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Fiat still targeting VEBA agreement as Chrysler IPO parade kicks off

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Fiat [F IM] is still targeting an agreement with the United Auto Workers union over its Chrysler stake despite preparations for an IPO of Chrysler gathering pace, sources familiar with the situation told dealReporter.

A first source familiar said that an informal beauty parade to get the mandate for an IPO involving 10 major banks has just taken place. Goldman Sachs, Morgan Stanley, Citi, Bank of America Merrill Lynch, JPMorgan, UBS, Societe Generale, BNP Paribas and Banca IMI were said to be among those competing. According to a second source, November has been pencilled in for execution of the IPO.

Despite these preparations, the sources said that there remains a good chance that the IPO will not take place. "Fiat will not necessarily do the IPO, in fact it wants to avoid it, but it has the obligation to support VEBA if it wants to do it," the second source said.

The Voluntary Employee Beneficiary Association (VEBA) trust, set up to pay the medical costs of Chrysler's union-member retirees, holds a 41.5% stake in Chrysler. The trust has the right to ask Chrysler to initiate proceedings for an IPO as part of a 2009 agreement.

Under the agreement between Fiat and VEBA, the Italian car maker holds options to buy tranches of 3.3% of Chrysler every six months from VEBA. But the question under legal scrutiny is at what price. Fiat reportedly filed a valuation for the whole of Chrysler of USD 4.2bn, while VEBA has claimed it is worth USD 10.3bn.

"The listing presents a problem for Fiat, because to merge Fiat and Chrysler, as it hopes to do, it has to buy out the Chrysler minorities," he said. He explained that this would create a situation similar to that with CNH Global [CNH US], where Fiat had to pay a very significant premium.

Whether Fiat gets its preferred outcome largely hinges on the ongoing court case in Delaware, the second source said. The court is to decide what constitutes a fair price for Fiat to pay VEBA for its stake in Chrysler.

The main issue is over the definition of a loan within Chrysler, which VEBA defines as equity and Fiat defines as debt, the second source said. "A lot will depend on how the Delaware court sets the price and how the two parties move forward on that," noted this source. The court is expected to make its ruling at the end of this month, he added.

Even if Fiat does reach an agreement with VEBA, a successful complete takeover cannot be guaranteed, as Fiat would have to put significant financing in place to acquire the outstanding shares, the sources said. It does have feasible options in this area, the sources explained.

The first source said that banks have indicated availability of a bridge loan to Fiat, but it wasn't clear how the bridge would be repaid.

"There is the ongoing debate about whether Fiat needs to raise equity," said a third source. "They could do it conventionally or they could do it by offering Chrysler shareholders Fiat shares, but this would dilute the Agnelli's [stake] either way, so [the Agnelli family] may have an issue with that," he added.

The first source also noted that the Agnelli family, which holds a 30% stake in Fiat through Exor, is reluctant to have its position reduced.

A second option is an asset sale, with Ferrari a possible candidate, noted the third source. This may not be workable as it would be hard to do that quickly enough if the situation comes to a head within a couple of months, he added. Ferrari, 90% owned by Fiat, posted EUR 2.4bn in revenues and net profit of EUR 244m in 2012.

The third option is new debt, which, while the company is not ideally placed to pursue it, would be achievable, the sources said. "It seems like a stretch at first look but when you consider Marchionne [joint CEO of Fiat and Chrysler] is a such a wily negotiator and a lot of banks want to keep in with him for the future, it's very feasible," said the third source.

Even with the banks' support, additional leverage could put Fiat in the crosshairs of the rating agencies, said the second source. Moody's is rating Fiat at Ba3 with negative outlook, while S&P has it at BB- with stable outlook.

The bridge loan could also be paid back with Chrysler cash post merger, he added, but at present this Chrysler cash is locked up due to covenants on loans, so these would need to be restructured to free up the cash, he added.

At 31 December 2012, Fiat's net industrial debt increased by approximately EUR 1bn to EUR 6.55bn. For Fiat, excluding Chrysler, net industrial debt increased by EUR 2.6bn, mainly as a result of the negative cash flow of EUR 2.5bn.

Fiat's total cash and cash equivalents were EUR 8.85bn, while Chrysler reported a similar figure of EUR 8.8bn.

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