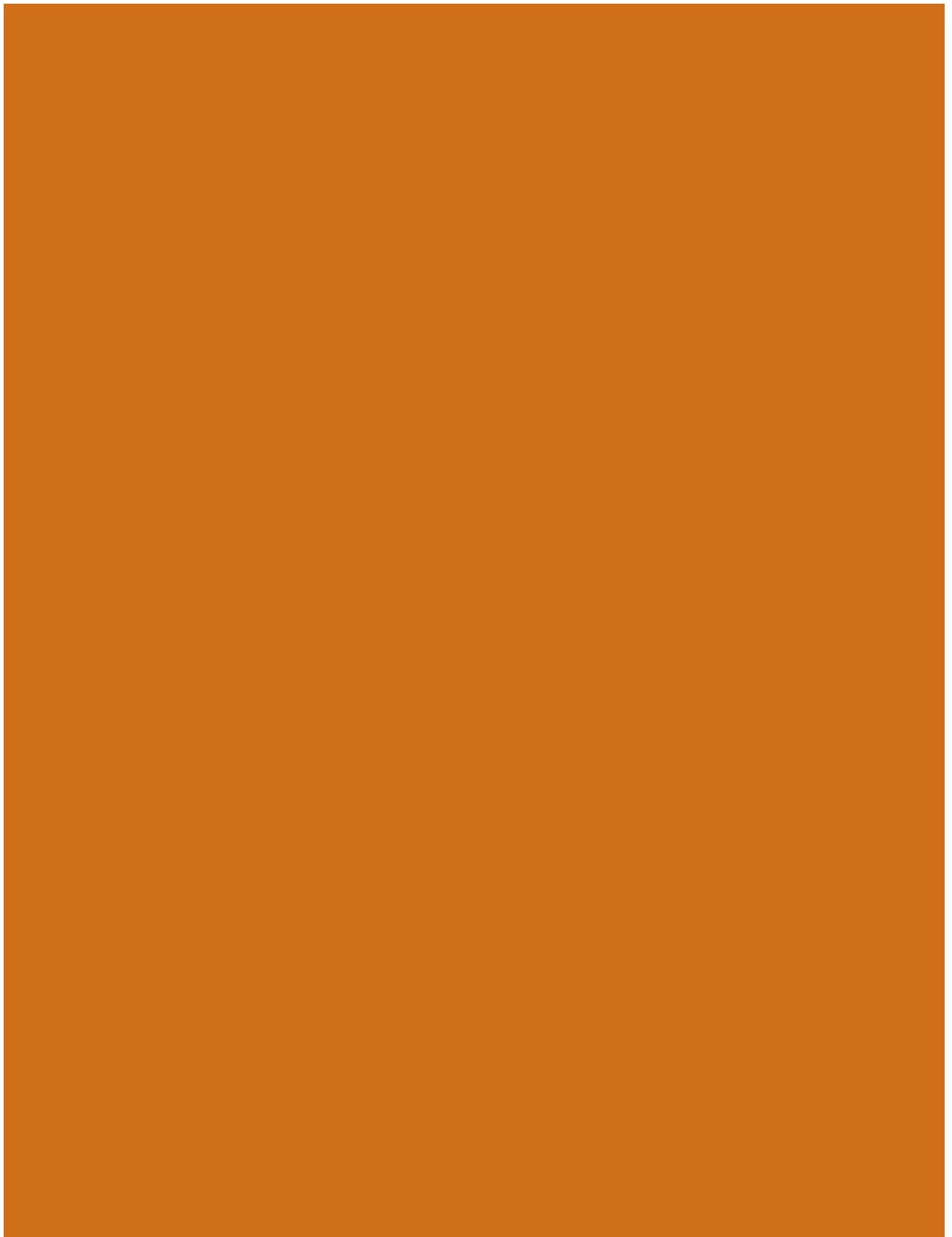


Transaction Services

# Drive value

Automotive M&A Insights 2009





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M&A will continue to drive the fundamental changes necessary for the near-term restructuring and long-term sustainability of the automotive value chain.

The heart of the matter

Distress caused global transaction value to soar as the industry restructured. Going forward, companies are continuously shifting focus from survival to growth.

We will long remember 2009 as one of the most turbulent and dynamic years in the global auto industry as the worldwide financial crisis and ensuing collapse of vehicle sales in North America culminated in the operational, financial and structural restructuring of the sector. Elsewhere, the deployment of market stimulus programs spurred a shift in the balance of automotive power from West to East that will likely become more pronounced as future cross-border deal flow anchors this position.

Distress caused multiple change-of-control situations, particularly in 2009's mega deals, causing global transaction value to soar to the highest on record. It also pushed banks, governments, and other debt holders, willingly or not, into equity positions. However, the distortion in deal value also brings with it the reality of a fragmented industry encumbered with excess capacity and guilty of destroying value prior to the downturn. These problems persist, making the political and social barriers to exit higher than ever as the traditional bastions of the industry wrestle with emerging competitors.

On the heels of a down deal market in 2008, the number of conventional mergers and acquisitions (M&A) remained depressed throughout 2009, evidenced by particularly weak middle-market activity as strategic

buyers were less willing to expend their limited cash reserves or take on additional debt. In addition, 2009 witnessed the limited reengagement of traditional financial buyers through nonconventional deal structures and the entrance of sovereign wealth funds as an alternate avenue to raise capital in a restricted credit lending environment.

Although deal activity was down sequentially for the past two years, we are now at a point in the cyclical recovery where those companies with stronger operating models and cash positions will likely leverage M&A to develop sustainable competitive advantage through the consolidation of scale and expertise. The recovery represents a critical period for industry players to achieve share growth that would otherwise be difficult to attain in a steady state market.

In early 2010, the operating environment is showing positive signs that the stress placed on the sector over the past two years has begun to effect meaningful change. While we embark on what will no doubt be a nonlinear path to recovery, it will likely ultimately fall to the industry's consolidators, both strategic and financial, to keep the momentum in delivering a healthier end state or risk falling victim to complacency and the dilution of urgency that upturns often bring.

An in-depth discussion

An unprecedented level of government involvement drove deal value distortion in 2009, while the broader deal market remained anaemic following the industry's near collapse.

# Global M&A trends

## Volume drops, but value soars as industry restructures

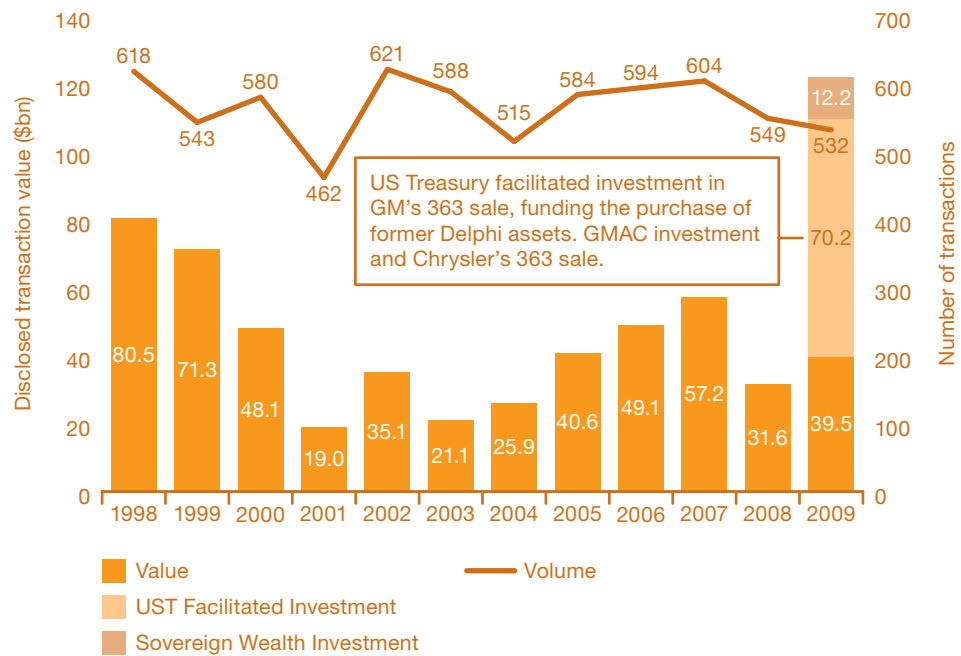
The industry-wide restructuring in 2009 was necessitated by the near collapse of the automotive industry in the previous year. The onset of the global financial crisis left the world's economies with weak credit markets and eroding consumer confidence. Coupled with soaring fuel prices in the second quarter of 2009, these trends drove a precipitous drop in vehicle sales, leaving major automakers and suppliers at the brink of bankruptcy.

Players across the automotive value chain reacted as they sought capital infusions, shed noncore assets, renegotiated debt obligations, and pursued mergers of

necessity. These restructuring efforts were captured in the automotive deal market, which includes targets in the vehicle manufacturer (VM), component supplier, retail, vehicle finance, leasing, rental, and other related sectors. Disclosed transaction value soared to \$121.9 billion for 2009, up 286 percent from a mere \$31.6 billion in 2008 (hereafter, deal values refers to disclosed values only).

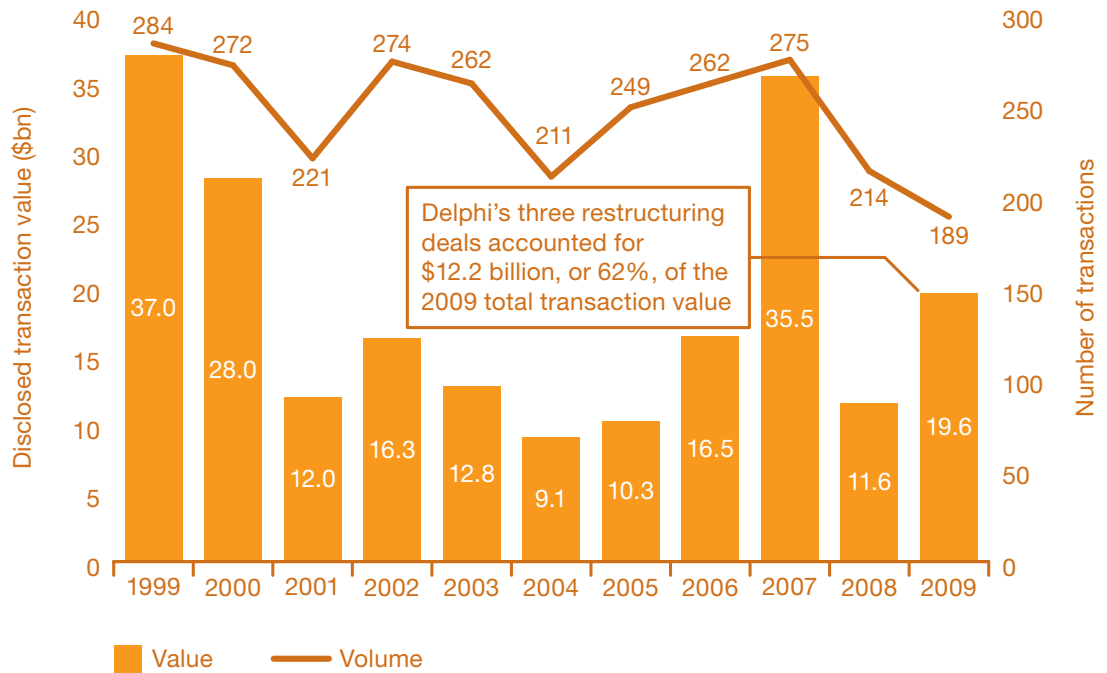
However, despite the headline figures, the deal market was anything but normal or robust. Total deal volume (disclosed and undisclosed) fell to 532 transactions — a modest decline of 3 percent from an already weak 2008 level but its lowest point since 2004.

**Global automotive M&A activity, 1999–2009**



Source: Thomson Reuters and other publicly available sources

### Automotive component supplier M&A activity, 1999–2009



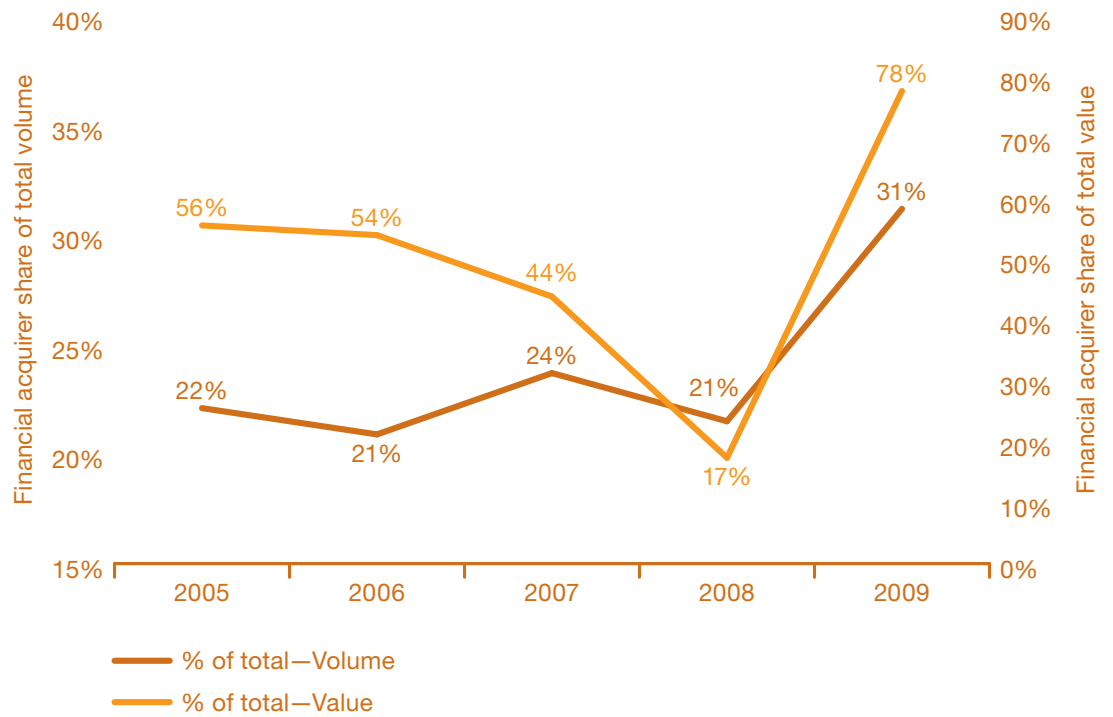
Source: Thomson Reuters and other publicly available sources

The sizable increase in deal value and the ongoing decline in deal volume underscore the presence of a handful of very large deals amid an otherwise quiet deal market. The top 10 deals in 2009, each valued at more than \$2 billion, accounted for \$112.4 billion, or 92 percent, of disclosed deal value, versus only \$21 billion, or 66 percent, in 2008. Prolonged weakness in the credit markets and uncertainty in the equity markets made it difficult for both corporate and financial buyers, apart from government, to finance deals, let alone find suitable targets. Although low equity prices arguably created opportunities for buying undervalued assets, the downside risk of bankruptcy left many buyers weary of investing.

### Reascendancy of financial investors

Acquisitions by financial buyers, broadly defined, not only rebounded from their 2008 lows, but also led much of the M&A activity in 2009. The evidence shows in record highs in financial buyer transaction value and volume, as well as their respective shares of global automotive M&A activity. Financial acquisition activity drove 78 percent of deal value, which is much larger than its historical share and more than triple its share in 2008. These acquisitions also accounted for 31 percent of total deal volume, as opposed to the historical average of 22 percent for 2005 through 2008.

### Financial acquirer share of global automotive M&A activity, 2005–2009



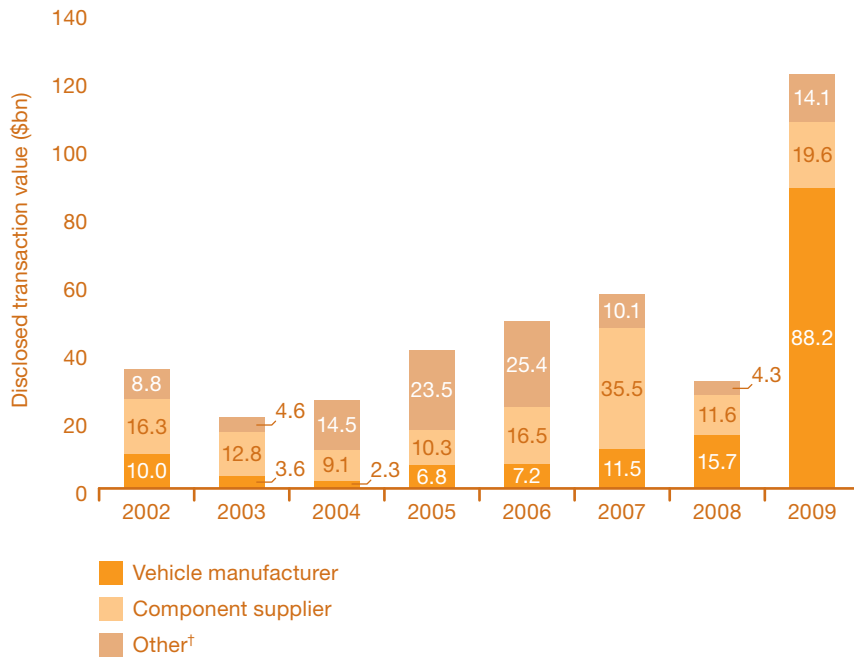
Source: Thomson Reuters and other publicly available sources

However, the growth in 2009 was not driven by private equity buyers, who had led financial acquisition activity in previous years, but by creditors, including the US government. Among the 13 acquisitions by financial investors valued at \$100 million or more, seven were restructuring deals. In these cases, control of the target company shifted as existing debt holders were granted equity positions or as new investors acquired distressed assets or liabilities in exchange for an equity stake.

The more conventional methods of deal financing, namely cash, debt, and equity exchanges, were less feasible than they

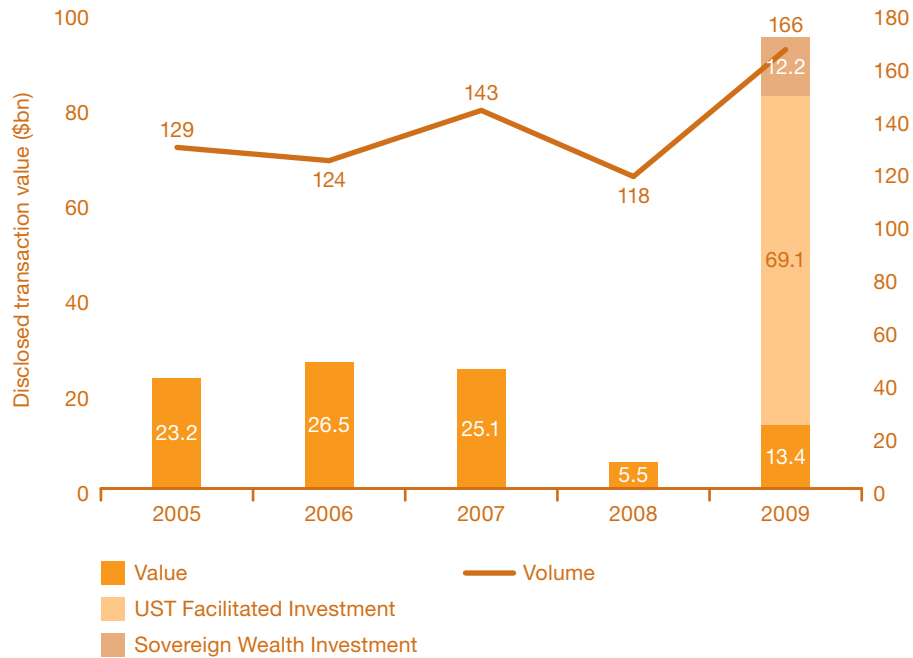
had been in the past, as strategic investors sought to conserve capital throughout the downturn. Cash was limited because of poor revenue performance and overleveraging, debt was less accessible because of the weak credit markets, and the exchange of shares between the target and acquirer was avoided because of depressed equity prices. Many of the entities that were able to make sizable acquisitions during 2009 used less conventional means of financing. An increasingly popular method, which enabled several restructuring deals, is the acquisition of distressed debt or liabilities in exchange for an equity stake.

### Global automotive M&A activity by sector, 2002–2009



† “Other” classification includes retail, aftermarket, rental/leasing and wholesale transactions  
 Source: Thomson Reuters and other publicly available sources

### Financial acquirer global automotive M&A activity, 2005–2009



Source: Thomson Reuters and other publicly available sources

Seven financial acquisitions exceeded \$1 billion in transacted value. Among these, five were restructurings — four of which were financed by the US Treasury — and the remaining two were investments made by sovereign wealth funds:

- The US Department of the Treasury led acquirer activity by investing \$69.1 billion to restructure GM, Chrysler, and GMAC — the last of which entailed two separate deals. There were also two sovereign wealth fund investments, in Volkswagen and Daimler, respectively. Each of these deals will be discussed further in the upcoming section titled “Issues in focus: Government investment.”
- Thus, only one of these seven deals was led by commercial investors: the \$11 billion restructuring transaction between Delphi Corporation and its creditors Elliot Management and Silver Point Capital. Having spent nearly four years in Chapter 11 bankruptcy, Delphi restructured under Section 363 of the US Bankruptcy Code. In doing so, Delphi divested several business operations, released its pension liabilities, and ceded ownership and control to its creditors. Three of its divestitures occurred in 2009, totaling \$1.2 billion. Delphi divested its steering business and four of its component manufacturing facilities to GM, which financed the deal using funds from the US Treasury. Delphi also sold its brake and suspension businesses to Beijing West Industries Co. and its exhaust business to Bienes Turgon SA de CV. The Pension Benefit Guaranty Corporation (PBGC) assumed \$6.6 billion in pension liabilities as part of the larger restructuring deal.

Moreover, the ascendancy of government and financial investors is not a surprise given the recent turmoil in the credit markets and

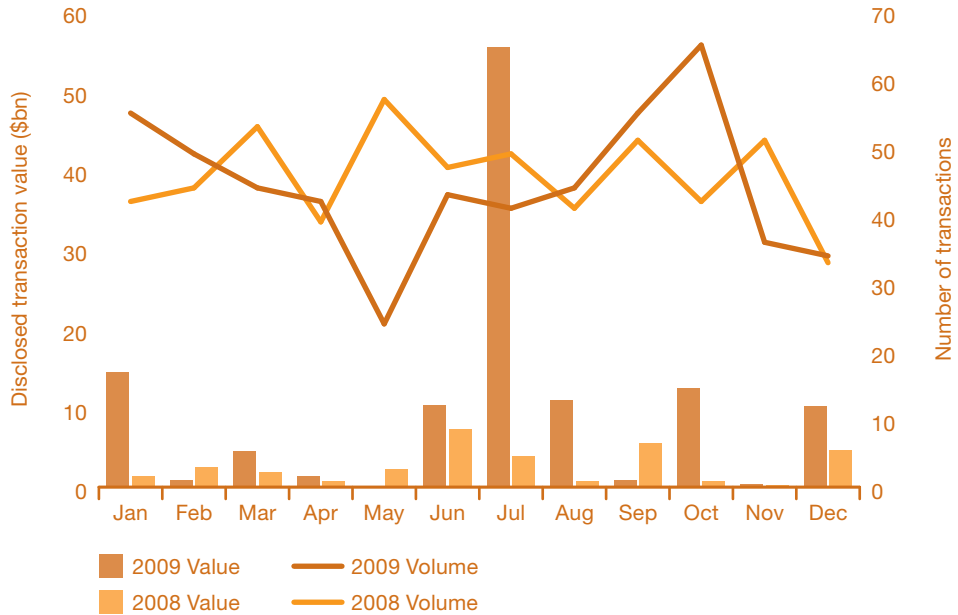
its impact on corporate or trade buyers. Strategic buyers who needed to protect their cash reserves were less willing to expend their limited cash or take on additional debt. As a result, strategic acquisition activity, which historically drove nearly 80 percent of deal volume, accounted for only 69 percent in 2009.

Among the 10 deals valued at more than \$2 billion, only three were strategic acquisitions, and each of these deals was initiated prior to 2009:

- Early in 2009, Porsche continued its pursuit of Volkswagen AG (VW) by acquiring a majority position of 51 percent. However, the takeover attempt left Porsche highly leveraged and susceptible to a reverse takeover by VW. Having acquired 49.9 percent of Porsche in 2009 VW has positioned itself to complete its acquisition by 2011. In a separate transaction, Volkswagen sold its Brazilian truck and bus manufacturing unit to MAN AG, a European industrial manufacturer.
- The other strategic transaction was between Schaeffler KG, a German manufacturer of rolling bearings, and Continental AG, a German automotive component supplier, for \$16.3 billion. Schaeffler KG continued its hostile pursuit of Continental by raising its stake close to 90 percent. Consequently, Schaeffler has seen Continental’s share price drop. Early in 2010, Schaeffler adopted a limited liability structure to allow outside investment, and Continental raised capital through an equity offering in order to refinance its debt obligations. After the capital increase, Schaeffler’s stake dipped to 75.1 percent. The two companies have yet to identify a time frame for completing the merger.

## A volatile year for value, volume, and flow

Monthly automotive M&A activity, 2009 vs. 2008

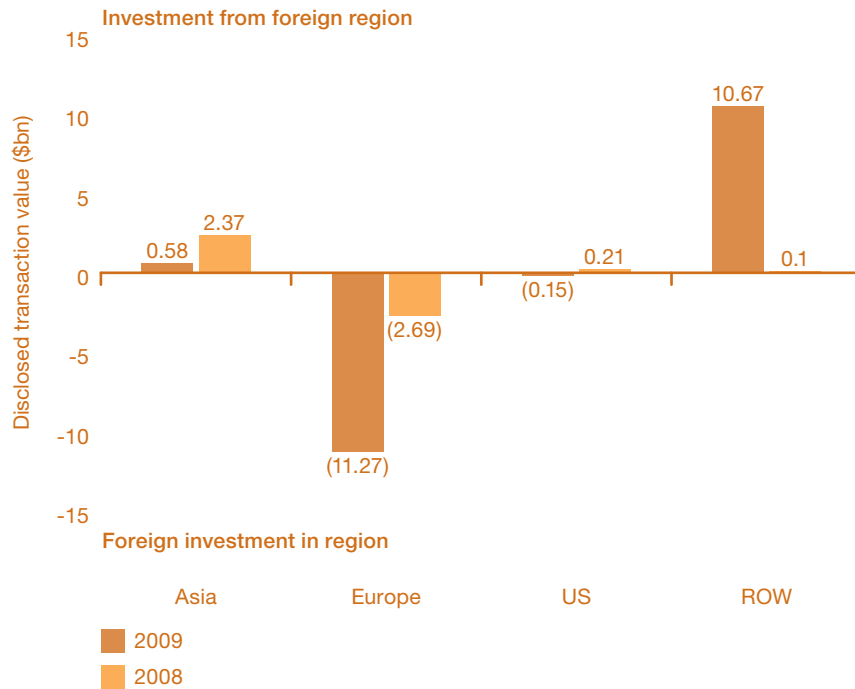


Source: Thomson Reuters and other publicly available sources

For M&A activity, 2009 was a particularly volatile year according to several metrics. The astronomical deal value of \$55.4 billion in July 2009, for example, resulted almost entirely from General Motors' restructuring, which accounted for 99.8 percent of the month's transacted deal value. However, monthly deal values were higher than their 2008 levels for nine of the 12 months, suggesting that the rebound in value was not just the result of a few isolated megadeals. In fact, 13 deals were valued at more than \$1 billion in 2009, versus only seven in 2008. Nonetheless, weak middle-market deal activity indicates that the deal market was far from healthy: The number of deals valued between \$50 million and \$500 million dropped 53 percent from 2008.

Monthly deal volume was also very volatile, as indicated by the trough in May and peak in October. In May 2009, players across the automotive industry awaited the fates of General Motors, Chrysler, and GMAC, all of which received funding from the US Department of the Treasury within the following two months. In October 2009, the abnormally high volume could be indicative of the industry's response to the major restructuring events in the VM sector a few months earlier as well as to early signs of a market bottom. Only three of October's 65 transactions were in the VM sector, indicating that the remaining industry participants were consolidating or restructuring in response to these changes.

### Net deal flow by region, 2009 vs. 2008



Source: Thomson Reuters and other publicly available sources

This was an unpredictable year for cross-border M&A as well. Cross-border transaction value totaled \$15.4 billion in 2009, up 160 percent from its 2008 value, but accounted for only 13 percent of total deal value, versus 19 percent in 2008. Inflow and outflow trends exhibited several characteristics in response to 2009 market conditions, including the use of M&A to build scale and density in familiar geographies and risk avoidance, since cross-border deals often involve greater risks than indigenous markets. In accordance with these trends, net outflows from Asia declined more than 75 percent, and deal flow into the United States exceeded outflows by only a small amount. However, these declines were dwarfed by a 320 percent increase in net inflows to Europe and a tenfold increase in net outflows from the rest of the world, driven by the two multibillion-dollar sovereign wealth fund investments from Qatar and the United Arab Emirates in Volkswagen and Daimler, respectively.

Overall, the automotive deal market was erratic, to say the least, in 2009. Transaction value reached a record high, while the number of transactions continued to decline. Major players across the value chain underwent large-scale restructurings with the ultimate goal of returning to the industry as leaner, more profitable companies prepared to meet changing consumer demands. Meanwhile, many players were either unable or unwilling to pursue transactions because of weak credit markets, cash conservation, and uncertainty over the state of the industry. The future health of the automotive industry and its deal market will depend on several factors, such as successful completion of companies' restructuring plans, strengthening of the credit markets, and revival of consumer demand.



## Issue in focus: Government investment

“The collapse of the automakers could devastate the Midwest beyond imagination. We were determined not to fail.”

Steven Rattner

Direct government action was pervasive in the automotive industry in 2009. Tax changes and incentives were used to stimulate markets and protect companies around the world. China, for example, reduced purchase taxes for certain passenger vehicles, offered a car subsidy program for rural areas to replace their light trucks with new vehicles, and gave additional subsidies for vehicle scrappage. The French government provided sizable, low-interest loans to Renault under the condition that the automaker maintain production in France. Sweden guaranteed a \$563 million European Investment Bank loan for Saab, which facilitated the deal announced in January 2010 in which GM would sell its Saab brand to Spyker Car N.V.

Some governments took a more active role by investing directly in particular automotive companies. In the past, state-owned enterprises in China and Russia were typical examples of government investment in the automotive industry. Last year, state-owned enterprises or government-run investment vehicles from China, Russia, France, and Canada invested in automotive firms or their divested assets in 11 deals totaling just short of \$500 million. This year, government investment took a new shape, however, as governments operated in a capacity similar to distressed investors. The unprecedented level of investment was evident in the automotive deal market, where transactions by government treasury departments and sovereign wealth funds totaled \$84.4 billion in 2009, or 68 percent of total disclosed value.

The US Department of the Treasury was the driving force behind the restructuring of the US automotive industry. The department coordinated and funded the restructurings of General Motors, Chrysler, and GMAC; facilitated the deal between Chrysler and Fiat SpA; and funded GM's purchase of assets formerly owned by Delphi Corporation and

American Axle and Manufacturing Holdings Inc. Collectively, these deals accounted for \$70.2 billion, or 84 percent of deal value in the United States.

Moreover, two Middle Eastern sovereign wealth funds boosted 2009 transaction value by \$12.2 billion through their investments in Volkswagen and Daimler, respectively.

### Government investment varies by sector

The VM sector accounted for \$70 billion of the \$82.4 billion in government-driven transaction value for the industry. Liquidation by either GM or Chrysler, if not both, would likely have affected employment drastically, not only in the VM sector, but in other automotive and peripheral sectors as well. Realizing the consequences of this employment multiplier effect, the US government decided to commit billions of dollars toward restructuring both companies.

The restructuring of General Motors alone accounted for 45 percent of the year's transacted value and was the largest automotive transaction in history. In July, the US Treasury committed \$55.3 billion to acquire a 61 percent stake in the struggling vehicle manufacturer, leaving the remaining shares divided among the Canadian and Ontario governments; the United Auto Workers' Voluntary Employee Beneficiary Association (UAW VEBA); and the Motors Liquidation Company. The latter entity was formed to house GM's remaining assets to be liquidated, such as its discontinued brands and factories slated for closure. Structured as a sale under Section 363 of the US Bankruptcy Code, the deal allowed the formation of a new entity to acquire the operating assets from the bankrupt GM, which enabled the deal to close quickly. This major restructuring deal was also accompanied by a separate transaction in which GM utilized \$1.1 billion

of its funding from the US Treasury to buy Delphi's steering business, four component manufacturing facilities, and other related assets.

In late April, the US Treasury Department committed \$2.5 billion toward restructuring Chrysler — a proportionally larger investment than the one in GM given the companies' relative revenues.<sup>1</sup> As part of the deal, the US government essentially brokered the strategic alliance between Fiat SpA and Chrysler, enabling Fiat to acquire a 20 percent stake in Chrysler with options to increase its stake to 35 percent. Although Fiat was not required to commit any cash to gain this equity position, the stakeholders agreed on a strategic alliance in which Fiat would enable Chrysler to leverage Fiat's technology and products for sale in the United States. Despite this high involvement, the US Treasury took a relatively small stake. As part of a newly formed holding entity, also created under Section 363 of the Bankruptcy Code, the US Treasury and the Canadian government acquired a mere 10 percent, leaving the remaining 55 percent to the UAW VEBA.

Investments from sovereign wealth funds also shaped M&A activity in the VM sector. Faced with limited access to financing, vehicle manufacturers looked to sovereign wealth funds to provide capital infusions. Sovereign wealth funds are potentially very attractive investment sources in that they share the long-term investing horizon that a strategic investor would have without the integration challenges that can destroy deal value. In March, Aabar Investments PJSC of the United Arab Emirates invested \$2.7 billion to acquire a 9.1 percent stake in Daimler AG. This stake provided

the automaker with an anchor investor and additional liquidity amid weak demand for its luxury car brand, Mercedes-Benz. As part of the deal, Aabar acquired 40 percent of Daimler's stake in Tesla Motors Inc., which will enable Aabar to cooperate with Daimler in the development of electric vehicles and the reduction of CO2 emissions.<sup>2</sup> The International Petroleum Investment Company, owned by the emirate of Abu Dhabi, is Aabar's largest shareholder.

Then, in August, the Qatar Investment Authority (QIA) invested \$9.6 billion in VW AG. In doing so, QIA acquired 17 percent of VW AG shares from Porsche, raising its stake to 19 percent, while also acquiring a 10 percent stake and a board seat in Porsche. This infusion helped Volkswagen complete its reverse takeover of Porsche in December by providing the capital to pay down Porsche's debt and avoid excessive leverage. The result is that roughly two-fifths of Volkswagen is now government owned, including the existing stake held by the German state of Lower Saxony.

Transaction value in other major sectors — retail, aftermarket, rental/leasing, and wholesale automotive — was also dominated by the US Treasury through its \$11.3 billion investment in the restructuring of the struggling lender and automotive financing company GMAC. As the economic environment challenged discretionary spending, hampered credit availability and accessibility further impeded vehicle sales. By bailing out GMAC, the US Treasury aimed to support the consumer financing that would ultimately stimulate car sales and an industry-wide recovery. This investment had strategic benefits in that support for GMAC would enable

1. Steven Rattner, "The Auto Bailout: How We Did It," *Fortune Magazine*, November 9, 2009.

2. Thomas Fröhlich, "Daimler and Aabar share investment in Tesla," Daimler Communications, July 13, 2009.

more accessible financing for GM and Chrysler cars, ultimately strengthening the likelihood of loan repayment from these vehicle manufacturers. To supplement its direct investments in these sectors, the US government also stimulated car sales through consumer subsidies, namely the Car Allowance Rebate System, commonly referred to as “Cash for Clunkers.”

Meanwhile, the US government played a smaller role in the component supplier sector. Among the sector’s top 10 deals, only one, the purchase of Delphi’s steering business by General Motors, was facilitated by the US government, and that deal accounted for only 2 percent of the combined transaction value of the GM and Chrysler restructurings.

Outside the realm of M&A, the US government provided some support to this sector to maintain a sustainable base of component supply to vehicle manufacturers. The volatile production schedules of vehicle manufacturers, particularly those of GM and Chrysler, were impairing working capital among component suppliers. Through the Auto Supplier Support Program, the US Treasury made up to \$5 billion in financing available to US auto suppliers. The program consisted of two key measures intended to ensure suppliers’ financial stability: The Treasury backed payments from vehicle manufacturers to suppliers; the program also enabled suppliers to sell their receivables into the program to obtain capital more quickly. At the outset, intervention in this sector was supported because of the need for a sustainable base of parts supply to the struggling vehicle manufacturers. However, as government intervention grew across industries, concerns arose over setting a precedent for bailing out failing companies.

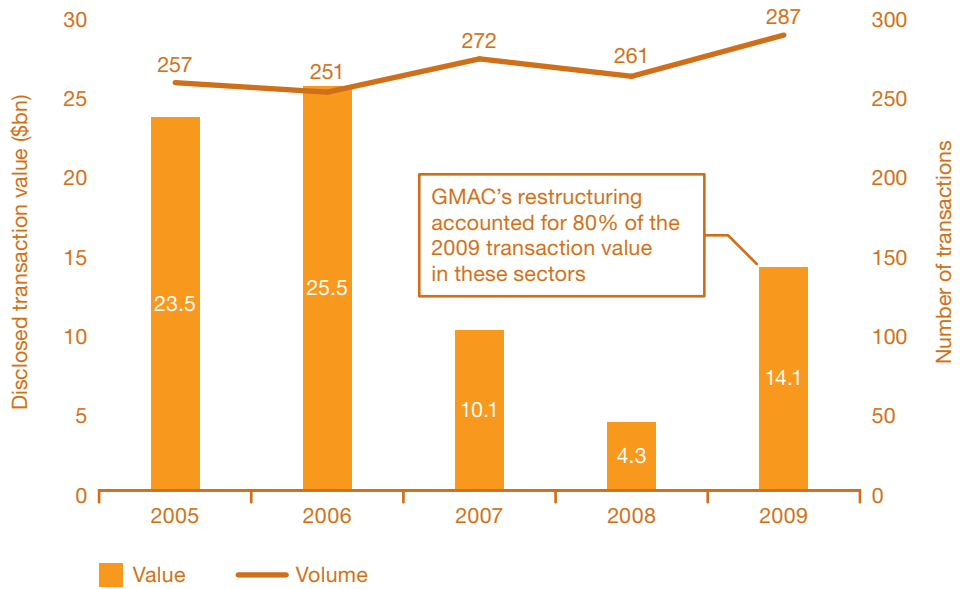
Although these multibillion-dollar investments by governments will affect the industry for years to come, they do not set the tone for M&A activity in the coming years. The past two years marked the rare confluence of events that led to intervention by governments around the world. In the particular case of the US automotive industry, it was deemed that liquidation of a major vehicle manufacturer would place too great a burden on employment and consumption. Moreover, providing capital in the form of loans would leverage the struggling companies to unsustainable levels, so the US Treasury acquired equity stakes. Global government actions appear to have been focused on managing downside risks and preventing harmful events for high-profile and high-impact players.

As the auto industry transitions to a cyclical upturn instead of downturn, the need for government intervention is likely to decrease in the near term. However, the pattern of intervention and the increase in industry barriers to exit will create an interesting precedent when the next inevitable cyclical downturn occurs.

The automotive industry has taken a new shape, nonetheless. The US government is now the majority shareholder of both GM and GMAC, and the QIA has a seat on Porsche’s board. It remains unclear how constrained companies will be in their autonomy over strategic decision making given this global increase in government involvement in the industry. The benefits of further government intervention — across the globe — must be weighed against the future costs to the long-term health of an industry still plagued by a fragmentation of scale and expertise.

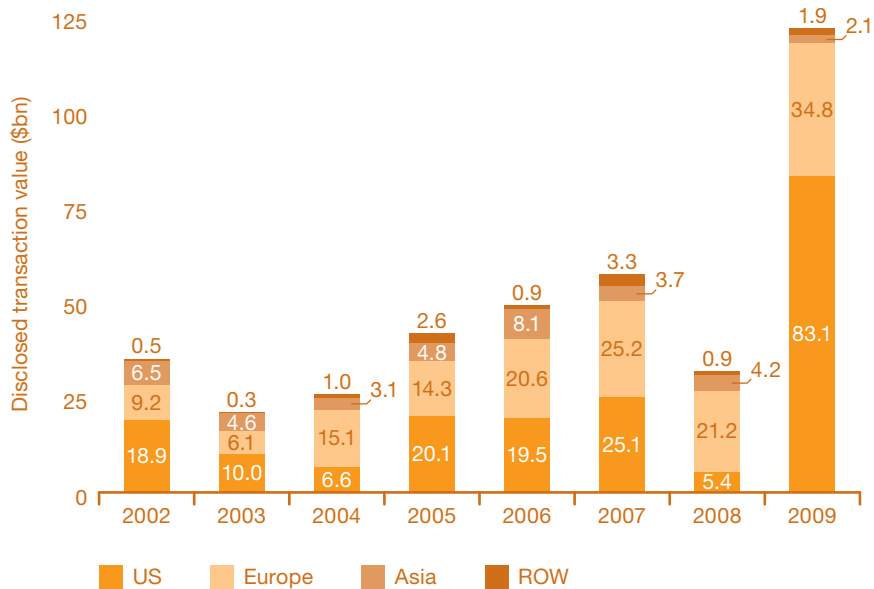
# Transaction activity by sector

**Retail, aftermarket, rental/leasing and wholesale automotive M&A activity, 2005–2009**



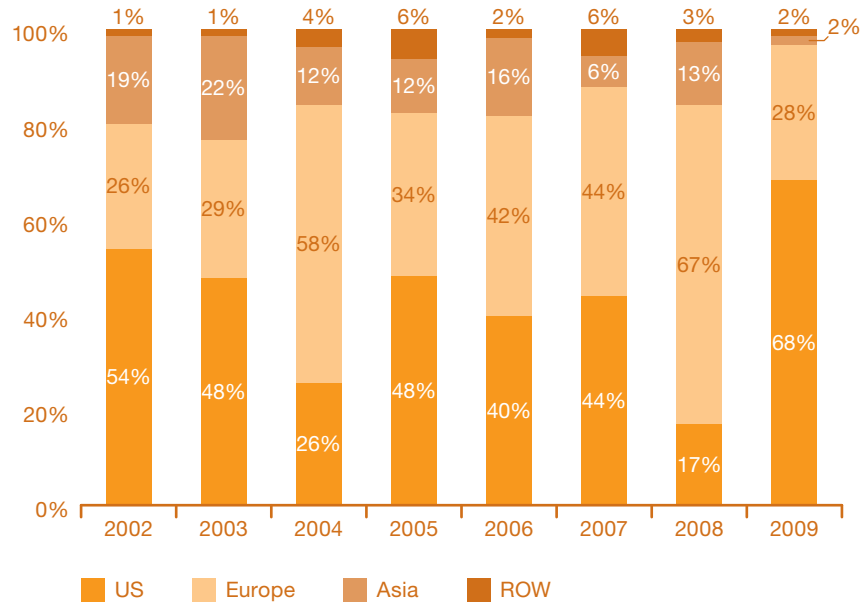
Source: Thomson Reuters and other publicly available sources

**Automotive transaction value by target region, 2002–2009**



Source: Thomson Reuters and other publicly available sources

**Automotive transaction value share by target region, 2002–2009**



Source: Thomson Reuters and other publicly available sources

## Top 10 deals by sector

Rank	Value (\$m)	Target	Target nation	Buyer	Buyer type	Buyer nation	% Acquired	"Date Effective"
Component suppliers								
1	10,982	Delphi Corp	United States	Elliott Management and Silver Point Capital	Financial	United States	100	10/6/09
2	5,819	Continental AG	Germany	Schaeffler KG	Trade	Germany	20	1/8/09
3	1,100	Delphi Corp-Steering Business	United States	General Motors Corp	Trade	United States	100	10/6/09
4	302	Smith Investment Co	United States	AO Smith Corp	Trade	United States	100	4/22/09
5	180	ArvinMeritor Inc—Wheels	United States	Iochpe-Maxion SA	Trade	Brazil	100	9/21/09
6	135	Key Plastics LLC	United States	Wayzata Investment Partners LLC	Financial	US	100	2/13/09
7	100	Haldex AB-Garphyttan Wire Division	Sweden	Suzuki Metal Industry Co Ltd	Trade	Asia	100	6/1/09
8	100	Delphi Corp-Global Suspension	United States	BeijingWest Industries Co	Financial	China	100	11/2/09
9	99	TC Debica	Poland	Goodyear Luxembourg Tires SA	Trade	Luxembourg	34	11/16/09
10	96	Mecachrome International Inc	Canada	Ace Management, Fonds de Solidarite des Travailleurs du Quebec and Fonds Strategique d'Investissement SA	Financial	France	100	12/18/09
Other								
1	7,500	GMAC LLC	United States	US Dept of the Treasury	Financial	United States	0	6/3/09
2	3,800	GMAC LLC	United States	US Dept of the Treasury	Financial	United States	21	12/30/09
3	727	HUGHES Telematics Inc	United States	Polaris Acquisition Corp	Financial	United States	100	4/1/09
4	392	Belron SA	Luxembourg	D'leteren SA NV	Trade	Belgium	16	9/3/09
5	264	Wavecom SA	France	Sierra Wireless France SAS	Financial	France	100	4/29/09
6	261	Kumho Rent-A-Car Co Ltd	South Korea	MBK Partners LP and KT Corp	Financial	South Korea	100	12/30/09
7	138	Autodistribution SA	France	TowerBrook Capital Partners LP	Financial	United States	100	3/2/09
8	95	Controlar SA	Brazil	Companhia de Concessoes Rodoviaras and Brisa Participacoes e Empreendimentos	Financial	Portugal	55	8/13/09
9	85	AUTOonline GmbH Informationssysteme	Germany	Solera Holdings Inc	Trade	United States	85	10/1/09
10	85	Toyotasa Toyota Sabanci	Turkey	ALJ Lubnatsi Marketing & Sales	Trade	Saudi Arabia	65	10/7/09

Source: Thomson Reuters and other publicly available sources

What this means for your business

M&A will continue to drive the fundamental changes necessary for the near-term restructuring and long-term sustainability of the automotive value chain.

M&A will continue to be one of the primary means through which players in the global automotive industry effect the fundamental changes that are necessary for their near-term survival and long-term success. In the short term, the deal market will remain a setting for companies' restructurings, divestitures, and capital infusions. However, long-term success will depend on organizations' ability to once again create and execute strategies for sustainable growth and value creation, and 2010 will begin to see the transition of the deal market to these drivers. The deal market will play a critical role as market participants pursue transactions with a focus on synergies — including enhancing productivity, providing cost savings, and adding revenue to their businesses.

However, the significance of M&A to the automotive industry is perhaps the only certainty for the coming years. The health of the automotive deal market depends on macroeconomic and industry factors. Growth in deal volume and value might continue to be constrained by investors' appetites for systematic and industry-wide risk and the accessibility of affordable financing. Despite this uncertainty, we believe the following 11 trends will occur in 2010 and beyond:

1. The deal market should return to a healthier but not yet normalized state as long as debt and equity markets continue to improve. As a result, strategic M&A should return because more companies would be better positioned to finance discretionary deals. Participants will likely seek to improve their concentration of scale and expertise as they shift their focus from survival to long-term profitable growth.
2. For the same reasons, as well as an improving market for initial public offerings, private equity should make a slow comeback. The IPO market has been reestablished as a viable exit vehicle across industries, enabling private equity firms and their investors to realize gains from holdings that have so far been illiquid. Greater debt financing options and "dry powder" in the sector also might encourage private equity firms to pursue more deals. However, poor returns in 2008 and 2009 have left institutional investors wary of committing fresh capital, which could challenge the industry's traditional fee structure and ability to act.
3. Divestitures will likely continue through 2010 as companies shed unwanted assets to focus on their core competencies while raising cash to decrease leverage, invest in research and development, and execute growth strategies. Distressed situations might catalyze many of these divestitures if depressed vehicle sales follow the end of major stimulus programs such as those in Europe. However, the sale of these assets depends on the appetite and availability of buyers.
4. Although 2009 ushered in a period of OEM consolidation, we expect to see more formalized strategic alliances through share acquisitions as VMs seek access to new markets and technologies. For example, Volkswagen AG announced in late 2009 that it intends to acquire a 20 percent equity stake in Suzuki Motor Corporation to bolster its competitive position in emerging Asia growth markets. Nonetheless, consolidation might overshadow acquisitive growth strategies in the near future as excess capacity continues to plague the industry.
5. Emerging from this crisis were fewer automakers, with an increased focus on global optimized platforms and production bases. This trend will now likely impact the supply chain, where M&A would be instrumental as suppliers capitalize on new demand from VM alliances.

6. The advent of new technologies, regulations, and consumer requirements will drive automotive M&A this year and likely for the next decade. The automobile is progressing from a mechanical device with some electronic enablers to an electronic device with some mechanical enablers. Other factors are new global CO<sub>2</sub>, fuel economy, and safety regulations; the growth of hybrid and electric cars; and an increase in the role of infotainment and communications in cars. The need for companies to add capabilities to capture growth from these trends will be a key piece of the strategic logic behind many deals.
7. The retail, aftermarket, rental/leasing, and wholesale sectors will also need to adapt to changes in the VM sector. Dealerships, for example, have been and may continue to consolidate as VMs seek to streamline sales of their core brands. Meanwhile, the success of automotive financing companies depends on the continued recovery of the credit markets.
8. We are witnessing a large shift of wealth and economic power from developed to developing countries, which will likely drive cross-border activity from West to East in the coming years. Primarily by acquiring technologies and intellectual property, developing automakers will better serve domestic demand and meet more stringent environmental and safety regulations. Zhejiang Geely, for example, hopes to do so by acquiring Ford's Volvo brand. Nonetheless, deal flow into emerging markets will likely continue as VMs in developed countries pursue growth opportunities in emerging markets. Cross-BRIC deal flow could be another visible trend. In December, GM and Shanghai Automotive Industry Corporation (SAIC) announced a joint venture to sell low-cost vehicles in India, which could pave the road for collaboration between SAIC and Indian automotive companies.
9. Within China's borders, we expect consolidation among VMs and their suppliers. The Chinese automotive industry is currently a regionally based and highly fragmented industry of more than 7,800 suppliers and 80 OEMs, partially because provincial governments have nurtured smaller players to support regional growth. The central government is now supporting consolidation, hoping for the emergence of a few large automakers that can compete on a global scale.
10. Deal structure will depend on the relative performance of the equity and debt markets. As credit markets improve, organizations may take on leverage to finance their acquisitions. As equity markets continue to improve, companies will have an incentive to take advantage of their high equity valuations by utilizing equity exchanges. However, given the ongoing lack of stability across the industry, it is unlikely that equity exchanges will be the dominant financing method in 2010. Thus, with improved credit markets, we expect acquirers to finance their deals through a larger proportion of debt than we have seen during the recession, but still not to the extent that was common in the prerecession period.
11. Further direct and indirect government investments are possible given the ongoing uncertainty in the global automotive industry, though the effects of this past year's investments will have lingering effects on the industry. Subsidies and tax incentives are likely to continue until global demand for automobiles stabilizes. However, the direct equity investments made in 2009 might increase barriers to exit and create other conflicts between public and private interests.

The outlook for the automotive deal market depends on a variety of factors. Clearly, the state of the macroeconomy will be a large driver in the success of the industry's ongoing restructuring efforts. The industry still needs to consolidate across many parts of the automotive value chain to improve insufficient returns, achieve scale to afford the R&D required by the changing and innovating industry, and eliminate the excess capacity and irrational competition present in many subsectors. Players across the automotive industry are waiting to understand the future strategic trajectory of several businesses and brands emerging out of bankruptcy or major restructurings. In turn, companies are increasing their focus on growth and traditional drivers of M&A, such as market entry, improved customer access, and increased concentration of scale and expertise in a given sector.

In the long term, the industry's success will depend on the ability of its players to pursue sustainable, profitable growth — and M&A will form a key part of that effort.

Given the wide range of challenges and opportunities facing the automotive industry, M&A will be a critical tool for players throughout the automotive value chain, whether they seek short-term survival or long-term success. This report serves as an introduction to our comprehensive blend of cumulative knowledge and direct experience in the automotive industry. Our services span the entire deal continuum, from strategy formulation, to target identification and screening, to deal execution to capturing synergies and exit. We have advised our clients in the automotive and financial communities on countless potential transactions and their underlying strategies, and we look forward to helping our clients navigate the roads ahead.

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