WHEN CARLOS MET MARY

AD PUNCTUM | Automotive Strategy

March 2017

How PSA Might Make Savings Through The Takeover Of Opel And Vauxhall

EXECUTIVE SUMMARY

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- Combining PSA and Opel will create cost savings in a range of categories
- The purpose of this presentation is to assess how reasonable those targets are and to give an explanation of how they might be achieved
- PSA's cost saving target of €1.7 billion per year by 2026 looks reasonable in the context of both the absolute spending levels and historic cost performance
- Further savings look achievable, but may require favourable headwinds
- PSA's statements that job losses may not be required seems unrealistic -- likely around 7,000 – 8,000 jobs will be lost, including admin staff, to make savings
- PSA may feel that there are revenue opportunities, e.g. filling gaps in each brands' portfolio with sister products, new markets (China)

THE SAVINGS A TAKEOVER WILL YIELD

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Start Immediately	Research & Development	Reduce new model development costs by sharing parts the customer doesn't notice
	Commodity Purchasing	Increased scale on bulk materials and non-production commodities (e.g. travel)
Feed In Over Time	Production Material	Savings in vehicle parts cost through increased scale (requires common design)
	Marketing & Selling	Reduce dealer and field staff footprint, economies of scale in advertising
	D&A / Capital Spending	Higher product commonality means greater sharing of facilities & tooling
Requires A Restructuring Plan	Plant Labour & Overhead	Close plants or reduce shifts to better utilise capacity (alternative is huge volume growth)
	Administrative Staff	More efficient combined central staffs in activities such as purchasing and finance

PSA'S 2026 ANNUAL SAVINGS TARGET -- €1.7BILLION

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Commodity Purchasing Production Material	• Economies of Scale • Use PSA cost where Opel is higher and vice versa • More European sourcing (i.e. PSA are saying Opel costs were too high because of GM's global strategy)	€ 0.5 Billion Per Year
Research & Development	• Economies of Scale • Better design (same function at lower cost) • Productivity in R&D through digitisation	€ 0.4 Billion Per Year
D&A / Capital Spending	• Economies of scale • Higher manufacturing efficiency • Cost savings from higher product commonality	€ 0.2 Billion Per Year
Administrative Staff Marketing & Selling	• Apply benchmark working practices & productivity • Eliminate duplication, gain scale benefit	€ 0.2 Billion Per Year
Plant Labour & Overhead	• Apply benchmark working practices & productivity • Plant modernization and efficiency	€ 0.4 Billion Per Year

1.7 Bn

Source: Company Reports

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Question:
How realistic do these targets look?

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Answer:

All targets look achievable and we think that the cost savings could potentially go much higher…

OUR SUMMARY ASSESSMENT OF PSA'S TARGET

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Saving Category	PSA's 2026 Target (€ billions / year)	Our Assessment	Potential Further Savings (€ billions / year)
Material and commodity purchasing	0.5	Achievable / Painless	1.0
R&D and capital spending	0.4	Achievable / Painless	0.4
Selling and general administrative expense	0.2 *	Achievable / Painful (~2,000 job losses)	0.2 *
Manufacturing costs	0.4 *	Achievable / Painful (5,000 – 6,000 job losses)	0.6 *
	1.7		2.2

* Requires job losses

Targets Look Achievable And There Are Potential Further Savings. This Indicates That PSA May Reach Its Savings Goal Earlier Than 2026.

Material and commodity purchasing:
Savings look reasonable. Further potential beyond the stated targets.

PURCHASING SAVINGS POTENTIAL

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- PSA automotive cost of goods sold* is around 80% of revenue and material spending is the largest element within these costs
- PSA and Opel / Vauxhall's combined material spending will be around €30 billion per year in Europe
- A cost saving of €510 million equates to less than 2% of the spending
- PSA's pre-takeover 2015 – 2018 target is a €700 / vehicle saving (not only material cost), or about €1.3 billion per year
  - New target is 1/3 of this absolute amount over 160% of the volume
  - This is incremental to existing targets but has a longer time frame for realisation (out to 2026)

* Also includes labour and overhead and depreciation and amortisation (but not warranty)

R&D and capital spending:
Savings look reasonable. Further scope beyond stated targets.

R&D AND CAPEX SAVINGS POTENTIAL

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- PSA previously said sharing C-SUV platform led to a 35% reduction in capital expenditure and R&D -- larger scale increase than most programs would see
- PSA is targeting ~15% reduction in relevant R&D costs (€0.43 billion per year)
- A €0.25 billion annual reduction in capital spending amounts to ~9% of combined PSA and Opel / Vauxhall 2016 spending
- Note:
  - PSA's headline R&D covers the entire group including Faurecia -- saving would only be on European automotive portion of this (~ €1.3 billion)
  - GME R&D spending above 8% of revenue versus GM global (5%) & PSA (4%)

Total Annual Saving Of €0.68 billion (~15% Of Relevant R&D And CapEx) Is Within The Range PSA Have Previously Claimed For Shared Platforms.

R&D AND CAPEX SAVINGS POTENTIAL

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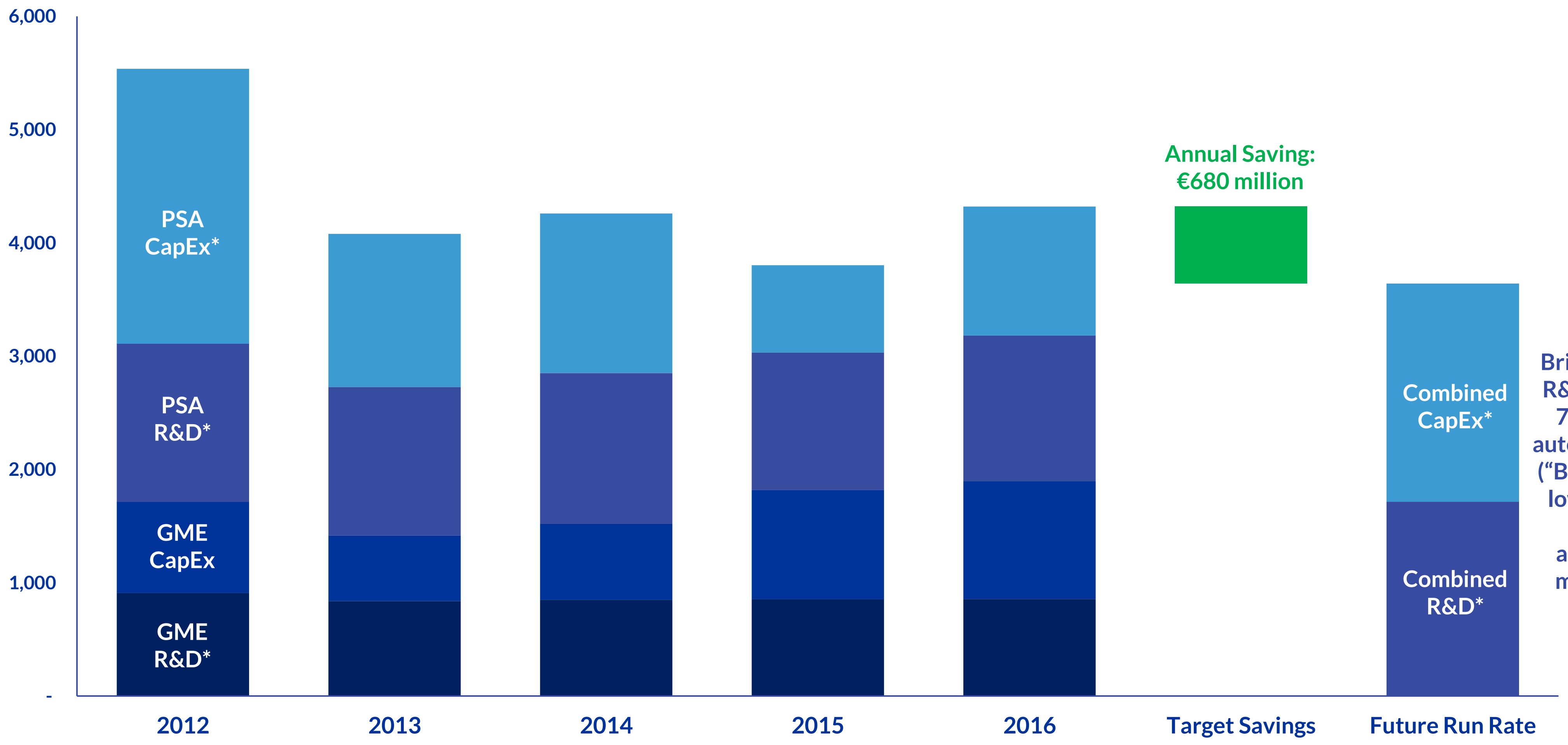
Spending On European Automotive Product Development And Capital Equipment By PSA And GM Europe



Bringing combined R&D and CapEx to 7% of European automotive revenue ("Back In The Race" lower end target) would save additional €400 million annually

Source: Company Reports, Ad Punctum Research

* Analytically derived European spending

Selling and general administrative expense: Savings look achievable but require restructuring or will take a very long time.

SG&A SAVINGS POTENTIAL

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- PSA and GM SG&A figures are not directly comparable because GM reports warranty spending in cost of sales

- Aligning to PSA's methodology, both spend around 12% of revenue on SG&A

- €170 million annual saving equates to around 3% of PSA / GME combined European SG&A
  - Could achieve this by reducing ex-GME by 10% without touching PSA staffs

- Reminder: PSA have reduced SG&A by >10% since 2013 -- enabled by a redundancy program

- Targets look reasonable but will mean <u>over 2,000</u> job losses -- long term attrition likely insufficient (depends on age profile), redundancies probable

SG&A = Selling and General Administrative expense

Manufacturing costs: Savings look achievable but require restructuring or mammoth volume growth.

WHAT HAS PSA SAID ABOUT RESTRUCTURING?

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- PSA implied no job losses or factory closures are inevitable, having said that…
- They attribute substantial savings to manufacturing efficiency
  - Either volumes must grow substantially or capacity must reduce
- Lower spending on Capex also implies fewer facilities
- There are "implementation costs" of €1.6 billion in PSA's presentation
  - Some of this is systems integration etc, but it suggests footprint reduction
- Ongoing saving target implies 5,000 – 6,000 job losses
  - Coincidentally, this would cost around €1.2 billion, leaving some implementation cost for SG&A headcount reduction*

* Based on per person separation costs for recent GM Europe factory closures

THE COMBINED COMPANY HAS SURPLUS CAPACITY

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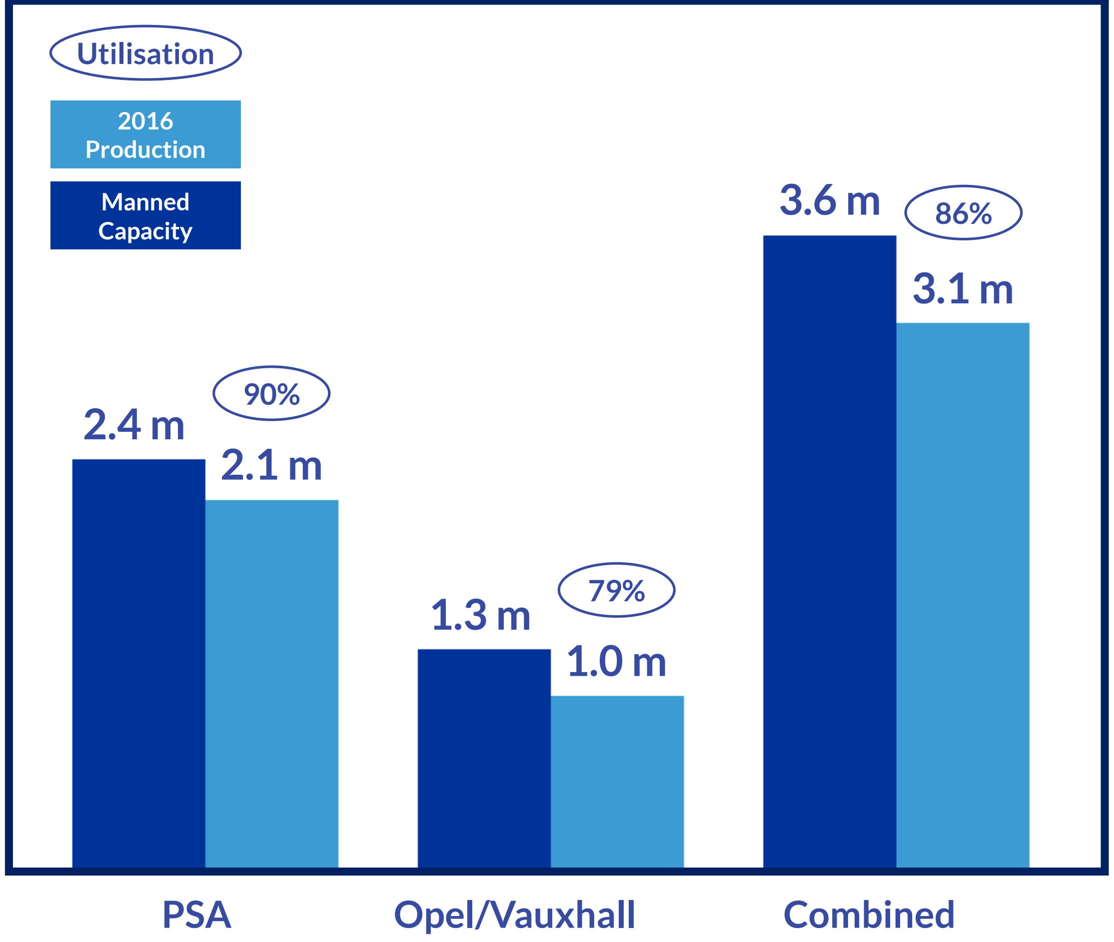
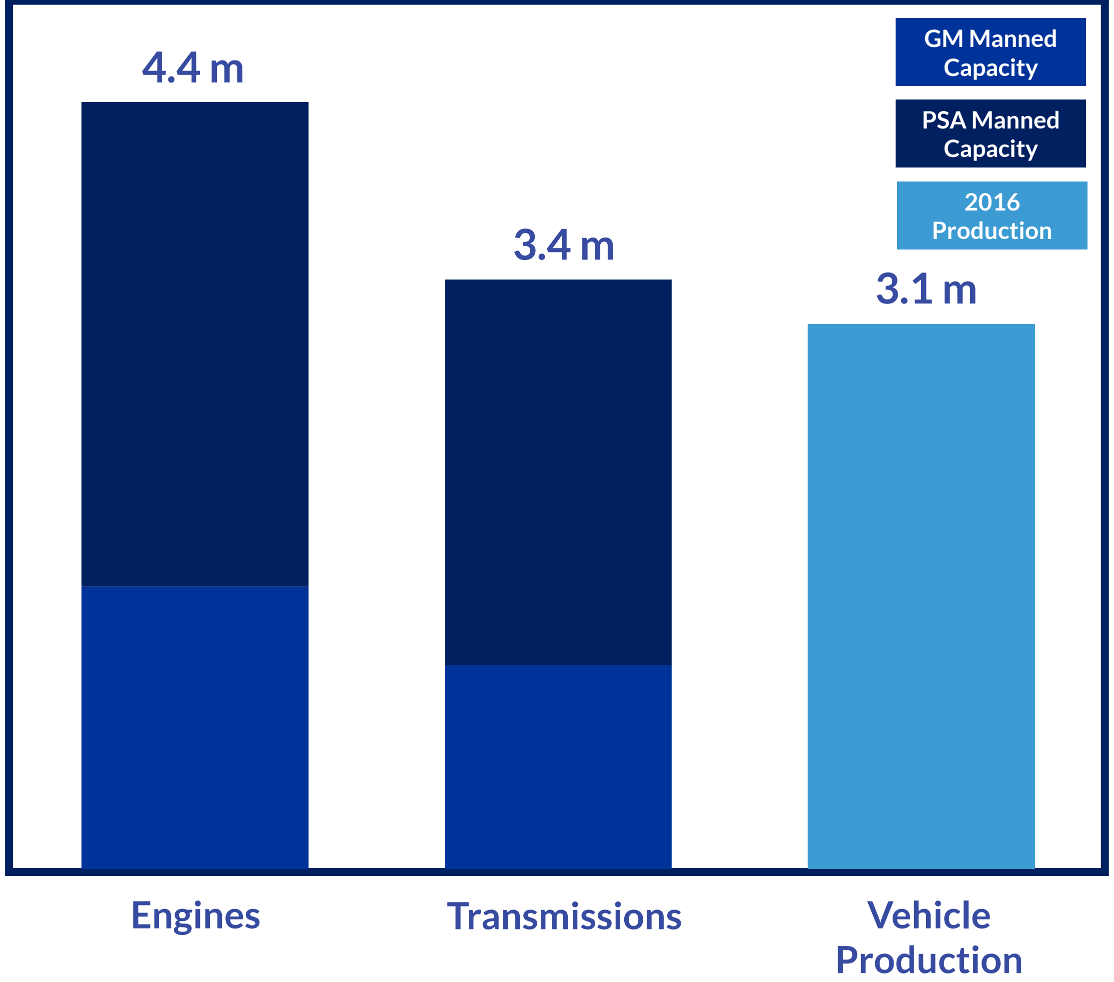
Surplus European Vehicle Capacity *



Surplus Capacity In Powertrain ^



Source: Company Reports, Ad Punctum Research * Excludes facilities not run by PSA or GM Europe ^ Includes announced 2017-18 investments

Without plant closures or shift reductions, “New PSA Group” efficiency would deteriorate and longer term targets would be missed.

There are clear areas where productivity can be improved… starting with Opel.

Question:
Why hasn't Opel's current restructuring plan put them in the black?

Answer:

Although the executive team may blame the business environment, productivity is little changed from 2008.

ALTHOUGH HEADCOUNT HAS FALLEN SINCE 2008…

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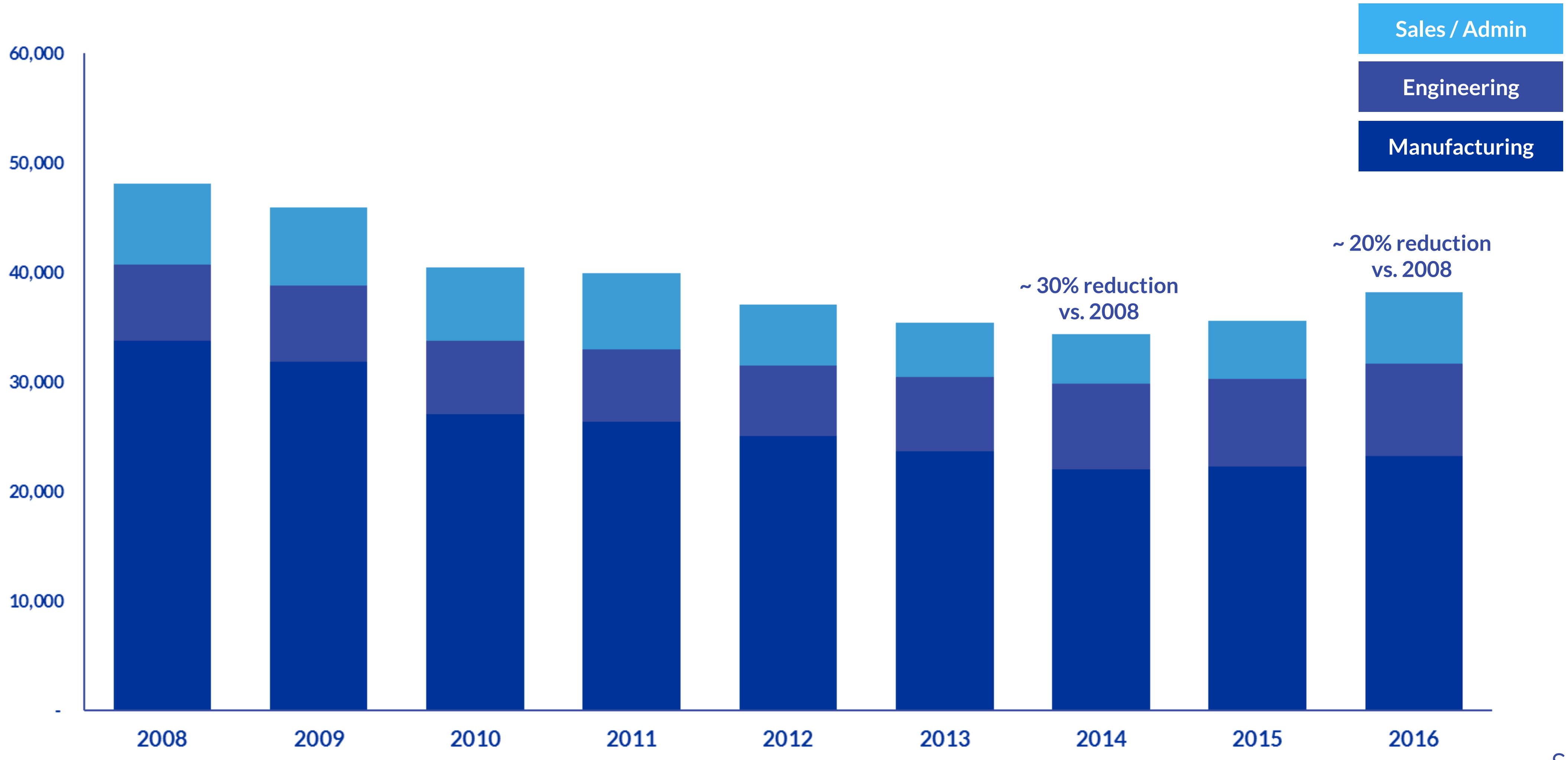
Total Opel and Vauxhall Headcount



Source: Company Reports, Ad Punctum Research

...SO HAVE VEHICLE SALES

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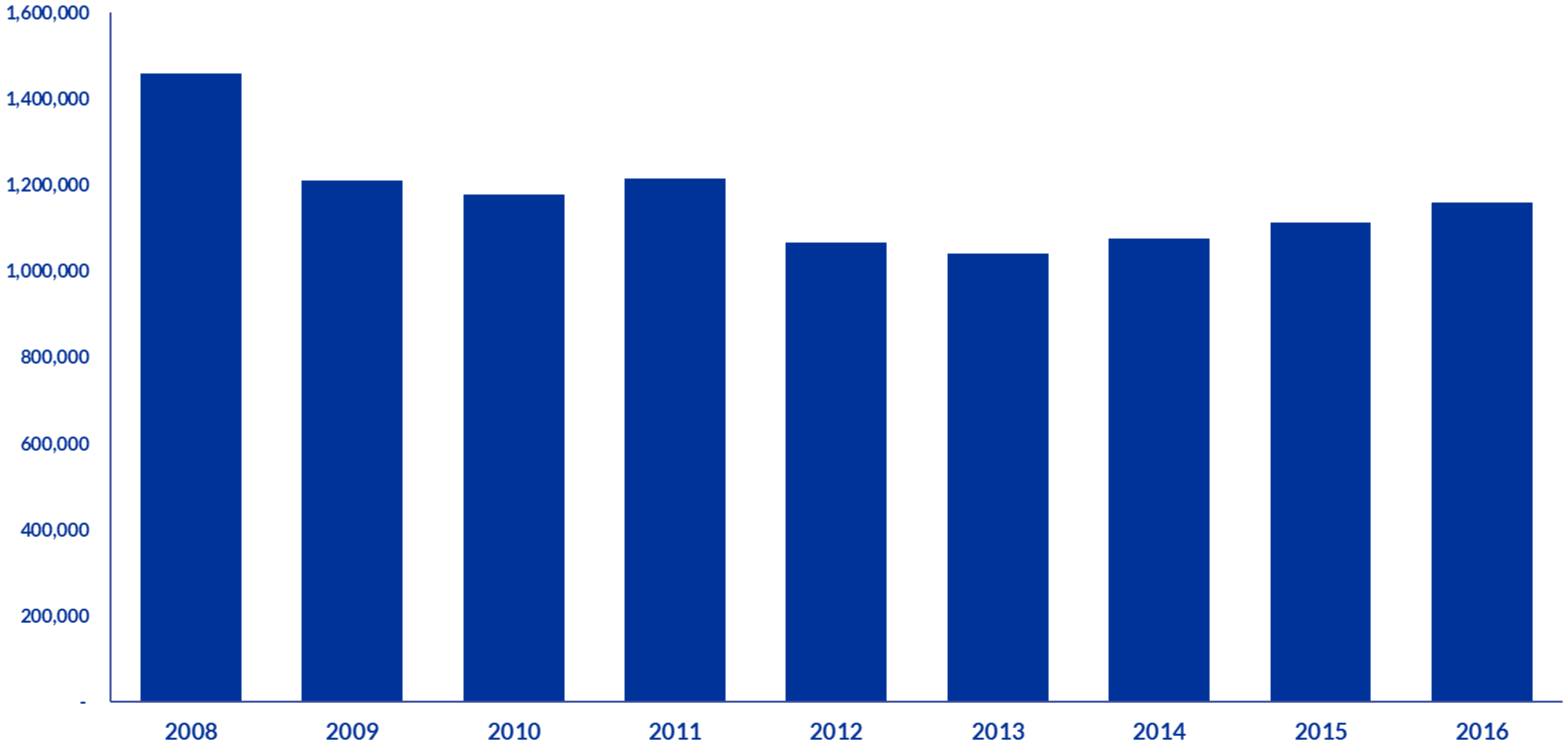
Total Opel and Vauxhall Registrations Each Year



Source: Company Reports, Ad Punctum Research

AS A RESULT… PRODUCTIVITY IS SIMILAR TO 2008

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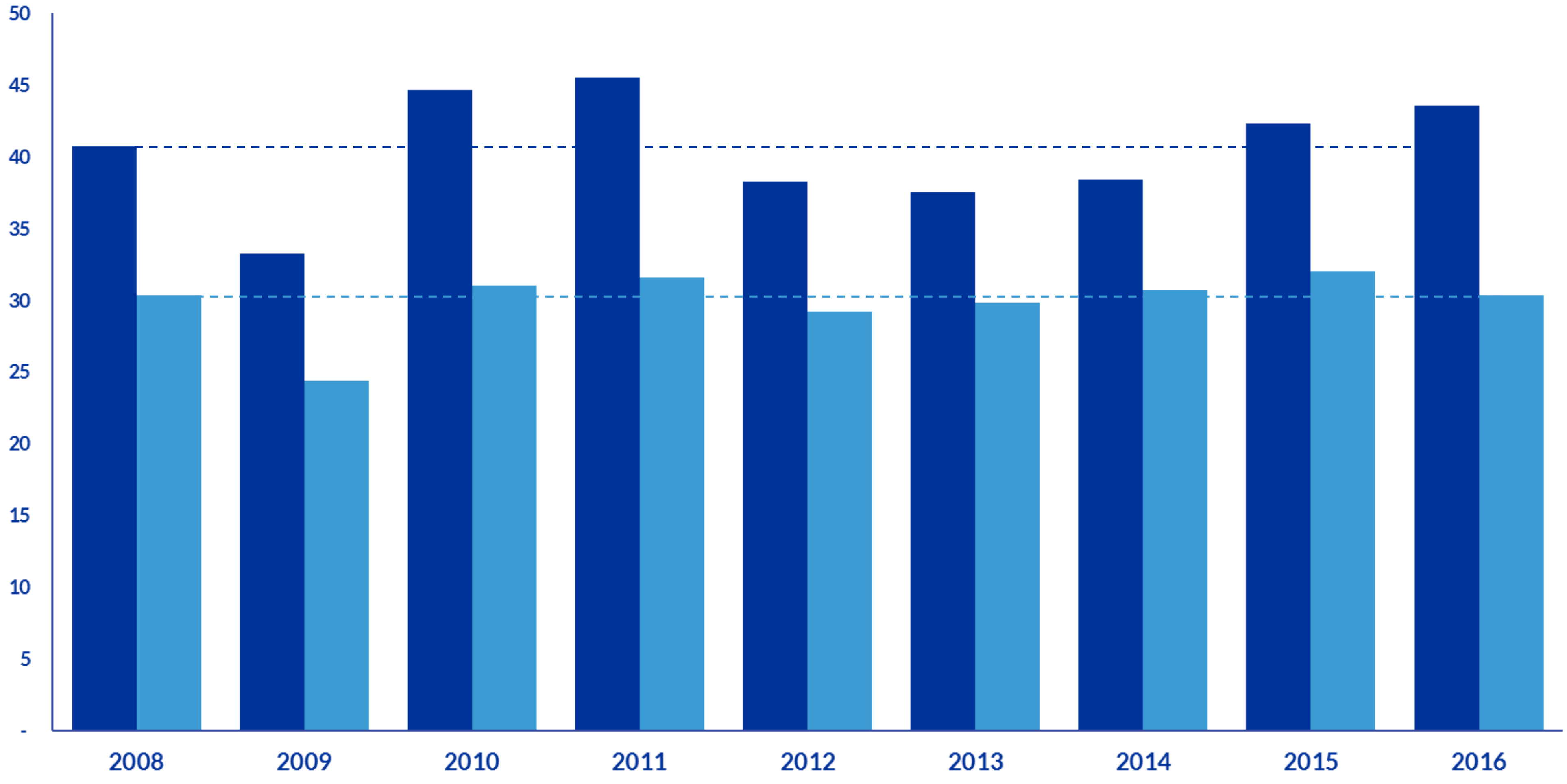
Vehicles Produced / Sold Per Employee

Vehicles built by Opel / Vauxhall per manufacturing employee (vehicle and powertrain employees)

Vehicles sold per Opel / Vauxhall employee (all employees)



Source: Company Reports, Ad Punctum Research

OPEL VEHICLE PLANTS -- SMALL & UNDER-UTILISED

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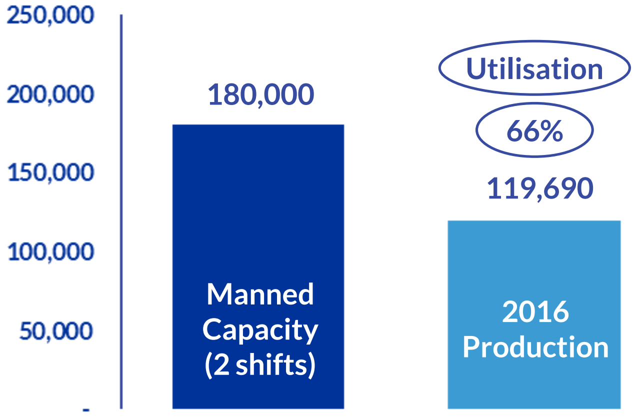
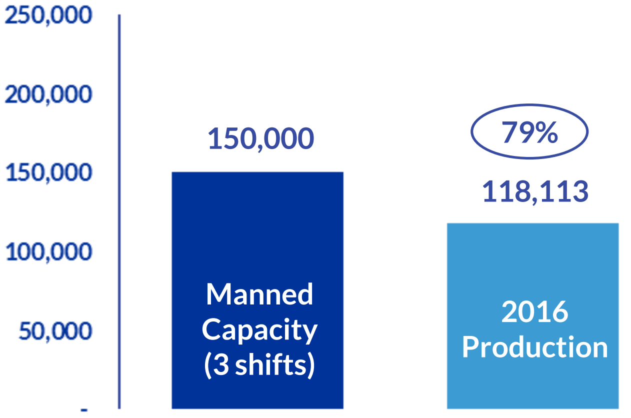
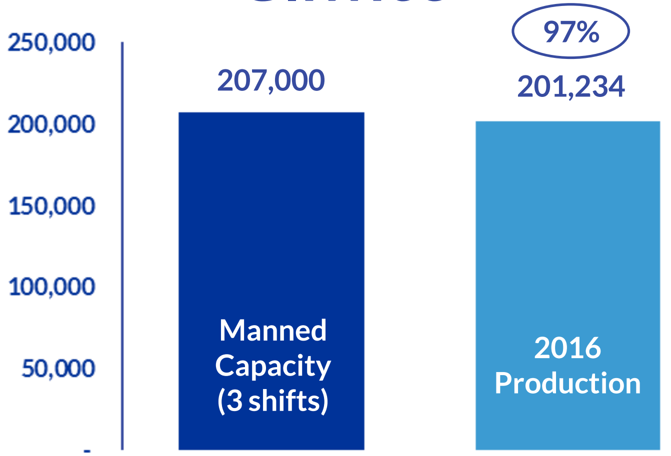
Eisenach



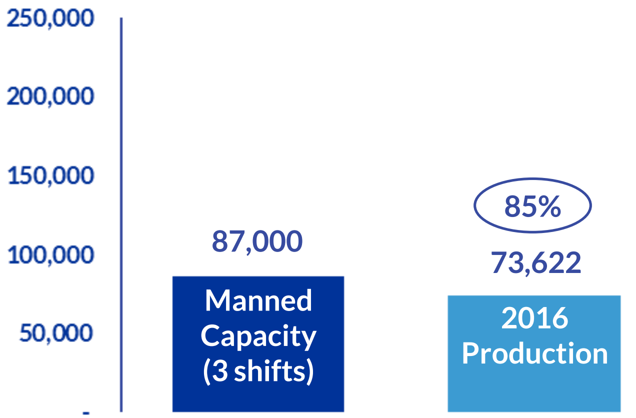
Ellesmere Port



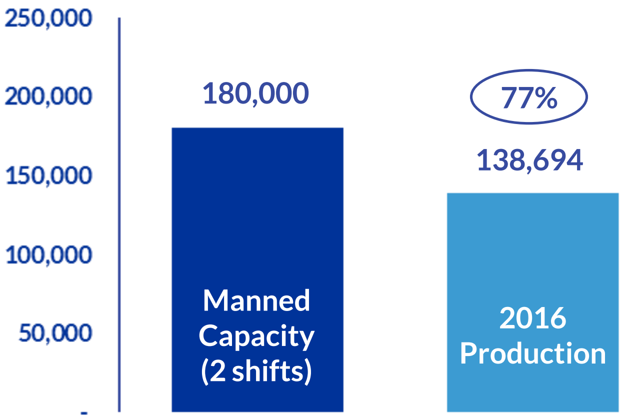
Gliwice



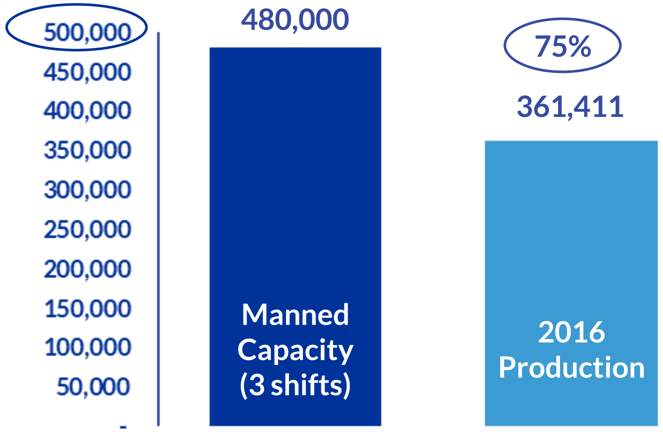
Luton



Rüsselsheim



Zaragoza



Source: Company Reports, Ad Punctum Research (see Methodology slide in Appendix for more details)

RESTRUCTURING -- CAN IT BE AVOIDED?

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"Of course, there is too much capacity - for us and many of Europe's car makers. But our objective is clear - to grow and fill the capacity; that is what winners will do, and it is the losers who will have to close factories. We want to be winners."

Karl-Thomas Neumann, GM Europe President (Opel's boss) -- 7th March 2017

- As we saw on a previous slide, Opel / Vauxhall's productivity has not improved much since 2008, despite a growing industry
- Although new CUVs may grow share, B and C cars will lose share to new products from Ford, VW and others in the next couple of years
- Restructuring should be considered as likely (as the "implementation" budget already implies) -- the following slides show how it might work

GME VEHICLE PLANT CLOSURE -- CONSIDERATIONS

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Plant	Current Status	Comments	Closure Risk
Eisenach (Germany)	Small, under-utilised	Already losing Corsa and Adam, gains Mokka X but other plants could make that	Very likely to close by 2019
Ellesmere Port (UK)	Small, under-utilised	Relatively easy to switch volume to Gliwice but useful in the event of hard Brexit	At high risk of closure, depends on PSA's view of hard Brexit
Luton (UK)	Small, okay utilisation	Only GM plant building this platform, at risk once product is common with SevelNord	At risk after 2020
Gliwice (Poland)	Small, good utilisation	Low cost, lead Astra plant	Unlikely to close
Rüsselsheim (Germany)	Small, under-utilised	It's the "Home of Opel", possible job losses elsewhere on site made easier by keeping vehicle production unchanged	Unlikely to close
Zaragoza (Spain)	Large, under-utilised	Next generation Corsa / Adam sourcing likely to improve utilisation	Unlikely to close

PSA VEHICLE PLANT CLOSURE -- CONSIDERATIONS

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Plant	Current Status	Comments	Closure Risk
Madrid (Spain)	Small, low utilisation	Plenty of other B and C car capacity	Very likely to close by 2019
Mulhouse (France)	Medium, good utilisation	Relatively easy to close -- components plant and Sochaux nearby to absorb labour	At high risk of closure, depends on mix of PTO / VO actions
Poissy (France)	Medium, okay utilisation	Already losing a shift	At risk, duplicates other plants
Rennes (France)	Small, low utilisation	Making unpopular large cars	At risk, duplicates other plants
SevelNord (France)	Small, low utilisation	Only PSA plant building this platform, at risk once product is common with Luton	At risk after 2020
Mangualde (Portugal)	Very small, okay utilisation	Unlikely to justify capex for new platform	At risk after 2020
Sochaux (France)	Large, okay utilisation	Just had a big modernisation program	Unlikely to close
Vigo (Spain)	Large, good utilisation	Mainstay of C platform production	Unlikely to close
Trnava (Slovakia)	Medium, good utilisation	Mainstay of B platform production	Unlikely to close
Kolin (Czech Republic)	Medium, good utilisation	Shared with Toyota, would be boosted by sharing Adam / Karl with 108 / C1	Unlikely to close

RESTRUCTURING -- WE USE 3 EXAMPLE SCENARIOS

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"Slow And Steady"

- Integration of powertrain facilities in the long term
- Avoid vehicle plant closures even though plants are sub-scale -- Justify takeover on the basis of R&D / CapEx
- PSA abandons wage target (11% of revenue)

"No Pain, No Gain"

- Integration of powertrain facilities in the long term
- Key VO closures before 2020, designed to be politically acceptable
- Fits PSA's restructuring budget
- Further VO closures in the event of recession

"Bring It On"

- Rapid integration of powertrain
- Vehicle plant strategy based on large/medium plants only
- Significant separation spending, but some hiring to allow re-arrange of footprint (towards low cost countries)

RESTRUCTURING SCENARIOS -- VEHICLE

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Action	Plant	Manned Capacity	Headcount	Comments
Start Point	All	3,649,000	~60,000	Utilisation at 86% (2016 Sales)
Close	Eisenach	(180,000)	(1,850)	Politics OK: Still have German sites
Close	Madrid	(130,000)	(1,842)	Politics OK: 2 x big plants in Spain
Close	Mulhouse	(255,000)	(4,000)	Politics OK: labour can move to Sochaux
Increase *	Sochaux	80,000	1,200	400k ➔ 480k, use ex-Mulhouse labour
No Pain, No Gain	All	3,169,000	53,500	Utilisation at 99% (2016 Sales)
Close	Luton	(86,500)	(1,530)	
Close	Mangualde	(60,000)	(730)	PSA may want to keep a Portuguese site ^
Increase	SevelNord	70,000	1,200	
Outsource *	Bursa (Tofas)	80,000	-	
Close	Rennes	(170,000)	(4,000)	May be difficult to create a social plan
Close	Ellesmere Port	(150,000)	(1,830)	PSA may want to keep a UK site ^
Increase *	Gliwice & Kolin	210,000	2,300	
Bring It On	All	2,982,500	48,910	Utilisation at 103% (2016 Sales)

NOTE: Zero VO Closures under the "Slow and Steady" scenario

* Implies capital spending / contingent liabilities

^ For political rather than efficiency reasons

RESTRUCTURING SCENARIOS -- POWERTRAIN

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Action	Plant	Manned Capacity ^		Headcount	Comments
		Engine	Transmission		
Start Point	All	4,430,000	3,404,700	~15,350	
Stop Transmissions *	Rüsselsheim	-	(175,000)	(800)	Politics OK: preserve most jobs on the site
Stop Engines *	Kaiserslautern	(230,000)	-	(1,000)	Politics OK: Site remains open
Close	Aspern Engine	(600,000)	-	(700)	Politics OK: Site remains open
Slow And Steady	All	3,600,000	3,229,700	12,850	Closer to vehicle production of 3.1m units
Close	Aspern Transmission	-	(1,000,000)	(690)	Complete Site Closure
Convert **	Tychy	(200,000)	1,000,000	-	
Bring It On	All	3,400,000	3,229,700	12,164	Capacity well matched to vehicle production and 3rd party commitments

* Other activities would continue on the site

** Implies capital spending / contingent liabilities

^ Includes announced 2017-18 investments

RESTRUCTURING SUMMARY

- PSA's annual cost saving target of €400 million implies labour reductions of around 6,000 people (or substantial volume improvement)

- Job losses likely to be across both powertrain and vehicle operations
  - Closing Eisenach and Madrid would mean around 3,700 redundancies
  - Partial closure of Rüsselsheim, Kaiserslautern and Aspern costs 2,500 jobs
  - In total, this would be just over 6,000 jobs plus asset write-downs

- A combined PSA / Opel / Vauxhall could go further than this (i.e. towards our "Bring It On" scenario), but for the moment may prefer political stability
  - A recession could change things…

- It's always possible that the €1.6 billion of implementation costs is for something completely different…

In Closing...

PSA'S SAVINGS TARGET LOOKS REASONABLE

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Saving Category	PSA's 2026 Target (€ billions / year)	Our Assessment	Potential Further Savings (€ billions / year)
Material and commodity purchasing	0.5	Achievable / Painless	1.0
R&D and capital spending	0.4	Achievable / Painless	0.4
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Manufacturing costs	0.4 *	Achievable / Painful (5,000 – 6,000 job losses)	0.6 *
	1.7		2.2

* Requires job losses

**Targets Look Achievable And There Are Potential Further Savings.
This Indicates That PSA May Reach Its Savings Goal Earlier Then 2026.**

WHY STOP AT €1.7 BILLION?

- Our Analysis indicates a potential €2.2 billion of savings annually beyond the PSA target, why aren't they talking about that? There are four key reasons:

- Conservatism -- PSA already has a history of setting achievable goals (e.g. average margin targets under "Push to Pass"), why set yourself up to fail?

- Cost headwinds -- PSA implies the €1.7 billion is a net benefit to the bottom line versus 2016, R&D spending and product cost will face new challenges
  - What's to blame? Emission control technology, electrification and autonomy

- Economic headwinds -- PSA and GME have yet to see full effect of Sterling weakening in financial results, recession also possible between now and 2026

- Don't rock the boat -- Our assumptions include footprint actions the management team would likely prefer to avoid unless absolutely necessary

CONCLUSIONS

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- Combining PSA and Opel will create cost savings in a range of categories
- PSA's cost saving target of €1.7 billion per year by 2026 looks reasonable in the context of both the absolute spending levels and historic cost performance
- PSA's statements that job losses may not be required seems unrealistic:
  - Cap Ex savings are in part through reduced footprint and volume needs to grow substantially to reach PSA efficiency targets with today's headcount
  - Likely around 7,000 – 8,000 job losses, including admin staff
- Further savings look achievable -- PSA may be sandbagging or anticipating profit headwinds from trends such as electrification and autonomy
- PSA may feel that there are revenue opportunities, e.g. filling gaps in each brands' portfolio with sister products

ABOUT AD PUNCTUM

AD PUNCTUM

- Consultancy and research firm founded by an ex-automotive OEM insider
- Ad Punctum researches emerging trends and key issues ranging from the disruptive impact of mobility to Brexit
- Ad Punctum likes to make some of its research freely available to drive understanding and debate on interesting topics
- Please contact sales@adpunctum.co.uk or visit www.adpunctum.co.uk to learn more about us and discuss any specific queries you might have

APPENDIX

NOTES ON METHODOLOGY

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Manned and Installed Capacities

- Ad Punctum derives its own assessment of plant capacities based on information around facility installation and headcount levels
- Ad Punctum assumes installed capacity to be running 3 shifts over 5 days but assesses manned capacity on the actual shift pattern at the plant (often 2 shift)
- For powertrain we include in-progress actions (e.g. Trnava, Tychy)

Analytical Financial Assessment

- In order to draw out meaningful comparison, some of the data presented is analytically derived from company financial statements
  - For example, PSA includes Faurecia in much of its financial reporting around manufacturing operations and only gives limited regional-level detail

CREDITS

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