China and India in the Global Automotive Industry
‘Synchronising Core Business Strategy for Successful Operations Internationally’

Eric Wallbank
October 2008
Agenda

► Overview comparison between China and India in the auto sector
► China
► India
Emerging Markets
Vehicle production in the “Rest of the World”

Note: Chinese production forecast to grow from 9.1M in 2008 to 17.1M in 2018 (way off the chart)
However, rapid growth is faltering

► India
  ► Market grew 2.8% year-on-year in September – the first rise in 2 months
  ► Passenger car sales expected to grow only 0.6% this year

► China
  ► Sales fell 1.4% in September, after a 6% fall in August
  ► Due to a slowing economy, rising fuel prices and natural disasters.
  ► Passenger car sales are up 6% over the first 9 months – half the growth rate of 2007

Sales growth in emerging markets is rarely continuous

The fundamentals are still sound for both countries:
  ► Large populations
  ► Low car ownership rates
  ► Growing GDP per head
# High-level comparison between India and China in the Auto sector

<table>
<thead>
<tr>
<th>China</th>
<th>India</th>
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<tbody>
<tr>
<td>Second largest auto market: 8m units/year</td>
<td>9th largest auto market: 2m units/year</td>
</tr>
<tr>
<td>VM production mainly as JVs with MNCs: product IP resides</td>
<td>Local VMs with own brands and IP</td>
</tr>
<tr>
<td>with the MNC</td>
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<tr>
<td>Products derivative or even seen as copies of existing</td>
<td>Local innovation – cheap Emerging market vehicles – the</td>
</tr>
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<td>existing products</td>
<td>global industry is watching</td>
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<tr>
<td>Limited vehicle exports to date – domestic consumption</td>
<td>Some VMs establishing India as a global source of</td>
</tr>
<tr>
<td>dominates</td>
<td>low-cost vehicles; local brands also exporting</td>
</tr>
<tr>
<td>Weak indigenous supply base - many JVs with MNCs in</td>
<td>Strong (but fragmented) local automotive supply industry</td>
</tr>
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<td>auto components</td>
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<td>Developing an engineering capability</td>
<td>Strong tradition and capability in Engineering: becoming a</td>
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<td>location for R&amp;D centres</td>
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<td>Inbound companies typically have to form JVs. Within the</td>
<td>More freedom to enter a market without forming a JV</td>
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<td>JV some activities are ‘owned’ by the Chinese JV</td>
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<tr>
<td>North America the main destination of component exports</td>
<td>Europe the main destination of components exports</td>
</tr>
<tr>
<td>Strong in Electronics (in all sectors)</td>
<td>Strong in castings, forgings, metal components and assemblies; also software</td>
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</table>
Agenda

► Overview comparison between China and India in the auto sector

► China

► India
China overview

- Top Vehicle Manufacturers:
  - SAIC
  - First Auto Works (FAW)
  - Dongfeng
  - Chang’an
  - Guangzhou
  - Chery
- Top CV Manufacturers:
  - FAW
  - Dongfeng
  - China Heavy Duty Truck

- Already third-largest light vehicle producing country, could surpass US and Japan for #1 by 2010
- Market growth of by at least 20% a year for the past three years
- Government encouraging consolidation to create 3-5 globally significant manufacturers within few years
- Local demand has absorbed production for recent years, strong export push possible after that; flood of new models from both foreign JVs and local makers driving down prices and spurring sales
- New taxes encouraging sales of smaller, more fuel-efficient vehicles
- Heavy and medium duty truck market dominated by national players, opportunity for JVs with international partners

2007 Chinese LV Production Share

- SAIC 17.5%
- FAW 14.7%
- Chang’an 9.1%
- Dongfeng 10.9%
- Guangzhou 5.8%
- Chery 5.1%
- Other 36.4%
China’s leading brands

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<tr>
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<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2007 Market Share %</th>
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<tbody>
<tr>
<td>VW</td>
<td>632,816</td>
<td>592,317</td>
<td>441,808</td>
<td>622,266</td>
<td>902,130</td>
<td>14.9</td>
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<td>Toyota</td>
<td>85,659</td>
<td>113,750</td>
<td>168,951</td>
<td>291,493</td>
<td>465,950</td>
<td>8.7</td>
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<td>Honda</td>
<td>123,322</td>
<td>215,909</td>
<td>258,037</td>
<td>324,268</td>
<td>422,835</td>
<td>7.9</td>
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<td>Buick</td>
<td>201,188</td>
<td>252,058</td>
<td>249,464</td>
<td>300,700</td>
<td>331,780</td>
<td>6.2</td>
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<td>Nissan</td>
<td>95,245</td>
<td>74,413</td>
<td>170,144</td>
<td>216,772</td>
<td>287,107</td>
<td>5.3</td>
</tr>
<tr>
<td>Chery</td>
<td>85,349</td>
<td>86,567</td>
<td>182,109</td>
<td>252,400</td>
<td>270,618</td>
<td>5.0</td>
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<tr>
<td>Hyundai</td>
<td>63,881</td>
<td>168,664</td>
<td>260,696</td>
<td>314,820</td>
<td>253,061</td>
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<td>Geely</td>
<td>74,335</td>
<td>102,776</td>
<td>150,678</td>
<td>204,331</td>
<td>219,512</td>
<td>4.1</td>
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<td>Chevrolet</td>
<td>3,912</td>
<td>11,795</td>
<td>100,560</td>
<td>145,459</td>
<td>192,806</td>
<td>3.6</td>
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<tr>
<td>FAW Tianjin</td>
<td>113,708</td>
<td>130,182</td>
<td>190,019</td>
<td>196,937</td>
<td>180,280</td>
<td>3.4</td>
</tr>
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</table>

Chery the leading ‘local’ brand: the others are produced in JVs between local producers and global vehicle manufacturers.
Some Market-leading vehicles in China

VW

Buick

Chery
Rising oil price and consumption tax adjustment could stimulate demand of small-engine cars: the consumption tax rises are:

- For models with engines larger than 4 liters is 40 percent, up from 20%
- For models with engines between 3 liters and 4 liters, a rise from 15% to 25%.
Vehicle Export & Import

- **Fast growth in January-June 2008 car imports**
  - China’s auto imports grew at a faster pace in January-June 2008, fueled by:
    - A stronger RMB
    - Possibility of higher taxes, which encouraged buyers to purchase earlier.
  - Vehicle imports rose 53% year-on-year to 212,800 units during January-June 2008, up 18 percentage points and three times the rate of overall passenger car sales growth.
  - Imports of SUVs in the first half jumped 79% to 108,500, accounting for nearly half of the total imports, a growth rate of 41 percentage points.

- **Chinese auto export growth slows**
  - China’s vehicle export growth slowed in January-June 2008 on economic controls and natural disasters (snowstorms and an earthquake).
  - Carmakers are boosting exports, with investments totaling at least US$20 billion by overseas automakers.
China's auto parts imports and exports increased in first half of 2008

► Imported automobile components totaled US$8 bn (Jan08-Jun08), up 20% over the same period last year
  ► Imports from Japan were US$3.2 billion, 39% of total imports.
  ► Other major import source countries were Germany, Korea, the U.S. and France.

► Total exports during Jan08-Jun08 were US$15 billion, a YOY increase of 21%.
  ► Exports to North America totalled US$4.1 billion, 26% of the total auto components exports.
  ► Other major target countries were Japan, Korea, Germany and the Netherlands.

► China’s auto part industry is very fragmented. There are over 5,000 companies, but only about 130 companies have annual sales of RMB100 million (US 12.4m) or more.

► Foreign invested auto parts manufacturers have a dominant market share in mid to high end product lines. Most of the world’s 1st tier suppliers have set up subsidiaries in China.

► China auto parts exports are beginning to accelerate, and the Ministry of Commerce has an ambitious plan to boost the export to US$120 billion in 10 years.
The Local Auto parts Manufacturers

- Currently there are four types of auto parts manufacturers in China:
  - Subsidiaries of major assemblers in the country
  - Auto parts factories set up by local government to support local assemblers
  - Private-owned enterprises, especially in China’s Jiangsu and Zhejiang Province
  - Foreign invested auto parts manufacturers, mostly JVs with top Chinese assemblers
- Many Chinese companies in the industry are under-scale and lack the necessary technical and financial resources to remain competitive in the growing market.
- Low entry barriers have enabled hundreds of companies to enter the market every year
- Industry consolidation, through Mergers and Acquisitions, is accelerating in recent years
- Smaller domestic Chinese parts producers are at an increasing disadvantage to global suppliers due to:
  - Often heavy debt loads
  - Lack of research and engineering expertise and facilities.
  - Rapidly increasing levels of vehicle technology sophistication, which is quickly surpassing their competitive abilities to produce or reproduce.
  - China’s accession to the World Trade Organization increasing global competition
- Such companies must either find capable partners or exit the industry.
Emerging Markets
China: Deal Environment

► China auto market is slowing in second half of 2008 due to surging material cost and softening of economy
► SAIC has taken a leading role in consolidating the market by M&A, including the 2007 merger with Nanjing Auto
► Still a fair amount of M&A deals in 2007 and 2008, mostly in the component and parts sector
► Chinese sellers prefer to maintain as much control as possible, while leveraging partner’s technology and global network
► Not many PE deals in auto manufacturing sector yet, Chinese companies not looking for just money, PE is relatively more active in dealership sub-sector
► Opportunity: minority investments in listed auto makers, including the potential IPOs of Chang’an and Guangzhou (there is a restriction of foreign ownership to 50% on car and engine joint ventures)
Unfavorable government policies towards multinational auto makers

► The China Automotive Industry is highly fragmented. The China government set policies and regulations to protect China’s automotive industry against multinational auto makers, meanwhile encourage its further development.

► Examples of protective policies:
  ► The China government issued China Automotive Industry Policy (the Policy) in 2005 to encourage consolidation among carmakers to boost their ability to compete with overseas competitor. According to the Policy, China only allows foreign auto makers to set up a maximum of two passenger-car and two commercial-vehicle joint ventures.
  ► By the end of 2007, the China government issued revised Catalogue for the Guidance of Foreign Investment Industries (the Catalogue). Per the Catalogue, Foreign investment shall not exceed 50% in joint venture companies manufacturing of complete automobiles.
There have been incidences of illegal copies of vehicles and automotive parts from time to time in the PRC automotive industry. Such misappropriation or infringement could have a material adverse effect on the financial condition, results of operation and company reputation of those intellectual property owners.

Companies seek to protect their intellectual property by taking certain measures. However, policing unauthorized use of intellectual property is difficult and sometimes practically impossible, and there is no assurance that the steps taken by companies will prevent misappropriation or infringement of the companies’ intellectual property rights.
Summary - China’s advantages:

► Huge domestic market already, with massive potential
► Huge strength in related sectors such as electronics
► Competitive manufacturing cost
► Building its own product IP and technical capability
► Political system means things can get done quickly
► Proximity to booming economies e.g. Asian countries
► Proximity to USA – shipping costs less than from other Low Cost Countries
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India overview

Top Vehicle Manufacturers:
- Maruti Udyog (Suzuki)
- Tata Motors
- Hyundai
- Mahindra & Mahindra (M&M)
- GM India
- Honda-Siel

Top CV Manufacturers:
- Tata Motors
- Ashok Leyland

India ranks as:
- The World’s Second largest 2-wheeler market
- Asia’s 3rd largest passenger car market
- The World’s 4th largest commercial vehicle market
- The World’s 5th largest bus and truck market (by volume)

Maruti (now majority owned by Suzuki) has dominated the market since deregulation in 1993 with its wide range of inexpensive small cars

Over 90% of vehicles sold in India cost <US$15K

After Suzuki, Hyundai was first foreign firm to set up own operations in the country, since joined by GM, Ford, Toyota, Honda and others

Tata Motors bought Jaguar & Land Rover, hope to launch Nano 1-lakh ($2,500) car later this year

Improvements to road network and infrastructure are the principal growth drivers of commercial vehicle segment, heavy truck market fell 15% in 2007 but is rebounding this year

2007 Indian LV Production Share

- Maruti 33.8%
- Hyundai 15.9%
- Tata 19.4%
- Mahindra 7.5%
- Other 23.4%
Indian passenger cars – key brands

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</thead>
<tbody>
<tr>
<td>Suzuki</td>
<td>52,010</td>
<td>52,315</td>
<td>-0.6</td>
<td>42.0</td>
<td>409,224</td>
<td>397,404</td>
<td>3.0</td>
<td>40.1</td>
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<tr>
<td>Tata</td>
<td>21,590</td>
<td>23,408</td>
<td>-7.8</td>
<td>17.4</td>
<td>174,617</td>
<td>183,864</td>
<td>-5.0</td>
<td>17.1</td>
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<tr>
<td>Hyundai</td>
<td>15,061</td>
<td>14,981</td>
<td>0.5</td>
<td>12.2</td>
<td>151,219</td>
<td>115,735</td>
<td>30.7</td>
<td>14.8</td>
</tr>
<tr>
<td>Mahindra &amp; Mahindra</td>
<td>13,222</td>
<td>15,487</td>
<td>-14.6</td>
<td>10.7</td>
<td>112,310</td>
<td>96,954</td>
<td>15.8</td>
<td>11.0</td>
</tr>
<tr>
<td>GM</td>
<td>4,415</td>
<td>2,969</td>
<td>48.7</td>
<td>3.6</td>
<td>27,114</td>
<td>17,945</td>
<td>51.1</td>
<td>2.7</td>
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<tr>
<td>Toyota</td>
<td>4,361</td>
<td>4,249</td>
<td>2.6</td>
<td>3.5</td>
<td>33,868</td>
<td>31,172</td>
<td>8.6</td>
<td>3.3</td>
</tr>
<tr>
<td>Honda</td>
<td>4,006</td>
<td>4,308</td>
<td>-7.0</td>
<td>3.2</td>
<td>34,744</td>
<td>35,067</td>
<td>-0.9</td>
<td>3.4</td>
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<tr>
<td>Ford</td>
<td>1,976</td>
<td>2,465</td>
<td>-19.8</td>
<td>1.6</td>
<td>15,660</td>
<td>24,020</td>
<td>-34.8</td>
<td>1.5</td>
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<tr>
<td>VW Group</td>
<td>1,943</td>
<td>845</td>
<td>129.9</td>
<td>1.6</td>
<td>12,420</td>
<td>6,981</td>
<td>77.9</td>
<td>1.2</td>
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<td>Renault</td>
<td>1,381</td>
<td>2,890</td>
<td>-52.2</td>
<td>1.1</td>
<td>14,096</td>
<td>8,056</td>
<td>75.0</td>
<td>1.4</td>
</tr>
</tbody>
</table>

- Maruti Suzuki – now controlled by Suzuki – continue to dominate the market
- A further two of the top 4 are local, independent companies
Indian market segmentation

The market is dominated by small vehicles
India’s best-selling vehicles

► Maruti

800

► Hyundai

i10

Indica, Indigo

► Tata

Indica

Nano

Swift

Getz
Indian automobiles: establishing its place in the global arena

- FY03 – FY08, Domestic sales grew at a CAGR of 10% while exports grew at a CAGR of 32%
  - Domestic passenger vehicles (PV) sales grew at a CAGR of 17%, while exports grew at a CAGR of 24.8%
  - Commercial vehicle (CV) segment reported a CAGR of 21% in domestic sales and 37% in exports
  - Two wheeler segment grew at a CAGR of 8.4% in domestic sales and 32% in exports
- Share of exports in total sales volume has increased from 3% in FY02 to 11% in FY08
  - Expected to reach USD 35 billion by 2016
- The recent decline in domestic sales is primarily attributed to increasing interest rates and input costs, resulting in a reduced demand from the highly price sensitive two and three wheeler market
  - However, the outlook for the overall industry continues to remain buoyant backed by the strong PV and CV demand
India is to become an auto manufacturing hub driven by investment plans by Global VMs

- Foreign carmakers have already invested USD 3 billion in India over the past five years
- SIAM estimates the investments to be around USD 9 million by FY09
  - Global VMs have already committed investments over US$ 6 billion to build small cars

<table>
<thead>
<tr>
<th>VMs</th>
<th>Amount</th>
<th>Investment Plans</th>
</tr>
</thead>
<tbody>
<tr>
<td>Daimler</td>
<td>USD 67m</td>
<td>Set up a plant for CVs at a capacity of 70,000 units p.a. through a JV with the Hero Group by 2013</td>
</tr>
<tr>
<td>Fiat India</td>
<td>USD 900m</td>
<td>To achieve a production capacity of 200,000 cars, 300,000 engines and 300,000 spare parts annually by 2012 at its plant near Pune</td>
</tr>
<tr>
<td>Ford India</td>
<td>USD 500 million</td>
<td>Expand its Chennai plant to a capacity of 50,000 units p.a. and eventually to 200,000, start of production of a new car, and set up an engine plant by 2010</td>
</tr>
<tr>
<td>General Motors</td>
<td>USD 300–400 million</td>
<td>Set up an one million engines facility in India, making it an export hub for Asia</td>
</tr>
<tr>
<td>Honda Siel Cars</td>
<td>USD 650m by 2016</td>
<td>Set up a powertrain facility with a capacity of 200,000 units p.a. and capacity expansion of its Noida plant by 50,000 units</td>
</tr>
<tr>
<td>Hyundai Motors</td>
<td>USD 40 million</td>
<td>Set up a R&amp;D center in Hyderabad, focusing on CAD and engineering for its global operations</td>
</tr>
<tr>
<td>Maruti Suzuki</td>
<td>USD 4 billion</td>
<td>Set up a R&amp;D center, a new car plant, up-gradation of the Gurgaon plant, set up a diesel engine facility, and in marketing initiatives</td>
</tr>
<tr>
<td>Volkswagen</td>
<td>EUR 580 million</td>
<td>Manufacture ‘Fabia’ at its new plant in Pune, and expand capacity of Aurangabad plant to 30,000 vehicle p.a. by the end of 2008</td>
</tr>
<tr>
<td>Volvo</td>
<td>na</td>
<td>To double the production of construction equipment unit in Bangaluru to 2,000 units</td>
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### Vehicle Manufacturers leveraging India's competitive advantage

<table>
<thead>
<tr>
<th>Planning to make India a vehicle Export Hub</th>
<th>Producing in India mainly for the for local market</th>
<th>India a component Sourcing Hub for Global Operations</th>
<th>India as an R&amp;D centre</th>
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<tbody>
<tr>
<td>Suzuki</td>
<td>Audi</td>
<td>BMW</td>
<td>Honda</td>
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<tr>
<td>Toyota</td>
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<td>Hyundai*</td>
<td>Daimler</td>
<td>GM</td>
<td>Suzuki</td>
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<tr>
<td>Renault/Nissan*</td>
<td>Fiat</td>
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<td>Ford</td>
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<td>GM</td>
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<td>Honda</td>
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<td>Isuzu</td>
<td>Peugeot</td>
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<td>Toyota</td>
<td>Renault/Nissan</td>
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<td>Suzuki</td>
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<td>VW</td>
<td>VW</td>
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<tr>
<td></td>
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<td>Volvo (Trucks)</td>
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* = Ultra Low Cost Car
Auto components: exciting time ahead

► FY04 - FY08, Auto components turnover grew at a CAGR of 28%, and exports grew 29% CAGR

► Growth drivers include:
  ► Growing domestic market and replacement parts demand
  ► Increasing outsourcing by global VMs

► The sector is fragmented with ~500 players in the organized sector and ~2,000 small and medium enterprises
  ► Organized sector contributes around 77% to the total auto components production
  ► Around 40% of which are JVs with foreign players
  ► Nearly every large global Tier 1 player has a presence in the country

► Major export regions are the US and Europe, accounting for almost 60% of total exports

► ACMA estimates the turnover of auto components in the country to reach USD 40 billion and exports to USD 20.9 billion by FY16
Emerging trends in the auto space

Pioneering the evolution of ‘ultra low cost’ cars

► The launch of Nano is set to revolutionize the PV segment, also showcasing India as an innovation hub
► Other VMs looking at launching cars in this segment, e.g.: Renault-Nissan (along with Bajaj Auto)—developing a USD 2,500 car for the Indian market
► VMs including GM, Hyundai, Honda, Toyota, Renault, and VW are planning to increase their presence in the small car segment.

Domestic players adopting inorganic route to expand international presence

► Indian VMs are establishing their footprint in the global automotive arena through acquisitions and alliances
  ► Tata Motors acquisition of Jaguar and Land Rover brands, and other acquisitions and JVs
  ► M & M - acquired in the engineering and forgings sectors
  ► Ashok Leyland — engineering and truck businesses

CVs to benefit from increasing infrastructure activity and heightened international interest

► Development of road network and infrastructure are driving the growth in the segment
► Global majors are adopting the joint-venture (JV) route to enter the fourth largest CV market in the world
► Entry of global players is likely to drive domestic manufacturers to enhance their focus on R&D initiatives and accelerate product development activities

Two and Three wheeler manufacturers are in a move to diversify

► Increasing availability of small, affordable cars has helped expansion of the passenger car market, affecting two/three wheeler demand
► This has lead two wheeler manufacturers to diversify:
  ► Hero Group is venturing into the CV segment through a 40:60 JV with Daimler
  ► Bajaj Auto is partnering with Renault-Nissan to enter the PV segment
Emerging trends in the auto space (continued)

- The Indian auto components industry has transitioned into the second wave of JVs, forming technical as well as production alliances with major global players.
- While Indian firms are increasingly expanding their scale of operations, these tie-ups help them move up the value chain and leverage the technological capabilities of their partners.

Auto components benefiting from global partnerships and alliances

- Increased R&D sourcing from the country

  - India's automobile and aerospace design industry is estimated between USD 3 - 5 billion annually; expected to grow to USD 16 billion by FY11.
  - Indian players are increasingly leveraging the country's software prowess (use of high-end software in automobile design and R&D).
  - Players are developing their R&D capabilities through organic as well as the inorganic route.
    - M&M is opening its USD 116 million auto R&D centre.
    - Dassault Systemes, France, has tied up with Argentum Engineering Design's Centre for Excellence to train automobile engineers.

- Auto retail is at a nascent stage in the country.
- Competition in the segment is set to intensify as more players are entering the segment offering servicing, parts retailing, auto finance, or used vehicles.
- Used vehicle market is also growing rapidly.
  - A number of VMs including have entered the used vehicle business.

Auto retail catching up in the country

- Indigenous product development:
  - Tata Motors: Indica, Indigo, Ace, Nano.
  - M&M: Scorpio.
  - Bajaj Auto: Pulsar.
- Local product development by global VMs and auto component companies.
Industry Challenges

► Infrastructure
  ► Roads, railways, seaports and airports: capacity constraints. In the process of being expanded / upgraded.
  ► Electricity: shortage in some states. Captive backup power required. Cost is also high.

► Labor
  ► Multiplicity of labor laws
  ► Lay-offs and retrenchment of permanent labor difficult
  ► Productivity (in general) lower than in China

► Taxation
  ► Multiple indirect taxes which have a cascading effect
  ► Higher tax rates than China
  ► Reducing import duties

► Business Environment
  ► Rising input prices
  ► Appreciating Rupee
Government initiatives for the industry

► The Government, together with the Industry, has drafted a ten year Automotive Mission Plan (AMP), promoting
  ► Manufacture of vehicles and components
  ► Export of services in areas such as design, engineering, and back office operations.

► Key objectives of the AMP by 2016:
  ► Increase sector turnover from US$35bn to US$145bn
  ► Increase employment to 25 million
  ► Increase exports from US$4bn to US$35bn

► Implementation of the National Automotive Testing and R&D Infrastructure Project (NATRIP) that aims at
  ► Setting up world-class automotive testing and R&D infrastructure in the country
  ► Facilitating introduction of world-class automotive safety, emission and performance standards in India
  ► To ensure seamless integration of Indian automotive industry with the global industry.
Summary - India’s advantages

- Huge potential market, already above critical mass in the sector
- Engineering traditions and capability, coupled with high quality standards
- Competitive manufacturing cost
- Recognisable commercial traditions and legal frameworks
- Stable economic policies - continuity in reforms and policies
- Proximity to booming economies like Asian countries and Africa.
- Proximity to Europe – shipping costs less than from other Low Cost countries
Questions?

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