FOLEY **EXECUTIVE BRIEFING SERIES**

A BETTER PATH FOR AUTOMOTIVE INVESTMENT: INDIA OR CHINA?
May 20, 2008

EVENT EXECUTIVE SUMMARY

As part of its ongoing Executive Briefing Series, Foley & Lardner held a seminar in its offices where automotive, financial and legal experts discussed the burgeoning automotive markets in both India and China.

Called "A Better Path for Automotive Investment: India or China?" the event featured Foley Partner Daljit S. Doogal; Foley Senior Counsel B. Kenneth Duck and AlixPartners senior management consultant John F. Hoffecker. The panel was moderated by Foley Partner Steven H. Hilfinger, Co-Chair of the Foley & Lardner Automotive Industry Team. Each speaker had many years' experience in doing business in Asian countries, particularly in the automotive arena.

John Hoffecker kicked off the session by noting that a growing consumer demand characterizes the automotive markets in both India and China. OE manufacturers located there include some of the strongest growth companies in the world, with a high return on investment. Many key suppliers, in turn, are finding that their returns on invested capital to be substantially higher in these markets than in North America.

Unlike in the U.S., where manufacturers and government policy have sent mixed messages about the commitment to maintain a viable heavy industry on its shores, government support and sponsorship of auto manufacturing in both India and China is strong. U.S. businesses have tended to find economies of scale by outsourcing commodity manufacturing in recent years, finding both cost reduction and growth opportunities overseas.

Hoffecker outlined a number of trends in the Chinese and Indian automotive industries, including both opportunities and challenges. Current plant utilization in China, for example, is operating on average below 60 percent. Additional capacity coming on line in these markets will continue to create downward pressures on vehicle prices in these markets.

Although automotive export revenue is increasing in China, the export market is still fragmented and there is little penetration into international markets. On the whole, Chinese OE manufacturers remain behind Western manufacturers in technical production know-how.

Chinese manufacturers are trying to remedy this situation by forming partnerships with global OEMs, where they can achieve a competitive advantage from the access to technology and well-known brand identification that flow from the working relationship. According to Hoffecker,

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more than 50 percent of Chinese auto industry firms are considering some sort of global mergers or acquisitions.

Both Hoffecker and the next speaker, Daljit Doogal, noted the tremendous growth of the Indian automotive industry since deregulation in 1991, which has historically averaged an increase of 18 percent a year. About seven years behind China according to Hoffecker, India’s industry is predicted to be the world’s fifth largest auto producer, doubling in size by 2010, and then doubling again by 2016.

Seeing the auto industry as a pillar for future economic growth, the Indian government has developed a direct investment program to attract foreign global manufacturers.

With a focus on small car development, forecasters see the upward trajectory based on growing demand from a sizable middle class with disposable income. Significant recent investments in India by OEMs like Renault, Toyota, Honda, Daimler, GM, Ford, Hyundai and BMW have proven the model of starting small, working with Indian companies and securing long-term agreements.

Still to be reckoned with is India’s long and cumbersome litigation process, which puts up legal roadblocks, plus hard-to-enforce intellectual property protections. But these are changing, Doogal noted, and India’s growth potential—coupled with an English-speaking, skilled and inexpensive labor force—are distinct advantages to doing business there.

Attorney Ken Duck rounded out the panel by pointing to current areas of concern with China’s auto market: rapid sales volume, but production overcapacity; too many players; falling prices; increasing costs and uncertain export expectations.

Although an entry-level workforce is readily available in China, it has a low-skill base, while skilled engineers and middle management expertise are scarce indeed. At the same time, current pressures from labor and governmental compliance regulations are driving up costs.

Investors need to be aware of the problems inherent in ventures with state-owned entities, Duck cautioned, with heavy M&A regulations, anti-monopoly legislation, export-import restrictions and potential conflicts of interests.

For more information about this topic, please contact Steve Hilfinger (shilfinger@foley.com), Daljit Doogal (ddoogal@foley.com), or Ken Duck (kduck@foley.com).