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Equity Research from Kepler Cheuvreux

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Autos & parts

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Europe

Bavarian impressions – feedback from the 2023 Munich Auto Show (IAA)

Key points:

- Trading update reconfirms 2023 market outlook and fiscal year targets across the board.
- Stronger focus on tech than on vehicles; a clearly visible presence of new rivals from China.
- The show did not deliver any impetus for us to turn more positive on the sector.

Overall impressions

- General trend: Owing to e-mobility, digitalidation and assisted driving, the exhibition has continued to evolve into an event with a stronger focus on related technologies for cars than vehicles themselves. In our view, this clearly reflects the technological transformation. In our perception, some suppliers have run larger booths than their OEM customers. We think this is due to the fact that specifically incumbent OEMs are still in the early stage of the ramp-up process of their BEV products.
- Trading update: FY2023 outlooks were confirmed across the board (unsurprisingly though), suggesting the recent weeks developed in line with overall industry expectations. We believe to have sensed a very subtle optimism as regards H2. The general market 2023 market outlook as it was depicted by the industry during Q2 reporting was confirmed with global demand rising YOY in 2023. Demand in the US seems to be doing well. While demand in China is not seen down, it was still largely seen as trailing expectations. Increased price competitiveness there was flagged by most OEMs we met. While everyone vowed not to participate in this game and to rather sacrifice volume for the sake of pricing and margin (emphasising their respective value over volume strategies), we remain cautious about this – the proof is in the pudding. Positive statements on China by singular OEMs and suppliers were in our perception largely related to company-specific short-term product cadence there. We are left with the impression that the situation in Europe has improved mildly as of late. We picked up some first indications that the industry is seeing chances for a global volume increase in 2024.
- Chinese competition: Chinese OEMs and technology suppliers had a very visible presence on the show (BYD runs in our perception one of the largest, if not the biggest booths of all). In our readout, this is also clearly emphasising the country's ambition to become a global force and to seize the opportunity provided by e-mobility in this context. Incumbent OEMs' comments suggested they all take Chinese newcomers very seriously, admiring their speed of product rollout and innovation as well as overall technological capabilities. However, there does not seem to be any panic persisting either. Brand equity and design as well as forthcoming product offensives were flagged as key differentiation factors by incumbent OEMs. While traditional OEMs will launch a plethora of fresh products in the 2024-27 period, this nevertheless means the litmus test still has to be run. We think this implies that investors' concerns about long-term shifts to the disadvantage of traditional OEMs is highly likely to continue persisting beyond the short term. German OEMs extended a plea for free trade in viewing Chinese newcomers as healthy competition. In our view, it will take some years for incumbent OEMs to demonstrate their ability to catch up with newcomers. This is simply owing to their respective product and technology schedules.
- Technology: The industry made another clear plea in favour of powertrain electrification (however, BMW expressed in that regard some concerns about the rigidness of politics to phase out combustion engines in Europe). Every incumbent OEM showcased all-new or concepts of soon-to-be-launched product in an attempt to clearly transfer the message that the race to catch up with newcomers is on. Concerning powertrain electrification, the focus was on extension of range, chiefly through new battery chemistries, and reduction of recharging times to enhance utility for consumers. Next generation electric powertrains are supposed to bring significant cost reductions versus current ones to improve economics of BEV for consumers, too.
- The single biggest surprise: Mercedes-Benz' CFO deliberated, if industrial operations could well be run with zero net cash (as opposed running it with ample net cash now), suggesting not all of the current net cash had to be viewed as a safety cushion. In our opinion, if meant seriously, then this would represent an entirely new approach, creating the vision of potential of more cash returns for shareholders, since up to now industrial operations are typically run with net liquidity positions including significant amounts of excess cash. However, we think this has to be taken with a pinch of salt. In our interpretation, this point was aimed more at underscoring the future cash conversion strength of MBG's operations. We also note that Schaeffler's management expressed a high level of confidence to exceed the self-imposed order intake target for e-mobility components.
- Conclusion: Overall, the event did not deliver any reason for us to turn more positive on the sector. Industry participants are aware of the challenges ahead, but sequentially weaker mix and more competitive pricing (particularly in BEVs) and cost inflation (e.g. wages) provide short-term headwinds.

Feedback on selective company presentations

- Mercedes-Benz (Hold, TP EUR79; represented by Harald Wilhelm, CFO): The group's appearance centred on the presentation of the CLA concept. The model is due for the launch of serial production in 2024 as the first vehicle derived from the electro-centric MMA architecture which covers the compact segment. We understand the architecture will feature many of the technologies of the record-breaking Vision EQXX. Powertrain efficiency takes energy consumption to 12kWh/100km and allows ranges of up to 750km, depending on battery technology (LFP for entry level version, NMC for the more upmarket versions). In our perception, MBG clearly aims to underpin technological leadership among incumbent OEMs. We understand MMA is constructed such that its supports BEV-ICEV margin parity in the long run. As for the trading update, MBG reconfirmed the FY2023 guidance. Management stated that the order book continues to support high levels of capacity utilisation throughout this year and they saw no reason to presume that 2024 would be weaker demand-wise than this year. Management made clear again that they aimed not to participate in any price wars and were rather willing to sacrifice volume for pricing. As for China, we have the impression though that the business seems to be largely carried by its ICEV portfolio, which can be viewed as positive for short-term margins.
- Volkswagen (Buy prefs, TP EUR205; represented by Dr. Arno Antlitz, CFO): Management stated that the recent weeks had developed in line with the outlook given during Q2 reporting, reconfirming the FY2023 targets. We understand that the order book recently shrank by 150,000 units to 1.55m due to better parts supply and logistics. In managements' expectations, flooding in Slovenia could wipe out some 100,000 units in production in Q3, which will have to be caught up with at a later stage. While overall pricing has been increased by 3-4% globally in the recent weeks, that for BEVs has not. The Q3 margin is expected by the company to come in at the lower end of the 7.5-8.5% margin target range. In China, the next two years will be spent to upgrade BEV product substance and to lower corresponding cost with MEB+ and LFP batteries as the key tools. The recently announced cooperation with Xpeng in China was described as complementing the existing BEV product plans and hence not stealing volumes from MEB. The idea of a share buyback programme was declined (unsurprisingly though, in our view). For 2024, VW aims for a rise in volumes of some 5%, in line with what it also expects for the global market by then.
- BMW (Reduce, TP EUR90; represented by Ritu Chandy, Head of Treasury and IR): Besides a trading update, the company focused very much on Neue Klasse, the family of BEV product to be derived from the company's first purpose-built BEV architecture. It was made clear that Neue Klasse is more than a BEV-only architecture, as it serves as a launch vehicle for a bundle of new technologies in the area of ADAS as well panoramic head-up displays and the change from prismatic to cylindrical cells (BMW will also launch LFP as cell chemistry with Neue Klasse)- We understand that Neue Klasse will start in 2025 with vehicles of the dimensions of the 3series and X3, which embody the entry levels for family. BMW reiterated that six models will be launched off Neue Klasse within 24 months as of 2025. The underlying architecture is designed to reach parity of contribution margins from BEVs with those of ICEVs by the end of the decade, once volumes have ramped up. We understand that the reduction of battery costs is key for cost reduction (50% reduction on pack level), as are additional efficiencies in the production system. Unsurprisingly, the 2023 financial guidance was reconfirmed with the recent weeks having developed in line with expectations. In our interpretation, BMW feels confident to be able to outperform the market in China in the short-term.
- Schaeffler (Buy, TP EUR7.5; represented by Matthias Zink, CEO of Automotive Technologies division): The company supported all arguments we used for our upgrade from Hold to Buy after the share's fall post Schaeffler's Q2 reporting in early August. Management made clear that the recent weeks since Q2 reporting delivered all grounds to support the upgraded guidance (which was consequently reiterated). We flag that the company displayed a high level of confidence of over-achieving the target of a EUR2-3bn order intake for components for e-mobility, noting that the EUR1.0bn order intake, which was posted in H1 was a negative in the eyes of the investment community and had it doubt the FY2023 order intake target. Delayed product launches in China will finally take off in H2 2023, thus also giving additional impetus to the top line, in our view, and contributing to fixed cost absorption. We think all of the above has the upgraded FY2023 guidance as per Q2 reporting, which the market was doubtful of at that time, appearing plausible.

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Company	Rating	Target
Daimler Truck	Buy	EUR41.00
Gestamp	Buy	EUR5.50
Michelin	Buy	EUR38.00
Stellantis	Buy	EUR27.00

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Company	Rating	Target
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ElringKlinger	Reduce	EUR6.70
Volvo Cars	Reduce	SEK38.00

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