

EDITORIAL – Johnson Controls auto business sell-off announcement shows an industry focusing on core competencies

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Concerns of increasing capital costs of R&D see suppliers going back to familiar territory

This last week, Johnson Controls (JCI) announced that it was exploring strategic options for the sell-off of its automotive business. In a statement, Alex Molinari, chairman and CEO, said, "Today's announcement continues our strategy of proactive portfolio management to drive focus on strategic product-oriented businesses where we can be a global market leader, drive more profitable growth and deliver maximum long-term value for our customers and shareholders."



Molinari believes selling the autos business will generate capital for needed to develop new products. The company is exploring a range of options for the business, including selling the business in pieces, spinning off the business into a separate company, selling majority stake as a joint venture, or divesting the business as a whole.

JCI has been steadily reducing its exposure to the auto industry over the last couple of years. In April, JCI reported net income had more than doubled year over year in the second quarter of 2015, though automotive revenue was down. Although, even if the company completely divested its "automotive" business, it would still make car batteries under its "power solutions" business.

In May, it sold its 50% equity stake in Johnson Controls Pricol Pvt Ltd, – which manufactures instrument clusters, displays, and body electronics – to joint-venture (JV) partner Pricol. In February of last year it sold its headliner and sun-visor business to private equity firm Atlas Holdings, and in January of 2014, it sold its automotive electronics business to Visteon for USD265m.

The exit from automotive would be the culmination of a dramatic change of direction for the company. Just five years ago, Johnson Controls was involved in an aggressive takeover attempt of Visteon's interiors and electronics business, offering USD1.25bn for the combined units. Now both have diversified away from the struggling interiors part of the business.

The move continues a trend across the automotive industry to sell off businesses that are either underperforming, or that don't represent part of a core product portfolio for the company. News of the potential sell-off comes in the same week that Bosch announced that it was considering a sell off or joint-venture partner for its Starter Motors and Generators business. The division supplies fuel saving technologies including start-stop system, advanced generators and motors which have strong growth potential given increasingly stringent regulations in fuel economy. Bosch believes this move will help the division improve its competitiveness and growth prospects

As part of a long restructuring, Delphi has shifted from an extremely broad supplier to a much more focused one since being spun off from GM and going through a long bankruptcy. In the last year, Visteon has spun-off its stake in Halla Visteon Climate Control and its interiors business in India.

In an industry that has traditionally been very horizontally integrated, certain suppliers are becoming more focused on its core businesses. Delphi's sale of its thermal unit to MAHLE in February was part of a strategy that focuses on higher margin technology products supporting fuel efficiency, infotainment systems and autonomous driving, as a way of creating a strategic advantage. The company has slimmed down its business lines from over 100 products to just 33, looking at each product and making a decision whether to continue or close the business based on performance.

Lack of willingness to provide the capital

Molinari also told *Automotive News* that reasons for the potential sell-off include the cyclical nature of the auto industry, as well as the seating division being in need of a significant capital investment.

This comment will raise alarm bells amongst industry watchers, as the trend of OEMs offloading research and development responsibilities onto suppliers increases. Because of this trend, the size of R&D budgets for the suppliers has been expanding to around 5% of sales over the last few years. In addition, the complexity of technologies that suppliers are having to develop and interact with has risen, with increased electrification requirements and greater semiconductor content in new vehicles. In its announcement, Bosch also cited tough competition and cost pressure as key reasons for exploring options for the division. For some, it may be a sign that the traditionally cyclical automotive industry could be again close to reaching another peak.

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