

Automotive Overview

The transformation is not here yet – the crisis is!

November 2019



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What

is

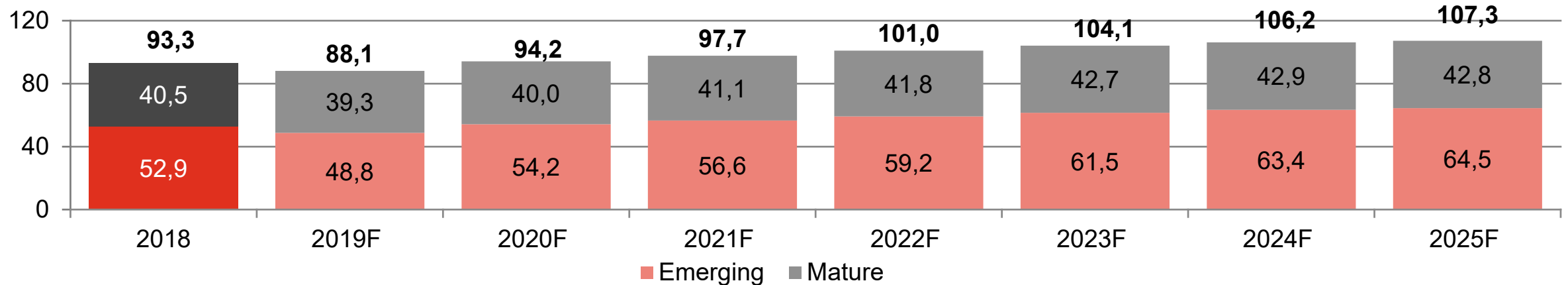
happening

in the market?

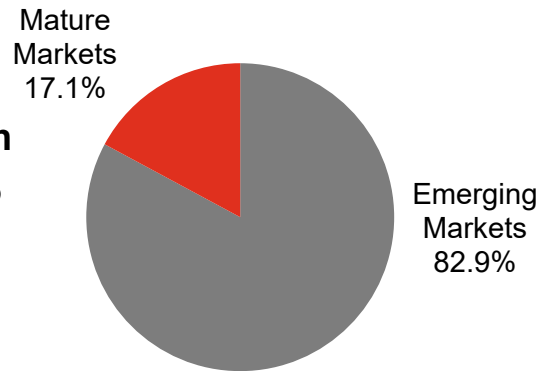
Global automotive will be still a growth market ...

Global – Light vehicle assembly

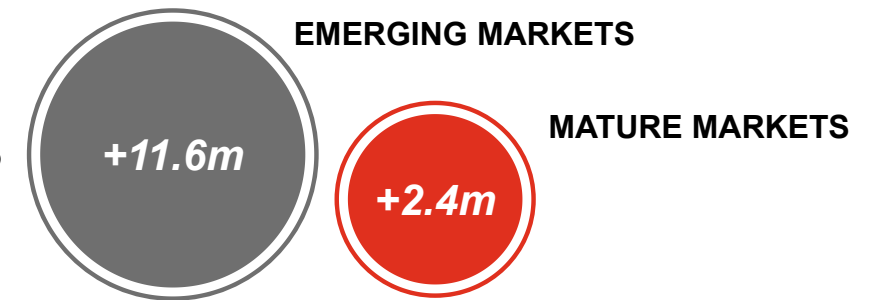
2018 – 2025F (millions)



Contribution to Growth
between 2018 and 2025
(percentage share)



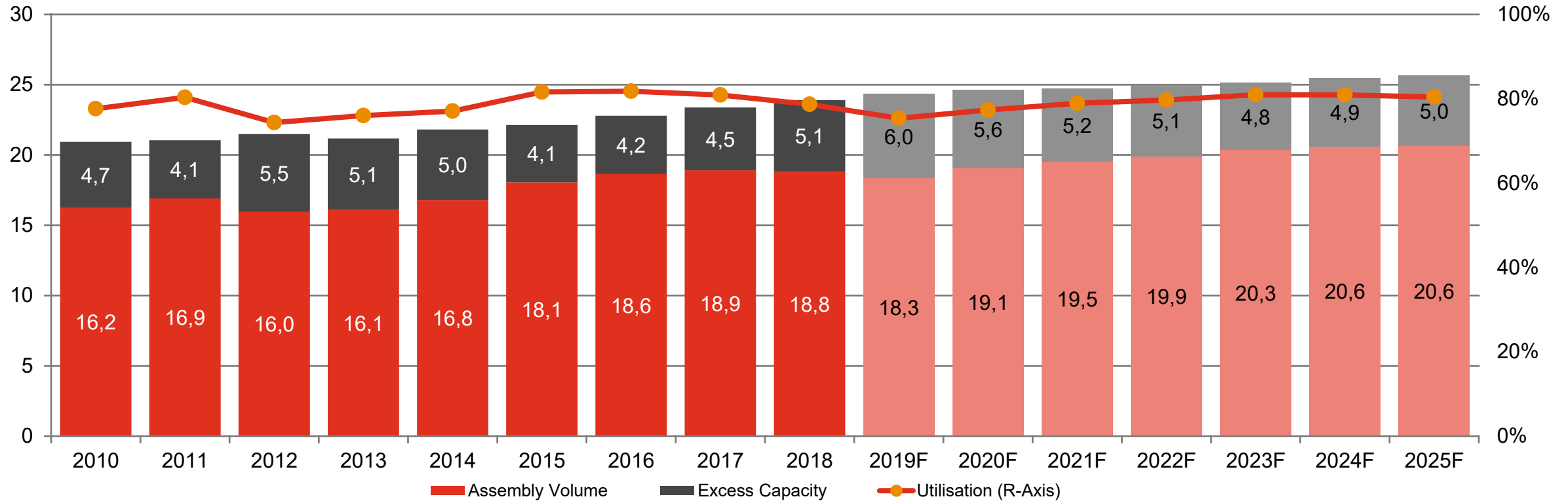
Volume change
between 2018 and 2025
(units)



Mature markets

... but for Europe we expect production to be flat for the foreseeable future

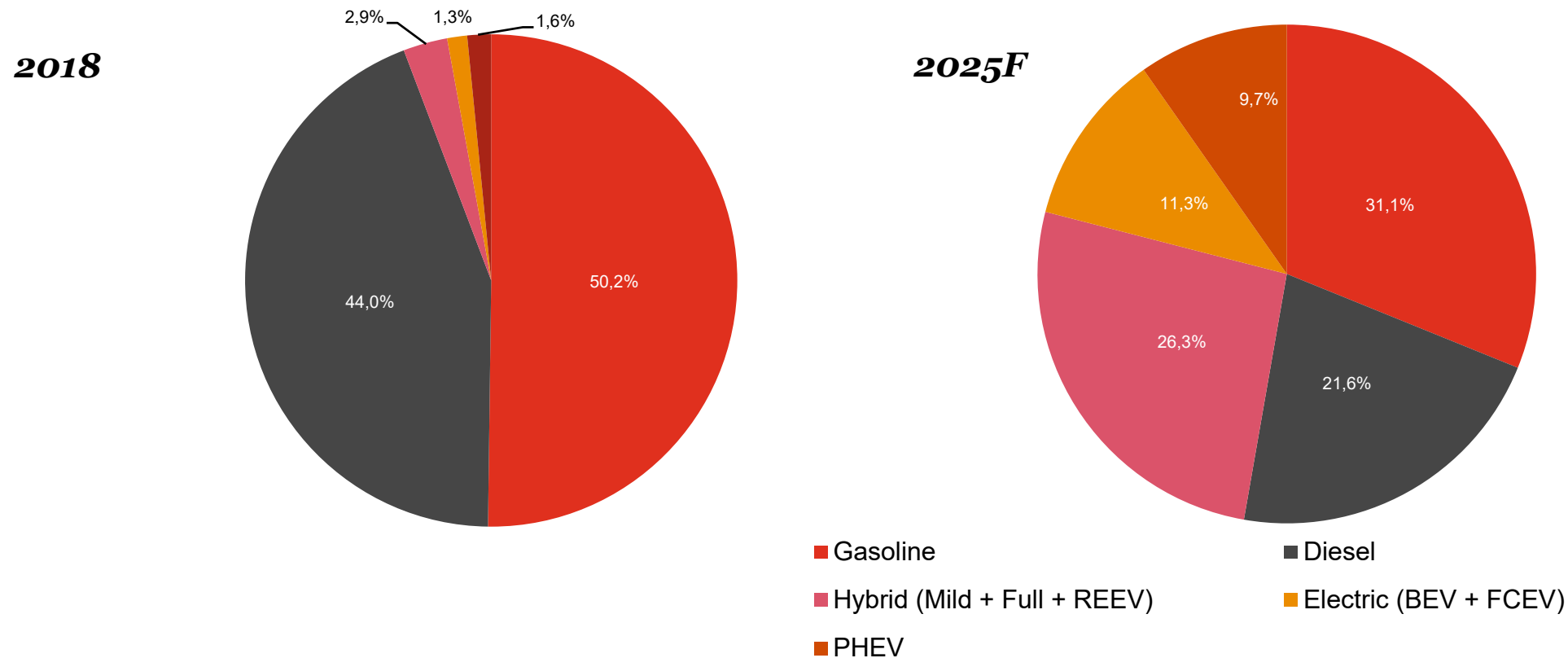
EU – Light Vehicle Assembly
2010 – 2025F (millions)



Source: Autofacts Q4 2019 Release

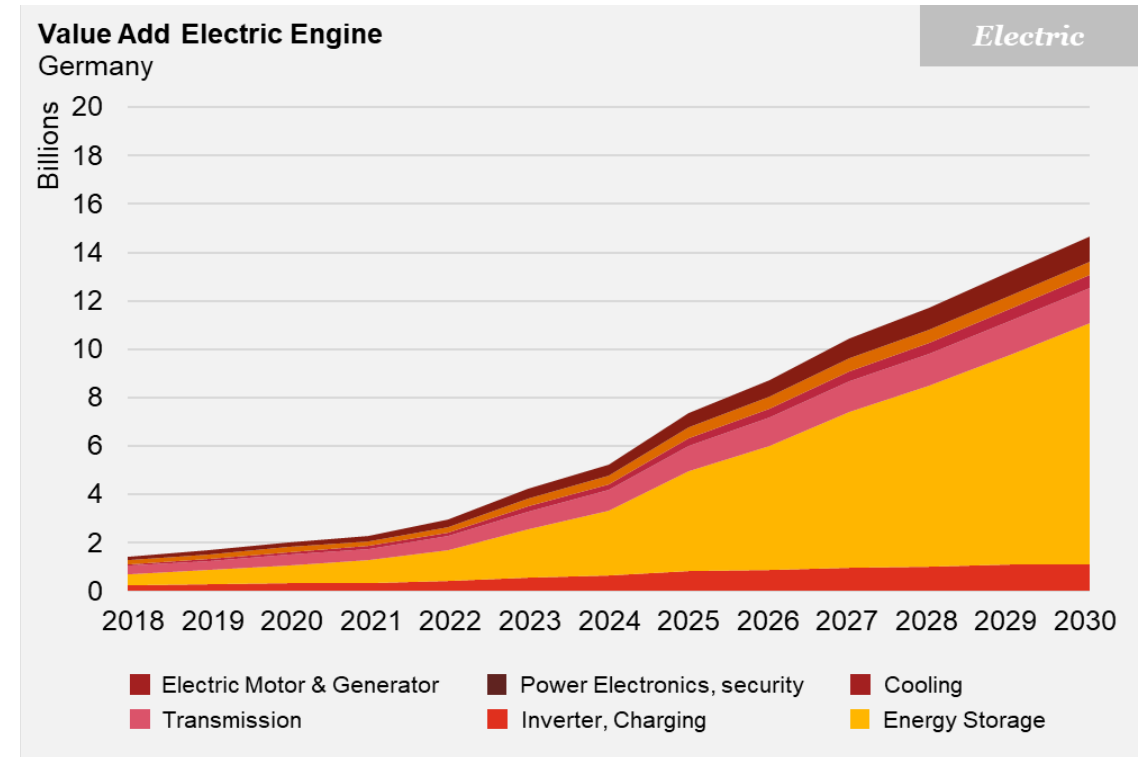
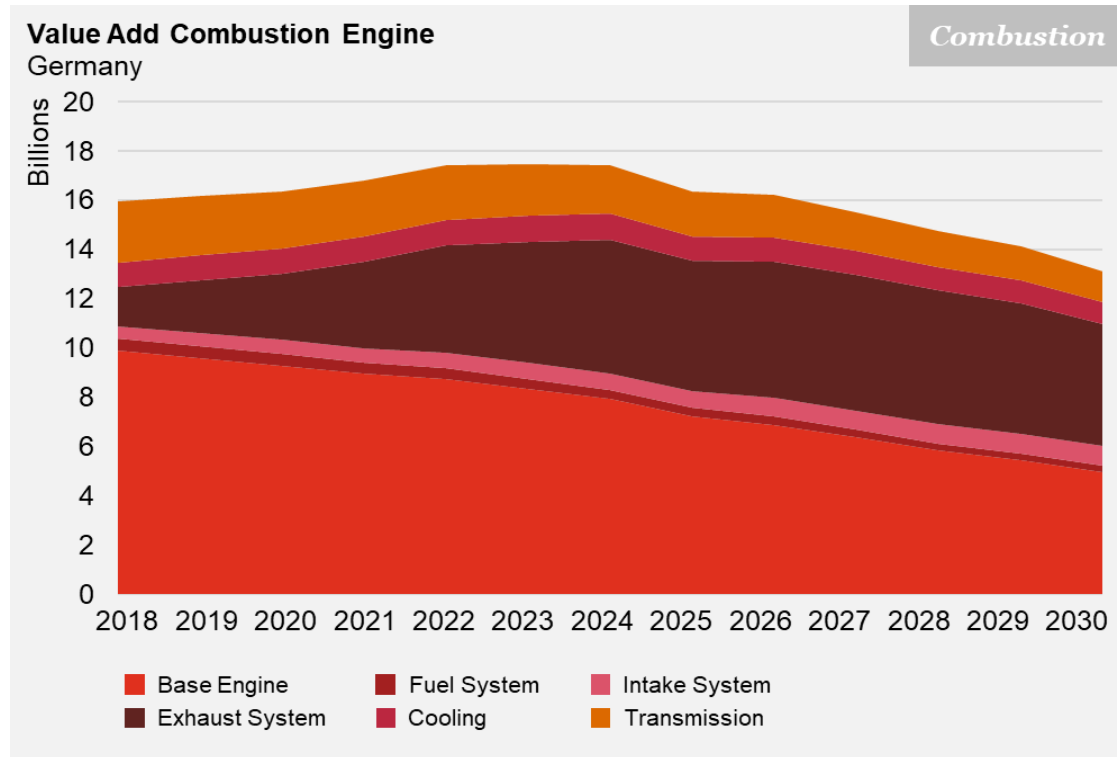
The pure electric powertrain will stay a niche until 2025 – which should leave enough breathing space for combustion

Vehicle Propulsion
2018 vs. 2025F (percentage share)



The transformation seems inevitable, but is not here yet

Combustion and electric engine vehicle outlook, value add 2016-2025F (Germany)

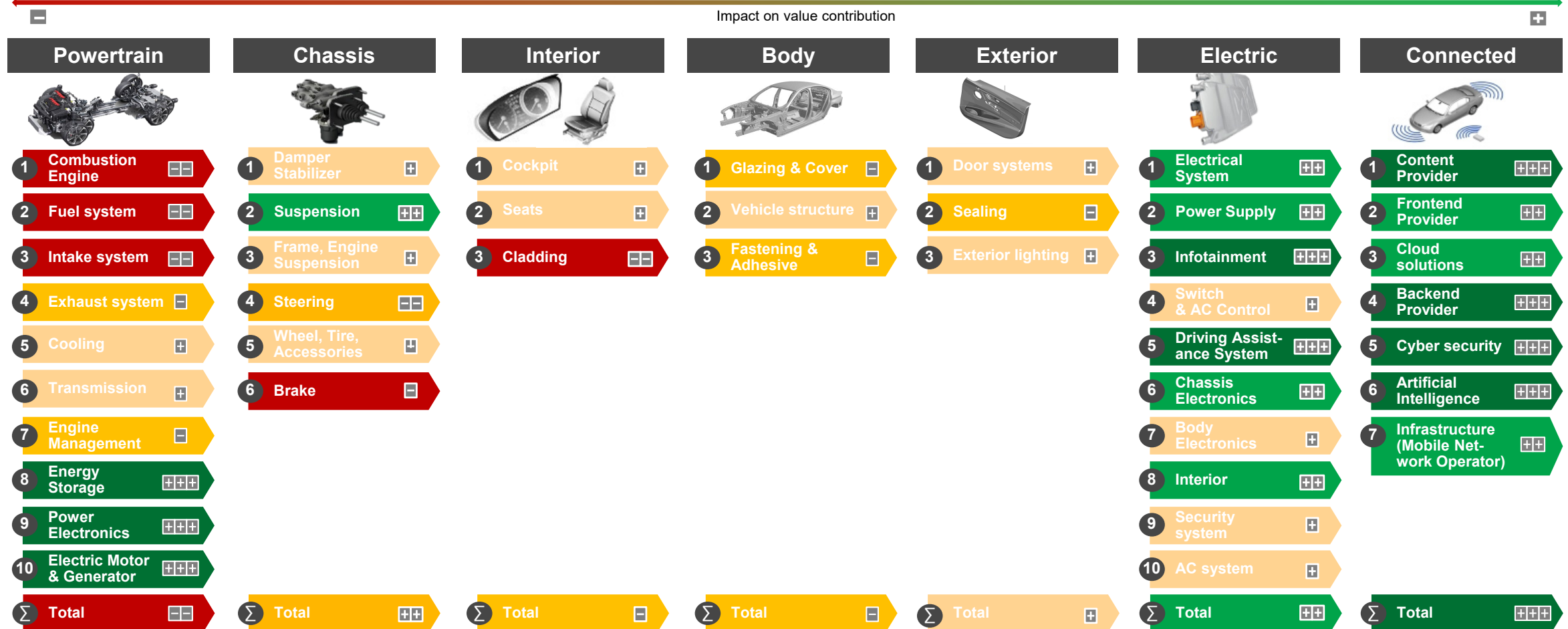


- **Stricter global CO₂ emission standards** require new powertrain technologies. The combustion engine needs significant innovations, especially **exhaust system**, to reach the new emission requirements.

- Even assuming **aggressive cost reduction potential**, the **fast rise** of electric drivetrain demand creates significant business opportunities, requiring fast decisions even today – but a **long-term strategy** and **large financial resources**.

The segment heatmap shows clear winners and losers in the upcoming transformation

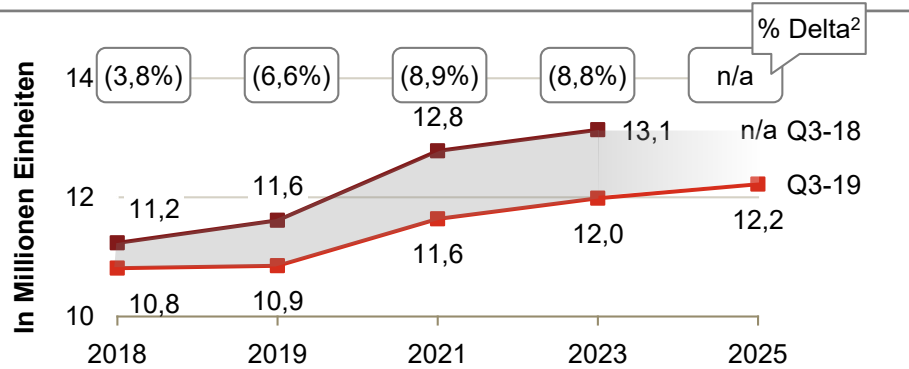
Powertrain most negatively affected – connected and autonomous with huge growth potential



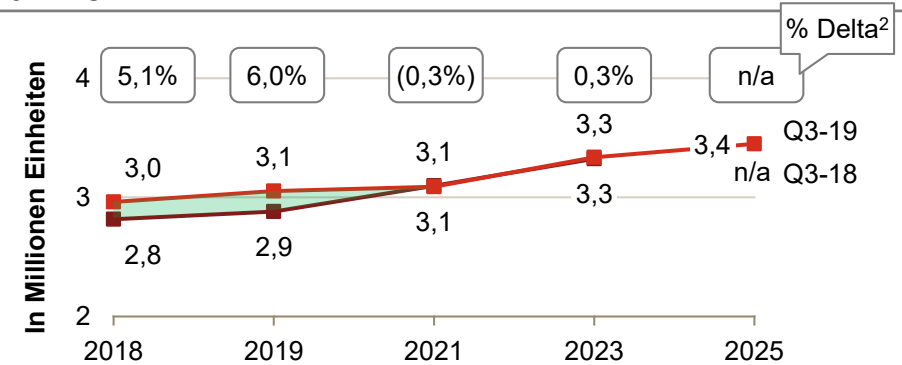
Industry projections show the impact of the current slowdown

Comparison of forecasts for selected OEMs, 2018-25 (Q3-19 vs. Q3-18)

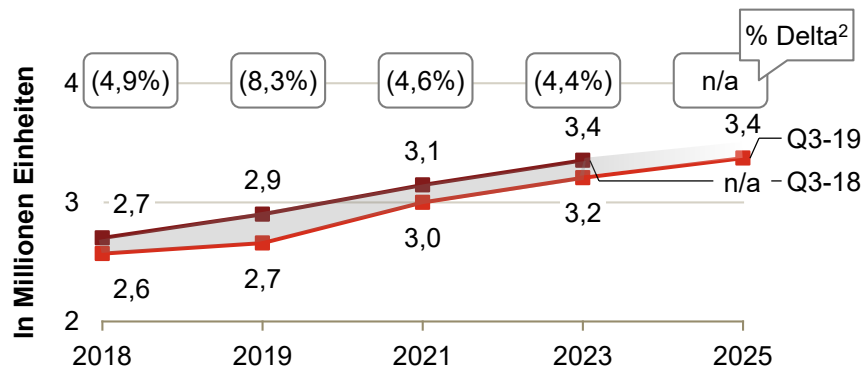
VW



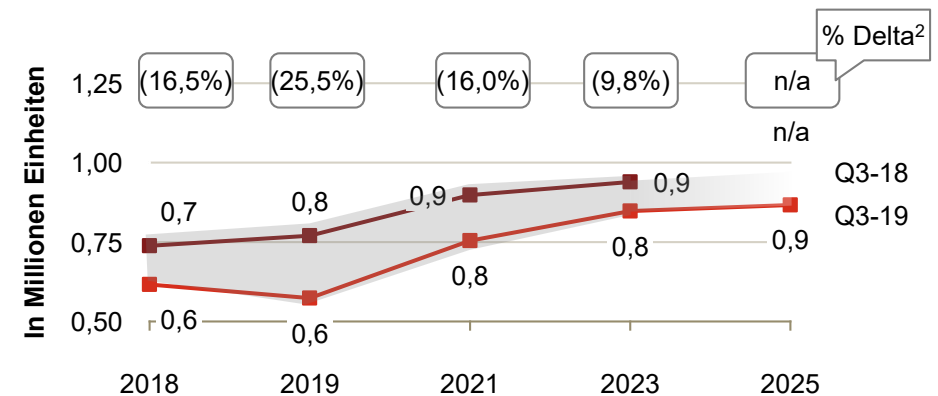
Daimler¹⁾



BMW



Jaguar Land Rover

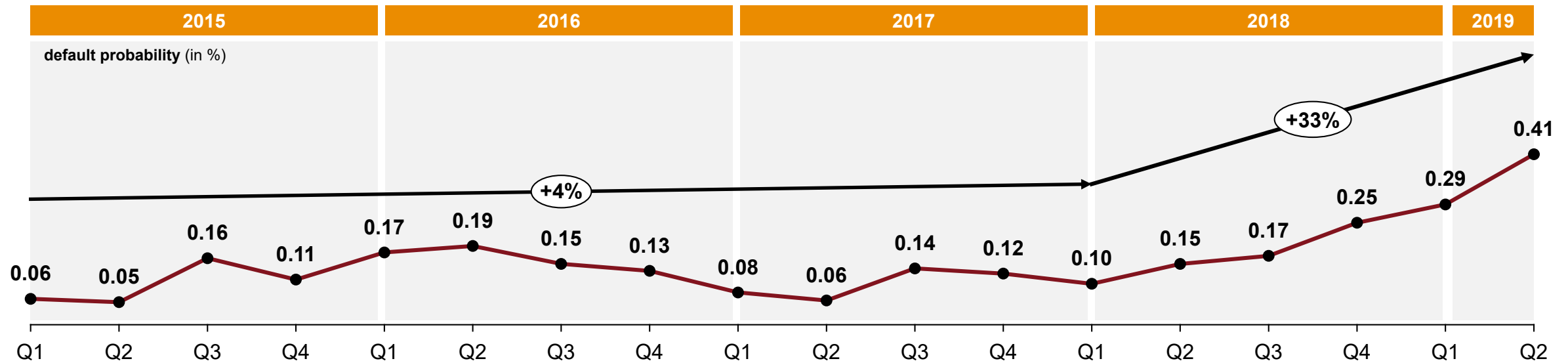



Quelle: PwC Autofacts (Q3-18, Q3-19) | Anmerkungen: 1) Vorläufiger forecast. 2018 actuals noch ausstehend.
2) % Delta Q3-19 vs Q3-18.

Legende: ■ positive Abweichung ■ negative Abweichung

Default risk for the leading suppliers increased significantly for the last 12 month

— Development of average default probability of 50 leading suppliers






Stagnating / moderate development of the default risk probability between 2015 and 2018
(CAGR: +4%)



Accelerating increase of the default probability since 2018
(CAGR: +33%)



Global trade conflict, weakening economic development in China as well as increasing expenditures for digitization and electro mobility as main drivers for sector development

However, the crisis is here



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Where

do

the problems

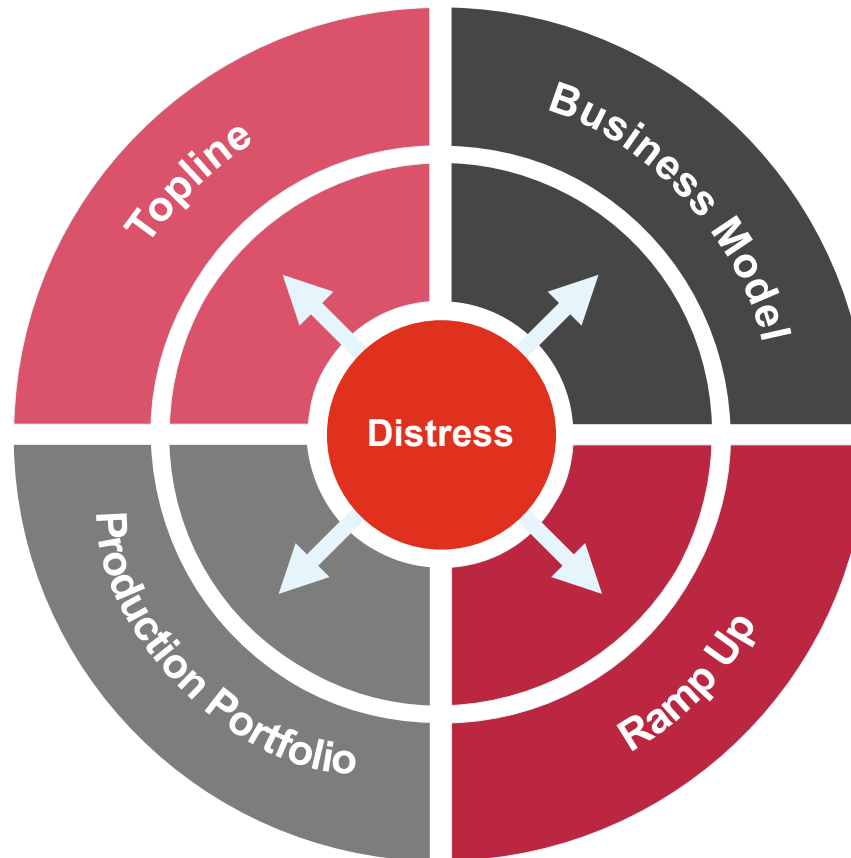
come from?

“Unfinished Homework” is the name of the game

Global: Four major topics

- Cooling down of certain markets reveals customer portfolio and order book risks
- Diversification will be required to ensure a balanced order book and revenue streams
- Evolution from combustion engines to electrical models will impact topline with market for the latter expected to grow by c.€13bn by 2030

- Typical product portfolios in distressed cases show over proportional ratios of complex and loss making products
- This is usually caused by weak transparency over calculated costs, actual cost and the bridge from nomination to serial production
- This leads to a lack of structure around processes regarding fact based, regular discussions with customers about technical changes and pricing for loss makers



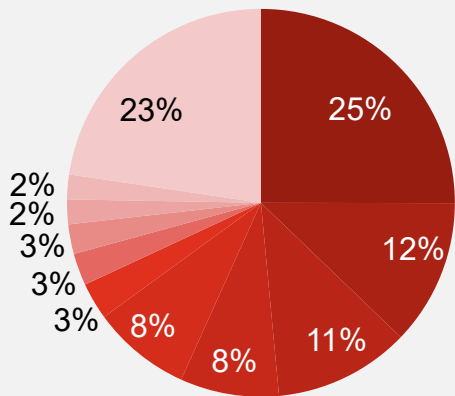
- Major disruption within the powertrain production (combustion vs electric engines)
- Critical view from debt providers
- Current sourcing trends increase supplier risk:
 - Significant pre-financing required
 - Unclear contract situations
 - Fixed raw material prices for lifetime

- Overshooting ramp-up costs destroy lifetime profits and cannot be recovered
- ‘Black holes’ before SOP create loss making positions. These typically include:
 - Unplanned scrap and higher resource need and personnel cost
 - Higher Investment need
 - Longer ramp-up phase
 - Lower steady-state margin

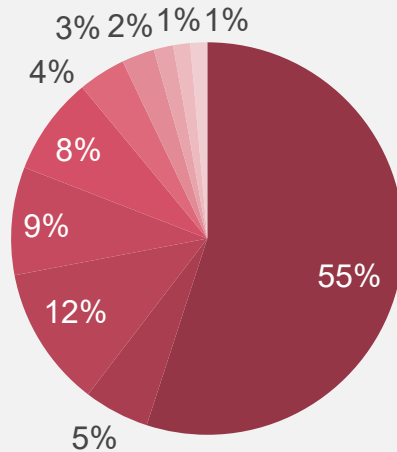
Top-line of suppliers under pressure – Short term risks vs. long-term growth

1 Topline: Cooling down of certain markets reveals order book weaknesses

'Balanced' customer portfolio

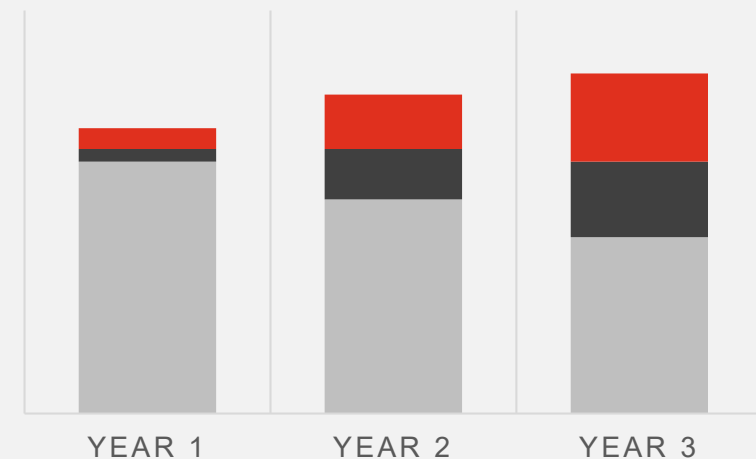


'Risky' customer portfolio



Orderbook analysis

■ Booked Business ■ Follow-up ■ Potential

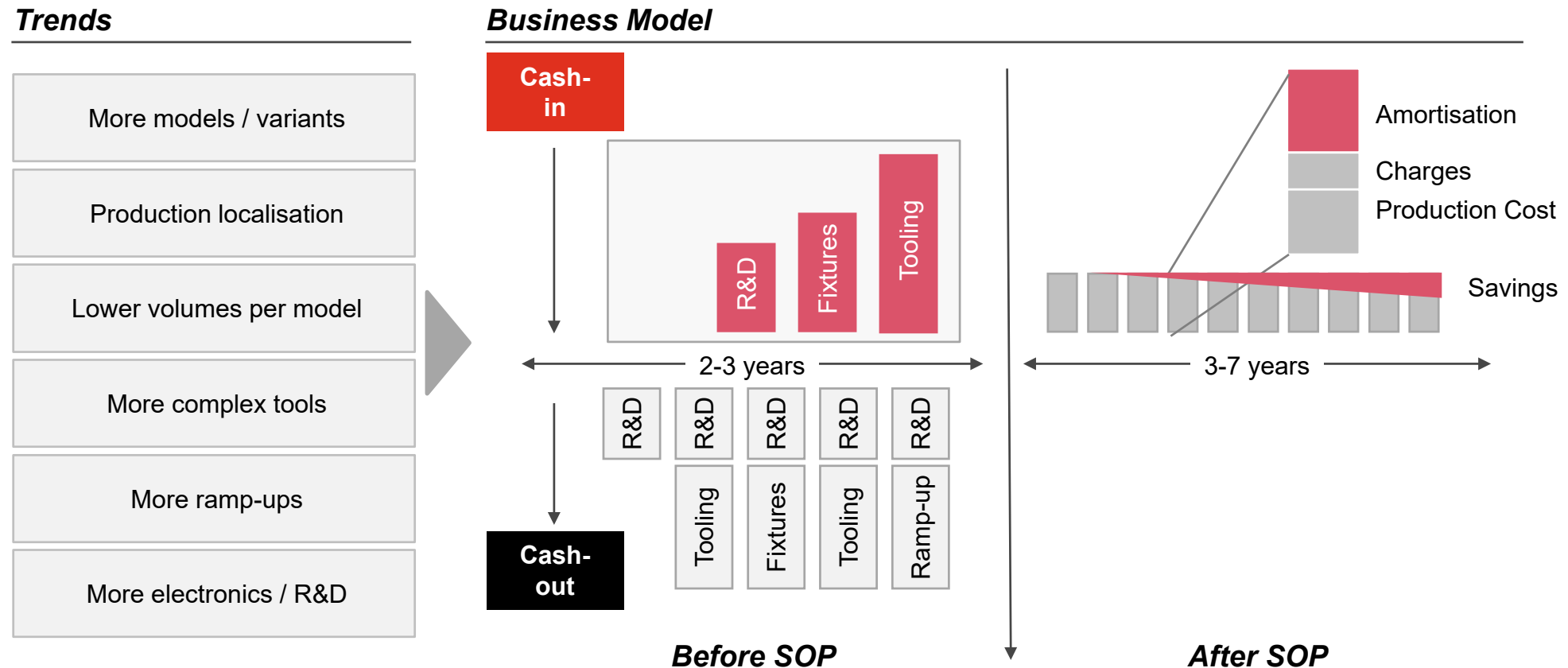


Questions to answer:

- Which dependencies exist on individual OEMs / corporations?
- Are there further dependencies or cluster risks based on tier 1- / tier 2 supply relationships?
- Which ranges are secured by booked business or follow-up orders? (incoming orders)
- For which customers and in which programs is the supplier active?

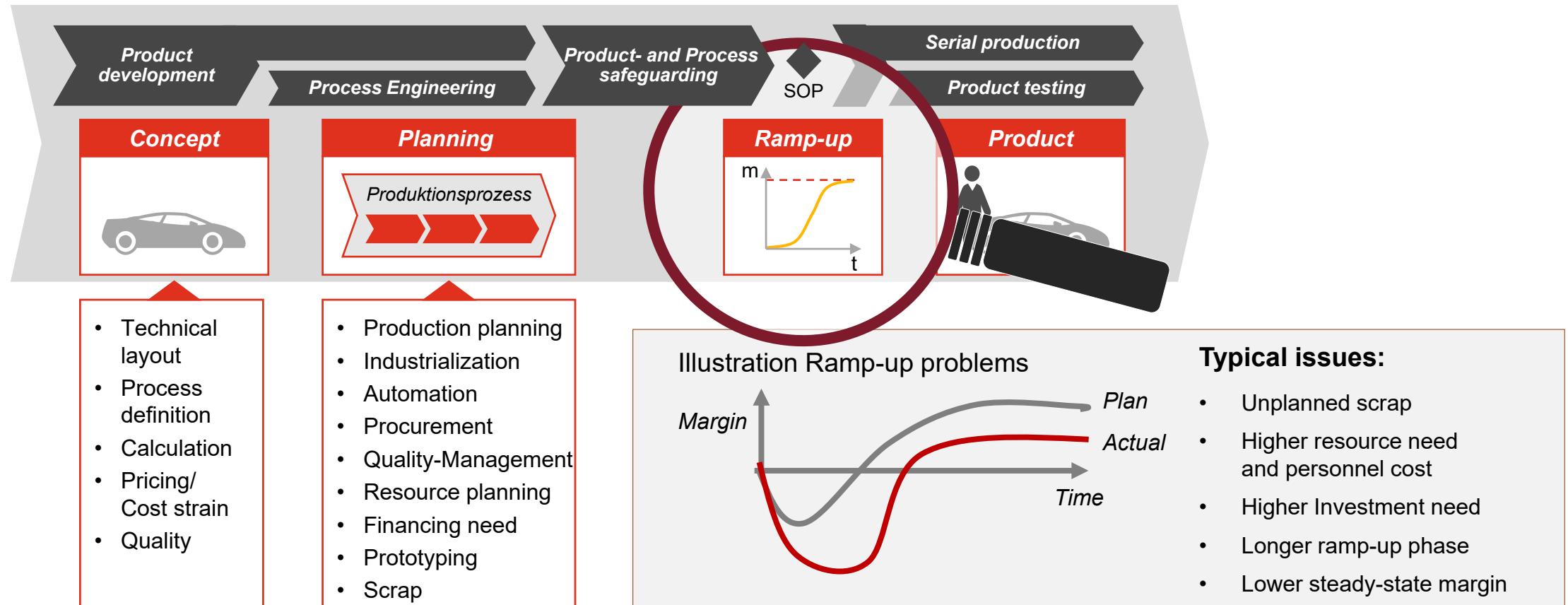
Current sourcing trends increase risk for suppliers...

2 Business Model: Pre-financing and OEM-risk (2/3)



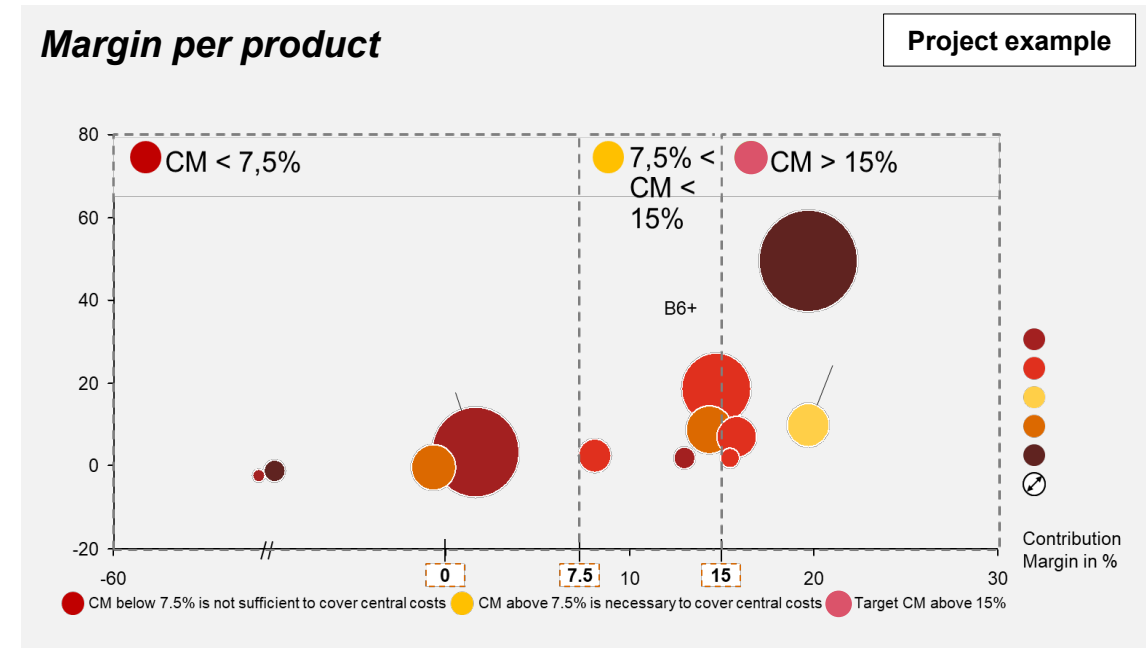
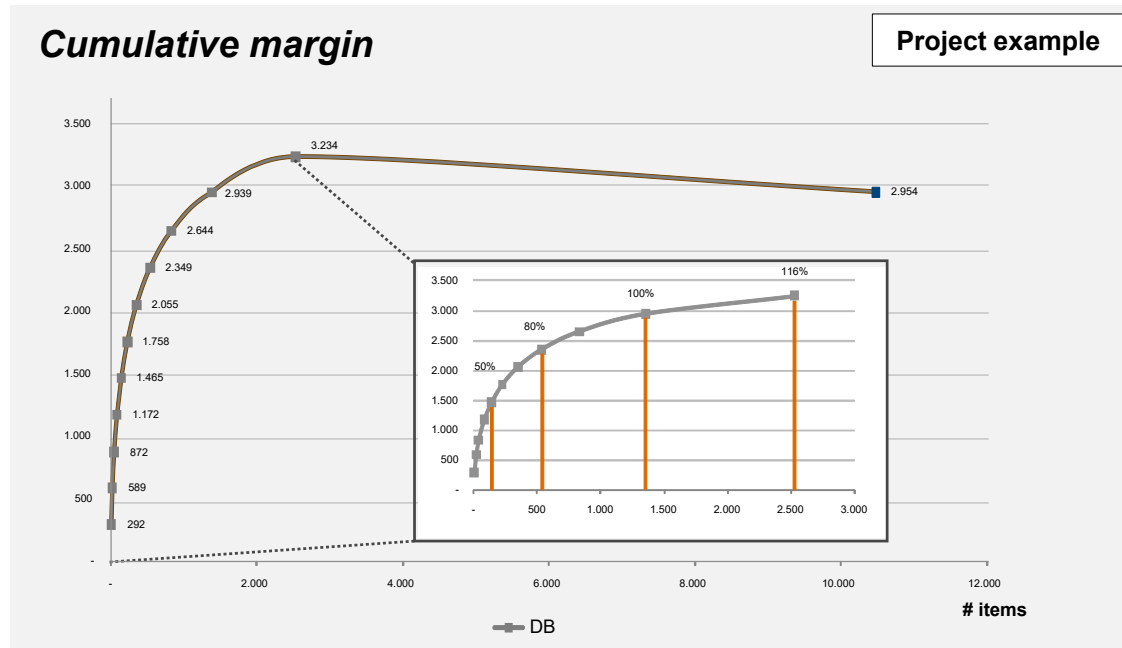
Overshooting ramp-up costs destroy lifetime profits and can't be recovered

3 Ramp-up: 'Black holes' before SOP create lasting loss situation



Addressing loss makers becomes crucial in a weaker automotive environment

4 Product portfolio: Loss makers and ongoing savings discussions



- Typical product portfolios in distressed cases show over proportional ratios of loss makers and complexity driving products
- Usually weak transparency on calculated costs, actual cost and the bridge from nomination to serial production

- Mostly weak contractual basis for price improvements during contractual phase
- No structured process for fact based, regular discussions with customers about technical changes and pricing for loss makers
- Usually weak on implementation of CIP measures and process

3

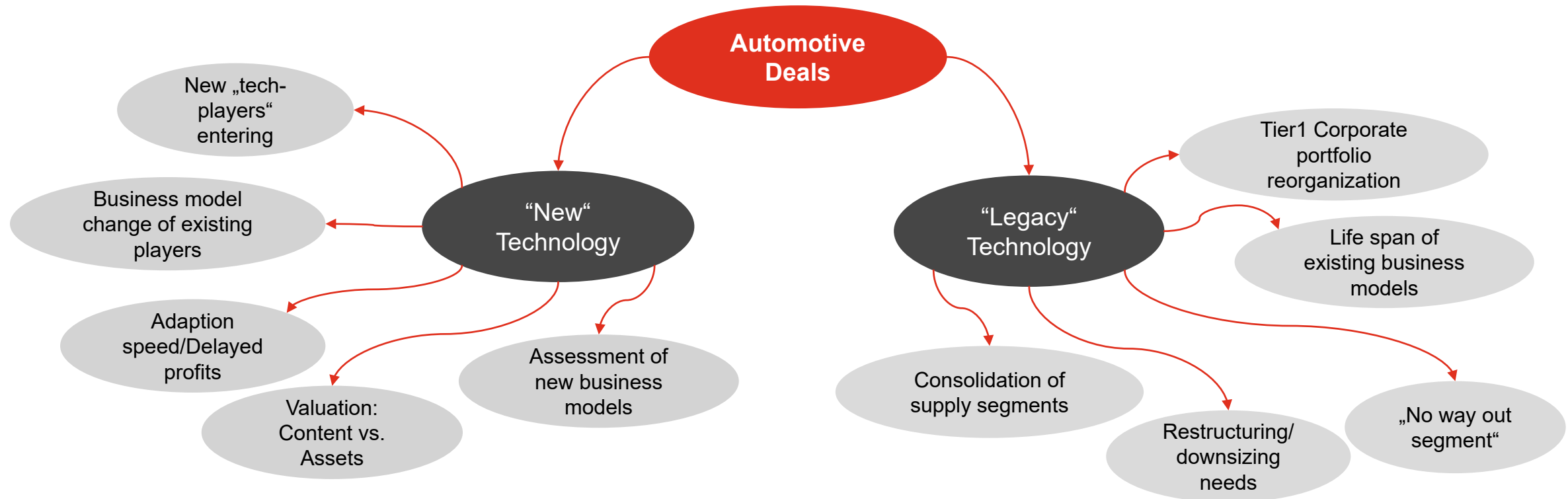
Restructuring

success

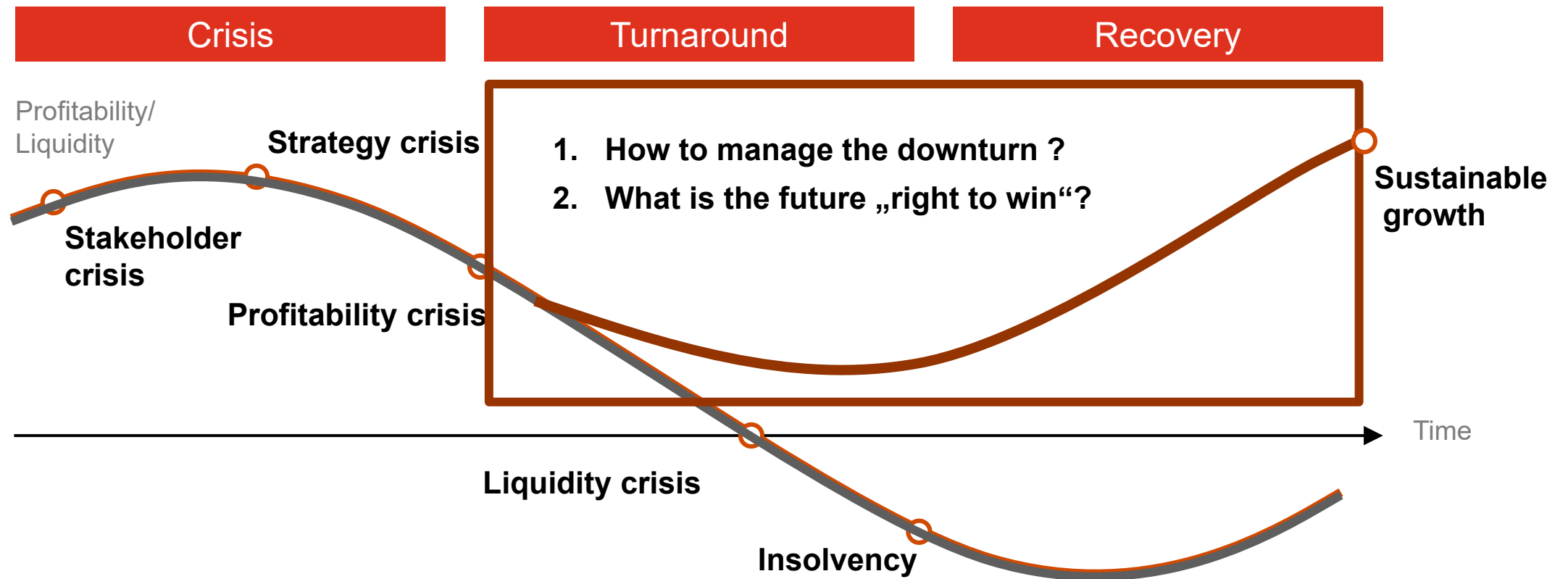
factors

Expect a more difficult automotive deals landscape for all stakeholders...

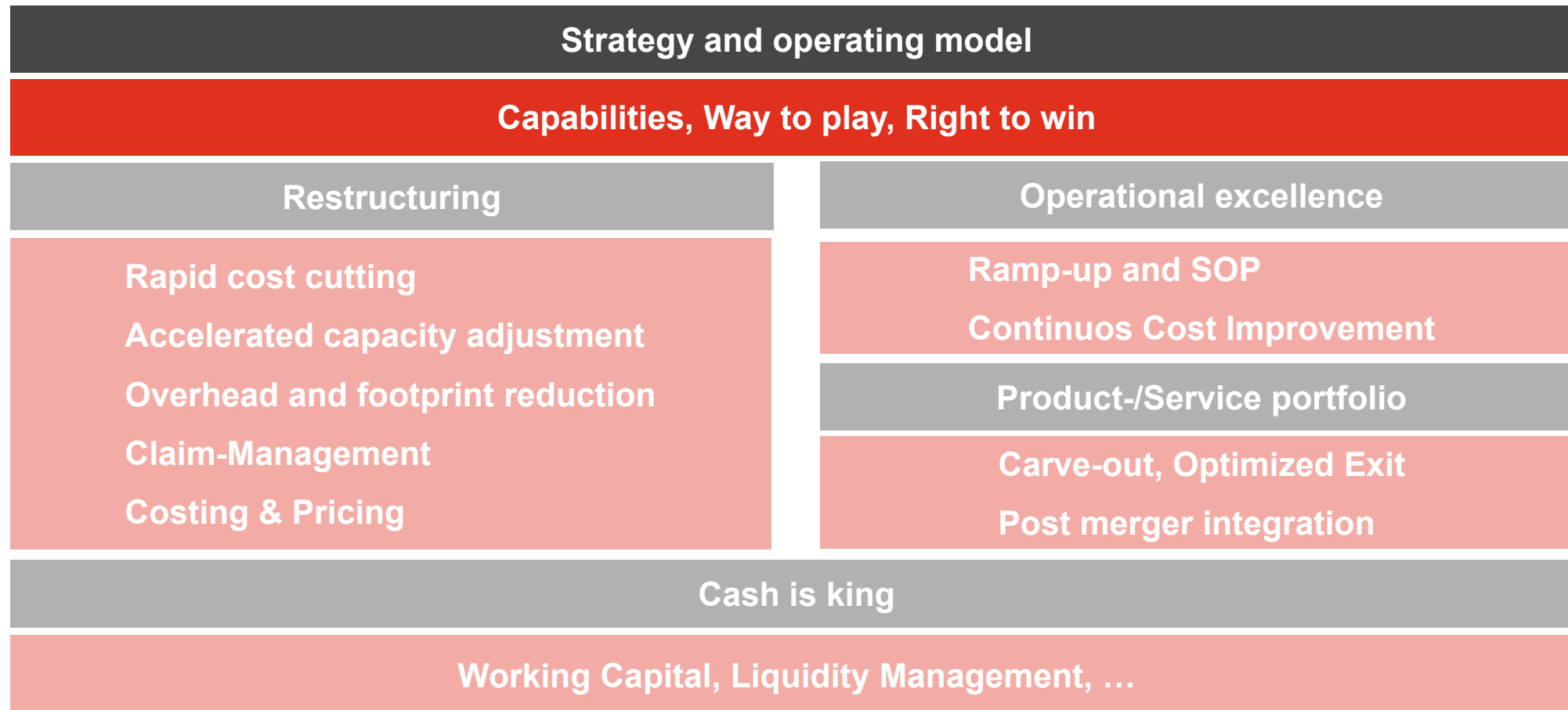
Global: Automotive deals landscape



What differentiates the future winners from the rest of the industry



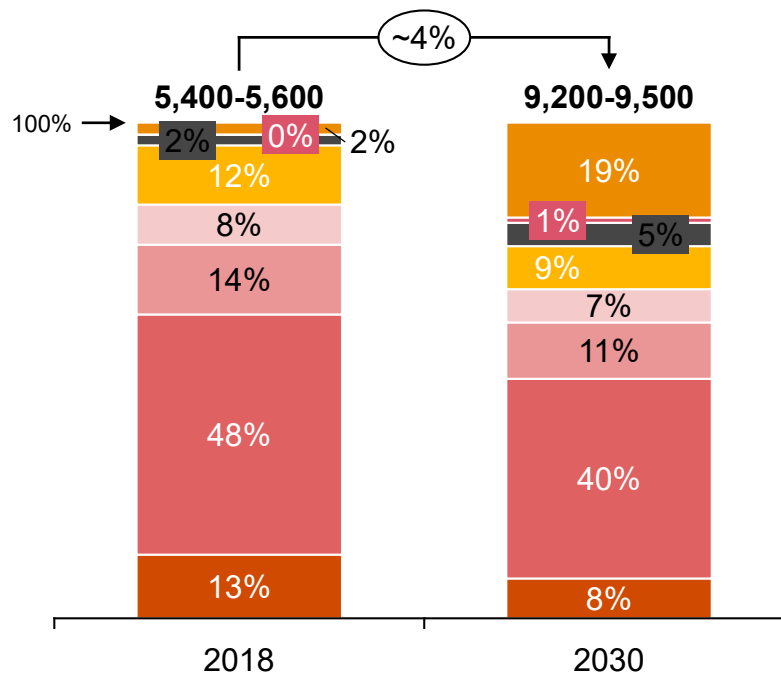
Strategy matters! Managing the downturn without a clear way forward is impossible



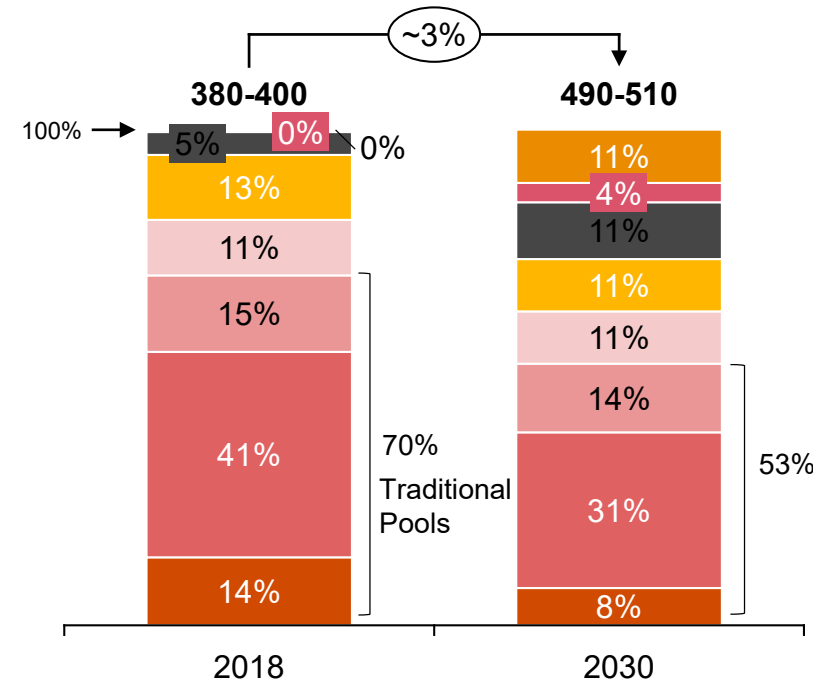
Strategy matters! Managing the downturn without a clear way forward is impossible

Significant shifts in global automotive value pools

Revenue distribution¹ (in \$bn)



Profit distribution¹ (in \$bn)



Key levers

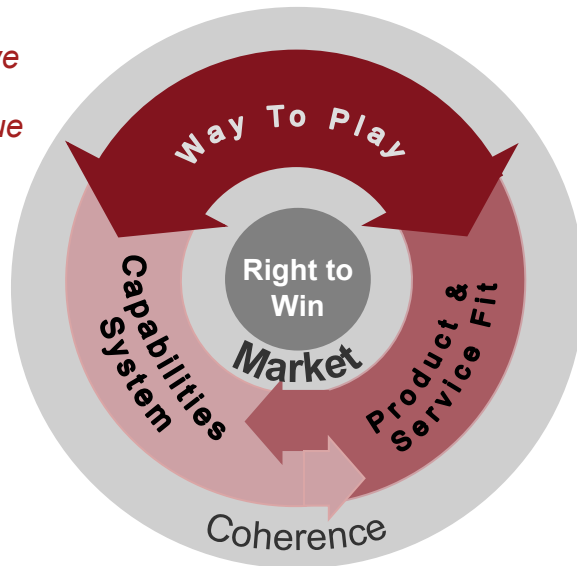
- Mobility as a Service (MaaS) increases **vehicle utilization** and vehicle wear and tear, leading to higher parts sales but a declining share of vehicle sales
- MaaS **fleet owners** emerge as an important new group of buyers, with higher bargaining power, leading to lower margins in aftermarket, financing and insurance
- **Autonomous features** increase vehicles' technical complexity, and the share of value provided by new tech suppliers. However, there are fewer collisions, cutting insurance and aftersales demand
- **Electric** powertrains are less complex than ICE equivalents and need less maintenance, which reduces traditional supplier revenue streams

Strategy matters! Managing the downturn without a clear way forward is impossible

Coherent way to play

A coherent company strikes a balance where the right product and service portfolio naturally thrives within a capabilities system consciously chosen and implemented to support a deliberate way to play within a defined market

How are we going to create value for our customers in this market¹⁾?



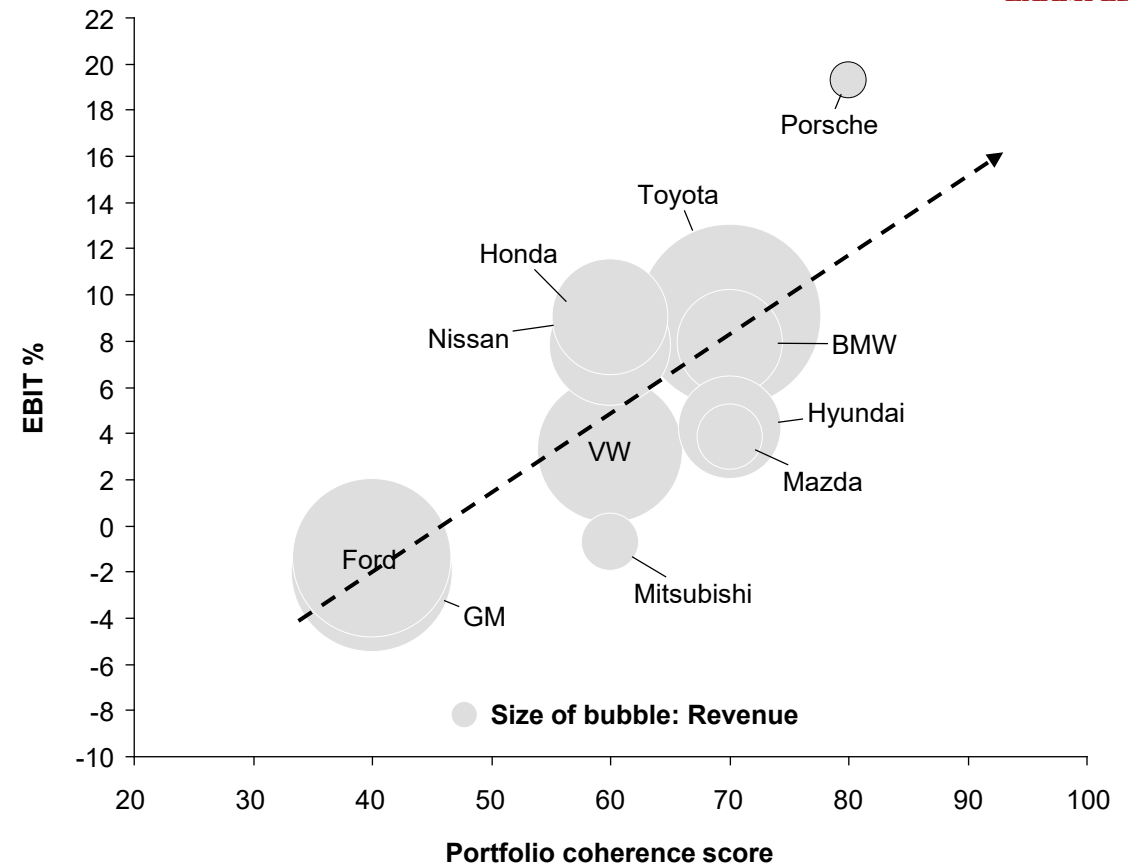
What are we going to sell in this market¹⁾ and to whom?

Companies with products and services that fit with a capabilities system have superior returns

What do we need to do well to deliver that value proposition? The engine of value creation is a system of 3 to 6 capabilities

Coherence premium – Auto OEMs

EXAMPLE



New roles require suppliers to refocus on selected capabilities



1) PwC Strategy& report “Transforming vehicle production: How shared mobility and automation will revolutionize the auto industry by 2030” 2) Strategy& analysis based on annual reports of several technology companies and suppliers; average R&D spent as percentage of revenue in 2018: 16% tech. vs. 6% supplier 3) Strategy& analysis based on OEM press releases 4) Tagesspiegel press release on Deutsche Bahn tickets 5) Strategy& analysis 6) PwC Strategy& report “Capabilities-driven restructuring – A manufacturing footprint strategy for a commodity automotive supplier industry”

Some lessons learnt from recent restructuring cases in the industry

- 1 Include the whole group of creditors (Banks, TCIs, OEMs) at an early stage in the process and consider individual positions and tactics
- 2 Generally, parties involved seem to be very alert: they position themselves in the early stage of the process
- 3 Stakeholders oftentimes ask for Restructuring Opinion (IDW S6) / IBR to be undertaken earlier than in the past
- 4 Cases tend to go into insolvency rather quickly (capex-heavy business models, unclear outlook on trends etc.)
- 5 Suppliers may be able to obtain support from OEMs if they are deemed critical e.g. improved payment terms and financing support
- 6 With volumes dropping dramatically and limited short term hope of returning, suppliers need to find ways to flex their fixed cost base

Thank you



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