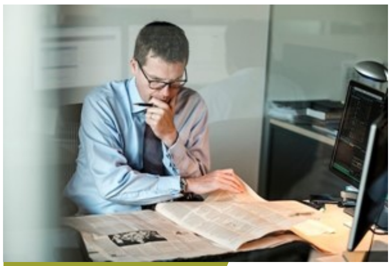


Friday Morning Coffee

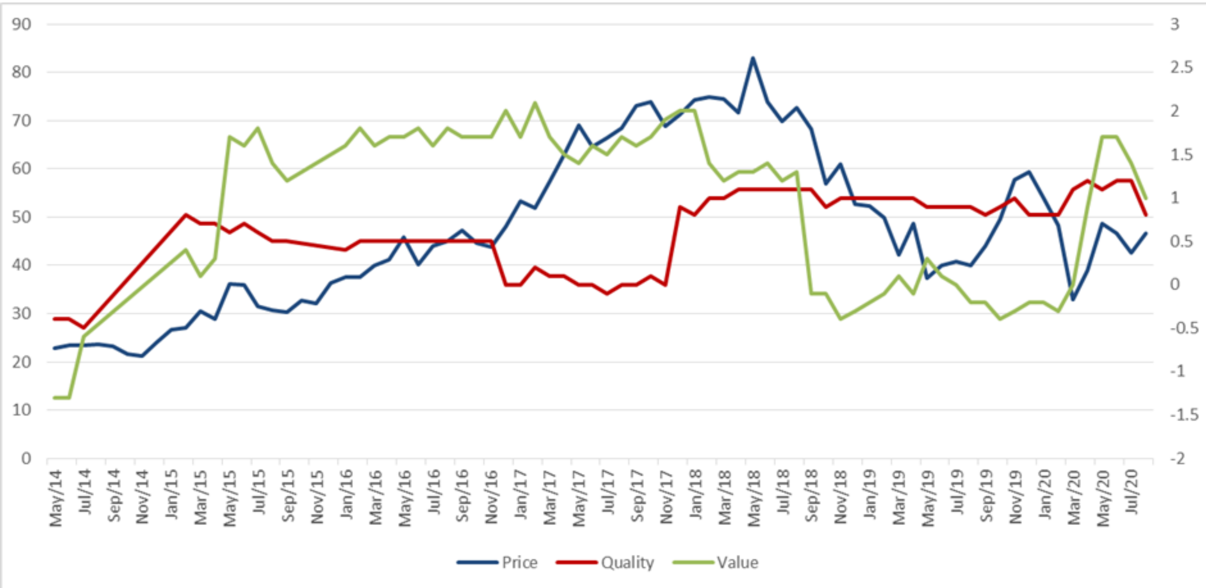
European Capital Partners

Nr. 115 — The rise of Stabilus

Think of an automotive supplier and the first thought that comes to mind is a “component pusher”. Given the relative small size of these players in comparison to global OEMs and the transactional nature of their relationships in this mature industry it is obvious to term them as price takers, which is partially true, especially if one compares the profitability of some of these players to that of OEMs. Wilson Kia Onn Wong in his book titled “Automotive Global Value Chain: The Rise of Mega Suppliers” describes the shift in balance of power from Automotive OEMs to Tier-1 suppliers over the last decade.

During this period, these few players have grown their market share via aggressive consolidation and technological breakthrough in their product offering, thereby turning the value chain into an oligopoly. Despite their envious status within the automotive value chain, many suppliers have little to no brand recognition. With that thesis in mind, we had been closely following Stabilus over past few years waiting for the right moment to invest and the opportunity rose during Covid-19 period.

Stabilus in the Quality / Value Framework



Source: ECP

Stabilus is a producer of gas springs, automatic drive systems (for example door closers) and hydraulic vibration dampers. It derives 60% of the revenue from automotive segment and 40% from general industrial/ commercial end use. In Gas springs, its largest business segment, it has 95% market share in the EU and NAFTA region whereas c. 40% in Asia. What sets Stabilus apart from other auto suppliers is its product offering. To give a bit of colour, the costliest product that Stabilus sells costs EUR 40 that goes into automotive vehicles with price tags in tens of thousands and a typical gas springs costs EUR 2 per unit.

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It seems unlikely, for example, Volkswagen switching to other suppliers to save a few cents on gas springs that goes into Porsche at the risk of losing on quality and availability. Also, its product offering enables Stabilus to have manufacturing units which are agnostic to car models i.e. if an OEM decides to launch a certain model, Stabilus can quickly adapt its production line and maintain utilization.

Lately, Stabilus is expanding its footprint in the industrial/commercial segment via opportunist acquisitions at the same time maintaining its decent ROIC as can be seen in the table below.

	2019	**2018**	**2017**	**2016**	**2015**	**2014**	**2013**	**2012**	**2011**
Total Debt	322	331	333	413	274	270	333	295	284
Total Equity	500	427	336	263	77	76	80	57	51
Net Deferred Tax Liabilities	43	33	48	53	34	36	51	52	54
Taxes Payabale	13	16	16	11	3	5	2	1	2
Pension accrued	60	52	53	59	48	48	39	36	35
Invested Capital	**937**	**859**	**787**	**798**	**436**	**435**	**505**	**441**	**427**
Post-Tax ROIC	**11%**	**12%**	**11%**	**13%**	**10%**	**7%**	**7%**	**6%**	**7%**
ROE	18%	28%	26%	28%	22%	13%	-23%	15%	23%

Source: ECP

The reason behind a stable and an improving ROIC profile are the flexible manufacturing lines, smaller and complimentary bolt-on acquisitions, and significant overlaps in their product offering. To give an analogy of the product overlap, imagine a pharmaceutical company developing a novel molecule for a certain disease and thereafter it adds many other indications to the drug by simply altering doses and the composition of that same molecule. Similarly, in the case of Stabilus, the gas springs which goes into cars can also be used in office chairs with certain modifications, requiring minimal R&D.

All these business characteristics make Stabilus an incredibly good quality business, which is rightly shown in our Quality-Value framework with a quality score of 1. Having said that, in the years 2018 -19 Stabilus was trading beyond what we were comfortable with for paying up until Covid-19 crisis made the company a quality at value play for us.

Have a nice weekend,

Léon Kirch, CFA
Partner & Chief Investment Officer
August 14 th, 2020