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working world

Mobility Quarterly

Analyst themes from 3Q19 earnings calls

Innovation cycles are shortening, and new digital technologies are pushing old ones into obsolescence, creating new business models that are transforming the entire ecosystem. The customer experience is the core driver of this accelerating pace of change. Mobility companies need to balance the increasing business complexity while improving the value they generate. Companies are intensifying their focus on the digital and electrified value chain, spinning off non-core assets, increasing agility with lean operations, and ensuring that stakeholder needs are addressed to enhance the customer experience and deliver improved value over the long term.

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Back to basics – sustainable business opportunities aiding long-term value growth are driving the agendas of mobility peers

Welcome to the *Mobility Quarterly*, a review of the top 10 themes discussed by leaders of 23 mobility sector companies during public earnings calls with analysts. Covered sectors include passenger vehicle (PV), commercial vehicle (CV), automotive suppliers, logistics and airlines. This update tracks the movement of themes from quarter to quarter to provide a perspective on shifts in the sector landscape.

Themes that stood out in 3Q19 include:

- ▶ **Geographic developments**, again at No. 1 on the list. Companies across the mobility peer group are responding to changing demand in Asia, Europe and North America. In the US, favorable consumer economic conditions are driving growth with strong retail and e-commerce sales. Growth is slowing in several segments in Asia because of local economic conditions and changes in trade policy. Performance in Europe remains weak, as a decline in Germany's industrial sector is dragging growth.
- ▶ **Operating costs**, unchanged at No. 2. Macroeconomic uncertainties are adding challenges to operations. Foreign exchange volatility emerged as the top operating cost issue. The higher costs associated with new technologies are expected to continue in the next quarter. Although new technology is increasing costs in the short run, it is expected to support top-line growth in the long term.
- ▶ **Restructuring initiatives**, retained at No. 3. Restructuring is becoming a "normal" aspect of business culture; corporate structures are being simplified with fewer business units and leaner leadership teams to reduce costs. Cost reduction programs are being run at all levels of the value chain. Companies are seeking to hire specialists while overall headcount is being reduced.

Randy Miller
EY Global Advanced Manufacturing & Mobility Leader

Top 10 themes from quarterly earnings calls

3Q19			2Q19	
↔	1.	Geographic developments	1.	Geographic developments
↔	2.	Operating costs	2.	Operating costs
↔	3.	Restructuring initiatives	3.	Restructuring initiatives
↔	4.	Evolution of mobility	4.	Evolution of mobility
↑	5.	Organic growth (products, services strategy and innovation)	5.	Product evolution
↑	6.	Working capital and cash flow management	6.	Inorganic growth (M&A, joint ventures and partnerships)
↓	7.	Product evolution	7.	Working capital and cash flow management
↓	8.	Inorganic growth (M&A, joint ventures and partnerships)	8.	Manufacturing and supply chain management
↓	9.	Manufacturing and supply chain management	9.	Regulatory issues
New	10.	Financing, pricing and affordability	10.	Organic growth (product, strategy, innovation)

Key themes

↔ 1 Geographic developments Market conditions by region

- ▶ In the US, favorable consumer economic conditions are driving growth with strong retail and e-commerce sales. The construction industry is anticipating higher demand on the back of state, local infrastructure and nonresidential construction activity.
- ▶ Latin America started seeing healthier trends driven by growth in vehicles sales despite a volatile political and economic environment.
- ▶ Most mobility peers are witnessing a sales growth decline in Asia, particularly in China. Chinese industrial production growth reached a 10-year low in July, and exports to the US have declined every month in 2019.
- ▶ Performance in Europe remains weak, and automotive companies are forecasting 2020 production to decline year over year. However, product categories related to safety, new technologies and electrification are witnessing an uptick.

↔ 2 Operating costs Gains or losses related to operating costs including raw materials, currency, technology and talent

- ▶ Several mobility peers are witnessing headwinds from major currencies such as the euro, British pound and Japanese yen, as well as emerging-market currencies, as they continue to weaken against the US dollar.
- ▶ Depreciation of the Chinese yuan is offsetting improvements in profits and sales growth in the Chinese operations of global companies.
- ▶ Launch costs and R&D spending remain elevated for most companies, while some peers reported moderations in costs on the back of cost refinement programs at all levels.
- ▶ Airlines are boosting their investments in employees by marking up compensation and increasing benefits. However, high pension costs remain a concern.
- ▶ Automotive companies are restructuring wages with new labor agreements, offering voluntary buyouts to increase manufacturing flexibility.

↔ 3 Restructuring initiatives Operational streamlining, business function reorganization and divestments

- ▶ Several peers are launching business-wide efficiency programs frugally and strategically examining each component of their cost structures, such as materials expenses; selling, general and administrative costs; and back-office and discretionary spending.
- ▶ Select PV peers and suppliers are reducing headcount as they optimize their manufacturing capacity and realign their corporate structures. More reductions are estimated in the next few years.
- ▶ Logistics peers are increasing the pace of integration and cross-utilizing networks to widen their offerings while also exploring tech-based solutions for efficiencies.



4 Evolution of mobility

Growth of connected, autonomous, shared and electric (CASE) vehicles

- ▶ Many automakers are announcing the launch of new fully electric vehicles and expanding battery capacity to comply with the upcoming emission standards by the EU, Japan and China, among others.
- ▶ CV peers continue to focus on autonomy, semiautonomy and remote operations, encouraged by higher-than-expected wins stemming from efficiency improvements and declines in safety incidents.
- ▶ PV peers are continuing with the joint development of autonomous vehicles (AV) with other automakers and technology companies, also growing their fleet sizes in select cities for increasing AV testing and validation.
- ▶ Major logistics companies are leveraging alternate delivery vehicles (ADV) built on autonomous, electric or a combination of both technologies. Some of these first- and last-mile solutions are being applied successfully in the real world.



To really reap the full rewards of smart freight, the cargo itself — not just the vehicles — will need to be autonomous. Digital ID technology and smart contracts powered by blockchain solutions such as EY OpsChain Tesseract solution may help enable containers that can generate their own bills of lading, for example, significantly reducing the costs and friction of traditional processes in warehouses and across national borders.

John Simlett, EY Global Future of Mobility Leader



5 Organic growth (product, service strategy and innovation)

Expansions or reductions of activity in key product lines and capacity adjustments

- ▶ Mobility companies are aiming for long-term growth by strengthening their existing product or service portfolios while developing allied digital platforms to tap into new sources of revenue.
- ▶ Logistics peers are expanding their current portfolios with e-commerce deliveries, catering to a broader consumer and geographic base.
- ▶ Airline peers are diversifying their businesses to achieve a greater revenue share from premium products, loyalty programs and other non-ticket revenue sources.



6 Working capital and cash flow management

Changes observed from the prior quarter

- ▶ Flexible production and agile supply chains are helping companies rightsize inventories at the micro level.
- ▶ Shorter lead times are allowing dealers to maintain less inventory and freeing up working capital.
- ▶ Few of the automotive peers reported leaner-than-warranted inventory due to reasons such as strikes at their manufacturing plants and the introduction of the worldwide harmonized light vehicle test procedure (WLTP) in Europe.
- ▶ Companies are witnessing improved cash flows after making discipline in working capital a top priority, supported by agile production and cost-control programs.



7 Product evolution

Shift in demand of vehicle types, increasing advent of R&D and product innovation

- ▶ The customer experience is driving innovations and improvements of existing products and services across subsectors.
- ▶ Logistics peers are stretching their capabilities to make their offerings speedier and more convenient for customers; services such as all-week delivery, later pickup for next-day ground delivery and enhanced network capabilities are targeted for large e-commerce companies.
- ▶ Synchronization of automation with the delivery, warehousing, tracking and sorting processes has led to efficiencies (both operational and financial), thus increasing interest from stakeholders to amplify their investments and speed to market of such technologies.



For automakers and dealers, the key is to focus on building a differentiated customer experience that delights and exceeds expectations. To build a differentiated brand experience requires a broad transformation of the customer purchase journey, rethinking digital and physical retail standards and finding new ways to interact with customers to provide an omni-channel, leading-in-class experience.

Hanno Lorenzl, EY Americas Automotive Retail and Distribution Leader



8 Inorganic growth (M&A, joint ventures and partnerships)

Efforts to increase market share, innovate products and services, and advance technical capabilities

- ▶ PV peers are targeting collaborations and partnerships to develop their electric and autonomous capabilities, optimize capital, pool their expertise and reduce their time to market.
- ▶ Suppliers are acquiring select businesses of peers and partnering with technology firms for advanced products; one supplier decided to fully spin off its power train business.
- ▶ Logistics companies are forming new strategic partnerships with retailers for exclusive and preferred shipping to customers as they fulfill same-day delivery commitments by e-commerce companies.
- ▶ National airline peers are partnering with regional airlines to expand their geographic footprint while ensuring a seamless travel experience and in-flight services.



9 Manufacturing and supply chain management

Modernizing and restructuring manufacturing and supply chain

- ▶ Automotive companies are modernizing manufacturing facilities; a few companies are also downsizing capacity in the existing plants to avoid plant closures.
- ▶ Lean programs and higher automation are reducing lag times while improving safety and quality.
- ▶ Airline and logistics companies are modernizing aircraft fleets and delivery networks in a bid to optimize their cost structures and enhance their competitiveness.



10 Financing, pricing and affordability

Pricing strategy, convergence of digital and in-person buying process, and sales incentives

- ▶ In the wake of continuing global trade tensions, logistics peers are reducing prices to increase affordability and maintain the freight volumes required to attain economies of scale.
- ▶ Many PV companies have prioritized price realization to offset increases in manufacturing costs.
- ▶ A favorable product mix, with an increasing share of high-margin SUVs, is enhancing the profitability of related OEMs.
- ▶ Suppliers in the US are reporting higher revenues and margins led by pricing increases, particularly in the consumer replacement business.

Companies included in the analysis

- ▶ AB Volvo
- ▶ American Airlines
- ▶ Aptiv PLC
- ▶ BMW AG
- ▶ Caterpillar Inc.
- ▶ Continental AG
- ▶ Daimler AG
- ▶ Delta Air Lines, Inc.
- ▶ Deutsche Post
- ▶ FedEx
- ▶ Ford Motor Company
- ▶ General Motors Company
- ▶ Goodyear Tire & Rubber Company
- ▶ Groupe Renault
- ▶ Honda Motor Co., Ltd.
- ▶ Lear Corporation
- ▶ Magna International Inc.
- ▶ Nissan Motor Co., Ltd.
- ▶ Tata Motors
- ▶ Toyota Motor Corporation
- ▶ United Airlines Holdings, Inc.
- ▶ United Parcel Service, Inc.
- ▶ Volkswagen Group

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