Twitter Thread by JPR007



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VW LOOKS INTO THE VALLEY OF DEATH

The disruptive threats Herbert Diess saw coming for big, incumbent automakers soon after he took over the top job at Volkswagen Group are playing out as predicted -- only faster and in more dramatic fashion

In an interview, Diess said additional cost reductions and a speedier overhaul of the German industrial giant are vital to withstand new rivals with superior financial firepower

He has been reflecting not only on trying to keep pace with Tesla but on the risk that Apple adds another mighty competitor with almost unlimited resources to the automotive arena

“Despite all efforts, we are currently in a rather more difficult situation than in 2018 when I took office," Diess said

"What really has changed -- and what I had not expected to this extent -- is the view of capital markets on our industry”

In the almost 2 1/2 years since Diess told investors VW needed to aim for valuation levels more in line with Apple, Amazon and Google to still be around for another two decades, the gap has only grown

Elon Musk has beaten him to the punch by fetching an almost $700 billion market capitalization with Tesla, making the company worth more than the next six most-valuable carmakers combined

This is more than just a matter of bragging rights

In a single week last month, Tesla and Chinese electric-vehicle makers Nio and XPeng raised $9.7 billion worth of capital by selling stock

The $5 billion that Tesla raised was equivalent to about half of VW's annual net cash flow

VW group sold 8.31 million vehicles through the end of November last year, dwarfing Tesla's full-year deliveries of almost 500,000 cars

But Tesla's ability to sustain profits for five straight quarters after years of losses ignited investor enthusiasm both about its business and those trying to replicate its success

China’s XPeng and Li Auto listed on U.S. exchanges last year along with several startups that merged with special-purpose acquisition companies, including Nikola Corp and Fisker

Some analysts are warning the trend is overdone

The combined roughly $1 trillion market cap of traditional global auto manufacturers remained largely unchanged over the past 12 months, while the value of new rivals went through the roof

“Valuations of and sentiment toward traditional vehicle manufacturers continue to be far too pessimistic," Sanford C. Bernstein analyst Arndt Ellinghorst said in a note last week

“We remain convinced that established companies with global reach, brand equity and strong balance sheets will play a dominant role in the future of mobility”

UBS Group analysts led by Patrick Hummel have made VW their top pick among European automakers, predicting that "winning EV strategies are likely to be rewarded with higher multiples”

VW Group aims to become a global EV force, with the industry's largest investment plan of almost $90 billion over five years

VW cautioned in November that ongoing fallout from COVID-19 will weigh on earnings this year but stuck to its mid-term financial targets, which include restoring net cash flow to more than 10 billion euros ($12.3 billion) as early as 2022

Delivering on these goals could go a long way to defy skeptical investors that remain unconvinced VW can become more nimble

“We haven't sufficiently proved yet that we can hold our ground in the new competitive environment -- our valuation is still located in 'old auto’” Diess said

“This leads to a grave disadvantage for us in terms of access to required resources”

Investments that VW and its peers are making in EVs, software operations, mobility platforms and self-driving technology will be enormous

Investors would face much higher dilution if the companies were to try raising funds by selling stock as Tesla has, and such a scenario is further complicated at VW by its complex shareholder structure

While profits from Porsche, Audi and its Chinese ventures have filled VW Group's coffers over the years, its high fixed costs were exposed when sales tanked during the pandemic

Earnings at several peers proved more resilient

"We must significantly improve our costs and work on efficiency, to gear the traditional auto business significantly more toward returns," Diess said

He sought to rally the troops last month by declaring VW would pit its largest factory in Wolfsburg, Germany, against Tesla’s plant still under construction near Berlin

VW also embarked on a plan to reduce material costs by -7% within two years and hammer out a deal with unions in the first quarter to lower fixed costs -5% by 2023

Diess, who ruffled feathers last year by trying to narrow the group’s focus on its main car operations, insists the company can ill-afford to waste time

"The overhaul is still progressing too slowly," he said

The former BMW executive received a fresh vote of confidence last month from VW's supervisory board to pursue his overhaul and trim costs

He warns there could be dire consequences if the company that employs 670,000 people worldwide does too little and too late to change

"Not everyone realizes the threat to our company to the same extent," Diess said