Global corporate divestment study

Maximizing divestment success in an uncertain economy

The COO perspective

EY

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The COO perspective — at a glance

Your time is precious. In order to get you the insights you need, as quickly as possible, we designed *The COO perspective* — a series of short executive briefing papers that provide a quick overview of the main findings of recent EY reports, with a particular emphasis on the relevance for you.

The role of the COO is hugely diverse, changing markedly from one company to another and across varying industries. Accordingly, in compiling *The COO perspective*, we've sought to highlight insights of relevance to one or more of the six fundamental components of the COO role, as illustrated by our wheel model that we believe collectively encompasses the full extent and potential of the COO role.

In a global marketplace for M&A, this *COO perspective* will resonate particularly with COOs of multinational businesses, but its lessons apply more widely too.

What is *Global corporate divestment study: maximizing divestment success in an uncertain economy* about?

In a sentence: many companies plan to accelerate the pace of divestments over the next two years, but nearly three-quarters of them are leaving value on the table — such missed opportunities are no longer an option.

EY's *Global corporate divestment study* analyzes current levels of divestment activity and surveys the outlook for the next two to three years — a period in which the rate of divestments is widely expected to increase.

The *Global corporate divestment study* is based on a survey of 567 corporate executives of companies representing more than 14 industry sectors. Respondents stated that they have direct knowledge of, or hands-on experience with, their company's divestment activity.

Empirical evidence from the study shows that companies that take the appropriate steps are achieving greater value and making speedier disposals. The report[1] identifies five leading practices that companies should employ in order to avoid leaving money on the table, and to help achieve a successful divestment.

Given COOs have a unique insight into their business and are closest to the day-to-day operations, they are invariably at the center of the five leading practices, which range from structured and regular portfolio review to separation planning. COOs are often found working closely with their CFOs and business development leads to ensure optimal returns on divestments are achieved.

[1] *Global corporate divestment study: maximizing divestment success in an uncertain economy*, EY, 2013.

How high performers approach divestments: five leading practices

While the appetite for divestments may be growing, the conditions for completing transactions remain challenging: boards, regulators and shareholders want assurance that the strategic and value creation objectives from divestments will be achieved; buyers, meanwhile, are scrutinizing potential deals more carefully than ever. For their part, COOs must ensure that businesses undertake even more thorough preparation prior to asset sales and help support the marketing of assets to the broadest range of potential suitors.

1. Conduct structured and regular portfolio management

With regular reviews of their portfolios, companies can use divestments as a strategic tool, rather than considering them as a reactive move to free up cash or pay down debt. More than half (55%) of leading companies regularly assess whether their assets are contributing to strategic goals or if capital could be used for other purposes. In contrast, only 40% of study respondents said they have adopted a structured approach to business portfolio analysis, and a further third said they have a structured approach that is carried out on an infrequent or ad hoc basis. COOs can and should play a key role in ensuring regular and structured portfolio reviews are carried out, and can co-lead on the reviews with their CFOs and make strategic recommendations to the board.

Currently, the key factor determining if a business stays within a company's portfolio, for almost 6 out of 10 respondents, is whether the asset dilutes or enhances earnings per share (EPS) and how it performs against financial benchmarks such as return on capital employed (ROCE). Alignment with overall strategy lags behind these two factors, suggesting many divestments are still reactively, rather than strategically, driven.

COOs can work closely with CFOs and CDOs to help develop a set of standardized performance measures to assess the company's portfolio, benchmark performance internally (against other business units in the company) and externally (against competitors), and review strategic fit of assets with the rest of the business. Given COOs have full visibility across the company's range of business activities, they are well placed to contribute to such assessments.

2. Consider the full range of potential buyers

Companies that think strategically about divestments set clear goals for the sale at the outset. They take a view on the value they expect to achieve and the speed with which the transaction can be completed. They understand where interest in the asset is likely to lie, but take a broad view of potential acquirers. COOs can play a role in facilitating both the setting of these objectives and their execution.

COOs understand their companies' assets intimately, working closely with operating units every day. Their role in a divestment is to provide the information and data necessary to their finance and business development colleagues, and to support — with tailoring — the data to specific buyers or groups of buyers. COOs are in the best position to assess and explain how the asset to be divested might provide a strategic fit for potential buyers by identifying likely synergies and execution risk areas. In the case of a private equity buyer, the COO can help articulate how the business could operate as a stand-alone and identify the additional operational costs and skills required post separation.

3. Articulate a compelling value and growth story for each buyer

Buyers are becoming more circumspect than ever about the growth potential of businesses being offered for sale. However, few sellers articulate a strong growth story from the perspective of the most likely buyers. Asked how they enhance the value story of a their divestment, less than 50% of companies said they carry out activities such as supporting the market or product growth story with independent review, developing a M&A plan for potential investors, providing their own view of synergy opportunities to buyers or developing a range of potential upsides.

COOs can improve these percentages by providing information about an asset's historical performance, locating sources for independent review and articulating a view of synergy and implementation opportunities for the acquirer. Gathering such information requires collaboration with the CFO, CDO or tax director.

COOs should also consider making themselves, and the management team of the asset being divested, available to answer questions from potential purchasers — without losing track of day-to-day operational responsibilities. By doing so, the buyer's confidence in the business is likely to increase. Further, potential acquirers will want to be certain that the management team of the asset being divested remains committed, and will continue to support the business throughout the transition period and beyond. The COO's role here is to motivate the management team to stay focused on the business, and to react positively to the sale process and the changes that go hand in hand with it.

4. Prepare rigorously for the divestment process

An uncertain economic environment increases the risk that a transaction will not be completed. By preparing effectively, companies can instill greater buyer confidence, gain more control over the process, move more quickly and realize greater value.

Many companies admit there is room for improvement. When respondents were asked how they would rate their preparation effectiveness for the most recent divestment, just 54% said they performed well in any one aspect of the process. Only 42% believe they were effective in involving key business functions in the preparation process. If those figures are to improve, companies need to ensure that preparation is a regular and ongoing activity, not something that only begins weeks before the company decides to sell an asset.

Fundamental to being prepared is the need to prioritize performance improvement initiatives. Deal success on value is closely linked to the seller being able to validate and support the upsides from performance improvement initiatives and demonstrate that these are not just short-term savings. COOs play a key role in ensuring performance improvement plans are running well in advance of a sale process, and are well prepared to share data on related initiatives, such as how cost savings are faring against key targets.

5. Understand the importance of separation planning

More than half of the respondents identified a clear separation road map as the most complex aspect of divestment. Being able to articulate a clear separation plan to buyers is critical to value protection. When sellers don't clearly communicate the separation challenges and a related plan for grappling with this, buyers are likely to perceive greater risk, and they reflect that perception in their offering price.

COOs should work closely with CFOs and the business development lead in thoroughly assessing the separation challenges and estimating both the recurring and one-off costs of separation. They are also typically heavily involved in TSA negotiations. All these factors should be considered in the separation planning. COOs are well positioned to play a key role in both the separation planning and implementation, given their understanding of business continuity.

The COO's divestment checklist

- [ ] Does your company conduct regular reviews of how each of its assets is contributing to overall strategic goals, and whether capital might be put to better use?
- [ ] Does your company have a good understanding of the full range of potential buyers for each of its assets, or an agreed process for identifying such buyers?
- [ ] Is your company able to support asset sale processes with material that will demonstrate the value and growth story of the business to be divested?
- [ ] Whose responsibility is it to develop such material – to commission independent reviews of for – sale assets, for example, or to develop M&A plans for each asset?
- [ ] How does your company seek to understand the strategic objectives of different types of buyer for its assets?
- [ ] How well prepared would you say your company is for asset sales, including assets where there are currently no plans for a sale?
- [ ] Are information exchange processes in place so that key performance data can be accessed instantly in the event that a divestment becomes likely?
- [ ] Is your company able to produce clear road maps explaining how separation will take place during a divestment process?
- [ ] Whose responsibility is it to address issues such as transition service agreements, tax planning and regulatory requirements?
- [ ] Do you have plans in place for dealing with the management teams of assets that might be divested, in order to retain their commitment and focus on the business during any sale process?
- [ ] Do you have clear business continuity procedures in place that address both the future of the asset to be divested and the remaining business in the event of a sale?
- [ ] Do you have mechanisms in place to measure the success of divestments, with assessments of metrics such as value achieved, speed of process and risk of disruption to the business? How do you act on such performance-measurement exercises?

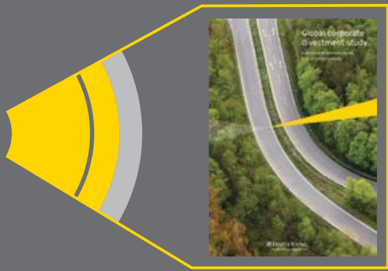
Further reading

- *Divesting for value*, EY, 2012.
- *Human capital carve-out study – strategies of successful sellers*, EY, 2013.

For a copy of the full report, please visit www.ey.com/divestment-study-2012

Alignment to the COO agenda

The Global corporate divestment study has a strong relevance for the COO's role. The yellow wedges highlight those areas that are influenced most strongly.



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