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Business breakup to better position Continental for megatrends

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A new trend is emerging as more companies consider separating business units with little overlap. It's good for shareholder value and it could be pivotal for survival in an increasingly competitive landscape, writes Megan Lampinen

Spin-offs, mergers and separate share listings could be on the cards for Continental as the supplier giant confirms it is considering a strategic overhaul. Speculation has been rife, forcing it to come forward earlier than it would have otherwise with a recognition that plans are underway: "We confirm that we are in the early stages of analysing how our organisation can become even more flexible in response to the fast changing environment in the automotive industry."

This restructure could take a number of different forms. Continental could break up the current businesses and then list shares of the more profitable operations separately. The company's Tire business, for instance, has had a much stronger operating margin than its Automotive Group units.

The analyst community in general has backed this move, and some have already been pushing for Continental to split up its business units. Berenberg analysts are particularly bullish on a separation of the Powertrain operations, noting: "The increased likelihood of Continental's problematic Powertrain business being separated or merged with a competitor would support a better outlook for the remaining parts of the business." For now, the supplier is only saying that its options remain "wide open."

Continental hosted a capital market day at CES 2018, at which it confirmed plans for a strategy review but declined to provide further details. Any split would require approval from the Schaeffler family, which own 46% of the company. So far, the family has declined to comment.

Josef Schuster, Founder of IPO research firm Ipox Schuster, suggests the company's statement indicates "it is actively planning and pursing strategies to respond to potential demands by activist shareholders to spin off certain units so as to increase shareholder value during a time when a 'window of opportunity' clearly exists in the industry." As he explained to *Automotive World*: "This would allow it to be more flexible to address the big challenges and opportunities set to impact the car industry over the next generation, brought about by the ascent of artificial intelligence, autonomous driving, electric vehicles, shared ownerships and alternative mobility."

Plenty of other automotive companies have taken similar steps to separate businesses that have grown in divergent directions or simply with little overlap. Schuster notes that these “almost always increased shareholder value” and may very likely be behind Continental’s decision. Daimler announced last year that it would transition to a holding company and create separate divisions for financing, cars and trucks by 2019. December marked the completion of Delphi’s separation into Delphi Technologies and Aptiv. The former groups together its powertrain activities while the latter encompasses all the projects around connected vehicles, smart vehicle architecture and new mobility solutions. At the same time, Autoliv has announced plans to spin off its Electronics business. It expects to launch a new, independent publicly traded company during the third quarter this year.

The trend shows no sign of stopping. “We expect OEMs and suppliers to increasingly reassess their business strategies and organisational structures to position themselves and to meet the heavy investment needs ahead for the transition to electrification and autonomous driving,” commented Vittoria Ferraris, Director, Sector Lead Automotive & Capital Goods, S&P Global Ratings. “We expect auto suppliers to surf the wave of the transition in the short term. However, in the long term we would expect a tougher competitive environment for auto suppliers linked to the lower complexity of electric cars and engines compared to combustion engines.”

Because of this, she added, the portfolio overhauls from the likes of Delphi and Autoliv come as no surprise. “We believe these moves are dictated by the expectation that there will be a first mover advantage for auto suppliers in a much tougher competitive market environment,” Ferraris told *Automotive World*