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2015 edition

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Volvo

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Contents

Introduction

Financial Overview

- Volvo Cars, financial highlights 2014 vs. 2013
- Volvo Cars, retail sales 2014 vs. 2013

Product and Platform Strategy

SPA

- SPA models could represent as much as two-thirds of Volvo output, and possibly more
- Europe and China will adopt the same manufacturing systems
- 90 cluster models will be at the heart of the new Volvo

Current Major Model Programmes

- V40
- S60/V60/XC60
- V70/XC70
- S80
- XC90

Powertrain Strategy

- New 4-cylinder engines
- Modular concept
- Downsizing strategy continues with 3-cylinder version
- Reduced fuel emissions underpin Drive-E concept
- Benefits of a common engine programme
- Plug-in hybrids

Purchasing Strategy

- Overview
- Country risk assessment
- Supplier awards and recognitions
- Geographic split of purchasing

Interviews

- Lars Wrebo, Senior Vice President, Purchasing and Manufacturing, Volvo Cars

4	– Introduction and evolution of the purchasing function at Volvo	23
6	– Size and scale of purchasing function	23
6	– Government support	27
	– Implications of the new platforms for manufacturing	27
8	– Directed sourcing, managing tier two suppliers	28
9	Supplier interview – Marcus Nyman, IAC	29
	Production Strategy and Manufacturing Footprint	31
	Introduction	32
10	– A growing manufacturing network	32
	– Recent changes to logistics arrangements in Sweden and Belgium	33
11	Sweden	33
	– Gothenburg – Torslanda	33
14	– Press shop	34
14	– Body shop	34
15	– Paint shop	34
15	– Trim and assembly	35
15	– In-house component assembly	35
	– Sequencing by suppliers	35
	– End of line finishing	35
17	– Skovde engine plant	35
17	– Floby component plant	35
18	Belgium	36
	– Ghent	36
18	– Introduction	36
	– Suppliers and sequencing	36
19	Incoming logistics	37
20	China	37
	– Major new investment	37
20	– Global quality standards	37
	– Teamwork is key	38
	– Employee training	38
22	– Chengdu supplier network	38
	– Environmental compliance	38
23	Forward Model Program	39

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Figures

Figure 1: Volvo XC90 safety cage	10	Figure 4: Volvo V70	15
Figure 2: Volvo V40	14	Figure 5: Volvo S80	15
Figure 3: Volvo S60	14	Figure 6: Volvo XC90	15

Tables

Table 1: Volvo Cars, financials 2014 vs. 2013	6	(2011–2018) by Nameplate	14
Table 2: Volvo Cars, retail sales 2014 vs. 2013	7	Table 7: Selected Suppliers on the new XC90	15
Table 3: Volvo Cars, global sales by model, 2014 vs. 2013	7	Table 8: Volvo: purchasing split by country	21
Table 4: Volvo vehicle production by fuel type	7	Table 9: IHS Automotive Volvo Production Forecast by Country and Plant	32
Table 5: IHS Automotive Volvo Production Forecast (2012–2018) by Platform	9	Table 10: Suppliers at Volvo's Ghent Plant	36
Table 6: IHS Automotive Volvo Production Forecast		Table 11: Parts Volvo sequences at the Ghent Plant	36
		Table 12: Volvo Forward Model Program	40

SAMPLE

CHAPTER ONE

Introduction

SAMPLE

Volvo is both one of the most iconic and best-known Swedish brands and also the last remaining Swedish car company, following the demise of Saab. It is now owned by Geely of China, and although a relatively small company, compared to automotive giants such as VW, GM and Toyota, it is nonetheless now on a growth trajectory and in the process of establishing a global manufacturing network. In addition to its long-established factories in Sweden and Belgium, it now also has two new vehicle plants in China and an engine plant there too. The company has confirmed it will build a factory in the USA in the near future as well.

Volvo's brand recognition derives in large part from its reputation for leading-edge safety technology and environmental compliance. It has long been seen, especially in the US, UK and some continental European markets, as the supplier of the archetypal middle class family car, especially its estate models. The advent of the original XC90 SUV and the subsequent smaller XC60 changed the company's overall image somewhat, but the focus on safety remained paramount. In China, Geely wants to emphasise the premium nature of its vehicles, and with the growth of the Chinese market, especially for premium vehicles, there is every likelihood that the Chinese influence on Volvo's future direction will increase.

In recent years, it has had quite an eventful history. It first lost its independent status when it was bought by Ford and remained a central part of Ford's Premier Automotive Group between 1999 and 2010. At this point, it was sold to Geely which paid Ford US\$1.8bn for the Swedish company. Initially, it was not entirely clear what the new owners were planning to do with Volvo, but it was soon given the go-ahead to develop a new range of engines, and also a vehicle platform, SPA (Scalable Platform Architecture), which underpins the new XC90 and will underpin all new large Volvos.

The revamping of its entire model range is well and truly under way, with the S90 and V90 expected to join XC90 in production in Sweden in the next couple of years; the S90 and other SPA vehicles will also be made in China, and possibly in the expected new plant in North America. In addition, it has begun work on a second platform, or architecture, known as CMA (Compact Modular Architecture) which is being developed jointly with Geely. This will form the basis of the next generation of vehicles of the size of the V40 (and other variants) and also C-segment and smaller vehicles for Geely.

As noted, a key part of the company's recent expansion has seen new factories open in China. The first car plant to open was in Chengdu where the S60 and XC60 are made;

the second plant is in Daqing and this is where the S90/V90 will be made, along with the old XC90 which will be sold in China as the XC Classic. The Chinese engine plant started production in late 2013. The launch of the new XC90 SUV has taken place on the back of a major investment programme at its home factory in Gothenburg (Torslanda). In addition to a general factory modernisation, the major part of the investment in Gothenburg has been to facilitate the production launch of vehicles made on the new SPA platform. In time a similar investment will be made at Ghent to make vehicles based on the second platform, CMA. These two platforms will underpin all its future Volvo vehicles, including those made in China and the USA. One of the key aspects of the design and layout of the new Chinese factories is that, as far as possible, they operate as mirror images of the existing European plants, using the same manufacturing systems, equipment and line layouts. The same approach is expected to be adopted in the USA in due course.

In 2014 Volvo's global retail sales rose to nearly 467,000 units, rising from nearly 428,000 in 2013. Although production is growing in Europe and now in China, Volvo remains a relatively small player at under 500,000 units a year. It is planning to raise its annual production volume to over 800,000 units and possibly more once the North American plant is confirmed. As part of the Ford Premier Automotive Group (1999-2010), Volvo had benefited from the scale benefits from Ford's global purchasing power and also a wide potential source of engines. Operating as an independent player, and even with Geely's backing, Volvo has been on a process of re-inventing itself in many key areas, including increasing its manufacturing footprint, developing its own four-cylinder engines, and reorganising and expanding its purchasing department for example; the purchasing function had been subsumed within Ford Purchasing under Ford's ownership, with a large number of key functions, especially cost analysis and estimating, having been transferred to Ford, reducing Volvo's own capabilities in the area.

This reinvention has involved some significant tweaks to the existing product range while the company worked on all-new products on brand new platforms. These have included:

- The launch of the world's first diesel plug-in hybrid, the V60H; this sold out of the initial planned modest production volume before the vehicles had reached showrooms, resulting in a threefold increase in the initial production plans to around 10,000 pa.
- The launch of the new Volvo V40 which replaced the S40/V50; Volvo has positioned the V40 as what it calls

a premium compact car. Soon after the V40's launch, it added a CC (Cross Country) version. This is not a full-blown SUV, but has similar off-road capabilities to the XC70.

- The launch in late 2013 of the new Volvo Engine Architecture (VEA). Engines made on this architecture are now in production under the Drive-E name; this programme encompasses a series of all-new petrol and diesel engines, all of which will be four-cylinder units. These produce significant fuel efficiency and emissions improvements over the outgoing six-cylinder and V8 units, which had hitherto been the mainstay of Volvo's powertrain offerings for many years.
- The launch of the Scalable Platform Architecture (SPA), with the first model to be made off this platform, the replacement for the XC90 SUV, starting production at the beginning of 2015. The start of production of the new XC90 also entailed the Gothenburg plant moving to a three-shift system from May 2015.
- Confirmation that a second platform, the CMA, will be launched in the near future. This is being developed by a Volvo-Geely joint enterprise, under the name CEVT – Compact European Vehicle Technology – which is based in Gothenburg and involves Volvo and Geely personnel working together for the first time.
- Investment in Gothenburg to produce vehicles on the new SPA platform, and the opening of two all-new vehicle plants at Chengdu and Daqing in China.
- In moves which highlight Volvo's determination to control the logistics and assembly elements of its cost chain, Volvo has acquired the logistics company DSV which used to provide some of the support services at Ghent; and in Sweden, in July 2014, Volvo acquired the assembly operations of JCI which had been delivering headliners and tunnel consoles for both the Gothenburg and Ghent factories.
- Confirmation in March 2015 that a new factory would be built in North America. The factory's location, in South Carolina, was confirmed in May. Volvo has said it will invest US\$500m in this factory and that it will start producing vehicles during 2018, with construction due to begin at the end of 2015. Volvo's objective is to sell 100,000 upa in the US; in all likelihood the first vehicle to be made would either be the S60 or possibly an SUV, ie either the XC60 or the new XC90.

In financial terms, Volvo is now profitable and has in fact been able to report modest profits in both of the last two

financial years (further details follow). A key driver behind the financial turnaround from recent losses has been the increase in sales in China which is now by some way the company's largest country market. Sales in China rose from just over 61,000 in 2013 to just over 81,000 in 2014; by comparison, Volvo sold just over 61,000 in Sweden and just over 56,000 in the US in 2014. Further details are provided later in this report.

Financial Overview

As noted above, Volvo Cars is now operating profitably once again, with the key financial figures for the last two years shown in the table below:

Volvo Cars, financial highlights 2014 vs. 2013

The table below shows how sales revenue and gross income rose year-on-year, while net profit actually fell over the period:

SEK millions	2014	2013	% change
Net Revenue	129,959	122,245	6.3
EBITDA	9,183	9,057	1.4
EBITDA margin %	7.1	7.4	-4.0
Operating (EBIT) income	2,252	1,919	17.4
EBIT margin %	1.7	1.6	6.3
Net income	834	960	-13.2

Source: Volvo Cars' 2014 financial report

The company attributes its improved revenue and operating income numbers to an increase in sales volumes which were up 6.3% year-on-year, plus some positive help from foreign exchange movements. It is worth noting that sales from Chinese companies are not included in the net revenue line, but the profit on these sales is reflected in the income lines. The net profit figures were negatively impacted by the capitalisation of development expenses included on the development of the SPA platform; these were 4,748m SEK in 2014 against 4,089m SEK in 2013, a 16.1% rise year-on-year. In addition, the company saw a rise in its current liabilities by 25%, or 3,821m SEK, to just over 19bn SEK, reflecting major tooling commitments for the new XC90, allied to an increase in vehicle sales which are covered by lease agreements.

Volvo Cars, retail sales 2014 vs. 2013

The table below shows how the only growth market in terms of Volvo sales volumes in H1/2013 was China, all other markets recording year-on-year falls:

Table 2: Volvo Cars, retail sales 2014 vs. 2013

Country/region	2014 sales	2013 sales	% change
China	81,221	61,146	32.8
USA	56,371	61,233	-7.9
Europe excluding Sweden	182,157	166,307	9.5
Sweden	61,357	52,260	17.4
Rest of the world	84,760	86,894	-2.5
Total	465,866	427,840	8.9

Source: Volvo Cars' 2014 financial report

As is clear from the table above, the major growth market in 2014 was China, followed by Europe, including Volvo's home market of Sweden.

Volvo sales in China grew faster than the Chinese market as a whole; the company attributes this to a combination of the company's expanding manufacturing and dealership network, allied to the widening product range on offer in the country. In Sweden, domestic sales were underpinned by the traditional V (estate) and the newer XC ranges; in fact while Volvo's sales rose 17.4% in Sweden, sales of XC models in the home market grew by 42.1% to nearly 23,000 units.

In the US, Volvo has had a difficult time of late and saw sales fall in 2014 compared to 2013 volumes; the company has now instituted a revival plan for the US market, and at the heart of this will be the new US factory referred to above. US demand was driven by the S60 sedan and the XC60. An interesting development in 2015 has seen Volvo China starting to export the long-wheel-base S60L from China to the US.

In terms of individual model sales, as the table below shows, Volvo's best-selling model in 2014 was the XC60, with nearly 137,000 sales against 2013's total of just over 114,000; this was a 20% increase which for a model of over five years' age is impressive. Unsurprisingly, given its fixation with European SUVs, the biggest market for XC60 was China, followed by the USA and Sweden. The second-best seller was the V40/V40CC, which rose by 11% from just under 100,000 units in 2013 to almost 111,000 units in 2014.

Table 3: Volvo Cars, global sales by model, 2014 vs. 2013

Model	2014	2013	% change
S60	44,255	61,579	-22.1
S60L	23,368	67	...
S80	7,668	7,951	-3.5
S80L	4,821	3,531	36.5
V40	84,771	78,307	8.3
V40CC	26,093	21,604	20.8
V60	61,977	54,666	13.4
V70	27,795	26,133	6.4
XC60	136,993	114,010	20.2
XC70	29,092	24,418	19.1
XC90	17,869	23,784	24.9
Others (S50, V50, C70)	1,164	11,790	-90.1
Total	465,866	427,840	10.9

Source: Volvo

In terms of trends in fuel types, Volvo's sales in recent years have been as follows:

Table 4: Volvo vehicle production by fuel type

Fuel/propulsion system	2012	2013	2014
Diesel	31.2%	28.2%	25.4%
Diesel with stop/start	14.1%	21.8%	23.1%
Diesel full hybrid	0.0%	0.8%	0.9%
Petrol, inc. E85	38.4%	27.4%	10.1%
Petrol with stop/start, inc. E85	16.3%	21.8%	40.6%
Petrol full hybrid	0.0%	0.0%	0.0%
Electric	0.0%	0.0%	0.0%
Total	100.0%	100.0%	100.0%

Source: IHS Automotive

The key things to highlight from this table are slow take-up of hybrids so far, and in terms of the forecast hybrid growth at Volvo, IHS' forecast suggests that full diesel hybrids will represent 4.5% and full petrol hybrids just 1.4% by 2018. At present the main fuel consumption reduction technology at Volvo looks like being stop/start technology. Volvo has not produced full electric vehicles in any notable volume, just a few hundred in 2011-12, with no sign that a full EV from Volvo is even under development.