How the intervention of governments changed the course of the worldwide automobile industry

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Thank you, and good afternoon, ladies and gentlemen.

It is always a pleasure for me to return to Brazil, where I was born and where I worked for several years early in my career in the automotive industry. Many formative events in my life are deeply rooted in this country, and I maintain close ties to this day.

I also follow events and developments in Brazil closely because Renault and Nissan have manufacturing operations and extensive dealer networks here. We offer a range of attractive products, and our ambition is to grow our presence even further to meet our local customers' needs.

Today, however, the theme of my remarks will go beyond the borders of Brazil to a global stage. In keeping with the focus of this forum, I want to talk about the financial meltdown of 2008 and 2009… about how governments intervened during this time of crisis… and about how those interventions have changed the course of the global automobile industry for years to come.

Some say that the financial and economic turmoil we have experienced over the past 18 months is akin to the Great Depression of the 1930s. That may be true, but I remind you that the auto industry was still in its infancy at the start of the twentieth century. So the recent financial crisis is, without doubt, the worst that has ever occurred in our industry. We had no playbook to guide us through it. We had no pattern from the past because much of what we have been experiencing has no precedent.

So let me take you back and describe how we saw the disaster unfold from our perspective inside one of the world's largest industries.

■ Description of financial crisis

I will start in 2008, even though experts say the seeds for the crisis were planted in the U.S. housing industry in 2007.

At the start of 2008, we started the year with optimism and expectations of growth. Serious trouble began in mid-September with the crumbling of the financial system in the United States, and soon the entire international banking system was thrown into a downward spiral. The credit markets became virtually frozen. This was a severe blow to all automakers

because we are big consumers of cash. We are big employers (350,000 employees for the Alliance). We are huge investors (6 to 7 billion dollars per year). We need cash for our supply chain (one to two months of revenue, 20 billion dollars) and to run our industrial operations.

We also need cash for our auto financing operations. Two-thirds of car buyers rely on loans to buy a new car. Buying a car is the second-largest purchase in household budgets after housing.

So when the credit markets froze, the impact in our showrooms was dramatic – car sales screeched to a halt. Global vehicle sales collapsed from 69 million units sold in 2007 to a trend below 60 million at the start of 2009. Gross revenues evaporated as 10 million units were suddenly out of the system. In economic terms, 10 million units at an average price of $15,000 per car is $150 billion of value. That would be the equivalent to the disappearance of 10% of Brazil's GDP[1]!

There were pressures in every direction. Credit had stopped. Cash was scarce. Suppliers were distressed. Dealers were failing. Car buyers were stopped in their tracks. In this chaos, automakers were forced to react quickly as the crisis evolved with speed and intensity.

Cash management became the priority of the day. We quickly began re-evaluating capital expenditures, implementing cost-cutting and focusing on tight inventory control to adapt to market changes. Within the Renault-Nissan Alliance, we were fortunate to benefit from synergies within our partnership. We put teams in place to push for greater commonisation and standardisation, making smart use of our scale and scope. We had no choice but to use the Alliance as a priority lever to go through the crisis and prepare for business in the post-crisis era.

■ Government interventions

The scenario at the end of 2008 and in early 2009 was bleak, and it was apparent that our industry needed help. And this is when governments began to intervene.

I recognize that the words "government intervention" may not be welcome in the world of free markets. But, in fact, governments have a long history of intervening in business affairs and influencing markets and consumer behavior.

Let me give you one example. In Europe, 60% of cars use diesel fuel, whereas the number of diesels in Japan or the U.S. is very, very small. Why is this? The same automakers sell cars in all the same markets, so product availability is not the issue. The big difference is due to government regulations and taxation: European regulations cause consumers to choose diesels as the most affordable choice.

So, in the face of the worst economic crisis in 80 years, governments intervened. They reacted to the crisis and to the sweeping recession by acting in variety of ways. Those actions included: bolstering credit markets… giving direct support to auto companies… offering purchase incentives to consumers scrapping older vehicles…and providing incentives to automakers to build cleaner cars.

Let me describe each one separately.

[1] Brazil's GDP in 2008 = US $1,575.2 billion (as of 12/9/09). http://devdata.worldbank.org/AAG/bra_aag.pdf.

The first action of governments was to intervene to thaw frozen credit markets and make cash more available. Central banks around the world cut interest rates and pumped billions of dollars into the capital markets to improve liquidity. They did not take this action because they were necessarily concerned about the car business. They acted because they were concerned about *employment*.

Auto companies are responsible for a massive number of jobs globally. More than 50 million people globally earn their living in the auto industry. Producing more than 60 million vehicles globally is equivalent to a global turnover of €1.9 trillion. If vehicle manufacturing was a country, it would be the sixth-largest economy in the world. Governments are not willing to sit on the sidelines when the jobs of so many voters are at stake.

In addition to the automaker jobs, there are rippling effects in the employment of automotive suppliers, auto dealers and auto service businesses. To give you a sense of the scale, the Renault-Nissan Alliance employs 350,000 people worldwide. Multiply that by 10 for the related businesses, and the number grows to more than 3.5 million jobs linked, directly or indirectly, to the Alliance worldwide. And we are just one group among many global automakers.

In addition to actions in the financial markets, governments supported auto companies directly through various initiatives. For example, the majority of stimulus funds[2] in the U.S. government went to General Motors and Chrysler. And driven by the need to prevent a mass collapse in employment, the U.S. government took 70% ownership of General Motors when the company declared bankruptcy – an unprecedented action that no one could have imagined before this crisis. The U.S. wasn't the only country extended support to automakers. Financial support was given by France, Japan, Sweden and Germany. Even governments that do not have national automakers, such as Spain and the United Kingdom, extended aid.

All this money was provided at a critical time, and it accomplished an important purpose. It gave automakers *time* to adapt to the volatility and headwinds in the market. It gave us time to reorder operating priorities and put measures in place to deal with the sudden loss in sales. And the drop in sales was severe.

So governments acted again, offering purchase incentives to stimulate the economy and preserve jobs through new vehicle sales. The so-called scrapping incentives made a simple offer: trade in your current car for a new, more fuel-efficient car and receive a financial incentive from the government. Government incentives – or, on the other side, regulatory penalties – are like the carrot and the stick. The appeal of the "carrot" steers action in positive directions. The threat of the "stick" has the same effect. The scrapping "carrot" was welcome… and effective.

Scrapping schemes were introduced in Japan, Germany, France, Italy, the United States, Russia and many other countries. In the U.S. alone, nearly 680,000 older vehicles were replaced by newer, more efficient models over the four months of the CARS Act of 2009[3]. Purchase incentives took other forms as well. For example, Brazil reduced the industrial products tax for important sectors of the economy, such as vehicles, white goods and building materials. China cut the consumption tax on cars and started a stimulus program for buyers in rural areas, offering up to 13% of the total price of a new car.

[2] Part of $700 billion Troubled Asset Relief Program (TARP)
[3] Consumer Assistance to Recycle and Save Act of 2009 Report to Congress, December 2009, p. 2.

Complementing the scrapping incentive schemes, governments also offered incentives to automakers to build cleaner cars and to encourage consumers to make eco-friendly car purchases. Many governments were looking for ways to inject money into their economies. They decided that they could kill two birds with one stone by using this opportunity to promote environment-friendly cars. In the United States, the government offered low-interest loans to develop alternative fuel or electric vehicles.

Nissan took advantage of this offer. We received a $1.4 billion loan to expand our vehicle plant in Tennessee to make our new zero-emission car, the Nissan LEAF, and to construct a new facility to build batteries for our cars. I will be in Tennessee next month to participate in the groundbreaking for our new EV battery plant.

Other government incentives took a different approach to "green" efforts. In China, the government reduced the auto purchase tax for cars with small engines and offered incentives for clean-energy car development. Malaysia developed a new National Auto Policy to attract investments in hybrid and EV segments. Thailand provided a 90% cut in import taxes for "green" auto parts. These examples of government interventions – and there were many more – could have happened over time *without* the financial crisis. But the crisis gave governments a trigger to advance environmental initiatives.

I have mentioned several actions governments took during the crisis. But it's also important to mention actions that were *not* taken – and I am referring specifically to protectionist actions, which were very limited during this period.

When national or regional economies are in distress, people can be tempted to "circle the wagons" and push for efforts to protect their own interests over all others. This did not happen in 2009. Cooler heads prevailed; there was more talk than action.

No major tariff changes occurred within our industry, and existing protections for local production remained in place. For the most part, governments recognized the importance of free trade and did not put in place rules that would favor their own national automakers over others.

■ How the auto industry has changed course due to government intervention

When I was asked to join this Forum, I was asked to speak about how these recent government interventions have altered the course of the global auto industry. And, without a doubt, they have.

I see the long-term effects in two areas:

- One, we are seeing the start of an *era* of more frugal cars; and
- Two, I believe governments' efforts to promote low or zero-emission cars will continue and even *strengthen* in the years to come, with a new kind of public-private collaboration.

As to the shift to smaller, fuel-efficient cars, part of this trend could be attributed to the general malaise in the world's economy, but part is linked to governments' incentives to push for low- or zero-emission cars.

The scrap incentives that were used last year put a lot of consumers in smaller cars. Of the 680,000 cars sold during the American CARS program, the vehicles that were traded in had an average rating of 15.8 miles per gallon; the new vehicles averaged 24.9 miles per gallon --

smaller, more efficient cars. This <u>shift to smaller cars</u> is also in line with a trend we see with the growing influence of emerging markets.
Over the past 10 years, the share of the global auto market in Western Europe, Japan and the United States has declined from 70% to 50%... and this trend will continue. Sales in Brazil, China and India multiplied fourfold in that time.

Today <u>entry and price-entry car</u> segments account for 20% of the global TIV of 60 million units, and the segment is growing. The push to small cars that we saw during the financial crisis is not going away. In developed markets and in emerging markets, the demand for price-entry cars will continue. <u>Emerging markets</u> will drive growth with frugal cars since first-time buyers are very focused on the entry-level price point. In <u>developed markets</u>, consumers will continue to be sensitive to vehicle size and fuel efficiency because they know <u>oil</u> and commodity prices could – and likely *will* – rise as the global economy recovers. Some people are making a <u>personal *choice*</u> of frugal cars. Luxury brands are expanding lineups to offer new, fashionable, smaller models. Small is here to stay.

The other lasting effect of government interventions in the auto industry is the <u>emphasis on environment-friendly cars</u>. When governments were deciding how they would put money into their economies during the crisis, they actually saw a rare opportunity to accomplish *three* important objectives at the same time. Scrappage incentives covered <u>economic</u>, <u>political</u> and <u>environmental</u> bases in one sweeping measure.

The <u>economic effect</u> was obvious. By incentivizing customers to buy new cars, they boosted automotive sales, which boosted auto production and, most importantly, saved tens of thousands of industry jobs at a very critical time in the recovery process.

The <u>political effect</u> was, perhaps, less obvious. The transportation sector depends on one commodity – oil. Most major car markets are net importers of oil. By requiring buyers to trade their old cars for more fuel-efficient cars, governments were able to lower the sector's dependence on imported oil and – perhaps – influence customers to change their car preference for the long term.

The last objective – the <u>environmental benefit</u> – is also obvious. Basing scrappage incentive criteria on trade-in vehicle fuel economy gap provided a win-win for consumers and for the environment. The emphasis on eco-friendly transportation is becoming a powerful force, among governments and among consumers.

This is why the <u>Renault-Nissan Alliance</u> is bringing a <u>lineup</u> of zero-emission cars at an acceptable, affordable price for consumers. We believe strongly that the best way to curb vehicle emissions is not to produce them at all. So we will be the first global automaker to mass-market affordable EVs, beginning this year with sales of the Nissan LEAF. This compact car will be part of a lineup that includes a small city car, a compact luxury car, a family car and a light commercial vehicle. We are committed to this technology. Across both companies, we have 4 billion euros of investment… eight products in development… our own battery technology and five plants to manufacture batteries… seven manufacturing locations for EVs… with a capacity of 500,000 units. We already have more than <u>50 agreements</u> with governments around the world that are partnering with us to advance zero-emission mobility, beginning with the LEAF.

Just last week, we announced a <u>strategic cooperation</u> between the <u>Alliance and Daimler</u>, a deal that includes us working together on projects relating to electric vehicle technologies that

will benefit both partners. And LEAF illustrates how governments' fiscal policies can drive customer behaviors. Many consumers make purchase decisions based on their pocketbook. They will welcome the incentives that will make buying the LEAF a good eco-friendly decision *and* a good economic decision as well.

■ Conclusion

The arrival of the zero-emission cars from Renault and Nissan is a bright spot after a long period that can be described as challenging or even *dangerous*.

It is no understatement to say that the global auto industry was at the point of implosion at the height – or, rather, the *depth* – of the crisis. Government actions in response have been timely and necessary. In a time of crisis, governments *should* intervene. Action is expected. And when governments can tie consumer incentives to promote environmental progress and influence positive change, then it's even better – for the automakers… for consumers… and for society overall.

Ladies and gentlemen, thank you for your kind attention.

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