

## Complete situation analysis (referring to page 35ff of START DIFFERENTLY)

### 1. External factors

#### External Factor: Economic/business environment

Exemplary questions to be asked (linked to the problem statement & scope):

- Which economic indicators are relevant for the development of the car market? [Purchasing power, Population growth]. How do you expect them to develop within the timeframe defined in the scope?
- Are there any population/workforce developments, which have an influence on the car industry? [Engineer graduates, labor cost]. If yes, how do you expect them to develop within the timeframe defined in the scope?
- Do you expect any other economic/business developments, which could have an influence on the overall profitability of the automotive industry in China? [emission standards, infrastructure measures].
- Which of those are tailwind? Which are headwind?

Facts	Conclusions
<p>Workforce:</p> <ul style="list-style-type: none"> <li>• Large pool of engineers (800.000 engineers graduate per year) and business graduates</li> <li>• During the last 5 years our labor cost has increased by 8,5% p.a.</li> <li>• The current economic outlook points to a similar or even higher trend in the coming years.</li> </ul>	<p>Labor cost is expected to get more expensive by 10% p.a.</p> <p>→ Key take away, Headwind</p>
<p>Emission standards:</p> <ul style="list-style-type: none"> <li>• China has pursued aggressive climate</li> </ul>	<p>Opportunity to prove to be a fast-reacting and innovative partner for our customers when it comes to implementing the new</p>

<p>and energy policies during the last years. Emission standards are expected to tighten further during the years to come.</p> <ul style="list-style-type: none"> <li>China is currently in the process of implementing its fourth-stage emissions standards, which would cap the allowed sulfur content at 50 parts per million next year, down from current levels of 350 parts per million.</li> </ul>	<p>emission standards policy in China.</p> <p>→ Comment: not relevant, not answering the problem statement (scope is only 3 years)</p>
<p>Economic indicators/purchasing power:</p> <ul style="list-style-type: none"> <li>Annual GDP growth rate: ~10%</li> <li>Annual inflation rate: ~ 3%</li> <li>Purchasing power: \$13.39 trillion</li> </ul> <p>Population:</p> <ul style="list-style-type: none"> <li>Population: 1,4 bn</li> <li>Currently 300 million car drivers in China</li> <li>Share of urban population expected to rise from currently 50% to 60% by 2020.</li> <li>Number of high income urban households expected to rise from currently 20% to 60% by 2020.</li> </ul> <p>Infrastructure:</p> <ul style="list-style-type: none"> <li>High investments in the quality of roads during the last years. National highway initiative: 33.000 km of new highways to be built started in 2011.</li> </ul>	<p>Those facts support our market environment key take-away.</p>
<p><b>Key take-aways:</b></p> <p><b>Labor cost is expected to get more expensive by 10% p.a.</b></p>	

**External Factor: Market environment**

Exemplary questions to be asked (linked to the problem statement & scope):

- What information do we have about market size and expected growth?
- Are any segments growing faster than others?
- Are any segments more profitable than others? Why?
- Who are our competitors in China? Are they more or less profitable than us? Why? Any relevant trends?
- Who are the customers? What are their market shares and trends? Are they profitable? Why? Why do they buy/not buy from us?
- Who are our consumers in China? Is there any consumer trend that has an influence on our profitability?
- Who are the suppliers? Are there any relevant facts, which have an influence on our profitability?

Facts	Conclusions
<p>Market size/growth:</p> <ul style="list-style-type: none"> <li>• 40 million cars produced p.a. in China</li> <li>• Growth rates:               <ul style="list-style-type: none"> <li>○ Annual growth rate automotive industry China: expected ~8% p.a. until 2020</li> <li>○ Annual growth rate SUVs China: expected ~ 13% p.a. until 2020, exceeding the growth rate of all other segments</li> </ul> </li> </ul>	<p>The market offers double digit growth rates in SUV segment.</p> <p>→ Key take-away, Tailwind</p>

<ul style="list-style-type: none"> <li>○ Small cars rate of total market expected to shrink by 2% p.a. until 2020</li> </ul>	
<p>Competition:</p> <ul style="list-style-type: none"> <li>• There are &gt; 5,000 manufacturers.</li> <li>• Majority of manufacturers are small to medium sized.</li> <li>• 40% are private enterprises and 20% are JVs.</li> <li>• Profitability EBIT margin (estimates):             <ul style="list-style-type: none"> <li>○ Private Chinese: 10%</li> <li>○ JVs: 2%</li> <li>○ Foreign owned: 5% (our profitability China: 4%)</li> </ul> </li> <li>• Foreign companies dominate many core technologies.</li> </ul>	<p>EBIT margin of our privately Chinese owned competitors is twice as high as ours.</p> <p>→ Comment: not relevant. Doesn't help us to solve the problem statement.</p>
<p>Customers: see internal factors sales</p>	
<p>Consumers:</p> <ul style="list-style-type: none"> <li>• China is number one car buying nation in the world, growing tendency.</li> <li>• Current trend: Chinese people with good income buy bigger cars, e.g. SUVs (lifestyle).</li> <li>• Consumer behavior between regions and cities/countryside varies widely.</li> </ul>	<p>Challenge to meet consumer needs in a very diverse market environment.</p> <p>→ not relevant. Doesn't help us to solve the problem statement.</p>
<p>Suppliers:</p> <ul style="list-style-type: none"> <li>• Suppliers for majority of production</li> </ul>	<p>The market offers more sourcing options than we are currently using.</p>

<p>materials available in China.</p> <ul style="list-style-type: none"> <li>Foreign owned companies tend to import already approved crucial parts/materials from overseas, as the approval process of new suppliers in automotive industry follows very strict rules and takes time.</li> </ul>	<p>→ Key take-away, Tailwind</p>
<p><b>Key take-aways:</b></p> <p>The market offers double digit growth rates in SUV segment.</p> <p>The market offers more sourcing options than we are currently using.</p>	

## 2. Internal factors

### Internal Factor: Sales

Exemplary questions to be asked (linked to the problem statement & scope):

- Why are we not making profit with certain segments/customers/etc. (refer to the questions asked in the factor “profitability”.)
- What drives buying decisions at our customers?
- Are we offering services which add to our cost structure, but have little benefit for them?
- How is the value chain of our industry? Who is making money where why?
- What would we have to change in our internal organization to increase profitability of certain customers? Why? (please note: people will propose actions, these will allow you to drill down to the right facts).

Facts	Conclusions
<ul style="list-style-type: none"> <li>• We make 75% of our turnover with our Top 3 customers.</li> <li>• We know from benchmarking that our profitability with B&amp;C customers is above the market average.</li> <li>• We have developed a pricing tool to calculate prices for B&amp;C customers some years ago and successfully trained our sales team to apply it. Since we introduced this new tool, our profitability with B&amp;C customers has improved significantly.</li> </ul>	<p>We are strongly dependent on a few big customers, which is a low-margin business.</p> <p>→ Comment: not relevant. Doesn't help us to solve the problem statement.</p> <p>The pricing tool in place for B&amp;C customers works well.</p> <p>→ Key take-away, tailwind</p>
<p>Customers:</p> <ul style="list-style-type: none"> <li>• More than 100 automakers in China licensed to produce passenger cars.</li> </ul>	<p>Potential to grow via new customers limited due to very consolidated market.</p> <p>→ Comment: not relevant. Doesn't help us</p>

<ul style="list-style-type: none"> <li>• Top 10 hold 84% of the market share.</li> <li>• Localization of auto parts &gt; 80%</li> </ul>	<p>to solve the problem statement.</p> <p>Plant closure in China/shift of volumes to European plants would lead to loss of our turnover in China, as auto-parts are mostly sourced locally.</p> <p>→ not relevant. Doesn't help us to solve the problem statement.</p>
<ul style="list-style-type: none"> <li>• Estimated 90% of our attention in the Sales team is dedicated to A customers (low profitability, see factor profitability on page xyz)</li> </ul>	<p>We spend too much time on low margin business (A customers) instead of high margin business (B/C customers)</p> <p>→ Key take-away, headwind</p>
<p><b>Key take-aways:</b></p> <p><b>The pricing tool in place for B&amp;C customers works well.</b></p> <p><b>We spend too much time on low margin business (A customers) instead of high margin business (B/C customers)</b></p>	

**Internal Factor: Purchasing**

Exemplary questions to be asked (linked to the problem statement & scope):

- Where do we buy? Why?
- How do we choose our suppliers? Why?
- How do we know that we buy the right quality? Why?
- Do we believe that our purchasing prices are above/below competition? Why?
- How do we achieve savings in purchasing?
- What would we have to change in our internal organization to reduce purchasing cost? Why? (please note: people will propose actions, these will allow you to drill down to the right facts).

Facts	Conclusions
<ul style="list-style-type: none"> <li>• We are buying 60% of our purchasing volume overseas, this is mostly done via global frame contracts negotiated by our European purchasing team. Only 40% is localized.</li> <li>• During the last 3 years only 5 new suppliers in China have been qualified successfully.</li> <li>• Our local purchasing team is quite young and inexperienced, but motivated.</li> <li>• Many suppliers we are using are long-term partners to our European subsidiaries, which have been qualified as suppliers with our Top customers long time ago.</li> <li>• We did a benchmarking exercise on the Chinese sourcing market two years.</li> </ul>	<p>Our imported parts are 15% more expensive than local Chinese benchmarks.</p> <p>→ Key take-away, headwind</p>



<p>Chinese suppliers are on average 15% less expensive than our current suppliers.</p>	
<ul style="list-style-type: none"> <li>• When we set up our Chinese factory, we transferred the specifications from Europe.</li> <li>• Most of the specs have never been adapted to the needs of the Chinese market.</li> </ul>	<p>Our specifications are over-specified for the Chinese market.</p> <p>→ Key take-away, headwind</p>
<p><b>Key take-aways:</b></p> <p><b>Our imported parts are 15% more expensive than local Chinese benchmarks.</b></p> <p><b>Our specifications are over-specified for the Chinese market.</b></p>	

**Internal Factor: Production**

Exemplary questions to be asked (linked to the problem statement & scope):

- How is our productivity in China in relation to our competition? Why?
- How is our productivity in China in relation to our productivity in our European plants? Why?
- What would we have to change in our internal organization to increase productivity? Why?

Facts	Conclusions
<ul style="list-style-type: none"> <li>• Our productivity in China is 25% lower than the average in our European subsidiaries.</li> <li>• We estimate our productivity to be 10% lower than our Chinese competitors.</li> <li>• Our equipment has been transferred from European sister companies.</li> <li>• The equipment is partly outdated and requires a high share of manual work.</li> <li>• At least 50% of the equipment we are using will not be sufficient to meet the requirements of the upcoming tighter emission standards.</li> </ul>	<p>Our labor productivity is 25% below internal benchmarks.</p> <p>→ Key take-away, headwind</p> <p>We are not equipped sufficiently to meet the new/tighter emission standards.</p> <p>→ Comment: not relevant. Doesn't help us to solve the problem statement.</p>
<p><b>Key take-aways:</b></p> <p><b>Our labor productivity is 25% below internal benchmarks.</b></p>	

**Internal Factor: Profitability**

Exemplary questions to be asked (linked to the problem statement & scope):

- Can we narrow down our profitability issue to certain customers/products/plants/etc.?
- Why are we more/less profitable in the different segments?
- What are the 3 most important drivers for our profitability?
- What do we know about our cost structure vs. competition?

Facts	Conclusions
<ul style="list-style-type: none"> <li>• Our margin with B &amp; C customers is 20% higher than our margin with A customers.</li> </ul>	<p>We have excellent profitability with our B&amp;C customers (account only for 25% of business).</p> <p>→Key take-away, tailwind</p>
<ul style="list-style-type: none"> <li>• 30% of our turnover is export business, which we are only doing because our A customers demand it. We do not make any profit on this business.</li> </ul>	<p>We do not charge full cost to our export customers (A customers)</p> <p>→Key take-away, headwind</p>

**Key take-aways:**

**We have excellent profitability with our B&C customers (account only for 25% of business).**

**We do not charge full cost to our export customers (A customers)**