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EDITORIAL – Nissan's sale of stake in Calsonic Kansei presents new challenges for the supplier

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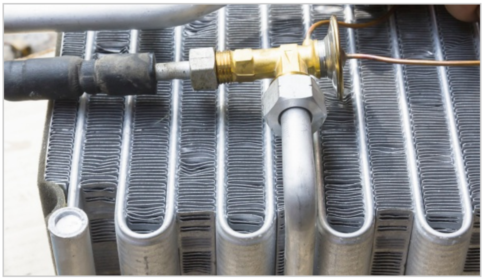
The Japanese supplier needs to reduce its dependence on Nissan, improve cost competitiveness and expand product offering to drive growth



Last week, US-based private equity firm KKR reached an agreement with Nissan Motor to acquire the latter's stake in Calsonic Kansei, in a deal that values the Japanese supplier at JPY498.3 billion (USD4.5 billion). Under the agreement, KKR will pay Calsonic Kansei's shareholder JPY1,860 (USD16.78) a share, a 28.3% premium over the stock's closing price on Tuesday (22 November). Nissan will receive around JPY206.9 billion (USD1.87 billion) for its 41% stake in Calsonic Kansei. To acquire the remaining outstanding shares, KKR will come with a tender offer in February 2017.

Reports that Nissan was considering selling its stake in Calsonic Kansei first surfaced in June this year. At the time, it was reported that Nissan was looking to sell its stake in the supplier to raise additional fund to bolster its research and development (R&D) activities in areas such as next-generation electric cars and autonomous driving. Nissan also needed additional funds to make a strategic investment in Mitsubishi Motors. Under an agreement reached between the two automakers, Nissan agreed to invest USD2.3 billion for a 34% stake in Mitsubishi Motors. The deal was finalised last month.

Renault-Nissan can pursue cost synergy more vigorously

The Japanese automaker had raised its stake in Calsonic Kansei from 28% to 41% in January 2015. In over a decade of association, which saw Calsonic Kansei becoming a subsidiary of Nissan Motor, the Japanese supplier has become more dependent on Nissan. Calsonic Kansei currently generates over four-fifths of its revenue from Nissan. The auto parts supplier's operations have become highly intertwined with Nissan's and in some cases the company has installed its own production lines as sublines inside the automaker plants to ensure just-in-time delivery.

Nissan conducts all its components and materials sourcing with Renault through a dedicated organization, the Renault Nissan Purchasing Organization (RNPO). The joint procurement of components and materials has played a vital role in increasing synergies between the two companies in recent years. The strategic alliance saw savings of EUR4.3 billion through the program in 2015, up 13% y/y. Renault-Nissan has set a goal to generate at least EUR5.5 billion in new synergies in 2018 through further streamlining of purchasing, engineering and manufacturing.

To realise this, RNPO is set to pursue cost savings through joint procurement more vigorously. The alliance partners are open to new suppliers if they can offer better products at a vmore competitive price. In recent years, the joint procurement helped Calsonic Kansei win orders from Nissan's strategic partner Renault as well. However, Calsonic Kansei's senior executives have recently admitted that securing new contracts from Renault-Nissan has become fiercely competitive despite being part of the Japanese automaker's group.

When Calsonic Kansei was Nissan's group company, the Japanese automaker was obliged to source components from the supplier. However, with the sales of its stake in Calsonic Kansei, the company will now be able to open the contracts previously fulfilled by Calsonic Kansei across the wider supplier base. According to Julian Buckley, Senior Analyst on OEM Sourcing at IHS Markit, this will benefit Nissan, as the tendering process should contribute to reduced landed part prices while opening up access to suppliers with different, and potentially better, technological solutions. Future supplier selection for those parts previously delivered by Calsonic Kansei could also be influenced by new suppliers' footprint, as a broader reach would better support part sharing across a global vehicle portfolio, while also reducing associated logistics costs.

Needs to diversify customer base, more aggressively than ever

Last year, Calsonic Kansei set a modest target to reduce its dependence on Nissan to 70% by the end of the current financial year, from over 80% in the previous fiscal year. In the past, Calsonic Kansei's association and dependence on Nissan might have been a hindrance in securing business from rival automakers. Under new ownership, Calsonic Kansei will need to pursue its diversification strategy more aggressively.

However, this is easier said than done. According to Buckley, as a preferred supplier to Nissan, it was possible that Calsonic Kansei's internal costs were not controlled as much as at other independent companies and these will have to be scrutinized to reduce unnecessary expenditure. This is also reflected in a relatively low operating margin, which has hovered between 3-4% in the past three financial years, compared with 7-10% in the case of Denso and 5-6% for Aisin Seiki, the two leading automotive suppliers from Japan.

As an independent company under KKR, Calsonic Kansei will have more control over what parts it looks to develop and supply in the future, leveraging existing expertise to launch new, improved products comparable to or better than those equivalents delivered by competing suppliers. In order to reduce dependence on Nissan, Calsonic Kansei will need to forge new partnerships across the wider auto industry. This will require the company to be an attractive alternative in all areas, such as cost, quality and delivery.

Under KKR, Calsonic Kansei will seek to become a global supplier that could compete with global peers such as Bosch, Continental and Denso. The company intends to use some funds generated from the sale of its own shares to acquire companies that broaden its portfolio. Calsonic Kansei holds a 41% stake in Tokyo Radiator Manufacturing, a major thermal system supplier. The company's new owner may acquire the remaining outstanding shares of Tokyo Radiator as well and consolidate the business with Calsonic Kansei.

However, there remains one apprehension of having a PE firm as an owner. Such firms are often not seen as long-term investors and are known to sell acquired business to make profit, sometimes piecemeal. Calsonic Kansei has a portfolio that offers an attractive break-up opportunity.

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