Automotive manufacturers
- The technology behind autonomous cars is making rapid progress
- Pure electric cars are still behind expectations, but a new generation of hybrid models is expected
- Fuel efficiency and connectivity continue to be major trends

Suppliers
- Suppliers with advanced technologies outperform automotive manufacturers in terms of growth and margins
- Share of suppliers in overall value chain still increasing
- Consolidation process continues

This study analyses the performance, trends as well as chances and risks which will influence the future development.
1. GENERAL CONTEXT

The figures presented below show analysts’ estimations as at 30 November 2015. Estimations only consider listed companies. It is expected that automotive suppliers will continue to outperform the manufacturers in 2016. The performance of French automotive suppliers is remarkable considering the weakness of the French automotive manufacturers. Nevertheless, French automotive suppliers face a serious challenge in defending their market share.

INDUSTRY NEWS

Suppliers are challenged by the rapid development of technology, requirement of fuel efficiency and further globalisation due to planned overseas investments by manufacturers.

The eco-friendly mobility trend

China

Eco-friendly mobility is becoming more and more important on a worldwide level. China wants to implement China V gasoline in 2018. In several regions and major cities this standard will already be implemented by the end of 2015. Furthermore, several Chinese cities including Beijing and Shanghai imposed limits on new-vehicle registrations.

Electric cars

Although eco-friendly mobility is becoming more important, pure electric cars are not gaining the envisaged market share. Manufacturers and suppliers are focusing more on a new generation of hybrid cars which will be able to cover considerable distances with only an electric engine. Nevertheless, these cars must be economically beneficial for the customers to be successful.

Aluminium

Eco-friendly mobility also affects the materials used by manufacturers and suppliers. The share of steel in raw material cost structures is slightly but continuously declining, whereas plastic and aluminium are increasing. This trend results from the goal of using lower-weight materials in order to increase fuel economy. A further increase of aluminium is expected in the coming years as the EU, US and China have set efficiency targets regarding fuel economy.

On the other hand, the use of steel might be encouraged by a decreasing steel price which can be expected due to significant overcapacities.

The autonomous cars trend

Nearly every manufacturer as well as several suppliers are working on highly autonomous and self-driving cars. The companies are making significant progress in their development and are testing models on public roads. At the same time, more and more countries are permitting tests of self-driving technologies in certain areas or on certain streets. Based on manufacturers’ announcements, the first self-driving cars should be on the street between 2017 and 2020. This is not just a technical question, however, but the legal framework has to be defined too.

Investment trends

Globalisation remains an issue for suppliers as manufacturers plan new plants or extensions of plants overseas. Daimler invests in Brazil and also in a joint-venture facility with Nissan in Mexico. Audi and BMW are also constructing new plants in Mexico. BMW is currently expanding its factory in South Carolina. Volkswagen plans to raise its Chinese plant capacity to more than the previously targeted 4 million cars a year by 2018. Peugeot will invest in a new factory in Morocco. Despite these investments, European factories remain important. Production in the home markets is essential for the manufacturers as well as for both suppliers in order to keep and develop the technical know-how.

Future of diesel

The impact of the Volkswagen emission scandal is still unclear. This is not only true for Volkswagen and some suppliers directly affected by the scandal, but also for the other German car manufacturers. German car manufacturers depend on a high share of diesel cars in order to achieve the CO2 emission limits which will become effective in 2021. Peugeot and Renault are also affected due to the high percentage of diesel models in Europe (about 60%). Due to the Volkswagen scandal, there is a risk of stricter regulation for the manufacturers.
2. 2016 PERFORMANCE

Suppliers are expected to grow faster and become more profitable than automotive manufacturers. The innovation leaders are expected to keep their momentum.

General expectations for 2016

Analysts expect growth for the German and French automotive industries. A slight decrease in sales is expected for Volkswagen as a result of the emissions scandal in 2015. The increasing share of suppliers in the valuation chain is reflected in the higher growth rate assumption compared to the manufacturers.

The graph shows the expectations for 2016. Investments in expansions of existing plants or in new plants which are planned in the coming years are therefore not considered in the short-term growth estimates. However, these will have an effect on the development of the companies after 2016.

The graph only contains listed companies. The development of non-listed companies is therefore not considered in the graph.

Key success factors

The companies assumed to be the most successful show some common characteristics:

Innovation
The companies are innovative. Know-how in technology protects the margin and reduces price pressure.

Organic growth
The companies show strong organic growth. External growth is usually limited to selected add-ons of already successful business units.

Strong operative cash flows
The companies usually generate strong operative cash flows which allows them to invest in research and development and which enables the companies to expand globally.

North America

In 2015, the US new car market is expected to achieve the highest volume of new cars since 2001. Growth was driven by the high mileage of the cars which made car purchases necessary, and low vehicle costs due to low interest rates and oil prices which also made more expensive cars affordable. The US economy is expected to continue on its course of trajectory.

A higher share of sales in the US market has positive effects on the profitability of the automotive manufacturers and suppliers as the US market is the most profitable market. This is also due to the fact that capacities were reduced during the most recent crisis.

Mexico benefits from the development in the US as an increasing share of cars for the US market are produced in Mexico. Car manufacturers and suppliers continue to invest in new production facilities in Mexico.

Multiples

Based on analysts' estimates, German automotive suppliers are currently more highly rated than French automotive suppliers.

Asia

Although the GDP growth rate in China is declining, China is still expected to achieve a remarkable growth rate in 2016. The Chinese domestic market has become more powerful in recent years which is supporting growth. A tax cut for small car models with engines of 1.6 litres and below will also help to increase car sales in 2016. The measure became effective on 1 October 2015 and shall be in place until end of 2016. Chinese car manufacturers and Volkswagen, as well as their suppliers, will especially profit from this measure as their share in these car models is higher than the share of other – especially Japanese – manufacturers.

No turnaround is expected in India as the issues hampering a sustainable growth remain the same. Less than 3% of India’s population is paying taxes. India therefore does not have sufficient resources to finance the required infrastructure projects which would be key in promoting sustainable growth.

Europe

Some manufacturers and suppliers reduced capacities in order to achieve a higher capacity utilisation.

Nevertheless, sales development in Europe has been positive in 2015. A continuation in the largest markets in Germany, UK, France, Italy and Spain is expected in 2016. This should compensate for declining sales in Russia.

Multiples

Based on analysts' estimates, German automotive suppliers are currently more highly rated than French automotive suppliers.

<table>
<thead>
<tr>
<th>Multiples</th>
<th>Revenue multiple</th>
<th>EBITDA multiple</th>
<th>EBIT multiple</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2015e</td>
<td>2016e</td>
<td>2015e</td>
</tr>
<tr>
<td>Suppliers France</td>
<td>0.85</td>
<td>0.80</td>
<td>6.25</td>
</tr>
<tr>
<td>Suppliers Germany</td>
<td>0.96</td>
<td>0.91</td>
<td>7.62</td>
</tr>
<tr>
<td>Difference</td>
<td>0.11</td>
<td>0.11</td>
<td>1.38</td>
</tr>
<tr>
<td>Markup</td>
<td>13%</td>
<td>13%</td>
<td>22%</td>
</tr>
</tbody>
</table>

Source: Bloomberg LP
### Opportunities

**Advanced technology**

Advanced technology protects the margin. Several French and German automotive suppliers are at the forefront of technological development. These companies are covering technology which will be key in the coming years such as automated driving and plug-in hybrids.

**Interest rates**

Interest rates remain at a low level in the eurozone. This is supporting automotive sales in these countries as the majority of car purchases are financed with credit. Although many market participants are expecting an increase of the US interest rates, these may also remain on a low level as too strong an increase of the US dollar against the euro is not in the interest of the US economy. US car sales might therefore also profit from low interest rates in the future.

**Oil price**

The price of oil has declined significantly since July 2014. The lower price of oil is reducing the overall vehicle costs for the car owners.

### Risks

**China**

The slowdown of the growth rate and the shift from investment-driven to consumer-driven growth is a challenge for China’s provinces. China’s provinces are highly indebted. Indebtedness increased more significantly in recent years than GDP; Income and expenses in the provinces are not balanced. Hence, provinces sell land in order to generate additional income stream, but with a slowdown of the economy and risks in the real estate market, this income stream is also at risk. Furthermore, the sale of land is a rather finite business model. The financial health of the provinces is a major risk for China’s further development.

The share prices in China started to decrease significantly in the second half of 2015, which also bears risks for further economic development.

**EU, Russia, Brazil and India**

The overall economic situation could be a risk for the automotive suppliers. Russia’s market is declining rapidly. The crisis in several EU countries has still not been resolved and achieved a new peak in 2015 in Greece. Brazil is also showing weak development and India is also not on track.

**Interest rates**

Should interest rates in the US increase, refinancing costs of investments in US dollars will increase. Furthermore, the US market might be negatively affected, considering that 85% of car purchases are made on credit.

**Price pressure**

European automotive suppliers will be put under pressure by Asian automotive suppliers regarding prices in areas which are not considered high technology.

**Electric cars**

Electric cars are not gaining market shares as envisaged. Among the reasons for this development are insufficient travel distances and the number of electricity chargers. It is likely that in most countries the targeted number of electric cars will not be reached.

---

**Chinese and US market**

The US as well as the Chinese market are expected to grow over the coming years. Growth in China is also supported by an increase of credit-financed car purchases. At present, only about 26% of car purchases in China are made on credit. Furthermore, China now allows car manufacturers to securitise car loans in asset-backed securities products.

### Charts

**SHASHR Index**

Finally, the growth perspective in China might also be hampered due to pollution. Seven cities in China have already limited the number of new car registrations.

**1. Weakness of euro is supporting exports.**

**2. Growth of Chinese and US markets expected.**

**3. Low interest rates are supporting car sales.**

**Vehicle costs reduced due to declining oil price.**

---

**USA**

Growth of the US market is expected to continue. More car purchases in the US are being financed with credit. Furthermore, the relatively low interest rates might support the US car market. However, US new car registrations have declined significantly in 2014, especially for models which are not sold in China.

**China**

Growth in China is supported by the strong Chinese economy. Credit-financed car purchases have increased significantly in recent years. Furthermore, China’s provinces are highly indebted. Indebtedness increased more significantly in recent years than GDP; Income and expenses in the provinces are not balanced. Hence, provinces sell land in order to generate additional income stream, but with a slowdown of the economy and risks in the real estate market, this income stream is also at risk. Furthermore, the sale of land is a rather finite business model. The financial health of the provinces is a major risk for China’s further development.

The share prices in China started to decrease significantly in the second half of 2015, which also bears risks for further economic development.

---

**India**

Growth in India is expected to continue. At present, however, about 10% of car purchases in India are made on credit. Furthermore, India is still not on track to achieve an economic development which is key for the car market.

**Brazil**

Growth in Brazil is expected to continue. At present, however, about 25% of car purchases in Brazil are made on credit. Furthermore, Brazil is also not on track to achieve an economic development which is key for the car market.

---

**China**

Growth in China is expected to continue. At present, however, about 26% of car purchases in China are made on credit. Furthermore, China now allows car manufacturers to securitise car loans in asset-backed securities products.

**USA**

Growth of the US market is expected to continue. More car purchases in the US are being financed with credit. Furthermore, the relatively low interest rates might support the US car market. However, US new car registrations have declined significantly in 2014, especially for models which are not sold in China.
3. FUTURE TRENDS

#1 CONSOLIDATION.
Pricing pressure and investment requirements due to the technology development as well as due to increasing global coverage, led to a consolidation process which is expected to continue in the coming years. Mergers and acquisitions continue today; economies of scale are increasingly viewed as a key success factor, but also the largest players are also facing significant changes. The share of US automotive suppliers declined significantly in the last decade. Japanese automotive suppliers have the largest share at the moment, but this position will be challenged in the future by the German automotive supplier industry. Chinese automotive suppliers are still not well represented in the top 100. Considering the growing market share of Chinese automotive manufacturers, however, the role of Chinese automotive suppliers can be expected to become more significant in future.

#2 SUPPLIERS’ ROLE.
The role of suppliers is increasing within the automotive supply chain. In fact, suppliers are more essential than ever before. The percentage of passenger car value creation directly attributable to suppliers has been steadily increasing for decades. In 2015, this figure is expected to represent 82% of car value creation, an increase of 13 percentage points since 2000 and 26 percentage points since 1985.

#3 VOLATILITY.
Automotive suppliers will have to react rapidly to significant changes. 2014 and 2015 showed foreign exchange rate changes, oil price developments and political crises which had not been expected only a few months before. Investment decisions are therefore getting more difficult. The ability to adapt the business quickly together with a balanced portfolio and a natural hedge of cash flows will be key for future success.

#4 NEW PLAYERS.
The automotive industry continues to gain new market entries from Asia. Chinese and Korean suppliers either enter the market with low prices or by acquisitions of French or German suppliers. Due to the technological development, competition will also increase by new players coming from other industries.

#5 CUSTOMER NEEDS.
To stay competitive, suppliers need to match their value proposition to customer needs. Buying patterns have shifted considerably over the past decade due to changing consumer attitudes and the financial crisis (the average age of a new car buyer is now over 50). Younger generations are opting for new solutions such as car sharing, a service that can be contracted over the Internet with insurance policies included. In Germany, more than 1 million people are registered with one of the 150 carsharing providers.

#6 INNOVATION.
Advanced technology protects the margin of automotive suppliers. Aside from cost, the top three concerns for car buyers today are pollution, safety and technology. Manufacturers should focus on lightweight, fuel-efficient vehicles, equipped with web-connected roadside assistance and multimedia components. The “Internet of Things” is unleashing a variety of connected objects that will be integrated into tomorrow’s intelligent transportation solutions.

This development will also affect the lifetime of car models. New technology is coming from industries with much shorter development cycles. Furthermore, the technology used will have a significant influence on the brand essence. Therefore, car manufacturers are reluctant to open their systems to other players.

In addition, development of self-driving-cars is advancing rapidly. In 2015, Volvo became the first manufacturer to announce that it will accept full liability for collisions involving its autonomous cars. While pure electric cars are currently not gaining market share as envisaged, the new generation of full hybrid cars will be able to cover significant distances without petrol.
THE ROAD AHEAD

The mega trends continue to be safety, fuel efficiency and connectivity. Technology of autonomous cars is developing rapidly. Despite the recent fall in oil prices, fuel efficiency will gain further importance due to pollution. European automotive suppliers are well positioned in the relevant technologies to increase their share in the value chain. Advanced technology is also necessary to protect profitability. Without this, suppliers are under significant price pressure and subject to intense competition.

The market share of Chinese automotive suppliers is still relatively low. Considering the increasing market share of Chinese automotive manufacturers, Chinese automotive suppliers can be expected to grow. Due to its stronger presence, growth in China will also help European automotive suppliers to gain market shares against Japanese suppliers which currently have the largest market share in the world.

Significant changes over short periods of time in political environment, foreign exchange rates and raw material prices are challenging the automotive industry. Assessment of investments are more and more difficult. A balanced portfolio, a natural hedge of cash flows and flexibility to react quickly will be key for the long-term development.

Mazars continues to monitor the development in the automotive industry. Blazing the trail is the second study prepared by Mazars focusing on French and German automotive suppliers.

CONTACTS

Dr. Christian Back
Head of Automotive Sector, Germany
cchristian.back@mazars.de

René Koellen
Senior Manager
rene.koellen@mazars.de

Marco Bergmann
Senior Manager
marco.bergmann@mazars.de

Detailed information available on www.mazars.de

Photos: Thinkstock