



FOCUS ON

Faster, Farther: The Components Sector Shifts Gears

Produced by the
Economic Analysis
and Research

EXECUTIVE SUMMARY

- **Between 2006 and 2016, the "production geography" of the world automotive industry changed:** ten years ago, Europe was the leading manufacturer of automobiles with three of every ten cars, while almost six of every ten were produced in the EU and North America combined. In 2015, the "Made in EU" declined to two cars out of ten (four of 10 with the USA), while more than one car in five was being built in China.
- The automobile and components industry **suffers from a lack of international scale and from competition that extends across at least 3-4 continents:** the Italian share of world exports is still between 1% and 4%, depending on the segment.
- While **automobile exports have shifted to areas with stronger demand** (the EU share of sales has declined from 80% to 54% in ten years), **the same is not true of the supply chain**, though still ninth-ranked worldwide with € 4.8 billion in net component exports.
- **It is important to support Italian sector** companies in confronting complex internationalization processes and entering the global supply chains, **especially in more-distant, higher-potential markets.**
- The forecasts for future component sales indicate that **12 markets of opportunity will generate over € 75 billion in additional sales in 2021:** a strong surge, especially in various Asian countries.



THE AUTOMOTIVE BOARD GAME: A FEW GOOD BATTLES, BUT THE WAR IS WON ELSEWHERE

"Well, in our country" said Alice, still panting a little, "you'd generally get to somewhere else - if you ran very fast for a long time as we've been doing." "A slow sort of country!" said the Queen. "Now here you see it takes all the running you can do to keep in the same place. If you want to get somewhere else, you must run at least twice as fast as that!"

This bit of dialogue between Alice and the Queen of Hearts in Lewis Carroll's book was cited in the presentation *Confessions of a Capital Junkie* by FCA CEO Marchionne in April 2015. On that occasion, he pointed out how the minimum requirements for the sector have changed radically over time, and that R&D investments are being consumed by this industry much faster than by other machinery sectors, requiring greater courage in industrial synergies and consolidation among players with vision. As we shall see, **our national automotive industry is present today in many geographical areas**, though with a smaller market share than in the past, and **exports are growing rapidly**. The component sector, on the other hand, **is still focused on the European markets** (80% of exports in the first half of 2016) **in a context of intense innovation of product** (fuel systems, bodywork, technology) **and purpose** (vehicle ownership and guidance, vehicle monitoring and efficiency, and continuous maintenance) that should promote synergies with industrial partners and a "break" with the Italian car and its historical outlets.

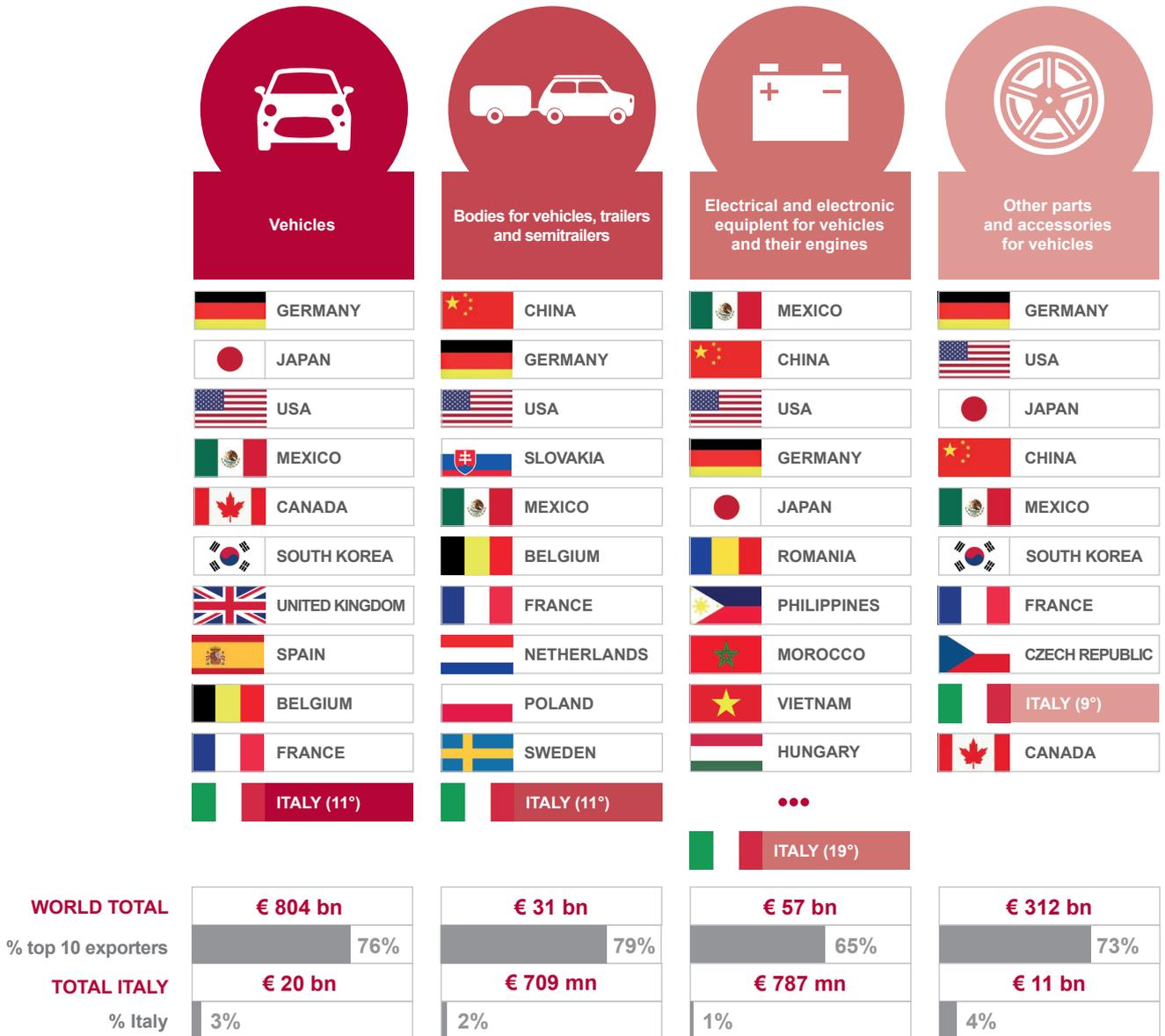
The automotive industry is growing globally, and Italian exports have followed in its wake, particularly in the advanced and "equipped" emerging markets⁰¹. Italy, however, remains the European country with the heaviest deficit in terms of domestic motor vehicle production: in 2015 the number of vehicles registered exceeded those produced by 700,000. Our ability to export is still limited, therefore, even considering the supranational structure of the industry and the importance of the continental networks for the production and purchase of motor vehicles. Germany, which manufactures in many countries, is a phenomenon with six million cars produced domestically and 3.2 million cars purchased, while in Italy the number of cars produced in 2015 did not exceed one million (990,000) against almost 1.6 million sold. This is well below the level of 2 million cars "Fabriqué en France", the 2.7 million cars "Fabricado en España" and the 1.2 million automobiles "Vyrobeno v České republice"⁰².

Italy ranks 11th worldwide in the exports of cars and bodies with a share, respectively, of 3 and 2% (while Germany holds the 21 and 17%), and 19th in electrical equipment for the sector: though not a giant, Italy can continue to play a major role in international trade. **However, our country ranks 9th worldwide in the export of components where 4 products out of 100 are Made in Italy while 16 are Made in Germany** (Table 1).

⁰¹ Markets that despite global uncertainties are still growing vigorously with the capacity to contract new debt at sustainable conditions and less dependent on commodities.

⁰² ACEA data.

TABLE 1: Principal global exporting countries of motor vehicles and components (2015; value of exports from these markets and relative share of total automotive exports)

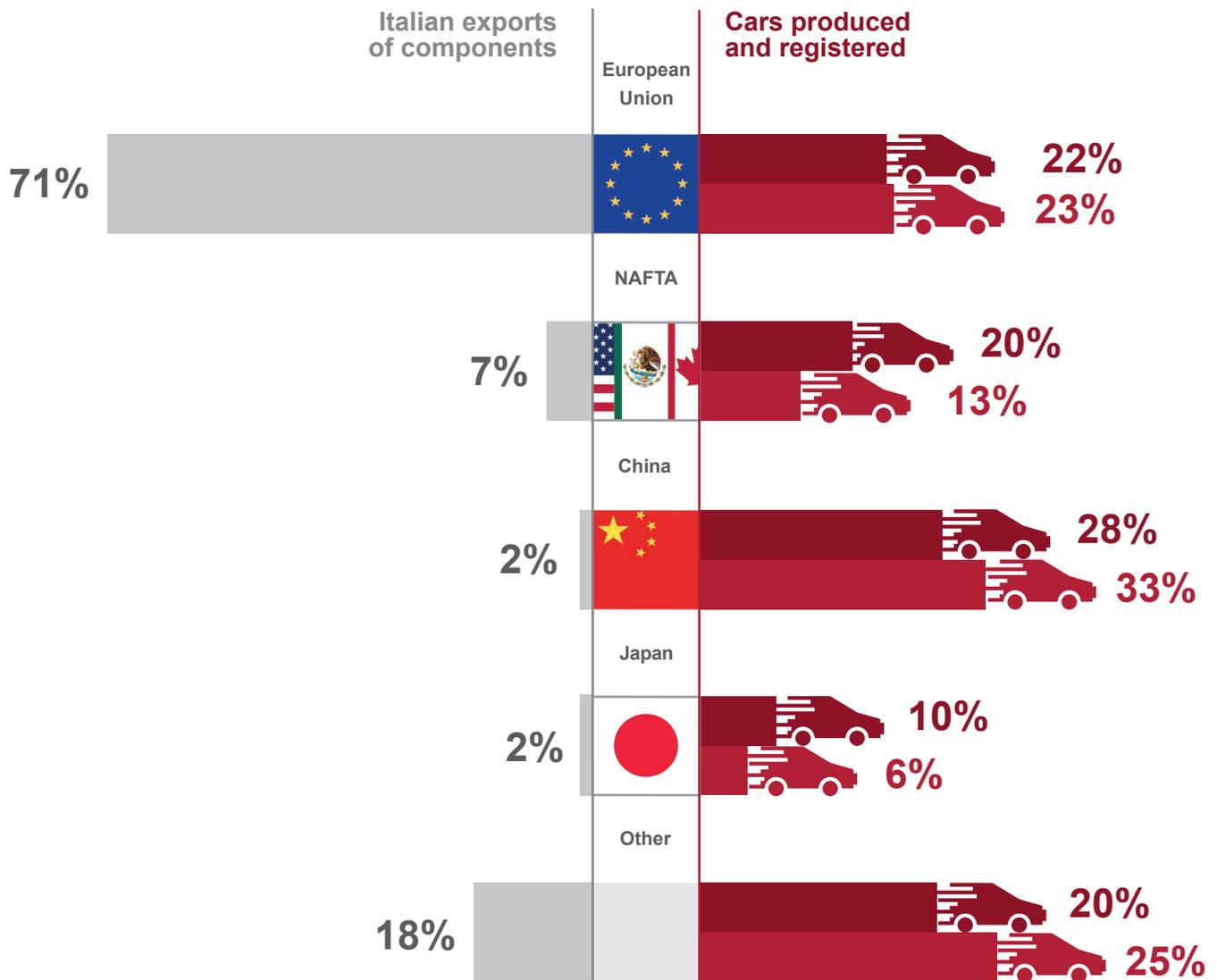


Source: SACE processing ICE data

The greatest potential for national production lies in components: despite our good placement, in fact, **the importing markets are not those that produce the most vehicles nor those with the largest number of registered vehicles**. Our exporters apparently need to strengthen their positions in North America, from Canada to Mexico, with an eye on the intentions of President Trump regarding the NAFTA agreement, inserting themselves into the vehicle assembly chain. **Considering the success the component segment could score abroad, however, it must be supported to find a place in the production chains of new markets**. Meanwhile, in fact, auto production has shifted elsewhere: while ten years ago Europe led the world in automobile production with three cars in ten, and

six in ten were produced in the EU and North America, EU-made cars had declined to 2 cars in ten in 2015 (four in ten with the USA), while more than one car in five was built in China (Figure 1).

FIGURE 1: Distribution of production and registration of motor vehicles and Italian exports of components in the first half of 2016



Sources: SACE processing OICA and Anfia/Istat data

The demand for vehicles and parts and accessories must guide the internationalization decisions of our companies, which in many cases are locked into models of the past. The number of countries behind the USA and Germany in automotive imports suggests that there are many markets where Italian exporters could find opportunity (Table 2).

TABLE 2: Countries of opportunity and ranking for Italian exports (2015)

Vehicles		Bodies for vehicles, trailers and semi-trailers		Electrical and electronic equipment for vehicles and their engines		Other parts and accessories for vehicles	
Countries of highest demand	Ranking for Italian exports	Countries of highest demand	Ranking for Italian exports	Countries of highest demand	Ranking for Italian exports	Countries of highest demand	Ranking for Italian exports
 USA	1	 USA	14	 USA	8	 USA	5
 GERMANY	3	 GERMANY	2	 GERMANY	1	 GERMANY	1
 UNITED KINGDOM	4	 CANADA	>20	 JAPAN	>20	 MEXICO	12
 CHINA	11	 NETHERLANDS	6	 MEXICO	>20	 CHINA	20
 CANADA	17	 UNITED KINGDOM	3	 CANADA	>20	 CANADA	>20
 FRANCE	2	 FRANCE	2	 UNITED KINGDOM	5	 SPAIN	3
 BELGIUM	9	 BELGIUM	8	 SPAIN	4	 UNITED KINGDOM	4
 ITALY	-	 POLAND	5	 FRANCE	2	 FRANCE	2
 SPAIN	5	 MEXICO	>20	 SOUTH KOREA	>20	 CZECH REPUBLIC	9
 AUSTRALIA	14	 RUSSIA	15	 CHINA	16	 ITALY	-

Source: SACE processing ICE data

FROM "PANDA-LAND" TO "BREMBO-LAND": REGAINING LOST GROUND

From 2006 to 2016, our country was a net importer of cars, though less than in the past, and a net exporter of parts and components (and motorcycles). The balance of trade in vehicles reflects a decrease in imports, which dropped from € 30.4 billion to € 24.5 billion, and an increase in exports, from € 13.5 billion to almost € 20 billion.



Motor vehicle exports are more diversified now that ten years ago: in 2015 the EU share of sales dropped to 54% versus 80% ten years earlier, due to the force of the USA market but also to the transformation taking place in traditional supply markets (Brazil, China, Japan, United Kingdom, Turkey). Many of these are fertile ground for low-price vehicles equipped with small, highly-efficient engines. These countries are innovating their range of vehicles and, in some cases, have become recognized platforms for the assembly and resale of cars to the high-income markets.

Exports of parts, on the other hand, are still concentrated in the European markets, which represent more than 70% of the total, are sharply declining in a few areas of more recent investment (contrary to cars), and are adapting interestingly to the emerging markets. In the period 2006-2015, the balance of trade for this segment showed a few marked trends:

- it was stable with the reference markets (Germany, France, United Kingdom, Spain);
- it was better with Brazil (from 159 to 426 million) and Mexico (from 26 to 183 million);
- it became positive with India (from a negative 29 to a positive 38 million);
- it stayed positive with the USA (from 701 million to 141 million) though dropping rapidly, due in part to the increased Italian local presence, which facilitates conformity to local standards and closer positioning to the customers, with Turkey (from 293 to 228 million), due to the current increase in production capacity, and with South Korea (from 37 to 4 million);
- it became negative with Poland (from a positive 77 million to a negative 170 million);
- it deteriorated with China (from 16 to 208 million) and the rest of the Far East with few exceptions (Japan improved from 5 a 26 million).

We improved our positioning in a few markets, but we are still absent from important areas for the industry, such as the Far East and North America.

We are still net exporters of parts and accessories with Germany, Spain, Turkey, Poland, and the Czech Republic, all European markets. In ten years, we became net exporters only to Brazil, where the industry is experiencing a crisis (the number of cars produced there declined in two years from 3 million to less than 2 million). In the past ten years, Italy's balance of trade has been worsening precisely with those countries with the greatest growth potential: USA, China, Canada, Chile, Mexico, and Vietnam, as well as a few Middle Eastern and African countries.

“GO EAST!” TO CHANGE PACE

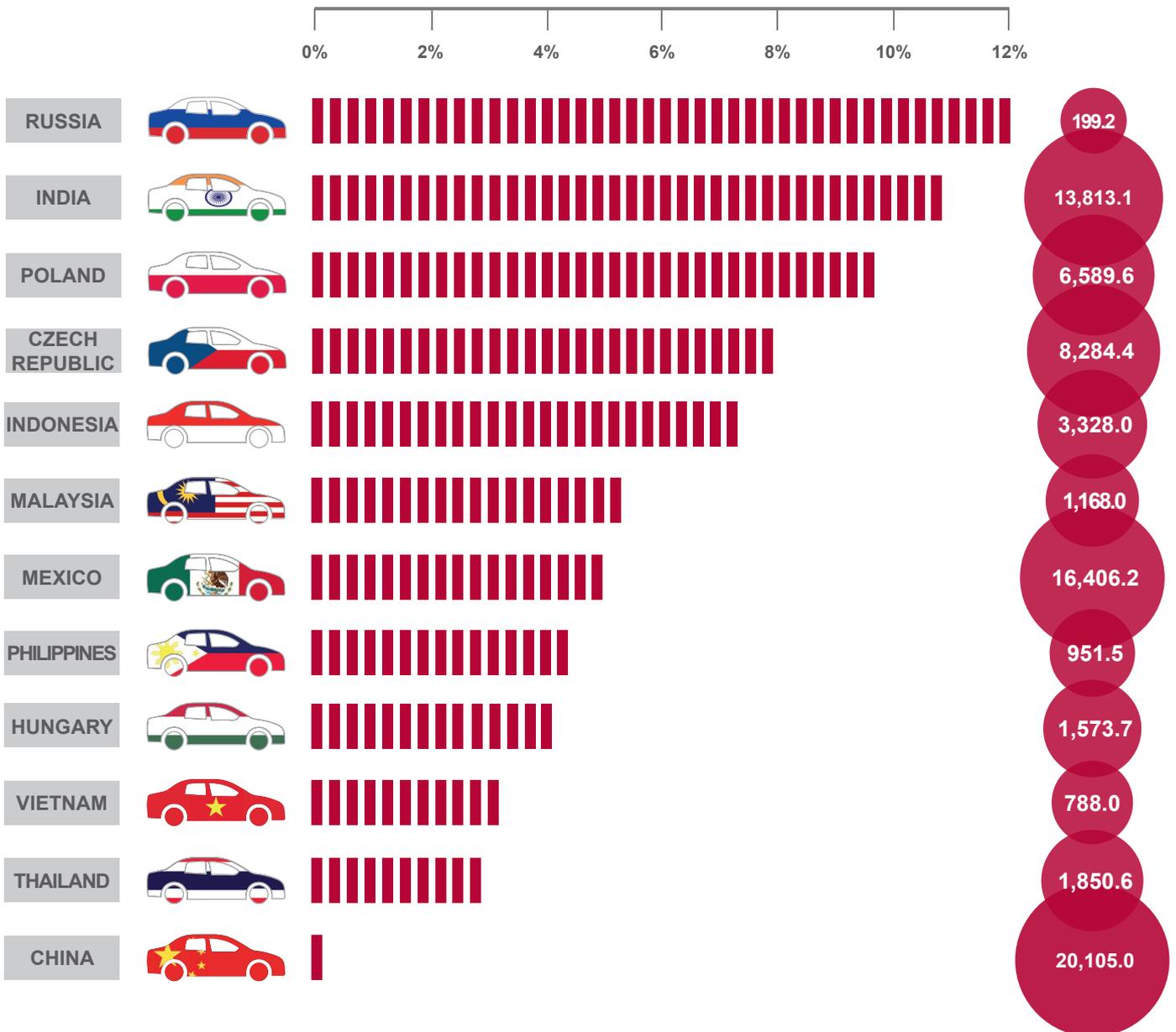
Should we concentrate on countries that traditionally dominate the market, although they are currently producing less, or approach other markets that over time have carved out a key role in the auto industry and are now the largest purchasers of components⁰³? **Projections on the future sales of auto parts indicate strong growth in various emerging countries, many of them in Asia:** these are the markets where demand is currently strong and may be the targets of internationalization (figure 2) with the right forms of risk protection.

⁰³ In developing this study, we decided to focus on the components segment, as it gives indications to a larger number of companies, mostly small ones.

We should note that the values vary greatly from one country to another: from € 252 million for Russia to € 451 billion for China. Even a slower growth rate still offers significant opportunities if applied to a higher value. The additional expected sales will be in China (almost € 20 billion), Mexico (16) and India (almost 14).

FIGURE 2: Projected average annual growth expected and values of sales of auto components (2017-2021)

Additional sales in 5 years (€ mn)



Source: SACE processing of IHS data



These 12 markets of opportunity will generate additional sales of € 75 billion in auto components in 2020.

Not all are easy to approach due to various short-term contingencies (the case of Russia). In addition to China and Mexico, various ASEAN members are present, an area of robust growth with interesting demographics and millions of inhabitants with rising purchasing power. These countries are not easy to approach, given the presence of international competitors, physical distance, and the small size of our exporting companies: they require well-defined, developed strategies, the selection of reliable partners in Italy and abroad, and sufficient financing to complete the investment. In addition to the most promising economy, India, attention should also be focused on nearby countries like the Czech Republic (with over € 8 billion in expected additional sales).

CONCLUSIONS

The complex game that is the automotive industry worldwide is conditioning our exports of vehicles and parts. Components are necessarily included and must seek out demand where it exists. The demand for products certainly comes from major international players such as **China** and **Mexico** and from fast-growing markets like **India**, but also from smaller countries with big prospects such as **Vietnam** and the **Czech Republic**. Seizing these opportunities requires complex strategies, given the fierce competition and the risks and difficulties associated with approaching certain markets. It might be necessary, for example, to offer financial support to the counterparty or consider investment abroad (with the guarantees of SACE and the equity support of Simest). The various **companies that have chosen SACE** to protect their investments include Geico S.p.A., a leader in automotive painting installations, which is continuing its internationalization process in **Brazil**. Are the markets mentioned above the only ones that can be approached? Certainly not, but they are the principal ones. There are also many success stories in other markets, such as that of GLM S.r.l., a major producer of muffler components, to which SACE has provided a financial guarantee to support investment in **Serbia**. It's not enough to run twice as fast: reaching the finish line requires a joint effort.

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