



Building Resilience

A perspective for automotive suppliers in the current economic climate

Table of contents

- 3 Growth opportunities for automotive suppliers
- 4 Batteries: leveraging the supply gap
- 5 Semiconductors: investing in growth
- 6 Impact of the current economic climate on automotive suppliers
- 8 Building resilience in a new economic and regulatory framework
- 9 Build balance sheet flexibility
- 10 Manage renegotiation of payment terms

Growth opportunities for automotive suppliers

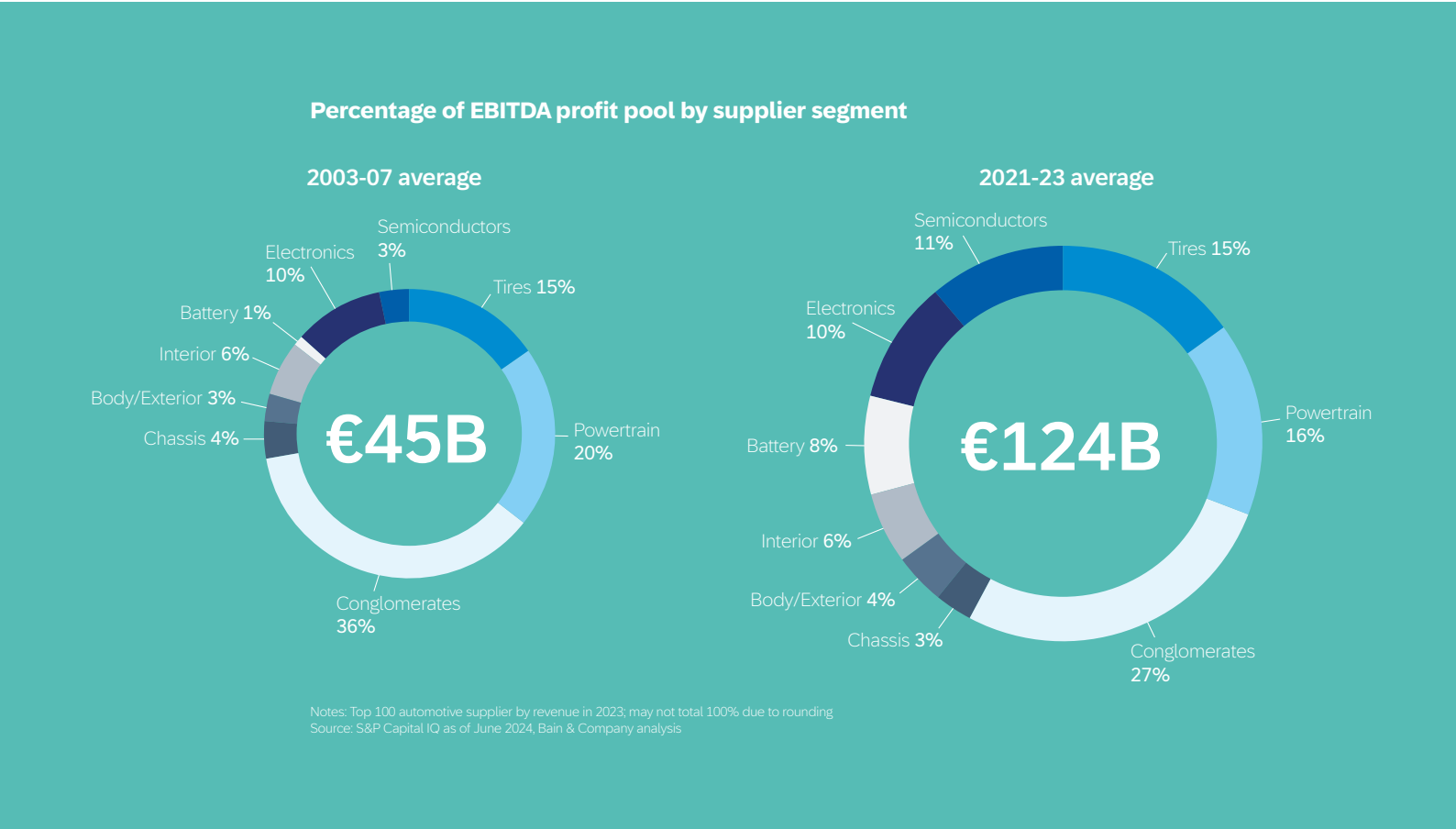
Top automotive suppliers have seen their profit pools expand significantly in recent years. However, in the current economic climate, suppliers face various challenges, including rising production and financing costs. As they navigate this landscape, it's more important than ever for suppliers to optimize cash flows, release trapped cash, and manage payment term renegotiations effectively.

Despite many obstacles, the automotive supplier sector has remained resilient over the past two decades, enjoying significant growth with average EBITDA margins of 10% to 11%¹. During this time, the annual profit pool of the top 100

automotive suppliers has nearly tripled – even though vehicle production has only grown by approximately 30%².

A key factor driving growth is the surge of software-defined vehicles with more content per vehicle. As a result, the semiconductors and batteries subsector profit pools have grown significantly over the past twenty years.

As the chart below illustrates, semiconductors and batteries represented a mere 4% of the €45B profit pool from 2003 to 2007. But by 2021-2023, these two subsectors commanded nearly 20% of the €124B profit pool.



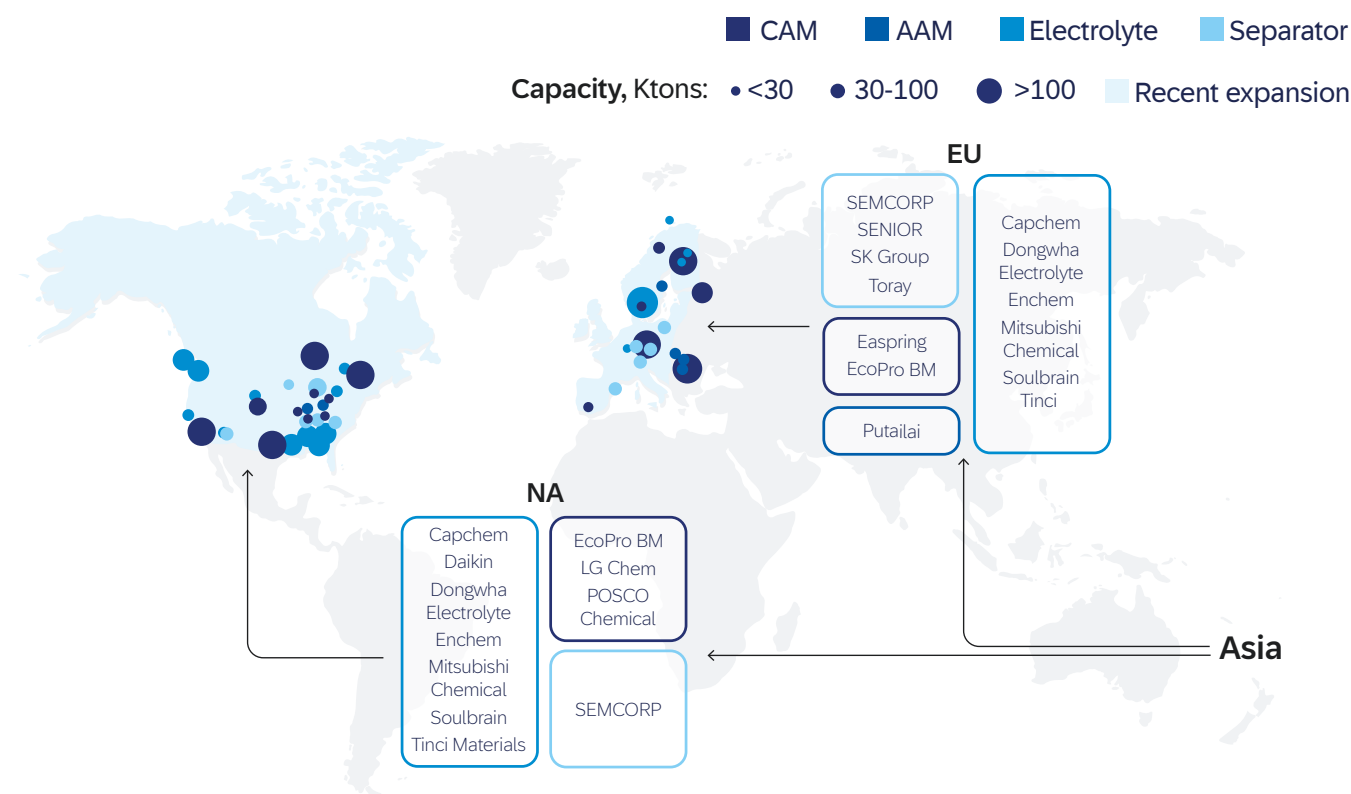
Footnote(s)
1. Bain & Company. "Navigating Ups-and-Downs in the Automotive Supplier Industry." Navigating Ups-and-Downs in the Automotive Supplier Industry, September 2024, <https://www.bain.com/insights/navigating-ups-and-downs-in-the-automotive-supplier-industry-snap-chart/>
2. Bain & Company. "Under the Hood: What's Powering Automotive Suppliers' Profit Pool Growth?" Under the Hood: What's Powering Automotive Suppliers' Profit Pool Growth?, 24 November 2024, <https://www.bain.com/insights/under-the-hood-whats-powering-automotive-suppliers-profit-pool-growth-snap-chart/>

Batteries: leveraging the supply gap

Within the batteries subsector, component and cell supply production is dominated by China, which has a 60%-80% market share³. China also has the capacity to export to North America and Europe, where a supply gap exists⁴. To take advantage of this supply gap opportunity, China, Korea, and Japan have announced the expansion of cell component facilities through local partnerships in North America and Europe, as shown on the map below.

Local partnerships and production also sit well with governments encouraging a regional approach amidst the changing geopolitical climate. In parallel, automotive Original Equipment Manufacturers (OEMs) are also expanding into the component industry, while new players are looking to differentiate their business through higher quality raw materials or superior technologies to gain a foothold in the market.

Recent expansion announcements for 2030 of incumbent cell component producers in North America and Europe¹



1 Non-exhaustive, based on company announcements between 2021 - 2023
Source: Company announcements

Footnote(s)
3. McKinsey & Company. "McKinsey Automotive & Mobility Spotlight: Battery cell component market perspectives." McKinsey Automotive & Mobility Spotlight: Battery cell component market perspectives, 12 July 2024, <https://www.mckinsey.com/industries/automotive-and-assembly/our-insights>
4. McKinsey & Company. "McKinsey Automotive & Mobility Spotlight: Battery cell component market perspectives." McKinsey Automotive & Mobility Spotlight: Battery cell component market perspectives, 12 July 2024, <https://www.mckinsey.com/industries/automotive-and-assembly/our-insights>

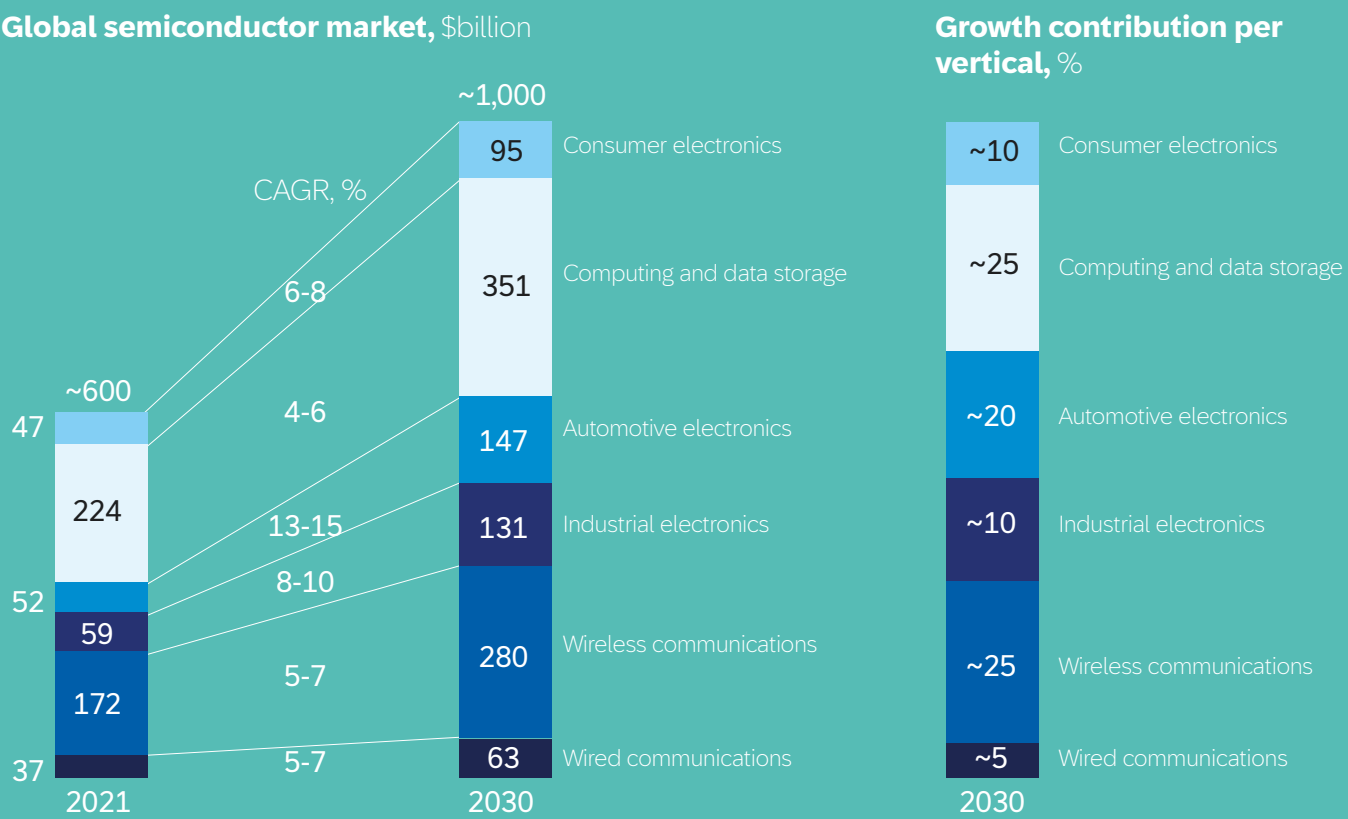
Semiconductors: investing in growth

Within the semiconductors subsector, companies plan to invest about \$1 trillion between now and 2030 in new fabrication plants located in Asia and the United States⁵. The investment will support

growth in semiconductor demand, with the overall market size expected to reach \$1 trillion by 2030. Automotive electronics is expected to take up a healthy 20% of that market share.

“Automotive electronics is expected to grow at **CAGR 13-15%** till 2030, contributing **20% of a \$1 trillion** semiconductor market.”

The semiconductor market is expected to reach \$1 trillion in value by 2030



Source: McKinsey & Company analysis

Footnote(s)
5. McKinsey & Company. "Exploring new regions: The greenfield opportunity in semiconductors." Exploring new regions: The greenfield opportunity in semiconductors, 29 January 2024, <https://www.mckinsey.com/industries/semiconductors/our-insights/exploring-new-regions-the-greenfield-opportunity-in-semiconductors>

Impact of the current economic climate on automotive suppliers

The current economic climate has significant implications for automotive suppliers—not least because emerging trends such as the rise of nearshoring and heightened volatility are likely to drive up costs.

Higher overall cost structures

Changes to economic conditions are likely to make nearshoring and reshoring more prevalent. Moving production to the US and Europe will invariably increase the cost of production, especially if the industry continues to focus on increasing automation.

The US and Europe are significantly more expensive in every aspect, which will translate

into higher up-front capital and operating costs. The cost of input materials is also set to increase due to countries displaying resource dominance amid a changing regulatory environment.

Mapping supplier exposure based on the value chain

Global supply chains are interconnected networks of suppliers that add value to each step of the manufacturing process before components are installed in an automotive. Any cost increases associated with a changing framework will depend on factors including component trees, types of value-added activity, and location.

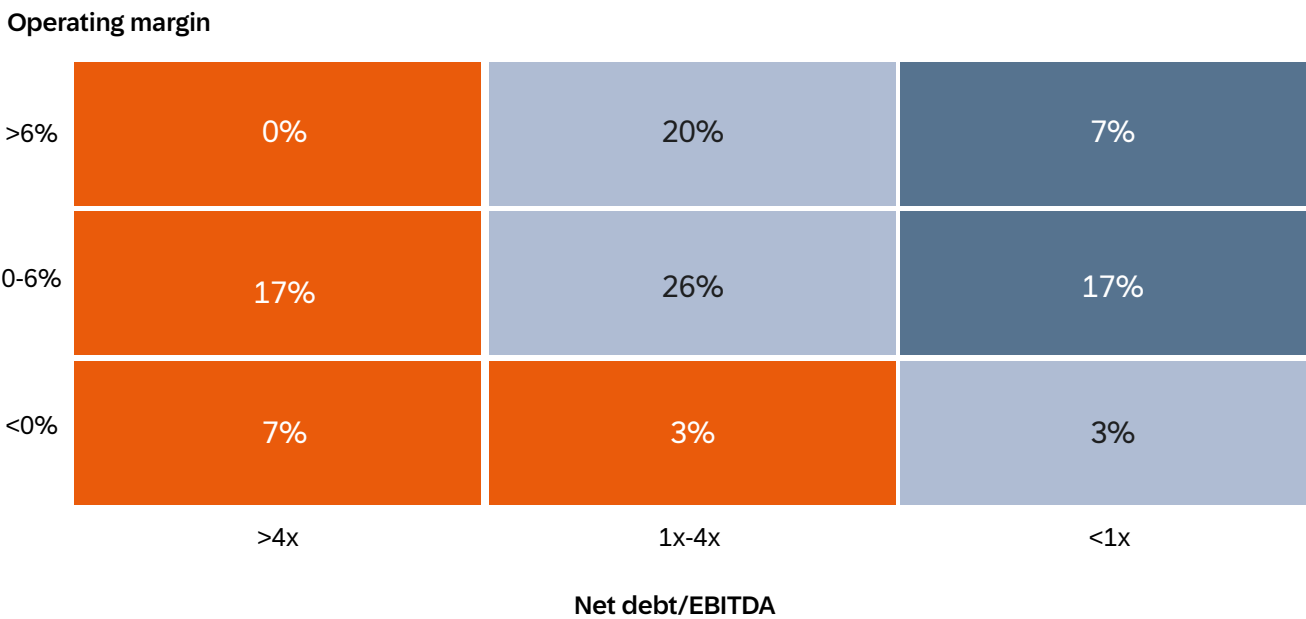
After mapping costs, suppliers must understand whether these costs should be absorbed by the supplier or passed on to the customer. The chosen approach will vary depending on the customer segment and its ability to absorb an increase.

Changes to availability and allocation of funds

Increased volatility and tightening credit will lead to an increase in borrowing costs. While all suppliers will be affected, mid-sized suppliers that are highly leveraged are likely to see the most significant impact.

An analysis by Bain & Company modeled a scenario where costs increased by 7% (of which 4% could be passed on to the customer), financing costs increased by 20%, and production volumes were unchanged. As summarized by the grid, the analysis found that regardless of operating margins, suppliers whose net debt/EBITDA is over 4x will discover that adding further leverage is unsustainable. Similarly, suppliers with a negative operating margin and a net debt/EBITDA between 1x - 4x will also be impacted.

About a quarter of leading global auto suppliers are unprepared for a “moderate storm”



Moderate storm readiness level: Financially not prepared Financially moderately well prepared Financially well prepared

Note: Financial simulation is based on 30 of the top 100 global automotive suppliers
Source: S&P Capital IQ, Bain & Company analysis



Building resilience in a new economic and regulatory framework

Focus on cash flow

Data from the last two decades shows that during the 2008 financial crisis and the Covid-19 pandemic, suppliers displayed increased discipline with cash flow management, as vehicle unit production fell. In both cases, cash flow from operating activities (CFOA) exceeded EBITDA. There are several reasons why cash flow may increase during times of crisis, including delayed investments, greater cost management, government subsidies, and support from OEMs.

“There are different ways to build discipline around cost management and cashflow optimization,” comments Andy Lee, Global Head of Receivables Management at SAP Taulia. “True sale receivables finance can be a highly effective tool with quick time to value. The right receivables finance structure contributes towards cash flow, without adding debt, while keeping a business’ productivity intact.”

“Over the next few years, with increased CapEx, COGS, and financing fees, suppliers need to

prioritize working capital, and receivables management is a critical part of that equation.” A recent case in point is an automotive powertrains manufacturer managed by a leading European PE firm. When the supplier’s top-tier OEM customers started applying pricing pressure, the CFO focused on cost management and cashflow optimization.

True sale receivables finance is less thought about but can be a **highly effective** tool with quick time to value.

The company worked with SAP Taulia to implement a €44 million true sale receivables finance facility to keep business operations running smoothly. The receivables program released cash trapped in the company’s progressive/milestone billing contracts.

Build balance sheet flexibility

A balance sheet review can be a valuable tool in helping companies manage upcoming debt amortization and review their use of facilities. In particular, suppliers with high leverage can consider repaying existing debt and diversifying their financing base.

Another PE-managed automotive powertrain manufacturer in the United States utilized alternative financing. The manufacturer needed incremental financing and a diversified funding base. By unlocking capital from project-based receivables, the supplier freed up \$44 million within five weeks.

True sale receivables adapt to your strategy, without adding debt to your balance sheet.

“The CFO had a clear goal to pay down existing debt, and he achieved that by using a simple true sale of receivable program,” explains Ade Omisore, SAP Taulia’s Head of Structuring North America & APAC. “As a result, he strengthened the company’s position for future borrowing. As a financial instrument, true sale of receivables has multiple benefits – it does not add debt to the balance sheet, offers up to 100% advance rate, could be used for select customers or a portfolio of customers, and is evergreen.”

\$44m

released from project based receivables within 5 weeks



100%
advance rate



Manage renegotiation of payment terms

As new supply chain frameworks unfold, customers will look to renegotiate or delay payment terms. While renegotiating terms, suppliers can strengthen customer relationships by offering extended terms in exchange for a higher revenue share.

“To see the concept of cash flow acceleration in practice, we can learn from a different industry,” Omisore explains, citing the example of a large, privately-held global IT services company that secured a new contract with its most important customer via SAP Taulia’s solutions. “We partnered with the IT services company to set up a receivables program to accelerate payments under a £250 million facility, funded by a network of financiers outside the company’s traditional financing ecosystem.”

As these examples demonstrate, multiple ways exist to continue navigating an uncertain supply chain environment. Automotive suppliers should build resiliency by strengthening cash flow, building balance sheet flexibility, and managing payment term renegotiations.

Get in touch

Reach out for an obligation-free analysis of outstanding receivables to understand the impact on your business’s liquidity and balance sheet metrics.

Connect with us at
paymeeearly@taulia.com

£250

million in additional
capacity sourced
by a network of
financiers