TI Fluid Systems Exit: A potential credit crisis argues for capital reallocation

Company:	TI Fluid Systems (TIFS LN)	**Market Cap:**	£546mio
Industry:	Auto fluid systems	**Net Debt:**	EUR 600mio (excl. leases)
Country:	Worldwide	**Revenue:**	EUR 3.26bn
Date:	15th March 2023	**Net Income:**	EUR 70mio (2.15%)
Dividend:	EUR 30mio (4.5%)	**Free Cash Flow:**	EUR 80mio (2.45%)
Entry:	£622mio	**Exit:**	£572mio

Positive financials…

TI Fluid Systems (TIFS) remains one of my top picks for turnarounds in this year. For once, I have not understood why TIFS has underperformed their competitors so badly from November 2022. Despite a bigger impact from China lockdowns, H2 2022 actually showed a similar adjusted EBIT as H2 2019. They valuation should hence be higher than the November 2022 lows.

TI Fluid Systems' financials

Full year

Item	2018	2019	2020	2021	2022
Revenue	3,473	3,411	2,815	2,957	3,260
Adjusted Ebit	374	340	173	213	180
Adjusted Net income	155	150	14	58	
Adjusted FCF	146	172	148	117	80
Net current assets	606	651	670	708	
Cash generated from operations	450	477	374	320	
Working capital	-32	-15	62	-14	

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H1

Item	HY 2018	HY 2019	HY 2020	HY 2021	HY 2022
Revenue	1,767	1,708	1,183	1,523	1,560
Adjusted Ebit	256	246	28	128	84
Adjusted Net income	78	65	-40	45	9
Adjusted FCF	21	17	35	46	-2
Net current assets	581	606	670	700	761
Cash generated from operations	165	184	142	151	91
Working capital	-92	-59	41	-34	-65

H2

Item	H2 2018	H2 2019	H2 2020	H2 2021	H2 2022
Revenue	1,706	1,703	1,632	1,434	1,700
Adjusted Ebit	118	94	145	85	96
Adjusted Net income	77	85	54	13	
Adjusted FCF	125	155	113	71	82
Net current assets	25	45	0	8	
Cash generated from operations	285	293	232	169	
Working capital	60	44	21	20	

Source: TI Fluid Systems

Positive production growth…

While H1 2023 will still show an impact of Covid related shutdowns in China over January, automotive production of their top 10 clients is expected to increase by 6.5% compared to 2022 (table below with details). Although total world automotive production will climb only slowly and is set to stay well below the pre-pandemic levels, the growth is positive for TIFS and their outperformance compared to global automotive production is set to continue.

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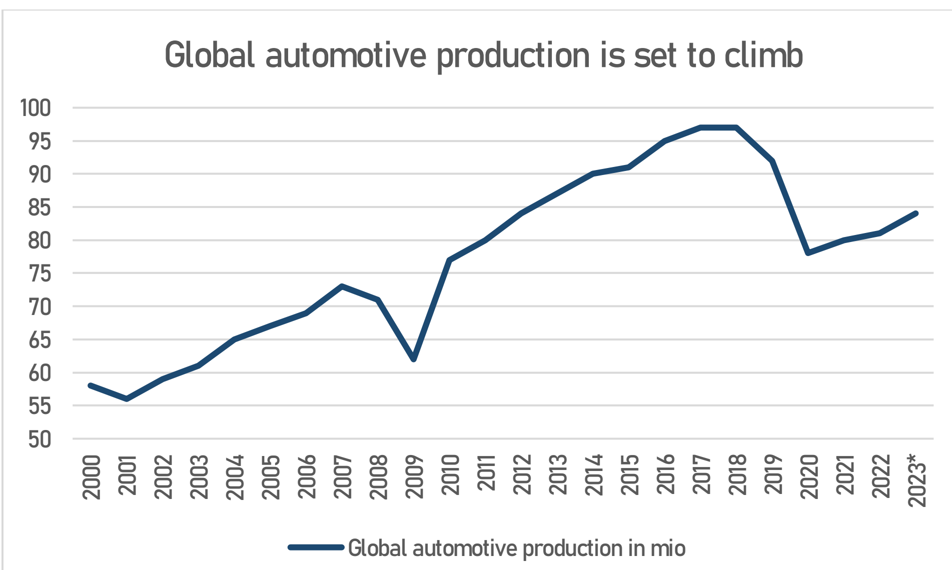
TI Fluid Systems' top 10 OEM client's production growth

OEM	ICE production 2022	(P)HEV production 2022	BEV production 2022	Total production 2022	Total production 2023	2019 vehicle sales	BEV growth 2022
Volkswagen	7,338	390	572	8,300	9,500	10,970	24%
Hyundai, Genesis	3,714	46	195	3,955	4,300	4,400	56%
Kia	2,376	396	132	2,904	3,200	2,821	51%
Mercedes-Benz	2,131	201	118	2,450	2,131	2,385	124%
Stellantis	5,491	224	288	6,003	5,738	8,700	41%
Toyota	7,636	2,724	40	10,400	10,600	10,740	1%
Renault	1,531	320	200	2,051	2,200	3,750	9%
Nissan	2,585	800	15	3,400	3,800	4,930	
Ford	3,891	50	90	4,031	4,800	5,400	
BMW	1,962	207	171	2,340	2,500	2,520	115%
GM	3,540	0	39	3,579	3,850	7,700	54%
Great Wall	1,050	0	150	1,200	1,380	1,059	
Geely	1,760	0	240	2,000	2,100	1,362	
Sum	**45,005**	**5,358**	**2,250**	**52,613**	**56,099**	**66,737**	**53%**

Source: TI Fluid Systems



Source: S&P Global Mobility

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Used car prices and what they tell you…

According to the BLS, US used car prices continue to decline. However, Manheim data has shown increases in car prices over the last two months. The reason for the discrepancy is that Manheim only tracks auction and hence what dealers are paying for cars, whereas JD Power tracks vehicle book values that auto lenders rely on, and, finally, CarGurus tracks asking prices from dealers. Industry sources are hence saying that dealers were short of inventory, bought it expensively at auctions, but then had to sell it at a discount to customers[1]. Although the source is a Twitter account, it is a reliable source I have used for analysing the used car market successfully in the past. What this means to me is that car supply is too low and consumers are also not willing or able to spend more on cars. This is the dilemma that led me to exit TIFS. The regional banking crisis in the US does not seem to be fully contained and more failures will likely emerge. Worse, Credit Suisse appears to face a major bank run, and if outflows of Q4 2022 repeat themselves, Credit Suisse will be going bankrupt. In any case, CS won't be able to turn a profit with a debt load of over CHF 170bn, or 32% of their balance sheet size of Q4 2022. And OEMs won't hurry to jack up production when we face something like a 2008 scenario, as can be seen in above chart… Therefore, long-end UK government bonds appear like a better investment at this point to me.

[1] https://twitter.com/GuyDealership/status/1635627306830946304

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