2014 GLOBAL STUDY ON OEM-SUPPLIER RELATIONS

Quality of Relations Deteriorates in 2014 as OEMs Increase Pressure on Suppliers to Contain Purchasing Costs, According to IHS Automotive

LONDON, October 2014 – Heightened friction between OEMs and suppliers on cost reduction matters is the main factor behind the deterioration of relations between automakers and suppliers globally in 2014, according to suppliers who took part in the annual Global OEM-Supplier Relations Study conducted by IHS Automotive. The unique global survey allows automotive suppliers to rate carmakers on a variety of matters, including technology sourcing, profit-impacting factors, quality management and intellectual property protection matters.

2014 study highlights include:

• Nearly 75 percent of carmakers have received lower ratings than in 2013, with an average SuRe index rating reduction of 2.8 percent. Profit potential ratings were down by 5.4 percent on average in 2014 vs. 2013.

• Toyota’s marginal improvement in 2014 is enough to secure the Japanese carmaker the first position in the SuRe index ranking, closely followed by BMW, which was also rated second in 2013. Despite occupying the top positions, both BMW’s and Toyota’s ratings remain significantly down compared to 2006 and 2007 highs (712 and 697 in the SuRe index scale respectively), confirming a shift in the way they handle relations with suppliers.

• Ratings for Hyundai, Kia and Volkswagen (and its controlled brands) suggest suppliers are less confident about their opportunities to win more business with these carmakers in the future, possibly linked to reduced growth prospects.

• OEMs pushing the boundaries of cost reduction with several suppliers highlighting the return to unwelcome practices, such as annual price reduction targets, which they deem unsustainable.

• Jaguar Land Rover named Most Trustworthy. Jaguar Land Rover, PSA and Chinese carmakers, Great Wall in particular, are among the winners of this year’s study, all for different reasons. With a 16 percent improvement in 2014, Jaguar Land Rover establishes itself as the most trustworthy OEM.

• OEMs’ Lukewarm Response to Global Recalls and Quality Management Misalignments. One supplier put it bluntly: “it’s all about cost - Is Purchasing or Engineering leading quality?”.

About the SuRe index
IHS Automotive developed its SuRe index based on an annual survey of the automotive supply industry which started in 2005. From its inception, the survey has included participation of more than 1,000 senior to middle managers working at automotive suppliers and directly interfacing with personnel at various OEMs. In 2014, nearly half (47 percent) of the 281 respondents were based in North America, 39 percent in Europe, 13 percent in Asia and one percent in South America. The 2014 study includes the views of representatives of 51 of the world’s top 100 automotive suppliers.
A variety of suppliers’ organizational functions are surveyed in order to include the different perspectives on the business relations and practices of OEMs. Respondents are active in marketing and sales, engineering, program management, research and development, quality and manufacturing. The 29 questions are organized under five categories: Profit Potential, Organization, Trust, Pursuit of Excellence and Outlook.

The questions cover the different phases of interaction, from request for quotation through development to warranty liability management. These result in a numeric value, ranging from 0 to 1,000. A SuRe index higher than 650 is considered a satisfactory result, while anything below 450 indicates the state of relations is poor.

Overall index ratings have decreased on average by 2.6 percent on average since 2013. The SuRe index is based on automotive suppliers’ ratings of 29 criteria, allocated across five categories: Profit Potential, Organization and Outlook, Trust, Pursuit of Excellence. In 2014, the Profit Potential category of the index has recorded the biggest average drop in ratings year-over-year (5.4 percent) with suppliers citing lowered profit opportunities due to OEMs aggressive cost reduction plans and increased cost liabilities.

With few exceptions, even the best performing carmakers have become more stringent on controlling costs in 2014, signalling a general shift for the OEMs towards greater cost focus and more aggressive ways to capitalize on their negotiation leverage with suppliers. For example, Jaguar Land Rover, which seems to offer the highest profit opportunity for suppliers based on the metrics of the study, has seen its Profit Potential rating drop by nearly two percent vs. 2013.

Ratings are based on the SuRe (Supplier Relationship) index scale, a comprehensive performance metric of the quality of relationship between suppliers and OEMs defined by IHS Automotive.

### OEMs pushing the boundaries of cost reduction

Several suppliers have highlighted the return to unwelcome practices, such as setting annual price reduction targets, which they deem unsustainable. While the standard annual price reduction in the industry hovers around two to three percent, it is not uncommon for OEMs to request cuts of 5 percent year-over-year, and in some extreme cases, as much as 10 percent. Suppliers seem to accept the notion that they have to find innovative ways to generate savings on a year-over-year basis, however they find it difficult to accept that they receive little or no support from the OEMs in doing so. This lack of support often results in strained relations between the two parties, therefore resulting in lower ratings in the IHS Automotive survey.

The survey results also show OEMs seem also keen to extract more savings from suppliers. However, savings are not always being pursued with a collaborative spirit. Expanded product liability guarantees and a greater financial burden in the event of recalls are among the other concerns that are impacting suppliers’ perception of their Profit Potential with the OEMs.

### Outlook and Organization

Other drivers which are also pushing average ratings down include a more negative assessment of long-term prospects of some OEMs, as measured by the Outlook category of the index, and less supportive vendor-facing organizations, based on responses in the Organization category. Suppliers are less confident than in the past about their opportunities to expand their business with Hyundai and Volkswagen (and its related companies), in particular.
IHS forecasts suggest that compounded growth for these two manufacturing groups will drop from double digit figures seen in 2009-2013 to low single digits in 2014-2018, corroborating the idea that the bonanza years for suppliers exposed to these customers could be soon drawing to an end.

Toyota returns to the top of the ranking, with a SuRe index rating of 627, thanks to a marginal improvement of relations with its supply base, largely driven by a more trustworthy organization than in previous editions of the study and outstanding results in Europe, where suppliers indicate it is the customer most yearning to excel particularly in quality and technology. BMW ranks the same as in 2013 with the same strong performance recorded in previous years, and remains the suppliers’ favourite premium carmaker to work with. While BMW’s final global rating might not have changed when compared to last year IHS Automotive has recorded a marked improvement of SuRe ratings (632, +5 percent year-over-year) in North America, where suppliers are expecting significantly larger opportunities as the German carmaker expands its footprint in that region, while in its European production hub its ratings have dropped from 649 to 626 (-3.5 percent), driven by lower marks in the Organization and Long-term Outlook categories. BMW outpaces Toyota among small and medium sized suppliers (up to $1 billion USD) enterprises, while Toyota is the benchmark for supplier relation in 2014 among companies with automotive sales in excess of USD $1 billion.

**Jaguar Land Rover named Most Trustworthy**

Jaguar Land Rover, PSA and Chinese carmakers, Great Wall in particular, are among the winners of this year’s study, all for different reasons. With a 16 percent improvement in 2014, Jaguar Land Rover establishes itself as the most trustworthy OEM assessed in the study this year. As an example of their efforts, Jaguar Land Rover offers a more comprehensive protection of suppliers’ intellectual property. It also is still rated among those offering the greatest profit potential to suppliers, even though it has declined slightly since last year.

**OEMs’ Lukewarm Response to Global Recalls and Quality Management Misalignments**

Recent recall fears do not seem to have translated in greater attention to in-bound quality, as suppliers indicated that all carmakers, except Subaru and a few Chinese manufacturers, have actually become more lenient with regard to quality, in terms of PPM levels, testing, and product or process validation. Even best-in-class carmaker BMW seems to have backtracked on this point compared to last year, with lower ratings of quality demands.
According to suppliers surveyed, the cost focus is also having an impact on quality. For most volume carmakers such as Volkswagen, FiatChrysler, Ford, GM and Renault, cost pressures on the supply base are increasingly overriding quality performance that these OEMs require of their suppliers, however results vary distinctly from the different purchasing sectors. One supplier put it bluntly: “it's all about cost - Is Purchasing or Engineering leading quality?

**OEMs lack consistency in their innovation sourcing strategy**

OEMs' R&D budgets get stretched in several directions by the increasing complexity and variety of new automotive technologies, and as a result, tough decisions need to be made about where to invest. Suppliers have therefore expanded their role as innovators and contribute an increasing share of the innovation that goes in today's cars as they take on additional R&D activities. Accessing supplier innovation is and will be increasingly important for the OEM success in the marketplace. The 2014 study shows that some OEMs have understood this lesson better than others.
Suppliers' regional biases emerge
Suppliers reported they favor working with different customers in the various regions. For example, Audi is considered the best carmaker to work with in Asia (primarily China) with a SuRe index rating of 697 in 2014, but seems to maintain more adversarial supplier relationships in Europe, (SuRe rating 569) and North America (532). On the other hand, Toyota achieves consistently better ratings in Europe than in other regions, as its Pursuit of Excellence ratings are markedly higher than in North America and Asia.

Few OEMs can boast having similar SuRe index ratings in the different regions, which indicates a consistent approach in managing their suppliers on a global basis. Hyundai, Mercedes and BMW are certainly among these, while Fiat and Audi record more dispersed readings across the three main regions assessed in this study.

Chinese OEMs gaining suppliers' trust
Chinese OEMs continue to lag behind other OEMs in the ranking and most remain in critical territory in the SuRe index scale, with ratings lower than 450. However some positive momentum emerges from this year's study as suppliers are targeting more business opportunities with Chinese carmakers and these OEMs' organizations are becoming more trustworthy in the eyes of suppliers. Ratings in the Trust category for Chinese carmakers have advanced on average by six percent compared to 2013.

### NORTH AMERICA

<table>
<thead>
<tr>
<th>Rank</th>
<th>2014</th>
<th>2013</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>SuRe Index Rating</td>
<td>SuRe Index Rating</td>
</tr>
<tr>
<td>1st</td>
<td>BMW 633</td>
<td>TOYOTA 624</td>
</tr>
<tr>
<td>2nd</td>
<td>TOYOTA 632</td>
<td>MERCEDES 613</td>
</tr>
<tr>
<td>3rd</td>
<td>MERCEDES 612</td>
<td>AUDI 610</td>
</tr>
</tbody>
</table>

### EUROPE

<table>
<thead>
<tr>
<th>Rank</th>
<th>2014</th>
<th>2013</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>SuRe Index Rating</td>
<td>SuRe Index Rating</td>
</tr>
<tr>
<td>1st</td>
<td>TOYOTA 646</td>
<td>BMW 649</td>
</tr>
<tr>
<td>2nd</td>
<td>BMW 627</td>
<td>PORSCHE 634</td>
</tr>
<tr>
<td>3rd</td>
<td>MERCEDES 625</td>
<td>TOYOTA 632</td>
</tr>
</tbody>
</table>
### PROFIT POTENTIAL

Areas Assessed
- Price reduction
- Reward cost-saving ideas
- Management of raw material price adjustments
- Payment of development costs
- Tooling cost reimbursement
- Satisfactory return on investments
- Payment terms
- Support in achieving cost reductions
- Quality and stability volume planning

### ORGANISATION

Areas Assessed
- Technical Competence
- Preparational model launch
- Quality of communication
- Support in improving quality
- Management of Engineering Change orders
- Time-consumingess of contract negotiation
- Redesign required

### OUTLOOK

Areas Assessed
- Attractiveness
- Long-term prospects
- Opportunities for new or increased business
- Openness in accepting new suppliers
ABOUT IHS AUTOMOTIVE

IHS Automotive offers clients the most comprehensive content and deepest expertise and insight on the automotive industry available anywhere in the world today. With the acquisition of Polk (in 2013), we provide insight across the entire automotive value chain, from product inception, to sales and marketing, to aftermarket solutions. That's why 92 of the world's top 100 suppliers and 20 of the largest automotive manufacturers rely on IHS Automotive's solutions to plan, execute, measure and optimize activities. No other source provides a more complete picture of the automotive industry.

IHS AUTOMOTIVE driven by POLK

For media inquiries, Please contact

US | Michelle Culver
Email: michelle.culver@ihs.com

EMEA | Kat Kosior
Email: katarzyna.kosior@ihs.com

APAC | Danny Cheung
Email: danny.cheung@ihs.com

Areas Assessed
• Shift of business to cheaper supplier
• Protection of supplier's intellectual property
• Keeping agreements on price

Areas Assessed
• Demands to achieve high quality
• Demands for best product technology
• Demands for better logistics
• Demands for product liability guarantees
• Demands test and validation
• Responsiveness to supplier innovation