

Capital Confidence Barometer

Automotive industry

A new paradigm?

Global M&A activity and volatility coexist

About this survey

Ernst & Young's Capital Confidence Barometer is a regular survey of senior executives from companies around the world conducted by the Economist Intelligence Unit (EIU).

Our panel, the "Ernst & Young 1,000" is comprised of selected Ernst & Young clients and contacts and regular EIU contributors.

This automotive subset of our findings gauges corporate confidence in the economic outlook and identifies boardroom trends and practices in the way companies manage their capital agenda.

Profile of respondents

- ▶ Panel of over 1,000 executives surveyed in July and August 2011; 96 executives from the automotive sector
- ▶ Companies from 22 countries, including Australia, Brazil, China, France, Germany, India, Japan, Russia, UK and the US
- ▶ 50% of respondents are CEOs, CFOs and other C-level executives
- ▶ Company revenues ranged from US\$250 million to over US\$20 billion



Our fourth Capital Confidence Barometer in the automotive industry predicts a new paradigm: corporate M&A activity and extreme market volatility coexisting. There is a surprising improvement in the appetite

to do deals over the next 12 months as respondents appear more resilient against the current market turbulence.

Leading companies have spent three years focusing on reducing financial risk, improving operational fitness and learning to live with volatility. Consequently, balance sheets are stronger with less leverage, many companies can draw upon cash war chests, capital market conditions are generally improving and earnings growth outlooks are positive.

These conditions have helped foster an improving M&A environment with a continued focus for growth in emerging markets. However, some barriers do remain. Mounting regulatory pressures could potentially impede growth, and there is the fundamental question of the economy. While our respondents' M&A attitudes are remarkably robust given the current environment, a slump into a double-dip global recession or another banking crisis could drastically change corporate outlooks.

Our latest findings again underline one critical point: how companies manage their capital agenda today will define their competitive position tomorrow. How they raise, invest, optimize and preserve their capital is vital to their future success. The Barometer clearly shows that many leading companies are positioned to thrive in the current automotive marketplace, while at the same time are prepared to address future uncertainty.

Pip McCrostie – **Global Vice Chair,**
Transaction Advisory Services

Jim Carter – **Americas Automotive Industry Leader,**
Transaction Advisory Services

The Capital Agenda

Based around four dimensions, it helps companies consider their issues and challenges and understand their options to make more informed capital decisions.

1. **Preserving capital:** reshaping the operational and capital base
2. **Optimizing capital:** driving cash and working capital and managing the portfolio of assets
3. **Raising capital:** assessing future capital requirements and assessing funding sources
4. **Investing capital:** strengthening investment appraisal and transaction execution

Survey highlights

Automotive respondents indicated that:

- ▶ 64% felt that the global economy was either stable or improving
- ▶ 89% expect to maintain or increase their workforce over the next 12 months
- ▶ 32% plan to refinance loans or debt obligations in the next 12 months
- ▶ 39% expect to make acquisitions in the next 12 months
- ▶ 23% see divestments as likely or highly likely in their organization over the next 12 months
- ▶ 55% indicate growth as their company's primary focus in the next 12 months

Economic outlook

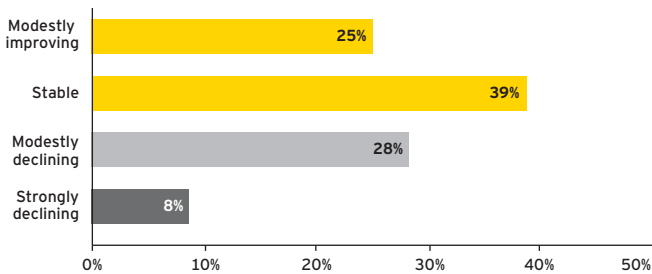
Global economic outlook resilient despite volatility

July and August marked a return to intense volatility not seen since the early days of the economic crisis in 2008. The US credit rating downgrade, debt crisis in the Eurozone and weakening economic data from around the world sparked dramatic stock market activity and, ultimately, the global repricing of risk.

Nonetheless, automotive respondents expressed optimism regarding the state of the global economy with 25% of respondents indicating the economy is improving and 39% indicating the economy is stable.

64% of automotive respondents said that they felt the global economy was either stable or improving, a similar sentiment echoed by our global survey participants.

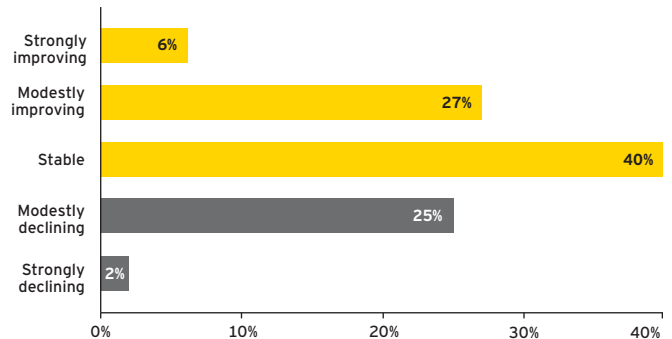
What is your perspective on the state of the global economy today?



Confidence in local economies rising

When asked their perspective on the state of their local economies, 73% of automotive executives cited a stable or improving environment in both October 2011 and April 2011, while 70% shared that view in October 2010. Surprisingly, in the face of significant volatility beyond local borders, confidence remains strong. This is driven by expected corporate earnings growth, increased cash balances and reduced debt.

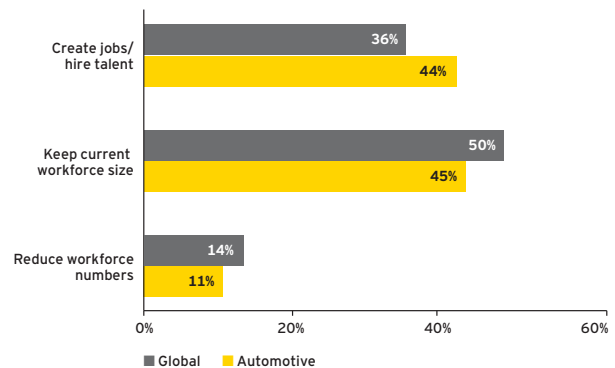
What is your perspective on the state of the local economy today?



Employment outlook brightens

Despite some high-profile announced layoffs, 86% of the Ernst & Young 1,000 expect to maintain or increase their workforce over the next 12 months. Within the automotive industry, a greater number of respondents (89%) hold the same view.

In regard to employment, which of the following does your organization expect to do in the next 12 months?

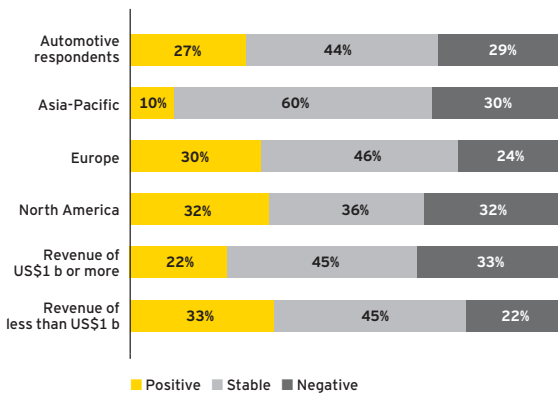


Access to capital

Confidence in credit availability improving

Seventy-one percent of automotive respondents believe credit availability is stable or positive. Capital markets are somewhat more receptive to automotive companies of various geographies and sizes than in the recent past as many companies have reduced debt loads and strengthened their balance sheets as a result of the rebound in vehicle production.

Please indicate your level of confidence in credit availability at the global level.

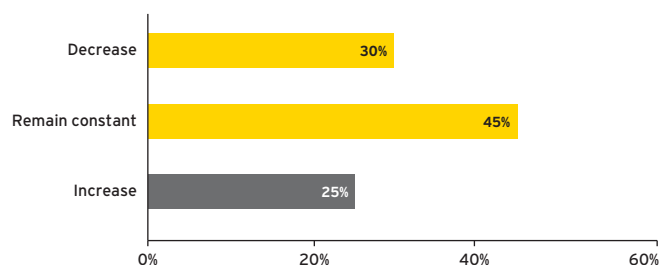


Trend toward debt reduction continues

Balance sheet leverage remains low: only 13% of respondents have a debt-to-capital ratio above 50%; 64% of respondents are below 25%.

Additionally, maintaining or lowering leverage remains an important theme in automotive. Seventy-five percent of automotive respondents believe their debt-to-capital ratio will decrease or remain the same in the next 12 months.

How do you expect your debt-to-capital ratio to change over the next 12 months?

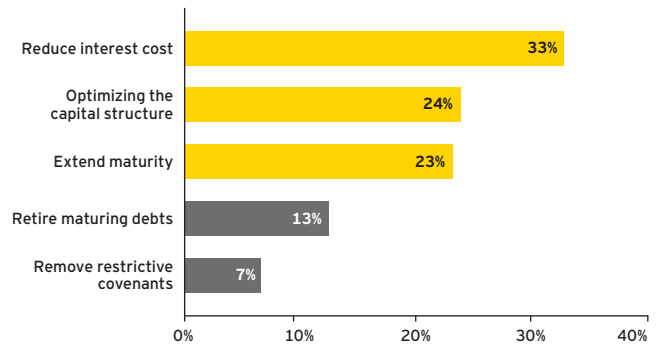


Attractive capital conditions increase refinancing activity

The majority of respondents (68%) do not intend on refinancing debt over the next 12 months as many companies have already materially reduced indebtedness, extended maturities or accomplished a refinancing. Despite this, however, the percentage of respondents planning to refinance in the next 12 months increased to 32% in October 2011, compared with 15% of respondents in April 2011. Respondents indicate that the primary purpose of refinancing is to reduce interest rates, optimize their capital structure and extend maturities.

Capital markets are currently far more receptive to larger cap, frequent issuers than to middle market borrowers. As the industry continues to improve, credit ratings for many companies within the sector have finally begun to trend toward investment grade.

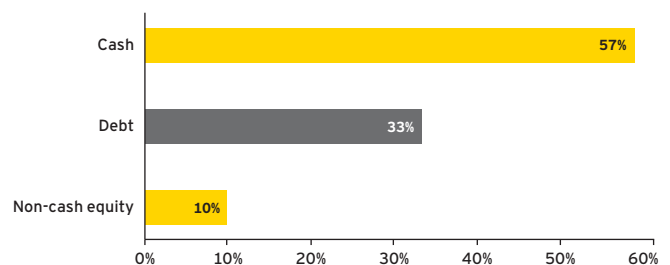
What will be the primary purpose of your refinancing?



Cash balances continue to supplement acquisition financing

Companies have continued to build cash reserves and are now poised to seize growth opportunities. Over half (57%) of automotive respondents indicated cash would be the primary source for deal funding in the next 12 months. Thirty-three percent cited debt as the primary funding for deals. However, 63% of respondents planning on using debt to fund deals have indicated they would finance less than one-third of the acquisition.

What is your likely primary source of deal financing in the next 12 months?

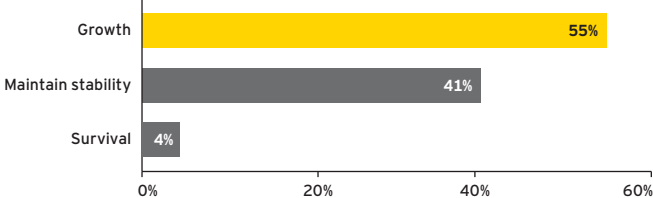


Growth

Automotive focusing on growth

Stronger demand and production schedules have driven improved earnings. Automotive companies are now better prepared for difficult economic conditions in the future than compared to 2008. Reduced cost structures and strengthened balance sheets have enabled companies to focus on growth initiatives, despite economic turmoil. Fifty-five percent of respondents indicate growth as their company's primary focus in the next 12 months; only 4% cite survival as an imperative.

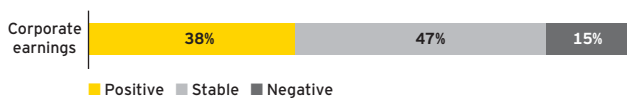
Which statement best describes your organization's focus over the next 12 months?



Corporate earnings outlook: stable to positive

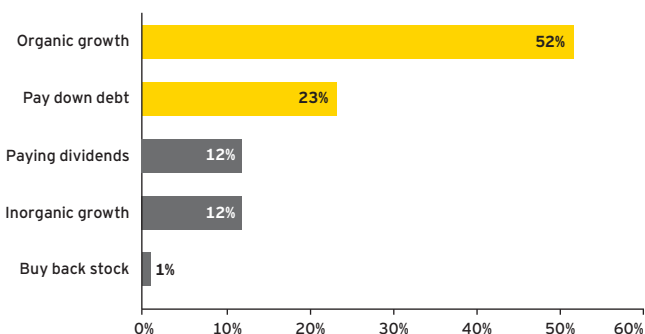
Additionally, measures taken during the financial crisis now have 85% of respondents feeling confident in the corporate outlook for stable to positive earnings outcomes, with only 15% of respondents reporting a negative outlook on corporate earnings trends around the globe.

Please indicate your level of confidence in corporate earnings at the global level.



For those with excess cash flow in the next 12 months, nearly two-thirds of all companies (64%) prioritize investing in growth, both organic and inorganic, followed by paying down debt (23%).

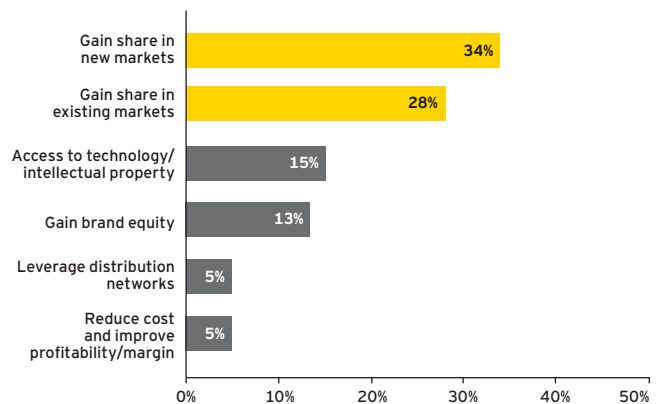
If you have excess cash, which of the following will be your priority over the next 12 months?



Quest for growth drives deal activity

Sixty-two percent of respondents said the primary purpose for making acquisitions is to gain market share in new and existing markets (products or geography). Other drivers, such as cost synergies, distribution network leverage and access to technology, are less important factors.

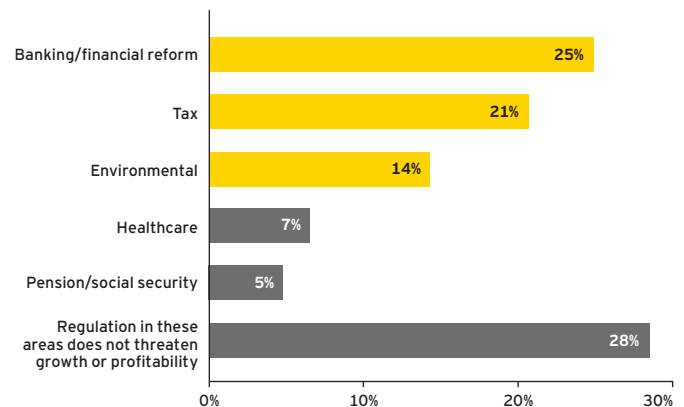
What are the main drivers of your company's planned acquisition in your chosen market or country?



Regulatory risks could threaten growth agendas

Seventy-two percent of respondents are concerned that mounting regulatory pressures across a number of areas could potentially impede growth. Banking and financial reform as well as tax regulation are the greatest of these concerns.

What areas of regulation pose the most significant risks to growth and profitability for your organization over the next 12 months?



Mergers and acquisitions outlook

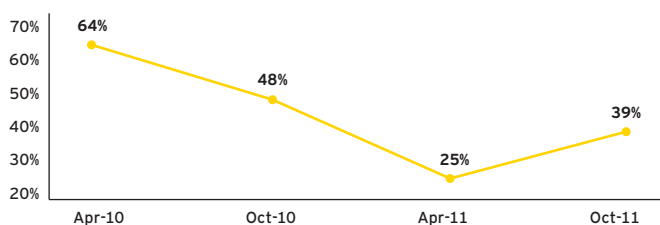
Deal activity and volatility now coexist: a new paradigm

In an unprecedented departure from the historical norm, the outlook for deal volumes is stable or improving against a backdrop of significant short-term volatility.

Automotive deal-makers' appetite to acquire has increased significantly, with 39% of respondents expecting to make acquisitions in the next 12 months, compared with 25% in April 2011. Additionally, respondents at companies with over US\$5 billion in revenue expressed a stronger desire to execute acquisitions with 53% expecting to make an acquisition within the next 12 months.

Many companies have learned to adapt and operate in a new and uncertain world. They are well-positioned to seize opportunities and plan to do so, as many have reduced their financial risk and have the ability to take on more business risk.

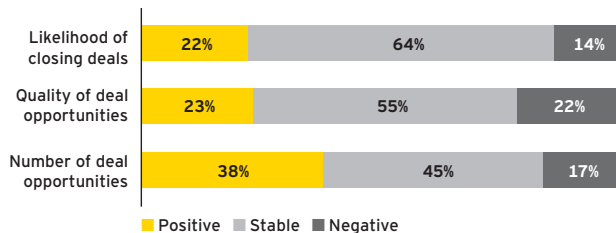
What percent of respondents expect to make acquisitions in the next 12 months?



Favorable environment for deal-making

Automotive respondents are broadly comfortable with the deal environment in terms of quantity and quality of deals, as well as likelihood of closing deals.

Please indicate your level of confidence in the following at the global level.



Emerging market opportunities fill deal pipelines

As automotive OEMs source more global platforms, companies are continuing to pursue emerging market investment opportunities. However, there is a desire to balance portfolios between emerging and developed markets to better position for growth and profitability.

Three of the top five most attractive investment destinations are emerging markets – China (1), India (2) and Brazil (4). The Asian emerging markets are among the most attractive due to their high growth potential, expanding domestic demand and resilience to current market volatility.

Germany and the US also remain attractive based on the size and diversity of their economies as well as the focus of established automotive companies in these regions. Additionally, other low-cost countries, such as Mexico and Singapore, remain attractive.

What are the most likely countries where you will make outbound investments?

1. China
2. India
3. Germany
4. Brazil
5. US

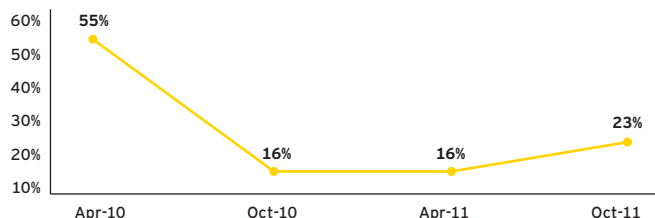
The most popular emerging market destinations beyond the BRICs are:

1. Singapore
2. Mexico
3. South Africa

Increasing appetite for divestments

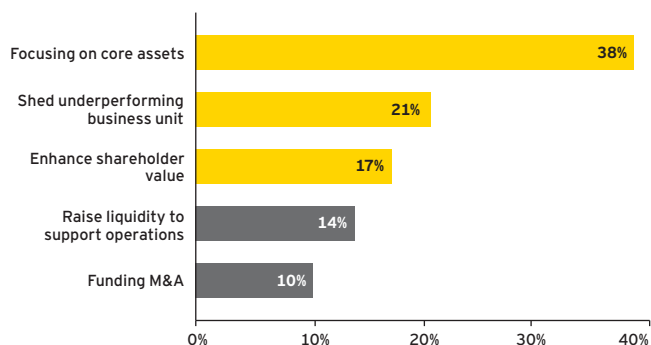
The willingness of companies to divest assets is the primary driver of increased deal activity. Twenty-three percent of respondents see divestments as likely in their organization over the next 12 months, an increase from 16% at April 2011.

What percent of respondents expect to make divestments in the next 12 months?



The top three reasons for executing planned divestments are focusing on core assets, shedding underperforming business units and enhancing shareholder value.

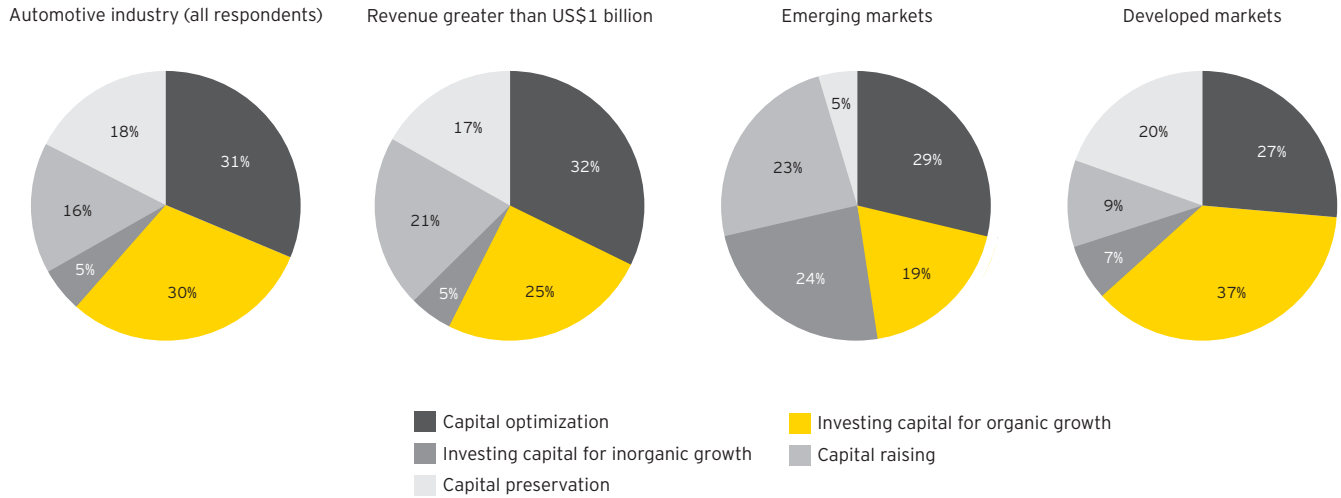
What are the main drivers of your company's planned divestment activity?



Understanding your Capital Agenda

A strong Capital Agenda needs to be at the heart of all strategic boardroom and management decisions. The findings of our Capital Confidence Barometer provide useful insights into the ways companies are optimizing, investing, preserving and raising capital.

We asked survey participants on which capital management issues their company is placing the most attention and resources.



Automotive companies have improved earnings, reduced costs and strengthened balance sheets. Profitable growth is now the primary focus, despite economic turmoil. Capital optimization is the single largest priority across the industry; however, capital raising and investing initiatives are the priority of over half of all automotive respondents.

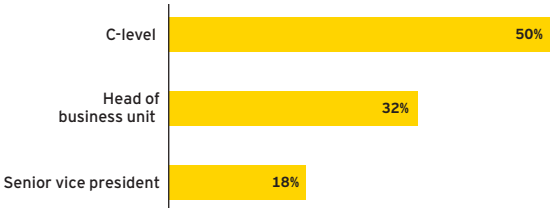
Capital raising is a greater priority for automotive companies with revenues greater than US\$1 billion, who are primarily looking to take advantage of improving credit markets to reduce their interest costs and optimize their capital structures.

Furthermore, capital management priorities clearly differ between regions. Inorganic growth (M&A) and capital raising have become particularly important to respondents in emerging markets. Investing and raising activities in these areas were a priority for 67% of respondents in October 2011, an increase from 44% in April 2011. Compared to emerging markets, developed markets show a much greater focus on investment in organic growth, a theme that has not changed substantially since April 2011.

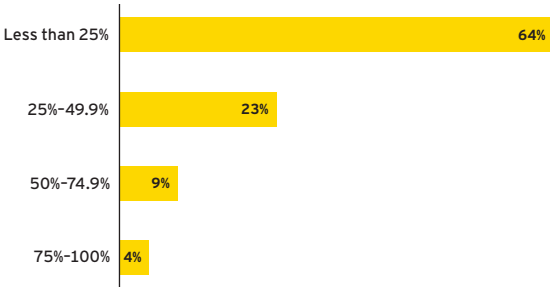
These findings underline one critical point: how companies manage their capital agenda today will define their competitive position tomorrow. How they raise, invest, optimize and preserve their capital is vital to their future success.

Survey demographics

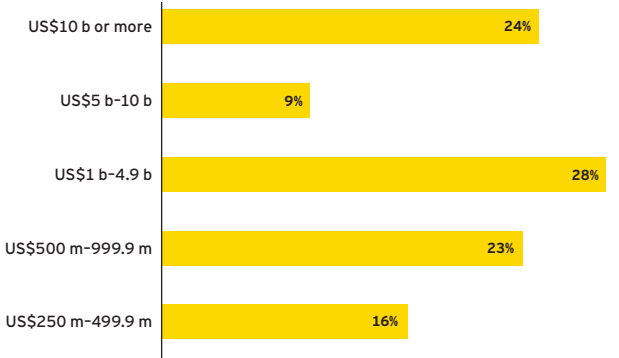
What is your position in the organization?



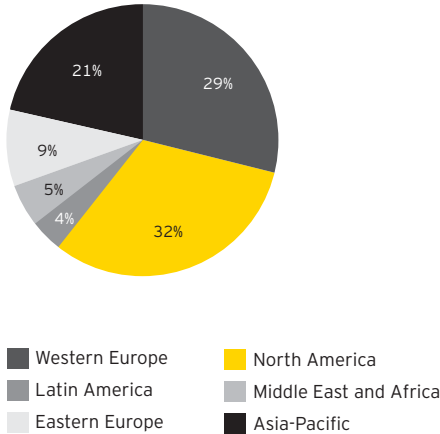
What is your current debt-to-capital ratio?



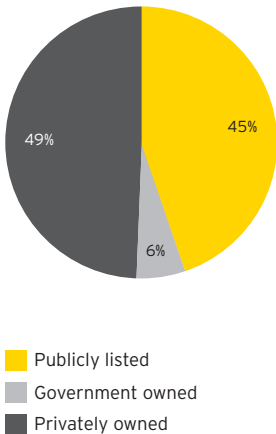
What are your company's annual global revenues in US dollars?



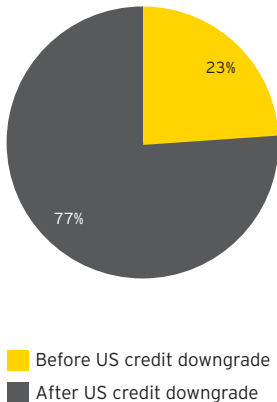
What region is your company based in?



What best describes your company?



Point at which respondents answered survey



Contacts

If you would like to discuss your company's capital agenda, please contact your existing Ernst & Young advisor or any of the contacts listed below.

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Acknowledgements

Our special thanks go to the Ernst & Young 1,000* for their contribution to this survey.

* The Ernst & Young 1,000 comprises an EIU panel of senior executives and selected Ernst & Young clients and contacts who participate in the Capital Confidence Barometer on a biannual basis. The surveys are conducted on an independent basis by the EIU.

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How Ernst & Young's Global Automotive Center can help your business

The global recession reset the automotive industry landscape. As the industry recovers, automotive companies across the value chain must focus on profitable and sustainable growth, financial and operational stability, investments in new technologies and seizing opportunities in high-growth markets. If you lead an automotive business, you need to anticipate trends, identify implications and make informed decisions that support your business goals. Our Global Automotive Center enables our worldwide network of more than 7,000 industry-focused assurance, tax, transaction and advisory professionals to share powerful insights and deep sector knowledge with businesses like yours. These insights, combined with our technical experience in every major global automotive market, will help you to accelerate strategies and improve performance. Whichever segment of the automotive industry you are in – from component suppliers to commercial or light vehicle manufacturers or retailers – we can provide the insights you need to realize your potential today and tomorrow.

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