



Deal Logic WABCO / ZF

WHU Finance Society

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Abstract

Anticipating future developments is not only a key task of every successful management team but also one of the most challenging ones. Sometimes, the pace of the markets towards a specific development can surpass the capable speed of change within a firm. In this case, acquisitions are a good option to not fall behind new or more agile competitors.

The electrification of the automotive industry calls for new, innovative parts beyond the combustion engine. Due to the Original Equipment Manufacturers (OEMs) low Real Net Output Ratio, the automotive suppliers will be required to do most of the anticipation. ZF Friedrichshafen AG (ZF) is betting on breaks to be vital demand driver of the future, with their acquisition of WABCO Holdings Inc. (WABCO).

It is not the first time that the global automotive supplier ZF has tried to enter the business of brake solutions. A failed attempt to acquire the Swedish firm Halex in 2016 was followed by an attempt to take over the firm at stake, WABCO. The negotiations, about two years ago, ended abruptly after the board decided against the transaction. The reasoning presented by the board was based on financial risk.

A year before the first talks with American-Belgian WABCO, ZF acquired the US-American TRW group for approximately EUR 10bn and the board inferred that another acquisition for only EUR 3bn less would be a substantial risk to the financing of future operations. This was the official statement, but insiders also indicated that the board chairmen, Andreas Brand, the mayor of the city of ZF's headquarters, Friedrichshafen, and former CEO of ZF, Stefan Sommer, did not have a very fruitful relationship. The bad blood between the two apparently led to decisions by the board, which were not healthy for the firm, according to experts.

The reason why the mayor of Friedrichshafen has so much weight in the decision process of ZF is due to the ownership structure of the firm. The mayor represents the Zeppelin Foundation, which owns about 93.8% of ZF shares. Foundations are a particularity to the German landscape of legal entities. They are institutions, which with the help of assets, pursue a purpose defined by the founder. In the case of the Zeppelin Foundation, the purpose was defined as the alignment of the firm's actions with the interests of the city of Friedrichshafen.

The new CEO, Wolf-Henning Scheider, is said to be more diplomatic with the board. Another reason why the current acquisition is under better preconditions boils down to the fact that ZF has massively

decreased their debt position over the last few years. This change in capital structure surely disarmed the concerns raised in the past.

From a business perspective, the acquisition of WABCO by ZF, which is expected to be completed in 2020, makes sense for two main reasons. First, the electrification of the automotive industry raises the need for a different business focus of suppliers. ZF is, among other segments, currently one of the world's biggest transmission producers. If one would expect a full shift towards electric vehicles (EVs), this business segment would become completely redundant, as the production of an EV does not require a transmission as a combustion engine would. Brakes, on the other hand, will become more important in the future, as they will be able to supply electricity from brake friction, which in turn can be used to charge the cars' battery. An efficient brake can therefore dramatically increase the range of an EV, which today is one of the major considerations for consumer to decide whether to purchase an EV. Especially in the high load segment of the commercial vehicle business, brakes will become critical. With Tesla's Semi, the firm's full electric truck, a shift of the market towards this development can be seen. WABCO, with its core business activity in the production of braking systems, is therefore a good add-on to ZF's portfolio. Second, it is the rising importance of size in the supplier business. OEMs are increasingly engaging with component or full solution providers rather than suppliers of individual parts. A supplier being able to provide a more diversified product portfolio and a more integrated value chain will have a competitive advantage. The acquisition of WABCO would boost ZF's revenue to more than EUR 40bn, making it the world's third largest automotive supplier after Continental and Bosch – quickly surpassing its Japanese competitor Denso.



All values in EURm, except Price, Initial (EUR) & Price, Paid (EUR)

Summary

Target	WABCO Holdings Inc.
Acquirer	ZF Friedrichshafen AG
Date, Announ.	28.03.2019
Date, Effective	Pending
Deal Attitude	Friendly
Consideration	100% Cash
%Held/%Acq.	0 / 100
Deal Value	6223.4
Price, Initial	121.37
Price, Paid	121.37
Total Fees	41.7
Premium*, 1d	13.0
Premium*, 1w	15.9
Premium*, 4w	20.4

* Pre-bid (%)

Sources: Thompson Reuters Eikon

Synopsis

- ZF Group, a unit of Zeppelin-Stiftung GmbH, agreed to merge with WABCO Holdings Inc., an Auburn Hills-based manufacturer and wholesaler of vehicle electromechanical products, for a total value of EUR 6.2bn (or EUR 121.37 per share in cash)
- The transaction brings together two leaders with highly complementary and innovative technology offerings to address future demand for advanced mobility in the area of commercial vehicles
- This all-cash transaction at a premium has been approved by the Boards of both companies and is expected to close in early 2020

LTM Transaction Multiples

	Target	Acquirer	Industry†
EV/Sales	1.9x		1.0x
EV/EBITDA	11.0x		8.3x
EV/EBIT	14.2x	**n/a	11.2x
EV/FCFF	17.3x		28.3x
P/E	16.7x		15.9x

**data not available for private companies

† Of Target, Auto, truck and motorcycle parts (SIC: 3714)

Rationale

- The main purpose of the transaction was for ZF Friedrichshafen AG and WABCO Holdings Inc. to diversify their product portfolio
- Especially the focus on brake solutions of WABCO Holdings Inc. enables a market access for ZF Friedrichshafen AG into a field highly relevant in the production of electric vehicles
- In addition to this, the aim of the transaction is to strengthen their operations, to increase shareholder value, and to expand presence in new and foreign markets

Financial Advisors

Target	Fees	Acquirer	Fees
Goldman Sachs & Co	23.3	JP Morgan	15.9
		Lazard	2.5

All values in EURbn, except EPS

Recent News*

- **2019/03** WABCO signs USD 180m agreement with Global Manufacturer to supply power steering gears
- **2019/02** WABCO is setting up its future global headquarters in the canton of Bern
- **2018/12** WABCO Board of Directors authorizes new share buyback program up to USD 600m
- **2018/09** WABCO will introduce the prototype of its first electric trailer. The model has an intelligent electric motor control to recover electrical energy when braking
- **2018/08** WABCO opens Global Technology and Innovation Center in Hannover, Germany

* Prior To Deal
Sources: Thompson Reuters Eikon, WABCO

Company Description

- WABCO, founded in 1869 and based in Brussels, Belgium, is a supplier of electronic, mechanical, electro-mechanical, and aerodynamic products for various manufacturers of commercial trucks, buses and trailers as well as passenger cars
- The company engineers, develops, manufactures, and sells braking, stability, suspension, and transmission automation as well as other conventional mechanical products
- As of end of 2018, WABCO employed more than 11,000 people in 34 countries worldwide and operated under five segments – truck and bus, aftermarket, trailer, car, and off-highway products

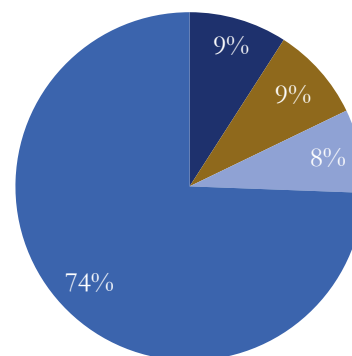
Key Management & Ownership Structure



Jacques Esculier
CEO
Since 2007



Sean Deason
CFO
Since 2019



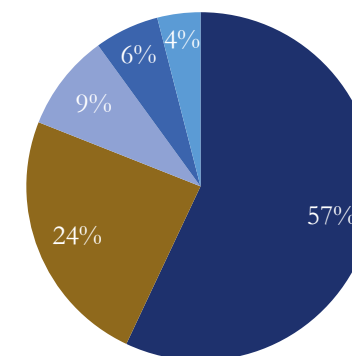
■ EdgePoint Investment Group
■ The Vanguard Group
■ FPR Partners
■ Freefloat

Key Financials

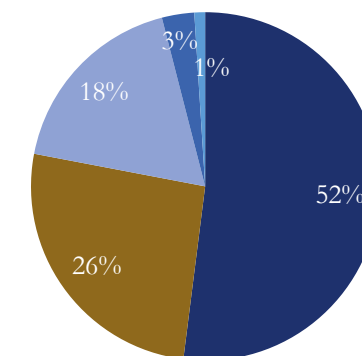
	2016A	2017A	2018R	2019F	2020F
Sales	2.5	2.9	3.3	3.4	3.4
% growth	6.9	17.6	15.9	1.7	1.1
EBIT	0.4	0.4	0.5	4.6	4.7
% margin	13.6	13.2	13.2	13.0	13.2
Net Inc.	0.2	0.4	0.4	0.4	0.4
% margin	7.8	18.2	10.4	9.9	10.1
EPS	5.2	11.6	7.9	7.9	8.3

Sales Split

FY2018



■ Truck & Bus Products
■ Aftermarket
■ Trailer Products
■ Car Products
■ Off Highway Products



■ Europe
■ Asia
■ North America
■ South America
■ Other

All values in EURbn, except EPS

Recent News*

- **2019/03** Automotive supplier ZF contradicts VW when it comes to electro mobility as the sole engine of the future
- **2019/03** The automotive supplier ZF Friedrichshafen has to pay around EUR 190m to the EU Commission as penalty for illegal price fixing of the ZF subsidiary TRW
- **2019/01** Ego Mobile and ZF launch mass production of people mover for urban mobility needs
- **2018/12** Over the next four years, the ZF Group will invest EUR 800m in the Saarland site to further develop its hybrid drive

* Prior To Deal
Sources: Thompson Reuters Eikon, ZF

Company Description

- ZF Group, originally known as Zahnradfabrik Friedrichshafen, is a German car parts manufacturer
- Founded in 1915, it is headquartered in Friedrichshafen, Germany
- The company produces transmissions, steering systems, axles and chassis components as well as complete systems for passenger cars and buses, trucks, commercial vehicles and other military and agricultural machines
- As of end of 2018, ZF had 230 production locations in 40 countries with approximately 146,000 employees, operating under three main segments: cars & commercial vehicles < 6t, commercial vehicles > 6t, and construction & agricultural machinery

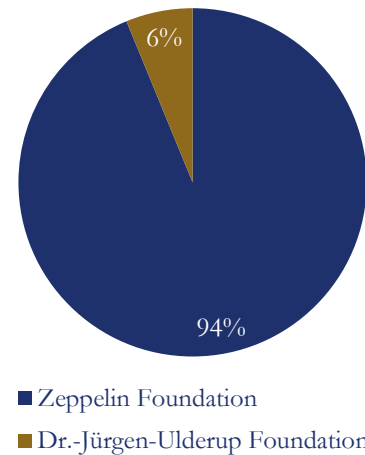
Key Management & Ownership Structure



Wolf-Henning Scheider
CEO
Since 2018



Dr. Konstantin Sauer
CFO
Since 2010



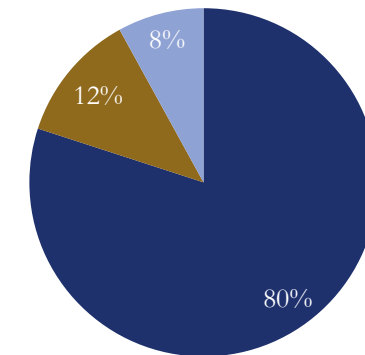
Key Financials

	2016A	2017A	2018E	2019F	2020F
Sales	35.2	36.4	36.9		
% growth	20.8	3.4	1.4		
EBIT	1.6	1.7	1.5		
% margin	4.5	4.7	4.1	**n/a	
Net Inc.	0.9	1.1	1.0		
% margin	2.6	3.0	2.7		
EPS			**n/a		

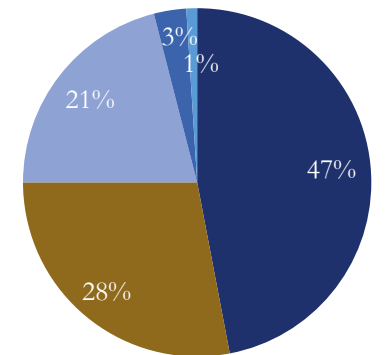
**data not available for private companies

Sales Split

FY2018



- Cars & commercial vehicles < 6t
- Commercial vehicles > 6t
- Construction & agricultural machinery



- Europe
- North America
- Asia-Pacific
- Africa
- South America

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