

## Unhappy Suppliers, Mixed Results

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My colleague, IRN president Kim Korth, is fond of using the opening line of Tolstoy's novel *Anna Karenina* as an analogy for what we observe in the automotive supplier population: "Happy families are all alike; every unhappy family is unhappy in its own way." As publicly-held suppliers begin to report their financial results for 2008, it is interesting to see how they fared and to review the variations on a theme of a very unhappy year.

Not that it started out that way. BorgWarner had a record first half, taking in \$3,015.5 million, up 14% compared to the first half of 2007. By the end of the year, sales were down 1.21% from a year earlier, and the company had a loss of \$36 million on sales of \$5.6 billion. A disappointing turn of events, but relatively mild compared to its peers. There are a number of reasons for BWA's ability to minimize the negative impact of market conditions, including its engine-technology-based product line, geographic sales profile (50% Europe, 30% Americas), and highly diversified automotive customer base. So although it is unhappy that those advantages didn't bear more fruit this year, its long-term plan of staying the course and pushing the powertrain technology envelope, while reducing its workforce and production capacity, should pay off in 2010, if not this year.

Gentex is another unhappy supplier that many would be delighted to trade places with. The company built a record of 22% compound annual revenue growth over a 20-year period (1987-2007). It is the ultimate niche supplier – focused on interior and exterior mirrors – with a phenomenal capacity to keep richening the mix through the use of mirrors as a platform for innovation and value-added features like automatic headlamp control, telematics, indicators, etc. Gentex' sales for the year were down 4.6% after a first half that was up by 9%. As for many of its colleagues, fourth quarter 2008 was the killer, with Q4 sales off by 28%. Gentex is still a deserving object of envy, because it managed to achieve a positive net income of 10% of sales, or \$62 million, for the year. This was about half the level of prior years, but an accomplishment under the circumstances. The quarterly loss of \$10 million that the company experienced was its first since 1984, so it was quite a shock, as were the layoffs of approximately 360 associates during the fourth quarter. This will be an interesting period for the company, now at \$624 million in sales. Its position and the need to fuel growth may drive it into having to supply more base-level product at lower margins for home and emerging markets. We will have to see whether it has a happier time in 2009 or whether 2008 marked the beginning of the end of the heyday for Gentex.

The only company we have seen so far that eked out an increase in sales for 2008 is TRW, but it ascribed the 2% increase to the positive effect of foreign currency translation during the first nine months of the year and to above trend sales of lower-margin modules; hence its less successful profitability result of a \$779 million loss, on about \$15 billion in sales. For the full year, TRW incurred \$932 million in goodwill, customer relationship, and fixed asset impairments and restructuring charges, so it is taking steps to prepare for a better 2009. TRW is the largest company in this sampling

we are looking at, but it has been working on a product strategy along the lines of these other, more focused suppliers. It is a bit of a stretch to squeeze \$15 billion in sales into a completely coherent product line, but TRW has designated its Chassis Systems division as 'Active Safety', its Occupant Safety Systems as 'Passive Safety,' (a third division contains all the left over components) and is pursuing a vision for its future under the theme "Cognitive Safety Systems: We put the thinking in safety systems." If the past experience of BorgWarner and Gentex is any indication, TRW is likely to be happier if it can successfully execute the intent of this new theme.

At an extreme level of unhappiness is American Axle, whose performance skews the scale on any chart we create. Its sales were down 35% in 2008 to \$2.1 billion, with a loss of \$1.224 billion, or 58% of sales. During the healthier part of the year, American Axle was busy with an 81-day labor strike, emerging with an all-in wages and benefits package averaging \$30-45/hour, as compared to \$73.48, and a plan to cut 2,000 people over 12 months, and close 3 facilities in New York and Michigan. The company estimated that the strike cost it \$370 million in sales, and full year results reflect the impact of approximately \$1 billion of special charges, asset impairments, and other nonrecurring operating costs associated with digestion of these moves. The \$64,000 question is whether, as AAM CEO Richard E. Dauch has said on more than one occasion, 'this has been a transformative year' for the long-term good or not.

With 2009 NA light vehicle production potentially in the 9-10 million unit range, this will probably be another year with plenty of unhappy suppliers to examine. Smaller ones are already quietly closing their doors, but these large public companies will be on view in one form or another, trying to beat the market and their competitors, and get to a happier place.