AUTOMAKERS

CHRYSLER AT A CROSSROADS

A buyout is all but inevitable. Here are three scenarios for possible sales, and how each one would play out

BY DAVID KILEY AND DAVID WELCH

FOR THE SECOND TIME in a decade, Chrysler is on the auction block. Even more amazing, despite nine years of woe under the ownership of Daimler-Benz, Chrysler has a line of potential buyers forming to kick its tires. Parties interested in the company or its parts range from General Motors Corp. to private equity groups and Asian automakers.

One possible outcome to a Chrysler sale would have been highly unlikely five years ago. Back then, GM controlled a comfortable 28% of the U.S. car market, and Chrysler 13%, so a merger would have drawn closer scrutiny in Washington. Today, though, GM is on the verge of losing its global car sales lead to Toyota, and Chrysler and Ford are fighting for their very survival, so anything seems possible.

At DaimlerChrysler's sprawling Stuttgart headquarters, the decision over how to proceed has split top management and board members into opposing camps: One backs a rapid sell-off of Chrysler Group, while the other favors first completing a restructuring effort into next year to bolster the selling price. A delay might reduce the final cost to Daimler of unloading Chrysler after subtracting its $22 billion in health-care liabilities. But the sell-it-now crowd appears to have the upper hand. "The chance that Daimler will sell Chrysler by fall of this year, before a new contract has to be negotiated with the unions, is probably 100%," says one senior Daimler-Chrysler official who asked not to be named.

Here are the most likely scenarios for buyers, and our estimates of the odds for each one happening:

GENERAL MOTORS

IT SEEMS LIKE a loopy idea, combining one flailing carmaker with another that is struggling to slim down. But this scenario has one big advantage—it would be the fastest way for DaimlerChrysler to be rid of Chrysler. If he decides to push the button on a deal, GM Chairman and CEO G. Richard Wagoner Jr. would be betting that for a negligible price he could add Chrysler's $62 billion in yearly revenue, or much of it, while cutting a big chunk of the structural costs. GM envisions selling close to 11.6 million vehicles per year worldwide through the combined company, but with a smaller staff of engineers, accountants, public-relations people, lawyers, and so on. GM accountants and strategists estimate they could save billions a year by merging the companies.

GM would need the cooperation of the United Auto Workers—and not just on reducing health-care costs. A deal could require the loss of 10,000 to 15,000 of the combined 125,000 production workers, so GM would need to arrange a buyout of some kind, says Sean P. McAlinden, chief economist at the Center for Automotive Research in Ann Arbor, Mich. The UAW has to figure that Chrysler jobs are going to be lost in any case, and workers would get the best security guarantees under GM.

Even if all the breaks go GM's way, though, it would be a messy slog. Put simply, buying Chrysler would double down on many of GM's existing problems. GM would pare the Chrysler lineup into one retail channel focusing on the best models: the Dodge Ram pickup and Charger sedan; the Jeep Wrangler, Grand Cherokee, Liberty, and Patriot; the Chrysler 300 and minivans. Even so, GM would be left with an unwieldy 11 brands to support in the U.S. with marketing and strategy.

Toyota Motor Corp., by way of contrast, has three. Says Goldman, Sachs & Co. analyst Robert Barry: "Buying Chrysler would add to GM's already bloated stable of brands and could complicate its current restructuring and global platform work, saddle it with more retiree liabilities, and create challenges in the dealer network."

A sale to GM may also be the costliest scenario for DaimlerChrysler Chairman Dieter Zetsche. Executives with knowledge of GM's position say it wants Chrysler for virtually nothing. It could cost $8 billion just to cut Chrysler down to size. And the company itself may only be worth $5 billion, according to Bane of America Securities analyst Ron Tadross.

PRIVATE EQUITY

VIRTUALLY EVERY MAJOR buyout firm, including Blackstone Group and Clayton, Dubilier & Rice (which bought Hertz from Ford Motor last year), is looking at Chrysler's books, according to one leading investment banker who regularly works with auto companies. And private equity investors in Germany have been buzzing since 2005 about the chances of bidding for control of parent DaimlerChrysler. The allure? Investors figure they could break up the company and unlock big gains from Mercedes' luxury car and commercial truck units. Analysts estimated then that the Daimler parts were undervalued by as much as $40 billion when DCX snares traded at about 40.

The stock price has since risen to 75 a share, but raiders still see DCX as undervalued. "You dump Chrysler, spin off the truck business, and get Mercedes for free," says a German executive privy to the conversations. Michael Raab, an analyst at private bank Sal. Oppenheim, pegs OCX's breakup value at 98 a share. Of course, if GM walks away from the table, OCX's share price may tumble, making a deal even more attractive for private equity.

Private equity firms see substantial breakup value in Chrysler alone. The Jeep brand plus its factories could bring $5 billion to $7 billion. At least a few of Chrysler's plants would be of interest to Hyundai Motor, Chinese automakers, Renault-Nissan, India's Tata Motors, and possibly Volkswagen. DaimlerChrysler Financial Services, almost a forgotten asset, earned about $2 billion last year. The wild card? A private buyer would have to negotiate UAW worker buyouts and figure out who pays for it.

ASIAN AND EUROPEAN CAR COMPANIES

RENAULT-NISSAN Chief Financial Officer Thierry Moulonguet has told institutional investors that

the company won't seek to buy Chrysler or strike an alliance. But that doesn't mean the French-Japanese automaker wouldn't look at the same individual assets as private equity outfits, says one high-ranking Nissan executive.

Although Jeep has suffered from the industrywide downturn in SUV sales, it remains a strong, iconic brand with worldwide appeal, especially in regions like South America, the Middle East, and China. "In those markets, Jeep is like a luxury brand that says 'I have arrived,'" says Jesse Toprak, executive director of industry analysis at Edmunds.com Inc.

Still, Asian companies seem like a long shot to buy all of Chrysler. A Daimler executive and a banker close to the company confirm that Hyundai has also lined up to examine Chrysler's books, despite official denials from the Korean automaker. Hyundai is hungry to double North American sales, to 1 million vehicles by 2010. But several observers see a culture clash between Hyundai's often imperious, top-down management style and independence-minded Chrysler managers. "On paper it makes some sense, but these kinds of deals are not executed on paper. It comes down to people making them work," says Gerald C. Meyers, professor at the University of Michigan Business School.

Could a Chinese automaker snap up Chrysler? That would accelerate Chinese expansion plans by a full decade. Up to now, the Chinese have had to live with limited joint venture agreements, like one just inked by Chrysler and Chery to produce small cars for Chrysler worldwide. But Chinese companies probably still don't have the financial or political savvy to nail such a huge U.S. deal. II

-With Gail Edmondson in Frankfurt

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