

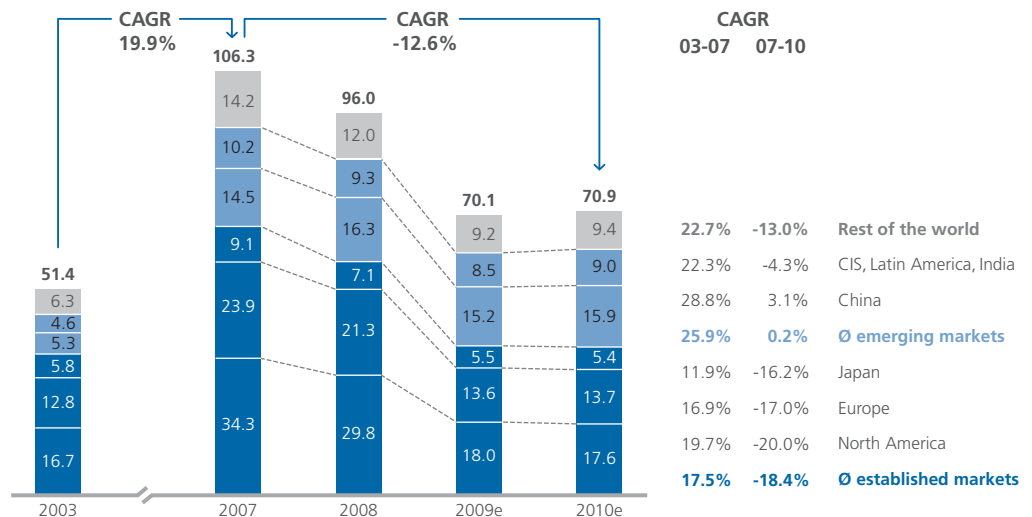
New Acquisition Opportunities in Emerging Countries

After years of strong growth, the global market for construction equipment is now going through a massive and continuous contraction. In emerging-market countries, the crisis is less pronounced, but this resilience still cannot offset the dramatic drop in demand sweeping through mature industrial countries. At the same time, though, there are substantial opportunities for Western manufacturers. Dramatically lower valuations of companies create favorable conditions for acquisitions in emerging countries and lay the foundation for a strengthened position after the crisis.

Oliver Wyman's new study, "Emerging Markets – Opportunity or Threat?", examined the markets and trends in the construction-equipment sector, and developed recommendations for manufacturers.

Between 2003 and 2007, the global market for earth-moving construction equipment more than doubled. Good economic growth and high replacement investments drove sales from \$51.4 billion to \$106.3 billion.

Global market for earth-moving construction equipment
Sales in \$ billions



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Deviations resulting from rounding possible
Source: Oliver Wyman study "Emerging Markets – Opportunity or Threat?", latest revision: May 2009

“Construction-equipment manufacturers should take advantage of the valuation levels in emerging countries in order to extend their position in attractive markets of the future by making targeted acquisitions.”

The recession's impact

Latest forecasts issued in May 2009 indicate that the market contraction will continue at least through 2010. Industrial countries will be hardest hit by the shrinkage of the global construction-equipment market to an overall volume of only \$70 billion in 2009 and 2010. Compared with its peak in 2007, these countries will see demand plunge by about 45 percent through 2009 and then stagnate in 2010.

In emerging countries, market shifts are not as dramatic. Following a noticeable decrease in 2009, moderate growth is expected next year, particularly in relatively crisis-resistant China. This will result not only from general investments in infrastructure being made by emerging countries, but also from crisis-related economic-rescue programs that will stimulate demand.

In addition to a massive need for restructuring created by falling sales and overcapacities, Western manufactures will face increasing competition in their home markets from China, the fastest-growing exporter of construction equipment. Between 2003 and 2007, Chinese exports grew by an average of 70 percent annually, reaching nearly \$9 billion. Driving China's exports are increased internationalization of the entire market, greater demand for reasonably priced products and, not least, the growing export orientation of Chinese manufacturers.

Four demand trends

Leading Western manufacturers should increasingly move into emerging countries in order to tap into growing demand there. They can succeed as premium suppliers offering a singular level of service, oftentimes even without having to make major product modifications. Strategies should take stock of four sector trends: intensified emission standards in many countries, the growing importance of the rental and leasing business, the advance of compact equipment, and the growing demand for service.

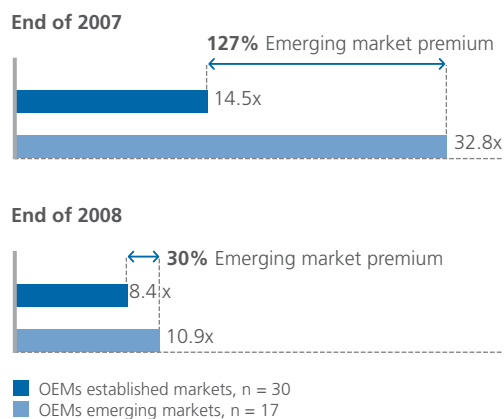
Recommended steps for manufacturers

For Western manufacturers, the best next steps are short-term and significant capacity adjustments, comprehensive cost-cutting measures, and refinement of sales and service ranges. In the end, though, this will not be enough; they must also make fundamental improvements in their business designs.

Initially, this should include establishing a clear profile, possibly as a regional specialist or global full-line provider, because players lacking such a well-defined profile are already much less profitable today. Once that profile has been determined, it must be vigorously

Falling company valuations

Median price-earnings ratio



Basis: Listed manufacturers of construction- and agricultural-equipment
Source: Oliver Wyman analysis

introduced. A regional specialist, for instance, must secure its profitable niche despite increased competition, and it may need engine-development partners as a result of rising emission standards. A global full-line provider, by contrast, should primarily strengthen its range and international footprint, particularly in emerging markets.

Seizing the opportunities

All Western manufacturers with multinational ambitions face the challenge of gaining a sufficient share of growth in emerging markets. Two factors will increase their chances in this regard:

First, domestic manufacturers have not made adequate investments in their networks, even though customers in emerging countries place a high priority on network reach. Second, dramatically lower valuations of companies raise the opportunity to gain market share in emerging countries. Since 2007, the valuations for manufacturers in emerging countries have plunged from 33 times earnings (price/earnings ratios) to 11 times earnings by the end of 2008. As a result, these manufacturers are not much more expensive than Western companies, with a P/E ratio of eight. The opportunities for acquisitions, equity participations, and partnerships could hardly be more favorable.