

The Detroit News

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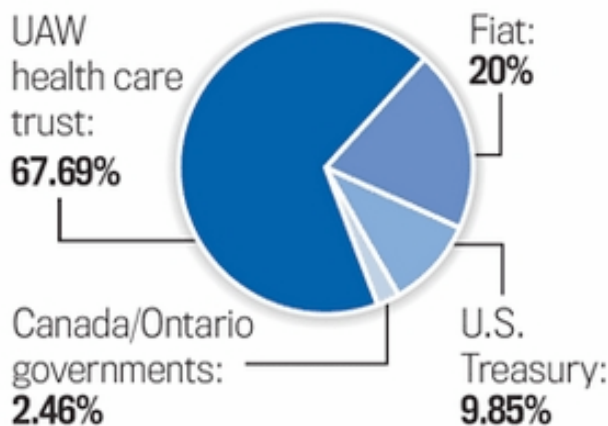
Saturday, June 20, 2009

Making sense of Fiat's noncash deal

Italian carmaker in charge of Chrysler only viable option, experts say

Alisa Priddle / The Detroit News

Who owns Chrysler



Sources: Chrysler, Detroit News research

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The arrangement is unusual: Minority shareholder Fiat SpA, having contributed no cash, is running the new Chrysler Group LLC and exerting clout far beyond what its 20 percent stake would suggest.

But in these unprecedented times, when governments are willing to finance but not manage an ailing automaker, and Fiat is willing to manage but not finance a troubled automaker, the auto industry's latest marriage is seen by many as an elegant solution to the ugly problem of salvaging Chrysler.

The whole deal -- an acquisition without cash, control with a minority stake, and the fact that it was brokered by government -- is unusual, said Mike Boudreau, a director with Bloomfield Hills turnaround firm O'Keefe & Associates. "But it was necessary to protect the industry."

It is a sign of just how desperate Chrysler's plight was that Fiat was able to swoop in with an empty wallet after a two-year search failed to find a global partner.

Without a financial suitor to replace Cerberus Capital Management LP, Chrysler would have collapsed in the wake of the biggest industry sales downturn in 40 years.

The Obama administration defends the terms as the best option on the bargaining table.

"Fiat is going to be in a strong position to help with the restructuring of Chrysler in ways that will be mutually advantageous, and so we think it's a desirable structure," said Larry Summers, President Barack Obama's chief economic adviser and co-chairman of the administration's auto task force. "At the same time, we're glad that there are a range of other stakeholders with ownership interests in the company."

With credit markets frozen and the auto industry on the verge of collapse, posing a threat to the broader economy, turnaround experts say the noncash deal was the only viable option.

'It does make sense'

"In this situation, it does make sense," said Van Conway, president of Conway MacKenzie Inc., a Birmingham management and restructuring firm.

Today, offering stock and options to lure new management with little investment is common in business. And in the private sector, the amount of money invested and shares held is not always proportional to management control.

The majority stakeholder in the new Chrysler Group is the voluntary employees' beneficiary association, a health care retiree trust run by the United Auto Workers.

The union from the outset said it did not want to be the majority shareholder -- it was essentially forced to accept equity in the VEBA in lieu of a cash contribution the bankrupt automaker could not afford -- and the union hopes to sell its shares as soon as possible. The union also has said it does not want to run General Motors Corp., where a similar VEBA will hold 17.5 percent of the automaker when it emerges from bankruptcy.

Chrysler Group LLC was created by combining certain assets of bankrupt Chrysler with Fiat, and the new company's ownership breaks down this way: the U.S. Treasury with 9.85 percent, Canadian and Ontario governments with 2.46 percent, the UAW's VEBA with 67.69 percent and Fiat with 20 percent.

Experts say it makes strategic sense for Chrysler to lean on Fiat at this time. "Fiat is the only shareholder that has automotive operating experience," Conway said. "Not only will they (Fiat) run it, they will add to it."

The Fiat deal is designed to allow the Italian automaker's stake to grow to 35 percent over the next two years if it meets certain conditions, such as building small engines and vehicles for Chrysler in the United States, and distributes Chrysler products abroad.

The original tie-up agreement called for Fiat to have a 35 percent stake from the beginning, but the task force dictated the new terms that now have Fiat's stake gradually increasing in 5 percent increments as it meets each condition.

Increasing Fiat's stake will reduce the governments' slice to 10 percent (8 percent for the U.S., 2 percent for Canada) and the VEBA will retain 55 percent.

The breakdown of Chrysler's nine-member board also does not fall in line with the equity. Fiat initially gets three appointments, including CEO Sergio Marchionne -- who doubles as chief executive at Chrysler -- the Treasury department appoints four, and Canada and the VEBA appoint one each. Once Fiat reaches 35 percent equity, it can appoint a fourth board member, and a Treasury appointee would step down.

Stake can increase

Upon repayment of \$6.6 billion in government loans keeping Chrysler afloat, Fiat can increase its stake to 51 percent between Jan. 1, 2013, and June 30, 2016.

The governance structure appeals to all parties.

For Fiat, the alliance dovetails with its global expansion goals but a lack of cash to execute it.

Fiat values the technology and engineering it is sharing with Chrysler at \$3 billion, said Alfredo Altavilla, head of business development. Chrysler will have access to small car, small engine and diesel technology -- all Fiat specialties. For Chrysler to duplicate the efforts from scratch would cost \$8 billion to \$10 billion, former Chrysler Vice Chairman Tom LaSorda said.

Chrysler also values the management services Fiat will provide, said spokeswoman Lori McTavish, noting Fiat was in the same financial straits five years ago that Chrysler is in now.

Marchionne is restructuring Chrysler along brand lines, similar to how Fiat is organized. But of the 23 people on Marchionne's Chrysler management team, only three are from Fiat. But the deal is not risk-free for Fiat, which has rebounded from steep financial losses in the late 1990s and early 2000s. With Chrysler under its belt, its liquidity, management and CEO will be strained.

For these reasons, Standard & Poor's Ratings Services said it is keeping Fiat on CreditWatch.

On a more positive note, "the new entity's structure is designed to be leaner, and the debt burden has been reduced," said credit analyst Barbara Castellano.