

## **Transcript**

# **Schaeffler AG Conference Call**

**20. August 2020 Herzogenaurach**

### **Operator**

Dear Ladies and Gentlemen, welcome to the Schaeffler Group conference call. As a reminder, all participants will be in listen only mode. After the presentation, there will be an opportunity to ask questions. If any participant has difficulties hearing the conference, please press star key followed by zero on your telephone for operator assistance. At our customer's request, this conference will be recorded, and the replay will be available shortly after the call on the website. May I hand you over to Renata Casaro who will lead you through this conference. Please go ahead.

### **Renata Casaro**

Thank you, operator. Dear investors, dear analysts, thank you for joining this short notice invitation to a very short conference call. Mr Rosenfeld, CEO of the Schaeffler group, Mr Patzak, CFO, and the IR Team are here in Herzogenaurach. After five minutes short introduction, we will take your questions. Since the call will be only 30 minutes long, please ask maximum two questions in order to enable also to other participants to intervene. I leave now the floor to Mr Rosenfeld. Klaus, the floor is yours.

### **Klaus Rosenfeld**

Thank you very much Renata. Ladies and gentlemen, good morning, everybody, and thanks for joining our short conference call today. As Renata said, I'm here with Klaus, and we have created some news flow this morning. We don't want to make it bigger than it is, but as authorised capital is new for Schaeffler AG, Klaus and myself, we thought it's important to be transparent and to convene a short conference call. You all got the IR press release, that is very clear. We are convening an EGM for authorised capital to be in the position to issue up to 200 million new non-voting common shares. And while this EGM does not require the free float investors to vote, we wanted to be open and explain the background for this move. As stated in the press release, the main reason for this is we want to be able, through this authorisation, to enhance our capital base over the next five years, to be able to play the transformation of the Schaeffler Group, the further transformation in the aftermath of this crisis from a position of strength, taking advantage of opportunities which may arise while we continue to focus on becoming more efficient our cost structures, enhance our competitiveness. And will, as we promised, in our conference call on 4th of August, remain

disciplined from capital allocation point of view. You all may wonder, why is that today? And I think you will all concur that while it's absolutely standard for many companies, and normally conveniently done on the same day as the regular AGM, these are interesting and challenging times and therefore, we decided to take the opportunity now and ask for the authorisation. We could have done this in the regular AGM back in May but as all of you know, that was in the middle of the storm, in the middle of the crisis. And in April and May we were clearly engaged with other pressing priorities - business continuity, focusing on the outlooks, business customers, and also on our, you know, normal program, like paying you a dividend. And therefore, at the time we decided against it and have now pulled this forward and presented it to you. Let me be very clear here: to start with, nothing has changed since our Q2 earnings call on August 4th, the business trend from July continues. It's a constructive environment, and also August looks promising so far. And also, our plan going forward has not changed. We will - let me make that clear, here - evaluate whether to guide in a detailed way for a full year 2020. We are, as we promised, currently working on additional structural efficiency measures. And later in the year, in November, we'll have our Q3 earnings, and also a Capital Market Update. At the same time, this EGM that is scheduled for the 15th of September is a governance step that we wanted to take sooner rather than later, and without waiting for the next AGM in spring '21 as I indicated. This is our thinking behind the authorised capital request. And let's stress already at this point that this authorised capital does not mean that there is an immediate transaction behind it. Schaeffler has - as you, I think, would share - a comparably robust balance sheet. We consider important to be in the position to improve its strengths. So by having this authorised capital, we can also have on one day to option to reduce our debt position even further, and to reduce also our leverage ratio. In terms of discipline, you see and saw what we have been doing on CAPEX and you already know that we are also working on the structural self-help measures going forward, on top of the temporary initiatives that we have already put in place. For me, it's even more important than to look forward and say as a company: with this environment, we want to be able to win in this market, we want to be able to take advantage of what the new normal will be, maximizing flexibility from my point of view and from our point of view in the post-COVID area is absolutely a must. We are convinced that COVID will bring these structural changes, and whether this is internal or external growth remains to be seen. In any case, our M&A strategy will not change, we'll follow the course that we've always promised to you. Let me also make clear - because there were already questions about this in the past and also now - we are listed, we are committed to stay listed, and we are committed to continue successfully our transformation of Schaeffler Group as an automotive and industrial supplier. And in particular, this mix gives us more opportunities than other companies that are more focused on one sector or on one customer group. And we are here clearly here, not only to win but to improve our value creation as we've always said. Let me add we are convinced that our next steps in our performance improvement journey will be compelling, and as a listed company, we hope that the existing and potential new investors that we may gain from this...from a potential transaction or capital increase will want to participate even more in such value creation. At the same time, we are aware that the current level of free float is not really optimal. Liquidity in the stock is comparatively low, if you compare companies of our size with us, and if one day we could also potentially have a higher free float. This could also help you, as our investors, in participating in the journey going forward. Let me

come to the end here and finish by saying: we are a leading player in attractive markets, the crisis offers opportunities, we will continue to shape our portfolio, and we are determined - Klaus and myself in particular - to make this company not only more competitive, but also future-proof. Our cash situation is healthy, the liquidity situation is strong, and we have only moderate leverage at the moment. This all enables us to think into the future and make Schaeffler even stronger. I stop here, I know that you're all interested in more background, and we are open to your questions. We want to keep this short, but we thought it's better to be available for you than leave too much room for speculation what's behind it. This is an authorisation, it's not a transaction, it's not a request for capital immediately. But it will give us optionality and it will give us flexibility, also with respect to a potential increase of our free float. Thank you very much, and back to you Renata.

### **Renata Casaro**

Thank you very much. Klaus, dear operator, we can open now the Q&A session, two questions per person, thank you.

## **Q&A**

### **Operator**

Thank you. Ladies and gentlemen, we will now begin our question and answer session. If you have a question for our speakers, please dial zero and one on your telephone keypad now to enter the queue. Once the name has been announced, you can ask a question. If you find your question is answered before it is your turn to speak, you can dial zero and two to cancel your question. If you are using speaker equipment today, please lift the handset before making your selection. One moment, please for the first question.

### **Kai Mueller (Bank of America)**

Hi, thank you very much and thanks for doing the call at such short notice. The first one, if I think about - obviously, you mentioned two areas: one is for the transformation, the second part for the growth. If you think about the capital requirements for both trajectories, how would you split them between each other? And in terms of transformation, do we think about transformation meaning more spending on potentially R&D on new product areas? Or is it transformation as in restructuring, changing the business around for the new world? The first one, and then the second one, maybe a bit more focused on the M&A side. You say, you know, your M&A aspect is the same as before. I understand in the past, you always, you know, looked at small clips, 100, 200 million deals. Now, obviously, something like this would give you much more scope. I mean, at the current share price it's about 1.2 billion in equity. What level of leverage would you be able to put on that in your view, and would you also consider a more transformational deal if those opportunities arise?

### **Klaus Rosenfeld**

Thanks, Kai, for the for the two important questions. And thanks for joining. The term transformation is clearly used in a broader sense here. It's something that Klaus and myself - and Klaus may want to comment here after his first three weeks - see as a long-term journey to move this portfolio forward, to allocate capital wisely and see where...how we built the company for the next five to 10 years. So, I wouldn't go into such detail that you request and say, is this now restructuring or internal growth or external growth and how would you allocate it? That's too early. The most important thing here, once again, is to have the optionality. There will be opportunities that we couldn't think about before the crisis, and we want to be ready for these opportunities when they arise. And that goes to the second question as well, and then I hand over to Klaus. M&A strategy has always been articulated as smaller transactions focused on technology and bold on acquisitions. You know, the size of this, we always said, is a three-digit number. We never said it's always below 100. So, let's not speculate too much about the size. You all know that such an authorisation doesn't have to be utilised in one go, it can be used in several steps. The most important again, is optionality. I don't want to fuel any

speculation here that this is now the preparation for any mega transaction. That's not the case. We will continue with our focus discipline, and also risk-conscious strategy in adding to the portfolio and adding to the technology, we have what we need in making this company successful.

### **Klaus Patzak**

Yeah, just add on that. I fully share that...the view that there is a benefit of having a complete toolkit available, right? Specifically, in the current times. You know, when you asked about transformation, what I believe is important that companies, you know, try to define now how they can, you know, replace interim measures, interim cost saving measures, with more long-term structural measures. Obviously, that that's then a topic of footprint. It's also something for...with regard to overhead structures. I have the experience that is, you know, quiet a room, typically in overhead structures, and that is something what I'm looking to right now. And I think that is something which also can make the company not only leaner cost-wise, but in the end, also fast in decision making. So we look at structural things here. Obviously, we look also at business mix and what that means. For me, it's a bit too early to have a final say on that. But in the end, I think we have to differentiate between the different parts of our business parts which are...which are more kind of, you know, geared in the direction of cash generation and cash performance and other parts where we, you know, have to grow, but with a view on profitability improvement over time, and this is how I look at it.

### **Klaus Rosenfeld**

Thanks, Klaus.

### **Kai Mueller (Bank of America)**

Yeah, maybe just one quick follow-up on this. And one quick follow-up, is when you think, you know, on the on the capital side, let's assume on the current share price is about 1.2 billion, is that...if...when you do it, also in order to improve your equity ratio, which is obviously with the write-downs you've been taking, falling? Or would you be able to take that 1.2 billion and actually, you know, run a similar debt to equity, leverage what you currently have, and actually have more firepower to do more things?

### **Klaus Rosenfeld**

I think you're asking questions that would relate to a potential transaction and it's too early to answer that...this is about a preparedness in a complex landscape and not...let's not speculate what the price would be, what we would do with...what...with the inflows. I think what you...what

you can take away - let me stress it - this is also a strong sign of trust from the family, from the major shareholder who says: we will give you flexibility. This is a capital...a potential capital increase with subscription rights, how that will be utilised, also in terms of participation by the IHO, remains to be seen. And that's what the press release says. It says it's there to strengthen the base, to push forward the transformation, and there's a second last sentence that also says there is a potential for higher free float. And that's a function of the participation of the IHO or not.

### **Kai Mueller (Bank of America)**

Fantastic, very clear. Thank you.

### **Renata Casaro**

Thank you, Kai. Next question, please.

### **Henning Cosman (HSBC)**

Yeah. Hi, good morning. Please, can I just ask about the timing of this? You mentioned that you had decided to not do it at the last regular AGM. And now I'm more interested why you think this can't wait until the next regular AGM? So, yeah, I mean, this is really the first question, if you can just - without leading you too much on this - if you could just explain again, how you think about this. And then just maybe in the context of both valuation and timing with respect to your Capital Market Day. At share price of six euros when you know, not too long ago was closer to 10, I would...I would think a lot of people hope you wouldn't execute it at such levels. If you could maybe give us an indication how you think about the level at which you think this would be...this would be interesting, relative to through how good an opportunity would have to be to do it at such a level? And then also timing-wise just, you know, before the Capital Market Day, which of course you want to do at year end - and I would suggest that there might currently be a missed valuation because of arguably a misconception, for example, your overexposure to internal combustion engine, which I suppose you were hoping to rectify at the capital market day - how you think about, again, in the context of why can't this wait until the next AGM? Why would you want to do it before you have the opportunity to rectify things, give midterm guidance at the Capital Market Day, allow the share price to go higher? If you could just sort of contextualise that a bit for us. Thank you.

### **Klaus Rosenfeld**

Sure. Absolutely. I mean, once again, this is not a transaction. And this is not a capital increase. This is an authorisation. And the authorisation is about having optionality. And it's good to have

optionality sooner than later. Why should...? I don't really understand, by the point, why should I wait now? It has nothing to do with the share price. It's an authorisation. And it's a governance and more technical point, in particular, in our situation with the capital structure we have. So, you can say, why did you miss it in the first ordinary one this year? That's a fair point. But there...I mean, you all know how unusual this crisis was, and how much we had to cope with dividend payments and getting the company on track. But I can tell you this is a part of a plan that was discussed for quite some weeks and months with the family to do the right thing. And it's now from our point exactly the time to get this through, get the authorisation, have it in place and have the optionality. Why wait with optionality, if in particular, if a crisis starts to, you know, become...slow down a little bit, and the optionality maybe come sooner? But again, you should not read anything like into this, that this is a transaction. It's an authorisation with a tenor of five years. It's significant numbers of shares. And I think it's good for us, because it prepares us for steps sooner than later. But the steps are not up for debate today. And if there's anything, and if we come up with something, we will let you know. But you can be rest assured that we're not going to buy or sell any shares. That's definitely not what the family is interested in.

### **Henning Cosman (HSBC)**

So you know, nothing imminent, more or less than it would have been the case at the Q2 stage, yeah?

### **Klaus Rosenfeld**

Correct. That's what I said. And, you know, if you read the steps and you try to find a logic in this. We were the first ones who had address balance sheet risk impairments. Q1, everyone wondered, what is that? Now we then said, we come out of this crisis a little bit stronger than others because the portfolio is diversified. It's not only automotive supply, it's Auto in Industrial. We are there with a strong liquidity position, and not because we raise debt somewhere and put it on the cash balance that now we have a great liquidity position. We have been very modest with any type of debt. And I think it's right at the moment, why should I raise all this debt to bolster my liquidity position then to have to repay it? So, it's unnecessary. Balance sheet is, you know, not really strong, it's comparatively, you know, the equity ratio, which is 15%, is that really, sort of, very strong? No, it's not. So, increasing that a little bit could help. But that's not the driver of this. The driver of this is being prepared for the transformation to come, as Klaus said. And I think this is nothing now to interpret and read anything into it. You know, there's tomorrow at transaction. That's not the case.

### **Henning Cosman (HSBC)**

Understood. Thank you. I'll get back into the queue.

### **Victoria Greer (Morgan Stanley)**

Good morning. Just a couple, please. I guess, totally understanding that you don't want to comment about the potential share price this could be executed at. But if we just take, I guess, today's share price as a starting point, let's say, about 1.2 billion, this could theoretically authorise you for...historically that, in better years, not talking about 2020, but that's a couple of years of free cash flow. So, historically, you have generated pretty good free cash flow. Should we think of future free cash flow as at least partly burdened by ongoing restructuring, and therefore incremental growth needs to be funded externally? Is that the right way to think about it? And secondly, thinking about your discussions with OEMs for new contracts: do you think that this greater flexibility in your ability to fund growth will help in winning contracts? Has that come up in in existing discussions? Thanks.

### **Klaus Rosenfeld**

Now, Victoria, thank you very much, much appreciated. I believe this is a once in a lifetime crisis and it will shake the industry. There will be winners and losers and there will be strong companies and there will be weaker companies. And if you want to win - then I start with your second question - at the customer front, our business in particular (automotive OEM) is a long-term business where you need to be a partner that the OEM can rely on. And therefore strengthening the capital base is not only financial metrics, it is something to - and that's in our specific situation, with a strong family ownership...that's an important sign to the employees but also to our business partners - to say we will stand behind this company. No one says, and that's your first part, that we will utilise anything like this in one goal. You are calculating, rightfully so the maximum possible, but it doesn't say that, it says up to 200. So, don't read from this: oh, they can't find their future goals. We will, as I said in my little introductory speech, be very consequent and disciplined, in particular also with Klaus' help now, on cash generation. And this is not a sign that we think we will lose our cash generation power in the future and therefore, now need something for internal growth. We will continue to be disciplined, but we also want to be in a position that we can say: we came out of this crisis with the right, flexibility with the right backing and with optionality that others may not have that have today leverage ratios that are increasing and increasing.

### **Victoria Greer (Morgan Stanley)**

Okay, great. And...

### **Klaus Rosenfeld**

...on the cash conversion, something, or the cash focus...?



## **Klaus Patzak**

Well, I think, you know, cash performance obviously is something which is in my heart. I believe that still there is room for improvement in the company. If I compare it with other companies, I believe in the end also in performance management, we made already in this first couple of weeks, a couple of positions - Klaus and myself, you know, how we can focus the company more on cash conversion rate, Capex ratios and things like that. Also differentiating again, differentiating between the different parts of the business, you know, differentiating in the period for amortisation we are now entering and things like that. So, you know, here we still have room to improve. And on top of these topics, I believe there is an opportunity on the overhead side which can also obviously...you know, there would be then a cash impact from improving the structure, but that would come with a significant payback and would also help us to fund growth out of that state.

## **Victoria Greer (Morgan Stanley)**

Okay, great. And so as you said....

## **Klaus Rosenfeld**

Is that okay for you?

## **Victoria Greer (Morgan Stanley)**

Yes, absolutely, and so...as you said, we shouldn't necessarily think that the whole 200 million shares would come all at once. Would it be structured, that you could do it, say, in two different tranches, or...how should we think about that? Yeah.

## **Klaus Rosenfeld**

It is...you know, it's a very flexible way to do it. The only thing that it says, it would be with subscription rights. And it's up to 200 million, you can use it several times. It's there available for five years. But it says nowhere that you cannot...you have to use it in one go. It's a framework, so to speak, an authorisation, that you can then use with the...a decision of the supervisory board and a decision of the board.

## **Victoria Greer (Morgan Stanley)**

Okay, so, okay, so once you have the EGM approval, you don't then need a further meeting to...say you suddenly wanted to do 50 million for some reason, you have the flexibility to do that?

**Klaus Rosenfeld**

Correct. Okay.

**Victoria Greer (Morgan Stanley)**

Great, that's clear, thank you.

**Klaus Rosenfeld**

Yeah. And then you can see what you do with it. Whatever structures are available, that's something that we need to investigate.

**Victoria Greer (Morgan Stanley)**

Great, thanks.

**Klaus Rosenfeld**

You're welcome.

**Sascha Gommel (Jefferies)**

Yes, thank you for taking my questions as well. The first one would actually be on the on the magnitude of the 200 million shares. Most companies have kind of a 10% authorised capital, you're going out for 30%. Is it just to kind of have a significantly higher flexibility, or...what's the reason for the large number? And my second question is actually on the share classes. Just to understand, in case you would go ahead, the family, despite owning the voting shares, would still have subscription rights? And then related to that, I think two years ago, you...there was a discussion if the family convert some of their voting shares. That's off the table now, indefinitely?

**Klaus Rosenfeld**

Let me go to the last point. I mean, some of you have been with us longer and know this transaction. And we clearly took our lessons from this. And you remember we did, at the time a little roadshow, with proxy advisors as some of our major shareholders, and got very mixed feedback. And that's why we decided to not pursue the transaction anymore. And you know, I

can say that it's a learning from the past, and there are no plans to convert or do anything similar as we tried at the time. I think this is a much more straightforward solution because if a transaction would be executed, the money would not go to the Schaeffler family, it would go into the company, to strengthen the company's capital base. That's why I said it's a sign of trust for the management team, it's a sign that the family stands behind this company, and would allow either higher free float, or would need to participate by putting money into the company. But there is no plan for a conversion, like we looked at in 2018. The magnitude, you know, you can now debate this. It's a framework. As I said before, there's no reason to go to 10%. There's no reason...final reason to go to 30%. It was, at the end of the day, a proposal where the family said up to 200 is fine. But that's it for the time being.

### **Sascha Gommel (Jefferies)**

Okay, and maybe one quick follow-up...

### **Klaus Rosenfeld**

For us, it's important that this is significant, and that we can do something with it. So, it was a balance between, you know, what is the maximum possible and what's reasonable. And that was the number we ended up with.

### **Sascha Gommel (Jefferies)**

I see. One quick follow-up on the timing as well. Why not wait for a transaction in terms of external growth that you can present and then link it to that, where investors understand better what you want with the additional capital, instead of just getting kind of a blank check of 200 million shares?

### **Klaus Rosenfeld**

This is not a blank check. This is what all other companies have in the DAX. I mean, this is...as Klaus said, this is a normal, standard part of the toolbox. And for some reason, in Schaeffler, it was not available...and maybe Klaus, you want to add, but all the other, bigger listed entities have these kinds of flexibility, and that's what we thought is good for Schaeffler as well. So, it's something where we basically, you know, complete the toolbox.

### **Klaus Patzak**

Yes, exactly.

**Sascha Gommel (Jefferies)**

Okay, appreciate that. Thank you very much.

**Klaus Rosenfeld**

You're welcome.

**Christoph Sandsdrom (Acuris)**

Hi, thank you Good morning. I strongly suspect the answer is no to both my questions, but I just want to double check. First of all, have you made any preparations already for a potential cap hike as such, in particularly mandates, advisors appointed, or any talks to shareholders or free commitments out of the vote or any potential deal? And second, on the same note, do you have a best guess today for when the cap hike my happen? And I'm trying to guess, basically, whether this is likely to happen in this year, or if it's just like a standard...standing authorisation that could happen anytime. Thank you.

**Klaus Rosenfeld**

Well, the first question is a very easy answer: the answer is no. We have not mandated any bank or anyone to do that. And the timing of a utilisation of the authorisation is something that I cannot comment on. We have always played according to the rules -we will communicate when we are ready, and we are not ready.

**Christoph Sandsdrom (Acuris)**

Good. Thank you.

**Operator**

We haven't received any further questions at this point. So, as a reminder, if you would like to ask a question, please press zero and one on your telephone keypad now. There seems to be no question after all.

**Klaus Rosenfeld**

Let's finish the call. Thank you very much, ladies and gentlemen. A pleasure that you joined on short notice. We know it's summertime, and we thank you for your attention. The recording

of this will be made available through the normal online tools. Once again, have a nice day. Goodbye, and thank you very much.

## **Operator**

Ladies and Gentlemen, thank you for your attendance. This call has been concluded. You may disconnect now.