

# **Recent Developments in the Automotive Supplier Industry in Japan and the EU**

December 10th 2004

## **Changes in OEM Purchasing Policy in Japan:**

**Some Suggestions from an International Comparison of Financial Data**

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# Purpose of this Report

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- Presenting the general characteristics of OEM purchasing policies and its changes after 90s in Japan
- Presenting some impacts of such changes on the automotive and auto-parts industry based on an international comparison of financial data
- Presenting some impacts on the relationship between OEMs and parts-makers in Japan
- Presenting the rationalization in Japanese auto-parts industry which advanced to cope with OEM purchasing policies and survive
- Finally presenting some issues based on the above

# Changes in OEM Purchasing Policy in Japan

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## General characteristics of OEM purchasing policies in Japan

- Price of auto-part is decided through the continual negotiations to adjust target cost of OEM and quotation of parts-maker
- Usually requesting price down regularly from OEMs to parts-makers
- Support from OEMs to parts-makers for achieving target cost and cooperative problem solving between them
- In contracts between OEM and parts-maker there is room of ambiguity for continual KAIZEN
- OEMs make contacts with parts makers maintaining cooperation among different functional divisions(ex. purchase, design and production)
- OEMs inspect work processes and operation standards in details during their visits to parts-makers

# Changes in OEM Purchasing Policy in Japan

## Changes in OEM purchasing policies in and after 90s in Japan

- Early 90s
  - Rationalization after bubble economy: standardization of parts and reduction of purchasing cost
  - Development of relations between OEMs and parts-makers beyond KEIRETU
- From middle to late 90s
  - Construction of global purchasing data base
  - Introducing global sourcing strategy
- From late 90s to early 00s
  - Efforts for modularization
  - Global platform strategy and reducing the number of suppliers
  - Establishing joint worldwide purchasing organizations with foreign capitals
  - Introducing cost reduction programs by Toyota and Nissan



# Changes in OEM Purchasing Policy in Japan

## Two programs with big impacts

### ■ Nissan Revival Plan (Oct. 1999)

- 20% cost reduction over 3 years
- Centralize parts and material purchasing
- Reduce the number of suppliers: 1145 → under 600
- Partnership with competitive global suppliers
- Using common benchmarking tools with Renault

### ■ CCC21 in Toyota (July 2000)

- 30% cost reduction over 3 years (1 trillion yen)
- Re-evaluating cost and benefit from design phase for improvement
- Verification of competitors for comparison
- From cost reduction based on comparison with existing models to cost reduction based on comparison with others

→ Shift to “most competitive cost in the world”

# Changes in OEM Purchasing Policy in Japan

## Reality of Japanese OEM purchasing policies in the world

- Price setting based on global benchmark and requesting quality equivalent to that of Japan in the world
- Fusion between Japanese way of quality requirement and Euro-American way of price setting based on market competition

## Some cases

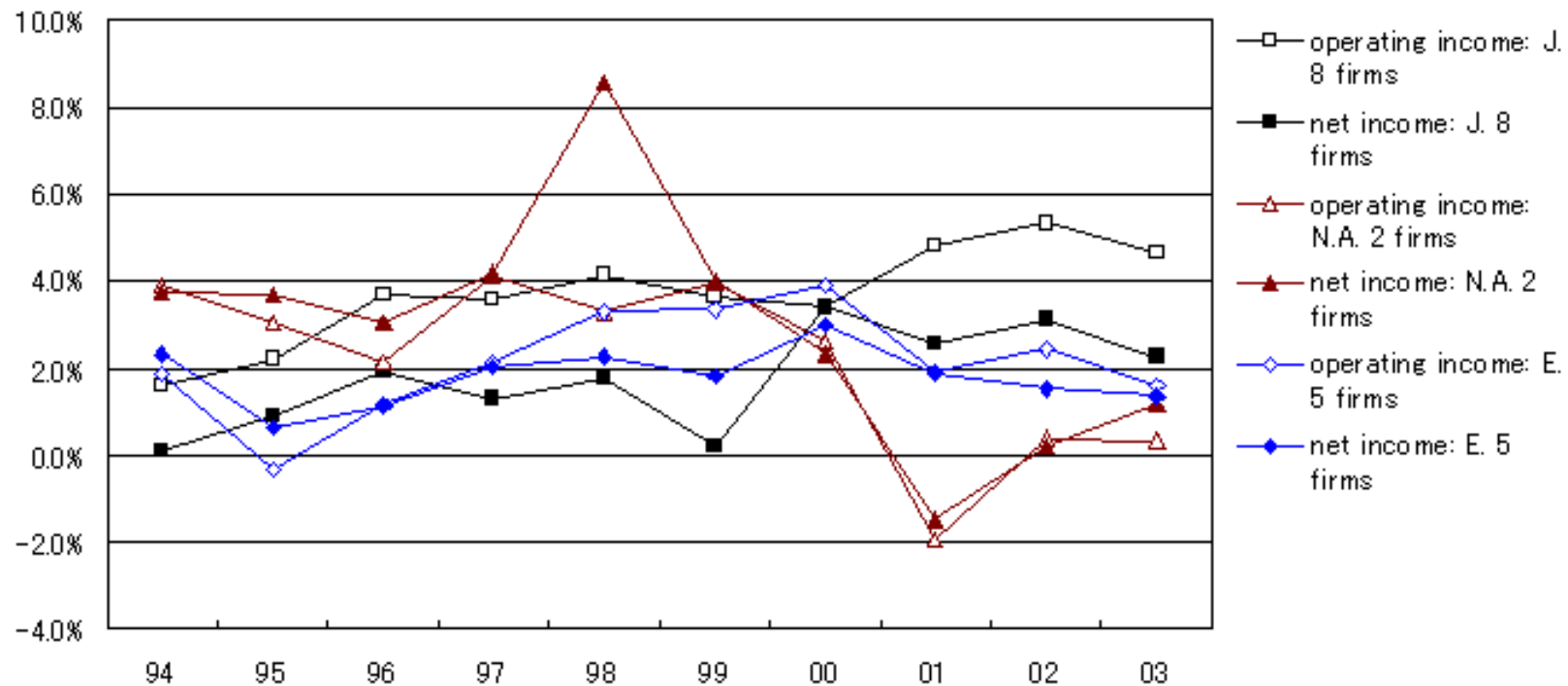
- Gathering information globally using internet, then requesting cost reduction based on it(a case of North America)
- Requesting a 20% reduction from the price in Japan in spite of the same design and quality as in Japan(a case of China)
- Requesting price down based on global benchmark, but changing partner suddenly after presented lower price is very rare(a case of Japan)

# International Comparison of Financial Data:

## Impacts from Changes in OEM Purchasing Policy in Japan

### ■ International comparison of profit rate in OEMs

Table 3-1 Operating income to net sales ratio and net income to net sales ratio in OEMs (consolidated)



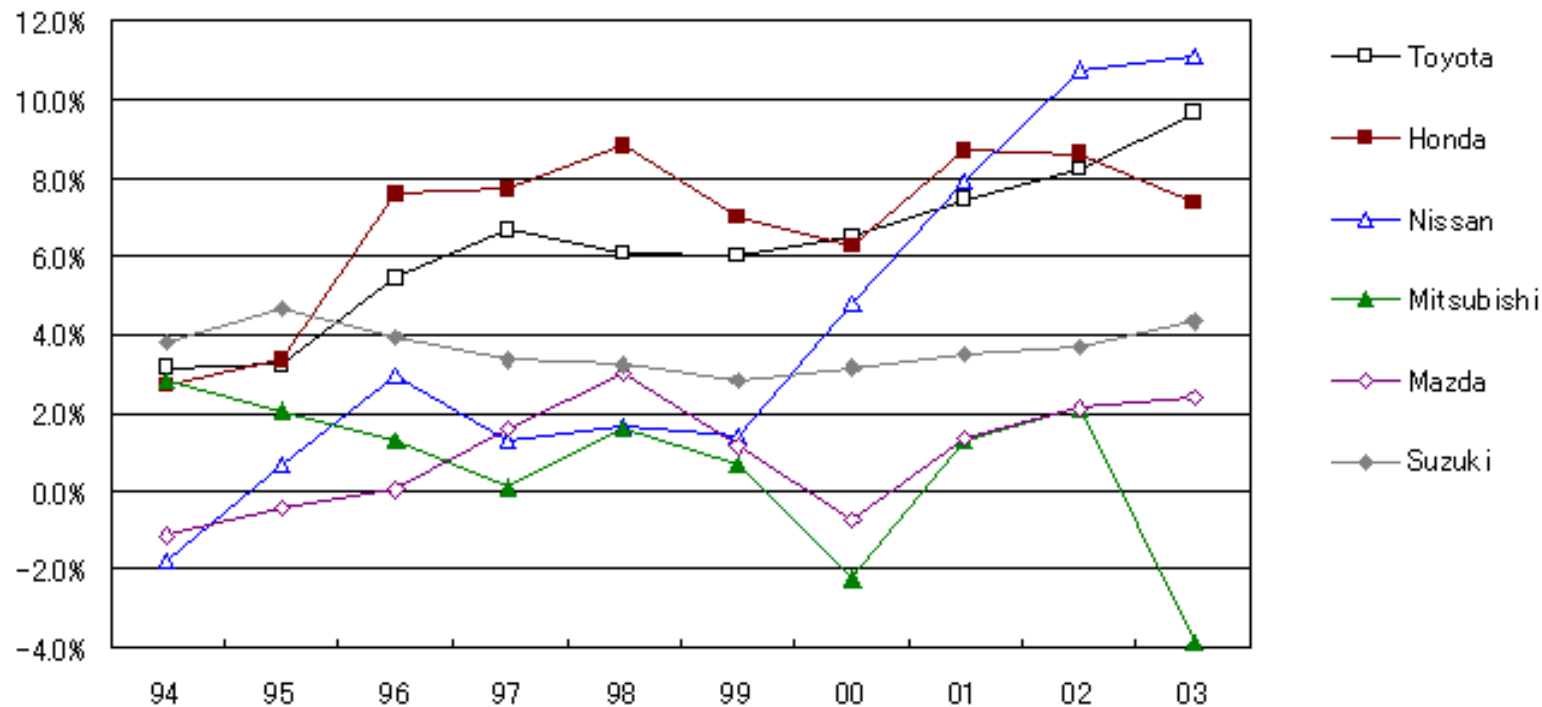
Source: Financial data of each firm.

# International Comparison of Financial Data:

## Impacts from Changes in OEM Purchasing Policy in Japan

### ■ International comparison of profit rate in OEMs

Table 3-2 Operating income to net sales ratio in Japanese OEMs  
(consolidated)



Source: Financial data of each firm.

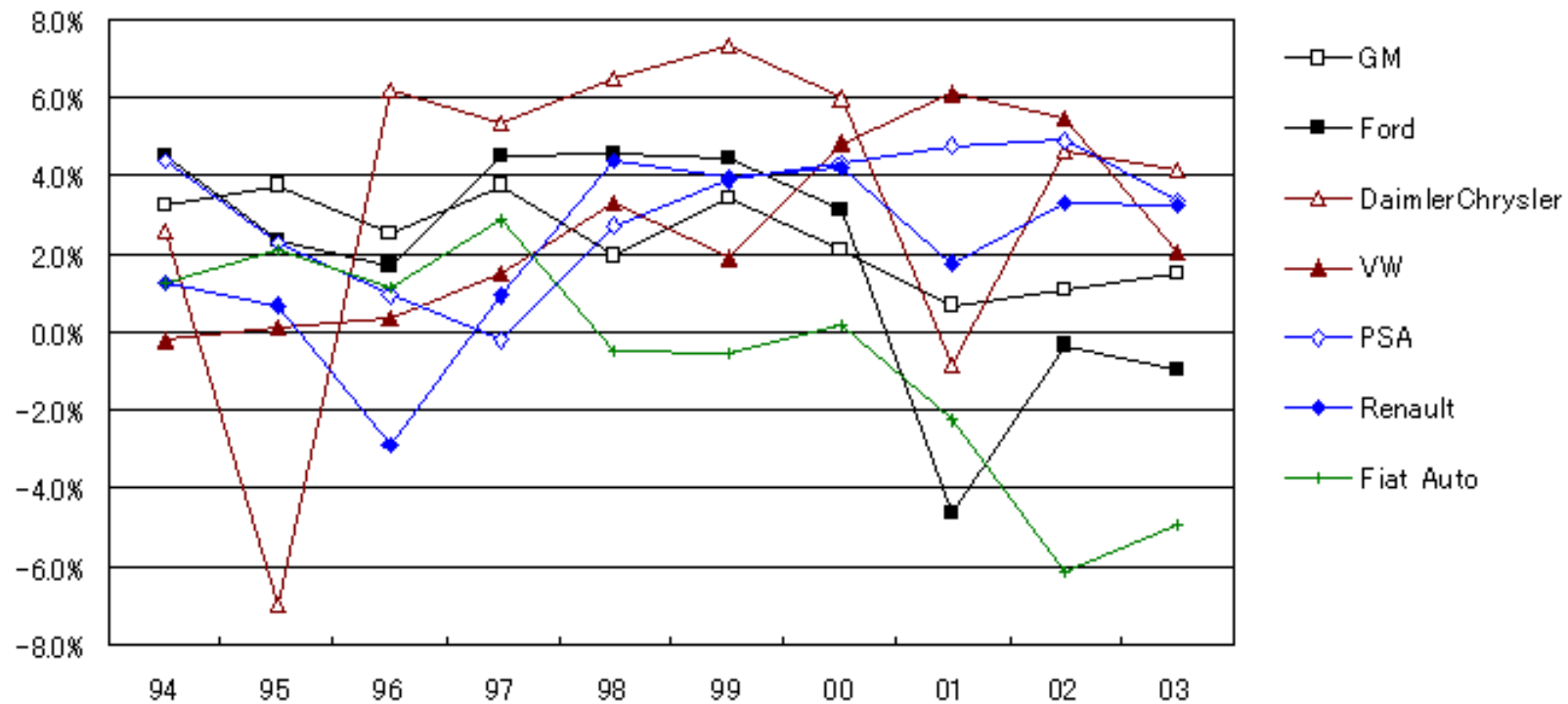


# International Comparison of Financial Data:

## Impacts from Changes in OEM Purchasing Policy in Japan

### ■ International comparison of profit rate in OEMs

Table 3-3 Operating income to net sales ratio in Euro-American OEMs (consolidated)



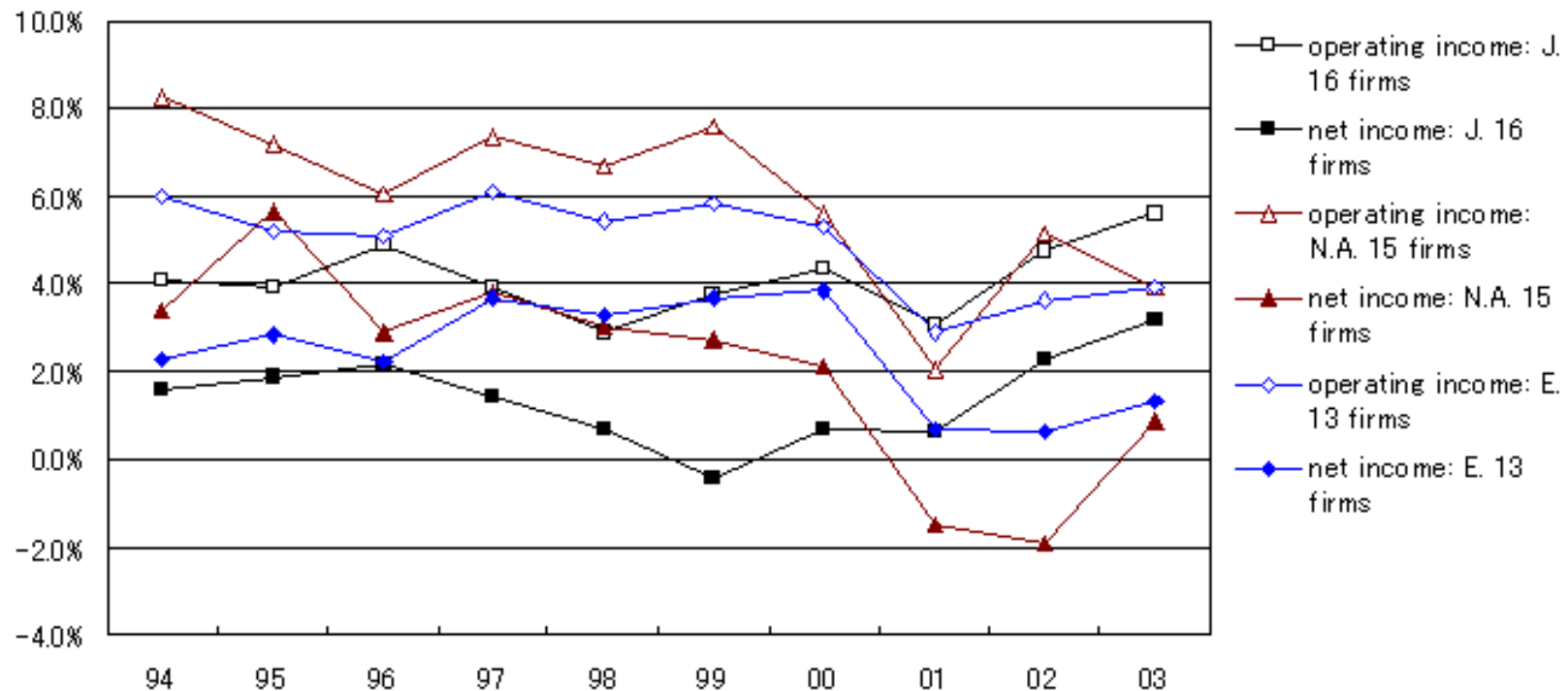
Source: Financial data of each firm.

# International Comparison of Financial Data:

## Impacts from Changes in OEM Purchasing Policy in Japan

### ■ International comparison of profit rate in Parts-Makers

Table 3-4 Operating income to net sales ratio and net income to net sales ratio  
in Parts-Makers (consolidated)



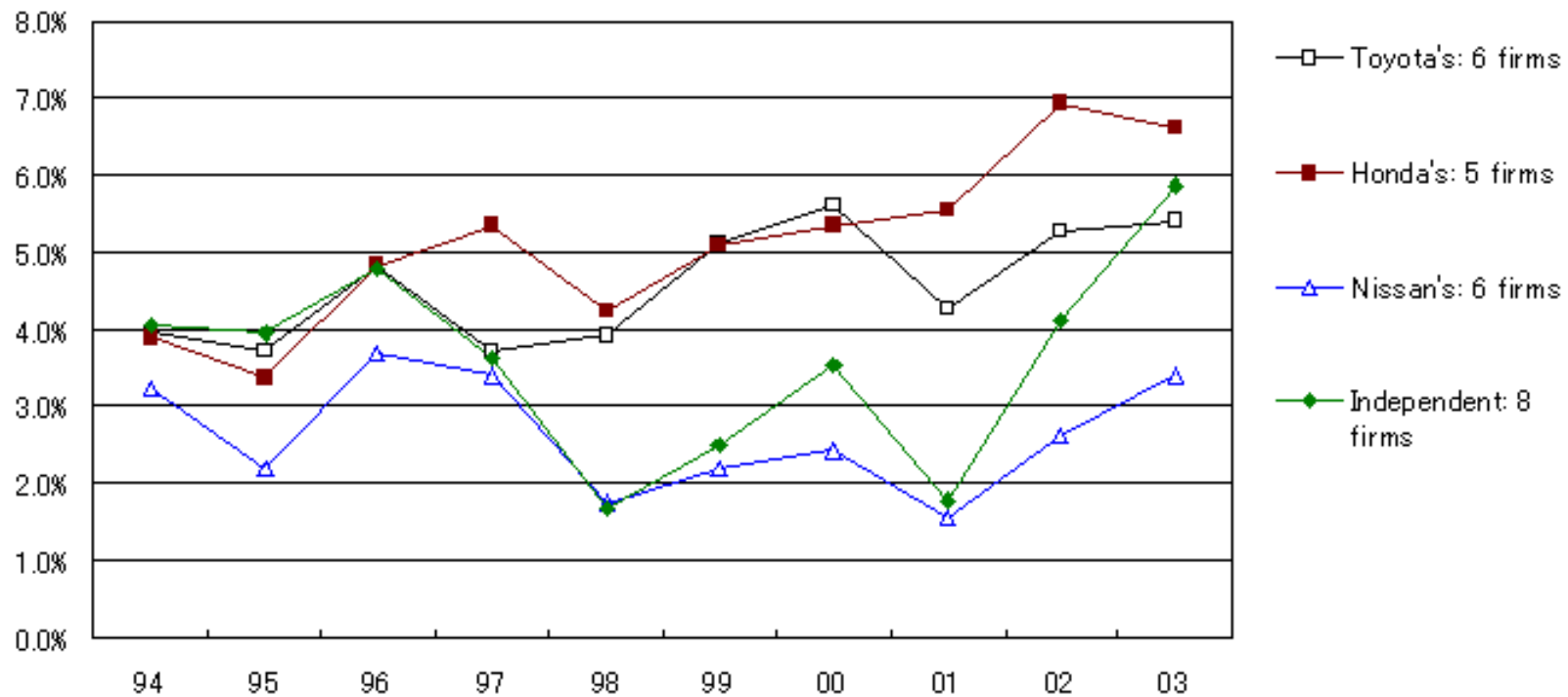
Source: Financial data of each firm.

# International Comparison of Financial Data:

## Impacts from Changes in OEM Purchasing Policy in Japan

### ■ International comparison of profit rate in Parts-Makers

Table 3-5 Operating income to net sales ratio in Japanese Parts-Makers (consolidated)



Source: Financial data of each firm.

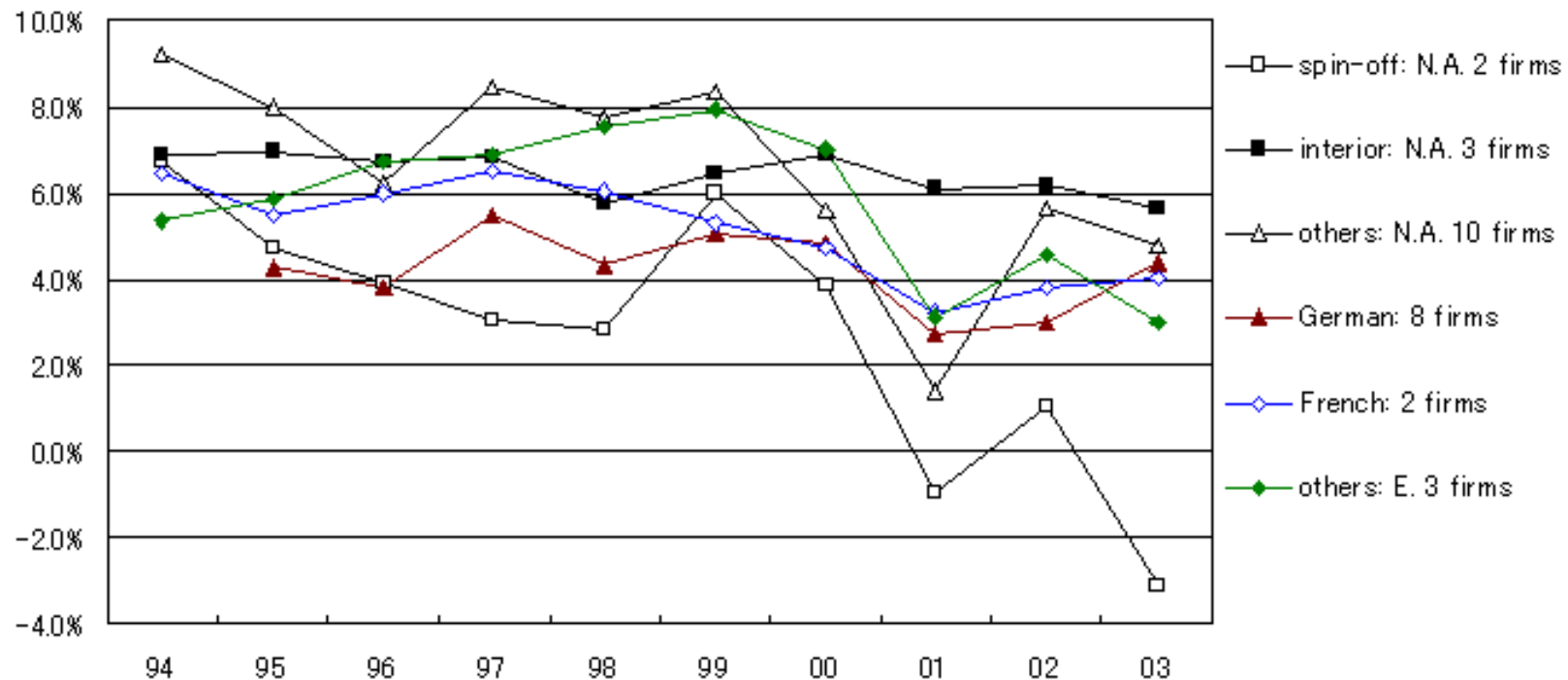
# International Comparison of Financial Data:

## Impacts from Changes in OEM Purchasing Policy in Japan

### ■ International comparison of profit rate in Parts-Makers

Table 3-6 Operating income to net sales ratio

in Euro-American Parts-Makers (consolidated)



Source: Financial data of each firm.



# International Comparison of Financial Data:

## Impacts from Changes in OEM Purchasing Policy in Japan

### American OEMs in extreme difficulty

- Incentive (July 2004)  
from *Nikkei News*  
Paper, 2004, 8.27.

	Brand of lowest incentives		Brand of highest incentives	
First	Mimi(BMW)	\$80	Cadillac(GM)	\$7,878
Second	Saion(Toyota)	\$212	Lincoln(Ford)	\$5,480
Third	Porsche(Porsche)	\$257	Jaguar(Ford)	\$5,248
	Japanese: 8/10, European: 2/10		American: 9/10, European: 1/10	

- Quality (Problems per 100 Vehicles for one model)  
from *Consumer Reports*,  
April, 2004, p.17.

	Brand of smallest problems		Brand of largest problems	
First	Lexus	9	Lincoln	31
Second	Infiniti	10	Jaguar	30
Third	Honda	10	Hummer	26

- New purchase policies in GM and Ford
  - GM gives suppliers tough terms that GM will switch suppliers after 30 days notice in case of the price higher than rival's (*Automotive News*, Dec.1 2003)
  - Ford gives suppliers tough terms that Ford will deduct funds from a supplier's account without notice, unilaterally charge suppliers half of a product recall's costs and terminate a contract for "any or no reason" (*Automotive News*, Feb.16 2004)

# International Comparison of Financial Data:

## Impacts from Changes in OEM Purchasing Policy in Japan

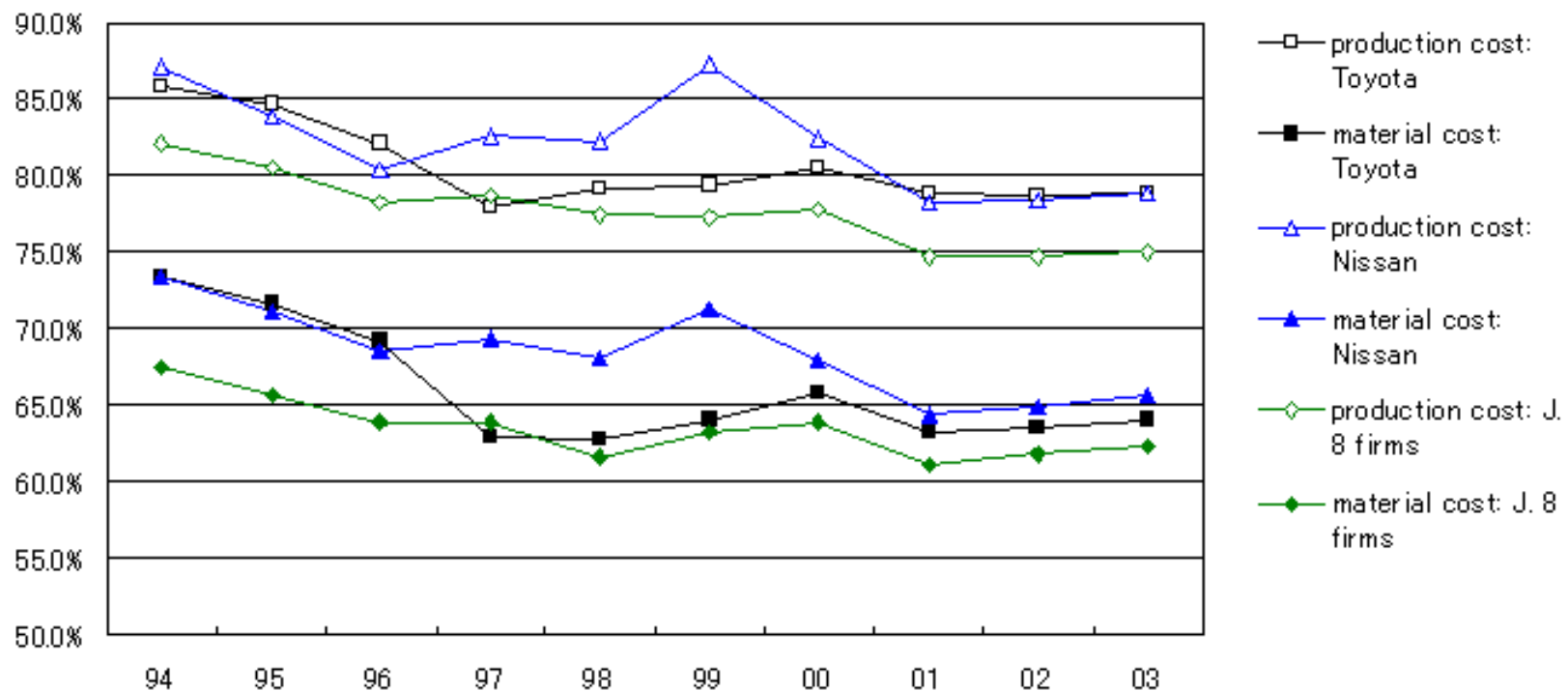
### Overview

- Toyota, Honda and Nissan have achieved positive earnings after 2000
  - New OEM purchase policies in Japan such as CCC21 and NRP have produced the desired effect
- Parts-makers in Japan also have achieved positive earnings
- Profit ratios of Euro-American OEMs are in falling tone , especially American OEMs are in extreme difficulty
- Profit ratios of Euro-American parts makers also are in falling tone
  - Because of the tough requirements of OEMs
- Relationship of mutual trust between OEM and parts-maker is undermining. Ex. some parts-makers won't sign the Ford contract (*Automotive News* July.19 2004)
- Global competitions have become intensified
  - = “Japanese quality level and lowest cost in the world”

# Impacts on Auto-Parts Industry in Japan

## ■ Relationship between OEMs and Parts-Makers in Japan

Table 4-1 Production cost to net sales ratio and material cost to net sales ratio  
in Japanese OEMs (non-consolidated)



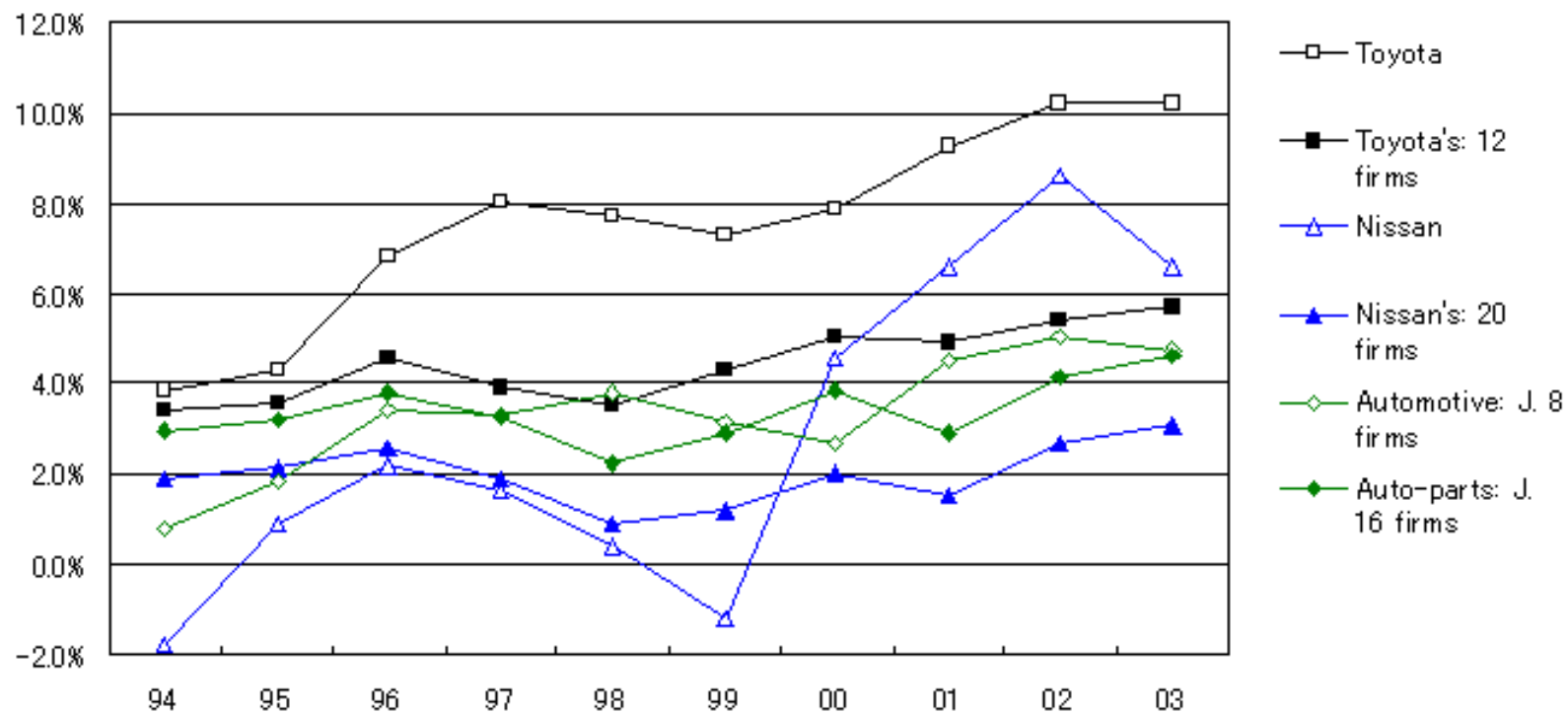
Source: Financial data of each firm.

# Impacts on Auto-Parts Industry in Japan

## ■ Relationship between OEMs and Parts-Makers in Japan

Table 4-2 Ordinary income to net sales ratio

in Japanese OEMs and Parts-Makers (non-consolidated)



Source: Financial data of each firm.

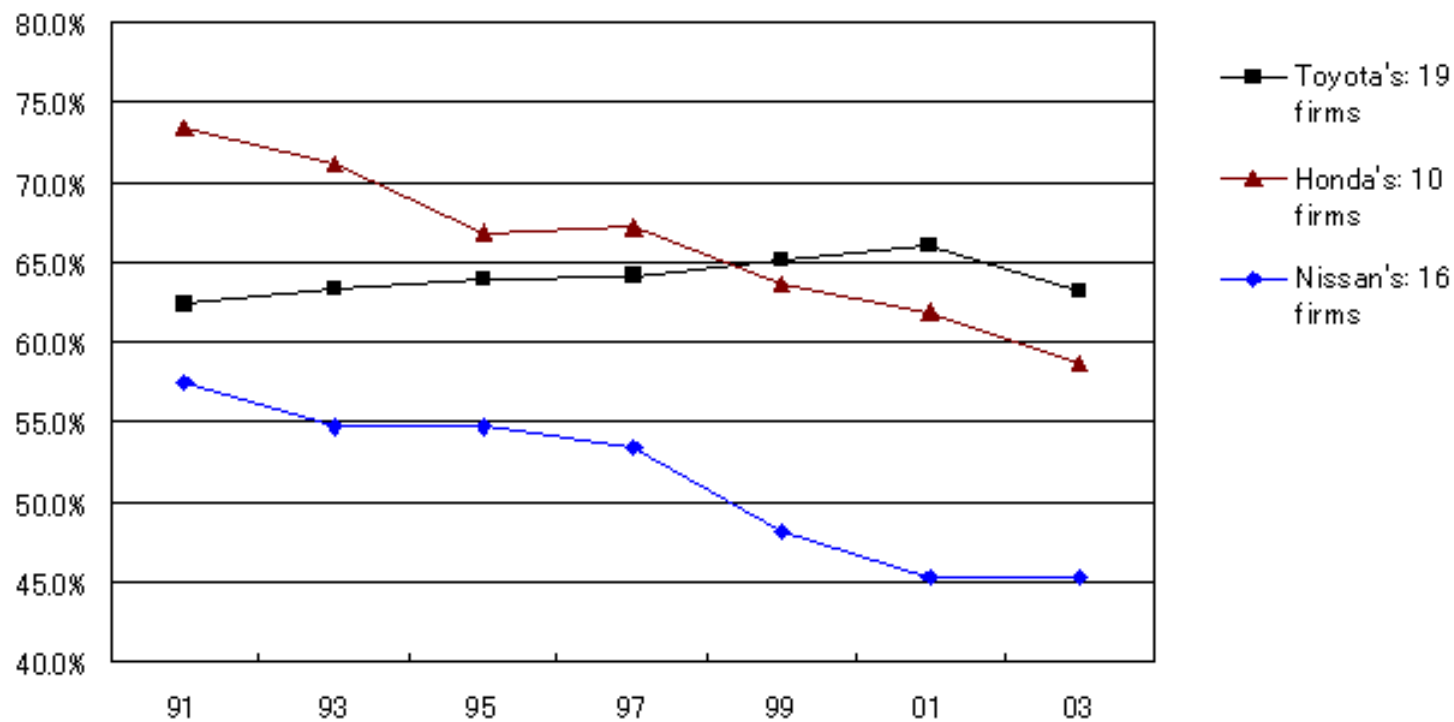


# Impacts on Auto-Parts Industry in Japan

## ■ Relationship between OEMs and Parts-Makers in Japan

Table 4-3 Degree of dependence on main customer

by Japanese Parts-Makers (non-consolidated)



Source: *Japanese Automotive Parts Industry, 91-04.*

# Impacts on Auto-Parts Industry in Japan

## ■ Analysis of Japanese Parts-Makers whose main customer is Nissan

Table 4-4 Shareholding ratio of Nissan in 35 firms

Nissan's shareholding ratio	1982	1989	1999	2001	2003
50% or more	6	6	4	3	2
25% - less than 50%	20	18	17	9	4
10% - less than 25%	9	11	11	10	2
less than 10%	0	0	3	13	27

Note: 35 firms that Nissan's shareholding is 10% or more in 1982.

Table 4-5 Some basic data in 73 firms

	1982	1989	1999	2001	2003
Employee number	1,012	1,068	1,004	914	813
Net sales(million yen)	33,541	41,866	44,921	46,366	49,313
Ratio of ordinary income to net sales	3.2%	2.7%	1.2%	3.2%	3.5%
Net sales per employee(million yen)	25.4	31.9	35.2	38.6	44.0

Source: IRC, *Nissan Group No Jittai*, 83, 91, 00, 02, 04.

# Impacts on Auto-Parts Industry in Japan

## ■ Analysis of Japanese Parts-Makers whose main customer is Nissan

Table 4-6 Transition of some basic data

1. Transition of employee number (1999=100%)					
Employee number (2003)	1982→89	1989→99	1999	1999→01	2001→03
1,000 or more (15 firms)	89.2%	93.0%	100.0%	94.7%	85.9%
500-999 (19 firms)	116.3%	122.6%	100.0%	88.9%	78.6%
100-499 (33 firms)	128.8%	135.6%	100.0%	95.7%	78.3%
less than 100 (5 firms)	144.4%	157.4%	100.0%	83.0%	76.5%
2. Transition of net sales (1999=100%)					
Employee number (2003)	1982→89	1989→99	1999	1999→01	2001→03
1,000 or more (15 firms)	70.5%	86.4%	100.0%	107.0%	116.8%
500-999 (17 firms)	74.5%	95.9%	100.0%	96.1%	94.0%
100-499 (27 firms)	96.0%	115.7%	100.0%	94.1%	94.4%
less than 100 (2 firms)	99.1%	148.5%	100.0%	80.9%	65.0%
3. Net sales per employee (million yen)					
Employee number (2003)	1982	1989	1999	2001	2003
1,000 or more (15 firms)	30.3	41.6	44.2	50.5	58.7
500-999 (17 firms)	23.6	29.2	35.7	39.4	43.5
100-499 (26 firms)	23.9	28.2	30.7	31.6	37.0
less than 100 (2 firms)	21.6	27.8	28.1	32.0	30.3

Source: IRC, *Nissan Group No Jittai*, 83, 91, 00, 02, 04.

# Conclusion

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## Consequence of the change in OEM purchasing policy in Japan

- Global competitions intensified
  - “Japanese quality level and lowest cost in the world” is getting global standard
- Cutting down of profit ratio in American OEMs and introducing new purchasing policies
  - Escalation of tough requirements to parts-makers
- Continual rationalization in Japanese auto-parts industry and concentration of business to larger firms
  - Fear of hollowing-out in small and medium-sized parts-makers which have supported Japanese manufacturing industry
- Need for reconsidering ways of fair and trustful relationship between OEMs and parts-makers
  - Need for developing an argument globally