Breaking up isn’t hard to do

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Restructures and asset sales are a growing theme among companies on the threshold of reporting season, with a tough earnings backdrop prompting many to hone their focus and free up cash.

Fund managers say the action has been triggered by a growing realisation that the pre-global financial crisis wave of credit-fuelled consumption is unlikely to return.

A focus on costs is also driving the push, with companies exposed to discretionary spending, the slowdown in commodities or structural change especially challenged. Telstra, Perpetual and Leighton recently joined the ranks of those divesting, while the structurally challenged News Corp earlier said it would spin off its newspaper assets and BHP Billiton is reportedly mulling the sale of its aluminium assets in Brazil.

“If companies are divesting to focus on their core business and it gives better debt to equity ratios to weather the downturn, then it should be a positive for investors, though there may be short-term pain in reduced earnings per share,” said Constellation Capital’s head of investment research, Peter Vann.

Lanyon Asset Management director David Prescott said companies with diverse and disparate business operations, such as conglomerates, had largely lost their appeal with investors. “Asset sales of non-core businesses undertaken at appropriate prices are almost always advantageous to shareholders,” he said.

“[Several] companies have entered this period with an inappropriate capital structure and are facing an urgent need to sell assets and repair balance sheets. Qantas, FKP Property and [several] retail and media companies are prime candidates.”

Patersons Asset Management’s head of equities, Jason Chesters, cautioned that asset sales could also be fire sales. “Any asset sale always benefits the advisers but sometimes it’s a question of whether shareholders benefit,” he said, pointing to the sale of Kagara’s Lounge Lizard mine for $68 million.

He said they could have expected up to $150 million for the asset, though the sale failed to save the company.

On the flipside, Mr Chesters pointed to Tap Oil as an example of a corporate which is divesting for shareholder benefit. Tap sold out of its Harriet joint venture interest for $10 million, an investment which had exposed the company to a $20 million litigation liability. “Now they have over $100 million in cash and a market cap of $157 million. The sale has benefited shareholders though is not reflected in the price,” Mr Chesters said.

Splitting up

Recent divestments

Parent company	Divestment	Date announced
Perpetual Investments	Sold its mortgage management business for undisclosed price	Jul 12
Leighton Holdings	Sold Thiess Waste Management for $218m	Jul 9
NewsCorp	Announces plan to spin-off publishing division	Jun 28
Fairfax Media	Reduced its holding in Trade Me by 15% to 51%, raising $160m	Jun 18
Telstra Corporation	Sold its subsidiary TelstraClear to Vodafone NZ for $660m	Jul 12
BHP Billiton	Rumoured to be mulling the sale of aluminium assets	

Historical performance of spin-offs

- Spin-off companies on a median basis perform in line with the parent immediately after a de-merger but start outperforming about 9 months later. The median outperformance of the spin-off versus the parent is 5 per cent over 12 months
- The parent company largely market performs for up to 12 months. The spin-off slightly underperforms the market in the near term before outperforming after 6 to 9 months
- The average performance of the two demerged entities has historically been in line with the market in the short term before outperforming over 12 months
- After 12 months the spin-offs appear to begin to underperform their parent

SOURCE: GOLDMAN SACHS, FINANCIAL REVIEW

He noted that BHP had not confirmed rumours of its aluminium sale in Brazil, suggesting a difficult backdrop given a lot of aluminium supply was coming on the market.

More broadly, Dr Vann said wealth managers were obvious candidates for divestments as equity investors remained on the sidelines and market-linked revenues slide.

Take Perpetual's recent announcement it would sell its mortgage-processing service. Australian Foundation Investment Company is a shareholder in Perpetual and its general manager, Geoff Driver, supports the move.

"It will be good if it helps their focus on wealth and other businesses, which is clearly their intention," he said.

Among the telcos, Telstra last week said it would sell its New Zealand operation TelstraClear to Vodafone New Zealand for $660 million, a move which analysts said lifted surplus cash for potential capital management or acquisitions.

In the structurally challenged retail sector, Investors Mutual portfolio manager Julian Beaumont suggested some of Fantastic Holdings' Fantastic Furniture assets in Adelaide were ripe for sale, but said it was more likely in the first half of next year.

"Myer has no real opportunity for asset sales or restructuring [while] Harvey Norman would love to sell or restructure overseas operations, particularly in Ireland, but it's tricky given the length of leases," he said.

Mr Beaumont pointed to Woolworths' sale of its unprofitable Dick Smith stores as necessary and suggested Wesfarmers would probably try to address issues in its Target and Officeworks assets rather than divest.

“Officeworks is difficult, with structural and cyclical issues, and Target will take time to get back into a solid position,” he said.

“[Target’s] margins have been too high the past five years and the Wesfarmers’ thinking is low prices for a value proposition.”

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