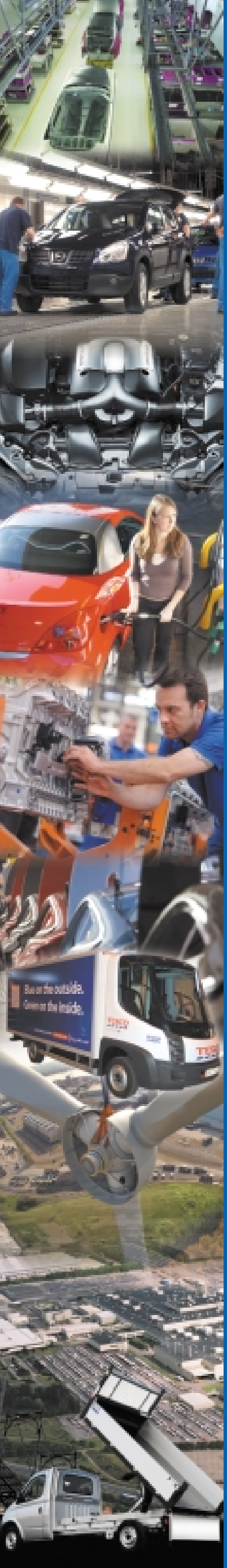
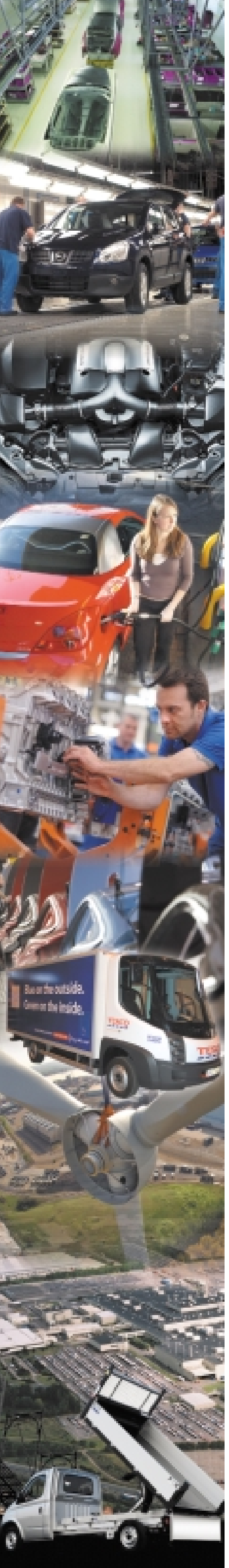


The Society of Motor Manufacturers and Traders Ltd.
Forbes House, Halkin Street, London SW1X 7DS
Tel: +44 (0) 20 7235 7000 Fax: +44 (0) 20 7235 7112
www.smmt.co.uk E-mail: communications@smmt.co.uk

Automotive Manufacturing 2007

The Industry Perspective

SMMT's Fifth Annual Issues Survey



Introduction by Graham Smith SMMT president

Welcome to *Automotive Manufacturing – the Industry Perspective,* SMMT's annual health check of the automotive sector in Britain.

This is the fifth year in which SMMT's president has collated the views of more than 100 senior executives. Responses are comprehensive and represent the opinions of directors and chief executives from car and commercial vehicle operations, the component sector and vehicle aftermarket.

Since its introduction, this report has primarily focused on key areas such as business confidence, skills, threats and opportunities and the international perspective. This year we have included questions on CO_2 and climate change reflecting the critical importance of the environment for individual members and for the sector as a whole.

The survey reveals an industry actively committed to reducing its environmental impact. Today, manufacturers are helping to deliver more sustainable motoring and are increasing R&D investment in CO_2 abatement technology for the future. The automotive industry has a key role to play in emissions reduction and we are taking our responsibilities seriously.

But there is a concern that progress is not always well understood. Our industry has made significant environmental advances. Since 1997, average new car CO_2 has been reduced by 12 per cent, saving an estimated one million tonnes of CO_2 a year in the UK alone. Each vehicle manufactured today in Britain requires only half the energy to produce than it did five years ago, cutting 700,000 tonnes of CO_2 a year.

The survey also highlights the crucial role of skills and training in underpinning automotive competitiveness. Working with our key stakeholders we have seen progress. The new National Skills Academy for Manufacturing and the Sector Skills Council for automotive retail will further narrow the skills gap but we need to continue our efforts.

In terms of regulation, we must achieve a more effective partnership with government. It is clear from responses that potential consequences of poorly conceived regulation are a concern for many companies in terms of increased costs, employment impact and the threat to manufacturing competitiveness in the UK.

It is vital that the SMMT continues actively to promote our industry's activities and achieve a more balanced approach to legislation.

The modern motor industry is a high value, forward-thinking sector with a bright future. Productivity is improving, and most companies remain optimistic about growth in the medium term. We should also never forget that ours is a highly rewarding environment in which to work.

We hope you find this year's report valuable. If you do have any thoughts or comments do contact me at president@smmt.co.uk

Graham Smith
SMMT president

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Background to Survey

Questionnaires were sent to more than 500 senior executives representing companies in the automotive sector in September 2007. A total of 102 responded by the deadline of 10 October, of which 83 per cent were at chief executive, chairman or senior director level in their company.

20 per cent of respondents represented companies with more than 500 employees, nine per cent for companies with between 250 and 500, 36 per cent with 50 to 250 employees and 35 per cent from companies with fewer than 50 employees.

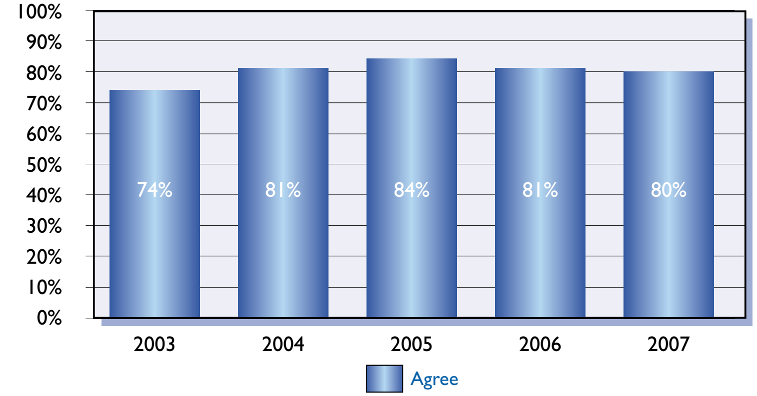
In terms of principal locations in the UK, over half of respondents represented companies in the West Midlands, South East and North West (20 per cent, 20 per cent and 11 per cent respectively).

Broken down by segment, the largest share of responses (31 per cent) came from component suppliers. Another 33 per cent came from vehicle makers, 18 per cent from car makers, nine from commercial vehicle manufacturers and six per cent manufacturers of other types of vehicle.

Business Prospects

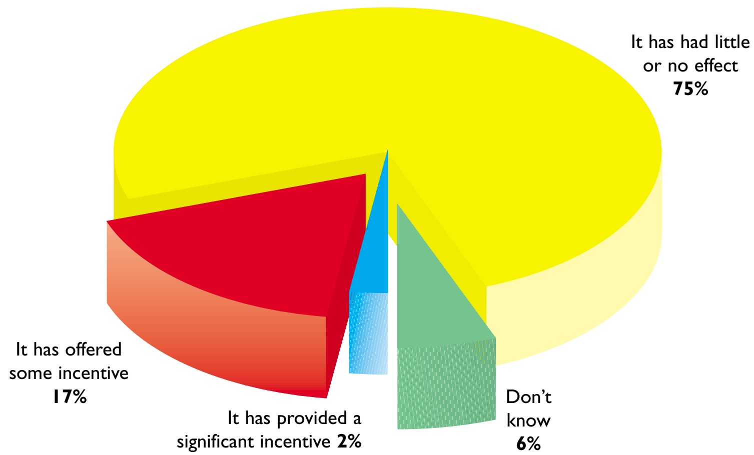
Most companies in the sector are optimistic about growth. In the short term 74 per cent of respondents felt growth prospects were likely. This rose to four in five – 80 per cent – when asking companies to look forward five years. 73 per cent plan capital investment in the next 12 months.

The growth prospects are good for our business in the next five years



SMMT asked respondents about enhanced R&D tax credits, following changes in recent budgets. Nearly a fifth of companies claimed that the changes had offered some or significant support for R&D activity. Nevertheless, nearly three-quarters said the moves have had little or no effect.

R&D tax credit changes



Once again, respondents were concerned by the rising costs associated with employment law; 94 per cent believed the burden would increase in the next five years. Furthermore, there was a belief that environmental legislation is likely to increase costs significantly in the next five years, according to 99 per cent of respondents.

96 per cent of respondents agreed that the motor industry is seen as an easy target when designing CO_2 abatement legislation.

Comments:

"Still struggling with currency issues as 75% of our business is exported to mainland Europe and beyond." Component supplier

"Competition from Europe is very strong, with no incentives in the UK in most areas, staffing, training etc" CV manufacturer

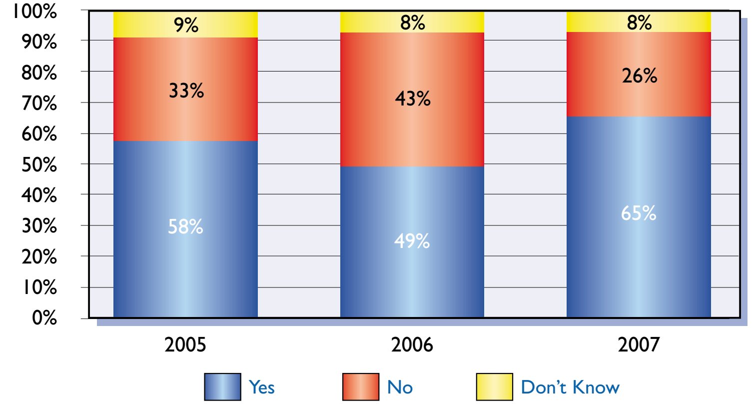
"Government support for R&D is markedly lower than in other EU member states." Volume car producer

Productivity and Skills

SMMT champions competitiveness, productivity, R&D and skills as central to the future of automotive manufacturing. It was therefore encouraging to see an increase in respondents who believe productivity is improving, 65 per cent in 2007, compared to 49 per cent last year.

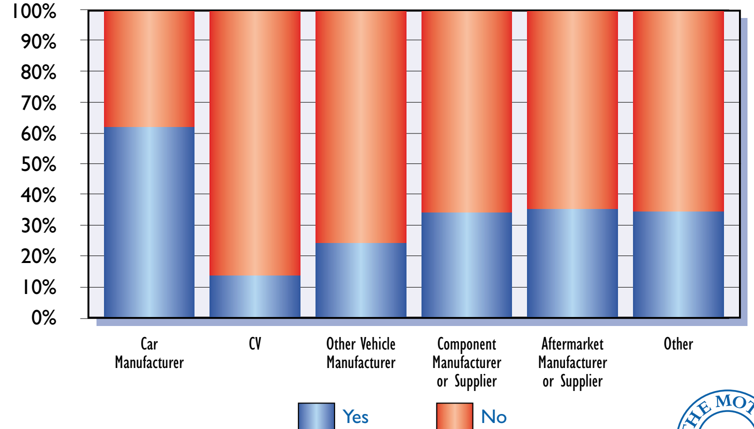
Car and commercial vehicle manufacturers were more confident in this area, perhaps reflecting high profile productivity improvements at sites across the UK (for example a 30 per cent productivity improvement at Ellesmere Port, helping the UK win production of the new Astra).

Do you believe the industry is improving productivity?



The industry still has work to do in improving the quality of recruitment and training, although car manufacturers were clearly more confident than other parts of the industry.

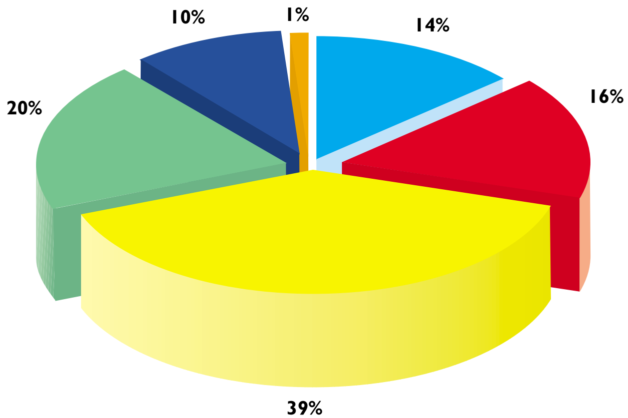
Do you believe the industry is improving the quality of recruitment and training?



More than half of those surveyed (56 per cent) said they were unable to recruit appropriately skilled employees and it seems that level 3 skills remain the biggest hurdle for employers. 39 per cent of respondents overall said they found it difficult to recruit this type of individual. Perhaps unsurprisingly, this rose to 47 per cent for component suppliers, and 75 per cent for companies in the 'other vehicle manufacturer' category which includes makers of trailers, buses and fire-fighting vehicles.

At what skills level do you find recruiting the most difficult?

(Base: All who disagree that their business is able to recruit appropriately skilled employees)



Comments:

"Basic engineering and practical skills are almost non-existent in the average school leaver."

Component supplier

"The demolition of the apprenticeship structure in industry in the late 70s and early 80s is now showing up as a lack of widely skilled individuals. 80 per cent of our senior technical managers are ex-apprentices now aged 50+."

Engineering company

International - Threats and Opportunities

SMMT's international team exists to make contacts on behalf of UK companies, and to establish opportunities with suitable suppliers outside the UK at trade fairs, conferences and international trade missions. For respondents to the survey, European markets are still seen as the richest seam for opportunities. Equally, China is regarded as the market with competitors that posed the most significant threat to those operating here.

Strongest opportunities for trading outside the United Kingdom (Ranked)

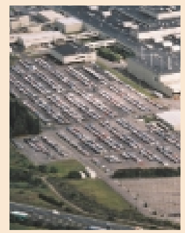
1. Western Europe
2. Central Europe
3. Eastern Europe
4. Russia
5. China
6. Middle & Far East
7. North America
8. South America

Outside the UK we see the most significant threat from competitors in the following international markets (Ranked)

1. China
2. Western Europe
3. Eastern Europe
4. Central Europe
5. Middle & Far East
6. Russia
7. North America
8. South America

This year we also asked respondents to rate in terms of importance, areas of business that give greatest concern in an emerging market like Russia, India or China. Rule of law and logistics were the areas of greatest concern

Topics that give concerns doing business in an emerging market (Ranked)



1. Logistics / customs / tariffs
2. Rule of law / IPR / Regulation / Bankruptcy / Payment
3. Political uncertainty / security
4. Currency stability
5. Production / product quality
6. Labour skills and education, quality / availability
7. Labour / management recruitment, deployment and employee rights
8. Lack of government support

Comments:

"Work is going to Asia. We are working very hard to stand still."

Component manufacturer

"The truth is that one company's threat is another's opportunity."

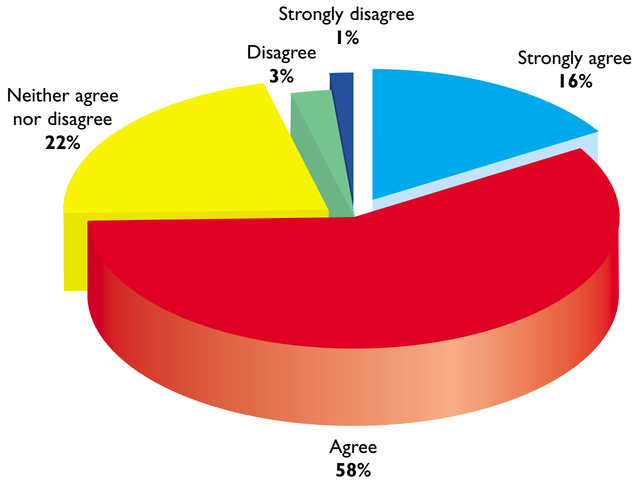
Aftermarket supplier

CO_2 and Climate Change

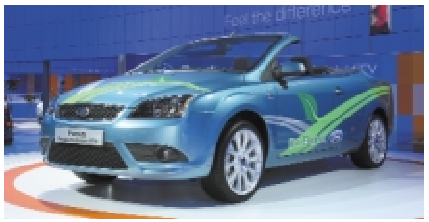
For the first time, this year's survey included two sections with questions dealing with issues relating to carbon dioxide emissions (CO_2) and climate change, reflecting the prevailing mood in political, media and public circles. It also reflects the sector's absolute commitment to its responsibilities, to investment in technologies for the future and its desire to be open, honest and accountable on progress.

Almost three quarters of respondents (74 per cent) felt that CO_2 and climate change is now the single most important issue facing the sector.

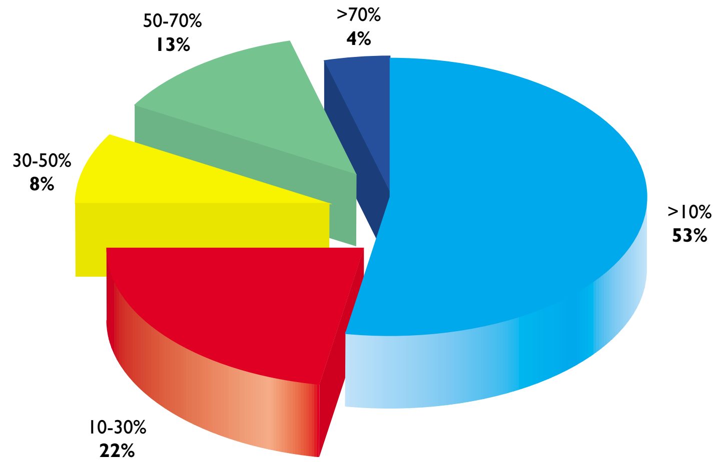
Carbon emissions and climate change are now the single most important issue for the automotive sector



Furthermore, companies report that more R&D will need to be spent on CO_2 reduction measures in the years to come. Currently 27 per cent of respondents said they devote 10 per cent or more of R&D expenditure to CO_2 reduction measures; in the next ten years however, 47 per cent of companies suggested it would be more than 10 per cent.

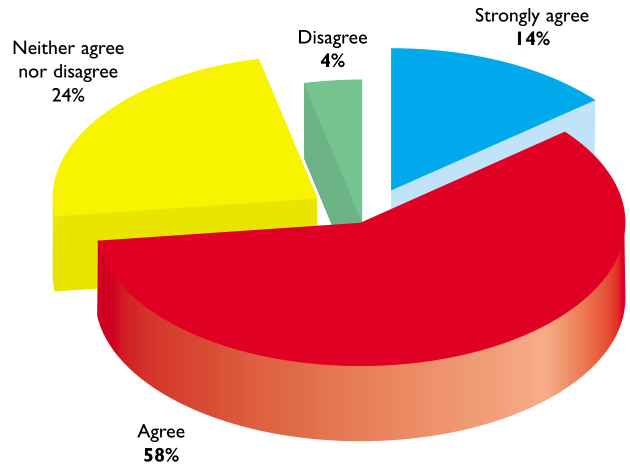


What proportion of your R&D investment in your company in the next 10 years will be targeted at CO_2 reduction measures?



The industry feels it is setting the agenda when it comes to delivering cleaner products to market. The survey asked if companies believe investment in greener technologies will lead consumer choice in the next 10 years, rather than responding to consumer demands. Nearly three quarters said it would lead consumers' buying habits.

To what extent do you believe greener industry products will lead consumer choice in the next 10 years, rather than responding to consumer demands



On national road pricing, companies were ambivalent about its environmental benefits. 22 per cent felt it would help cut CO_2 while 20 per cent felt it would increase it. 58 per cent believe it would have no effect at all. However, respondents were clear on their thoughts in terms of its cost to business; 87 per cent felt it would add costs, with just one per cent optimistic of a reduction.

Comments:

"As long as taxation measures are completely inconsistent, market-to-market, it is next to impossible for manufacturers to optimise investment in green technologies and solutions." Volume car producer

"This greenhouse bandwagon is causing everybody grief." Sports car maker

"Politicians attack soft targets. They do not take the long term view on difficult issues." Volume car producer

Integrated approach to CO_2 reduction

The survey shows the industry believes it is leading consumer choice, by delivering lower carbon solutions to market. This is borne out by a belief that low emissions still come low down the list of priorities when buying a vehicle.

What do you feel your customers look for when choosing a vehicle? (Ranked)

1. Price
2. Specification
3. Running costs
4. Performance
5. Safety
6. Low emissions
7. In-vehicle entertainment

Initiatives like the new car colour-coded label in showrooms and partnership with government on the *ActOnCO*$_2$ campaign are clearly helping raise awareness. However, we asked if there were any priorities in terms of areas of support beyond technology solutions: better consumer information, tax incentives / cheaper fuel, strong re-fuelling infrastructure and sustainable fuel production.

Interestingly, 56 per cent of respondents said they could not identify a single key factor in driving demand for cleaner vehicles, supporting the view that governments, fuel companies, the industry and consumers must work together to drive demand. However, for those who felt able to rate one factor over another, cost to wallet clearly took precedence.

The key factors which are driving demand for environmentally friendly alternative fuels (Ranked)

1. Tax incentives / cheaper fuels at pump *(cost to consumers)*
2. Re-fuelling infrastructure *(practicality)*
3. Sustainable fuel production *(consumer perception)*
4. Better consumer information *(awareness)*

Comments:

"No single factor is going to make someone buy a cleaner car; the thinking must be joined-up and include financial incentives to go green – in the showroom and at the pump." Volume car producer

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SMMT
The Society of Motor Manufacturers and Traders Ltd
Forbes House, Halkin Street, London SW1X 7DS