



3 Reasons Bombardier Inc. Will Sell its Rail Business by the End of 2017

Description

Bombardier Inc. ([TSX:BBD.B](#)) is the world's only maker of trains and planes, and this is a source of pride for the company. But this may not be the case for long. Bombardier is planning an initial public offering (IPO) of a minority stake in its rail business, which will likely happen in Germany.

The IPO will help "crystallize the full value of Bombardier Transportation," making it easier to sell the whole thing down the road. In fact I would expect Bombardier to sell the whole unit by no later than the end of next year. Below are three reasons why.

1. Bombardier needs the money

Of course, this is the biggest reason why Bombardier will sell its rail business. The company's financial position has gone from bad to worse, mainly because of development costs with the C Series. Total debt now stands at roughly US\$9 billion, an extraordinarily large amount for a company of Bombardier's size.

Making matters worse, the company has burned through more than US\$1.5 billion in the first six months of this year, and has only US\$3.1 billion in cash left. The rating agencies have taken notice. In early August Moody's downgraded Bombardier's debt to B2. Then a week later, both S&P and Fitch downgraded the company's debt to B. All three rate the company's debt below investment grade.

But a sale of the rail business could fetch US\$5 billion, allowing the company to pay down most of its debt. Clearly such a step is needed.

2. There is no synergy between trains and planes

There's a reason why Bombardier is the world's only maker of planes and trains: there are practically no benefits that come from combining these two businesses. Bombardier's two businesses don't share the same technology, nor the same customers, nor the same employees (except senior management). They're even located in different parts of the world.

The company may respond that its rail business helps diversify revenue, something that's badly

needed in the volatile aerospace industry. But that's a flimsy argument at best; investors can easily diversify their portfolios by buying a basket of stocks themselves.

3. Bombardier Transportation has been mismanaged

The rail business has underperformed for years. One can even go back to 2004, when Bombardier announced 6,600 layoffs in its rail business, along with US\$777 million in restructuring charges. Furthermore, low margins at Bombardier Transportation have disappointed investors for many years.

There's a good possibility that this business can improve if it has a dedicated management team, one that doesn't have to worry about an aerospace division as well. That could mean Bombardier will get a good price once it divests BT.

In any case, this marriage simply hasn't worked out, and it's time for a split. New CEO Alain Bellemare has only been on the job for six months, so you shouldn't expect this immediately. But he almost certainly knows what needs to be done. It's only a matter of time before this happens.

CATEGORY

1. Investing

TICKERS GLOBAL

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