Betting on a new marque in China as Detroit wanes

Layoffs. Output cuts. These are some of the buzzwords of today’s business world where just about everyone is trying to become as lean as possible to outlive a deep and prolonged recession most have never experienced until now.

But what about recruiting staff, building a new plant and creating a new brand from scratch - and that in the struggling auto industry where Detroit’s Big Three would probably have gone under, if not for life support funding from the US government?

Taiwan’s Yulon Group, which has been assembling and selling cars for Japan’s Nissan Motor Co. and Mitsubishi Motors Corp. since the 1950s, is trying for a second time to build a marque it can rightfully call its own. As bold as it would appear at any other point in time, Yulon is making its move at a time when the local auto market has been mired in a slump not seen in decades.

In January, Yulon officially declared its ambition of launching the “Luxgen” brand in China as well as Taiwan. The first Luxgen offering—a seven-seater multi-purpose vehicle (MPV)—is due to hit the Taiwan market in the second quarter to June.

“Luxgen must be a double-edged blade for Yulon,” says Felix Yang, an analyst at Taipei-based SinoPac Securities. “This kind of billion-dollar investment may cut others or yourself.”

Against a shrinking domestic market, the Luxgen must also prove itself in an already quite crowded market on the Chinese mainland. Even there, growth began to slow markedly in the second half of 2008 due to the global financial crisis.

Taiwan’s sales of new vehicles peaked at 510,000 in 2005. After a 30 per cent plunge last year, another contraction of up to 10 per cent may bring the total to just below 210,000 in 2009.

In China, sales of new vehicles suffered their first decline in a decade last October – a drop of about 20 per cent. Even steeper falls in the final two months of the year pushed down full-year growth to less than eight per cent, a worrying figure when compared with the 20-30 per cent increase people have taken for granted in previous years.

In defence of the timing, Yulon Group Chairman Kenneth Yen reminds sceptics of the considerably lower costs for everything from materials to people only possible in a slowing economy. In the face of a universal downturn that spares no one, Yulon considers the brand launch a calculated risk worth taking.

Observers believe Yulon, or the Luxgen for that matter, is heading for a red sea rather than a blue ocean in China. The bulk of the still growing but slowing market, characterised by a bloody price war, is already dominated by joint ventures formed
by major car manufacturers such as Volkswagen, GM, Toyota, Honda, Hyundai and Ford, as well as the mainland’s homeboys Chery and Geely.

Yet a window of opportunity does exist for this upstart from across the Taiwan Strait. Its positioning as a less expensive alternative to Toyota’s Lexus may actually work at a time when the price tag matters and even dictates purchases. The strategy will be especially effective if Luxgen somehow can find some sort of middle ground between major foreign brands and 100 per cent local options.

“Hard to believe as it may seem, Luxgen’s opportunity may also lie in the current recession where frugality often takes precedence over luxury,” says Yang of SinoPac Securities. “Those who aspire for a Lexus but can hardly afford it may settle for a Luxgen.”

Yulon is still awaiting the go-ahead from the Chinese authorities for its 50-50 joint venture with Zhejiang province’s Zhongyu Automobile to assemble and market Luxgen vehicles on the mainland. Back home in Taiwan, Luxgen will not have its own production lines as its parent company will handle the assembly on contract.

The Luxgen is derived from a combination of “luxury” and “genius.” It epitomises Yulon’s ambition to roll out a new line of luxury cars fitted with enhanced features ranging from audio-video entertainment, communications and GPS to safety.

Yulon is drawing heavily on Taiwan’s prowess in IT manufacturing to make ‘intelligent’ vehicles. The list of its local partners speaks of what features are to be expected on Luxgen vehicles: smartphone maker HTC Corp., LED manufacturer Everlight Electronics Co., solar cell maker E-Ton Solar Tech Co., and digital-camera contract maker Altek Corp.

Yulon’s dream of creating an indigenous auto brand dates back to more than half a century ago. “Placing four wheels on a car of our own” drove Yen Ching-ling – the incumbent Yulon chairman’s late father – to found the company in 1953.

Yet three decades passed before Yulon even dared to try to make that dream come true. At the expense of infuriating its Japanese partner, Yulon launched in 1986 ‘Feeling 101’ – a self-developed passenger car dropping Nissan for Yulon – only to fail miserably. The flop was hardly a surprise as Yulon’s aspirations for building a car of its own could not find a big enough domestic market to keep it going for long.

“Creating our own brand has been a lifetime commitment passed down by Mr. (Kenneth) Yen’s parents,” says a senior Yulon official who declined to be named. “This commitment runs so deep that he is making a bet many must consider way too risky and would inevitably pose a threat even to Yulon’s existing business in its home market.”

That is, the Luxgen will also compete with a fair number of brands Yulon sells for others. Yulon Nissan Motor Co., a 2003 spin-off, handles sales of Nissan-branded vehicles in Taiwan. Yulon Motor’s affiliate China Motor Corp., which is also chaired by Kenneth Yen, is the local partner of Mitsubishi Motors and Chysler.

In December, Yulon was forced to take full control of its four-year-old joint venture with financially-strapped General Motors Corp., acquiring the latter’s 49 per cent stake for a symbolic NT$1. Yulon General Motors is now Taiwan’s general dealer of GM’s Cadillac, Opel and Buick brands.

“It’s going to be very tough for Luxgen to hit it off,” says Yuanta Core Pacific Securities analyst Kevin Fang. “A price difference of 5-10 per cent is unlikely to convert brand loyalty – anyone will be quite cautious about making a purchase that is normally to last for 10 years or longer.”

Above all, it’s hard to imagine how a latecomer such as the Luxgen can expect to win a spot in China where the top 15 existing players already command 90 per cent of the market, he adds.