



ATLANTIC

FINANCIAL GROUP

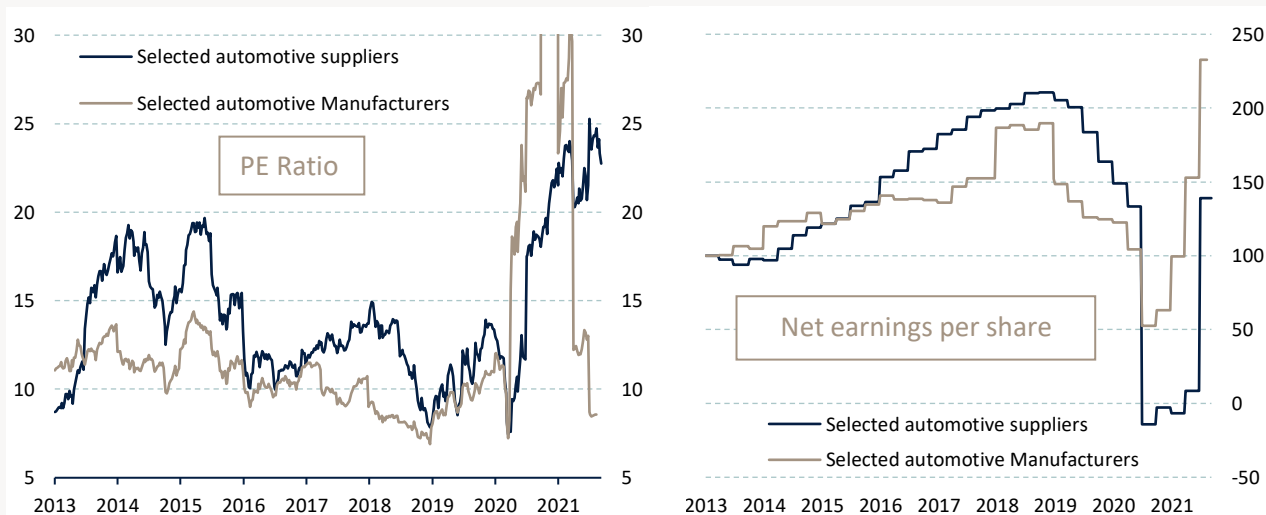
Weekly Investment Focus

September 13, 2021

"AUTOMOTIVE EQUIPMENT SUPPLIERS AT THE HALFWAY POINT".

- ◆ The relationship between manufacturers and subcontractors is often the key to success...
- ◆ ... to meet the new challenges facing the automotive sector
- ◆ Recent results are encouraging in Europe, mixed in the US

CHART OF THE WEEK: "PEs still showing a cycle bottom with depressed net results"



Source: Bloomberg, Atlantic Financial Group

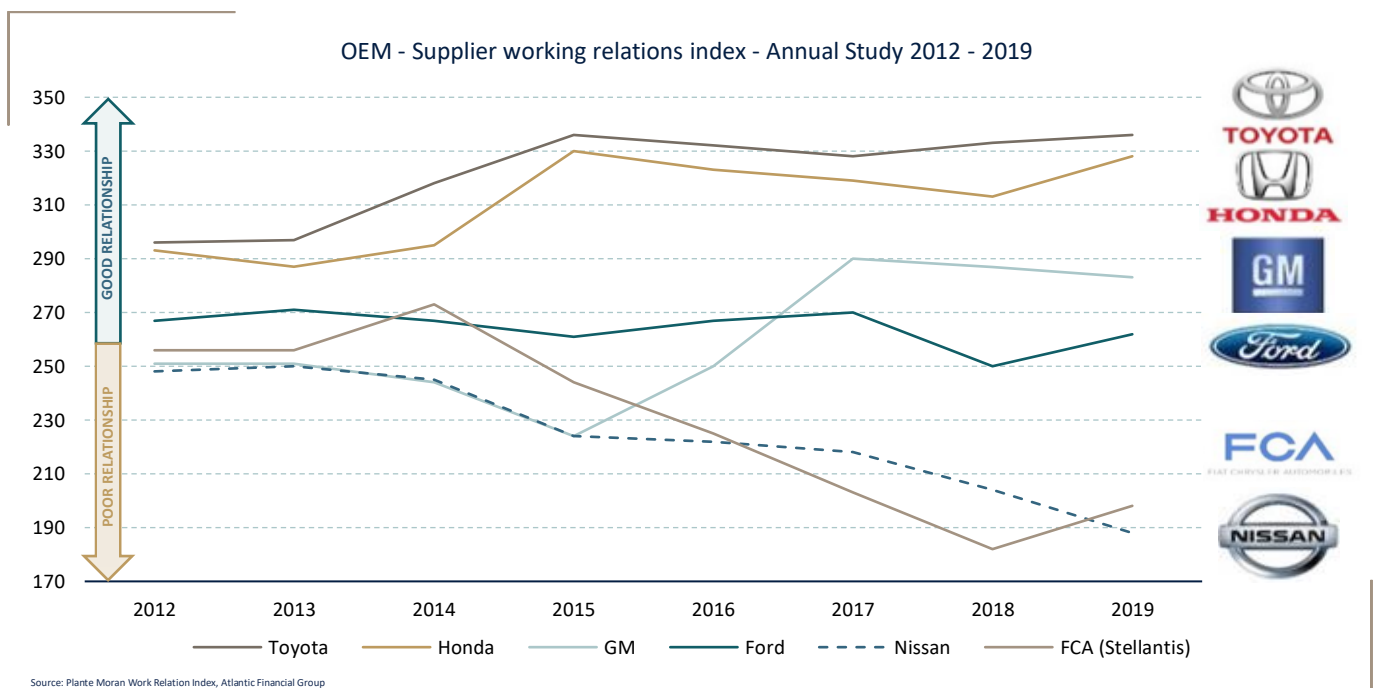
ANALYSIS OF FINANCIAL MARKETS

US automotive suppliers have performed very well over the last twelve months, up 59%. In Europe, the 12-month performance of automotive suppliers is less impressive up 24% vs 29% for the euro Stoxx 600. Valuation multiples are still at high levels, while **investors are already anticipating a strong recovery in new car sales, supported by subsidy programs**, especially for the purchase of electric or hybrid cars.



Over the past decade, automobile suppliers have enjoyed a valuation premium over automakers. However, the latter are expected to produce higher net earnings this year than in 2019. The results of the subcontractors should only recover their 2019 levels next year. The market may have been too quick to anticipate the rebound while results still appear depressed. **The shortage of semiconductors has slowed the production chain and the low number of cars produced is penalizing subcontractors whose business model is based on economies of scale.** For their part, carmakers have managed the slowdown by giving priority to selling the highest value-added models, ignoring volumes.

Fig. 2 - Index of labour relations of Japanese and American car manufacturers



◆ **The relationship between manufacturers and subcontractors is often the key to success...**

Historically, **the working relationship between automotive manufacturers and suppliers has not always been a good one. In fact, they have sometimes been adversarial**, which was not good for either party. Plante Moran's new Workplace Relations Index (WRI) study shows that supplier relationships significantly influence the competitive dynamics of the automotive industry, especially in times of uncertainty.

Resource constraints due to the continuing COVID-19 crisis, as well as chip and material shortages, have challenged the major car manufacturers and auto-parts suppliers. **The strategies developed over the past decades of minimizing inventories (just-in-time policy) and manufacturing where labour is cheap (globalization) are now being challenged.** For manufacturers, good relationships with their suppliers have therefore become essential to secure the supply of parts.

Beyond the Covid-19 crisis, **the transition to electric vehicles has accelerated** and the manufacturer-supplier relationship is also becoming a guarantee for success. **Many suppliers, who support the production of internal combustion engines (ICEs), are also working on the electrification of vehicles.** The

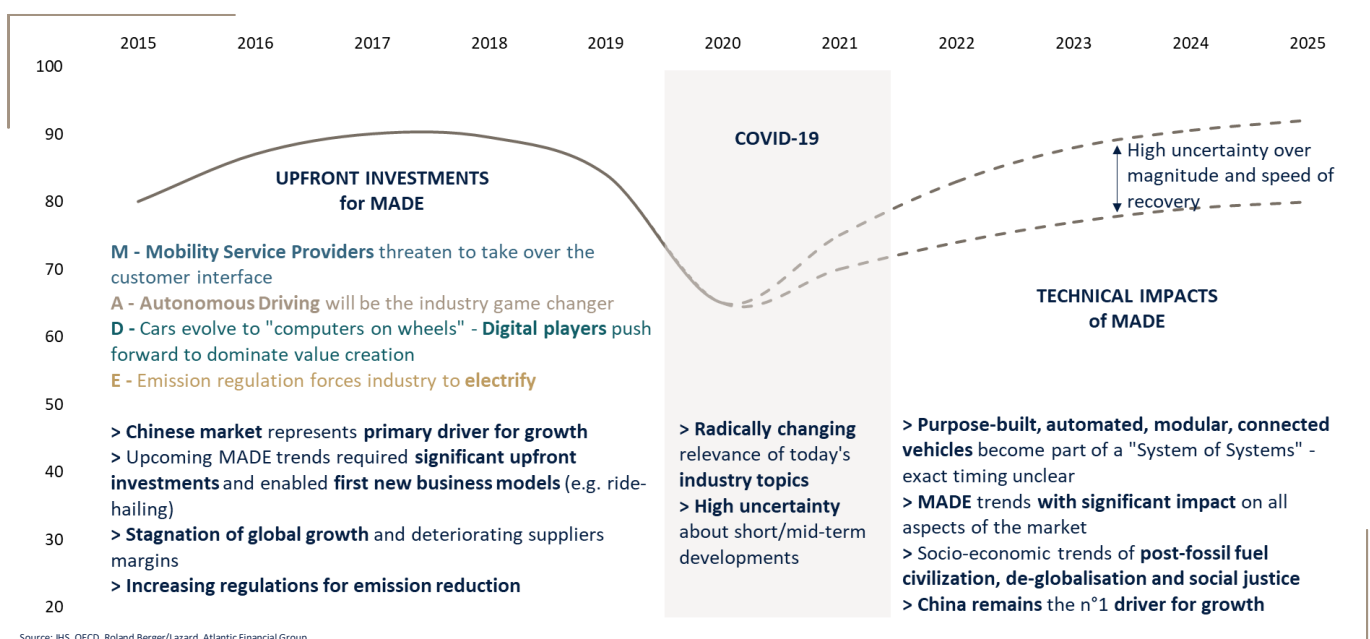


transition must be made in a good understanding so that manufacturers and suppliers can optimally allocate their capital and workforce (see Fig 3).

Finally, **cost competitiveness has always been the major source of friction between automotive OEMs and suppliers**. Here again, it turns out **that greater transparency on cost models from suppliers** shortens negotiation times, helps minimize expenses and **benefits all players in the production chain**.

The automotive industry has many challenges to overcome, and **the leaders will be those who establish best business practices throughout their production chain**. The top-ranked automotive suppliers in the Workplace Relations Index (WRI) today are also among the industry leaders: Toyota, Honda and GM (see Fig 2). Good corporate governance is therefore paramount. **#ESG**

Fig. 3 - Light vehicle sales - what's changing?



◆ The new challenges facing automotive suppliers

Market trends such as **the use of lighter materials, vehicle electrification, and the transition to alternative fuel powertrains** will disrupt the automotive industry. Automotive suppliers will be pushed to **spend more on research and development**.

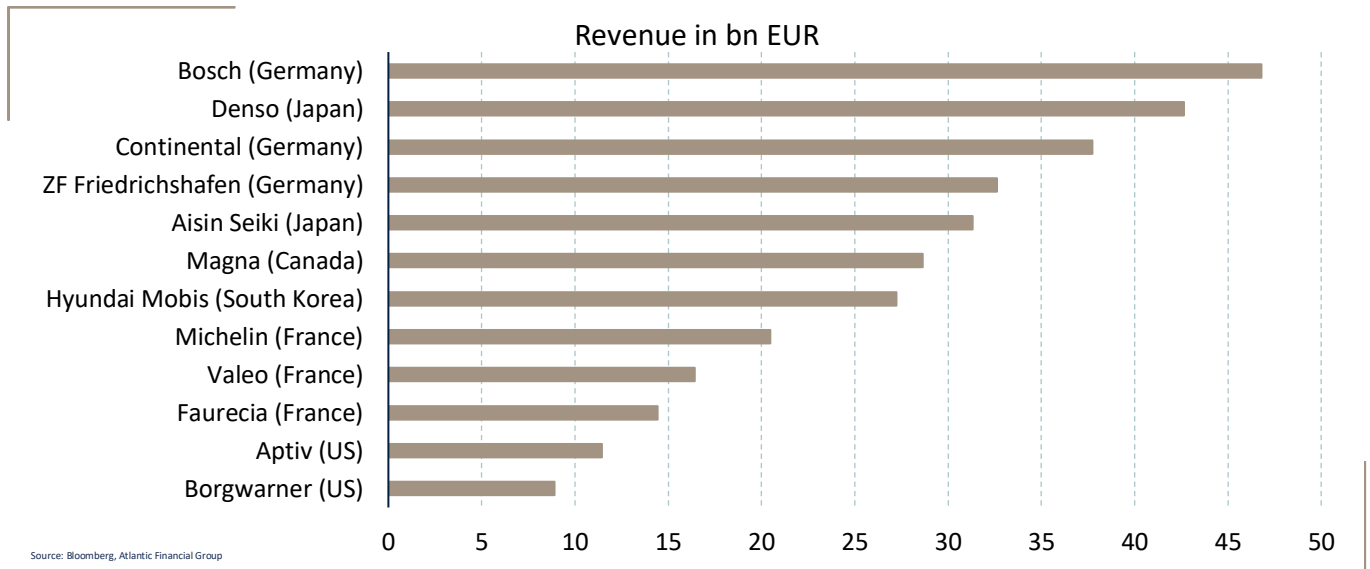
Suppliers are increasingly focusing on electrifying mobility, connectivity and autonomous driving (ADAS). **Companies are repositioning their businesses** by spinning off business units that no longer fit into the long-term portfolio and, buying assets where gaps in future offerings appear.

One example is Continental's joint venture with Osram, which is to stand for innovative lighting and laser technology for autonomous vehicles. The aim is to develop intelligent lighting and sensor systems for the mobility of the future. This technology is intended to ensure communication between autonomous cars (C2C) and with other road users (C2X).



On their side, **Valeo and Siemens have been working together since 2016 through their JV "Valeo Siemens eAutomotive GmbH**. This is dedicated to high voltage propulsion systems. Their intention is to become world leaders in the electric mobility market.

Fig. 4 -



With sales of approximately 46.8 billion euros in its fiscal year 2020, **Bosch Mobility Solutions is the largest automotive supplier in the world** (see Fig 4). For a long time, the Bosch Group has competed with a small number of automotive suppliers. However, **the market is changing due to the expansion of electrification, automation, connectivity, electronic architectures, and the increasing amount of software in vehicles. These changes are attracting new suppliers from industries as diverse as consumer electronics, semiconductors, and mobility platforms.**

The trend towards consolidation among traditional manufacturers and suppliers is likely to continue. This can be seen in the recent takeover announcement of the German automotive supplier Hella, known for its headlights and lighting systems, by the French supplier Faurecia.

◆ **Recent results have been encouraging in Europe, but more mixed in the US.**

A number of European equipment manufacturers announced good results and above all raised their expectations for 2021, creating a surprise. For example, cost reductions have enabled Plastic Omnium, a manufacturer of bumpers and tanks, to raise its earnings estimates for this year.

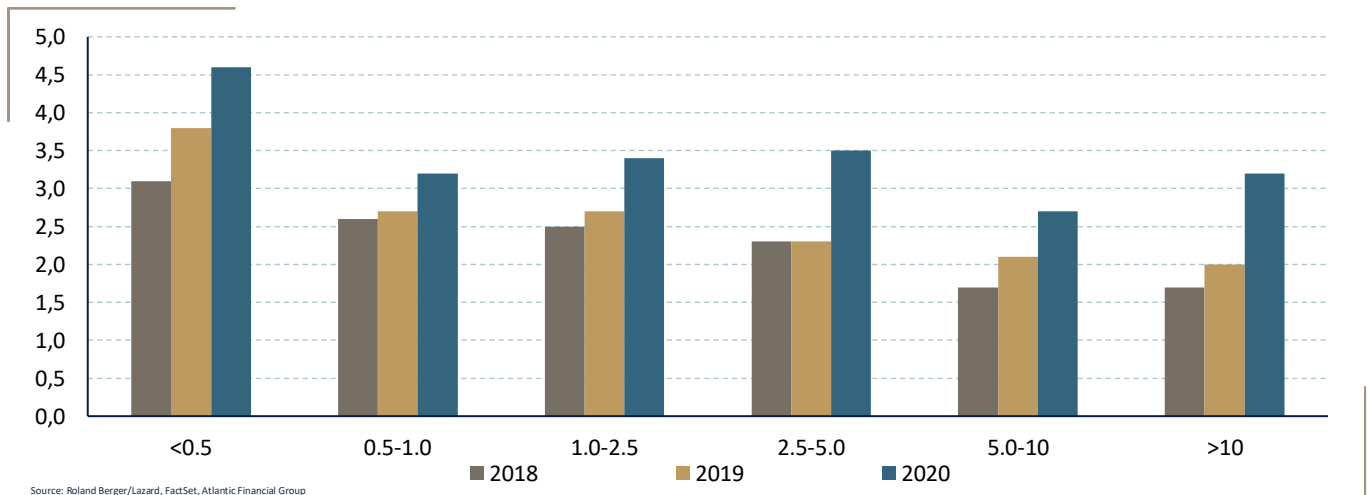
However, **expectations must remain on the side of caution given the shortage of semiconductors and high logistics costs that are weighing on companies' profitability. CAPEX and R&D expenses have been sharply reduced** compared to 2019 in order to avoid deteriorating finances during the crisis. **Yet these expenses are crucial to maintain market share and technological advantage against new entrants.**



On the other side of the Atlantic, suppliers, like Adient, **disappointed** and lowered their expectations for 2021, citing rising raw material prices (steel and chemicals) and the disruption in the production chain caused by the shortage of semiconductors, pushing some to stop production altogether.

Lastly, **we need to keep an eye on debt, which has surged** following the crisis to high levels of 4.6x net debt to EBITDA for small caps and 3.2x for larger caps. (see Fig. 5). The increase in debt ratios is **due to the decline in business volumes since 2018 and investments needed to transform the sector**. Moreover in 2020, the ratio deteriorated rapidly with the collapse of companies' gross operating surplus.

Fig. 5 - Net debt to EBITDA ratio of suppliers by size (bn euros of sales)



The tyre industry, on the other hand, posted much stronger results, supported by good sales volumes of used vehicles and a very advantageous price/mix ratio. On the other hand, the industry is facing increasing difficulties in sourcing natural rubber from Asia and other regions due to the shortage of containers. Goodyear is optimistic about the outlook for U.S. tyre demand in the second half of the year. **Vehicle miles should normalize as economic activity picks up. Government subsidies to consumers and high used car prices should also support industry growth.** Finally, with new vehicle production delayed due to the semiconductor shortage, Goodyear expects the improved product mix (higher weighting of replacement tires) to contribute positively again in the second half.

Conclusion:

As in previous crises, automotive suppliers have to be more flexible than their customers and be creative in finding the necessary resources until new vehicle sales growth returns. The second quarter of this year marked a pause after three quarters of improvement since the first lock down. **The year 2022 is expected to be a better one** and the sector could then benefit from renewed interest by the end of the year.





RETURN ON FINANCIAL ASSETS

Markets Performances (local currencies)	Last Price	Momentum Indicator (RSI)	1-Week (%)	1-Month (%)	2021 Year-to-Date (%)	2020 (%)	2019 (%)
Equities							
World (MSCI)	737.3	51.35	-1.2%	0.9%	15.7%	16.9%	27.3%
USA (S&P 500)	4459	47.54	-1.7%	0.6%	19.9%	18.4%	31.5%
USA (Dow Jones)	34 608	36.99	-2.1%	-1.6%	14.6%	9.7%	25.3%
USA (Nasdaq)	15 115	54.86	-1.6%	2.3%	17.8%	45.1%	36.7%
Euro Area (DJ EuroStoxx)	467.1	47.71	-0.8%	-0.5%	19.9%	0.8%	27.3%
UK (FTSE 100)	7 029	40.80	-1.5%	-1.0%	12.0%	-11.4%	17.2%
Switzerland (SMI)	12 061	34.48	-2.4%	-2.4%	15.8%	4.3%	30.2%
Japan (Nikkei)	30 447	76.50	4.3%	9.0%	11.7%	18.3%	20.7%
Emerging (MSCI)	1 309	54.56	-0.5%	0.9%	3.0%	18.8%	18.8%
Brasil (IBOVESPA)	114 286	37.18	-2.3%	-6.5%	-4.0%	2.9%	31.6%
Russia (MOEX)	4 003	63.02	0.2%	3.9%	26.9%	14.8%	38.4%
India (SENSEX)	58 105	82.54	0.8%	2.2%	23.1%	17.2%	15.7%
China (CSI)	4 984	58.30	5.5%	0.4%	-2.2%	29.9%	39.2%
Communication Serv. (MSCI World)	118.50	54.70	-0.9%	1.5%	18.6%	24.2%	25.1%
Consumer Discret. (MSCI World)	403.9	55.05	0.2%	0.0%	7.2%	37.0%	28.2%
Consumer Staples (MSCI World)	280.9	49.31	-0.9%	0.7%	6.8%	8.8%	22.4%
Energy (MSCI World)	171.2	49.16	-1.1%	-0.3%	22.6%	-27.7%	13.9%
Financials (MSCI World)	148.1	50.05	-0.8%	-0.3%	22.2%	-3.1%	24.1%
Health Care (MSCI World)	360.5	42.26	-2.6%	0.3%	14.7%	15.4%	23.3%
Industrials (MSCI World)	330.1	50.81	-1.2%	0.8%	15.4%	11.8%	27.2%
Info. Tech. (MSCI World)	538.8	55.07	-1.4%	2.5%	19.4%	46.2%	47.5%
Materials (MSCI World)	366.9	46.06	-1.1%	-0.9%	15.0%	21.6%	20.8%
Real Estate (MSCI World)	226.7	44.37	-2.8%	1.3%	18.1%	-5.7%	24.0%
Utilities (MSCI World)	157.9	48.12	-1.7%	1.6%	6.9%	4.8%	22.3%
Bonds (FTSE)							
USA (7-10 Yr)	1.34%	48.70	-0.1%	0.4%	-1.7%	9.3%	7.4%
Euro Area (7-10 Yr)	-0.05%	41.93	-0.1%	0.9%	-1.1%	4.5%	6.7%
Germany (7-10 Yr)	-0.33%	36.01	-0.2%	-1.1%	-1.9%	3.0%	3.0%
UK (7-10 Yr)	0.76%	41.75	-0.3%	-0.4%	-3.2%	5.4%	4.8%
Switzerland (7-10 Yr)	-0.27%	34.91	-0.4%	-1.0%	-1.0%	0.4%	2.0%
Japan (5-10 Yr)	0.05%	33.94	-0.1%	-0.2%	0.1%	-0.1%	0.0%
Emerging (5-10 Yr)	4.30%	65.78	-0.1%	1.0%	0.1%	5.2%	13.3%
USA (IG Corp.)	2.01%	52.68	0.1%	0.2%	-0.2%	9.9%	14.5%
Euro Area (IG Corp.)	0.27%	36.26	-0.1%	0.5%	0.2%	2.8%	6.2%
Emerging (IG Corp.)	4.25%	53.08	0.2%	0.1%	0.6%	8.1%	13.1%
USA (HY Corp.)	3.79%	80.78	0.1%	1.2%	4.9%	7.1%	14.3%
Euro Area (HY Corp.)	2.87%	84.39	0.1%	0.2%	4.0%	2.3%	11.3%
Emerging (HY Corp.)	6.43%	68.36	0.1%	0.9%	1.5%	4.3%	11.5%
World (Convertibles)	453.7	54.17	-1.1%	1.1%	6.0%	38.8%	17.3%
USA (Convertibles)	615.1	54.64	-1.4%	1.3%	6.9%	54.5%	22.8%
Euro Area (Convertibles)	4 180	46.89	0.0%	0.5%	1.6%	6.1%	7.6%
Switzerland (Convertibles)	187.3	36.29	-0.2%	-0.2%	0.3%	0.5%	2.4%
Japan (Convertibles)	202.4	74.90	1.4%	2.3%	4.1%	2.8%	2.6%
Hedge Funds (Crédit Suisse)							
Hedge Funds Indus.	713.5	44.43	n.a.	0.3%	6.3%	2.5%	9.3%
Distressed	#N/A N/A	73.83	n.a.	-0.9%	9.5%	1.5%	1.4%
Event Driven	#N/A N/A	71.67	n.a.	-0.5%	9.6%	3.1%	8.2%
Fixed Income	#N/A N/A	78.28	n.a.	0.6%	4.4%	2.2%	6.1%
Global Macro	#N/A N/A	70.55	n.a.	0.1%	6.3%	2.0%	10.4%
Long/Short	#N/A N/A	72.36	n.a.	1.4%	6.8%	3.6%	12.2%
CTA's	#N/A N/A	64.11	n.a.	0.9%	7.2%	-3.2%	9.0%
Market Neutral	#N/A N/A	62.94	n.a.	0.5%	4.6%	-0.1%	1.6%
Multi-Strategy	#N/A N/A	76.28	n.a.	1.1%	5.5%	1.4%	7.3%
Volatility							
VIX	20.95	62.41	27.7%	24.8%	-7.9%	65.1%	-45.8%
VSTOXX	20.36	56.04	11.9%	17.8%	-12.9%	67.5%	-41.5%
Commodities							
Commodities (CRB)	556.2	n.a.	-0.3%	-0.4%	25.3%	10.5%	-1.9%
Gold (Troy Ounce)	1 791	46.85	-1.8%	0.6%	-5.7%	24.9%	18.3%
Oil (WTI, Barrel)	69.72	53.61	0.6%	1.1%	43.7%	-20.5%	34.5%
Oil (Brent, Barrel)	73.22	57.05	0.7%	1.8%	42.3%	-23.0%	24.9%
Currencies (vs USD)							
USD (Dollar Index)	92.783	53.69	0.8%	0.3%	3.2%	-6.7%	0.2%
EUR	1.1787	46.43	-0.7%	-0.1%	-3.5%	9.7%	-2.2%
JPY	110.10	47.36	-0.2%	-0.5%	-6.2%	5.3%	0.9%
GBP	1.3822	52.02	-0.1%	-0.3%	1.1%	2.8%	3.9%
AUD	0.7350	50.08	-1.2%	-0.3%	-4.5%	9.5%	-0.4%
CAD	1.2668	44.86	-1.1%	-1.2%	0.5%	1.8%	5.0%
CHF	0.9197	45.04	-0.5%	-0.4%	-3.8%	9.8%	1.4%
CNY	6.4542	56.67	0.1%	0.4%	1.1%	6.7%	-1.2%
MXN	19.888	58.87	0.1%	0.0%	0.1%	-4.9%	3.8%
EM (Emerging Index)	1 738.8	59.41	-0.2%	0.8%	1.1%	3.3%	3.1%

Source: Bloomberg, Atlantic Financial Group

Total Return by asset class (Negative \ Positive Performance)



DISCLAIMER

This document is issued by Atlantic Financial Group (hereinafter "Atlantic"). It is not intended for distribution, publication, or use in any jurisdiction where such distribution, publication, or use would be unlawful, nor is it aimed at any person or entity to whom it would be unlawful to address such a document.

This document is provided for information purposes only. It does not constitute an offer or a recommendation to subscribe to, purchase, sell or hold any security or financial instrument. It contains the opinions of Atlantic, as at the date of issue. These opinions and the information herein contained do not take into account an individual's specific circumstances, objectives, or needs. No representation is made that any investment or strategy is suitable or appropriate to individual circumstances or that any investment or strategy constitutes a personal recommendation to any investor. Each investor must make his/her own independent decisions regarding any securities or financial instruments mentioned herein. Tax treatment depends on the individual circumstances of each client and may be subject to change in the future. Atlantic does not provide tax advice. Therefore, you must verify the above and all other information provided in the document or otherwise review it with your external tax advisors.

Investment are subject to a variety of risks. Before entering into any transaction, an investor should consult his/her investment advisor and, where necessary, obtain independent professional advice in respect of risks, as well as any legal, regulatory, credit, tax, and accounting consequences. The information and analysis contained herein are based on sources considered to be reliable. However, Atlantic does not guarantee the timeliness, accuracy, or completeness of the information contained in this document, nor does it accept any liability for any loss or damage resulting from its use. All information and opinions as well as the prices, market valuations and calculations indicated herein may change without notice. Past performance is no guarantee of current or future returns, and the investor may receive back less than he invested. The investments mentioned in this document may carry risks that are difficult to quantify and integrate into an investment assessment. In general, products such as equities, bonds, securities lending, forex, or money market instruments bear risks, which are higher in the case of derivative, structured, and private equity products; these are aimed solely at investors who are able to understand their nature and characteristics and to and bear their associated risks. On request, Atlantic will be pleased to provide investors with more detailed information concerning risks associated with given instruments.

The value of any investment in a currency other than the base currency of a portfolio is subject to the foreign exchange rates. These rates may fluctuate and adversely affect the value of the investment when it is realized and converted back into the investor's base currency. The liquidity of an investment is subject to supply and demand. Some products may not have a well-established secondary market or in extreme market conditions may be difficult to value, resulting in price volatility and making it difficult to obtain a price to dispose of the asset. If opinions from financial analysts are contained herein, such analysts attest that all of the opinions expressed accurately reflect their personal views about any given instruments. In order to ensure their independence, financial analysts are expressly prohibited from owning any securities that belong to the research universe they cover. Atlantic may hold positions in securities as referred to in this document for and on behalf of its clients and/or such securities may be included in the portfolios of investment funds as managed by Atlantic.