



## China

# Growing Fast in a Complicated and Competitive Market

**Selling both passenger and commercial vehicles, it was a very fruitful year for us at Dongfeng Motor Company, which is a 50-50 joint venture between Nissan and China's Dongfeng Motor Group. Our passenger vehicle sales volume was 158,000 units—2.6 times more than in fiscal 2004. This represents the number one growth in the market. We also received more than forty awards, including Car of the Year for Tiida and the top ranking in the J. D. Power Asia Pacific 2005 China Customer Satisfaction Index Study.**

Overall, the passenger vehicle market fell within our expectations, with total growth of about 25 percent. While very healthy, compared to the nearly 70 percent rate of fiscal 2003 that was not outstanding. Still, few markets can claim even a 20 percent increase.

Three vehicles were our main engines of growth during fiscal 2005: The Teana, which we introduced in September 2004, and the Tiida sedan and hatchback launched in 2005. All three have gained favor in the market. The Teana moved ahead of its main rival, and the two Tiida models offer some desirable values to customers in the mid-sized segment. In June we introduced the Sylphy, positioned between the Teana and the Bluebird.

On the commercial vehicle side, the total industry volume was down, particularly in the mid- and heavy-duty truck market. Although everyone suffered, our commercial vehicle division did take the number one share in China in that market. Our LCV business was extremely good, growing more than 40 percent in volume. Fiscal 2005 was a very good step for future growth, and confirmed the company's solid base here.

Commercial vehicle customers are very business-oriented, and buying a truck is a serious investment. China's latest five-year economic development plan

ended in 2005, and the government often changes policies at this juncture. If customers don't have solid confidence in the future, it's very natural for them to hesitate. This was one of the factors that contributed to the slowdown in the mid- and heavy-duty truck market last year.

Another cause was due to macroeconomic control measures by the government. The economy was also overheated, especially in real estate investment, and there were some environmental problems. Based on the overheated economy, many new customers had already bought trucks in fiscal 2004, but businesses began struggling from the second half of last year.

Customer expectations are also changing. Now people are either moving up to heavier trucks or down to LCVs. In May 2006, we released a new heavy-duty truck called the Tianlong. Incorporating Renault Trucks' 11-liter diesel engine and Nissan Diesel's cabin technology, the Tianlong was designed for customers seeking a reliable vehicle for long-distance hauls and heavy transport.

As for passenger vehicles, to realize the volumes we want, we need to expand our dealership network. We figure that one dealer can sell up to 2,000 units. However, increasing sales beyond that will not be easy even in big cities like Shanghai and Beijing, because our dealers in China sell on average 800 units per year. In order to sell more than 300,000 units, we need 400 dealers. Last year our target was 250, and we achieved that. This year, we're going for 350. By 2007, we'd like to have 400 dealers. We already have at least one dealer in each province, including Tibet. Now we're trying to place dealerships in medium-sized cities in each province.

We are concentrating heavily on localization efforts in order to achieve cost competitiveness. We decided to establish a dedicated R&D center in Guangzhou, for example, to test chassis and bodies,



as well as assess plastic parts for weather-related durability in conditions of heat, humidity, low temperatures and so on.

We also started producing 1.6- and 2.0-liter power plants at our new engine plant in February this year. These are volume-selling engines in the China market. The plant will initially be producing 180,000 units a year, but will eventually have a capacity of 360,000 units. We are already using locally produced 1.6-liter engines in the Tiida. The quality of these localized engines is very competitive even when compared to those made in Japan.

We are planning at least one or two passenger vehicle launches a year. Because of these planned annual product launches, we need to expand production capacity. We have capacity in Guangzhou of 150,000 vehicles, and we've already decided to boost that to 270,000 units. The next expansion after that will be 360,000 units.

We typically have two growth scenarios, one a conservative or pessimistic scenario and the other optimistic. Even for the more pessimistic one, it is natural for us to want to invest more, because the market is growing. The timing of investment, however, does create some risk. It's very natural for a country like China that's growing rapidly to present

up and down market conditions, so our policy for investment is step by step and based on the potential return on invested capital or ROIC.

The main difficulty in China is not the market growth but the severity of competition. Almost all the global makers are here and have growth strategies, and have either invested or plan to do so. China's national brand is also making some progress.

The heart of our strategy involves enhancing the Nissan brand for passenger vehicles and Dongfeng for the commercial ones. In the first area, we're promising challengers, and in the second, we're champions. The Dongfeng name is already a great asset, and Dongfeng customers are very loyal to the brand.

Our relationship with Dongfeng is a major asset in this very competitive market, the backbone of our future development in China. It has come to resemble the close one Nissan has with Renault. I am confident that this relationship will bring us continued success in China.

Our most recent news is that we have relocated our headquarters to a new facility in Wuhan, the capital of Hubei Province. This is something we had planned to do when the joint venture was formed three years ago. Now we are ready to grow DFL into a globally competitive car manufacturer.



Nissan dealership in Guang Da



The new Dongfeng Nissan engine plant (Huadu)



Unveiling the new Sylphy