



The Automotive Industry

STRATEGY AND BUSINESS IMPROVEMENT CONSULTING

Minority Business Development: Economic Value And Benefits

MED Week 2001

**The
Asaba
Group**

This Report Was Written And Produced For:

U.S. Department of Commerce

Minority Business Development Agency

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By:

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This analysis on the economic value and benefits of the automotive industry was prepared by The Asaba Group and is the Group's interpretation of the economic trends of the automotive industry. The study is not a Commerce Department report, but was developed for the sole purpose of discussion amongst industry experts. The conclusion and analysis of the report do not necessarily reflect the views of the U.S. government.

Express Gratitude And Acknowledgement For Contributions To The Project:

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State of Minority Business Development

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Project Charter

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Develop A Report That Shows The Economic Value Of Doing Business With Minority-Owned Companies

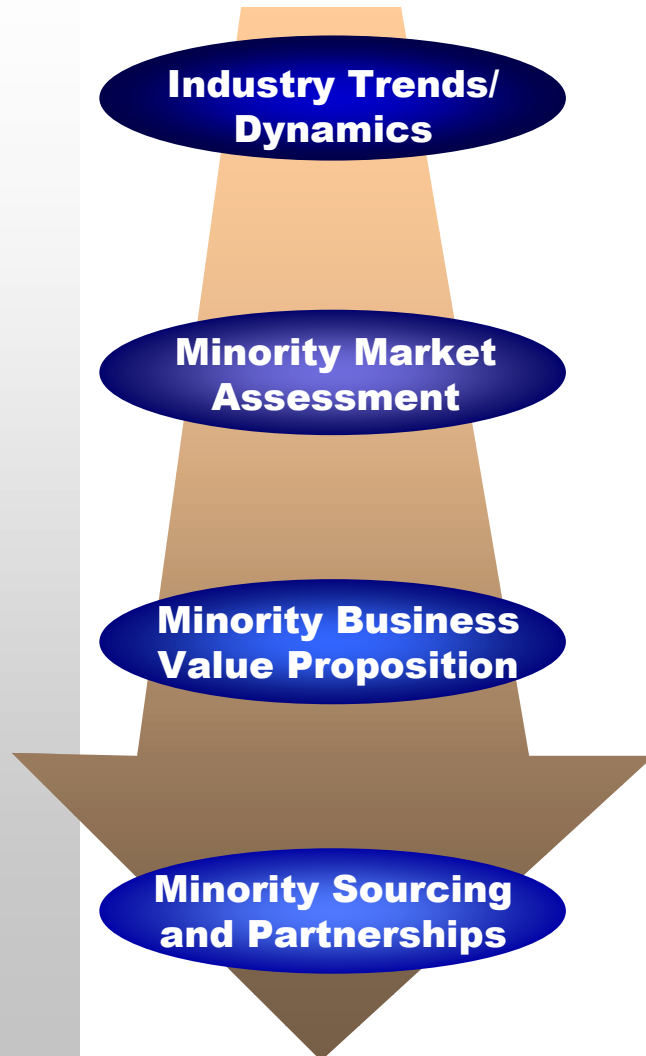
Business case should place emphasis on the following:

- Focus on business imperatives and free market forces
- Leverage minority demographic shifts and emerging purchasing power
- Ensure alignment with current industry trends and strategies of key players
- Drive increased Fortune 500 participation in minority business development

**The Asaba Group Retained To Assist In
Building the Business Case**

Project Approach

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- Macroeconomic / Market Forces
- Supply Chain Realities
- Major Players' Response
- Shareholder Value Created
- Market / Customer Opportunities
- Revenue Expansion Opportunities
- Channel / Market Access
- Brand Differentiation
- Supply Chain Flexibility
- Current State
- Issues / Challenges
- Future Perspective

Executive Summary

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Long-term competitiveness of a corporation lies in developing business models which create both shareholder and stakeholder value

- Minority Business Development initiatives create value for both shareholders and key stakeholders
- Automotive Manufacturers realize the strategic value of Minority Businesses

Automotive Manufacturers are in search for new market revenue opportunities

- Minority Automotive markets are estimated at \$112 Billion and growing
- Minority consumers will account for significant share of future revenues

Positive correlation exists between market share gains and minority suppliers and dealers development

- Minority suppliers and dealers contribute to Automotive Revenues

Minority suppliers weak value chain positioning largely a function of current metrics and measurement

- Focuses on “quantity of spend” rather than “quality of spend”
- Metrics not reflective of industry realities – Supply Chain transformation and competitive dynamics

Executive Summary

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Positive correlation between “Doing Business With Minority Enterprises” and above-average Market share

What we observe in analysis of Top 15 Minority States (78% of total minority population)

- In states with high concentration of Domestic minority suppliers
 - Total Big 3 automotive market share is greater than Big 3 national average
- In states where Big 3 minority dealers are under-represented (compared to national average) versus import minority dealerships
 - Big 3 automotive market share is lower than national average
- States with both high concentration of Big 3 minority suppliers and equal or greater Big 3 minority dealership representation
 - Big 3 market share much greater than national average

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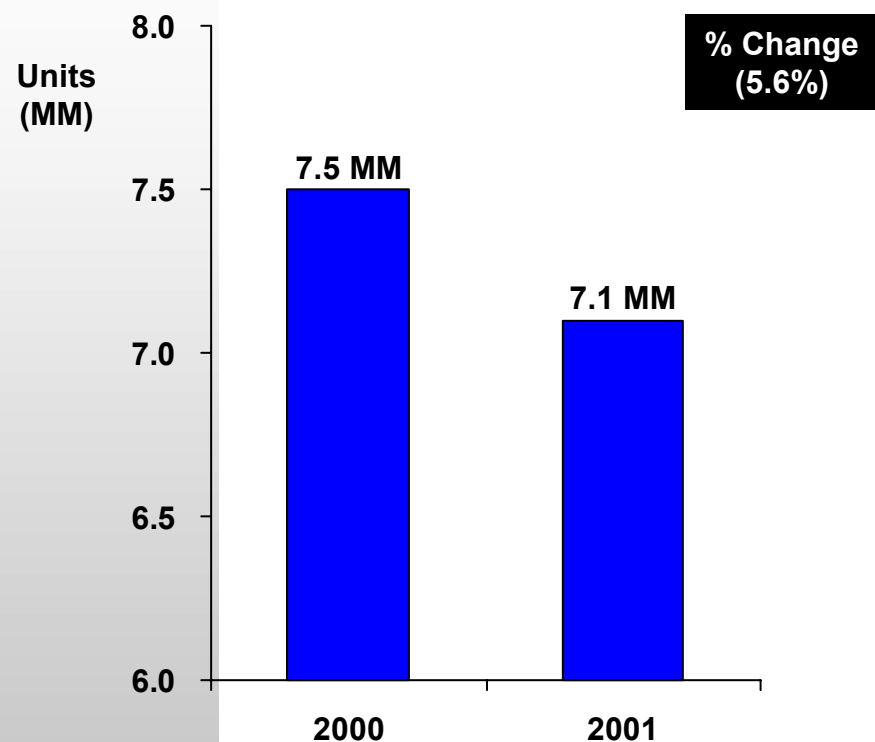
Minority Automotive Markets 23-31

Minority Business Value Proposition 32-40

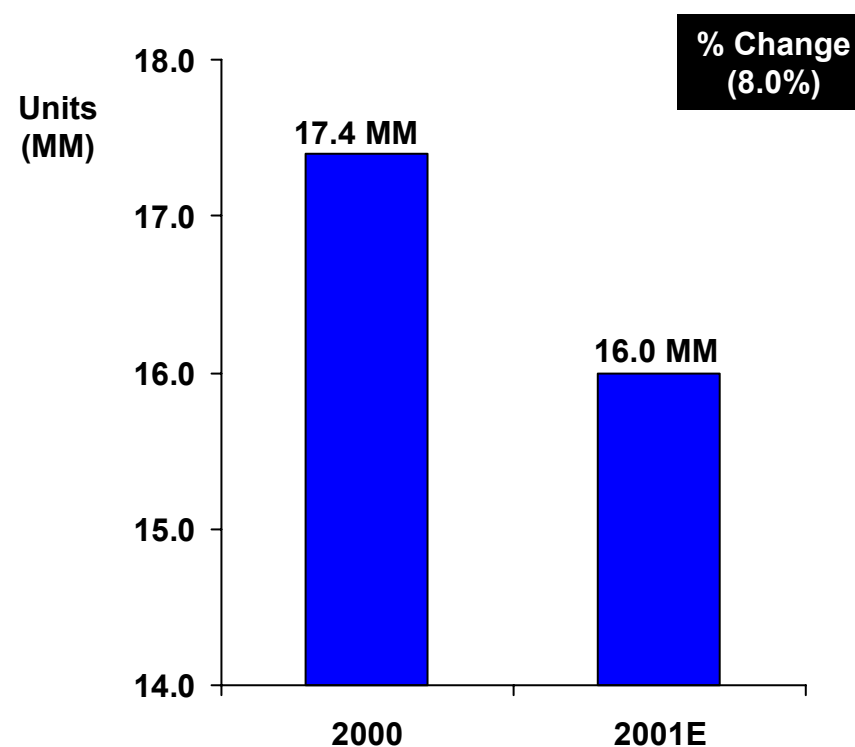
State of Minority Business Development 41-55

Automotive Sales On A Downward Trend After Record Year In 2000

January to May Sales



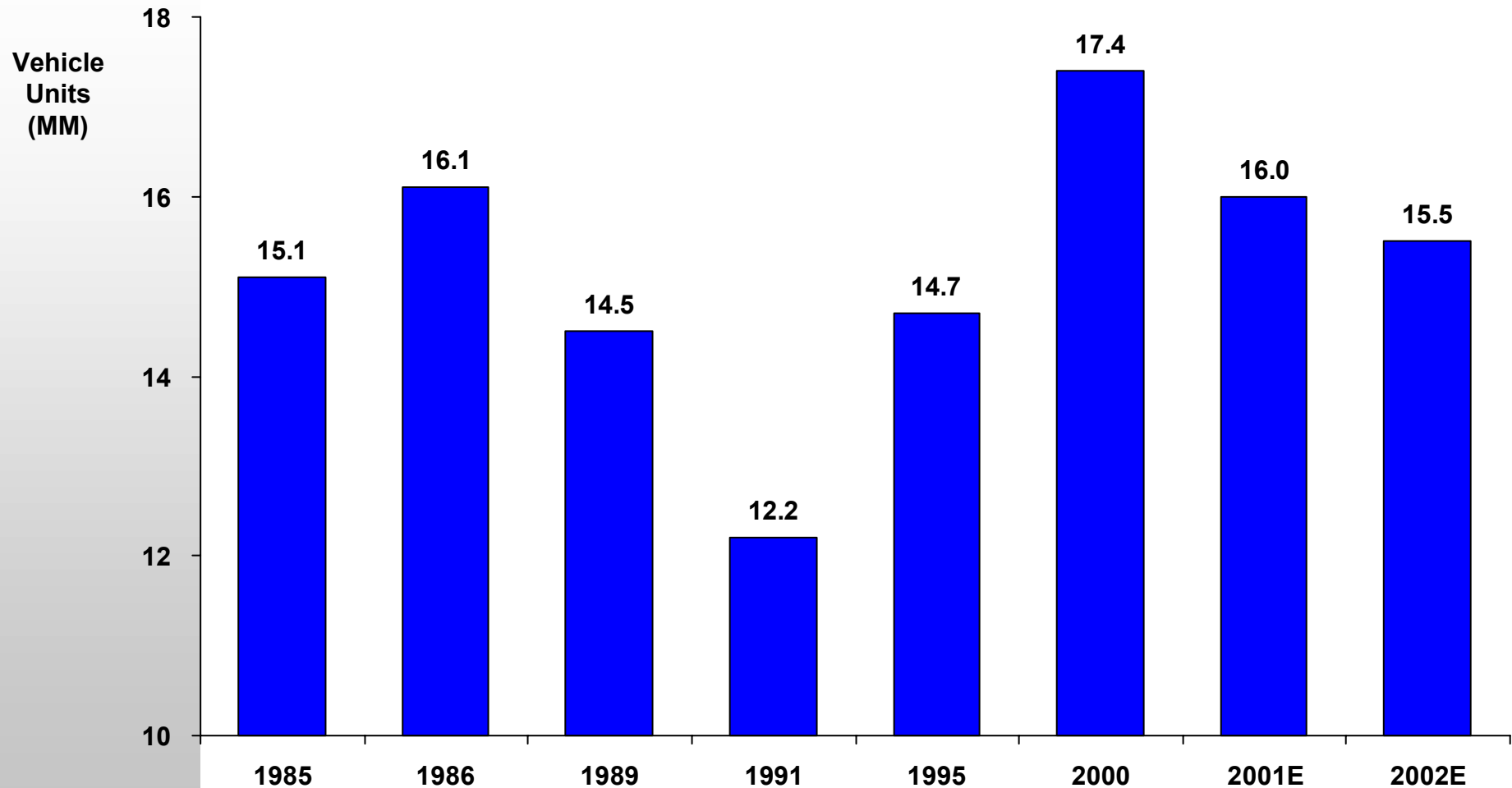
Annual Sales



Strong Impact On Industry Performance

Automotive Future Sales Likely To Continue On A Downward Trend

U.S. Light Vehicle Sales

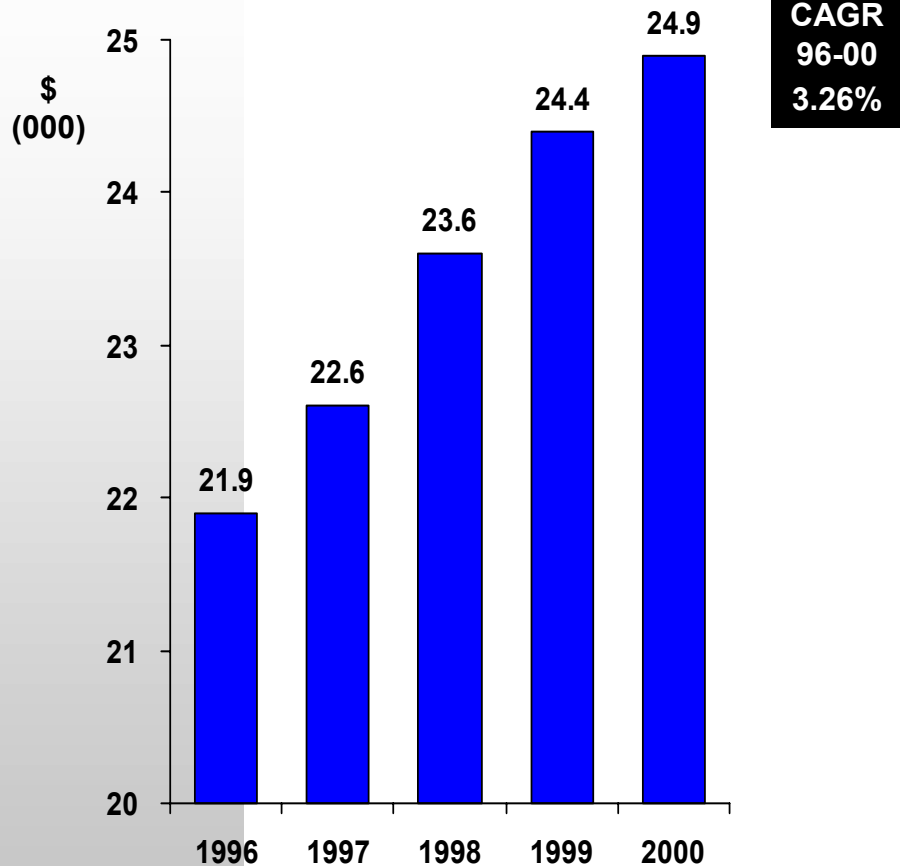


SOURCE: PricewaterhouseCoopers, Salomon Smith Barney, Asaba Group Analysis

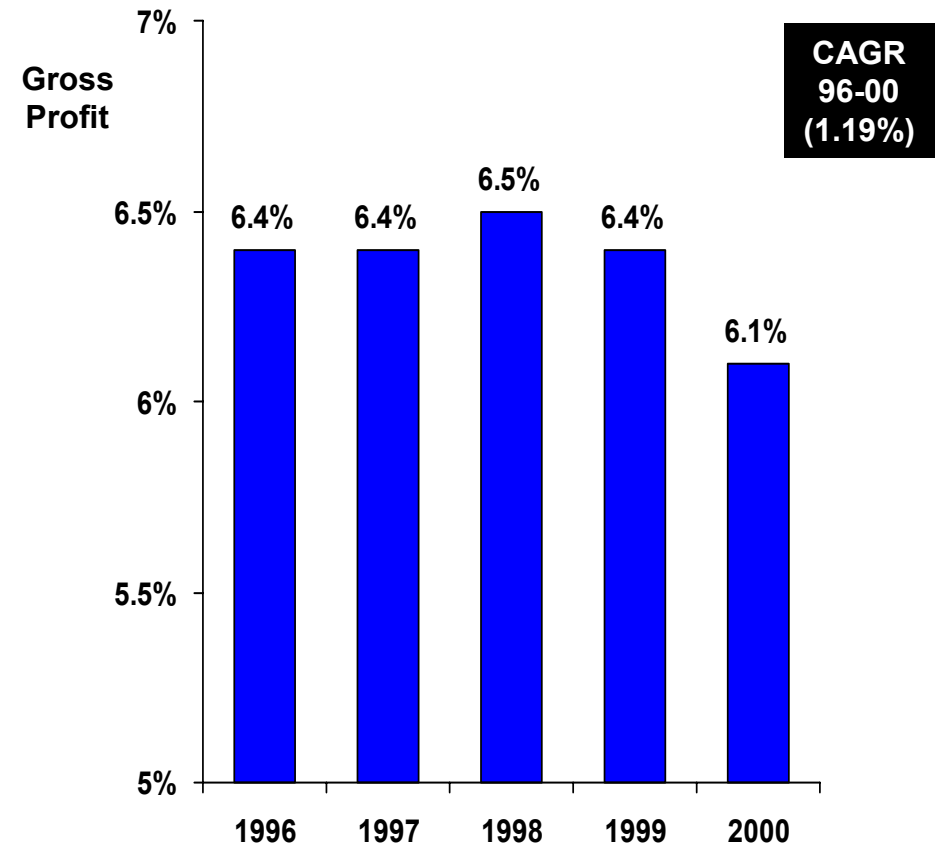
While Sales Have Soared In Prior Years, New Vehicle Profits Have Been Flat

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Average New Vehicle Price



New Vehicle Retail Gross Profit



Expect Declining Profits With Slowdown

Industry Players Feeling The Pain From Slowdown

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General Motors first quarter profits down 88%

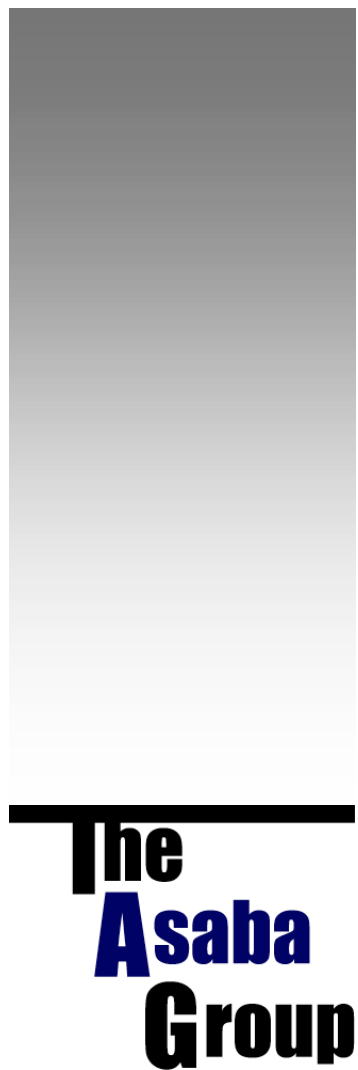
- General Motors cutting 10,000 jobs and ditching the Oldsmobile brand

DaimlerChrysler announces widespread restructuring of U.S. operations

- Chrysler Group cuts production by 15% and plans to cut workers by 20%
- Total restructuring costs estimated at \$5 Billion

Ford Motor Company has:

- First quarter production down 16% from 2000 levels
- Second and third quarter production rate expected at 14% and 10% below production rate in second and third quarter of 2000, respectively



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Key Highlights

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Consumers view cars to be similar in quality and features

- Brand differentiation not as distinct
 - Reflected in consumer willingness to pay a price premium

Automotive manufacturers have achieved competitive convergence in each product category

- e.g. Luxury cars: Ford (Jaguar/Lincoln), GM (Cadillac), Toyota (Lexus), DaimlerChrysler (Mercedes-Benz)

Declining profitability driving Automotive Manufacturers (OEM's) to seek new profitable revenue segment

- After sales revenues more profitable and experiencing strong growth

Large automotive suppliers gaining more influence on product attributes (quality, differentiation, etc.)

- New core technologies rapidly diffused among OEM customers to leverage R&D investments

Key Highlights (cont'd)

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After-sales revenue sources concentrated with category competitors (non-automotive) and automotive dealers

- Retailers and dealers consolidating and becoming multi-franchised
 - Reducing dependence on any one auto manufacturer
- After-sales revenue concentrated with dominant customer-focused competitors

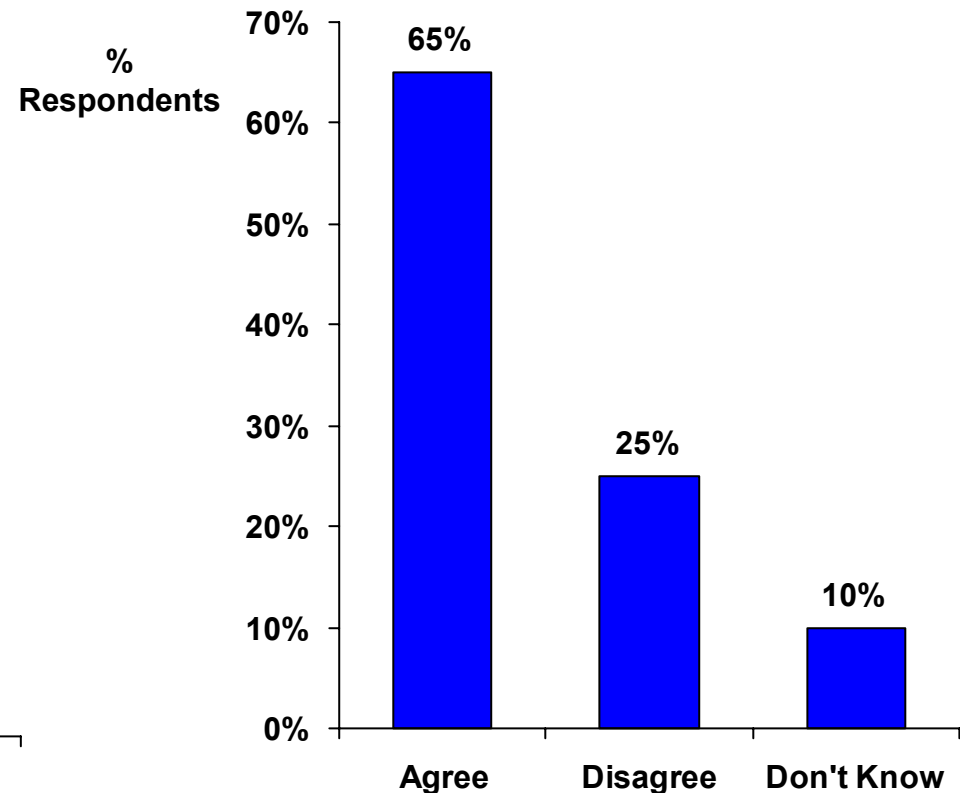
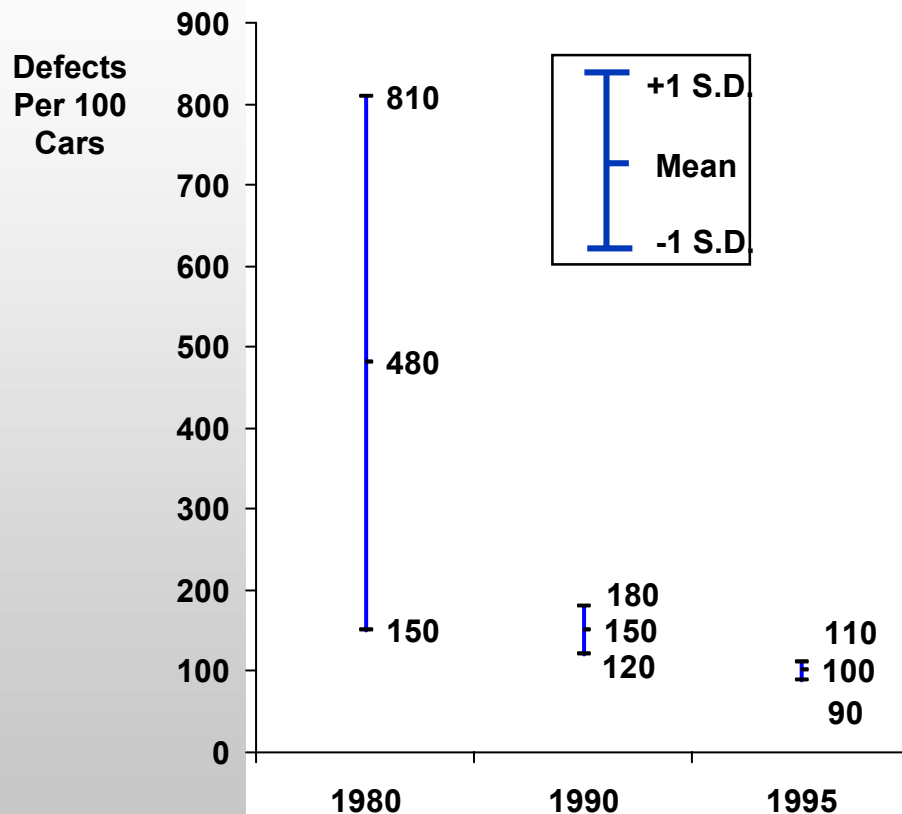
Automotive manufacturers desire to increase shareholder value by focusing on consumer

- Product-life management new mantra with automotive manufacturers

Product-Based Differentiation Declining Among Automotive Manufacturers

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Vehicle Quality Convergence (U.S.)

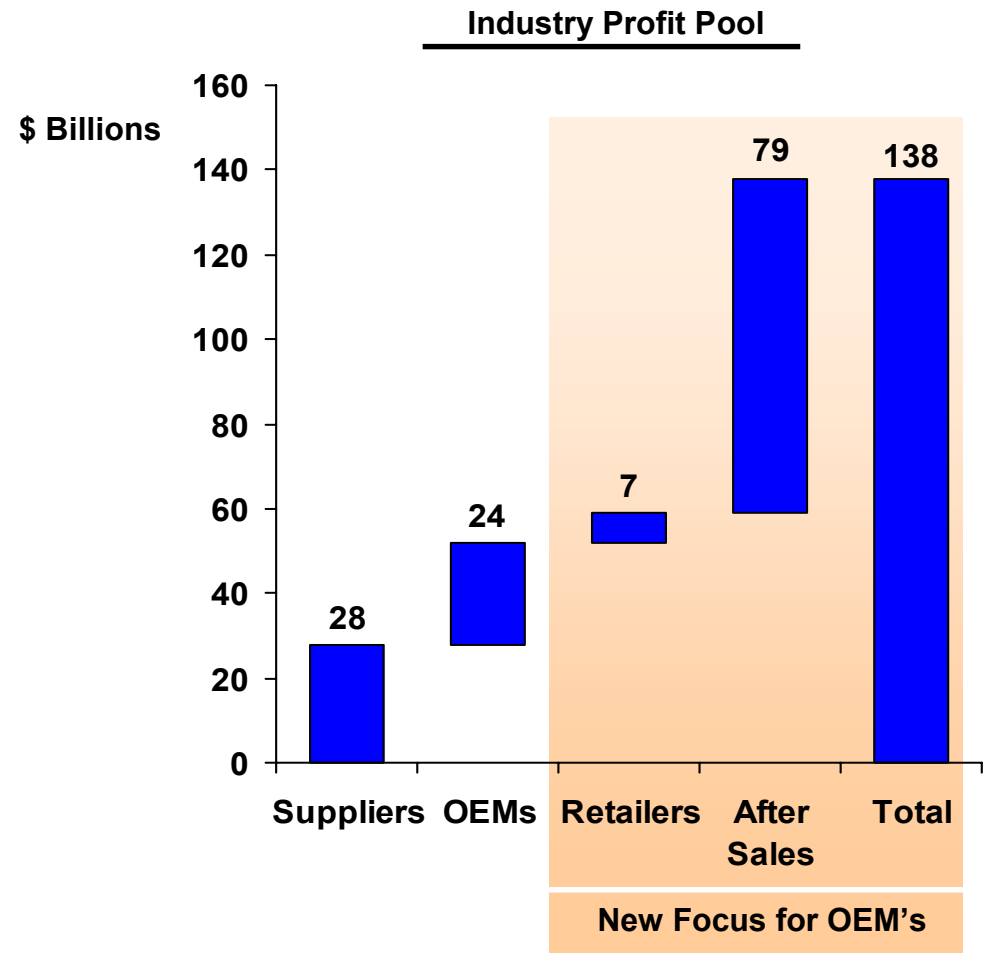
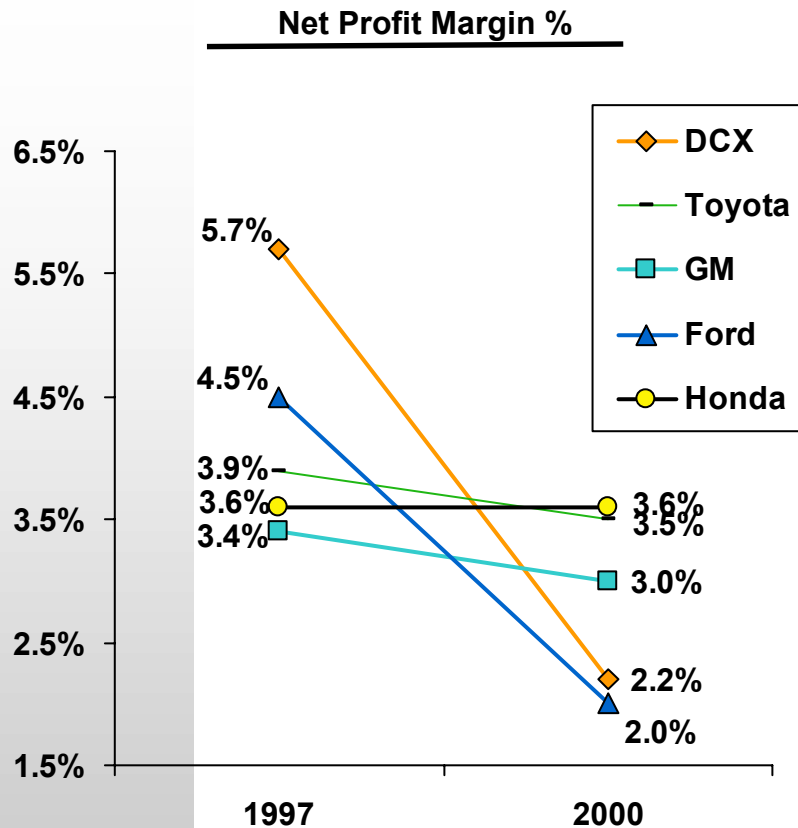


“Cars seem more and more alike in terms of quality and features than they were 5-10 years ago”

OEM's Seek New Ways To Build Differentiation

Declining Profitability Margins Driving OEM's To Search For New Profits

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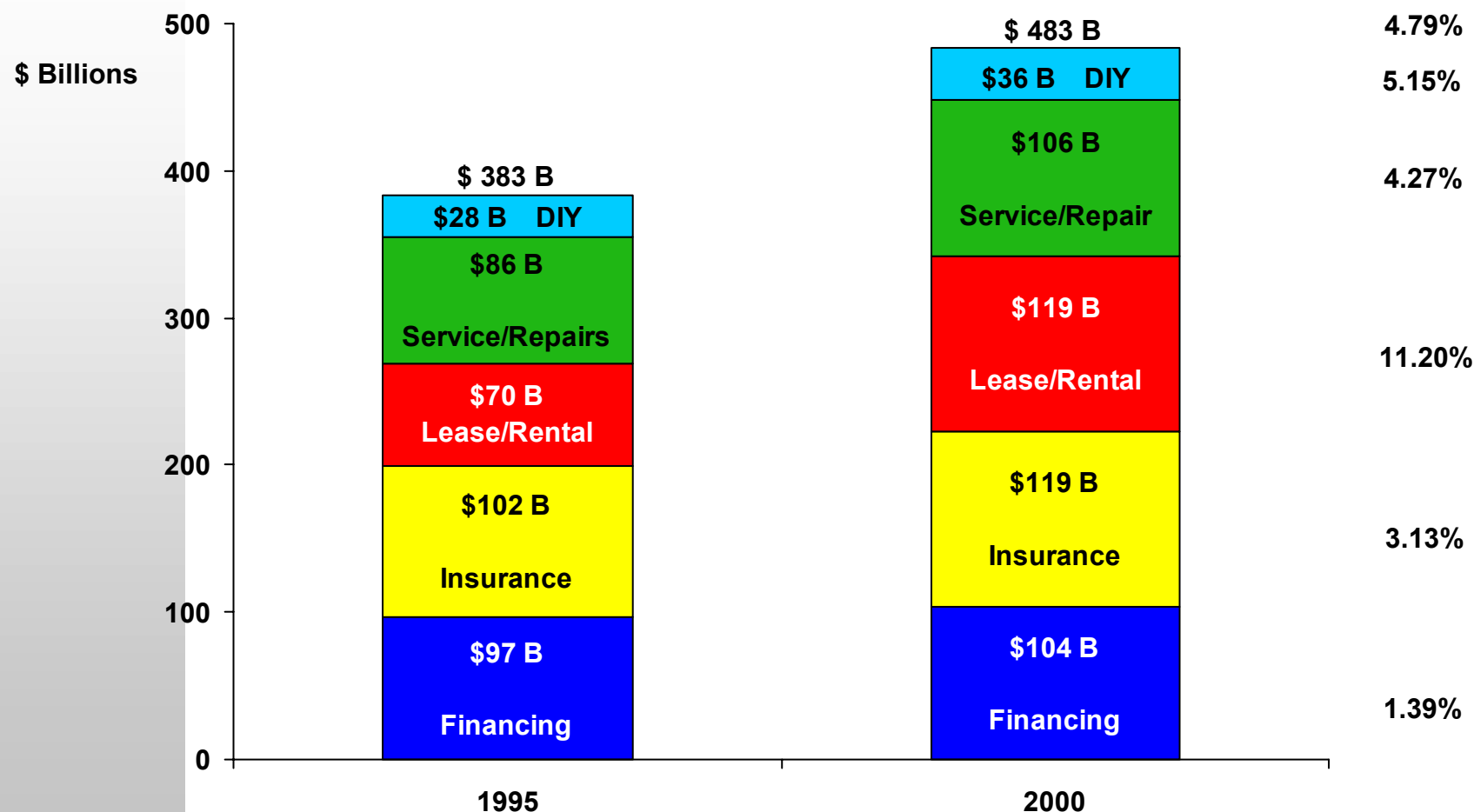
After-Sales Revenues Is New OEM Focus

Strong Growth In After-Sales

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Automotive After-Sales Revenues

**CAGR
95-00**



SOURCE: CNW Marketing/Research, Piper Jaffray Equity Research, Asaba Group Analysis

After-Sales Revenues Provide Profitable Growth Opportunities

Challenges Exist With Dominant Category Competitors



Service & Repair

Multiple Channel Options

- Independent Auto Dealers
- Auto Service Centers (NTB)



Financing

Local Banks/Credit Unions

- Fleet/Comerica
- Employee Credit Union



Rental/Leasing

Retail/Leasing Companies focused on individual segments/niches

- Dealers
- Finance Companies



Insurance

Local Neighborhood Rep Low Cost Channels

- State Farm
- GEICO



DIY Aftermarket

Dominant Category Killers

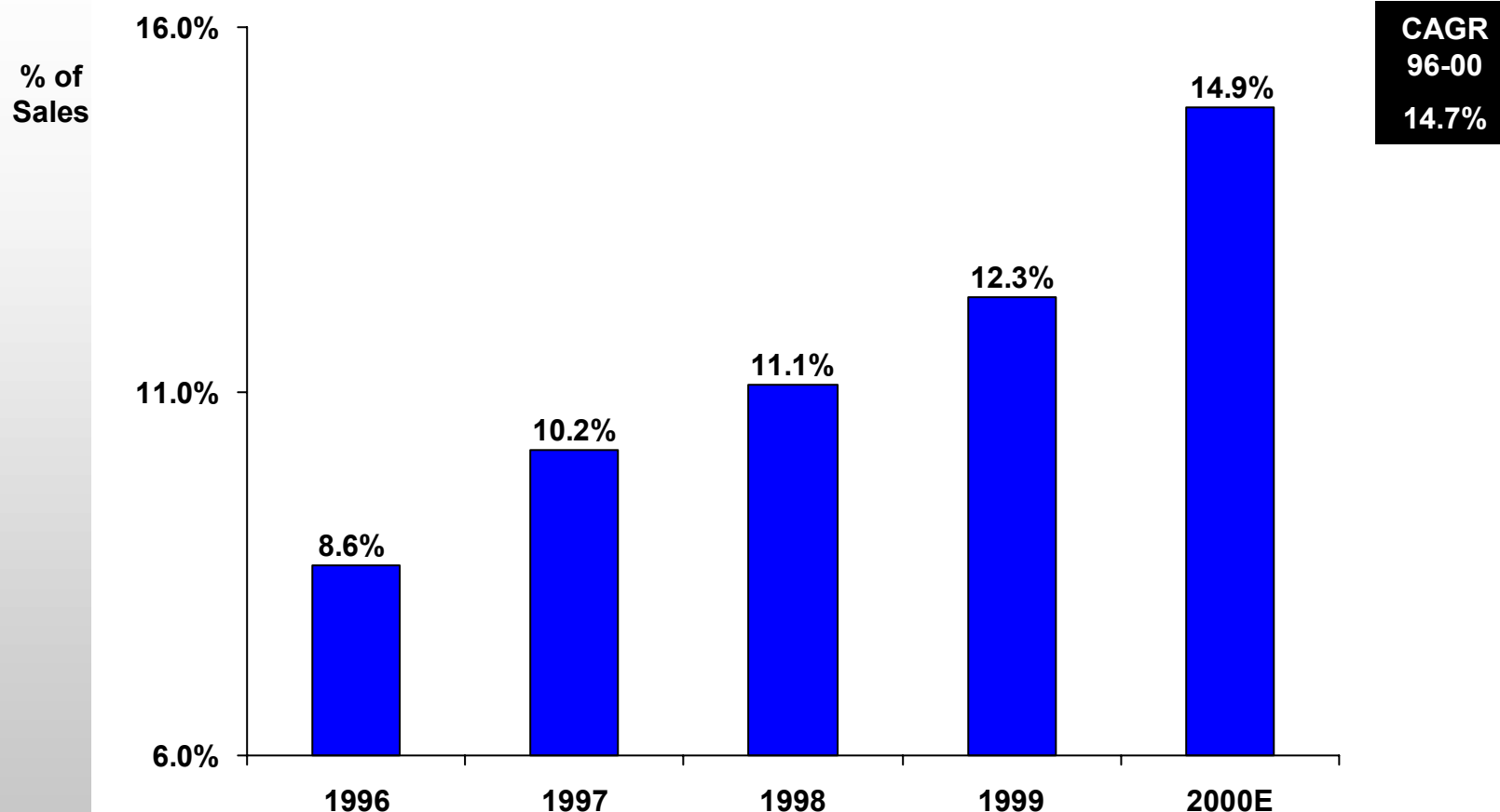
- PepBoys
- AutoZone

OEM's Can Leverage Minority Business To Access Minority Markets

In The Dealer Channel, Big Dealers Are Getting Bigger

20

Top 100 Dealers Percent Of Total Sales

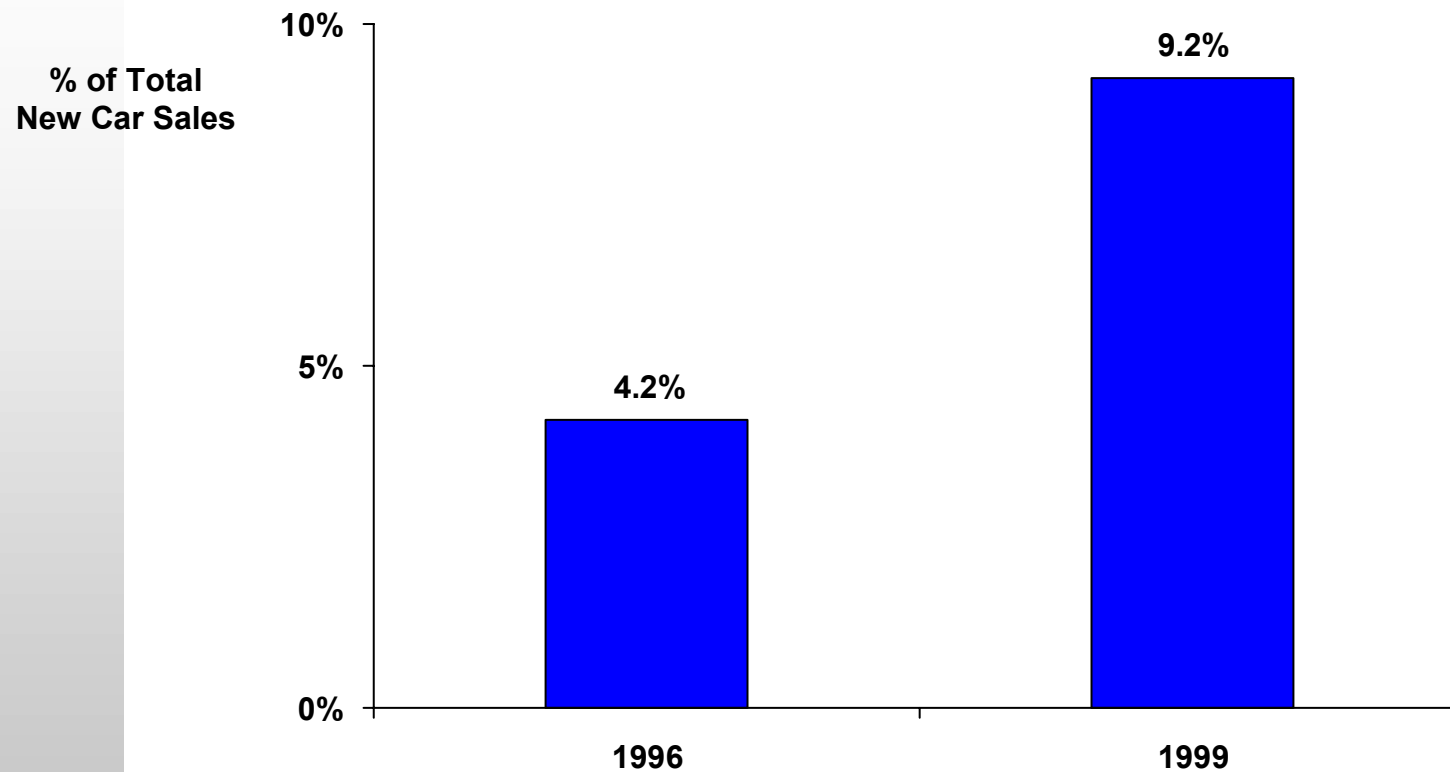


Increasing Their Leverage With Automotive Manufacturers

Multi-Franchised Dealer Sales Also Increasing

21

Top 20 Multi-Franchised Dealerships



Reducing Dependence On Any One Automotive Brand

SOURCE: National Automobile Dealers Association (NADA), Asaba Group Analysis

Automotive Manufacturers Realize The Need To Focus On Consumers

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Huge emphasis and investment in brand and product line management

Saturn has built its brand on consumer buying and lifecycle automotive experience

- Early pioneer in building customer relationships as a competitive advantage

Ford Motor Company vision changed to reflect consumer focus

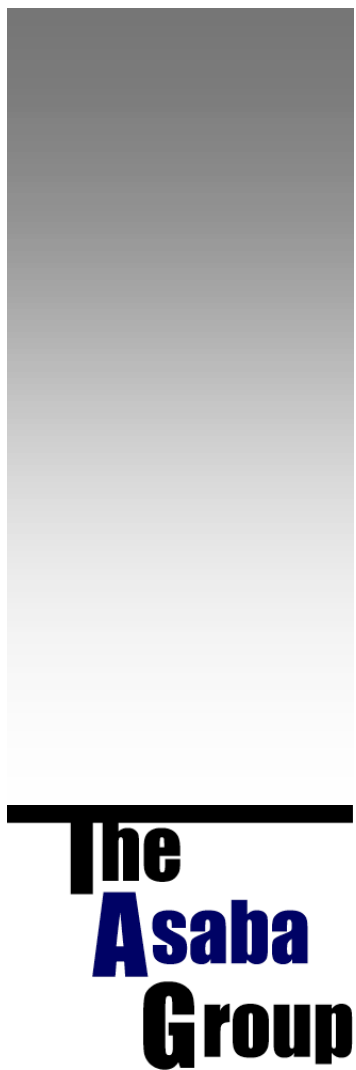
- “To become the world’s leading Consumer Company for automotive products and services”

General Motors recently appointed brand managers for its product lines

- Created marketing positions for minority segments

DaimlerChrysler, while striving for cost saving among platforms, has created strict rules to prevent dilution of Mercedes-Benz image

**Minority Business Development Is An Avenue
To Access Minority Consumers**



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Minority Consumers Are An Attractive Market For Automotive Manufacturers

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Automotive-related market spending in 2000 estimated at \$112 Billion

- New and Used Cars Sales estimated at \$67 Billion

Top 10 Minority Concentrated States account for 50% of new car sales

- Minority consumers have strong impact on automotive revenues

Minority Consumers will account for significant share of entry-level car buyers in the future

- Entry-level car buyers possess no legacy knowledge of past quality gaps between imports and domestic brands
- Top 10 Minority States account for 63% of Minority entry-level car buyers

Over-Index in used car purchases compared to general market consumers

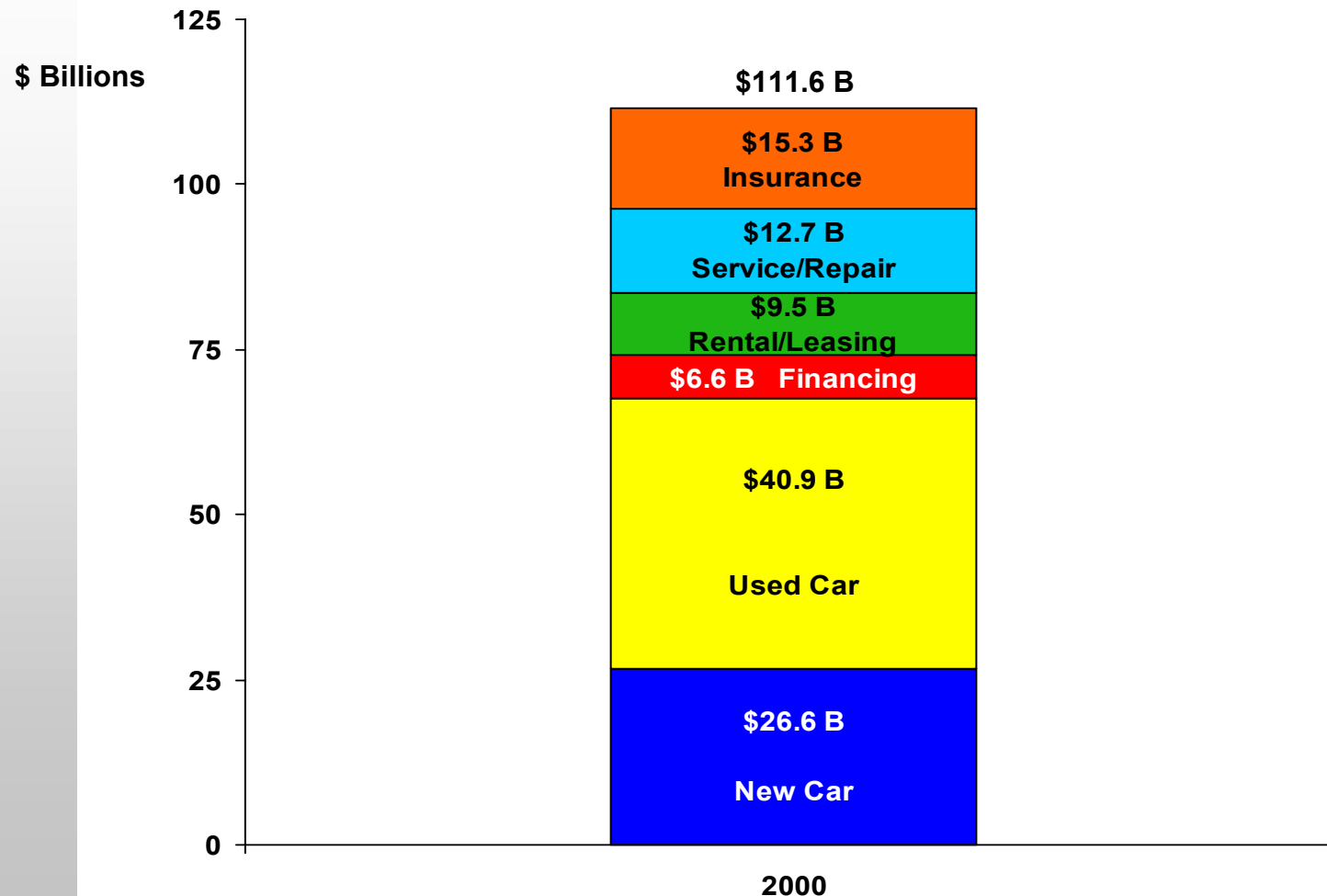
- Opportunity to capture more purchases through franchise dealer channels and after-sales revenues
- Opportunity to migrate minority consumers to situation where OEM's begin to capture the sales
 - Sales and profits currently captured at dealer level

Minority Automotive Spending Estimated At \$112 Billion

Minority Businesses Are Vital Links To An Ever-Expanding Minority Consumer Market

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Minority Automotive Spending

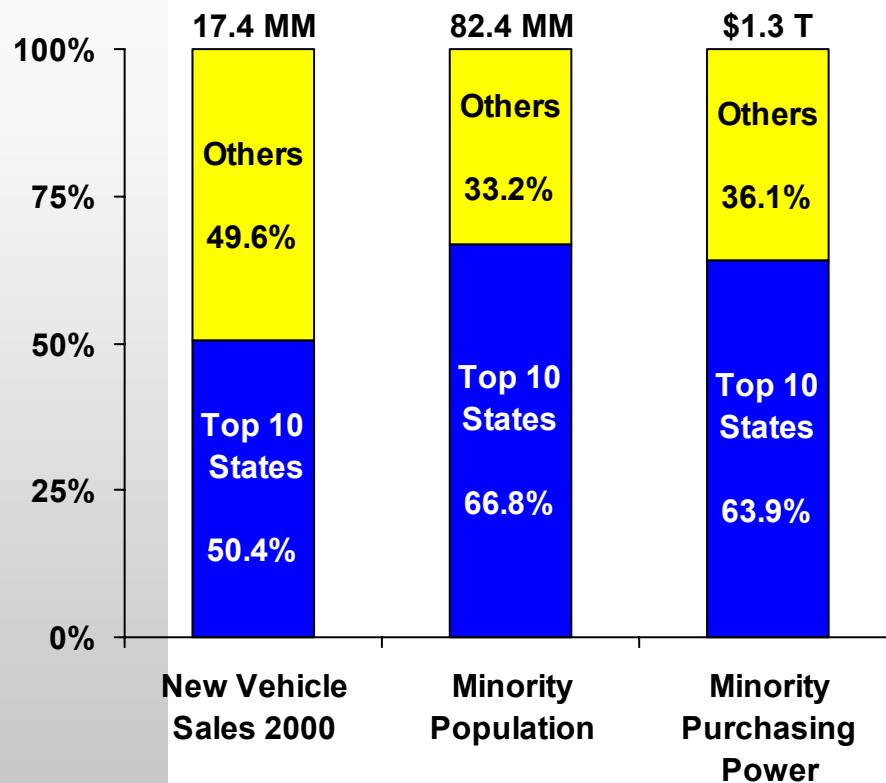


SOURCE: Minority Business Development Agency (MBDA), Bureau of Labor Statistics Consumer Expenditure Surveys, Asaba Group Analysis

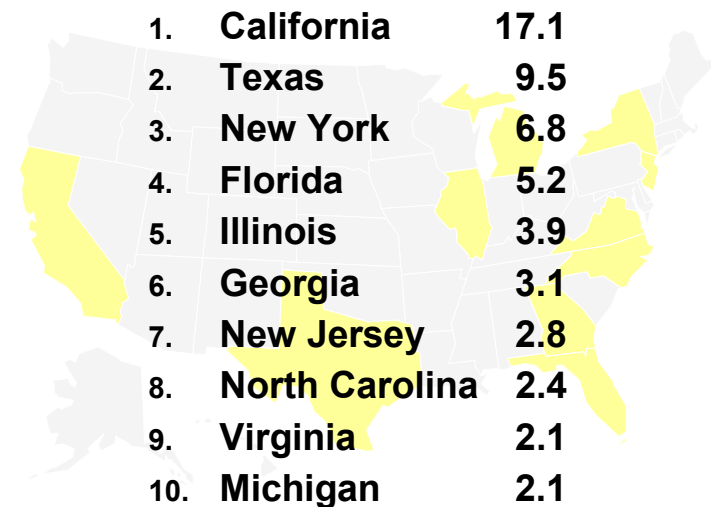
Top Ten Minority Concentrated States Account For 50% Of Total Automotive Sales

Also Account For Greater Share Of Minority Population And Purchasing Power

Top 10 Minority States Share



**Top 10 Minority States
(Ranked by Population MM)**



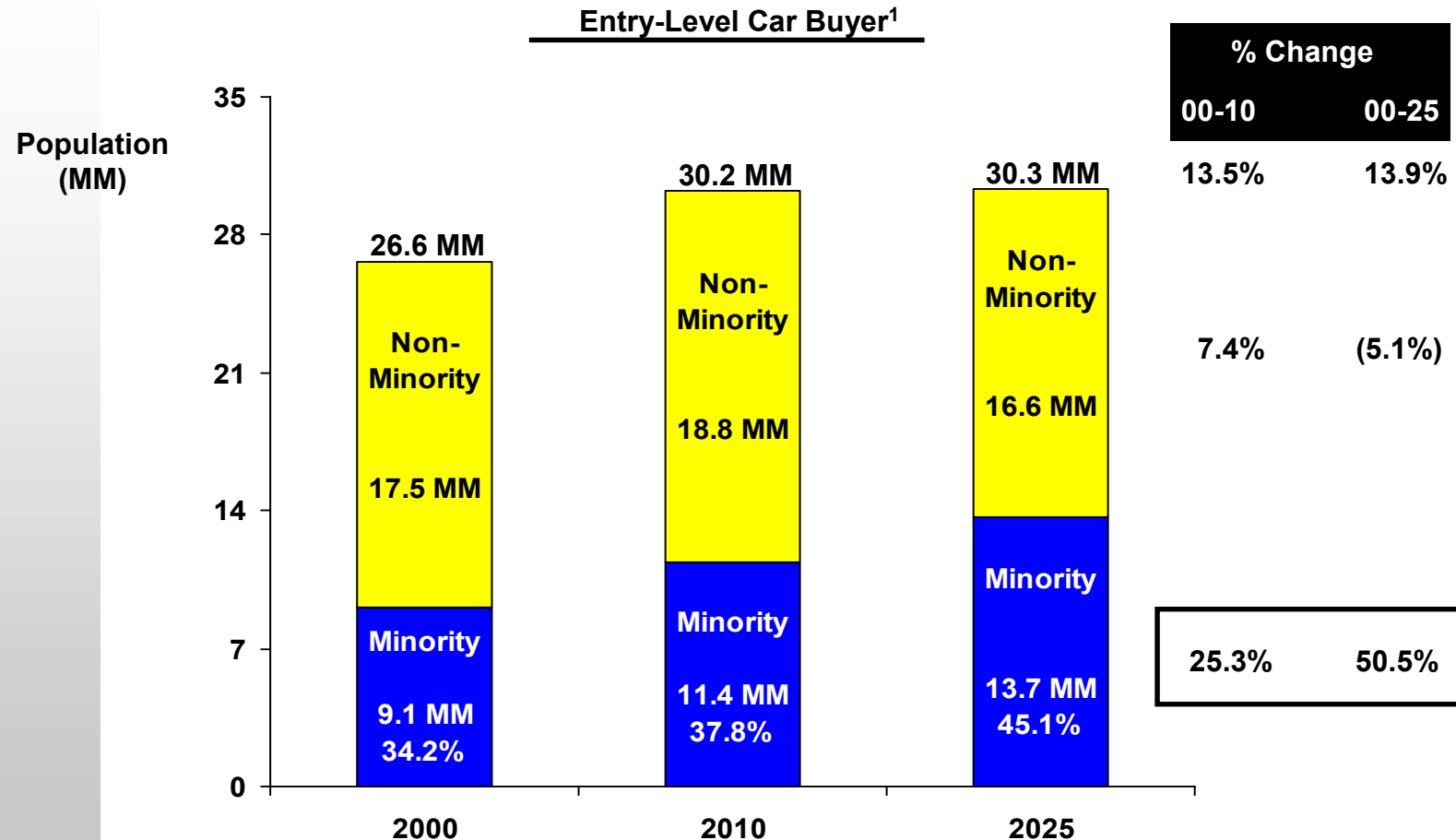
Strong Impact On OEM's Sales In These States

Minority Consumers Account For Significant Share Of Entry-Level Car Buyers

Auto Manufacturers View Capturing Entry-Level Car Buyers As Strategic

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Early opportunity to build brand loyalty

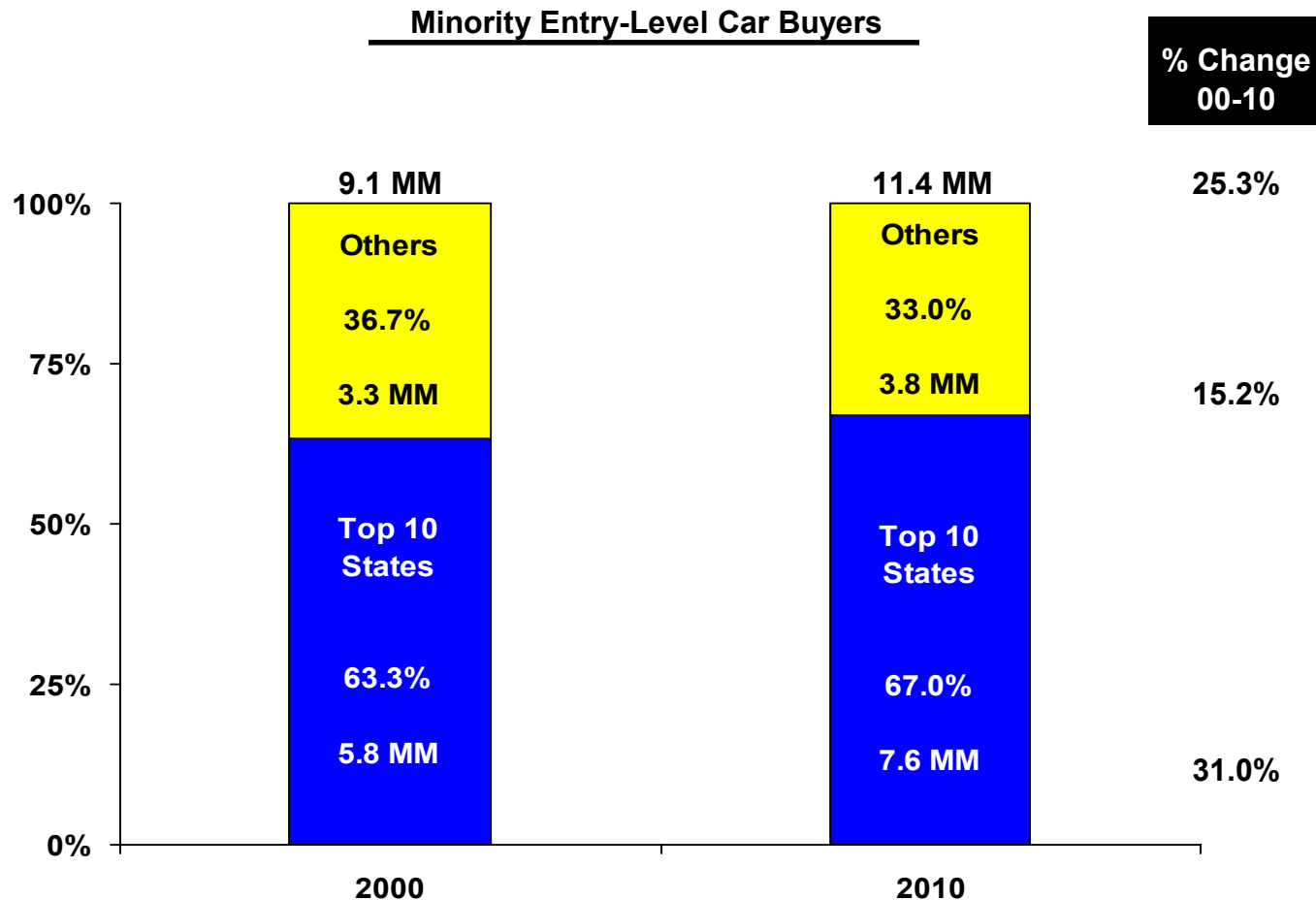


Minorities Are The Growth In This Segment

1. Represents 18 to 24 years Age Group or Proxy
SOURCE: U.S. Census 2000, Asaba Group Analysis

Top Ten Minority States Represent Significant Share Of Minority Entry-Level Buyers

And Most Of Future Growth

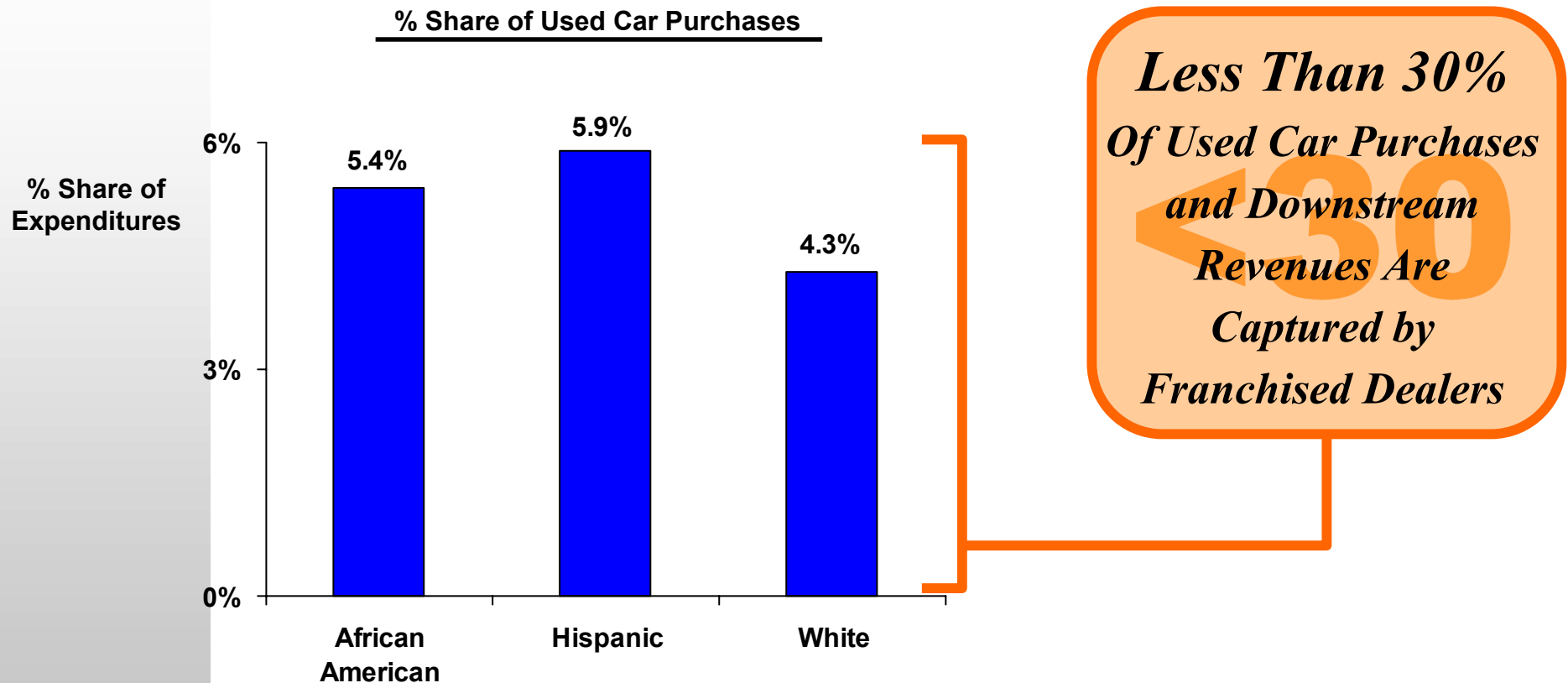


Capturing Minority Car Buyer Is Essential For Future Revenue Growth

Minority Consumers Have A Higher Incidence Of Used Car Purchases

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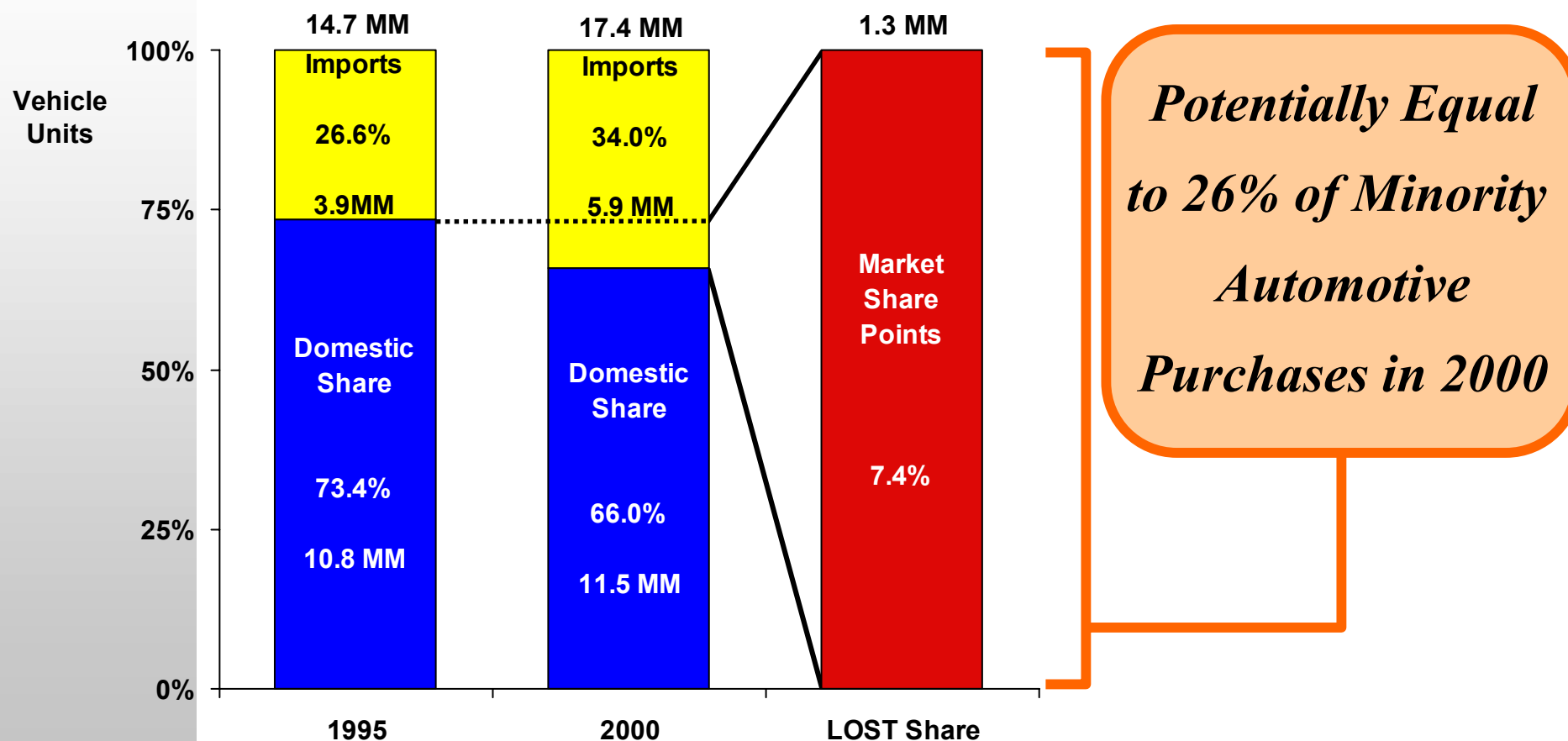
Most sales captured in the retail channel by non-franchised dealers



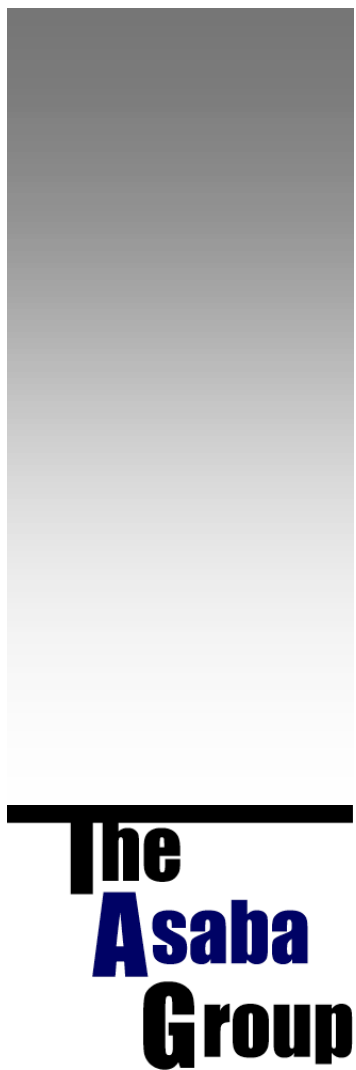
Auto Manufacturers Must Leverage Minority Dealer Relationships

Minorities Make A Difference In Auto Manufacturers Performance

Illustrative Example



SOURCE: Merrill Lynch, Automotive News, Asaba Group Analysis



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Value Propositions For Doing Business With Minority-Owned Enterprises

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Most Business Relationships Develop Value Proposition Around The Following:

Market Access

Provides access to new growth and strategically important market segment or consumers.
e.g. Alliances that enable entry into International emerging markets

Increase Customer Loyalty

Enables increased and sustained profitability from existing customer base
Provides opportunities for new revenue sources – Increase Share of Wallet (SOW)
e.g., Loyalty drives down cost associated with customer retention and acquisition.

Supply Chain Flexibility

Provides second sourcing alternative in Supply Chain
– Reduces supplier concentration risks

Stakeholder Satisfaction

Satisfy needs of key Stakeholders
Develop and Enhance Citizen Image
– Environmental Coalitions/Organizations

Regulatory Value

Enhances ability to meet government mandate/compliance without sacrificing profits or increasing cost
e.g. CAFÉ standards

Minority Business Enterprises Value Proposition

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Benefits

Minority Business Value Proposition (OEM's/Large Suppliers)

Implications/Realities

Market Access

- Minority dealerships provide access to important minority dominant markets
- Brand differentiation from Minority Sourcing (Think "Intel Inside" approach)
- Tier One suppliers access to aftermarket segment
- Ability to capture after-sales revenue potential/licensing revenues
 - Less dependent on automotive product attributes

- Minority business as channel partners in key markets
- Not effectively utilized today by Automotive Manufacturers
- Not effectively capturing after-sales market potential
- Minority consumer over-index in purchases of aftermarket lifestyle products

Consumer Loyalty

- Minority consumers more brand loyal than general market
 - Reward manufacturers who contribute to community well being
- Minority Channel partners critical in building loyalty for Auto Manufacturers
- OEM's reward Tier One suppliers with more sourcing opportunities

- Big 3 minority loyalty rewarded in States with significant minority suppliers
- Need to build loyalty to brand in key minority states
- OEM's selection criteria of large suppliers to include minority sourcing objectives

Minority Business Enterprises Value Proposition (cont'd)

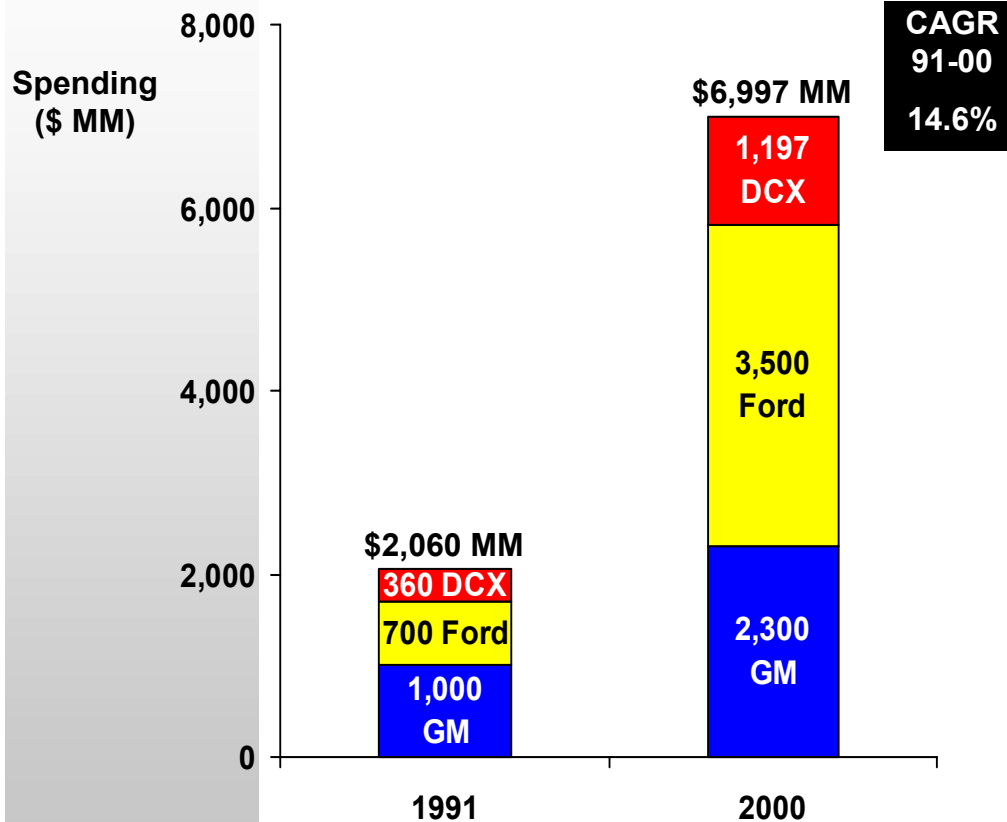
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Benefits	Minority Business Value Proposition (OEM's/Large Suppliers)	Implications/Realities
Supply Chain Flexibility	<ul style="list-style-type: none"> • MBE lower operating cost provides ability to reduce total delivered system costs to OEM's • Potentially can provide second source alternative (to certain commodities) <ul style="list-style-type: none"> – Lower sourcing risks and provides category competitiveness • Large Tier One Suppliers can leverage MBE's lower cost structure in Supply Chain • Alternative source for technology and global competition 	<ul style="list-style-type: none"> • MBE are lower cost alternative to certain internal business processes <ul style="list-style-type: none"> – Outsourcing partners, e.g. commodity management • MBE Tier One Joint Ventures provide alternative low cost sources to commodities • MBE tend to have lower factor costs compared to large suppliers
Stakeholder Satisfaction	<ul style="list-style-type: none"> • Meet needs for special interest consumer advocacy groups • Satisfy generally accepted diversity inclusion best practices 	<ul style="list-style-type: none"> • Diversity in the workplace <ul style="list-style-type: none"> – Minorities growing share of employees • Diversity related lawsuit increasing
Regulatory Value	<ul style="list-style-type: none"> • Assists OEM's to meet government contract / sourcing requirements • Enhances relationship with government entities 	<ul style="list-style-type: none"> • Loss of Government revenues <ul style="list-style-type: none"> – Annual spend approximately \$1 Billion • Minorities voting power increases • Decision makers increasingly minorities

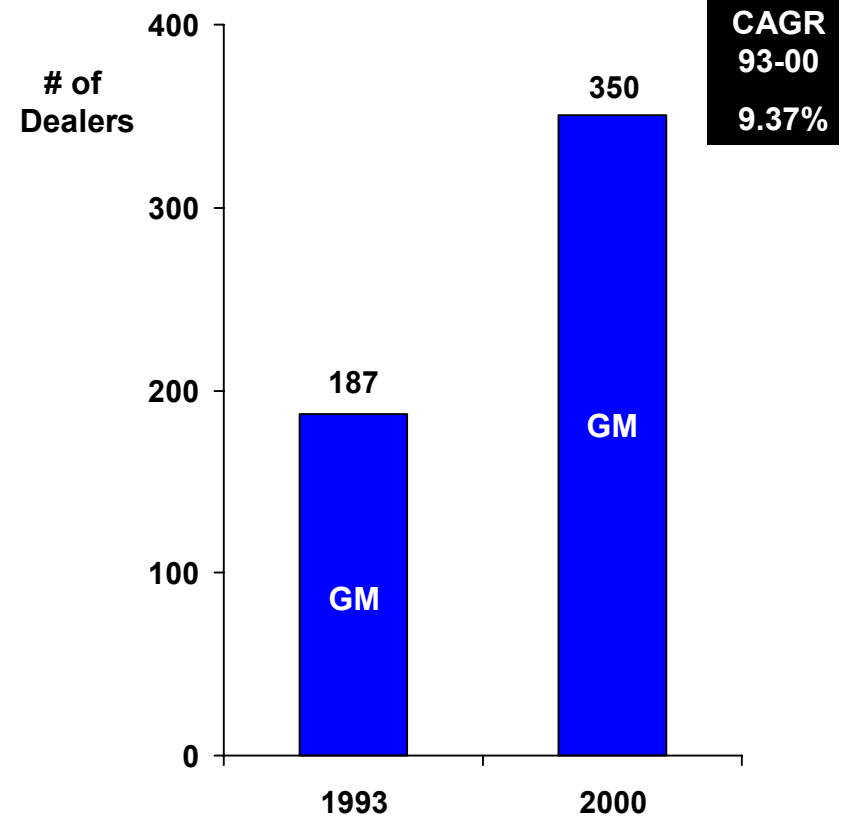
Domestic Automotive Manufacturers Committed To Minority Sourcing And Dealers

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Minority Suppliers



Minority Dealers¹



Clearly Understand The Benefits Of Doing Business With MBE's

1. GM as growth proxy
 SOURCE: Company Reports

Automotive Manufacturers Commitment To Minority Sourcing

“ ...The inclusion of minority suppliers into our supply base contributes to long term economic, political, and social stability of our industry by including important diverse customers in its economic activity.”

- *Jacques A. Nasser*
President and CEO
Ford Motor Company

“ Minority procurement is no longer an issue of social conscience. Our very future depends on capturing and retaining the loyalty of a growing consumer market audience.”

- *Thomas Sidlik*
EVP Procurement
DaimlerChrysler

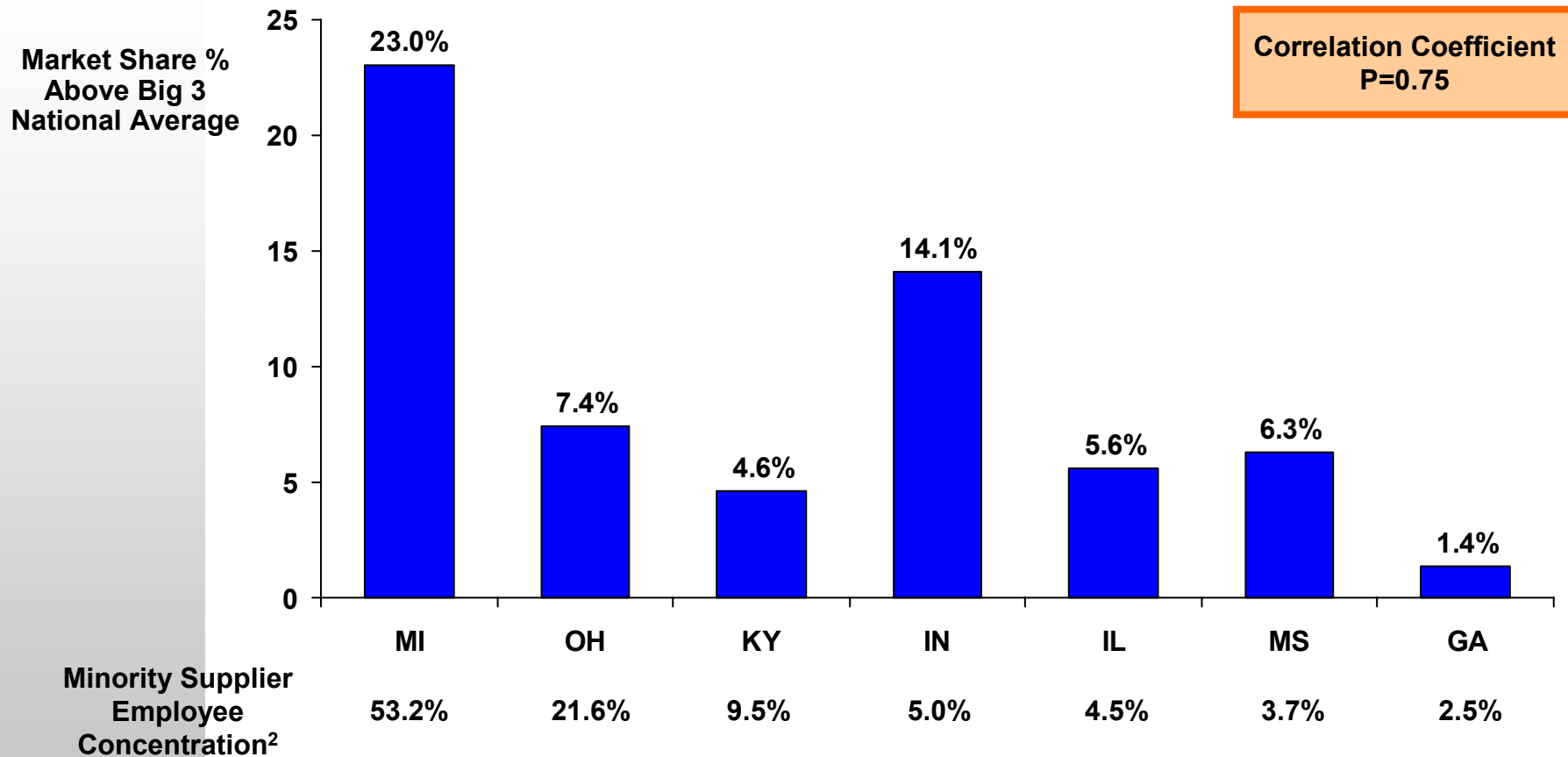
“ Our primary focus is to develop strong and viable minority suppliers as well as support the business growth of our minority joint venture partners...”

- *Harold R. Kutner*
Group VP Worldwide Purchasing
General Motors

Big 3 Minority Suppliers' Employees Buy Big 3 Products

In States With High Concentration Of Minority Suppliers' Employees, Big 3 Manufacturers Have Higher Than Average Market Share

Big 3 Market Share % Above U.S. Average By State¹



Positive Correlation Between Big 3 Market Share And Minority Suppliers

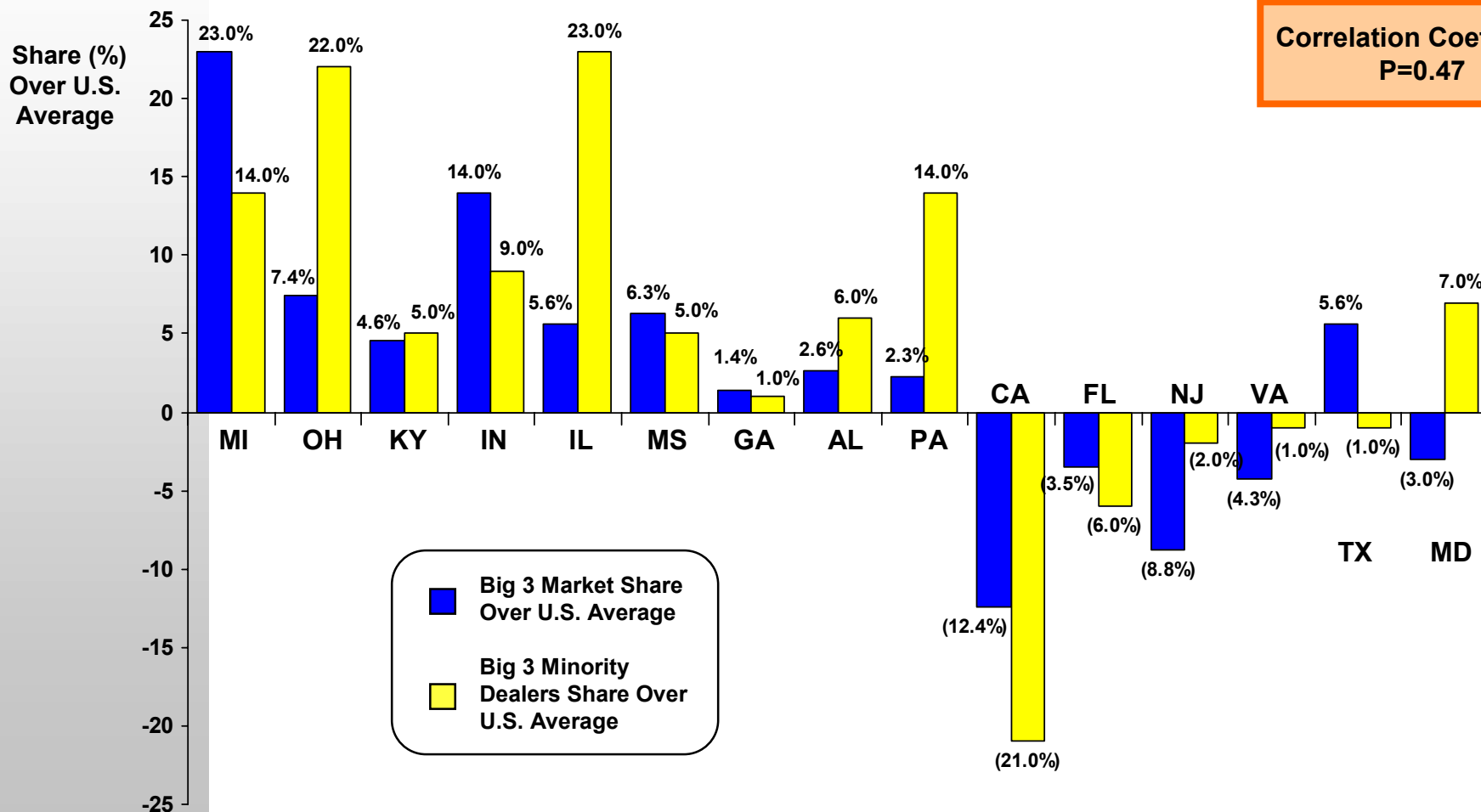
1. States also have high concentration of Big 3 facilities
 2. Approximately 300 Minority Suppliers
- SOURCE: Asaba Group Analysis, Automotive News

Minority Dealers Play A Role In Automotive Market Performance

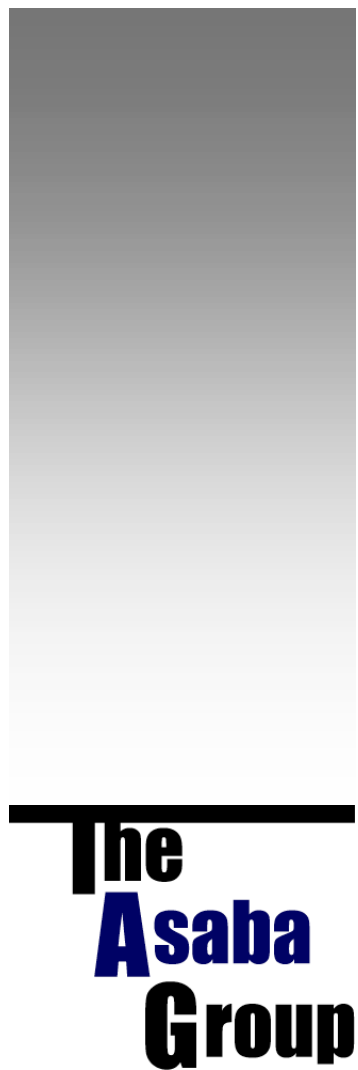
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In Top 15 minority markets, some correlation between Big 3 market share and Big 3 minority dealers

Big 3 Market Share and Minority Dealer Share



SOURCE: Ward's, Asaba Group Analysis



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Key Observations

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Observations

1. Under-capitalized—Working capital/cash flow issues

Problem Drivers/Issues

- Financial institution investment attractiveness
- Capital structure constraints
- Weak management/operations

Key Implications

- Increase supplier management cost
 - Technical assistance
 - Short-term financing
 - Procurement cost
 - Quality issues

2. Presence in low threshold commodities

- Low margin, volume sensitive

- Weak value chain positioning
- Corporate buyer procurement mindset
 - Unwillingness to take risks
 - Direct sourcing dollars with low risks

- Sensitive to industry volume
 - Increased operating risks
- Impaired ability to meet productivity commitments
- Bid competitiveness issues

3. Procurement mindset vs. “Strategic Sourcing”

- “Chasing next contract/part”

- Corporate buyer procurement mindset
 - Implicitly defines market opportunity/space
 - Individual buyers with minority supplier objectives making low-risk procurement decisions
- Minority business economic model
 - High volume/high profit dollar

- Increased supply base fragmentation
- Unsustainable business model
 - Impairs ability to reinvent
 - Reduces investment attractiveness

Key Observations

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Observations

4. Focus on reporting “size of Minority dollars”

- Little emphasis on quality of spending

5. Significant top line operating risks

- Concentrated sales/revenues

6. Corporate organization buy-in

- Lack of clear business benefits

Problem Drivers/Issues

- Government and advocacy groups metric/performance definition
 - Not reflective of industry realities/dynamics

- Lack of diversified revenue streams
 - By OEM/Platform/Industry
- Minority companies downplay emphasis/need for strategy development and planning

- Articulation of program rationale
 - Clouded with social/community benefits
 - No clear tie-in to economic value added
- Corporate marketing operations not leveraging MBE supply chain program for consumer differentiation

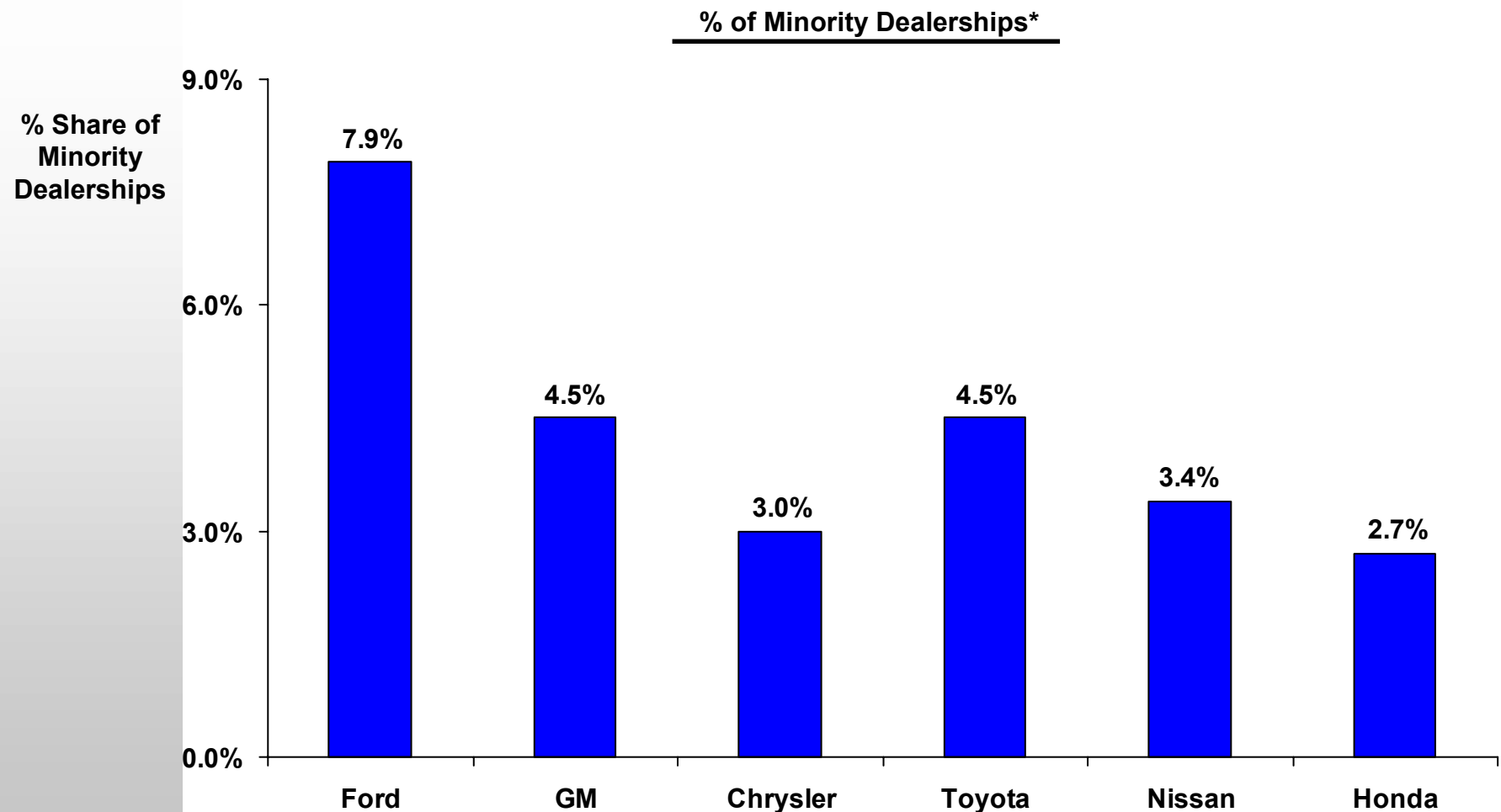
Key Implications

- Forced to maintain direct small suppliers
 - High presence of minority suppliers in non-production
- Increased supply base fragmentation

- Risks to supply chain increased
 - Supplier performance more sensitive to production swings
 - Supplier operating risks leads to higher cost due to assistance provided

- Lower market share with minority car buyers
 - Not leveraging inherent advantage as added component of building brand differentiation

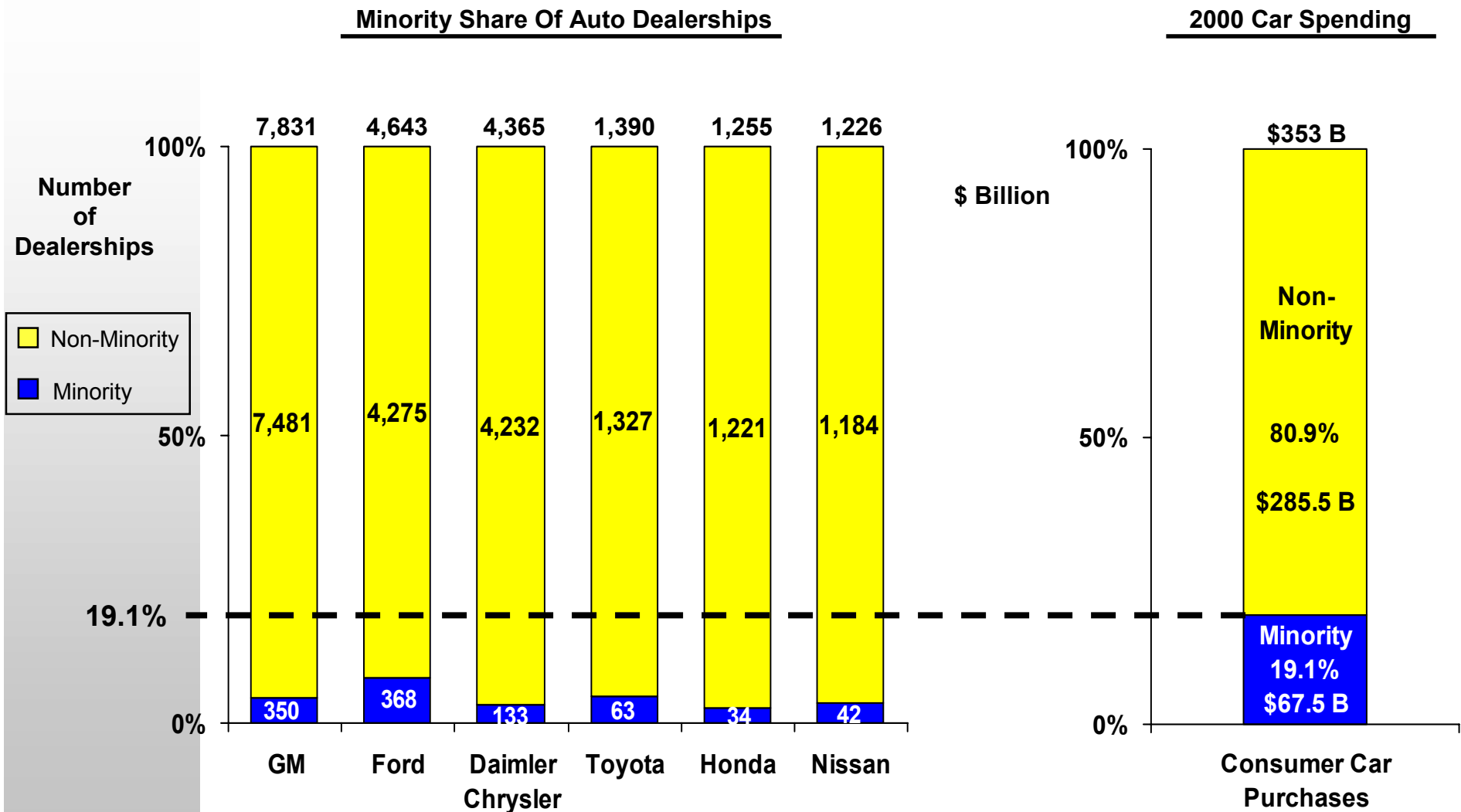
Disparities Exist With Share Of Minority-Owned Dealerships Among Manufacturers



* GM, Ford, Chrysler exclude European luxury makes: Nissan, Toyota, Honda include luxury division

Minority Dealers Under-Represented In The Industry Compared With Automotive Purchases

43



SOURCE: National Automobile Dealers Association (NADA), Automotive News, Asaba Group Analysis, Bureau of Labor Statistics Data

Does Minority Ownership Capital Structure/ Investment Attractiveness Affect Growth?

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<u>Top Five Dealership Groups</u>		<u>Top Five African American Dealerships</u>		<u>Top Five Hispanic Dealerships</u>	
1. Auto Nation Inc*	\$19.6 B	1. Prestige Automotive	\$657.7 MM	1. Burt Automotive	\$1.2 B
2. Sonic Automotive*	\$5.6 B	2. March-Hodge Holding	\$324.5 MM	2. Ancira Enterprises	\$594 MM
3. United Auto Group*	\$4.9 B	3. Mel Farr Automotive	\$298.5 MM	3. Elder Automotive	\$483.5 MM
4. Asbury Automotive	\$4.5 B	4. Ray Wilkinson	\$268.6 MM	4. Lloyd Wise	\$336.4 MM
5. V.T. Inc.	\$4.3 B	5. The Harrell Companies	\$268.5 MM	5. Tara Ford	\$195.5 MM
<hr/> Total Top 5		<hr/> Total Top 5		<hr/> Total Top 5	
\$38.9 B		\$1.82 B		\$2.8 B	

Challenge Is How To Drive Growth

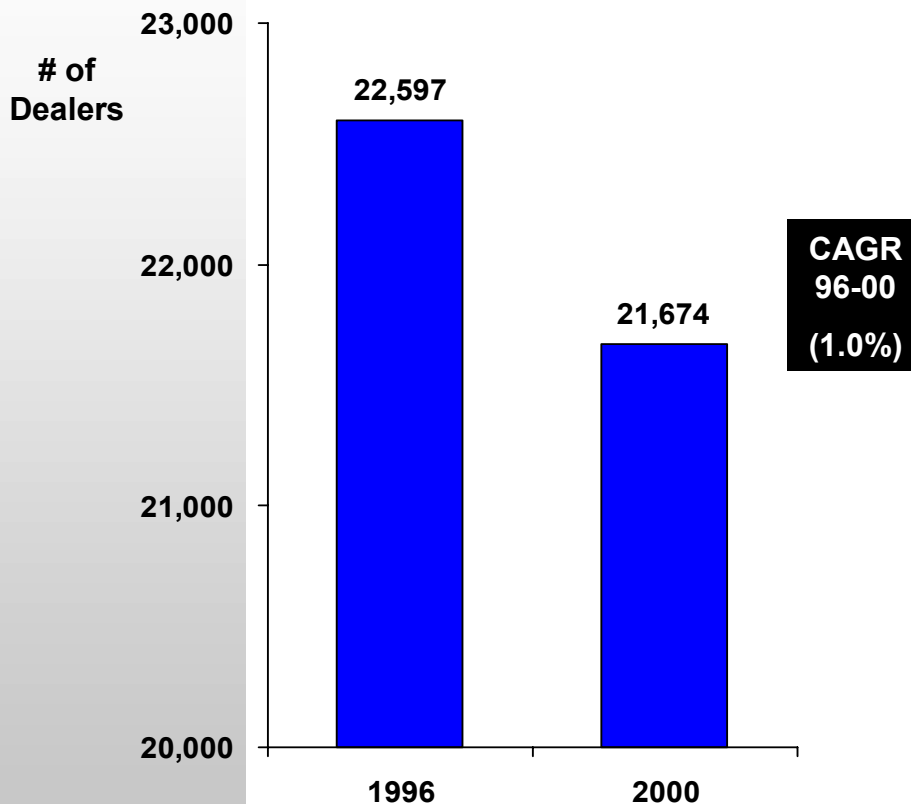
* Publicly held companies

SOURCE: Automotive News, Black Enterprise, Hispanic Business

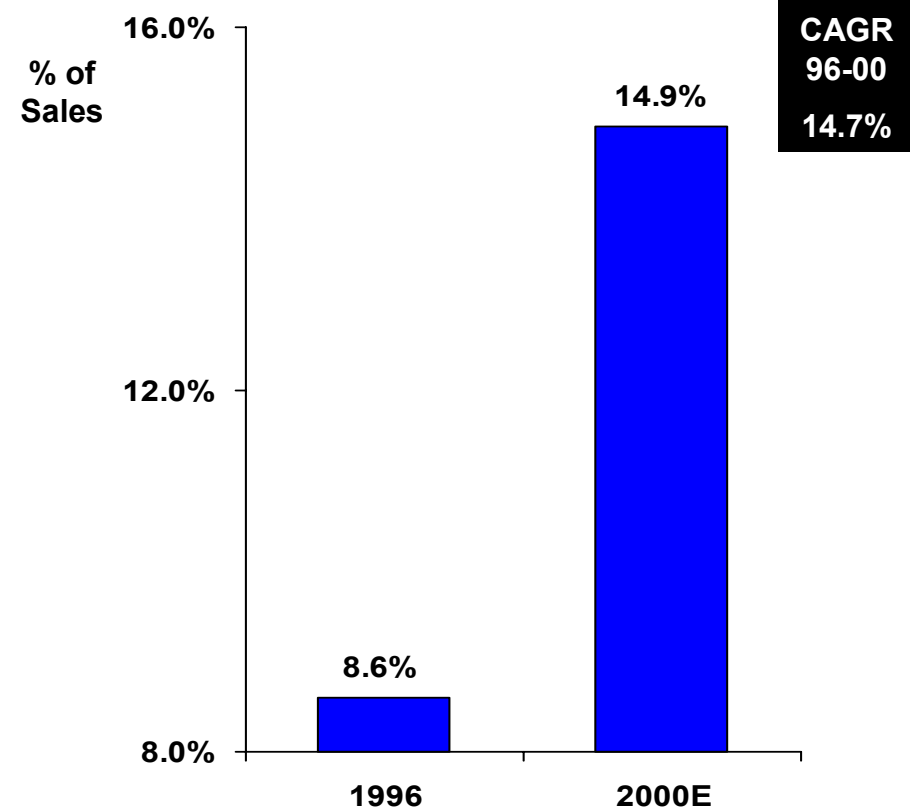
Total Number Of Dealerships Declining, But The Large Dealerships Have Grown!

45

of US Auto Dealerships



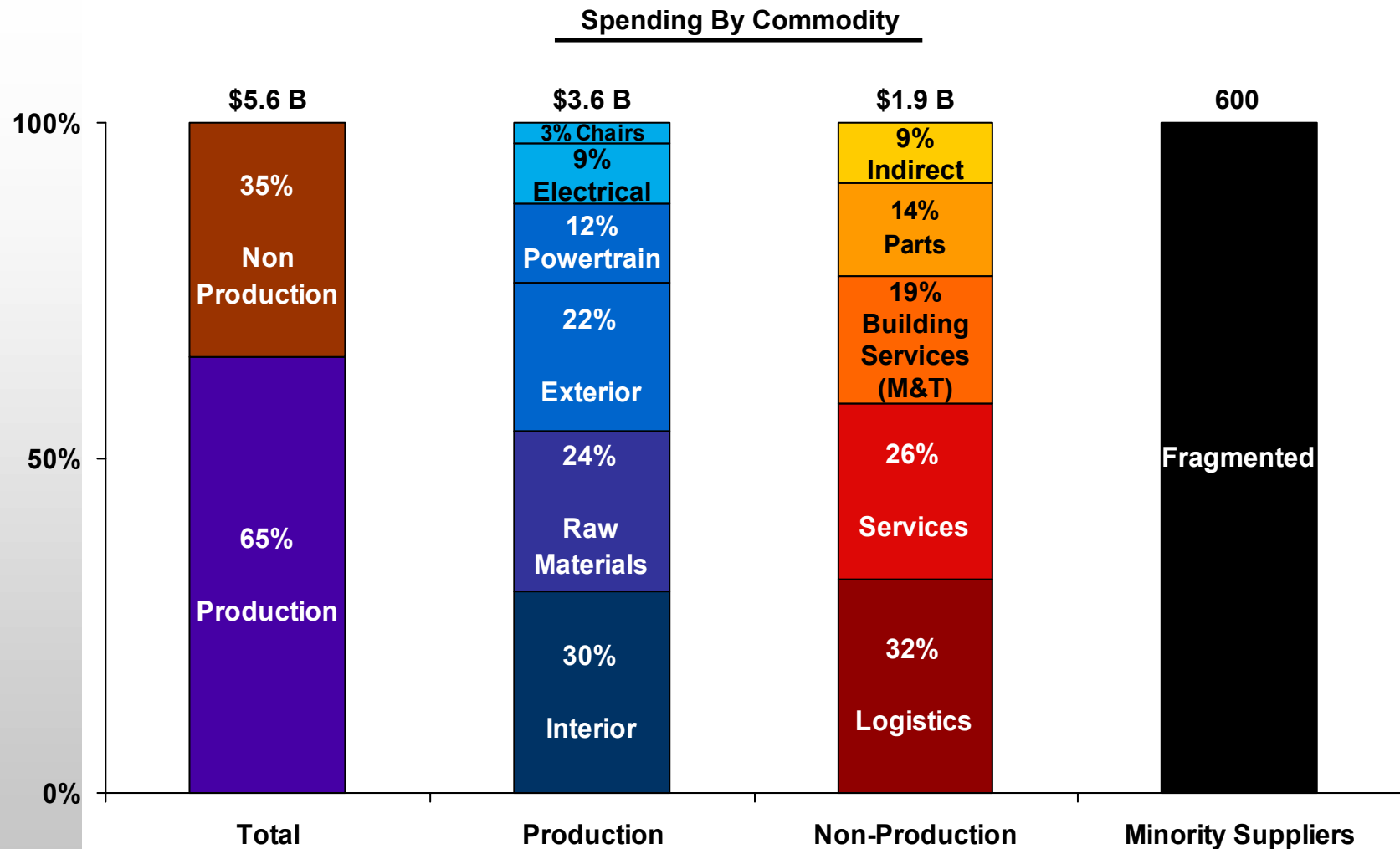
Top 100 Dealers % of Total Sales



How Can We Drive Minority Dealership Growth In This Environment?

Minority Spending By Automotive Manufacturers In 2000 Shows Broad Commodity Participation By MBE's

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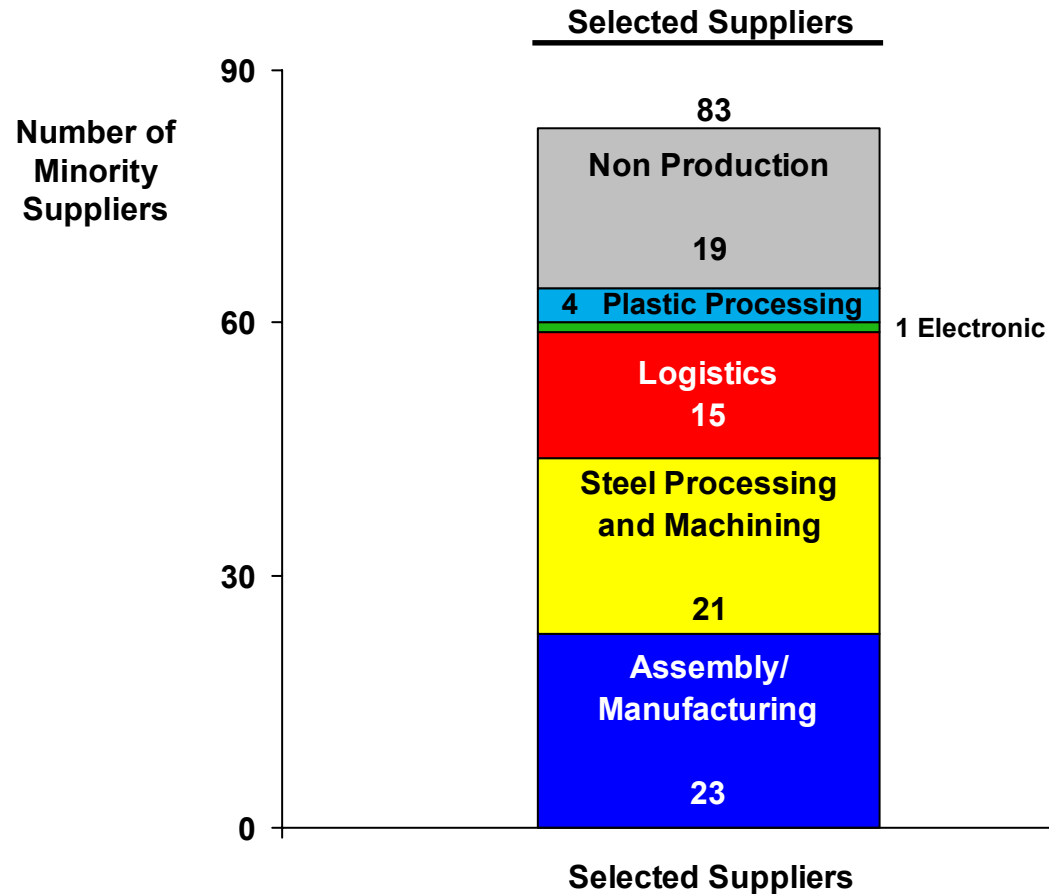


Issues Around Size/Scale And Value Chain Positioning

Auto Manufacturer Attempt To Grow With Fewer (Selected) Minority Suppliers

Responding To Supply Chain Realities

Few in high value-added activities



Emphasis Should Be On “How Much Value Is Added?”

The Problem With Cascading Minority Sourcing Objectives

Focuses On “Quantity of Spend” Versus “Quality of Spend”

Illustrative Example

VP Sourcing/
Purchasing



- Set goal for 5% of total purchases for minority suppliers
- Cascade 5% objective to commodity buyers

Commodity Buyers

Chassis



Interiors



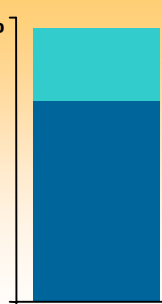
Non-
Production



Electrical

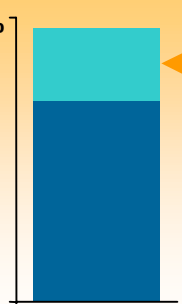


100%



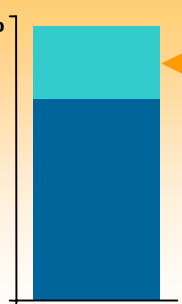
Commodity A

100%



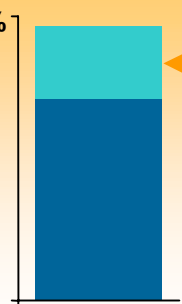
Commodity B

100%



Commodity C

100%



Commodity D

- Need to meet 5% minority supplier objective
- Also rewarded on achieving commodity wide cost savings and lowering supply chain risks

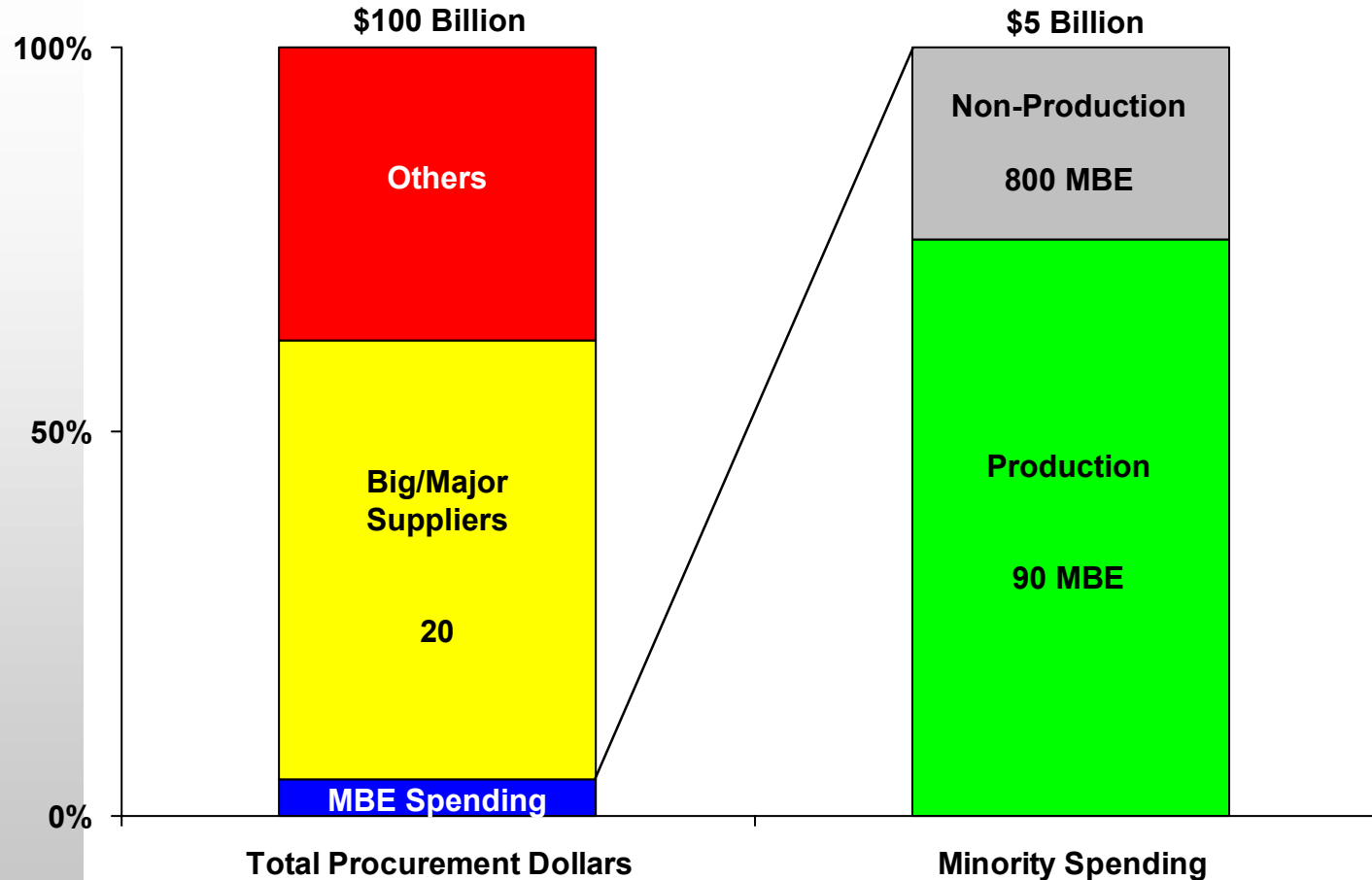
Danger Exists That Buyer May Source to Minority Suppliers Their Low Value\Margin Products

Leads To High Fragmentation And Weak Value Chain Positioning

Minority Procurement Spending Typically Very Fragmented

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Illustrative Example



Incurring Significant Costs In Supplier Management And Commodity Savings

Widespread Consensus On The Need To Change Current MBE Spending Metrics

“We deal with bigger suppliers who can do more and build total modules and systems. It takes a lot for Minority Suppliers to do this and remain Tier One Suppliers.”

“People have to understand our industry better... Maintaining small suppliers as Tier One is very difficult and adds cost.”

“It’s the metric... stupid. It only recognizes Tier One minority dollars.”

“Not all MBE’s can JV with big suppliers so as to maintain Tier One status. We need to change the metrics and recognize Lower Tier spending.”

Proposed New Methods/Framework To Measure MBE Spending

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Places new emphasis on measuring “Quality of Spending”

Asaba Group Quality Index (AGQI™)

Functions of the following

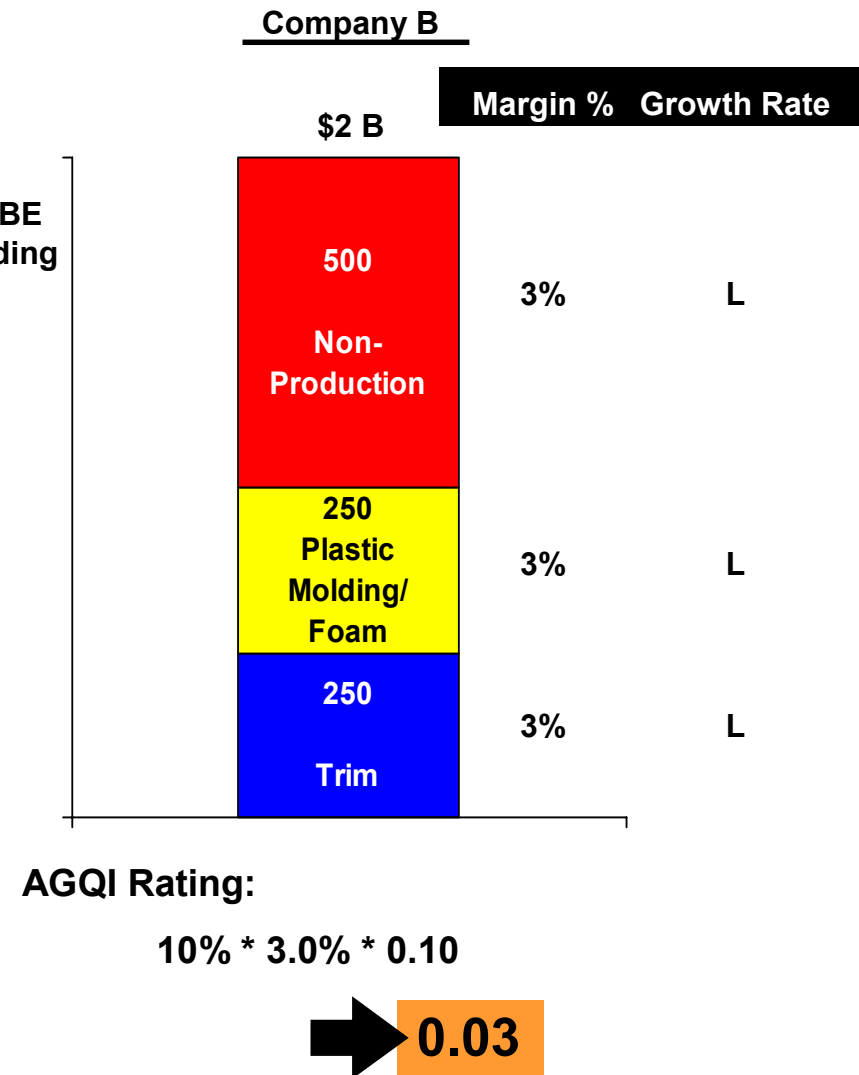
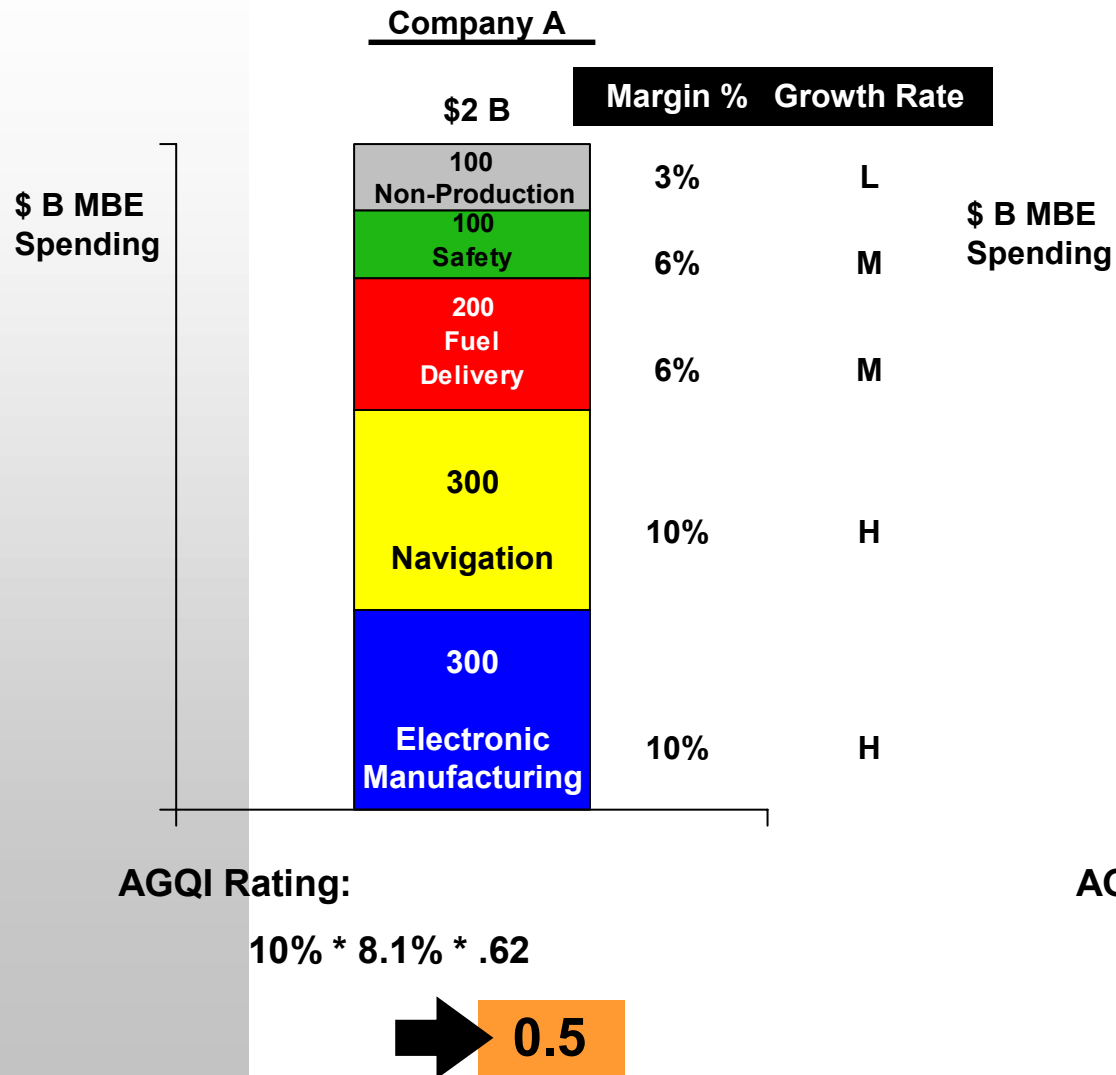
- Total Minority Spending (% of Total Purchases)
 - Weighted average commodity category margin
 - Weighted average category growth factor (0.1 = Low, 0.5 = Mid, 1 = High)
- **AGQI solves the issues of MBE Concentration in weak value chain positions**
 - Forces Commodity Buyers to provide higher quality opportunities
 - **AGQI enables better recognition of Lower Tier minority efforts**

**Reflects Industry Supply Chain Realities
Without Compromising Inclusion**

Asaba Group Quality Index (AGQI™) – Illustrative Example

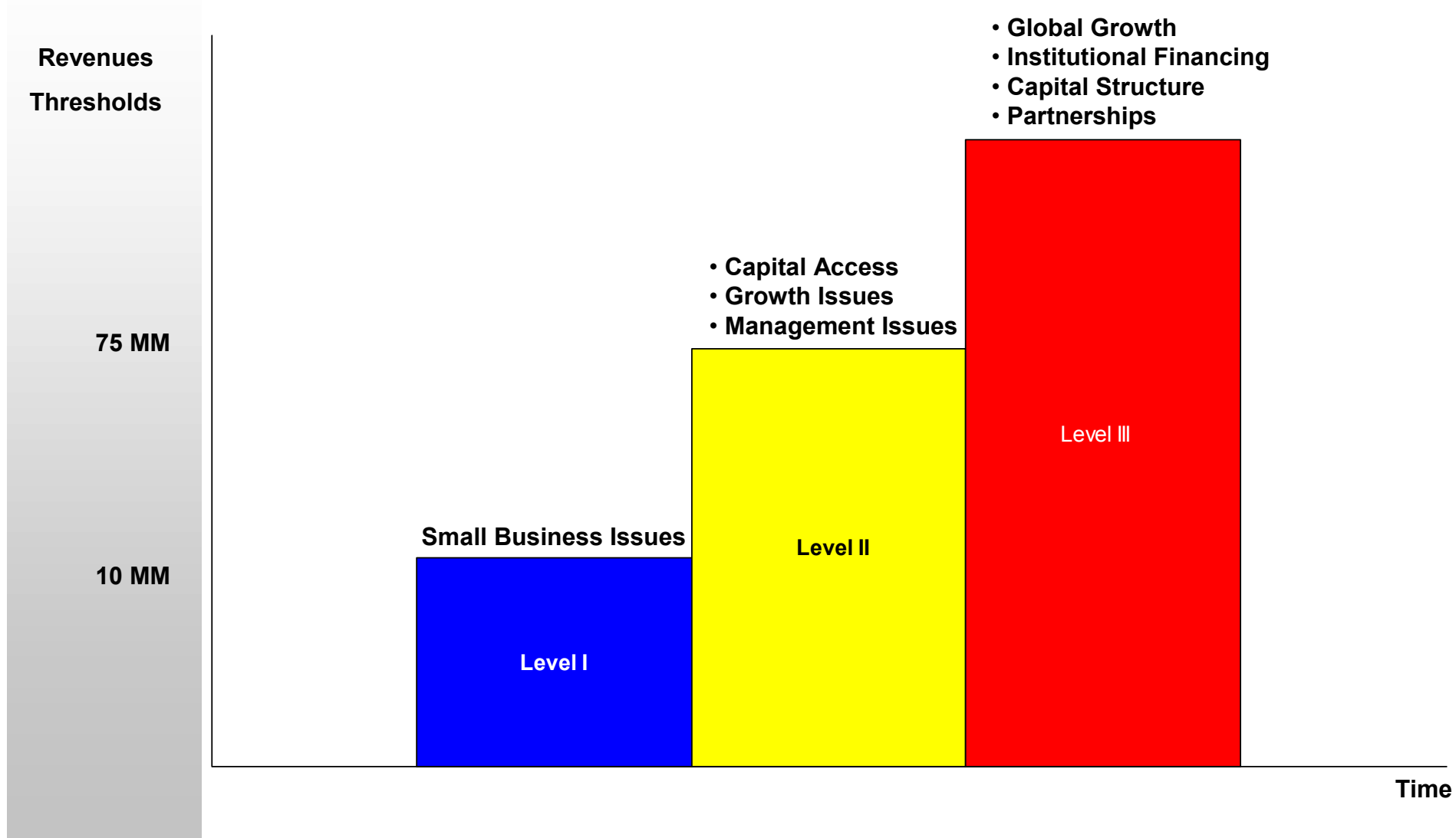
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Two companies with \$2 Billion in MBE spending (10% of total purchases)



A Multi-Tiered Approach To Minority Supplier Development Is Required

Different issues, different metrics, and different solutions!



The Asaba Group

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