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"Impressions from the Detroit Auto Show"

I went to my first Detroit Auto Show in 1958 as a very young Windsor boy looking to kill a Saturday with my older brother. Believe me, the show has changed a lot over the years.

It is now called the North American International Auto Show (NAIAS) and this international aspect is perhaps the biggest change in the show over the years. GM, Ford and DCX still dominate in terms of space and press interest - after all we are in Detroit.

But with a few exceptions, the entire global auto sector comes to Detroit each January with the very best of their new and future product offerings. And product is what it really is all about. Of course there is the networking and the entertainment and it's a place to be seen but if you want to understand Detroit you need to understand the role of product in our industry.

The show demonstrates the importance of product in many ways. The most obvious is the $300 million dollars in cars and light trucks that are on the show floor. There are also dozens of concept vehicles shown each year, most of which will never see the light of day. However, many of the design cues built into these vehicles do evolve into marketed product.

In addition, any negative buzz about a particular product influences the end product we eventually see in the show room. The OEMs host more than 12,000 media and industry insiders at this show and they listen to what these people have to say. OEMs closely follow the chat rooms and other discussions to understand whether they have hit the mark with their products.

One of the lesser known activities in Detroit each year are the dozens of financial analyst meetings held with Wall Street, Bay Street and various OEMs and OE parts producers. For instance, long after most media people had gone home, GM met with the financial community and what they had to say to investors was not pretty. GM provided 2005 earnings per share (EPS)

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guidance of $4.00 to $5.00 vs. $6.00 to $6.50 anticipated in 2004.

GM also indicated it no longer expects to achieve its original earnings target of $10 by mid-decade. Management attributed the bulk of the anticipated lower earnings outlook (versus 2004) to higher health care and pension expense benefits, continued weakness in Europe, and slightly lower earnings coming from its finance arm, GMAC, due to the rising rate environment.

Management at most OEMs also have a realistic view of the difficult landscape they face and also recognize that there are limited strategic options. For GM, Ford and DCX the strategy is very clear and it starts in Detroit.

...there was no lack of new product at the 2005 NAIAS in Detroit.

Barring a tear-up of their UAW/CAW contracts, they must take the long road out of their difficulties. This involves a number of factors: driving volume by any means to maintain market size in North America and thus prevent their legacy costs from rising; maintaining a liquid, if leveraged, balance sheet; focusing more on product; and riding the growth wave in China.

Under this scenario, the top-down pressure on the entire automotive value chain will likely continue. The rapid pace of discounting may slow in 2005 as OEMs try to claw back the pricing that has

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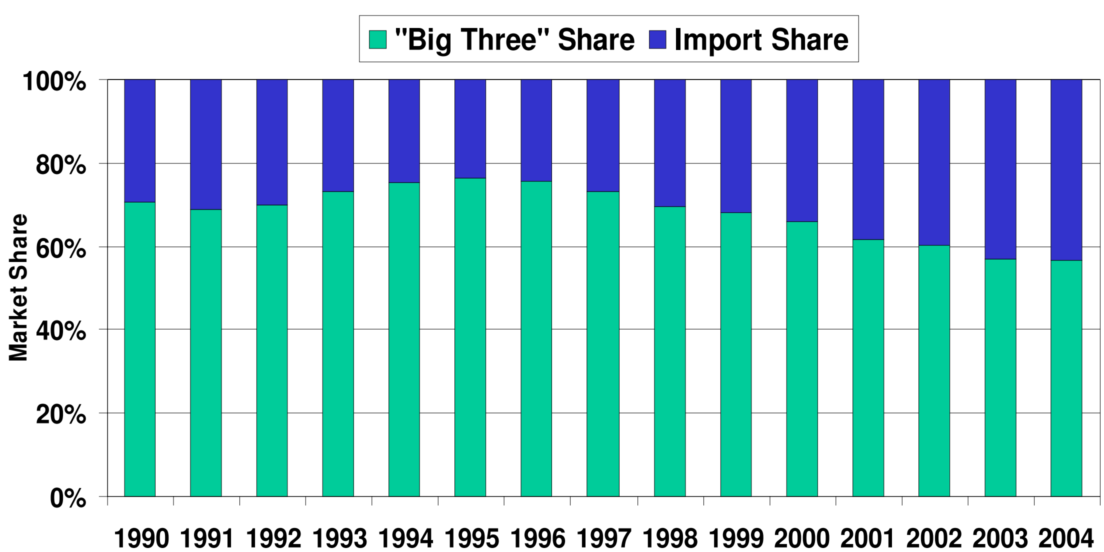
Canadian New Vehicle Market Share
"Big Three" vs. Import Nameplates



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been lost over the last three years. But this is likely to be a temporary event unless there is a big upswing in the economy, which is the most significant demand variable.

However, significant economic improvement is questionable. High incentives will in fact support unit volumes, but the result is continued pressure on the entire automotive value chain's margins from the top down. Additionally, increasing input costs, specifically raw materials and health care, will create pressure from the bottom up.

On the input side of the equation, costs - including health care and raw materials - will likely continue their upward trend in 2005. New highs for some raw materials, and health care costs are probable in 2005. On top of all this, the industry continues to struggle with excess capacity.

Revenue growth is the only way out of this box and that brings us right back to the Detroit Auto Show. The fix for GM and Ford and DCX, of course, is product and that is why 12,000 media and auto analysts come to Detroit each January. They want to see how the OEMs are meeting the challenge.

Product is how most OEMs get themselves into difficulties and product is how most OEMs can get themselves out of trouble. Witness the successful positive impact of the 300C on DCX.

Without a doubt, there was no lack of new product at the 2005 NAIAS in Detroit. In fact, there was so much new product that the show was somewhat confusing and - believe it or not - boring. There just wasn't the buzz that we have seen at previous shows. I believe this is because most new product has become uniformly spectacular. The bar has been set so high that we are almost immune from any OEM being "over the top" with what they are showing. In addition, OEMs are increasingly unveiling product in advance of the show. The result is that, with a few exceptions, there was little in Detroit this year that we had not already seen.

...2005 may be a watershed year for the Canadian automotive industry.

Never before has there been so much new product in the pipeline and ironically, this factor may result in some challenges for vehicle companies and dealers in Canada. The main difficulty for companies will be to differentiate themselves within this new-product-crowded landscape. Consumers will benefit from the amount of choice available, but paradoxically, too much choice causes confusion.

Product distinctions, or unique selling propositions, are essential to successful marketing. But automotive product differences are becoming blurred and this includes vehicle categories. What now, for example, is

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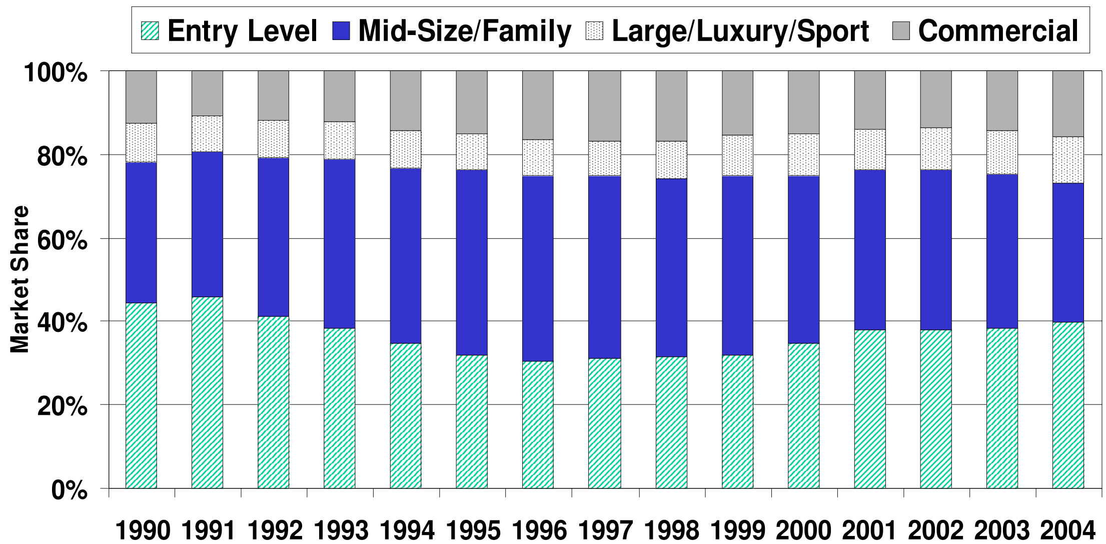
Canadian New Vehicle Market Share



Source: DesRosiers Automotive Consultants Inc, CVMA and AIAMC

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the difference between a car and a light truck? I'm serious! The Dodge Magnum looks like a station wagon to me but it is classified as a luxury sport utility. Where do we position the many crossover vehicles being introduced? The Hyundai Tucson is a sport utility but it is built on a car platform. What is the definition of a luxury vehicle when dozens of vehicles could be considered luxury based on their specifications? The Ford Five Hundred is considered a small luxury unit but has the price tag of an intermediate passenger car.

While each new product is important, some vehicle launches in Canada will be more critical to their parent vehicle companies than others. 2005 will be a key year for Volkswagen as they launch the new Jetta and Passat. The arrival of a new Civic at Honda is always an important event. Kia will launch the new Rio, which is a very important vehicle to them and the Canadian subcompact market in general. The Mazda5 will place Mazda in a unique position as the only purveyor of a sporty compact van. GM will be watching closely as the recently launched Cobalt, Pursuit, and redesigned minivans filter through the market.

Not that long ago OEMs were predicting fuel cell vehicles for 2010.

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Canadian Light Vehicle Market

Year	Total Market	Entry Level	Entry Level Share	Mid-Size/ Family	Mid-Size Family Share	Total Large/ Luxury/ Sport	Large/ Luxury/ Sport Share	Primarily Commercial	Primarily Commercial Share
1990	1,285,788	573,457	44.6%	432,275	33.6%	119,538	9.3%	160,518	12.5%
1991	1,266,482	582,803	46.0%	437,100	34.5%	110,971	8.8%	135,608	10.7%
1992	1,204,348	495,362	41.1%	459,481	38.2%	108,505	9.0%	141,000	11.7%
1993	1,164,677	448,625	38.5%	471,190	40.5%	102,753	8.8%	142,109	12.2%
1994	1,224,949	426,281	34.8%	514,380	42.0%	109,150	8.9%	175,138	14.3%
1995	1,130,211	362,019	32.0%	500,784	44.3%	98,639	8.7%	168,769	14.9%
1996	1,173,090	356,416	30.4%	521,253	44.4%	101,260	8.6%	194,161	16.6%
1997	1,387,950	432,918	31.2%	605,770	43.6%	113,156	8.2%	236,106	17.0%
1998	1,389,126	435,705	31.4%	592,599	42.7%	124,746	9.0%	236,076	17.0%
1999	1,501,099	476,927	31.8%	647,882	43.2%	142,236	9.5%	234,054	15.6%
2000	1,549,441	536,797	34.6%	623,570	40.2%	154,435	10.0%	234,639	15.1%
2001	1,570,629	598,691	38.1%	599,990	38.2%	153,729	9.8%	218,219	13.9%
2002	1,703,246	648,709	38.1%	650,341	38.2%	169,583	10.0%	234,613	13.8%
2003	1,593,506	610,554	38.3%	585,870	36.8%	166,980	10.5%	230,102	14.4%
2004	1,534,415	609,622	39.7%	512,712	33.4%	170,770	11.1%	241,311	15.7%
Change	**-3.7%**	**-0.2%**		**-12.5%**		**2.3%**		**4.9%**	

Source: DesRosiers Automotive Consultants Inc., AIAMC and CVMA

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I believe 2005 may be a watershed year for the Canadian automotive industry. We are in a very saturated vehicle market and moving new product in 2005 is going to cost money. Lots and lots of money. Incentives are a given. Canadian consumers expect some form of incentives and at the very least will demand OEM financing that beats the bank by a good margin.

To avoid the possibility of a key new model being lost in the flood of new product, companies will have to put some exceptional and costly resources behind product launches to get the word out. Marketing budgets will increase, with the majority of the money being spent on new product launches. Vehicle companies will be looking for the biggest bang for their buck, with the result that media outlets will have to seriously begin looking at non-traditional methods of advertising like ride and drives to attract these marketing dollars.

Both the environment and the consumer may win.

The small amount of new product suitable for the Canadian market was noticeable at the show. The total entry-level segment (including subcompact and compact cars) was 40 percent in Canada last year, almost four times larger than the large/luxury/sport segment that was emphasized at the show. The lack of product in Detroit targeted to this

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segment is particularly worrisome.

The OEMs are pouring enormous amounts of money into concepts and super cars but in my view they are sacrificing the more realistic and higher volume part of the market. This was particularly the case for GM, Ford and DCX. Not only did they have no production vehicles on the floor that fit into the entry-level segment, but also there was no indication, from their concepts, that they are leaning in that direction. I cannot help but feel this reaffirms my opinion that in some areas, the energies of the traditional Detroit Majors would be better focused on making improvements to existing products rather than putting so much of their effort into new "blockbuster" category entries.

This year there was much more focus on diesel-electric with at least three companies showcasing prototypes....

However, we do have to give them credit for their efforts to recover in the mid-size car business, as with the Ford Fusion and Dodge Charger. As for the import players, Volkswagen launched their next-generation Jetta and Kia appears to be serious about making an impact in the subcompact market with its Rio entry.

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Canadian New Vehicle Market - Big Three vs Import Nameplates

Year	Total Market Big Three	Total Market Big Three Share	Total Market Import Nameplate	Total Market Import Nameplate Share	Total Market Japanese Nameplate	Total Market Japanese Nameplate Share
1990	906,572	70.5%	379,216	29.5%	305,163	23.7%
1991	872,593	68.9%	393,888.50	31.1%	323,647.50	25.6%
1992	843,345	70.0%	361,003.22	30.0%	299,059.22	24.8%
1993	852,132	73.2%	312,545.08	26.8%	251,755.08	21.6%
1994	923,347	75.4%	301,601.99	24.6%	234,375.93	19.1%
1995	863,338	76.4%	266,873	23.6%	204,037	18.1%
1996	888,555	75.7%	284,535	24.3%	218,230	18.6%
1997	1,016,452	73.2%	371,498	26.8%	297,059	21.4%
1998	965,953	69.5%	423,173	30.5%	329,458	23.7%
1999	1,021,831	68.1%	479,268	31.9%	364,677	24.3%
2000	1,023,955	66.1%	525,486	33.9%	383,173	24.7%
2001	965,349	61.5%	605,280	38.5%	430,678	27.4%
2002	1,024,279	60.1%	678,967	39.9%	485,915	28.5%
2003	908,839	57.0%	684,667	43.0%	493,983	31.0%
2004	867,436	56.5%	666,979	43.5%	495,030	32.3%
Change	**-4.6%**		**-2.6%**		**0.2%**	

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Environmental issues were a factor in all of the presentations to media, with most of the near-term focus being on hybrid vehicles. However, it was disconcerting to realize that OEMs are now talking about production fuel cell vehicles being closer to 2030 than 2020. Not that long ago OEMs were predicting fuel cell vehicles for 2010. The window for this technology is being pushed so far into the future that I question whether it will happen at all. Almost everything we saw in Detroit was an interim solution comprised of three main groups: gasoline-electric hybrid vehicles; diesel-electric hybrid vehicles; and hydrogen-powered internal combustion vehicles.

General Motors was the only company that talked of actual fuel cell vehicles that they will put on the road in the near future - a fleet of experimental buses that should hit the roads within the next couple of years. Their justification for focusing on implementing fuel cell technology in buses is that because this is going to be a very low volume technology GM should implement it where it could have the most impact despite low volume. The factors limiting volume are cost, and - more practically - only a handful of fuel stations across North America can supply fuel for hydrogen vehicles.

One of Ford's proposed solutions to resolving the infrastructure problem would be in building hydrogen internal combustion vehicles such as the Supercharged V10 hydrogen-powered Econoline bus. This vehicle was used to shuttle media to and from Cobo Hall at the Detroit show. These types of vehicles are the "bridging technology" that Ford thinks will support the growth of refueling infrastructure for hydrogen. "Bridging Technologies" are ones that take the industry from where it is at today to the fuel cell which offers so much potential for the future. The issue here is that if fuel cells don't come of age the industry may not have anything to bridge to. I wonder if it would make more sense for the industry to stop using the term "bridging technology" since it is not known what it is realistically bridging to, and instead simply call it "evolving" technology aimed at lessening dependence on fossil fuels.

We at DAC are very bullish on diesel and diesel hybrid for Canada.

Another type of bridging technology being implemented by some major manufacturers is various forms of hybrid vehicles. This year there was much more focus on diesel-electric with at least three companies showcasing prototypes, some of which were almost production-ready.

The Opel Astra with a 1.7 litre direct injection diesel and the Mercedes S400 CDI with a V8 direct injection diesel looked ready to go on sale very soon. The

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Mercury Meta 1, also with a diesel-electric hybrid drive train, appeared to be in the concept vehicle stage.

The advantage of diesel hybrid over the existing gasoline hybrid vehicles is two-fold: the additional fuel efficiency of diesel engines as well as being able to take advantage of lower cost fuels in markets both inside and outside North America. Diesel hybrids are also better suited for heavier vehicles such as the Mercedes S Class and SUVs because of their higher torque characteristics. We at DAC are very bullish on diesel and diesel hybrids for Canada.

An interesting twist on the gasoline hybrid vehicle scenario is fuel efficiency technology with robust power - not only no compromise on performance, but even producing enhanced performance. The hybrids from Toyota (Lexus RX400h, GS450h) and Honda (Accord Hybrid) are actually more powerful vehicles than the non-hybrid versions. GM also said their upcoming hybrid vehicles will not compromise performance for fuel economy. At least three automakers (DaimlerChrysler, GM and Honda) also touted their cylinder de-activation technology as a major step forward in fuel efficiency and the quest for a cleaner environment.

... the industry puts out its best... then holds its breath waiting for a response.

This emerging focus on meeting higher environmental standards without sacrificing performance, and possibly even improving performance, is perhaps the most important new trend evident at the show. In the past, the vehicle companies complied with what our governments asked in terms of social policy concerns such as environment, fuel efficiency and safety, but there were serious compromises for the consumer.

Faced with the choice between the environment and performance the consumer usually chose performance. We now are very close to an era in the automotive sector where there will be less compromise required and thus more acceptance by the consumer. Both the environment and the consumer may win.

Overall, one of the reasons I like the Detroit show so much is because it is a microcosm of the entire world automotive industry. Whether it is obviously brilliant solutions, or difficult struggles with challenges, the global automotive industry puts what it considers its best business models and product solutions right out in front, for everyone to see, and then holds its breath waiting for a response. DAR

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