



The Automotive Industry

STRATEGY AND BUSINESS IMPROVEMENT CONSULTING

Growth Opportunities For Minority-Owned Businesses

MED Week 2001

**The
Asaba
Group**

This Report Was Written And Produced For:

U.S. Department of Commerce

Minority Business Development Agency

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By:

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

Express Gratitude And Acknowledgement For Contributions To The Project:

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Project Charter

Develop A Report That Identifies The Opportunities For Minority-Owned Businesses In The Automotive Industry

It should place emphasis on the following:

- Industry trends and issues with the industry
- Market opportunities for growth
- Growth strategies and critical success factors
- Address current issues/challenges to Minority Business growth

The Asaba Group Retained To Assist In Identifying Growth Opportunities And Strategy

Project Approach



Executive Summary

Automotive Industry experiencing a slowdown in sales from record sales year in 2000

- Industry analysts forecast continued sales decline through 2003

Slowdown has created a difficult business environment for small to mid-sized businesses

- Minority suppliers not immune to these problems

Evolving Supply Chain roles present challenges to MBE's in Tier I positions

- Higher degree of cost surveillance, higher demands for investment in innovation and manufacturing
- Some MBE's will have to focus on Tier I and II Suppliers to achieve sustainable growth
- Tier I Suppliers beginning to push cost pressures down the Supply Chain

Operating risks associated with industry sales slowdown can be reduced through diversification

- By platform, customer group and targeting Tier I Suppliers

Growth opportunities identified in different areas of the Supply Chain

- Will require focused strategies to achieve sustainable value creation

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Key Highlights

Industry experiencing a slowdown in sales from a weakening economy

- Auto manufacturers sustaining 16 Million sales run rate by increasing marketing expenses
- Rising fuel prices and unemployment weakening demand for new vehicle purchases
- Industry analysts forecast continued sales decline through 2003

U.S. Automotive market seeing increased competition from foreign manufacturers

- Domestic Automotive manufacturers losing share to foreign manufacturers
 - Historical profit centers, Minivans, Pickups and SUVs, face eroding profits

Automotive manufacturers cutting production levels in response to slowing sales and reducing fixed costs

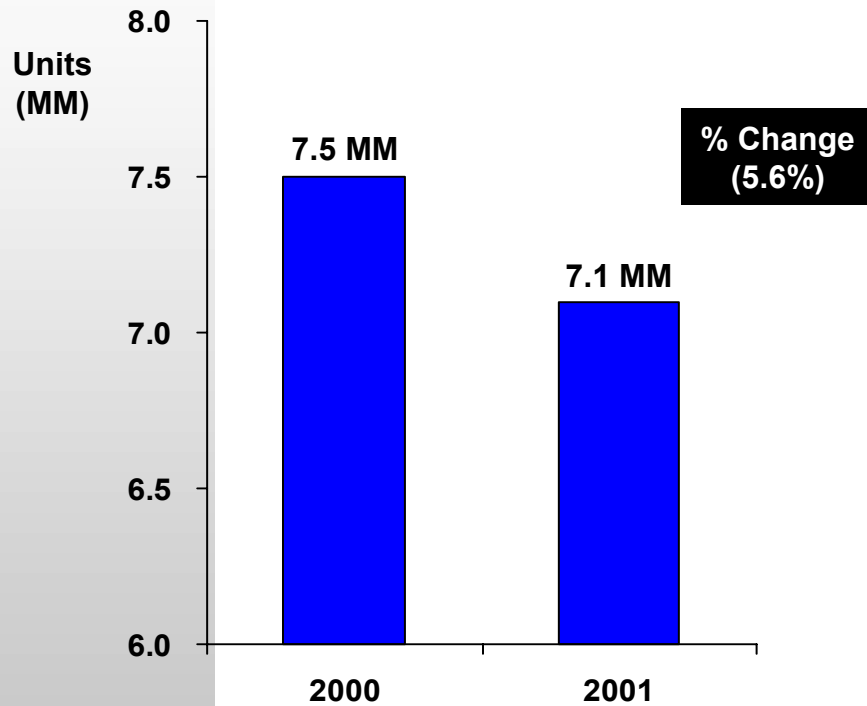
- DaimlerChrysler announcing plans for 40% cost reduction over next 5 years
 - Plans 15% cut in overall production level in 2001 compared to 2000
- GM and Ford have announced company-wide cost reduction between 10% and 16%
- Production plans cut about 15% on average compared to 2000

Diversified conglomerates continue to divest automotive operations

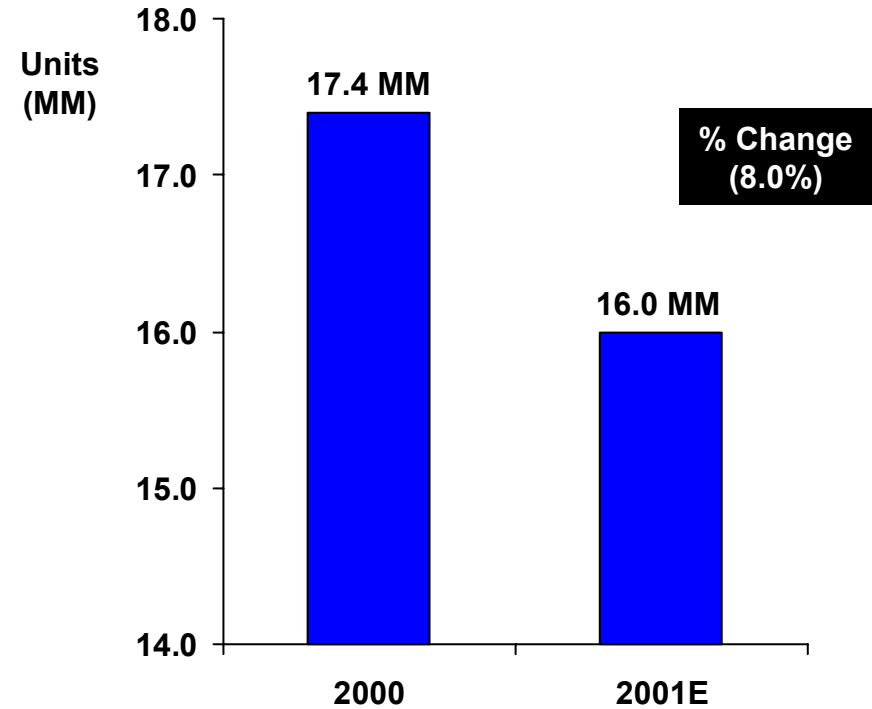
- Textron, Inc. – divest its automotive business in the wake of a slowdown
- Small to mid-size businesses experiencing difficulty in this environment

Automotive Sales On A Downward Trend After Record Year In 2000

January to May Sales



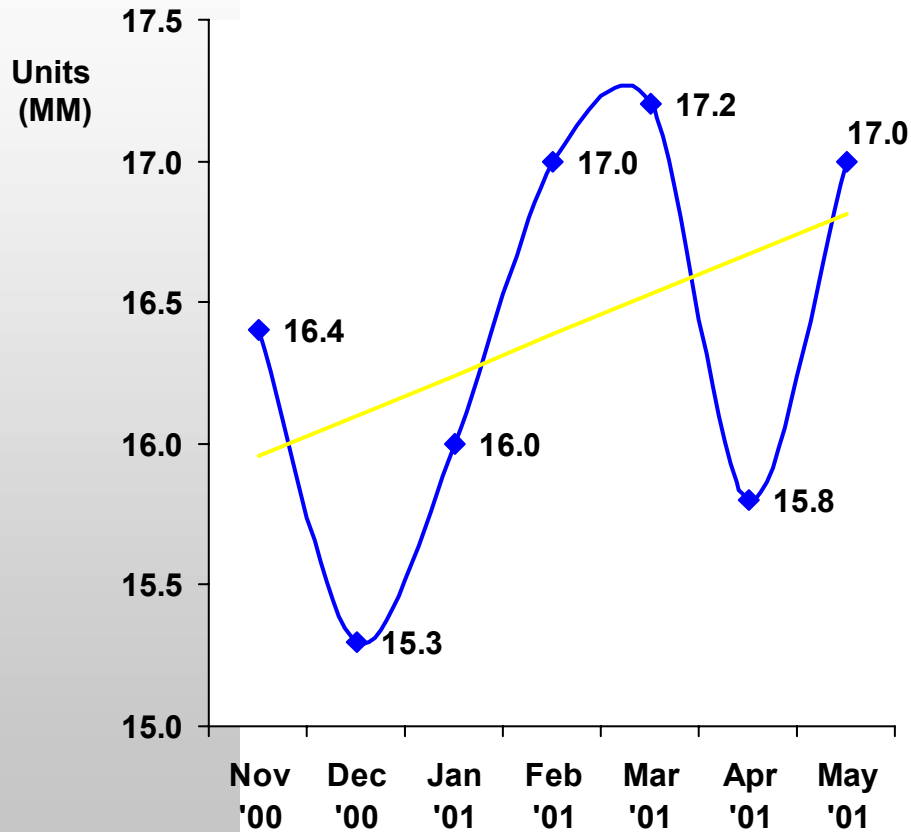
Annual Sales



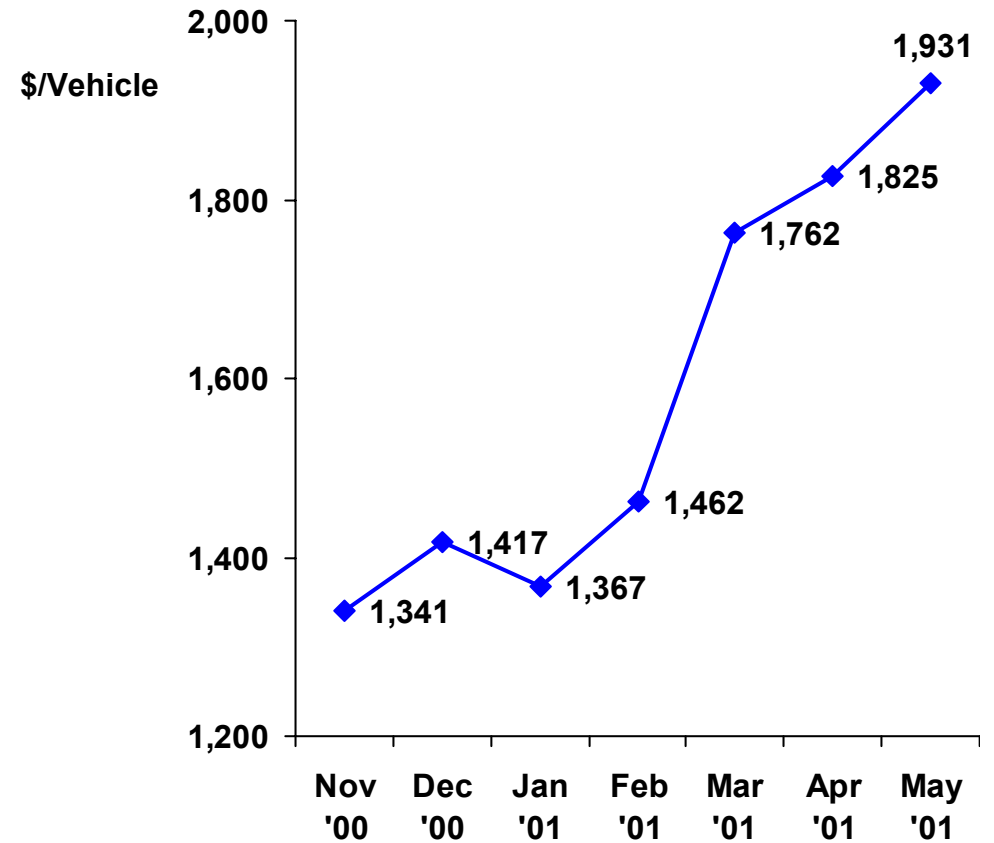
Strong Impact On Industry Performance

The Current Year Sales Maintained By Increased Levels Of Marketing Incentives

Seasonally Adjusted Annual Rate (SAAR)

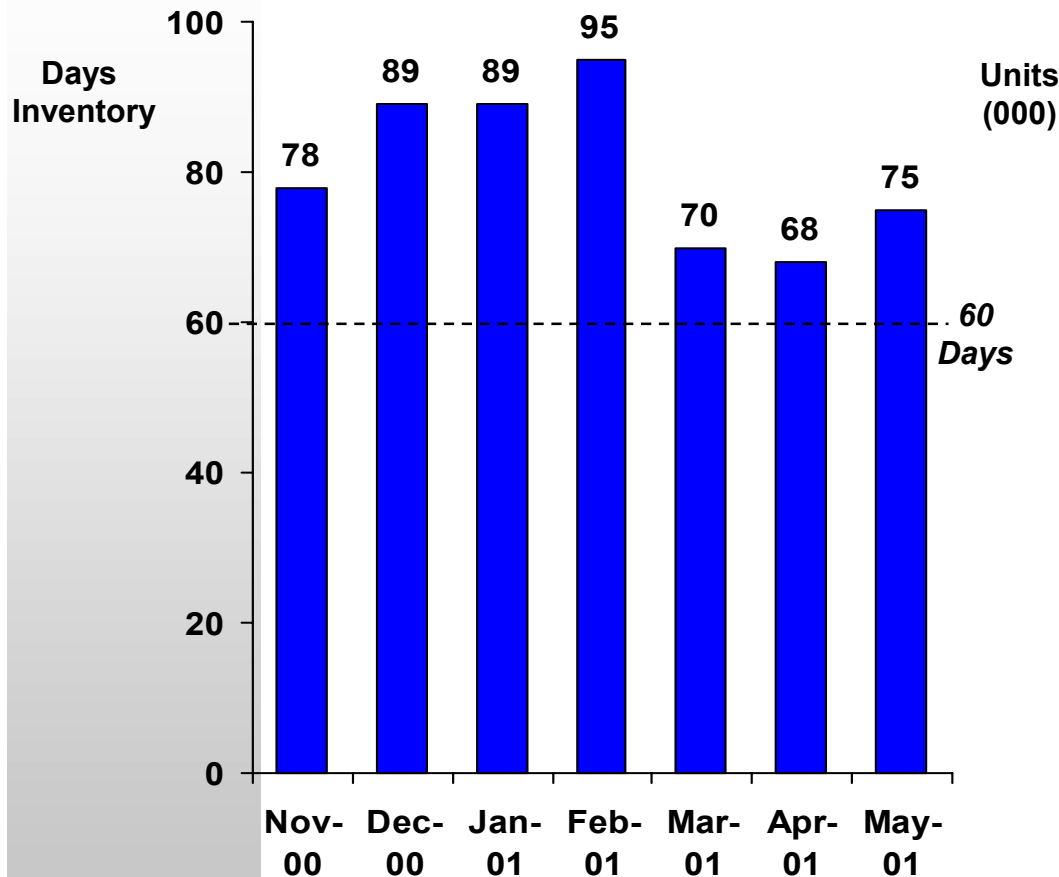


Average Incentives/Vehicle

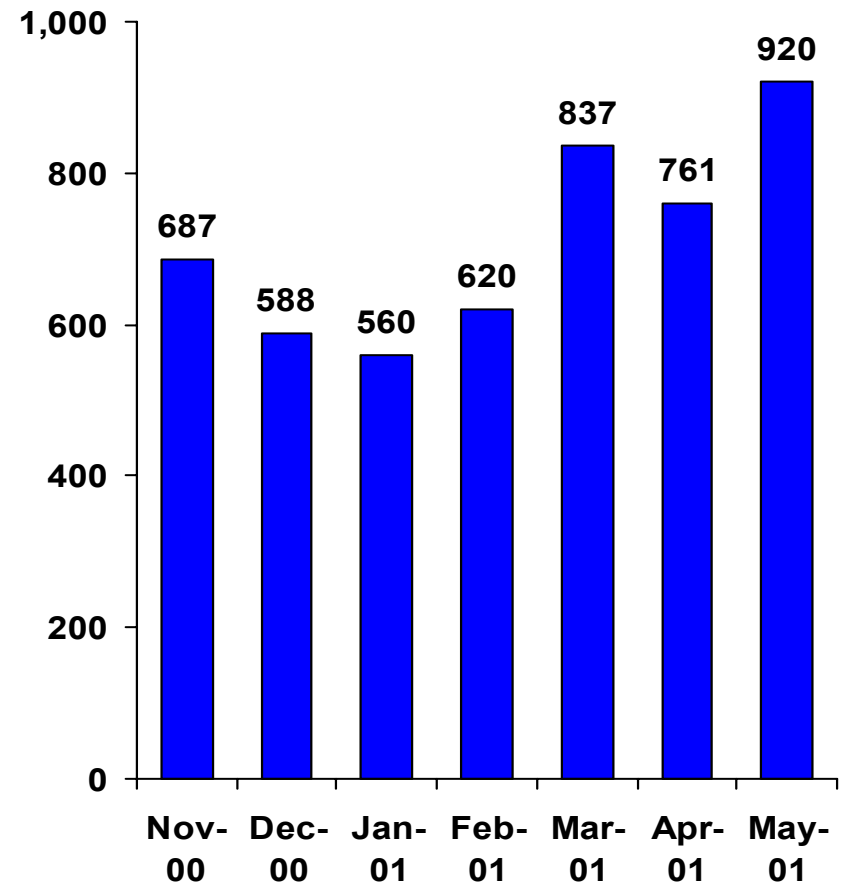


Existing Inventories Have Dropped In Response To Incentives And Reduction In Production

Big 3 Inventories (Days Supply)

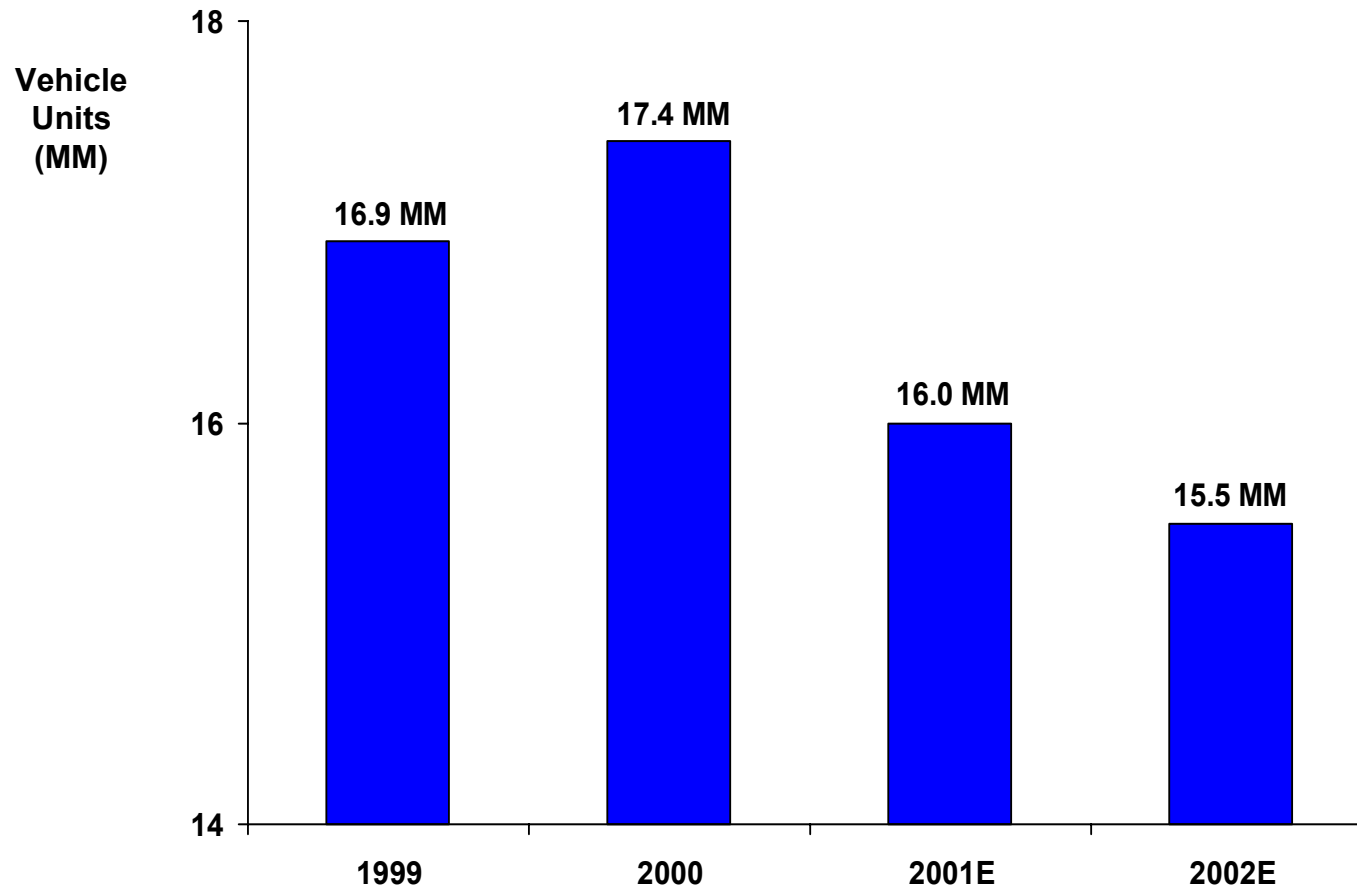


Big 3 Domestic Production



Implications For Minority Suppliers?

Industry Slowdown Forecasted For 2001 And 2002

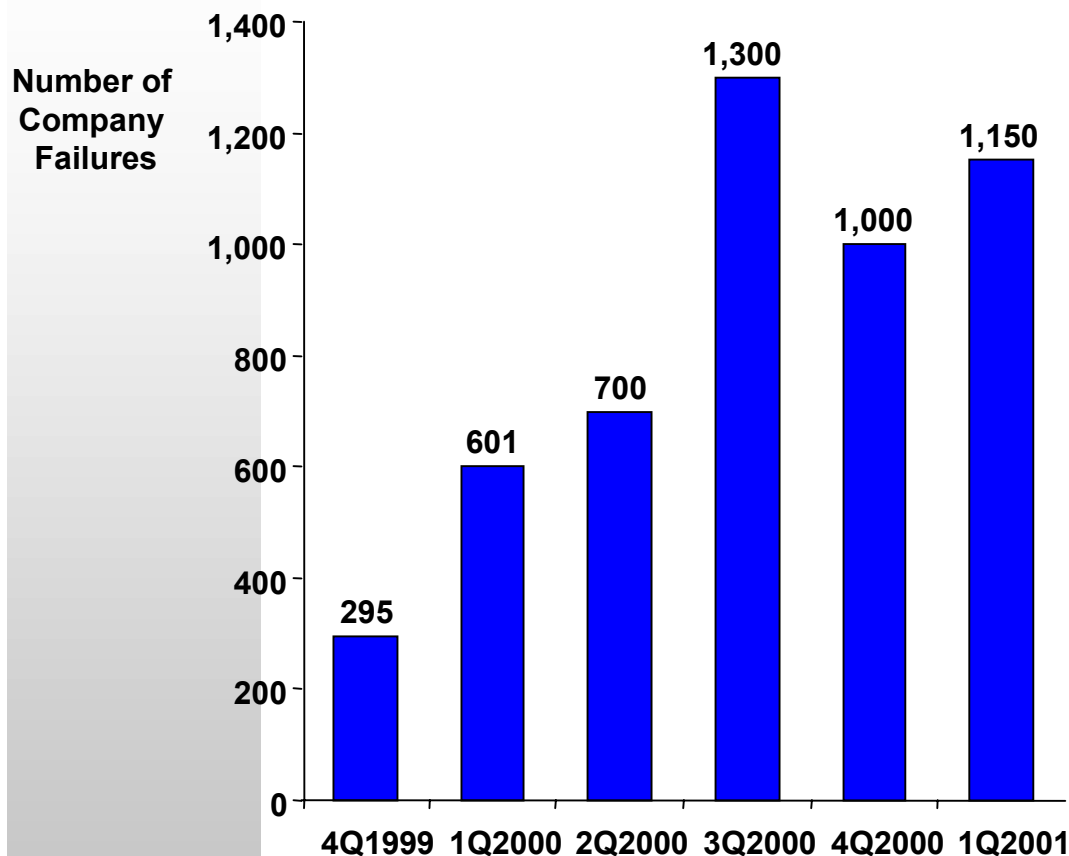


How Will This Affect Minority Suppliers?

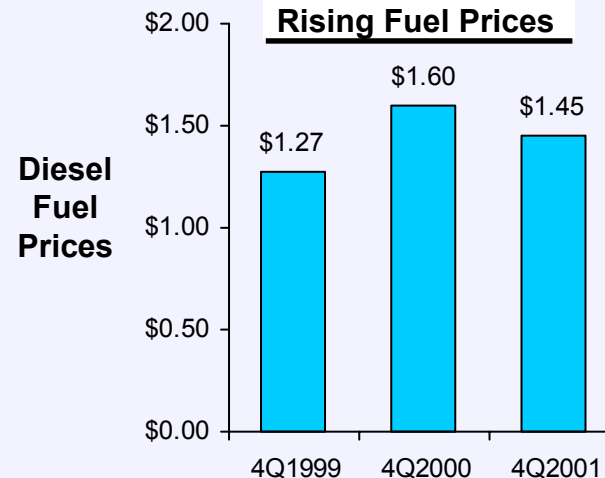
Industry Slowdown Creates A Difficult Business Environment For Small And Mid-Sized Companies

Example: Trucking And Logistics Companies Have Been Vulnerable

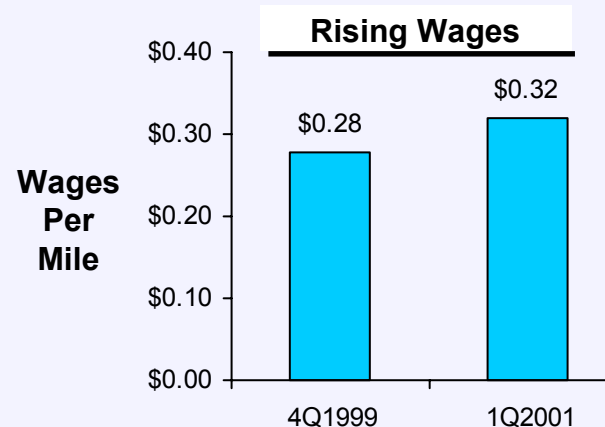
Trucking Company Failures



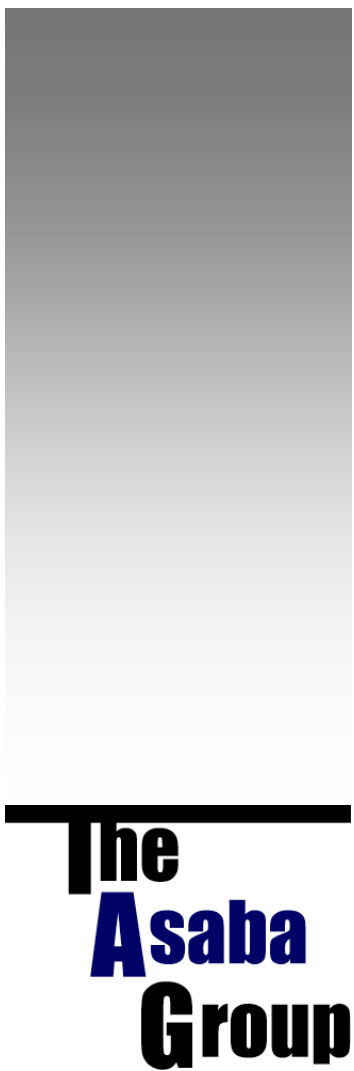
Rising Fuel Prices



Rising Wages



Minority Suppliers Not Immune To These Pressures



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Key Highlights

Automotive Manufacturers (OEM's) declining profitability will increase focus on cost reduction

- Tier One Suppliers remain under price pressure and cost surveillance from OEM's
- Grow in importance through innovation and manufacturing large modules and systems

Manufacturers reducing costs and levels of investment capital (Fixed Costs)

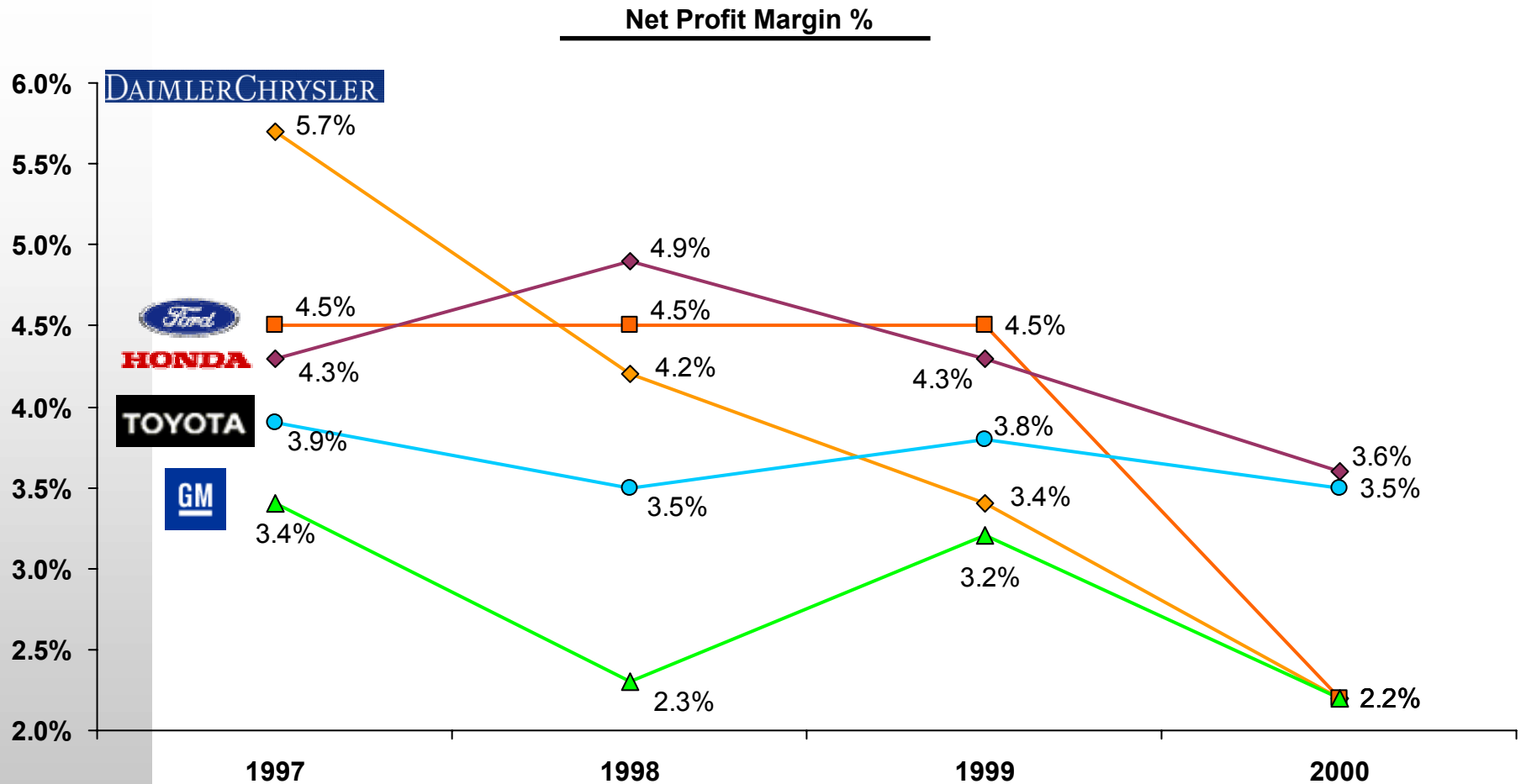
- Reducing number of car platforms
- Outsourcing more to large suppliers (Product, Technology Development, Product Testing, etc.)
- Driving investment efficiency with Facilities and Tooling related decisions

Tier One Suppliers that survive industry consolidation will drive for cost reduction at lower tiers

- Most planning rationalization of supply base (Tier II and III Suppliers)
- Minority Suppliers need to focus efforts on big suppliers to achieve sustainable growth

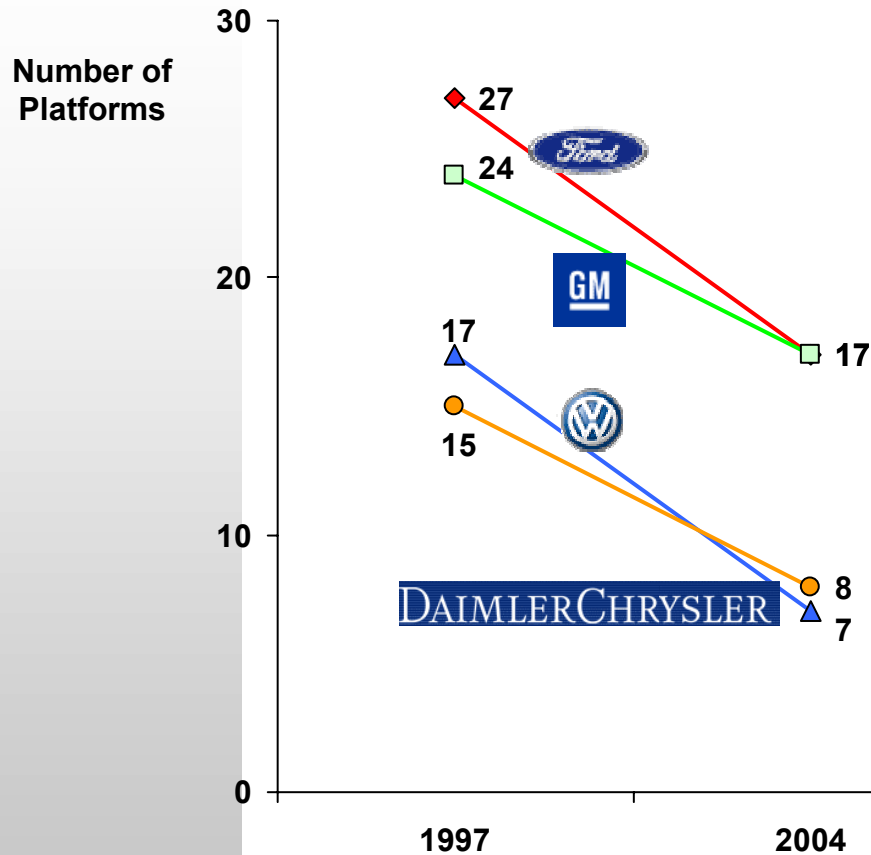
Auto Manufacturers Have Experienced Declining Profitability

Likely To Continue With Declining Sales And Overcapacity



Cost Surveillance/Squeeze Will Continue On Tier I Suppliers

Automotive Manufacturers Continue To Rationalize Car Platforms



Implications

- OEM's achieve greater part/system commonality
 - Increases economics of scale
- Limits OEM's ability to achieve huge profit differentiation
- Increases dependency of few large suppliers

Increase Concentration Of Purchasing With Larger Suppliers

Automotive Manufacturers Moving Large Chunks Of The Vehicle To Fewer Suppliers

General Motors announces outsourcing of complete interiors business

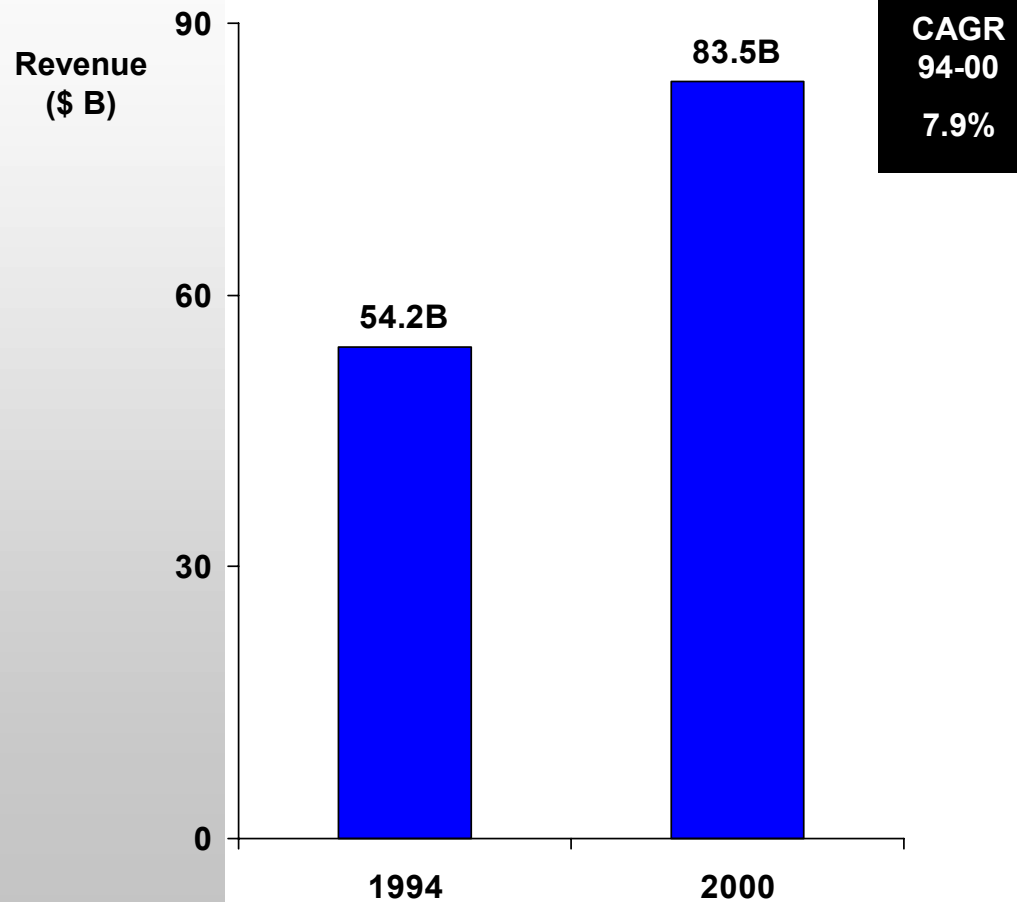
- A single supplier for each vehicle program
- Suppliers (System Integrators) must be able to design, engineer, and manage all other suppliers and components
- Suppliers are expected to identify minority supplier partnerships and content in order to be considered
- Key System Integrators are:
Visteon, Delphi, Magna, Faurecia, Johnson Controls, Inc., Lear and Venture

Minority Suppliers Should Understand These Dynamics

Large Automotive Suppliers Getting Bigger To Meet Demands Of OEM's

Driven By Continued Industry Consolidation And Divestitures

Top 10 North American Auto Suppliers



Top 10 Suppliers (Revenue)

1. Delphi (\$25 B)
2. Visteon (18.5 B)
3. Dana (\$9.5 B)
4. Lear (\$14 B)
5. Johnson Controls (\$11.8 B)
6. Magna (\$10.1 B)
7. Bosch (\$17.8 B)
8. TRW (\$11 B)
9. Denso (\$16.4 B)
10. Eaton (\$4.0 B)

The Consolidation Has Led To 3 Or 4 Global Suppliers For Each Major System

Engine/Transmission/Torque Management

- Bosch
- Lucas
- Denso
- Delphi

Rolling Chassis/Drive Train

- Dana
- Magna
- Thyssenkrupp
- Delphi

Cockpit Systems/Driver Interfaces/Interior Trim

- Johnson Controls, Inc
- Faurecia
- Lear

Corner Modules and HVAC

- Delphi
- Visteon
- Valeo
- Behr

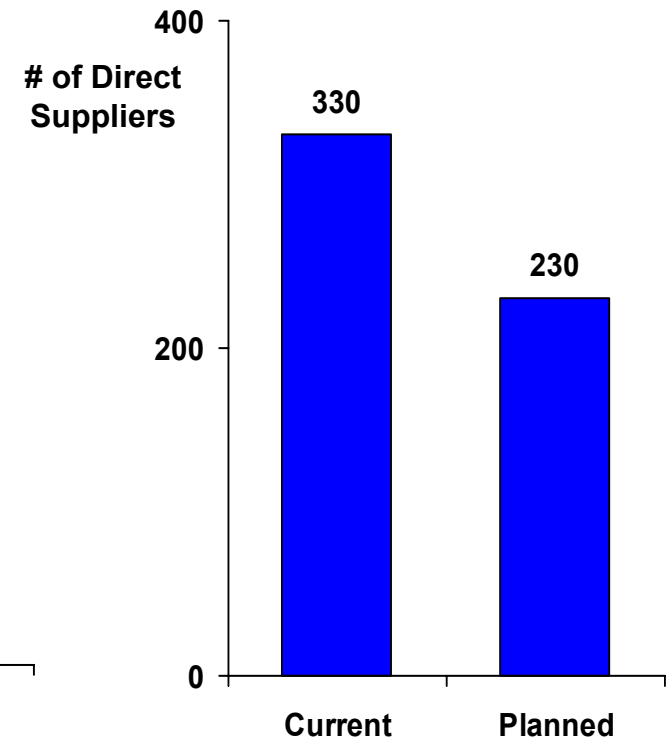
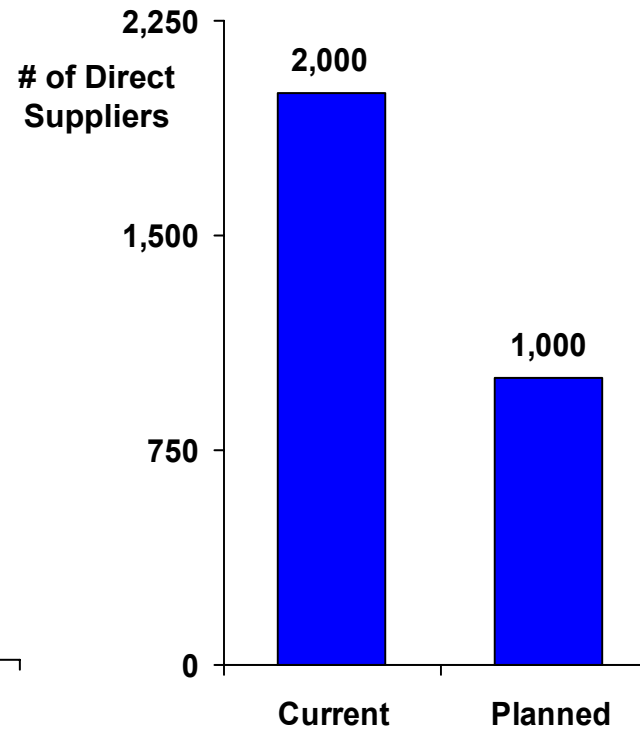
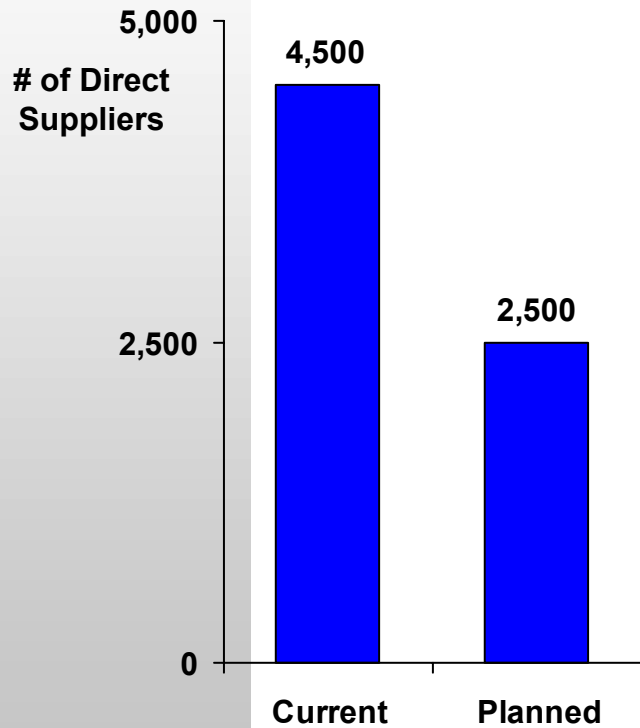
Minority Suppliers Must Focus On These Suppliers For Growth

Tier One Suppliers Beginning To Rationalize Their Supply Base

Delphi Spend: \$13.5 B

ArvinMeritor Spend: \$8.1 B

American Axle & Mfg Spend: \$4.7 B



Large Suppliers Bear Increased Responsibility For Cost Reductions

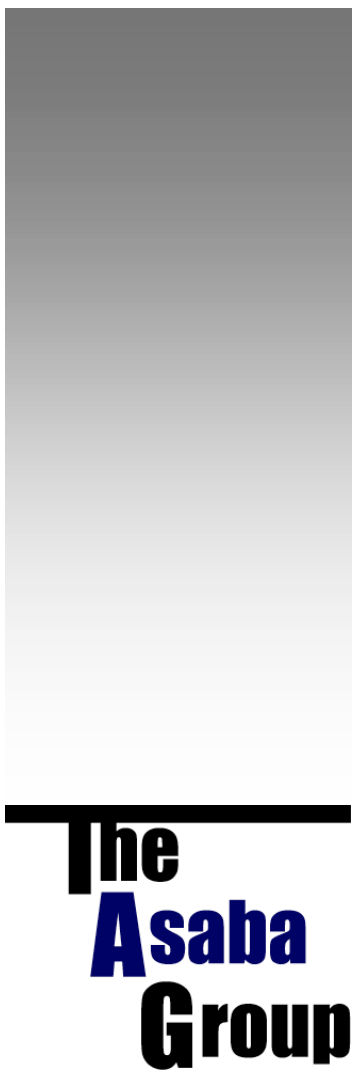
Most will cut costs by 20 to 30%

Will drive shake-out and consolidation in the lower tiers

Capturing effective responsibility for technology, design, manufacturing and sourcing choices

Pushing standardisation across customers and avoiding being backed into supplying the 'tail' of low-volume, non-standard products

Both cutting cost and investing in capabilities



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Key Highlights

Top line risks can be mitigated by revenue diversification

- Focus on high volume platforms, i.e., greater than 500,000 units
 - Ford CW170 or VW A4
- Diversify revenues by customer group; sales incentives may be masking demand weakness
 - Domestic Manufacturers versus Imports
- Diversification can be achieved by targeting Tier One Suppliers

Identified growth initiatives must be articulated by value chain roles

- Tiering nomenclature not adequate for strategic decision-making
- Gross profit dollars (value added) lies with component specialist and system / module suppliers

Geographic scope of supplier competition can be defined by an optimisation

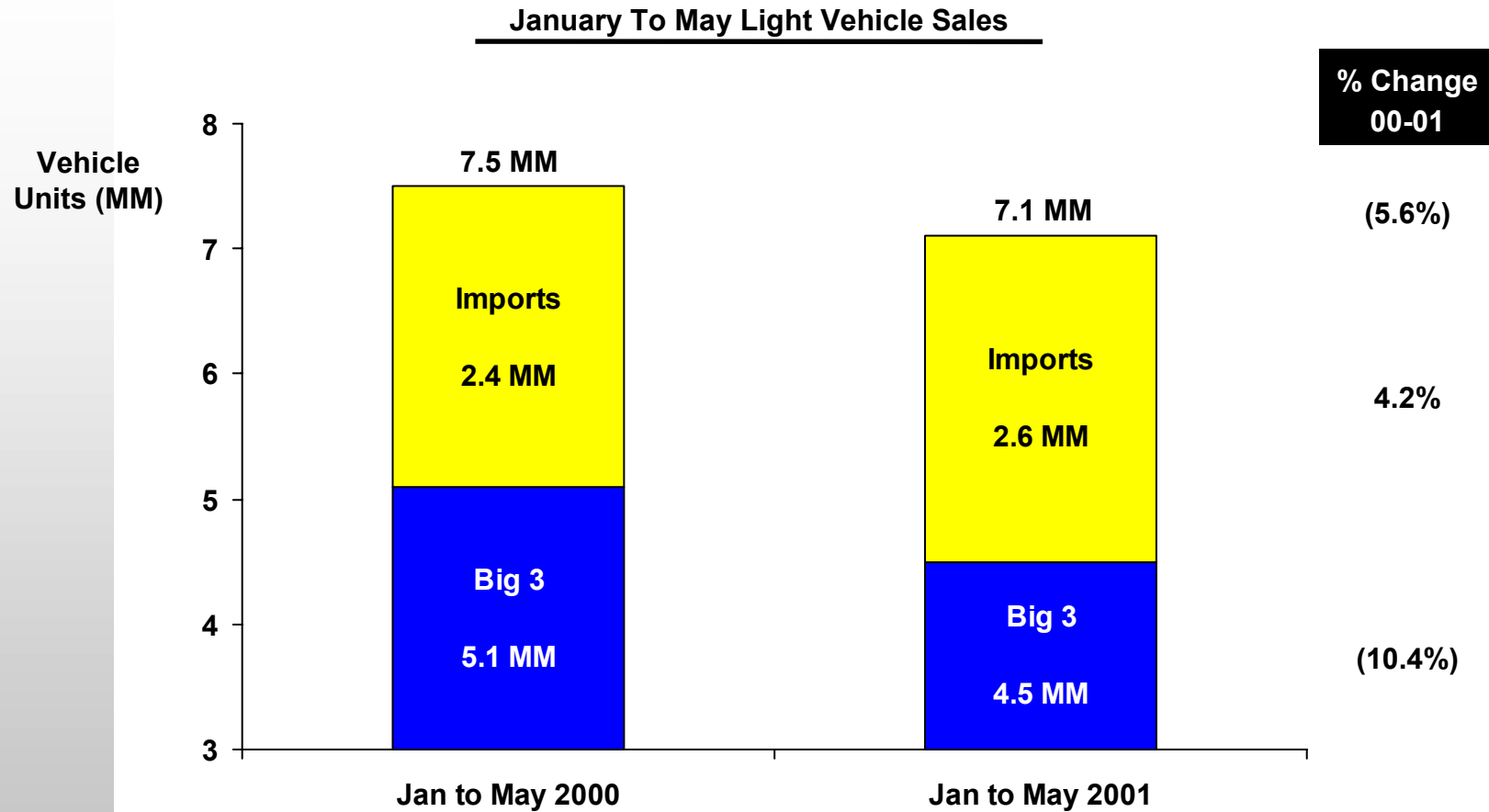
- Trade-off between product-specific cost and freight

Three growth paths are available to Minority Suppliers

- Largely independent of commodity and industry dynamics
 - Low cost
 - New categories/markets
 - Solutions provider

Big 3 Manufacturers Sales Declining While Imports Growing

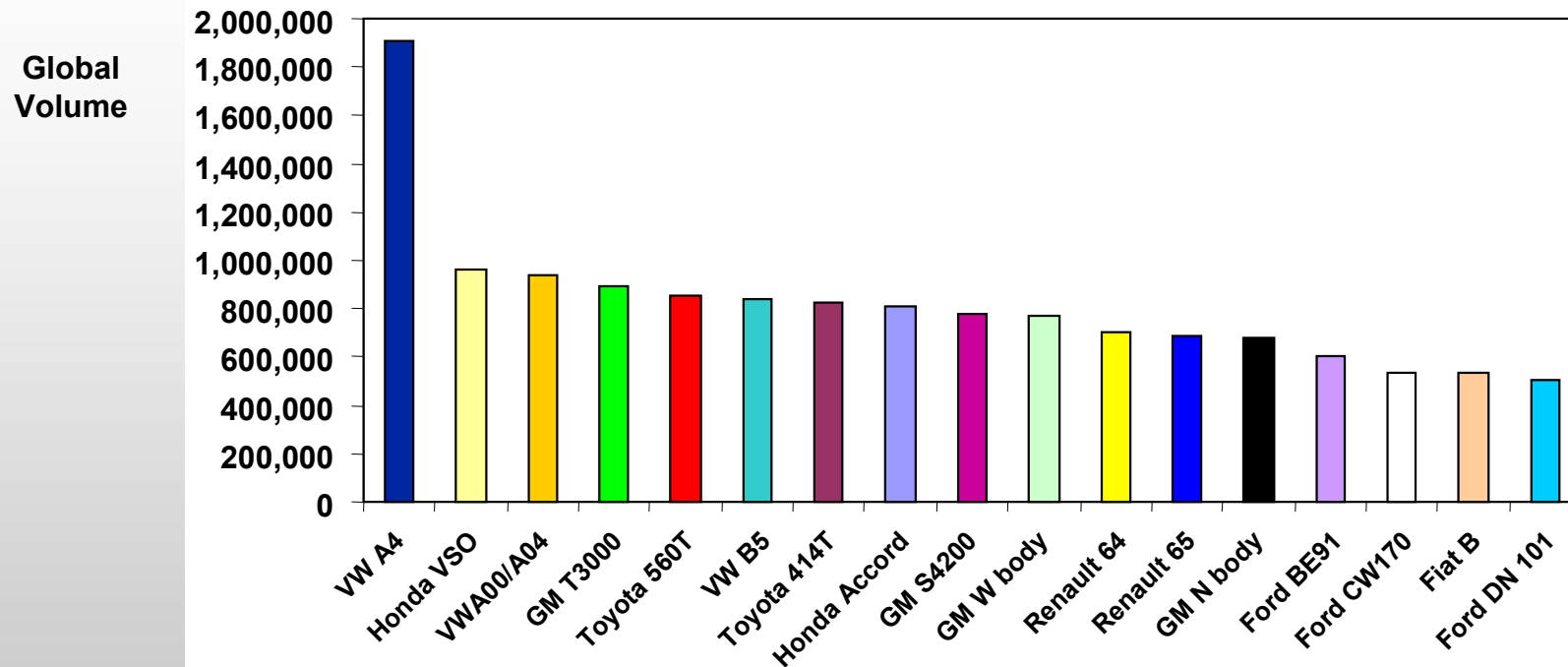
Significant Revenue Risks Associated With Big 3 Customer Concentration



**Minority Suppliers Must Diversify Revenues
By Reducing Revenue Concentration**

Minority Suppliers Can Reduce Industry Volume Sensitivity By Focusing On High Volume Platforms

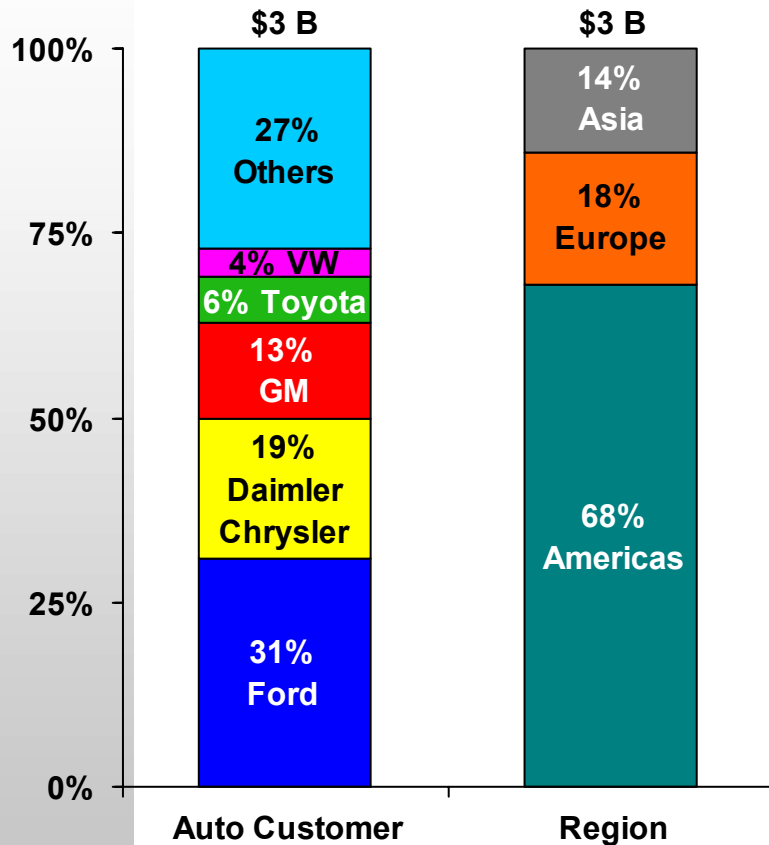
Top 20 Passenger Car Platforms, 1999



Minority Suppliers Must Target High Volume Platforms To Be Successful

Reduction Of Top Line Revenue Risks Can Be Achieved By Targeting Tier One Suppliers

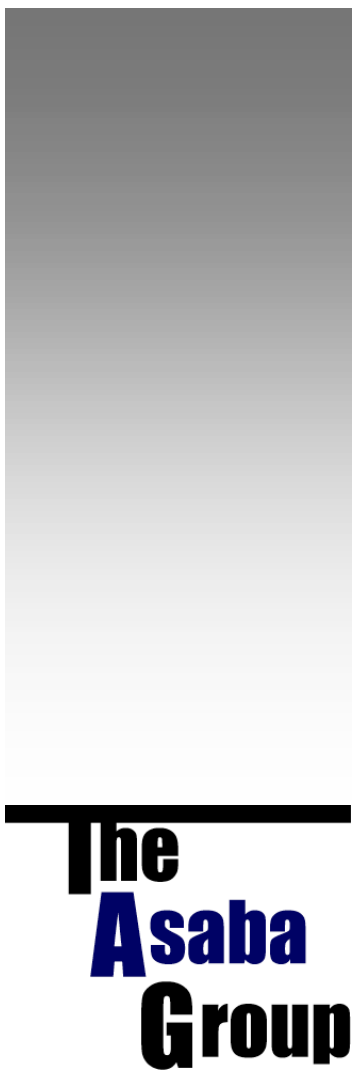
Example: Borg-Warner Is a Global Supplier of Components/Assemblies for Power Train Applications



Insights

- Drives for part commonality across customers and region
- Company focuses on being a component/technical specialist
 - Innovation to drive growth and margin

MBE's Must Seek To Do Business With These Companies



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Three Identified Growth Strategies

Independent of Commodity and Industry Dynamics

Low Cost

Lowest Cost and
Best Value for
Key Commodities

**New Growth
Categories/
Markets**

Focus on High
Growth Application

**Solutions
Provider**

“Doing More
for Customers”

Each Requires A Different Strategic Orientation

Each Requires Unique Focus And Capabilities

	<u>Process/Commodity Examples</u>	<u>Basis of Success</u>	<u>Growth Approach/Tacticals</u>
Low Cost Commodity Producer	<ul style="list-style-type: none"> • Injection molding • Metal processing • Cut & Sew/build-to-print/shoot & ship 	<ul style="list-style-type: none"> • Economies of scale • Understanding cost drivers (ABC) 	<ul style="list-style-type: none"> • Rollup consolidation • LBO/Acquisitions
New Growth Categories/ Markets	<ul style="list-style-type: none"> • Light materials • Electronic applications • Navigation Systems 	<ul style="list-style-type: none"> • Engineering and design • Application development • Low-cost/flexible manufacturing 	<ul style="list-style-type: none"> • Build compatibility <ul style="list-style-type: none"> - JV/Alliance - M&A
Solutions Provider	<ul style="list-style-type: none"> • Automotive testing (non-production) • Subsystem assembly/development • IT/Sequencing operations 	<ul style="list-style-type: none"> • Commodity management • Lower transaction cost <ul style="list-style-type: none"> - Outsourced operations 	<ul style="list-style-type: none"> • Extend geographic reach • M&A • JV

Low Cost Strategy

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Focused On Low Value Added Commodity Group And Processes

Plastic Processing (Injection Molding)

Supplier	Global Sales 1999 (\$MM)	Global Sales 2000 (\$MM)	% Change 1999-2000 (\$MM)	NA Sales 1999 (\$MM)	NA Sales 2000 (\$MM)	% Change 1999-2000 (\$MM)
Lacks Enterprises	255	255	0.00%	222	219	-1.35%
Becker Group	300	235	-21.67%	300	235	-21.67%
Carlisle Engineered Products Inc.	315	303	-3.81%	312	294	-5.77%
Plastech Engineered Products Inc.	300	300	0.00%	300	300	0.00%
American Showa Inc.	736	976	32.61%	300	351	17.00%
Key Plastics, LLC	551	576	4.54%	358	380	6.15%
Average Size	410	441	7.65%	299	297	-0.73%

Little or no growth in North America

- Players stole share or grew by acquisition
- Global growth largely acquisitions

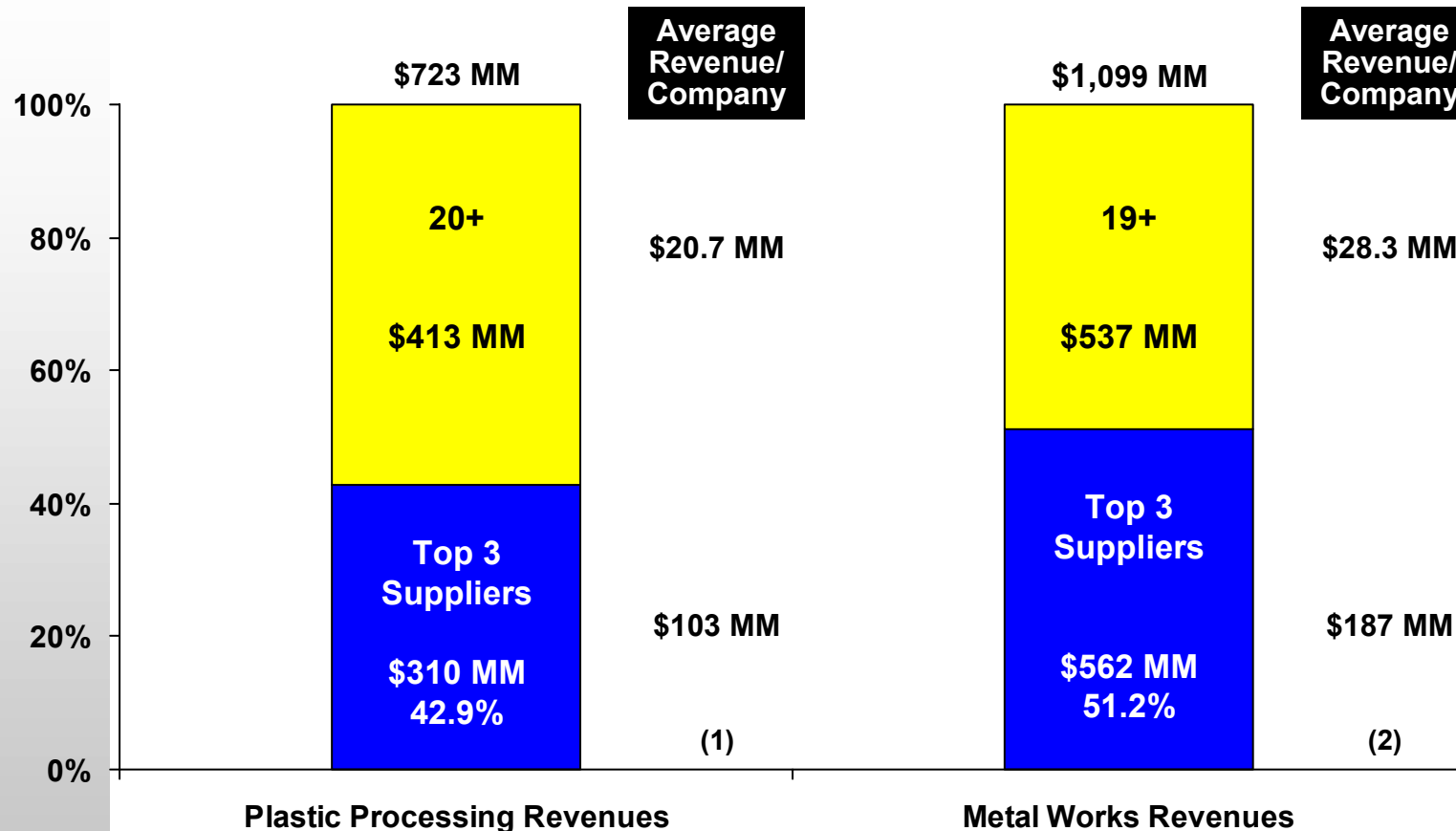
Same Observation With Metal Processing – Machining And Stampings

Supplier	Global Sales 1999 (\$MM)	Global Sales 2000 (\$MM)	% Change 1999-2000 (\$MM)	NA Sales 1999 (\$MM)	NA Sales 2000 (\$MM)	% Change 1999-2000 (\$MM)
Global Metal Technologies	225	228	1.33%	214	217	1.40%
Pilot Industries Inc.	300	260	-13.33%	246	237	-3.66%
Gibbs Die Casting	280	340	21.43%	252	282	11.90%
Talon Auto Group	290	300	3.45%	276	285	3.26%
Ogihara America	363	369	1.65%	289	295	2.08%
Harvard Industries	318	318	0.00%	312	312	0.00%
Amcast Automotive	451	500	10.86%	271	315	16.24%
Mayflower Vehicle Systems	650	540	-16.92%	406	335	-17.49%
Citation Corp.	395	409	3.54%	391	405	3.58%
Shiloh Industries	535	630	17.76%	535	630	17.76%
Average Size	381	389	2.29%	319	331	3.79%

Critical Mass Appears To Be \$300 MM To \$400 MM

Opportunity In Commodity Groups With High Degree Of Fragmentation

Plastics and Metal Processing Highly Fragmented and Captive to Auto Industry



Consolidation/Rollup Opportunity to Attain Required Critical Mass for Cost Competitiveness

(1) Includes Injection, Extrusion and Blow Molding Suppliers (2) Includes Machinery, Welding and Stamping Suppliers
 SOURCE: Data based on a sample of 210 minority suppliers to major Automotive Manufacturers; Asaba Group Analysis

Heartland Industrial Partners Provides A Model From Consolidation And Tier II Growth

Heartland Industrial Partners Led by David Stockman (former OMB Director)

- Focus on becoming a “Tier II Titan”
- Based on two platforms: Metals and Interiors
- Each platform expected to grow to \$6 Billion within six years

Metals Platform

Designer and supplier of low cost metal formed assembly modules

Acquired Companies to form new company called Metaldyne Corp.

- MascoTech, Inc. – \$1.1 Billion in Revenues; metal forming
- Simpson Industries, Inc. – \$150 Million in Revenues; precision machining
- Global Metal Technologies, Inc. – \$228 Million in Revenues; castings

Interiors Platform

Acquired companies to form interior component parts supplier

- Collins and Aikman – \$1.9 Billion in Revenues; interior trim and molded parts
- Becker Group – \$235 Million in Revenues; plastic parts/molding
- Joan Fabrics – \$NA Million in Revenues; automotive fabrics

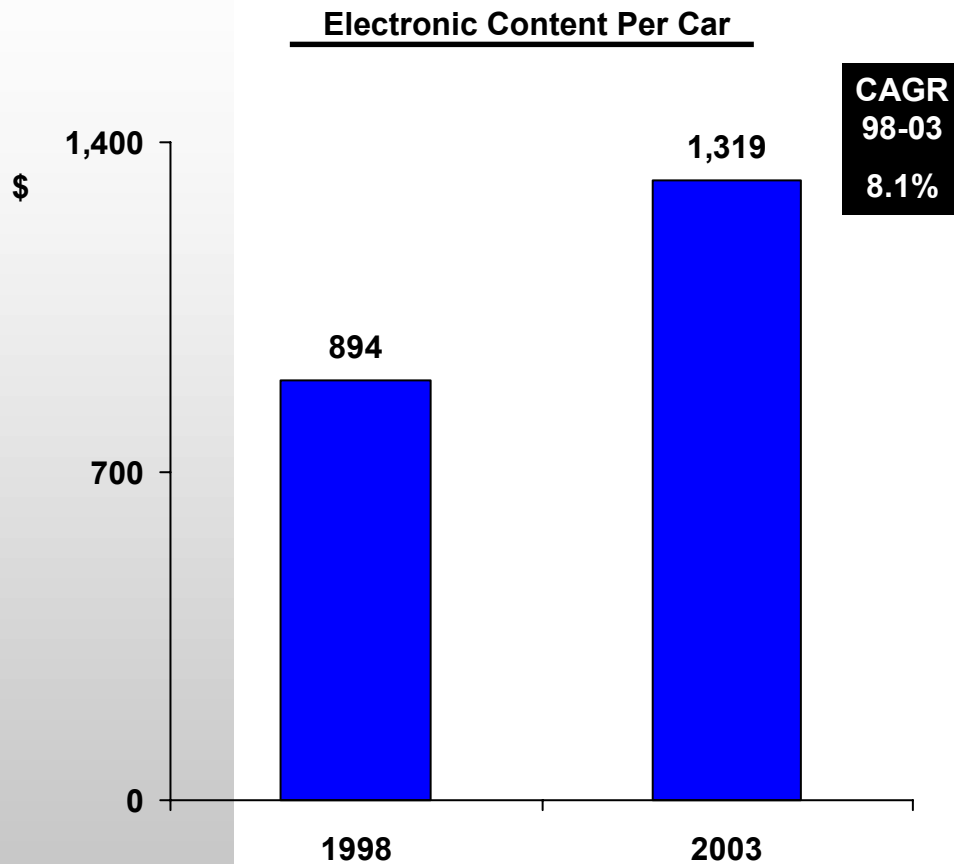
New Markets/Categories Strategy

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Electronics Segment/Application Strong Area For Growth Opportunities

Driven by Continued Innovation in Automotive Safety, Comfort, and Entertainment



Key Features/Applications

- Next Generation Braking Systems
- Steering Systems
- Plug and Play capability for entertainment systems
- Climate-Control Systems
- Dashboard Instrumentation
- GPS Navigation System
- Airbag Control Modules

Strong Growth Compared To Industry Growth Of 2% to 3%

Emerging Electronic Applications And Technologies

Security

- Access Control
- Burglar Alarms
- Roadside Emergency Assistance

Infotainment

- On-Demand Content
 - Audio
 - Video
 - Games
- Mobile Internet
- In Car Entertainment

Vehicular Functions

- Remote Diagnostics
- Brake
- Headlights
- Suspension
- Dash board Instrumentation

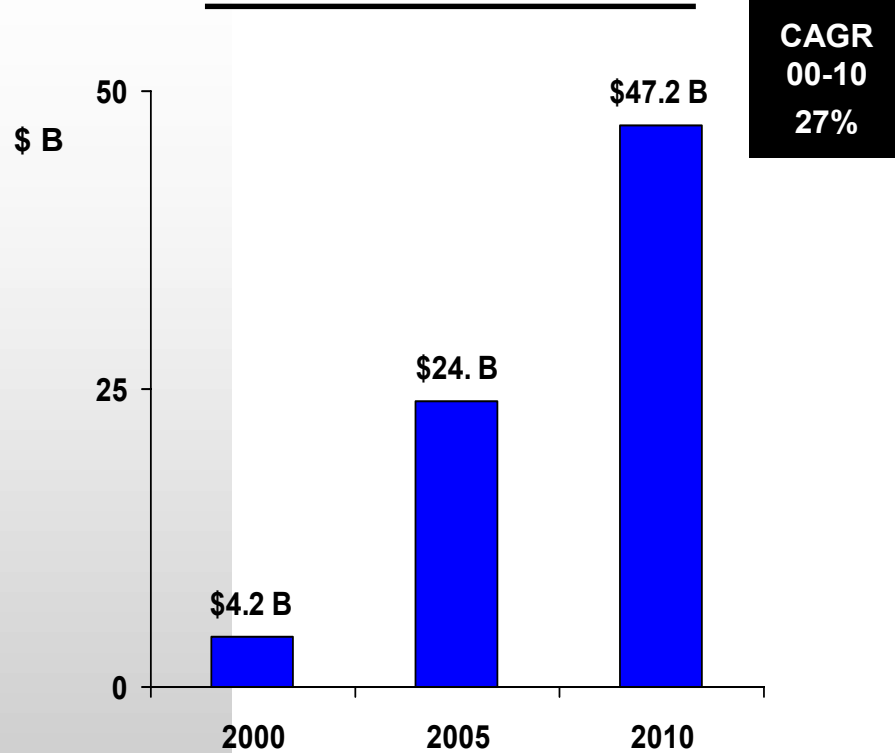
Telematics

- Dynamic Navigation
- Traffic Information
- Concierge Services

Minority Suppliers Must Consider Partnering With Companies With Core Technology Expertise

Telematics And Navigation Are Highest Growth Opportunities

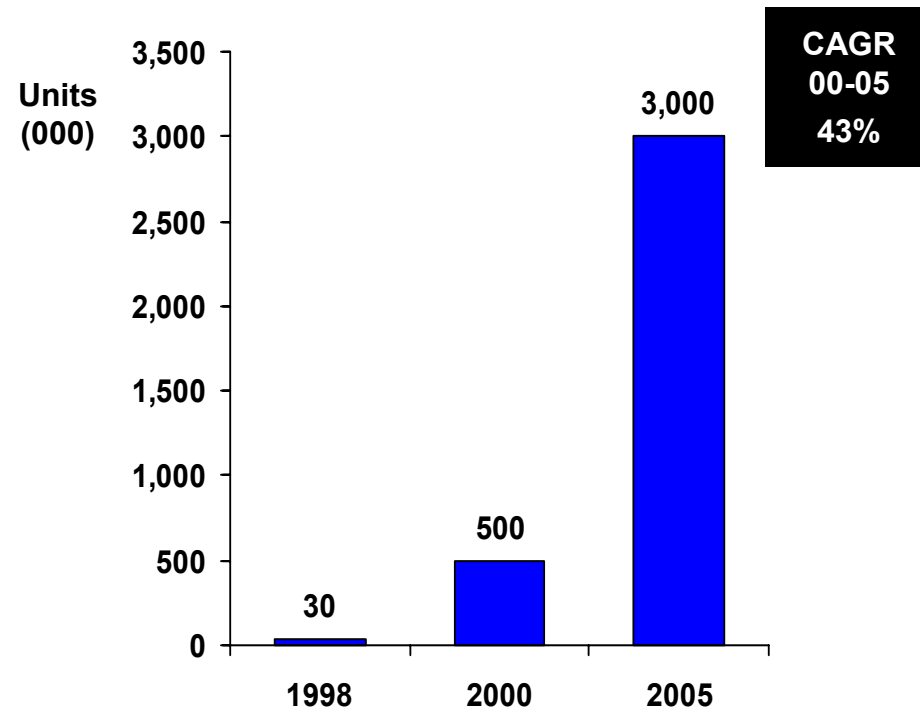
Worldwide Telematics Market



Key Suppliers To Target

- Bosch
- Fujitsu
- Delphi
- Visteon
- Siemens

Navigation Systems (US)



Purchased Components

- Dashboard Displays
- Driver Interface Boards
- Software and Database Services
- Higher Voltage Batteries

SOURCE: UBS Warburg

Minority Suppliers Must Position Themselves In Core Areas Of The Value Chain

Electronic Commodity Value Chain



- | | | | |
|---|---|--|--|
| <ul style="list-style-type: none"> • Passives • Sensors • Fasteners | <ul style="list-style-type: none"> • Cables • Wire Harnesses • PCB | <ul style="list-style-type: none"> • Application Modules • IC Integration • ASIC/Optical | <ul style="list-style-type: none"> • Fuel Systems • Navigation Systems |
| ↓ | ↓ | ↓ | |
| <ul style="list-style-type: none"> • Offshore Manufacturing • Asia, Africa, Latin America | <ul style="list-style-type: none"> • Low Cost Manufacturing • Mississippi, Ohio • Mexico • Honduras/Philippines | <ul style="list-style-type: none"> • Design/Engineering/Test/Qualification • Manufacturing • Mexico | |



Electronic Category Shows Strong Growth In U.S. And Globally

Electronic Components/Sub-Assemblies Suppliers

Supplier	Global Sales 1999 (\$MM)	Global Sales 2000 (\$MM)	% Change 1999-2000 (\$MM)	NA Sales 1999 (\$MM)	NA Sales 2000 (\$MM)	% Change 1999-2000 (\$MM)
Hitachi Auto Products	390	422	8.21%	386	418	8.29%
Sumitomo Electric Wiring Systems	400	499	24.75%	380	474	24.74%
Saturn Electronics and Engineering	250	500	100.00%	245	490	100.00%
Stoneridge Inc	675	700	3.70%	574	581	1.22%
Osram Sylvania Inc	600	689	14.83%	396	455	14.90%
Alps Automotive	677	780	15.21%	310	359	15.81%
Clarion Corp. Of Am	931	992	6.55%	298	268	-10.07%
Hella NA Inc	1,438	1,625	13.00%	259	349	34.75%
Stanley Electric U.S.	1,710	1,790	4.68%	434	422	-2.76%
Average Size	786	889	13.10%	365	424	16.27%

Growth Due To Increased Content Per Vehicle

Electromechanical Applications Are Evolving Into Electronic Solutions

Electronic Modules Suppliers

Supplier	Global Sales 1999 (\$MM)	Global Sales 2000 (\$MM)	% Change 1999-2000 (\$MM)	NA Sales 1999 (\$MM)	NA Sales 2000 (\$MM)	% Change 1999-2000 (\$MM)
Motorola Inc.	2,680	2,700	0.75%	1,822	1,701	-6.64%
Panasonic Auto Electronics Co.	1,950	2,100	7.69%	604	630	4.30%
Mitsubishi Electric Auto America	3,000	3,090	3.00%	720	742	3.06%
Siemens Automotive	3,600	3,700	2.78%	1,260	1,295	2.78%
Calsonic NA Inc	2,717	3,826	40.82%	519	800	54.14%
Eaton Corp.	4,200	4,000	-4.76%	2,940	2,800	-4.76%
GKN Automotive Inc	3,900	4,300	10.26%	1,404	1,548	10.26%
Average Size	3,150	3,388	7.57%	1,324	1,359	2.66%

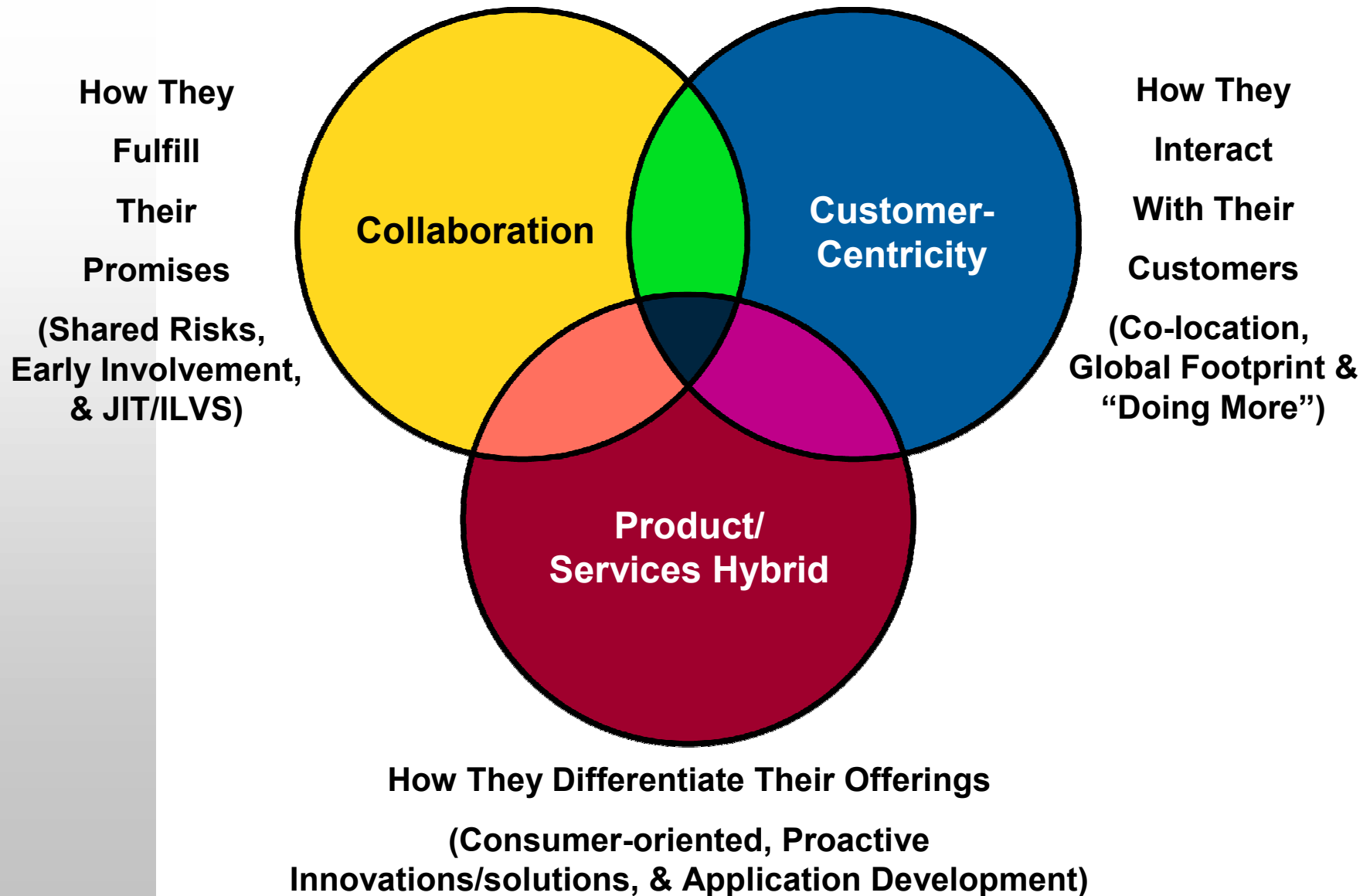
**Large Suppliers With Design And Integration Skills
 – Possible Joint Venture Partners**

Solutions Provider Strategy

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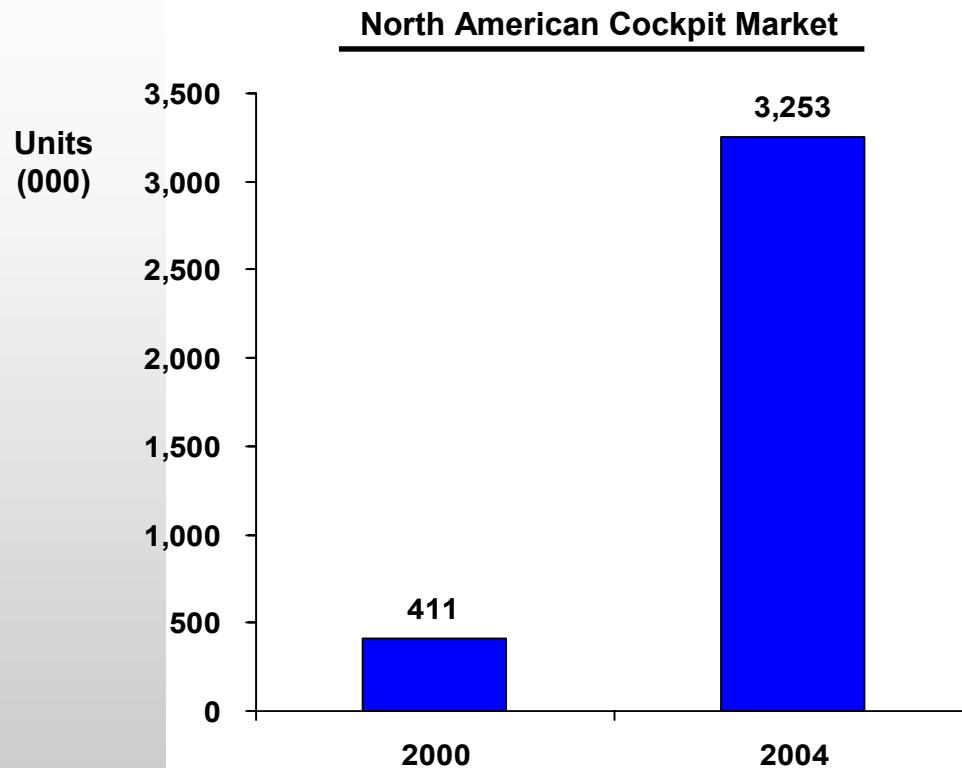
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Minority Suppliers Who Aspire To Be Solutions Providers Must Think Like Their Customers: Systems Integrators!



Most Opportunities Are Linked To Large Tier One Suppliers Focused On Delivering Total Systems

Example: Interiors/Cockpit Systems



Estimated at \$140 Billion Globally

Key Suppliers

- Johnson Controls, Inc.
- Delphi
- Faurecia
- Lear
- Venture

Some Opportunities

- Sub-Systems and Modules
- Components/Parts
- JIT and Sequencing

In Most Situations, These Are Opportunities To Create JV's With Suppliers

Non-Production Opportunity – Automotive Testing Services

Estimated at \$15 Billion globally and growing about 3-5% yearly

- U.S. Market size estimated at approximately \$6 to \$8 Billion

Market boundaries not well defined

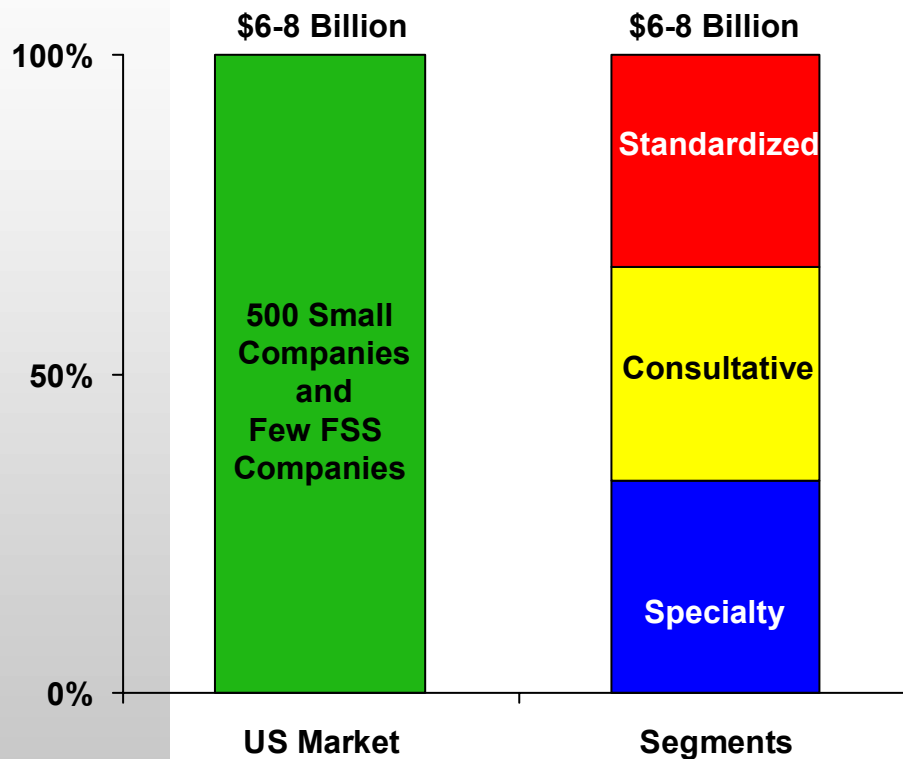
- Automotive manufacturers in-source large portions of the testing needs
 - With value chain reconfigurations and OEMs' new focus, expect willingness to outsource most in-house functions
 - Most large suppliers preoccupied with OEM product development issues
- Current outsourced market highly fragmented and in “low-tech” areas

Value proposition exist in ability to provide specialized know how, shorten time to market and lower economics

- OEM's – Seeking third party validations and standards
Want Tier I suppliers to perform full systems testing
- Tier I – Looking for turnkey solutions for testing needs, both at component and sub-system level

Automotive Testing Is A Fragmented Marketplace

U.S. Testing Market



Industry Observations

Involve all activities

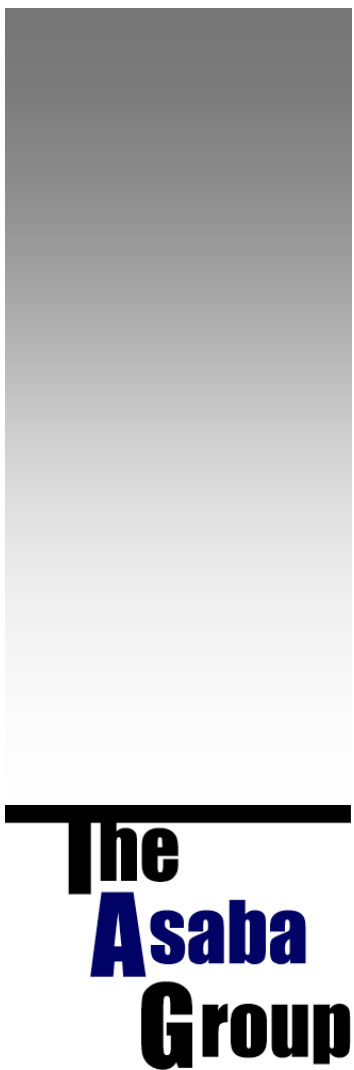
- Testing Raw Materials
- Components
- Systems and Modules
- Prototypes

Most companies are under \$100 Million in revenues

Full-service engineering and design firms offer testing services

- Much larger in revenues

Minority Suppliers Should Capitalize On This Opportunity



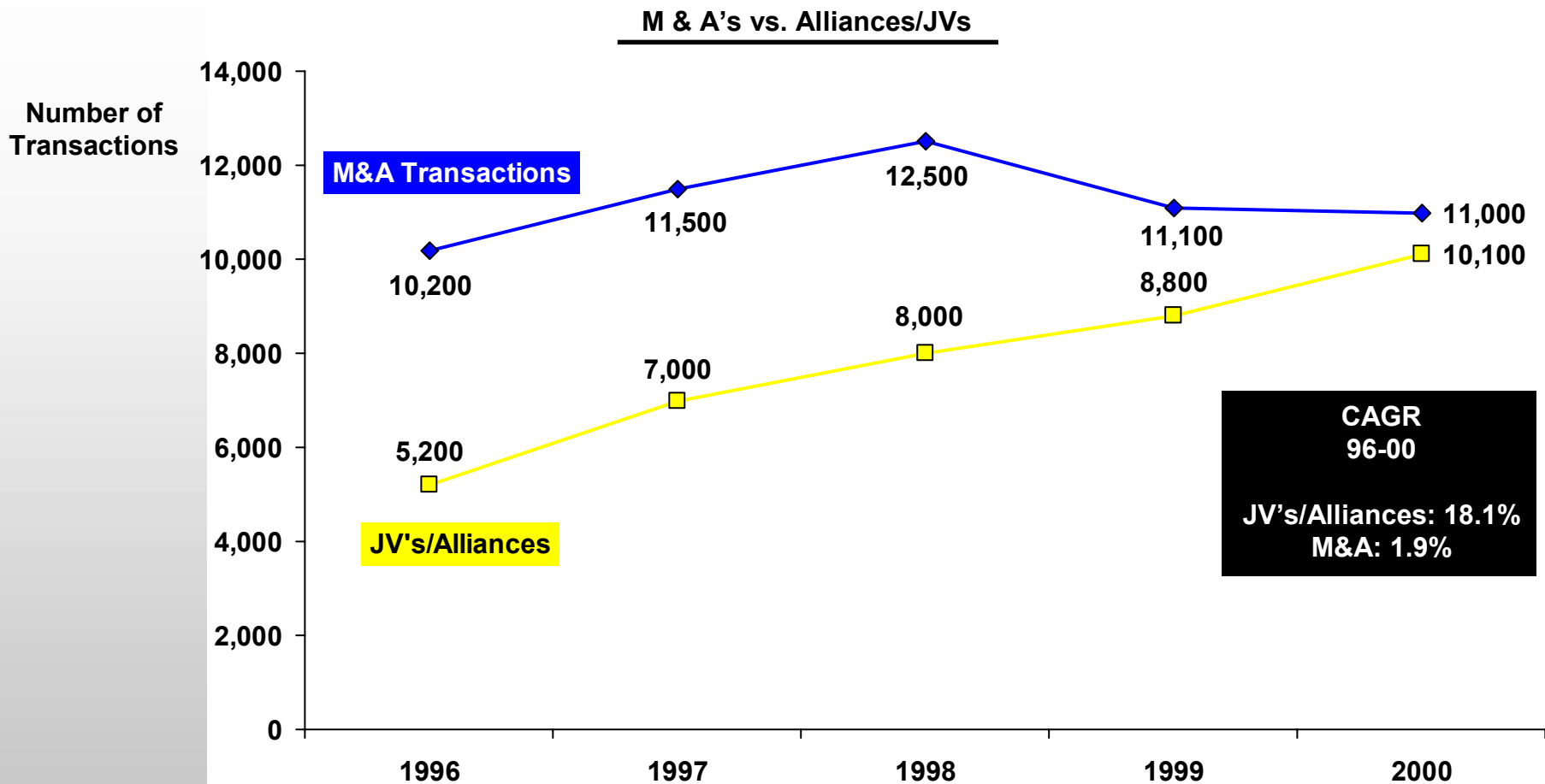
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STRATEGY AND BUSINESS IMPROVEMENT CONSULTING

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Joint Ventures And Alliances Are Common Growth Vehicles

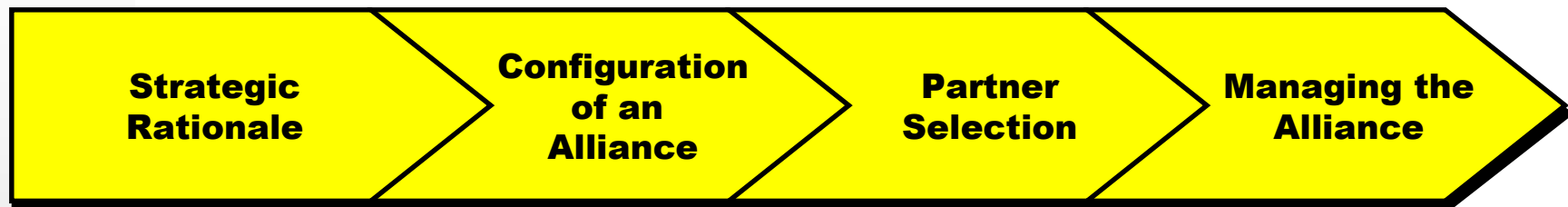
Similar To Mergers And Acquisitions



Minority Suppliers Must Leverage Alliances To Grow And Achieve Tier One Status

An Approach To Develop Alliances

The process has four major dimensions. They are:



Careful attention must be paid to each dimension to give an alliance the proper foundation for success

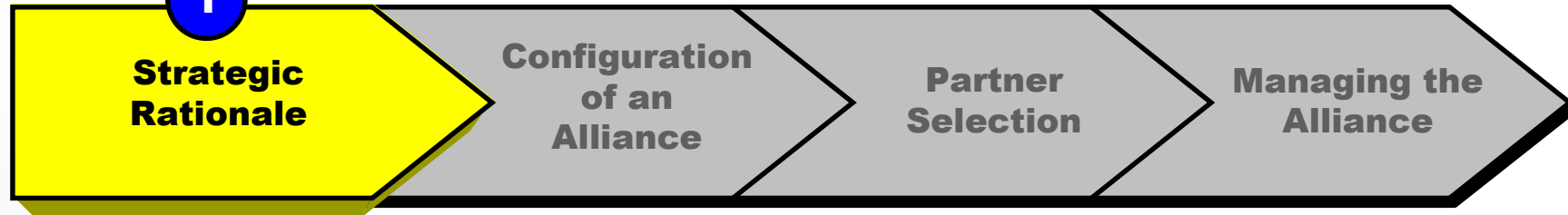
Strategic alliance needs to be firmly grounded in a clear strategic understanding of current capabilities and those needed in the future to be successful

Alliance planning process that can establish objectives and evaluate alternatives

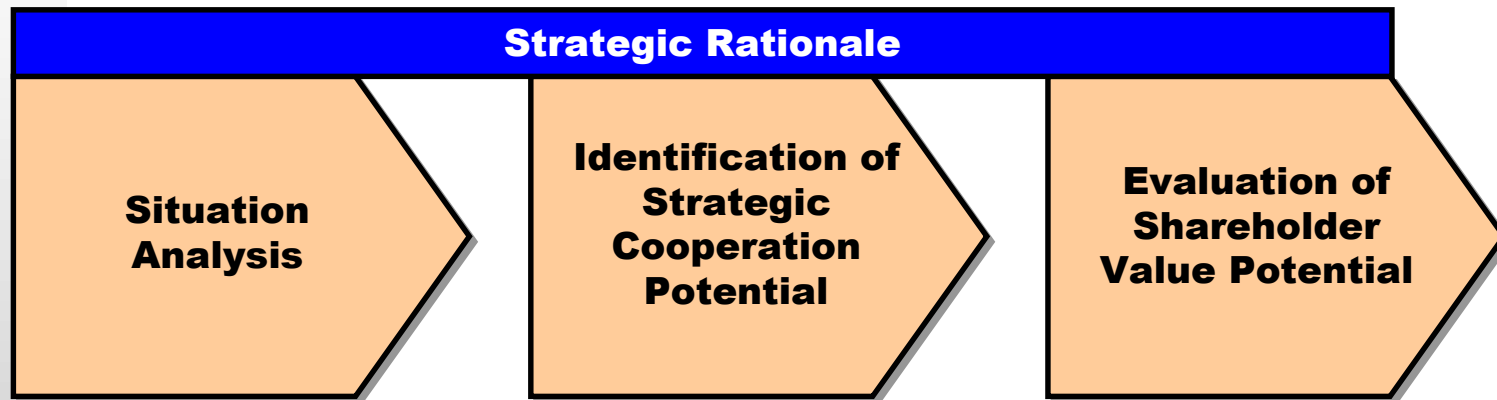
Alliance Planning Process

Dimension #1 — Strategic Rationale

1



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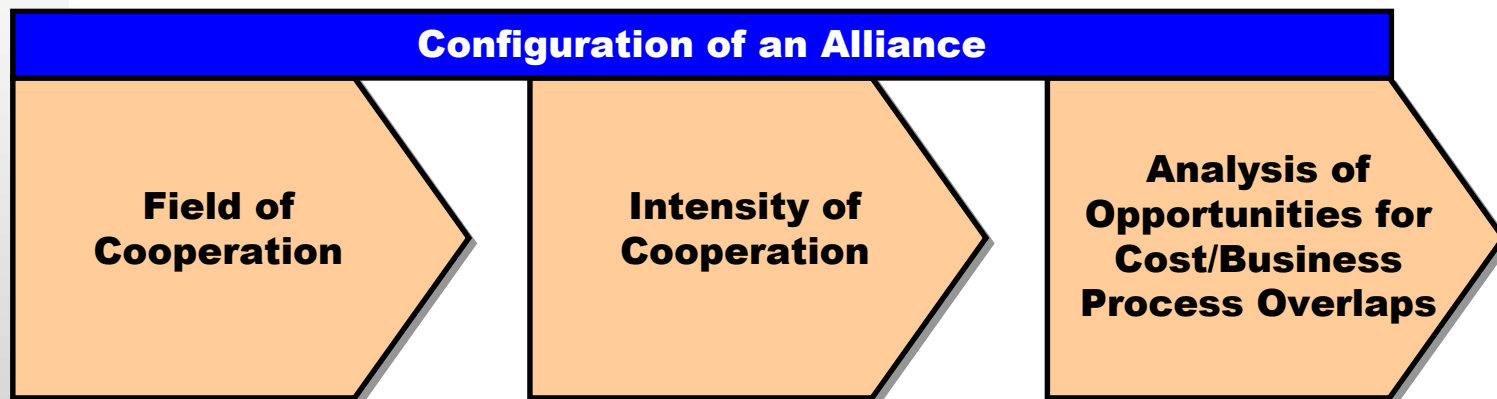
- Globalization
- Deregulation
- New markets
- Developments in technology
- Changing Demographics
- New entrants

- Internal trends
- Own strengths
- Own weaknesses
- Time as a competitive weapon

- Contribution to free cash flow
- Value drivers

Alliance Planning Process

Dimension #2 — Configuration of an Alliance



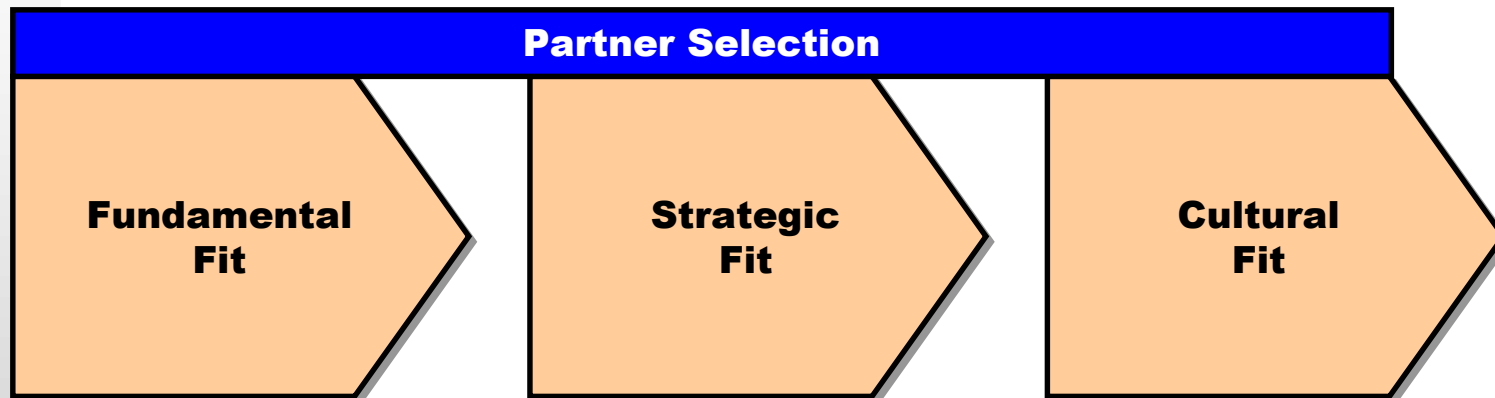
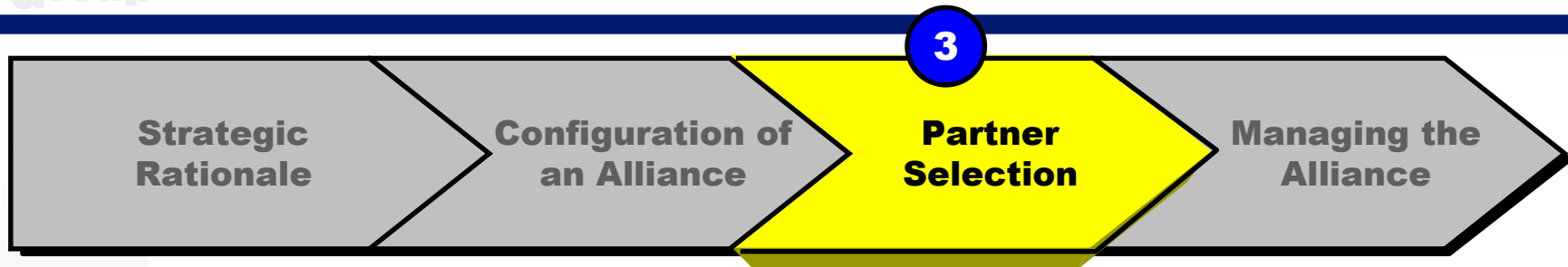
- Horizontal, vertical or diagonal direction
- Research and development, marketing and sales, production and logistics, procurement, or recycling

- Time horizon
- Resource allocation
- Degree of formalization

- Systems
- Processes
- Products/services
- Competencies
- Brands

Alliance Planning Process

Dimension #3 — Partner Selection



- Common intention
- Compatible visions
- Balanced positions of power
- Mutual gains
- Controlled risks
- Potential for increasing shareholder value

- Harmony of business plans
- Common specification of appropriate configuration
- Similar planning horizons
- Global market fit

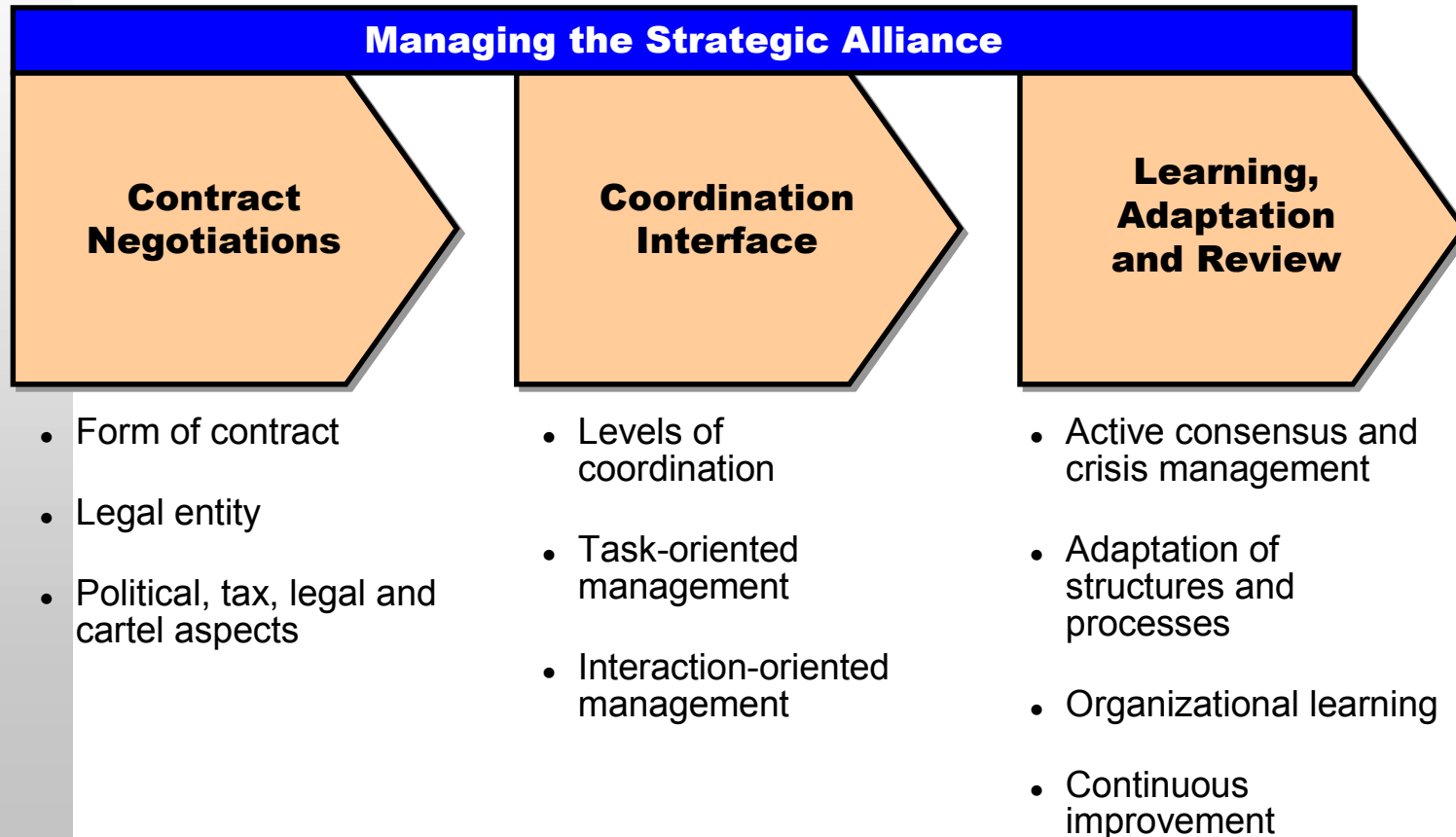
- Assimilation
- Transfer
- Resistance
- Decision processes
- Entrepreneurial

Alliance Planning Process

Dimension #4 — Managing the Alliance

4

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Keys To Success

Build Knowledge

The up-front analysis prior to negotiations lays the groundwork for building a solid base:

- Assessing mutual needs
- Establishing share risk
- Developing common goals in an environment of trust between potential partners

Gain Experience

Enabler of success is a function of people selected by each organization. The more experienced and capable, the greater likelihood of success.

Leverage Credibility and Success

Manage the partnering process as a portfolio leverages the knowledge, learning and key competencies developed from prior experiences. Leverage it.

Framework To Guide Alliance/JV/M&A Decisions

Growth Options	Primary Business Rationale	Minority Supplier Options			
		Commodity/ Processing Supplier	Sub-System/ Sub-Module Assembly	Component/ Technology Specialist	Module Developer/ Solutions
Low-Cost Commodity Producer	<ul style="list-style-type: none"> Economies of Scale 	<ul style="list-style-type: none"> Acquisitions/ Roll ups 	<ul style="list-style-type: none"> --- 	<ul style="list-style-type: none"> --- 	<ul style="list-style-type: none"> ---
New Growth	<ul style="list-style-type: none"> Geographic Markets 	<ul style="list-style-type: none"> Acquisition 	<ul style="list-style-type: none"> Joint venture Acquisition 	<ul style="list-style-type: none"> Joint venture 	<ul style="list-style-type: none"> Joint venture
	<ul style="list-style-type: none"> New Products/ Categories 	<ul style="list-style-type: none"> --- 	<ul style="list-style-type: none"> Joint venture 	<ul style="list-style-type: none"> Acquisition 	<ul style="list-style-type: none"> Acquisition
Solutions Provider	<ul style="list-style-type: none"> New capabilities 	<ul style="list-style-type: none"> --- 	<ul style="list-style-type: none"> 3rd party sourcing alliance 	<ul style="list-style-type: none"> --- 	<ul style="list-style-type: none"> Joint venture Shared resources
	<ul style="list-style-type: none"> New technologies New applications 	<ul style="list-style-type: none"> --- 	<ul style="list-style-type: none"> --- 	<ul style="list-style-type: none"> Strategic Investor 	<ul style="list-style-type: none"> Strategic Investor

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