VDA German Association of the Automotive Industry

COVID Report

from China; April 19, 2022

Content

COVID Situation in China

The first half of April has witnessed Chinese Mainland's efforts in battling the epidemic. Major epidemic control areas include Changchun of Jilin Province, Shanghai, Shenyang of Liaoning Province, and Guangzhou of Guangdong Province. Below are the statistics.

Table 1 COVID-19 Report of Major Cities

City	Cumulative locally confirmed cases April 1-18	Cumulative locally asymptomatic cases April 1-18	Risk area as of April 18	
			High risk	Medium risk
Beijing	47	3	1	0
Shenyang	15	331	0	0
Changchun	7106	18329	3	36
Shanghai	26068	335225	0	13
Guangzhou	223	70	0	3
Hong Kong	309841	(No release)	0	0

Source: National Health Commission, as of April 18

Status Quo of the Automotive Industry in China

According to the data published by the China Association of Automobile Manufacturers (CAAM) earlier this week, affected by the macro-economy status, the development of the automotive industry is facing triple pressures of shrinking demand, supply shock and weakening expectations.

In March, auto production and sales reached 2.241 million and 2.234 million respectively, with reduction of 9.1% and 11.7% year-on-year, exported 170,000 vehicles which decreased 17.1% compared to the month earlier. The sales of passenger cars were 1.864 million units, down 0.6%; sales of commercial cars were 370,000 units, down 43.5%.

There are some seriously hit areas which are still suffering from the latest wave i.e., Changchun, capital of Jilin province and Shanghai, who are two major car-producing cities which account for 20% of the car production of 2021. According to the figures published by National Bureau of Statistics, the national automobile production of 2021 reached 26.5 million units, of which Shanghai produced 2.83 million units, accounting for 10.68% of the total, meanwhile, Jilin province produced 2.42 million units that accounted for 9.14% of the total.

Pandemic Hit Areas: Speed of Recovery is much Slower than Expected.

- **Changchun (Jilin Province)**

The epidemic has been greatly eased after more than 45 days' battle. On April 14, Changchun of Jilin Province announced that it has attained social clearance of infection, i.e., there is no source of infection in the community, all infections are detected in collective quarantine. Jilin Province is orderly promoting the resumption of work and production. According to the local government, it will strive to achieve the maximum prevention and control effect at the least cost.

- **Shanghai**

Shanghai is among the places that have been hardest hit, the epidemic situation is still at a high level with an average of 10,000 asymptomatic infections per day. According to the estimation by the China Passenger Car Association (CPCA), if the current epidemic situation could not be alleviated effectively, it may lead to a decline of 15%-20% in the national automobile production, of which the lost production of Shanghai accounts for about 10%.

- **Jiangsu Province**

Suzhou, Changzhou, Wuxi and Kunshan of Jiangsu Province, where the electronic and electrical as well as auto parts industry are based, take cautious epidemic control measures due to their geo-distance to Shanghai. Employees in office enterprises mainly work at home. Production enterprises arrange shifts and ensure the production line workers to commute in "two points and one line". Due to the strict highway measures taken in Shanghai, the industrial transportation of Jiangsu Province to Shanghai is rather limited.

- **Shenyang (Liaoning Province)**

After the epidemic control for over 1 month, since April 13, Shenyang has orderly restored normal work and production. To ensure the safety and stability of the industrial chain and supply chain, classified and differentiated epidemic prevention measures will be adopted.

- **Guangzhou (Guangdong Province)**

After the infection clearance of Shenzhen, the epidemic situation in Guangzhou occurred one after another. Learning from the lessons of Shenzhen and Shanghai, Guangzhou has hold stricter and more frequent large-scale nucleic acid detections and strong epidemic control measures since the beginning.

Guangzhou Automotive Group Motor Co., Ltd (GAC) 's joint venture’s engine plants in Guangzhou began to stop production since April 13, which may last 3-4 days. In addition, Dongfeng Nissan's two plants in Huadu district, Guangzhou also stopped production, which is expected to last 3 days. GAC Passenger Cars has no plan to stop production for the time being, despite the potential risks.

VDA Members: Surfaced Problems Need to be Solved Urgently.

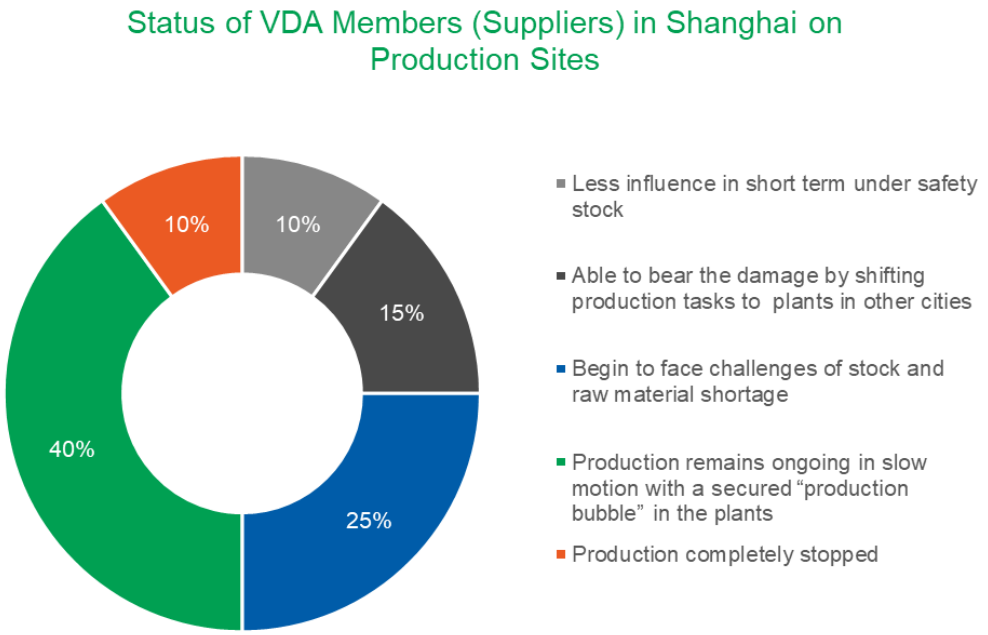
The recent exchanges with VDA members in China have shown that the current epidemic situation and prevention control policies are causing significant challenges for the automotive industry at different levels.

The OEMs such as,

- FAW-Volkswagen in Changchun has resumed production since April 17.
- SAIC-VW in Shanghai is preparing for resumption of work and production.
- BMW-Brilliance in Shenyang have resumed production, with office staff stay home office until further notice.

According to VDA China's communication with its members, among the suppliers whose plants are located in above hit areas,

- 10% companies are under safety stock, with less influence in short term.
- 15% companies (mostly Tier 2) are able to bear the damage by shifting production tasks to their plants at other cities.
- 25% companies (mostly Tier 1) were under safety stock in March, however, is currently facing challenges of stock and raw material shortage.
- 40% companies managed to contain the loss to a rather medium level by securing a "production bubble" in their plants with fewer shifts, production remains ongoing in slow motion.
- 10% companies have completely stopped production.



However, the situation is changing on a daily manner based on the local prevention policy. Even though some of the members are currently "safe", more and more challenges are surfaced and to be solved urgently. The speed of recovery is certainly slower than expected particularly in Shanghai and its neighboring cities, where the manufacturing plants are located, including most of the VDA members.

Challenges & Impacts: A Chain Reaction of the Whole Industry.

Freight & Logistics

Smooth logistics is the key to win the latest battle against COVID-19 and is also critical to ensuring a stable supply chain.

However, the epidemic in Shanghai has spilled over and has affected the surrounding provinces who have put strict transportation measures to prevent infections, e.g., some places take excessive cutting-off measures to arbitrarily restrict the passage of freight vehicles and drivers. In Shanghai, trucks cannot move in and out of the city without special permits, which are only valid for 24 hours and on specific routes. Such regulations have also been expanded to other regions, and some local authorities have adopted epidemic control policies.

Transportation and logistics are hampered at various levels: blockades of highways in various cities have hindered the transportation of goods; plenty of truck drivers are stuck on the highways; the transportation routes get much more complicated; the freight costs get lifted immediately etc.

Supply Chain

Both the upstream and downstream of the supply chain get heavily hit.

On one hand, the unsmooth logistics causes the transport of raw materials or finished parts stuck, therefore, the purchase of raw materials in a timely manner is impossible, further causing the production comes to a standstill, thus creates a vicious circle; on the other hand, warehousing becomes a challenge too as the goods are kept long in stock.

The impact is not limited within the circulation within China, the imported and exported goods are facing the same challenges.

Manufacturers

If suppliers in Shanghai and neighboring cities can't find a way to dynamically resume production, then probably all automakers in China will have to halt production by May, according to Mr. Xiaopeng HE, the Chairman and CEO of XPeng, an EV manufacturer of China. The same thought was shared by Mr. Richard YU, the executive director and CEO of Intelligent Automotive Solution BU of Huawei.

It is obvious that the impact has spread from the epidemic-hit-areas to other cities, and even abroad. **A lot more OEMs have announced that their production got suspended due to the disruption of the supply chain especially the key suppliers.** Besides the OEMs sitting at the major epidemic cities like SAIC-VW, FAW-VW, BMW-Brilliance and Tesla, the other ones in China like Great Wall, NIO, as well as the overseas manufacturers like Mitsubishi, Honda and Suzuki have claimed their halt in production, with the same challenges ahead.

Government Measures

With the industry facing turbulent amid the pandemic, the Chinese government have initiated several approaches to help ease the pressure from pandemic on the automotive industry.

- **April 11, the State Council issued a notice to ensure the smooth transportation of important production materials such as freight logistics, raw materials.** It is strictly prohibited to block or close highways without authorization. It is not allowed to shut down the highway service area without authorization.
- **April 14, the State Council issued a notice to make every effort to ensure the smooth transportation of freight logistics. “Vehicle Pass” for transportation of key materials will be issued according to the national unified pattern.** Qualified enterprises across the country can apply for the Vehicle Pass. The notice also emphasized that all localities should ensure smooth passage for vehicles with a "pass" to enter and leave epidemic related areas across provinces, and special channels should be set up in areas where conditions permit to ensure rapid passage.
- **April 16, Shanghai issued the guidelines for enterprises to resume production in an orderly manner under the premise of controllable epidemic situation.** MIIT has recently sent a working group to Shanghai to promote resumption of production and give priority to those key enterprises in key industries such as integrated circuit, automobile manufacturing and equipment manufacturing.
- **April 18, Ministry of Transport (MOT) stressed that sufficient number of national unified “Vehicle Pass” shall be issued and used. The nucleic acid test results shall be mutually recognized throughout the country within 48 hours.** The passage shall not be restricted on the grounds of waiting for the nucleic acid results.

The government measures may somehow ease the difficult situation; however, it has brought great challenges to local governments to follow the policies and take quick actions considering the potential risks of "following Shanghai's footstep".

VDA China Interpretation

China is 20% of global demand but its role in supply chains is considered much more important than that. **The impact on the entire industry chain is expected to further expand from the cities got heavily hit to the whole country, even to the international automotive industry. It is possible that the hit on the automotive industry brought by the pandemic is even severer than 2020.**

In short term,

- As major automotive areas, the production of Shanghai and Jilin Province in total accounts for nearly one fifth of the national production, **it is predictable that the halt of the production of the two cities will greatly affect the production and sales in key areas of China in April.**
- **The shortage of raw materials and the price rise of auto parts in particular chips and power batteries have directly led to the price lift of vehicles, as well as delay in delivery, resulting in insufficient consumption momentum and affecting sales.** It could be a short-term impact, when the production and delivery are back to normal, the consumption momentum of consumers will gradually recover.

In long term,

- The impact of the sudden shutdown of local production this time caused by epidemic prevention control **may trigger enterprises to transfer investment to other provinces and regions in China, in order to build backup production bases and reduce risks as an insurance.**

In addition,

- The new EV players are operated with asset-light strategy and production by contract manufacturers, with smaller volume of production and sales compared with traditional OEMs. Therefore, the risks and pressure are greater for them facing the crisis in supply chain.

The long chain of automotive industry requires aligned coordination in production and logistics. With the currently pandemic prevention policies, it is highly unlikely that the main challenges are to be solved in short time, let alone to resume to the pre-pandemic status of this year. It is possible that more problems will emerge in the coming 1-2 months.

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