AUTOMOTIVE UPDATE

FEATURE OF THE MONTH

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FEATURE OF THE MONTH

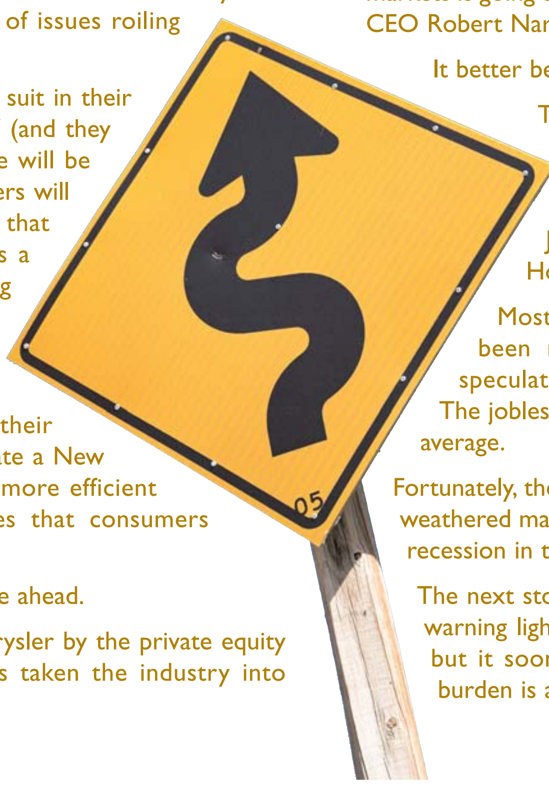
Dangerous Curves Ahead

The U.S. auto industry can scratch the contract negotiations between General Motors and the United Automobile Workers off its lengthy list of challenges.

In a throwback to a bygone era of labor strife, unionized workers stormed off their jobs at GM after talks hit a snag in late September. The nationwide walkout - the first in 37 years -sent 73,000 workers to the picket line. Two days later, a landmark agreement was reached. The key provision of the new contract is an independent, health care trust that would get G.M.'s massive liability off its books.

The quick end to the strike was terrific news for the badly battered industry. They won't have to crimp the supply of strong-selling crossovers or delay the rollout of the Chevrolet Malibu this fall.

Before the settlement, experts had widely predicted that the two sides would reach an agreement, noting that it was in their interest to find common ground to better ensure their survival. Both sides know they have to address a mounting list of issues roiling the industry.



If Ford and Chrysler follow suit in their negotiations with the UAW (and they usually do), a new challenge will be created. American automakers will no longer have the excuse that their health care burden is a barrier to effectively battling the Japanese.

That won't hold water now. Instead, automakers will have to deliver on their promises that they can create a New Detroit, with lower costs, more efficient factories and with vehicles that consumers really want.

That is hardly the only curve ahead.

The recent takeover of Chrysler by the private equity firm, Cerberus Capital, has taken the industry into completely new terrain. There has never been another automaker owned by a private equity firm, and no private equity firm has ever owned such an iconic company.

A slowdown in consumer spending as a result of the fallout from the subprime mortgage crisis is another issue regularly grabbing the media spotlight. The housing market remains depressed. Foreclosures are high. Cars, meanwhile, have a longer life than ever before. Purchasing one is now seen as eminently postponable for people experiencing financial difficulties.

Meanwhile, the recent threats of hurricanes in the Gulf of Mexico has driven oil prices over $80 per barrel. The upward pressure has left gasoline prices near $3 per gallon. Except for short spurts, prices haven't retreated much since Hurricane Katrina smashed into New Orleans two years ago.

Not enough? India's Tata Motors may bid to take over two of Ford's financially plagued luxury brands - Jaguar and Land Rover. Many question whether a takeover by a maker of workhorse trucks and low-end mass-market cars for the two luxury brands would make business sense.

All told, Detroit's Big 3 are facing potentially pinched profits, excess capacity, too many workers and not enough sales. They responded by lobbying for the Federal Reserve rate cuts that took place last month.

"Getting consumer confidence and cash back into the markets is going to be a good thing for everyone," Chrysler CEO Robert Nardelli said recently.

It better be.

The Big 3 market share has tumbled almost 3 percentage points in 2007. Car sales have declined a whopping 13.5%. Truck sales trail 2006 sales significantly. Even Japanese automakers like Toyota and Honda suffered sales declines this summer.

Most major forecasts for new car sales have been reduced. J.D. Power & Associates has speculated that sales won't recover until 2009. The jobless rate in Detroit is five-times the national average.

Fortunately, the Big 3 have always proved resilient. They weathered major storms before, most recently the auto recession in the early 1980s and early 1990s.

The next storm, though, could be the worst ever. The warning light may not be flashing auto recession yet, but it soon might. Reducing Detroit's health care burden is a step in the right direction.

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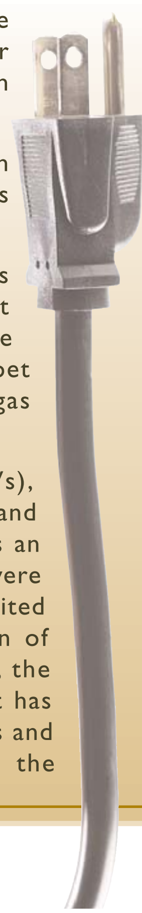
CONCERNING THE CONSUMER

There are nearly 800 million cars currently on the planet. There could be 1 billion cars on the road by 2020, according to the Wall Street Journal. Forrester Research puts the number at 1.2 billion, according to Reuters. It could turn out to be considerably more than that.

What we do know with absolute certainly is that more cars, means more oil. The world currently produces around 84 million barrels of oil a day. Its biggest consumer, far-and-away, is the United States, which consumes around 20.5 million barrels a day. Almost 70% of that goes toward powering transportation needs. According to the Institute for the Analysis of Global Security, world oil consumption will mushroom by 60% between now and 2020.

For most, the nation's dependence on fossil fuels goes beyond fuel prices. The devastating impact oil consumption is having on the air we breathe is a major concern. According to the EDTA, severe air pollution -- which vehicles have been acknowledged to have some role in -- is responsible for anywhere from 500,000 to 1 million deaths around the world annually.



Switching to cleaner cars seems an obvious solution. Unfortunately, that's easier said than done.

One possibility gaining serious attention are electric cars. At least that is the message automakers are sending to consumers as they trumpet plans for cars that can bypass the gas pump.

Backers of electric vehicles (EVs), floated similar ideas in the '70s, '80s, and '90s. But today, almost no one drives an EV. Low-emission, electric vehicles were always rejected by automakers, who cited a lack of demand. But with a gallon of premium gas frequently topping $3, the push to get EVs back on the market has come to a shove. And with carmakers and entrepreneurs pouring money into the latest generation of EVs, the prospects appear brighter.

Trading the internal combustion engine for batteries could bring well-publicized advantages: reducing pollution, raising mileage and promoting energy independence. EVs could deliver the gasoline equivalent of 100 miles a gallon or more. For consumers, that would in effect roll back the clock to buck-a-gallon gas. Car owners could save money in their sleep, recharging in the off hours, when electricity is cheapest.

And compared with hydrogen fuel-cell cars, the infrastructure for electric cars already exists, requiring only more plugs in more places. Aside from home recharging, it would be easier to install pay-per-use outlets at curbsides and in parking lots than to spawn a network of hydrogen filling stations.

There are, however, problems. There is still not a single EV or plug-in hybrid available that can approach the driving range, interior room and performance of a typical gas-powered family sedan, at anywhere near the price that an average consumer would pay.

Experts say the EV arrival hinges on a number of issues:

- *Developing safe, affordable lithium-ion batteries lasting 100,000 miles.*
- *Overcoming a psychological barrier among people who can imagine the benefits, but can also see themselves stranded with a dead battery.*

Ultimately, EVs may be just one part of a whole no-emission alternative. Other options on the table include: hybrid cars, plug-in hybrid cars and fuel cell cars. Any one of them will involve investing heavily in new infrastructure.

What's clear is that such practical, affordable cars are on the way. Many believed that the development of "plug-in hybrids" - electric cars, with gas-engine backups - are the more immediate solution.

The problem is that people may be ready for them now

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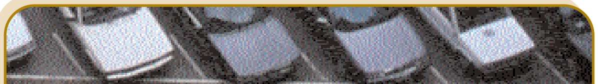

ON THE ADVERTISING FRONT

There's a strange, new phenomenon going on at luxury auto dealerships around the United States. Would-be-buyers are being spotted displaying surprised and even puzzled expressions as they stroll through premium-marquee, showrooms that were always known for the prestigious aura emanating from their high-end, luxurious models.

In an attempt to enlarge their consumer bases, esteemed carmakers are attempting to appeal to young buyers who yearn to own extravagant vehicles, but cannot yet afford to do so. To that end, Mercedes-Benz, Volvo and BMW are diversifying their lineups mightily. They are now set to offer, amazingly enough, loads of quite affordable models.

The quandary for these companies is maintaining their lofty images among core consumers, while also luring a younger, edgier demographic.

Mercedes C-Class (MSRP starting at $31,975) and Volvo's C30 hatchback ($22,700) have different approaches in dealing with this relatively new class of cars, which are now widely known as "lower luxury."

Mercedes says the recent launch of its C-Class is its biggest ever. Last month, they broke out network TV spots titled "Why?" and "Why?/Performance." The ads highlight engineering and handling, with no explicit overtures to a younger demographic. The seven-week campaign includes a significant Web presence and a flurry of ride-and-drives. It targets men and women 30-45 with an average household income of $110,000. Mercedes is on course to far-outspend the $204 million they spent advertising these cars last year.

Volvo, conversely, is airing 16 three-minute humorous Webcasts titled Mr. Robinson's Driving School, to support the C30's October launch. The episodes, on MSN.com, features Craig Robinson (from NBC's comedy The Office) "teaching" young adults how to drive a C30.

Volvo's approach could damage the overall brand if current and traditional potential owners see the automaker diluting its product. A disconnect could certainly occur if owners are going to see this as a reflection of the brand they are driving. Volvo said a typical C70 driver likely wouldn't see the Internet ads for the C30. The C30 push seeks males 28-38 making under $100,000. This groups spends much of their free-time on the Internet.

None of the luxury carmakers want to forfeit their gilded status for the sake of marketing their lower luxury cars. These automakers, with their long histories and legendary brand names, must tread with caution by not overproducing or overselling these automobiles.

Such hype could, conceivably, turn off an upscale, young buyer. These consumers already aspire to get into a BMW or a Mercedes. Historically, these company's believed interested consumers would bend over backwards to put these cars within their financial reach. With that in mind, luxury car dealers did not see a need to come up with unusual gimmicks.

That's no longer the case.

BMW will soon join the fray. They are preparing for the rollout of the 2008 1-series. It is expected to hit with a starting MSRP of about $30,000. Dealers placing orders now are already complaining about the small number being allocated - 40,000 for the entire U.S. Marketing for its official launch will not target the typical BMW driver. Creative will launch online and via event marketing, before TV hits late in the year.

Saab plans to roll out a lower luxury vehicle in 2010

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MONTHLY AUTOMOBILE SALES CHART

Automobile Manufacturers	September 2007	September 2006	Percent Change*	Year-To-Date	Percent Change
Audi of America	8,021	8,044	-0.3%	68,479	2%
BMW of North America	20,488	18,239	12.3%	233,120	20%
BMW brand	16,457	15,275	7.7%	200,046	21%
MINI brand	4,031	2,964	36.0%	33,074	15%
Chrysler Group	159,799	168,888	-5.4%	1,578,823	-8%
Chrysler brand	38,668	47,211	-18.1%	408,677	-9%
Dodge division	83,671	79,784	4.9%	806,477	-14%
Jeep	37,460	41,893	-10.6%	363,669	4%
Ford Motor Company**	189,850	238,876	-20.5%	2,029,026	-19%
Ford division	155,037	204,077	-24.0%	1,667,821	-20%
Jaguar	1,031	1,158	-11.0%	11,987	-43%
Land Rover	4,190	3,469	20.8%	36,074	19%
Lincoln	9,764	7,362	32.6%	102,449	-2%
Mercury	11,403	13,119	-13.1%	129,743	-35%
Volvo	8,425	9,691	-13.1%	80,952	-8%
General Motors	338,644	338,380	0.1%	2,970,973	-22%
Buick	17,754	19,463	-8.8%	143,945	-29%
Cadillac	20,398	20,217	0.9%	154,983	-9%
Chevrolet	194,637	190,825	2.0%	1,748,548	-25%
GMC	44,754	39,141	14.3%	381,238	-8%
Hummer	5,080	6,739	-24.6%	42,754	-30%
Isuzu	1,004	1,397	-28.1%	9,349	-12%
Pontiac	31,817	37,376	-14.9%	276,589	-27%
Saab	2,424	3,069	-21.0%	25,685	-11%
Saturn	20,776	20,153	3.1%	187,882	-10%
American Honda Motor Co.	127,190	116,226	9.4%	1,238,486	-7%
Acura division	14,369	16,323	-12.0%	136,726	-21%
Honda division	112,821	99,903	12.9%	1,101,760	-5%
Hyundai Motor America	33,214	33,384	-0.5%	358,407	-8%
Kia Motors America	24,087	23,877	0.9%	232,043	1%
Mazda North America	25,098	20,261	23.9%	218,379	0%
Mercedes-Benz USA	22,459	19,873	13.0%	172,026	-1%
Mitsubishi Motor Sales	12,102	10,287	17.6%	113,065	-14%
Nissan North America	94,269	88,340	6.7%	806,993	2%
Infiniti division	10,250	10,378	-1.2%	93,573	-10%
Nissan division	84,019	77,962	7.8%	713,420	3%
Porsche Cars of N. America	2,641	2,216	19.2%	25,880	1%
Subaru of America	16,457	16,128	2.0%	138,620	-18%
Suzuki Motors	7,653	7,940	-3.6%	82,000	-1%
Toyota Motor Sales USA	213,043	182,950	16.4%	2,001,681	-7%
Lexus division	25,114	25,700	-2.3%	244,653	1%
Toyota division	187,929	157,250	19.5%	1,757,028	-8%
Volkswagen of America	27,062	28,332	-4.5%	193,375	15%
Preliminary Total	1,322,077	1,322,241	0.0%	12,461,376	-12%

Sources: Advertising Age, September 13, 2007; Automotive News, September 17, 2007 and September 24; Auto Channel, September 25, 2007, Brandweek, September 17, 2007; CNN Money, September 25, 2007, CNN World Business, September 16, 2007; The New York Post, September 25, 2007, The New York Times, September 23, 2007; The Wall Street Journal, September 27, 2007.

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