Continental Media Webcast: Fiscal 2020

Comments of the Chairman of the Executive Board
of Continental Aktiengesellschaft,
Nikolai Setzer,
and the company's Chief Financial Officer,
Wolfgang Schäfer,
on the occasion of the
Continental Media Webcast: Fiscal 2020
on March 9, 2021

Check against delivery!

Please note that all statements are preliminary numbers that still need to be approved or determined by the Supervisory Board.

Wolfgang Schäfer, CFO:

Ladies and gentlemen,

The market environment in 2020 was historically weak. Yet despite the unprecedented number of challenges, we navigated this crisis year in a safe and stable manner. In a highly volatile environment, we had to make adjustments continuously. Our operating performance is impressive! In addition, we remained financially sound despite all the uncertainties. Nonetheless, the bottom line is that we suffered extensive setbacks – in terms of both sales and earnings. So we are not satisfied with our performance in 2020. But we finished the year stronger overall than we had feared in the spring.

Our sales totaled €37.7 billion in 2020, which is 15.2 percent less than in the previous year. After adjusting for exchange-rate effects and changes in the scope of consolidation, we posted organic sales growth of minus 12.7 percent. That means we outperformed the market, since the latest estimates indicate that global automotive production fell by about 16 percent worldwide in 2020. In other words, our organic sales were more robust than the market because the market decreased by over 3 percentage points more than our decline in organic sales..

In this extremely challenging market environment, we achieved an adjusted operating result of €1.3 billion. The adjusted EBIT margin was 3.5 percent. In the previous year, the margin was 7.3 percent.

Our adjusted EBIT does not include additional significant special effects which had a considerably negative impact on our operating result. For instance, we booked non-cash goodwill impairments totaling €649 million in the third quarter. Why? To reflect lower assumptions about the market. In addition, the company in 2020 incurred expenses totaling €998 million, which were largely due to our structural program.

These two situations essentially led to a negative operating result of €718 million. The EBIT margin in 2020 was minus 1.9 percent.

Our Automotive Technologies group sector has been hit hard by the upheavals in the automotive markets and structural change. The sector consists of the Autonomous Mobility & Safety and Vehicle Networking & Information business areas.

Their combined sales totaled €15.3 billion.

In organic terms – that is, without the influence of exchange rates and changes in the scope of consolidation – this represented a 15.8 percent decline in sales compared to the previous year. The production of passenger cars and light commercial vehicles decreased in the same period by about 16 percent globally. That means our performance was in line with the trend in the worldwide automotive market. And we accomplished this despite our strong presence in the European and North American markets, which have been hard hit by the coronavirus pandemic.

The EBIT margin of Automotive Technologies was minus 9.4 percent, while it was at minus 7.6 percent the year before. This was mainly due to the goodwill impairment and expenses arising from our structural program that I mentioned earlier.

Purely in operating terms and after adjusting for special effects, the performance of our automotive business resulted in an adjusted EBIT margin of minus 1.8 percent.

The Powertrain Technologies group sector achieved sales of nearly €7 billion in 2020. Its organic sales growth was minus 8.7 percent and therefore much better than the market decrease of 16 percent. The reason for this outperformance was higher global demand for electrified powertrain technologies. Last year, this already served as an encouraging confirmation of the strategy of the powertrain area to focus on this business field.

The operating result in 2020 came to minus €451 million. The EBIT margin was minus 6.5 percent. In 2019, it stood at minus 8.5 percent.

The adjusted operating result amounted to minus €56 million, and the adjusted EBIT margin came in at minus 0.8 percent.

The effects of the coronavirus pandemic also had a negative impact on the performance of our business with rubber and plastics technologies. The reported sales of the Rubber Technologies group sector fell year on year by 13.2 percent. Organic sales decreased by 11.1 percent.

In 2020, the Tires business area sold nearly 130 million tires for passenger cars and trucks worldwide. That’s 15 percent fewer tires than in the previous year. This decrease was primarily due to the weak winter tire business and low sales with automobile manufacturers, particularly in Europe. In contrast, sales of all-season and two-wheel tires were higher than the previous year. Business in China increased as well. The same is true for the ContiTech business area. Its business in China was likewise higher than in the previous year. In addition, business with industrial customers turned out to be less vulnerable than with automobile manufacturers.

In total, the Rubber business held its adjusted EBIT margin nearly unchanged at the previous year’s level. It was 11.3 percent, compared with 12 percent in 2019. The adjusted operating result totaled €1.8 billion. Given the adverse market conditions, that is an impressive performance. The strong development in the fourth quarter was particularly helpful.

All in all, the company’s bottom line was a negative net income of €962 million. Based upon this, the Executive Board has decided to propose a suspension of the dividend for fiscal 2020 to this year’s Annual Shareholders’ Meeting. This is in line with Continental’s dividend policy, which calls for a distribution to shareholders that equals 15 to 30 percent of net income for the fiscal year.

All in all, following this historically challenging year, our balance sheet remains stable and solid. Our equity ratio is 31.9 percent. At the end of 2019, it stood at 37.3 percent. Our liquidity cushion is extremely comfortable. It totaled €10.7 billion at the end of 2020. This means that we increased it by €2.7 billion compared with the previous year.

Our net indebtedness rose only slightly by €67 million compared to the end of 2019. It stood at €4.1 billion at the end of 2020. That makes our gearing ratio, which is the ratio of debt to equity, a very reasonable 32.7 percent.

In other words, we have a very healthy balance sheet structure overall.

When the coronavirus pandemic broke out, we acted quickly and decisively. We slammed on the brakes in terms of costs. As the economic consequences of the pandemic became increasingly apparent, we trimmed our cost base even further.

We were therefore able to lower our fixed costs in 2020 by more than €860 million versus the same period in the previous year. That represents a decrease of 8 percent. We thus reached our target of reducing our fixed cash costs by more than 5 percent compared with 2019.

In 2020, we also scaled back our capital expenditure on property, plant and equipment, and software by €1 billion. In total, we spent €2.2 billion, which is a year-on-year reduction of more than 32 percent! All business areas contributed to this decrease.

Despite challenging conditions, Continental generated very strong cash inflows before financing activities in the past fiscal year. As a result, free cash flow before acquisitions and carve-out effects totaled €1.1 billion. In comparison, in 2019 we generated €1.3 billion.

And now to the outlook:

The fourth quarter of 2020 has shown that the worst is behind us. The economic environment is gaining momentum again. The start of the current fiscal year has, however, been subdued so far due to the shortage of semiconductors. The effects of the ongoing coronavirus pandemic remain a source of uncertainty too. All in all, 2021 will therefore continue to be challenging. We nevertheless anticipate that the market will recover significantly compared with 2020.

We expect the production of passenger cars and light commercial vehicles to increase year on year by 9 to 12 percent. But we still do not expect to reattain the record level of global automobile production we saw in 2017 before 2025.

On the basis of our assumptions about the trends in our markets and industries for 2021, we anticipate consolidated sales of around €40.5 million to €42.5 billion and an adjusted EBIT margin of around 5 to 6 percent.

We expect the new Automotive Technologies group sector and the former Powertrain division to generate combined sales totaling around €24 billion to €25 billion and an adjusted EBIT margin of around 1 to 2 percent. Here we have already taken into account expenses such as extra freight costs totaling about €200 million resulting from the shortage of semiconductors. It also includes capital expenditure and expenses for the further expansion of our business with assisted and autonomous driving. Mr. Setzer will go into more detail about that in a moment.

Sales in the Rubber business areas Tires and ContiTech are forecast to total around €16.5 billion to €17.5 billion, with an adjusted EBIT margin of around 11.5 to 12.5 percent.

As you can see, although our expectations for the fiscal year remain subdued in some cases, they are upbeat overall.

And on that note, I will now hand over the floor to Niko Setzer.

Nikolai Setzer, CEO:

Ladies and gentlemen,

2020 was an enormously strenuous year for us.

The coronavirus pandemic, the transformation of the automotive industry and our structural program: All that combined demanded a great deal from us.

Given the multitude of challenges that we faced, the Continental team acted quickly and decisively. We demonstrated a high level of discipline when it came to reducing our expenses and capital expenditure and adjusting our cost structure. I am therefore especially grateful once again to all employees worldwide for their extraordinary commitment, their cost discipline, and their adaptability. We have become crisis-proof as a result. We are looking forward once again. We are on the way back up.

We enhanced our comprehensive protection concept for our employees right at the start of the coronavirus crisis in order to ensure a working environment that was safe during the pandemic. Around 85,000 members of our Continental family worked from home last year. In Germany, 80 to 90 percent of our office employees are currently working remotely.

Our employees in all countries have exchanged ideas and started projects via the various Continental networks. Their goal was to help other people around the world. They provided effective assistance, for example by producing protective equipment. One of our four corporate values is “For One Another.” And we experienced that here. Here, too, I am grateful for what our workforce has accomplished.

My – and our – thanks also go to my predecessor at the head of our organization, Elmar Degenhart, who stepped down from his position at the end of 2020 due to heath reasons after more than a decade in office. In the more than 11 years he served in that role, he established a crucial foundation on which we base our future viability and long-term value creation.

Elmar Degenhart and I always enjoyed a very close and trusting working relationship, especially when it came to creating our strategy and implementing our transformation. I hold him in highest esteem – as a leader, as a person, and as an adviser. I would like to take this opportunity to thank him once again for his support and encouragement, and I wish him all the very best for the future, especially when it comes to his health.

The next steps in Continental’s journey are clear. Our roadmap is ready. We unveiled our realigned strategy at the end of 2020 at our Capital Markets Day event. It is based on the following three cornerstones:

First: our future portfolio strategy. Our approach is deliberate and differentiated. We will differentiate systematically between two different areas of focus: namely “growth” and “value.” These are two different kinds of value creation over time. When focusing on “growth,” we are developing and designing products and product sectors in a dynamic and innovative environment. When focusing on “value,” we are developing and designing products and sectors in saturated markets with stable market structures.

The second cornerstone: our operational performance, which we are increasing continuously. After all, it is the prerequisite for all entrepreneurial freedom.

And the third: our strategy for connected and sustainable mobility. Here, we see opportunities emerging from the accelerated pace of transformation. We will harness these opportunities with greater determination than ever before, and above all, with much more focused energy.

The growth field for advanced driver assistance systems and automated driving serve as an important example for the future. The market is highly dynamic in this area, creating further growth potential for us. We will fully exploit these opportunities by pooling our resources and intensifying our efforts. We are not alone here. We are opening ourselves up even further to cooperation with technology partners and start-up companies. These already include NVIDIA, Aeye and, as recently announced, Recogni.

In this area we are already one of the pioneers. For instance, in 1999 we played a key role in the world’s first volume-produced adaptive cruise control for the Mercedes S-Class.

Since then, we have been leading the pack when it comes to assisted and automated driving systems. Just in the years 2018 to 2020 alone, we received orders for these systems totaling more than €9 billion from car manufacturers worldwide.

We intend to increase this amount substantially in the coming years, as the potential scope of our supply will go up in value many times over as the degree of automation grows. That is why we are increasing our investments and expenditures. In this year alone, we are planning to spend about an additional €200 million to €250 million more.

By doing so, we are accelerating the pace with which we are positioning ourselves as a top player in the autonomous mobility market. After all, our goal is and will continue to be the global leadership when it comes to assisted and automated driving!

Automated driving fosters anticipatory and safe driving, and thus sustainable mobility. This fits in well with our ambitious goals that we already set ourselves early in December 2020. With our comprehensive sustainability roadmap, we are paving the way for a new global industry standard. Part of the roadmap relates to emission-free vehicles: From 2022 we will have achieved carbon neutrality in our global business for emission-free cars, buses, trains and other vehicles.

At the same time, we are working intensively to reduce our own CO2 footprint even further. In 2020, for example, we introduced green electricity in every plant. Our entire procurement of electricity thus became

CO_2 neutral all at the same time. This step alone saves more than 2 million metric tons of CO_2 every year.

Our targets are ambitious but they are within our grasp: by the end of 2040, we aim to reach CO_2 neutrality throughout Continental's entire production network.By 2050 at the latest, we aim to be 100 percent carbon neutral across our entire business, from one end of the value chain to the other.

We are investing in a sustainable manner, and by doing so, we are investing in the future: in safe, connected and sustainable personal mobility. And at the same time, we are investing in our own future. This is demonstrated by our research and development expenses of €3.4 billion in 2020, which was at the same level as in the previous year.

This means we strengthened our technological expertise further. And by doing so, we are implementing new key solutions and getting them on the road.

Overall, we successfully launched more than 800 production series worldwide. In Automotive Technologies alone, we delivered more than 1.4 billion components and systems. Once again, let me express my sincere gratitude to everyone in the global team for their continuing hard work and commitment!

Numerous products and systems for VW's fully electric ID.3 model are some of the successful production launches. A highlight in the car: Continental's high-performance computer.

In total we have already achieved an order volume of more than €4 billion for high-performance computers. That makes us one of the top players when it comes to both high-performance hardware as well as high-performance software.

More and more often, software is what matters in our markets. It is becoming ever more powerful – in some cases with the help of the automotive industry's fastest computer, which we put into operation in 2020 for the artificial intelligence area. With this, we are substantially speeding up the AI training of advanced driver assistance systems. Weeks become hours: that is all we need to train new assistance features. And with simulations, we are also replacing some of the actual test drives on the road.

And that is where performance counts. A current example is our first radar-based turn assist system for retrofitting trucks. It helps truck drivers in unclear situations by lighting up the blind spot and providing a timely warning, thus preventing accidents with cyclists or pedestrians.

We are also strengthening our technology position in the area of tires with high tech. Here, we are connecting tires with sensor systems, telemetric data, algorithms and the cloud. That is the future of tire monitoring. The car-sharing provider SHARE NOW is already benefiting from our services. It was our first customer where we deployed our cloud-based monitoring of tread depth – in real time with millimeter precision. The algorithms of this service ensure disruption-free mobility.

ContiTech's service business is being expanded and digitalized, too. Here, we will also rely on drones going forward. We are equipping them with powerful cameras so that they can automatically monitor kilometer-long conveyor belt systems. Artificial intelligence ensures our customers smooth processes and greater service quality at lower costs.

All these examples create a sustainable basis for expanding our business. Our structural program is sustainable too. The implementation of our transformation is making good progress. We are working in a solution-oriented manner with our social partners at the locations that are affected by the program. Our aim is to create sustainable prospects for those employees that have been affected, while at the same time securing the future viability of our company. It is absolutely clear that this process is sometimes painful. But global competition is becoming increasingly fierce. Therefore, we will only be able to secure our future success and thus jobs if we undertake the appropriate adjustments.

Despite all the challenges, we remain confident about our prospects in 2021. A year, by the way, in which we celebrate our 150th anniversary.

Since its foundation, our organization has celebrated many highs and overcome many lows. We are now experiencing a profound turning point in our industry that we will use to springboard our start into a new era. Now comes the next crucial step as we transform ourselves into a global technology company for connected solutions, with the focus on mobility. To do this, we are not just exploiting our traditional strengths – we are also considerably expanding in particular the areas of digitalization, software and sensor technology.

Ladies and gentlemen,

We have a success-driven global team, a pioneering technology portfolio and comprehensive software expertise. These strengths will make us one of the winners of the transformation of the mobility industry.

For me, it is clear that Continental makes the difference in today's mobility market – as it will in the next 150 years.