The Economic Significance of the Supply Base: The Largest US Manufacturing Sector

- 686,000 direct employees
  - 898,500 intermediate jobs
  - 1,701,800 expenditure induced
- 3.29 million jobs (4.8 multiplier effect)

Considering only direct employees, the supplier sector is the largest manufacturing industry in Michigan, Ohio, and Indiana as well as Kentucky, Missouri, Oklahoma, South Carolina and Tennessee.

- In total, the light duty, heavy duty and aftermarket parts suppliers account for approximately $390 billion of shipments

Source: MEMA Moving America. Part by Part. (www.mema.org)
The Supplier Sector – Top 15 States

<table>
<thead>
<tr>
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<tbody>
<tr>
<td>Michigan</td>
<td>111,224</td>
<td>145,818</td>
<td>(34,594)</td>
</tr>
<tr>
<td>Ohio</td>
<td>80,600</td>
<td>97,323</td>
<td>(16,723)</td>
</tr>
<tr>
<td>Indiana</td>
<td>66,721</td>
<td>86,934</td>
<td>(20,213)</td>
</tr>
<tr>
<td>Tennessee</td>
<td>44,172</td>
<td>45,749</td>
<td>(1,577)</td>
</tr>
<tr>
<td>Illinois</td>
<td>36,033</td>
<td>40,063</td>
<td>(4,030)</td>
</tr>
<tr>
<td>Kentucky</td>
<td>34,656</td>
<td>35,102</td>
<td>(446)</td>
</tr>
<tr>
<td>North Carolina</td>
<td>26,078</td>
<td>27,589</td>
<td>(1,511)</td>
</tr>
<tr>
<td>California</td>
<td>24,677</td>
<td>28,596</td>
<td>(3,919)</td>
</tr>
<tr>
<td>Texas</td>
<td>24,664</td>
<td>20,175</td>
<td>4,489</td>
</tr>
<tr>
<td>Alabama</td>
<td>21,654</td>
<td>15,965</td>
<td>5,689</td>
</tr>
<tr>
<td>New York</td>
<td>20,367</td>
<td>31,017</td>
<td>(10,650)</td>
</tr>
<tr>
<td>South Carolina</td>
<td>19,492</td>
<td>20,943</td>
<td>(1,451)</td>
</tr>
<tr>
<td>Missouri</td>
<td>17,828</td>
<td>18,888</td>
<td>(1,060)</td>
</tr>
<tr>
<td>Wisconsin</td>
<td>17,662</td>
<td>21,502</td>
<td>(3,840)</td>
</tr>
<tr>
<td>Georgia</td>
<td>16,165</td>
<td>22,701</td>
<td>(6,536)</td>
</tr>
</tbody>
</table>

Source: MEMA Moving America. Part by Part. (www.mema.org)
The Great Amount of Uncertainty is Driving Pessimism Through the Supply Chain

Compared to Two Months Ago, How has Your 12 Month Outlook Changed

Supplier Sentiment Index

Positive

Negative

Source: OESA Supplier Barometer
1Q 2009 NA production ended 52% down year-over-year
There is greater probability than ever we will hit the lowest part of any forecasting range
D3 receivables for March are estimated down 70% from 4Q 2008 run rate; Chrysler at 82,000 units for 2Q 2009
The OESA February survey revealed 31% of respondents were in severe financial distress or risk of bankruptcy before the end of 2Q 2009. A full 62% put themselves in that camp by the end of 2009.
Tracking D3 Monthly Supplier Receivables

Billions of US Dollars

Source: OESA based off of May 2009 CSM Worldwide production numbers
Supplier Revenue Will Be Down Significantly . . Can We Make It To the Other Side?

Budgeted Revenue Change

Note: Revenue Change Code
1 = > -30%; 2 = -20 to -29%; 3 = -16 to -19%; 4 = -10 to -15%; 5 = -6 to -9%
6 = -1 to -5%; 7 = No Change; 8 = +1 to +5%; 9 = +6 to +10%; 10 = > +10%

Source: OESA March 2009 Supplier Barometer. Responses = 123
Capacity Utilization Will Continue Falling and So Will Operating Income

- Parts makers were running at 51.8% utilization in March
- Company’s are readjusting BE to 60 to 70% utilization rates
- AlixPartners’ analysis: ROCE has a 68 percent correlation to capacity utilization
- These losses will be driven by:
  - Volume declines
  - Mix change from truck to car

Source: U.S. Federal Reserve Board of Governors
Current Supplier Financial Metrics

- 23% are currently in loan covenant violations;
- An additional 24% anticipate being in covenant violation by the end of 2009;
- 54% have been approached for shorter payment terms by their sub-tier suppliers; and
- 12% do not have access to working capital to support a 10% or greater increase in North American production builds.

The financial situation is even worse for small suppliers with revenue under $250 million:
- 34% are currently in violation of bank loan covenants;
- An additional 33% anticipate being in covenant violation by the end of 2009;
- 53% have been approached for shorter payment terms by their sub-tier suppliers; and
- 18% do not have access to working capital to support a 10% or greater increase in North American production builds.

Source: OESA Supplier Financial Health Survey, May, 2009
Greatest Risk to the Whole Economy:
GM and Chrysler Wind Down Scenarios

- **Chrysler**: A two year process includes a C11 and an orderly wind down – requires $24 billion in DIP and results in 300,000 jobs lost at Chrysler and its suppliers

- **GM**: presented three scenarios:
  - **“Out of Court/Pre-Packaged”** – $33 billion Required Financing – Tendering bondholders would be required to vote affirmatively to accept a Chapter 11 Plan of Reorganization, agreement in advance on VEBA, a government commitment, existing shareholders entirely diluted – in and out within 65 days. Predicted only a quick hit to showroom traffic and subsequent revenue hit in near term.
    - **Suppliers would require $8 billion in additional governmental funding**
  - **“Pre-negotiated Cram-Down”** – $86 billion Required Financing – larger debt to equity conversion (up to 100%), reduction in obligations from others (e.g., contract rejection damages), up to 100% VEBA equity conversion – in and out up to 6 months
    - **Suppliers would require $9-10 billion in additional governmental funding**
  - **“Traditional C11”** – $103 billion Required Financing – 18 to 24 months using all tools available to debtors to restructure through the court process
    - **Suppliers would require $13-17 billion in additional governmental funding**

Sources: February 17, 2009 respective submissions to the US Treasury
The Transformation Must Protect the Supply Base or the Interdependency of the Supply Base Can Cause a Top-Down or a Bottom-Up Implosion

The fabric of the supply base connects all OEMs.

- Any OEM failure will propagate itself through the supply chain
- Any first tier supplier failure creates risk in at least two OEMs
  
  ✓ All OEMs becoming very aggressive on their supplier monitoring

Percentages represent the number of common suppliers in the other OEMs’ supply base

Source: CSM Worldwide
How an “Uncontrolled” OEM Bankruptcy Would Propagate through the Supply Chain

1 month

- OEM C11 Slows Payments to All but Critical Suppliers
- 20% of Suppliers in Loan Covenant Violation. OEM C11 Triggers 1/2 to Fail
- Given Auto Economic Multiplier, OEM and Supplier C11s Reduce Economic Activity and Vehicle Sales Further

2 months

- Further Auto Financial Crisis Pushes Additional 10% (1/2 of the Current Weak D3 Suppliers, less those that failed in 30 days)
- Supplier Disruptions Spill Over to Disrupt Foreign OEM Production Pushing Crisis Thru Industry
- Vehicle Sales and Production Declines Continue to Reinforce U.S. Economic Downturn

3 months

- Supplier Failures Stabilize with 20 to 25% Failures Throughout the Chain
- OEM Supplier Re-sourcing Begins to Stabilize Supply Chains and Re-Balance Supply/Demand
- Surviving OEMs Stabilize; Supplier Liquidations and Restructurings Continue

- The increased depth of the economic trough depends on how “orderly” the bankruptcy is
- Add 6 to 9 months onto when the trough is expected
- Add 12 to 18 months to when the markets return to 2006-2007 levels
The Industry, Banks and Government Must Work Together For the Industry To Move Through Recapitalization Without Major Disruption

Production Capacity
- Redefine Labor Relationship
- Consolidate Dealer Network
- Rationalize Brand Portfolios

Employment

New Vehicles & Technology
- Pursue Growth Markets
- Focus on Core Brands in NA
- Leverage Key Relationships (Labor, Dealers, Suppliers)

Resize/Rationalize

Industry Reinvest/Recapitalize


General Motors and Chrysler Recapitalization

Source: Casesa Shapiro Group with additional interpretation by OESA
The Best Picture of Things Yet to Come . . .

Chart 1: An illustrative example of how the Big Bang may play out in North America

Source: John Murphy, B of A/Merrill Lynch, Big Bang Theory, November 3, 2008
Drivers of a New Business Model

- Fractionalized OEM sales and production shares
  - Increased complexity for suppliers
- Government integration in auto business model
  - Increased decision making complexity
- Capital structure complexity
  - Non-traditional owners from the US and Canadian governments to the UAW VEBA Trustees
  - For NA suppliers, a majority of major supplier competitors will be foreign or privately owned
- Environmental, energy, ... Labor, tax, trade public policy focus
  - How stable will the playing field be?
## The Global Top Dozen

<table>
<thead>
<tr>
<th>Supplier</th>
<th>2008 Global Revenue - Billions</th>
<th>2007 to 2008 Change in Position</th>
</tr>
</thead>
<tbody>
<tr>
<td>Robert Bosch</td>
<td>$ 33.9</td>
<td>-</td>
</tr>
<tr>
<td>Denso</td>
<td>$ 27.8</td>
<td>-</td>
</tr>
<tr>
<td>Continental</td>
<td>$ 25.0</td>
<td>+ 1</td>
</tr>
<tr>
<td>Magna</td>
<td>$ 23.3</td>
<td>+ 1</td>
</tr>
<tr>
<td>Aisin Seiki</td>
<td>$ 20.8</td>
<td>+ 1</td>
</tr>
<tr>
<td>Johnson Controls</td>
<td>$ 19.1</td>
<td>+ 1</td>
</tr>
<tr>
<td>Delphi</td>
<td>$ 18.1</td>
<td>-2</td>
</tr>
<tr>
<td>Faurecia</td>
<td>$ 17.7</td>
<td>-</td>
</tr>
<tr>
<td>ZF</td>
<td>$ 16.9</td>
<td>+ 1</td>
</tr>
<tr>
<td>TRW</td>
<td>$ 15.0</td>
<td>+ 1</td>
</tr>
<tr>
<td>Lear</td>
<td>$ 13.6</td>
<td>- 2</td>
</tr>
<tr>
<td>Toyota Boshuoku</td>
<td>$ 12.3</td>
<td>+ 6</td>
</tr>
</tbody>
</table>

Source: Automotive News, June 1, 2009
A Vast Share of Suppliers Have Restructured To Be At Break Even Even at Lower Volumes

Source: OESA Supplier Financial Health Survey, May 2009; n = 71
The Auto Industry Needs a Healthy Working Relationship with Bankers . . .

But When We Ask About Lending Relationships . . .

- **Most Significant Relationship**
  - **Commercial Bank** (64 responses, median response = 5)
    - Very Engaged (1 or 2) = 6 responses
    - Aggressively Exiting (6 or 7) = 24 responses
  - **Parent Company** (5 responses, median response = 5)
    - Very Engaged (1 or 2) = 2 responses
    - Aggressively Exiting (6 or 7) = 0 responses
  - **Family Ownership** (4 responses, median response = 5)
    - Very Engaged (1 or 2) = 1 responses
    - Aggressively Exiting (6 or 7) = 0 responses

Source: OESA Supplier Barometer, March 2009. Responses = 121
U.S. Treasury Supplier Support Program

- $5 billion program to arrange for guarantees or buy-back of GM and Chrysler Receivables

- **Advantages**
  - Provides protection should a GM or Chrysler bankruptcy occur
  - Provided some confidence for restoring lending into automotive suppliers
  - Showed awareness of industry economic significance

- **Limitations**
  - Targets only GM and Chrysler U.S.-based suppliers
  - Limited to selected suppliers
  - Does not help lower tier suppliers
However, Additional Supplier Assistance is Needed to Minimize Bottom-Up Implosion Risk

- **Short-term Operating Cash Flow**
  - 23 percent of members report they are out of compliance with loan covenants
  - Receivables limited; what receivables there are, lending from traditional lenders against these are significantly constricted, inventories worked down to a bare minimum
  - Options: expand loan guarantees, additional cash into deal

- **Mid-term Expansion Credit**
  - Commercial banks severely limiting lending for tooling and capital investment programs
  - Options: governmental backstopping of loans, additional cash into deal

- **Long-term Restructuring Capital**
  - DIP financing unavailable, hedge fund and private equity capital on the sidelines
  - Options: government seed money to encourage private capital back into the industry
## Supplier Financial Assistance Pathway

<table>
<thead>
<tr>
<th></th>
<th>Short-Term Cash Flow</th>
<th>Mid-Term Expansion</th>
<th>Long-Term Restructuring</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Existing Programs</strong></td>
<td></td>
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<tr>
<td>US Treasury</td>
<td>Supplier Support Program</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SBA</td>
<td>Loan Guarantees up to $2 million (7a Program)</td>
<td>Assistance for $1.5 to $4 million loans (504 Program)</td>
<td></td>
</tr>
<tr>
<td>DOE</td>
<td></td>
<td>$25 billion advanced technology support (Section 136 loans)</td>
<td></td>
</tr>
<tr>
<td>US Department of Agriculture</td>
<td></td>
<td>Business and Industry Guaranteed Loans up to $10 million</td>
<td></td>
</tr>
<tr>
<td><strong>Potential Programs</strong></td>
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<tr>
<td>Federal Government</td>
<td></td>
<td>Direct Supplier Loan Guarantees</td>
<td></td>
</tr>
<tr>
<td>Federal and State Governments</td>
<td>Interest Rate Deferrals</td>
<td>Cash for Collateral Valuation Support</td>
<td></td>
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<tr>
<td>Federal and State Governments</td>
<td></td>
<td></td>
<td>Public/Private Mezzanine Fund</td>
</tr>
<tr>
<td>Federal Reserve of NY</td>
<td></td>
<td>TALF – Asset Based Lending Facility</td>
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</tr>
</tbody>
</table>
Supply Base Assistance Will Not Help Unless Sales Rebound . . . That is Unlikely With Negative GDP Growth without Some Form of Vehicle Demand Stimulus Like Other Developed Countries Have Adopted

<table>
<thead>
<tr>
<th>Country</th>
<th>Program Start</th>
<th>Description</th>
<th>Result</th>
</tr>
</thead>
<tbody>
<tr>
<td>Germany</td>
<td>Jan. 2009</td>
<td>Apx. $3,150 bonus for scrapping a 9+ year old vehicle</td>
<td>Year-over-year increases immediate (Feb – highest rate in 10 years, +22% Y-O-Y)</td>
</tr>
<tr>
<td>France</td>
<td>Nov. 2008</td>
<td>Apx. $1,250 for scrapping a 10+ year old vehicle</td>
<td>30-40% of sales associated with the program</td>
</tr>
<tr>
<td>Italy</td>
<td>Feb. 2009</td>
<td>Apx. $1,900 to $6,300 for scrapping a 10+ old vehicle</td>
<td>Program generated “significant registrations.”</td>
</tr>
</tbody>
</table>

Source: John Murphy, Merrill Lynch, “Scrappage Program Might Not Save The SAAR, April 6, 2009.
Through All the Turmoil – Keep Your Eye On The Drivers of Value

Automotive Supplier Value Drivers

- OEM Sales/Production Volumes
- Customer Health
- Financial Strength
- Labor Costs
- Capital Markets
- Material Price Exposure
- Vendor Health
- Geopolitical Issues
- Customer Concentration
- Product/Process Technology
- Value-Added Content
- Management Strength
- LCC Strategy
- Geographic Reach
- ERP Systems/Infrastructure

Impact on Value

- Higher Impact, Higher Control
- Lower Impact, Higher Control
- Lower Impact, Lower Control
- Higher Impact, Lower Control

Degree of Control

- Lower
- Higher

Source: SRR Presentation to OESA Chicago Regional Meeting 2009
The supply base is the fabric interconnecting the vehicle manufacturers and the complex value chain from material suppliers to system integrators.

The supply base faces unprecedented market and credit market headwinds.

Chrysler and GM restructurings will likely create two “new” competitors in the short term and force on-going bankruptcies as “bad company” assets are disposed.

Government, industry and the financial community must work together to support the supply base and prevent a top-down or bottom-up implosion.

The US Treasury Supplier Support Program provides receivables protection from Chrysler and GM bankruptcies, however . . .

There is a critical need for immediate working capital, near-term program investment and restructuring capital – overarching everything is vehicle demand stimulus.

OESA and MEMA are the suppliers’ voice in Washington on these issues and other public policy issues.
In This Time of Distress . . . OESA Provides a Wide Range of Tactical and Strategic Value to Survive and Thrive

- **12 peer group councils**: CEO, CFO, Chief Purchasing Officers, China Strategy, Communications, EH&S, HR, Legal Issues, Sales & Marketing, Product Development, Small and Medium Suppliers, Warranty, Govt. Affairs

- **OEM Town Hall Meetings**: GM, Ford, Chrysler, Toyota, VW

- **Member Surveys**: Benchmarking, Organizational Issues, Material Markets, Commercial Issues, Financial Practices

- **Member Industry Studies**: Terms & Conditions, Intellectual Property, Supply Chain, Customer Diversification, Warranty Management, Global Manufacturing Footprint…

- **Automotive Industry Events & Seminars**: addressing the challenges and issues suppliers face, developing strategies to compete

- **International Collaboration**: CLEPA-Europe, JAPIA-JAPAN, ACMA-India, others

- **The Network**: OESA provides a forum, a source of industry information, and a vast network of suppliers and affiliates
Thank You

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