our people and capabilities.

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