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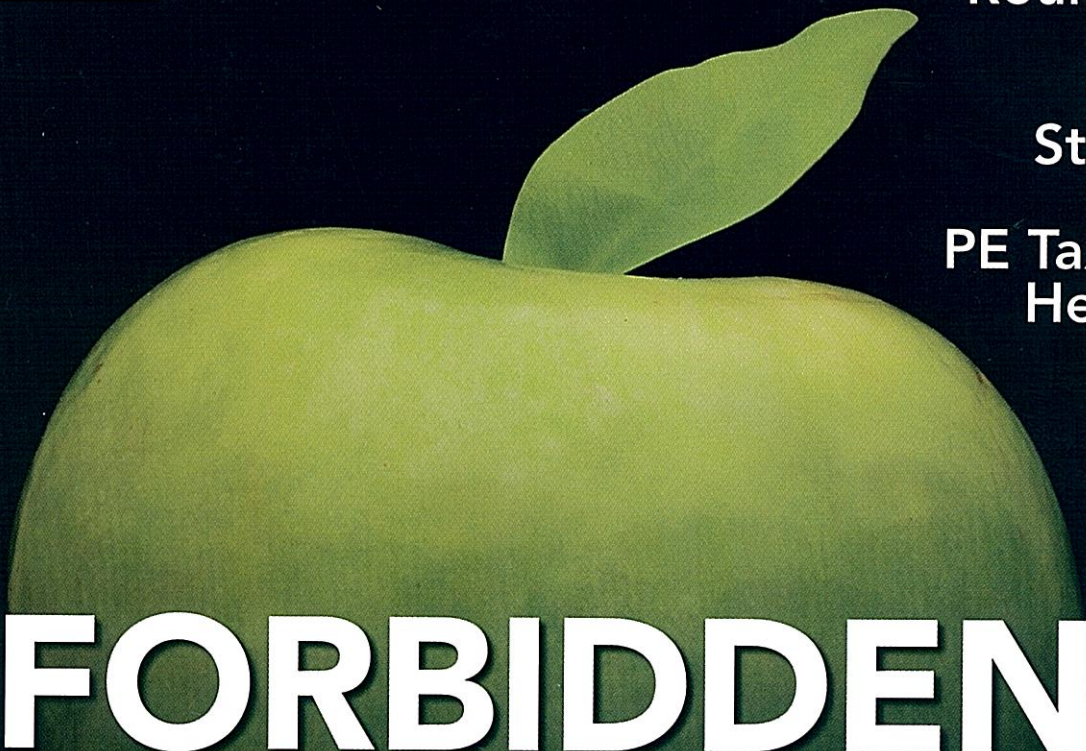
Association for Corporate Growth

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Hedge Fund
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Cash is
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Heats Up



FORBIDDEN FRUIT

Insider trading is back, and even
smaller deals are vulnerable

Spinoffs: The Next Best Alternative

As the credit squeeze has put some deals into question, some companies are seeking another option

By Joan Harrison

“ Nearly two-thirds of respondents anticipate healthy levels of spinoffs in their sectors over the next year. ”

It wasn't long ago when investors valued diversified companies — the thought process being that multiple lines of businesses would help parent company ride out economic ups and downs. But as the economy again could be susceptible, such mosaic strategies now seem like an anachronism. In the recent past, companies have maintained a desire to streamline their operations by shedding their underperforming assets, and looking ahead, many pros anticipate that spinoffs will only continue to gather steam.

Take the case of **3Com's** \$430 million acquisition of **TippingPoint**. Just roughly three years after the purchase, 3Com announced plans at the end of June to spinoff the company through an IPO. And the rationale behind the move? 3Com's CEO **Edgar Masri** cited that it would allow both entities to “focus on their core strengths, target markets and strategic goals.”

Another recent example came when **Altria**, at the end of August, said it would spinoff **Philip Morris International**, which closely follows a similar move in March, when the company cut ties with **Kraft Foods**.

When it comes to spinoffs, the explanation given from 3Com's Masri has become the cliché, although one that may be perfectly appropriate.

Many CEOs and corporate development officers, in fact, anticipate a slew of spinoffs over the next 12 months, according to research commissioned by law firm **Allen & Overy**. The FT Research Centre, the *Financial Times'* on-demand research service, conducted the study.

The survey, which polled senior executives at Fortune 500 and FTSE 350 companies, revealed that nearly two-thirds of respondents anticipate healthy levels of spinoffs in their sectors over the next year or so, and 87% of those surveyed pegged pressure from activist and private equity investors as a key driver of much of the activity.

Spinoffs, or demergers, typically follow an intense period of dealmaking action. Now as the latest M&A boom appears to slowing down, more companies may eye spinoffs as a means of boosting shareholder value.

Media, telecommunications, consumer services,

energy, pharmaceuticals, biotechnology and financial services will be among the fertile spinoff markets, notes **Michael Gilligan**, a partner in the New York corporate/M&A group of **Allen & Overy**. In fact, any industry that has grown rapidly in recent years will be ripe for brisk spinoff activity, he adds.

According to Gilligan, respondents expected the highest levels of spinoffs to occur in the United States, given the country's robust private equity market and stepped-up shareholder activism, although demerger levels also will be significant in Asia and Europe, he notes.

Waning acquisition activity resulting from uncertainties in the credit markets could also propel spinoffs over the next year, notes **Steve Goodman**, a New York-based partner at law firm **Pryor Cashman**, who specializes in the acquisition and sale of intellectual property and technology assets.

Steven Bernard, director of M&A analysis at **Robert W. Baird**, agrees with Goodman but notes, “If you had asked me about spinoffs three to six months ago, I would have anticipated a bit more activity than I do now.”

He explains that the debt markets are currently impacting the large end of the market, which will trickle down and result in lower valuations for all deals due to market volatility and tighter financing. “So, some companies might decide to hold off and wait until prices rise,” Bernard says. “It will depend on the aim of the [seller].”

But with the market in upheaval, spinoff opportunities could abound. In mid-August, for example, energy holding company **TXU Corp.** stated in a regulatory filing that if its acquisition by **Kohlberg Kravis Roberts** and **Texas Pacific Group** falls through, it probably would split itself into three separate entities.

Meanwhile, the credit squeeze has also forced **Cadbury Schweppes** to ditch plans for the sale of its U.S. soft drinks business. The confectionery and beverage maker instead announced in mid-August that it's moving ahead with a spinoff of the unit instead of a sale. **MA**