QUARTERLY
BBK Review
WINTER 2008

Manufacturing in Mexico: *Gearing up for Growth*

by Richard Leal, Senior Director

In February, BBK Managing Director Guy Morgan presented one of BBK's many success stories of an engagement in Mexico at the RESA conference. RESA is the Evaluation and Review of Automotive Association forum sponsored by Bancomext, along with INA, the Mexican Association of Automotive Parts Manufacturers. According to INA, an organization that represents over 1,000 Tier One suppliers, Mexico can expect to increase its automotive GNP from its current value of approximately $35B to $78B by 2015 and $118B by 2030, clearly making automotive Mexico's number one industry.

INA also reported that in 2007, Mexico's vehicle exports increased 4.2 percent over 2006, primarily due to the Japanese OEMs (Honda, Nissan and Toyota) as well as Volkswagen. Another contributing factor is the strategic location of Mexico with its free trade agreements with the U.S., Canada, Japan, Europe and most of the South American countries. It is INA's view that this upward trend will continue (INA membership is expected to grow to more than 2,000 suppliers by 2015 and 3,000 by 2030) and consequently, the Mexican auto parts industry has been rapidly gearing up for its next stage of growth.

Paving the way for this substantial industry growth has required significant preparation and ample resources. In 2005, the Mexican government, under the direction of President Felipe Calderon, created a policy council called **ALITEC AUTO** (ALITEC). This council in the Ministry of the Economy represents an alliance between government, academia and the automotive industry, represented by INA and AMIA (the Automotive Manufacturers International Association which is comprised of OEM corporations doing business in Mexico). On the academia side, various Mexican universities are represented by FUMAC, the US-Mexico Foundation for Science. Interestingly, FUMAC is studying a proposal funded by the Ministry of the Economy to develop incubator companies in the U.S., possibly in the Detroit area, which would allow these companies to create business partnerships with U.S. Tier Ones.

ALITEC created an organization known as **A3P**, or the Automotive Alliance for Improving Productivity and Overall Enterprise Competitiveness, which linked the Ministry of the Economy, Bancomext and several leading OEM and Tier Ones together to address the challenges ahead and to ensure Mexico's supply base is ready to produce vehicle subsystems with high value-add content. These Tier Ones include Nissan, Sanluis, Magna, JICA (Japanese International Cooperation Agency) and TRW.

As anticipated, challenges were revealed as a result of a study conducted by the Ministry of the Economy in February 2007, which indicated that Mexico's automotive supply base needed to improve its global competitiveness in cost, quality and delivery. The report also stressed if Mexico is to be successful in building a large export-dominated supply and assembly business, investment has to occur not only in infrastructure, but also

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ANNOUNCEMENTS

BBK is proud to announce the following team additions:

Frank Bunte, Manager
Frankfurt

Walter Crate, Managing Director
New York

Vijay Erasala, Manager
Chicago

Robert Jennings, Associate
Detroit

Patti Mohr, Executive Assistant
Detroit

Michael Petrik, Senior Director
Frankfurt

Grace Zhu, Manager
Shanghai

BBK is proud to announce the following promotions:

James Downes, Manager to Director

Marcus Hudson, Manager to Director

Josh Hunter, Analyst to Associate

Tim Monahan, Director to Senior Director

Bruno Ricciuti, Associate to Manager

Mark Ripple, Manager to Director

Tim Turek, Senior Director to Managing Director

Andrew Zeleney, Associate to Manager

IN THIS ISSUE

For more information on any of the articles shown here, please contact marketing@e-bbk.com

CASE STUDY

Winery Sale is a Go

There are 20 million acres of vineyards in the world producing 62 million tons of grapes each year. About 8 billion gallons of wine are made from those grapes. The biggest wine producers worldwide are France (19 percent), Italy (17 percent), Spain (13 percent), and the United States (9 percent). California produces 90 percent of all the wine in the United States.

Microsoft® Encarta® Online Encyclopedia 2007

BBK was recently retained by the Official Committee of Unsecured Creditors in the bankruptcies of 360 Global Wine Company and its wholly-owned subsidiary, 360 Viansa LLC.

Shortly before the Chapter 11 filing, management had been replaced. An onerous DIP loan facility was negotiated with the senior secured lender after the filing had already taken place.

BBK was charged with determining whether the winery, on which capital expenditures were being funded from the DIP loan facility, could be turned around. The capital expenditures had not yet resulted in any material improvement in operating performance. Management's plan was to rebuild and refinance the winery business for the ultimate benefit of all its creditors.

Time was of the essence as the Bankruptcy Court had imposed a strict deadline on the filing of a Plan of Reorganization. In addition, funds to pay professionals were seriously constrained.

BBK's specialists in the wine industry quickly determined that the debtor's financial records could not be relied upon as indicators of potential future performance, that management's business plan was highly optimistic and that management lacked the skills and access to capital necessary to enhance the enterprise's value beyond the level of the senior secured debt and the balance outstanding on the DIP loan.

BBK urged the debtor to revise its business plan and accelerate the sale process that had recently been initiated while at the same time negotiating for some nominal recovery for the unsecured creditors. The winery was sold to the senior secured lender pursuant to a Plan of Reorganization that also paid a large convenience class of unsecured creditors a 25 percent dividend. ■

AEROSPACE

Commercial Aircraft Industry Continues Record Growth

by Alexander Craig, Managing Director

Unlike the automotive industry, the commercial aircraft industry is presently operating at record levels. Sustained growth in the civil aircraft market boosted the aerospace industry in 2007, taking total sales to yet another record level. More aircraft were delivered in 2007 than in any of the previous 25 years, even as the order backlogs for new airplanes continued to grow.

In the business and general aviation segment, the General Aviation Manufacturers Association reported industry record sales totaling \$21.9B and delivery of 4,272 new aircraft in 2007. New business jet deliveries accounted for more than 25 percent of the total, a 28 percent increase over 2006.

In the air transport segment, Boeing Commercial Aircraft reported record sales of \$33.3B and delivery of 441 new aircraft in 2007. Airbus likewise, reported record delivery of 453 new aircraft. Both Boeing and Airbus also reported record level future delivery backlogs of \$255B and \$157B respectively, including the largest pre-certification order book in history for the new Boeing B787 Dreamliner with over 857 orders to date.

DID YOU KNOW?

BBK's Aerospace Practice has the expertise and experience to help clients drive productivity and profitability improvements including:

- Supply Chain and Manufacturing Effectiveness
- Lean Manufacturing/Continuous Improvement
- Quality Operating System/ Performance Measurement

But can these manufacturing companies keep up with their ever increasing order books?

In the business and general aviation segment, Cessna led the industry in new aircraft deliveries with 1,274, totaling \$3.91B in revenue. However, they also had a backlog that grew to a record \$11.9B at year end 2007. New orders for a Cessna Citation jet today may wait three or more years for delivery of a new aircraft.

In the air transport segment, the Boeing B787 Dreamliner aircraft is experiencing critical parts and supply chain issues, resulting in certification delays. First B787 deliveries have been delayed from 2008 into 2009. This will impact operating profits of B787 customers as the new aircraft will replace less efficient ones currently in their fleets.

A truth that many may not realize, is that significant operational improvement opportunities exist to increase production rates and efficiencies that could address these record backlogs. Successfully increasing production rates and improving productivity will provide the additional benefit of improved quality and make historically *good* financial results into truly *great* results. ■

Source: General Aviation Manufacturers Association, Boeing, Textron, and Airbus

VIEW FROM EUROPE

European Automotive Manufacturing Goes East

by Manfred Schönleber, Managing Director European Operations Group Lead

For many years "Made in Germany", "Produit en France" or "Built with Pride in UK" were valid arguments for vehicle buyers. "Made in" and its European equivalents have lost their value in the last 20 years. "Engineered in" has replaced it since, while today "Engineered by" is the only important factor for mass production customers. There is little appreciation left for where a vehicle is actually built. This is increasingly true even for premium manufacturers.

Fierce competition among manufacturers in Europe has forced a price war that could only be sustained by reacting with products manufactured at lower cost for a given design.

For European OEMs this frequently meant shifting the manufacturing and sourcing footprint steadily from the west to the east. This move started shortly after the end of the Cold War period and the demolition of the Iron Curtain in the early nineties with peace between the Eastern and Western blocks, opening new business across borders.

Most OEMs started to motivate their suppliers to open Greenfields or upgrade existing local Brownfields using the significant labor cost differential between Western and Eastern European countries.

Although pure labor cost differentials are not that meaningful, it is the availability of an educated, highly motivated workforce with ambitions to move from low-tech/agricultural industries to high-tech industries such as automotive. In these countries, labor cost ranges from less than 10 percent to 40 percent of German labor cost for comparable work. For this range, there are more than seven countries where such rates can be contracted: Czech Republic, Slovakia, Poland, Hungary, Romania, Bulgaria, Ukraine and Russia.

We frequently hear the argument that wages are challenged by the local unions for increases of up to 10 percent annually. Simple math would tell you that even adding 10 percent each year on labor rates would take multiple model cycles before these rates would meet the current Western levels, which during the same period of time may also see annual increases of 1-3 percent.

But again, lowest cost does not count if productivity and quality are not up to world class standards. True unit labor cost should be the factor compared. However, given the fact that most OEMs have global standards for labor allocation and quality, new plants with new people will quickly reach these levels. Even if labor is at a lower cost, it does not mean that employees are hired in excess which would lead to overstaffing, at least not too long after start-up and reaching peak volume. Some of the booming regions of these countries are already experiencing a shortage of skilled workers—and retaining trained people is critical.

From my own observations, I can state that these Greenfields, on average, incorporate the latest principles of lean, both in manufacturing and the supply chain. The investment in machinery and equipment is state-of-the-art and typically differs only with less automation, wherever manual work can replace machines and not create a quality risk.

Nothing is more flexible for product change, volume fluctuation or manufacturing sequence than manual work. The right balance is essential.

People are hired and trained with these principles rather then retrained, since most of them come from other career paths or industries to join the automotive world.

Suppliers are the first ones to move to new territories, frequently asked by their OEM customers to move there and create sustainable cost advantages in order to stay price competitive long-term.

Most European OEMs have sourcing targets for low cost countries, such as a certain amount of material to be sourced by a defined timeframe. Some leave the selection of countries to their supplier, others prefer the supplier to move to certain countries where the OEM has its own assembly plant or is planning to go in the future.

Some European OEMs already have more than 40 percent of all purchase value coming from these "new" countries, with plans in place to exceed 50 percent with new models starting from 2010.

According to Ron Harbour Associates, there is still significant improvement potential among existing OEM facilities in Western Europe. Ron Harbour was recently quoted in German Automotive Week claiming existing data shows compact cars can be assembled in less than 15 hours (Nissan, UK) compared to more than 30 hours per vehicle (Volkswagen, Germany) with comparable content.

New Greenfield plants are and will be erected in countries like Slovakia and Czech Republic (Kia/Hyundai) as well as in Russia (Toyota, Ford, VW, GM/OPEL/Chevrolet, BMW, Fiat, Renault, and others), with the vision to follow the growth in new markets. However, these plants could create plus-capacity in Europe, while the overall demand in Europe will not drastically grow. Existing Western plants will be challenged with each new model as to where it will be built. Plants will compete with each other more severely than in the past—this process will have winners and losers.

For the most part, they will find a developed local supply base, and if not, they must make sure there is one to support localization from day one. More than 70 percent of these suppliers are either global players with their own plants or JVs with existing suppliers that need to be raised to international standards using foreign investment.

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Mexico

in improving technical and engineering skills of its supplier to provide the OEMs total systems, not just components, and move from current technology to more advance technologies.

Another hot topic during the RESA conference and significant challenge for Mexico is the intense competitive pressures of China and India. For example, according to INA studies and reports, the globalization plans of multinationals still favor China. To combat this and compete globally, as Guy Morgan indicated in his presentation, supplier development, such as training the Mexican workforce in lean principles, establishing a team environment, and viewing the entire enterprise value chain (not just the manufacturing plant) will be essential. Further, to impact this globalization plan, the government of Mexico, with a consortium of government ministries, must provide incentives to promote foreign direct investment.

"Despite the challenges, sourcing from Mexico will continue its upward trend... but suppliers must be ready."

Fortunately, the Ministry of the Economy has endorsed using the United Nations Development Program as an internationally accepted process for supplier development in Mexico, according to newly installed AMIA president Eduardo Solis. This is critical since it could allow ALITEC to receive government funding to strengthen the Mexican supply base by providing financial assistance to obtain experienced advisory firms like BBK to help them become more competitive.

Despite the challenges, sourcing from Mexico will continue its upward trend and the industry will continue to grow but suppliers must be ready. In a 2007 Bancomext conference in Dearborn, Alejandro Farias, manager of the economic studies at INA, discussed that sourcing from Mexican suppliers typically involves one or more of the following reasons: high ratio of weight to value, quality intensive product, industries that require just-in-time delivery and experience frequent design changes, protection of intellectual property, and/or technological turnover.

Additionally, Farias stated that OEMs continue to rationalize production in the region based on plant location, availability and cost of inputs such as labor, raw materials, energy and capital, as well as the structure, length of the supply chain and the proximity to the local market. These factors have combined to make sourcing from Mexico very attractive to the Southeast U.S. automotive corridor—and as stated earlier, a trend that is likely to continue and strengthen.

Suppliers will need to maintain a strong focus on total enterprise solutions and improved productivity that will help solidify their global competitive advantage. The Ministry of the Economy, working with INA and the AMIA, are committed to develop results in these areas, and again, through ALITEC, potential access to government funding means that suppliers may finally have the critical financial support needed to train people in lean principles and improve their manufacturing processes. If this moves forward, suppliers should quickly identify and secure the right partners to help them get to the next level.

When selecting a partner, it is our view that suppliers choose those firms with ample experience and a solid track record of working in Mexico. They will benefit most from a firm that intimately understands the Mexican culture and its 62 indigenous groups, as well as one that has solid working relationships with all the key constituents driving its automotive sector.

For a copy of Guy Morgan's presentation or for more information regarding BBK's qualifications in Mexico, contact marketing@e-bbk.com ■

EXPANDING LEADERSHIP

Walter Crate joins BBK in New York as a Managing Director in the Corporate Advisory Group. He has forty years of extensive professional experience in the areas of investment banking, restructurings, asset and value identification and realization for a wide variety of industries including aerospace, automotive, consumer goods, manufacturing, and transportation and logistics.

To contact Walter:
212.572.6284 or wcrate@e-bbk.com

INDUSTRY EVENTS

BBK voiced its thought leadership at the following industry events:

January 31, 2008 Dow Jones Distressed Opportunities Summit, Pierre Benoit, Managing Director, participated on the panel "Industry Spotlight: Real Estate".

January 31, 2008 TMA Detroit Meeting, Tim Monahan, Senior Director, participated on a panel discussing "Troubled Loan Workouts".

February 6, 2008 TMA Toronto Symposium, Ken Munn, Managing Director, participated on the panel "Automotive Industry Supply: Is the End of the Turmoil in Sight?".

February 21, 2008 Distressed Real Estate Investing Summit, Greg Coppola, Senior Director, moderated a panel on "Opportunities in Foreclosed Real Estate".

February 27, 2008 Turnaround Management & Distressed Investing Forum, Tim Turek, Managing Director, spoke on "Issues and Opportunities in the Auto Industry".

March 12, 2008 Commercial Finance Association's Spring Connections Conference, William G. Diehl, President and CEO, presented "Automotive: A Distressed Industry Sector".

For information on upcoming events, contact marketing@e-bbk.com

LETTER FROM BBK

Starting New in Music City USA

On November 1, 2007, BBK set up shop in Nashville, Tennessee in response to the evolving, more regionalized needs of our clients. As a firm known for providing experienced support with a high degree of urgency, it was important for us to improve our geographic position and to live up to our reputation! It is a win-win situation—in addition to providing better support for our clients, establishing a presence in the Southeast enhances our opportunities for growth.

As we delved into our expansion, we began to experience an interesting dynamic. BBK's "starting new" meant that many in the region would not be familiar with our capabilities. Obviously, we would have to undertake an effort to build and increase awareness of BBK, with the clear upside of this activity being our continued liberation from some old "stereotypes" and "misnomers". We are extremely proud to be a firm that has been around for over 30 years. However, because our roots are in automotive and we have a strong track record in that industry, many people wrongly assume that we are limited to that specific business. The fact is that BBK's core competency is manufacturing, regardless of industry, and the skills and experience of our growing team has enabled us to successfully expand into other areas, such as health care, distribution, real estate and retail.

BBK's advisory activity surrounding performance improvement and supply base risk management clearly creates the most interest today. The recognized need is at an all time high—poor quality, delivery, scrap, downtime and other operational issues can no longer be accepted or tolerated for any length of time. Companies now understand that these performance issues tend to be the first "warning signs" of financial trouble ahead. It's important for these companies to realize that continuous financial *and* operational monitoring is essential and any delays in solving operating issues (internally or externally) will contribute to customer dissatisfaction, drain manufacturers financially, and/or increase supplier-generated risk.

For BBK, the decision to expand our presence in the Southeast and to make our home Nashville was initially one of logistics and client support (and perhaps a little music on the side!). As we have further explored the market and have had the opportunity to meet with local business and community leaders, we also realize the tremendous opportunity we have to fulfill a need throughout the region—helping great manufacturers who are struggling or just looking to perform better, given the current operating environment.

Early this summer, BBK will host an educational summit in Nashville, bringing together a diverse group of influential and knowledgeable subject matter experts to discuss a wide variety of important topics such as continuous improvement/industry best practices, distress, bankruptcy and turnaround opportunities in the Southeast, investing, foreign relations and more. This summit is another example of how we hope to bring value to the community.

Thanks to everyone who has already graciously welcomed BBK to the South. We are excited to work with you and those of you who we are sure to soon meet.

For more information regarding our services and activities in the Southeast, please feel free to contact me at 731.445.1493.

Keith Updike
Senior Director

BBK PE POWERTRAK

A new, regular feature in the BBK QR!

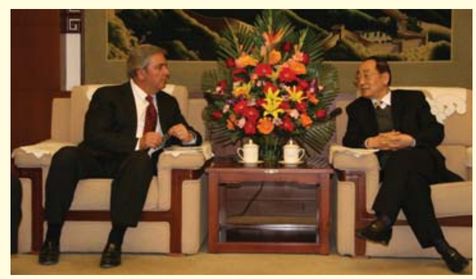
Top Five International Private Equity Firms in Automotive Related Deals:

Current Equity Investor	# of Auto Investments
3i Group Plc	24
COFIDES, S.A.	14
Carlyle Group	12
Court Square Capital	9
Group Siparex	8

Source: Capital IQ as of First Quarter 2008

BBK PE PowerTrak identifies monthly changes and activities relative to private equity firms with significant automotive related investments. For more information on PE PowerTrak, contact marketing@e-bbk.com

BBK AROUND THE WORLD



BBK President and CEO, William G. Diehl, met with Mr. Bao Xuding, President of China International Engineering Consulting Company (CIECC) in December 2007 to discuss the opportunities of a cooperative business relationship.

CIECC is the leading engineering consulting service in China, and is responsible for approving all projects in China that involve a large amount of government investment.

For more information on CIECC, visit www.ciecc.com.cn

BBK Managing Director and North America Operations Advisory Group Lead, Guy Morgan, stands with Ramon Suarez, Executive President of INA (Mexico's Automotive Parts Manufacturers Association) in February 2008 after Guy presented at the Automotive Sector Evaluation Forum in Mexico City.

For more information on INA, visit www.ina.com.mx

VIEW FROM EUROPE

European Manufacturing *(continued)*

According to Ron Harbour's quote again, only the best combination of productivity, quality, and supply base capability, with the lowest possible logistics cost, will determine future competitiveness and survival in vehicle manufacturing.

Imagine the competitive position for lean plants built in these low cost countries with the available local supply chain costing, on average, 25 percent less than compared to traditional countries.

Even premium manufacturers' facilities will only survive long-term if they use all improvement opportunities that exist to become lean and procure parts under the best conditions.

We have observed the caravan steadily moving from country to country, from west to east during the last 10+ years. There is no indication that this trend will end anytime soon. Although we see wages going up in the East at rates unseen in Western regions, it will take many years before the lines will cross, given the absolute starting point for wage increases in Eastern countries.

For global suppliers, such as Bosch, Denso, Magna, Continental and others, going east is a copy-paste exercise of the many expansion plants around the world, since they have all the intelligence needed to successfully build and start up.

It is the increasing number of midsize, often owner-operated companies that will struggle when faced with all the new challenges including culture, language, habits, ethics and laws. Their pool of talent for such undertakings is often very limited, especially without previous foreign country exposure. ■

DID YOU KNOW?

- BBK assists companies that decide not to build facilities in new countries in becoming lean and in maximizing operations in order to stay competitive.
- BBK supports midsize companies who move east with:
  - -Project/Program Management
  - -Plant Readiness
  - -Launch and Ramp Up

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