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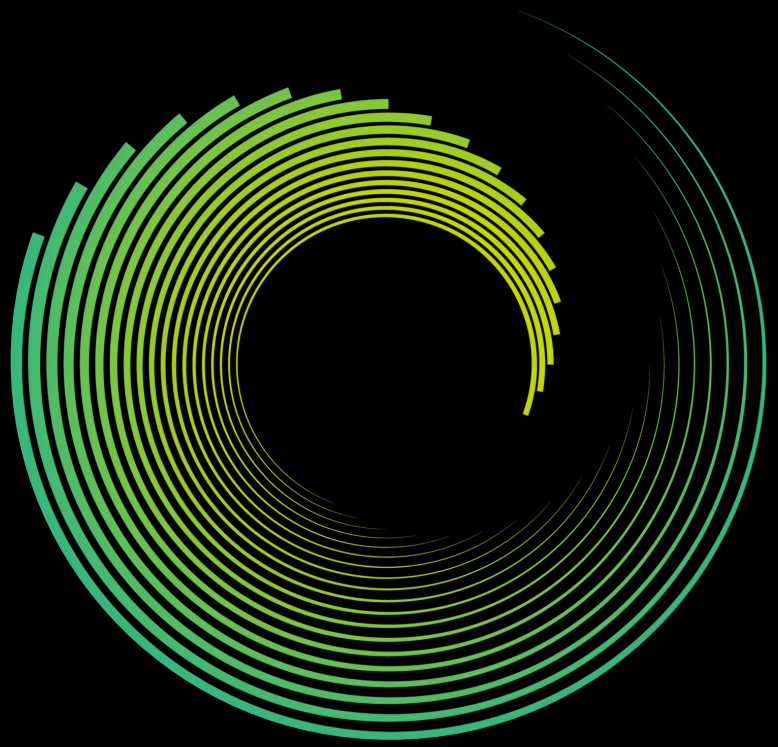


Is it time for a break?

How to maximize divestment success

M&A

Contents

Introduction

In low growth economies, where much actual earnings growth is delivered through focused corporate strategies, divestment is increasingly seen as a key lever to deliver shareholder value and ensure strategic alignment. Companies are reviewing their portfolios of assets and asking if they are the right owners of any given business. Where the existing portfolio is not delivering optimal shareholder value or does not have a clear strategic fit, the result is often a decision to divest under-performing or non-core assets. Companies then use the resulting additional time, resources, and capital to focus on growth activities.

According to Deloitte's global M&A Index, there has been a significant recent increase in major divestment activity, with companies announcing nearly USD 200 billion worth of global divestments in 2016 alone, compared to USD 150 billion in 2014.[1] This increase can be primarily attributed to three reasons; there has been an increase in mega deals and divestments are necessary to get regulatory approval; organizational portfolio review and optimization to focus on core growth areas; and activist pressure to shed assets.

However, getting value from divestments is challenging. Companies report that many divestments do not yield expected value, that the sale process is often more costly and more drawn out than anticipated, and that non-financial costs such as impacts on morale, reputation, and customer perceptions can be significant.

How can companies meet these challenges and avoid common errors of strategy and execution? To help answer these questions Deloitte recently surveyed 123 global organizations to obtain their perceptions on how they delivered value through divestments. This initiative builds on two previous surveys conducted in the UK and US in 2012 and 2013, respectively.[2,3] In addition, we interviewed a number of senior executives with extensive experience in delivering value to their organizations through divestments.

The survey and interview responses provide valuable insights into what our clients and professionals consider the key emerging issues in divestment strategy. These include the sharp increase in political and economic uncertainty which is making asset valuation more challenging; the appearance of new buyer populations, particularly emerging market buyers; the expansion of data sources relevant to divestments and the introduction of powerful data analytics; and finally the increasingly strategic and long-term acquisition approaches adopted by private equity buyers.

Methodology

This report is based on a survey of professionals from 123 global organizations who have recently been involved in divestment activity. Deloitte engaged a third-party organization to perform the survey on our behalf. The survey was conducted in July 2017, and was followed by a series of interviews with senior executives experienced in delivering divestments to gain further insights and perspectives.

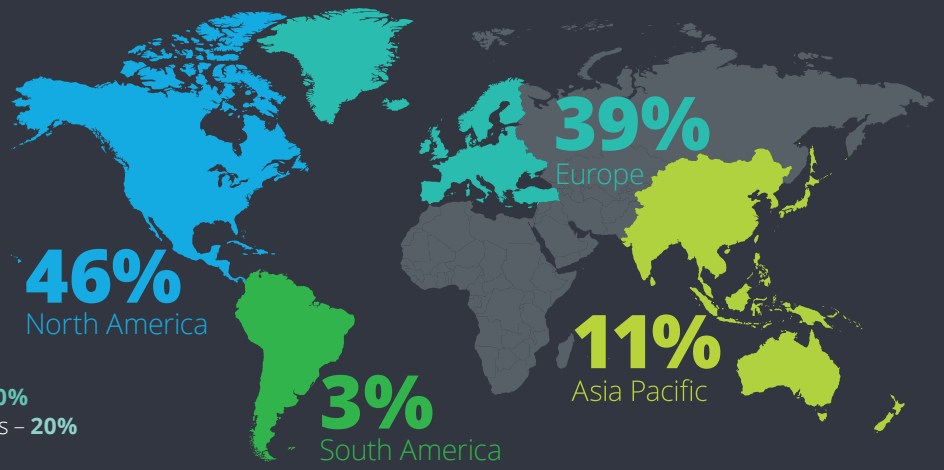
Of the total survey respondents, 48 percent were CEOs, 22 percent were board members or C-Suite, and 19 percent were either heads of M&A or part of the survey respondents' corporate development team, while 80 percent of the organizations surveyed had over USD 500 million of annual revenue.

The organizations surveyed represented a cross section of sectors:

Financial Services – **22%**
Technology, Media & Telecommunications – **21%**
Life Sciences & Health Care – **20%**
Consumer & Industrial Products – **20%**
Energy & Resources – **18%**

In addition, the survey captured a number of global organizations with headquarters based in North America (46 percent), Europe (39 percent), and Asia-Pacific (11 percent).

We thank all participants for their time.



The changing market

Expectations for dealmaking are on the rise. A third of respondents in the Deloitte Survey say their organizations undertook more than one divestment in the last three years, and 70 percent expect to make at least one divestment in the next two years (with 15 percent expecting to undertake three or more). Yet even though divestment activity and intentions are strong, that doesn't necessarily mean that deals are getting easier to transact.

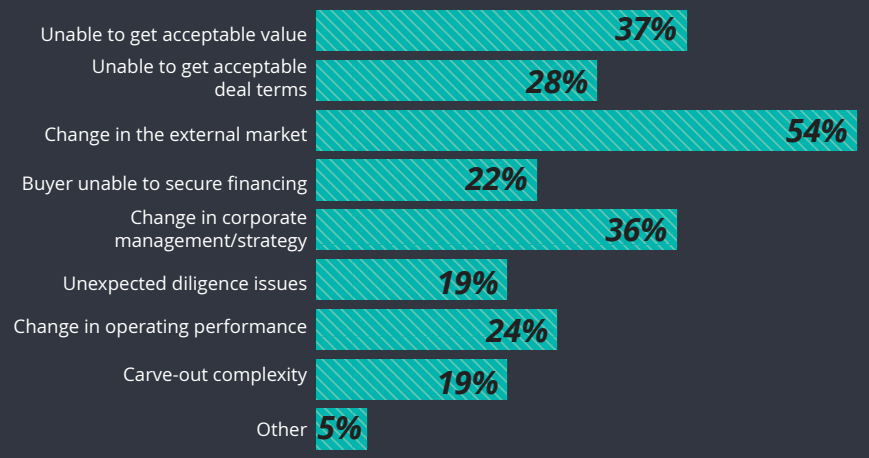
According to our survey, 54 percent of organizations expect that divestments will be more difficult to deliver in the next 12 months due to external market changes. We see this top-line result as indicative of a strong sense of corporate uncertainty about the near future, an uncertainty that is making it harder to conclude deals.

The common theme is uncertainty. As Iain Macmillan, Deloitte global head of M&A, says, "the decision to buy or sell is becoming more critical. It's not a question of do I pay or accept 5 percent more or less. The question is, do I want this level of uncertainty in my business?" Pricing that uncertainty accurately is the key to divestment success.

Risk sensitivity is having a number of specific effects in the market for divested assets, as we highlight in our results. Buyer demands are changing, deals are becoming more complex and involving more data and analysis, and shareholder activism and regulatory change are adding to the risk calculation.

"Divestments are now recognized as a core part of an organization's priorities, yet the complexities of how to identify and execute these successfully is changing rapidly. Sophisticated businesses are adapting their strategies to ensure they capture maximum value from these activities," says Larry Hitchcock, Deloitte head of Global Divestments.

Figure 1. What do you consider are the main drivers that will make divestments difficult to complete this year? (Please select all that apply)



"Value in the eyes of a seller or a buyer is a prediction about the future."

Andrew Robinson, Deloitte UK Head of Valuations

Why divest?

Divestment has always been part of the corporate renewal cycle. New businesses are created and even though they may thrive, they may not be best served by remaining part of the portfolio. Businesses are acquired but may not have delivered the synergies or growth that was first envisioned. Changes in the shape or strategy of the wider business may leave perfectly viable businesses orphaned and in need of an owner who can offer better strategic fit.

"There are two important motivations for divestment," says Natalie Hall, Deloitte UK Transaction Services Divestments. "One is that the company believes that by splitting off part of the company they will increase shareholder value. The other is a portfolio optimization exercise, where the company believes that even though the business does not justify further investment, it can still retain some of the value of the business through a sale."

- **Businesses are most likely to be divested when they are viewed as non-core.** Over half of survey respondents say reshaping their portfolio to focus on the core business is their primary motivator for divesting assets. But for most divesting companies this is an issue of strategic fit and not of growth potential. When asked the reason for designating a business as non-core, a third of organizations cite non-synergistic products, followed by poor operating performance and weak market position. Only 19 percent say that a business was viewed as non-core because it had limited growth potential. Some companies urge caution about publicizing the status of a potential divestment as "non-core"; for example, the Separation Director at a UK-headquartered banking group says "announcing a 'non-core' strategy can be damaging for your position with business leaders and buyers. It becomes very hard to go into negotiations with anything other than a fire sale mind-set."

- **Fewer than half of organizations say they review their portfolio from a divestment lens on an annual or bi-annual basis.** Organizations which regularly perform portfolio evaluation say profitability metrics and product fit are the primary methods to assess whether a business remains core.

- **Market and competitive landscape changes are growing in importance.** Forty-four percent of survey respondents say that market changes are motivators for divestments. This is a marked increase from just five percent of respondents in our 2012 survey.

- **Shareholder activism is driving divestment.** An increase in shareholder activism and interest in portfolio management is the third most-cited motivator to divest.

Smart steps

Companies that regularly review their portfolios using a strategic, structured approach are likely to derive more value from divestment. Many companies do not conduct frequent strategic reviews. "In theory this is something that is done annually as part of the resolution and recovery planning process," says the Corporate Development Director at a large Global banking group. "In practice businesses are only thoroughly evaluated every three years."

1. Companies should be able to clearly articulate their mergers, acquisitions, and divestment strategy to shareholders seeking to understand the rationale for retaining perceived non-core assets.

2. Regular rather than ad hoc strategic reviews are preferred. "To focus the portfolio, review has to be a regular activity," says the director of Mergers, Acquisitions, and Divestments at a global electronics group. "This is better overall, and better from the perspective of the business to be disposed, because it means you will be more focused on its growth and potential."

3. Look at your business from an "outside-in" approach. Conduct an independent review on divisions, products, portfolio and geographies and ask yourself am I the right owner? How could I deploy this investment? Does this fit with our strategic priorities?

"Often divested businesses tend to become orphans—receiving less and less attention from the group until the business starts to under-perform and then the disposal has to happen quickly at the last minute."

Head of divestments, leading health technology company

Figure 2. How would you characterize what has motivated divestment activity at your organization? (Please select all that apply)

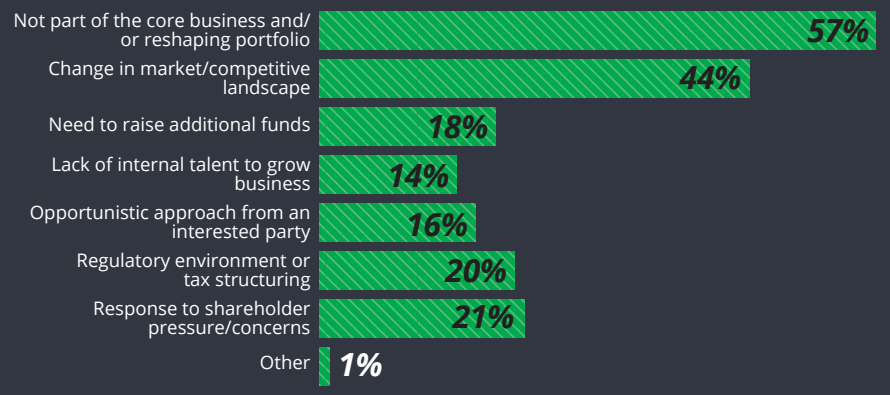


Figure 3. Having pursued a divestment in order to move away from a non-core business, what do you consider was the reason for the business to be non-core?

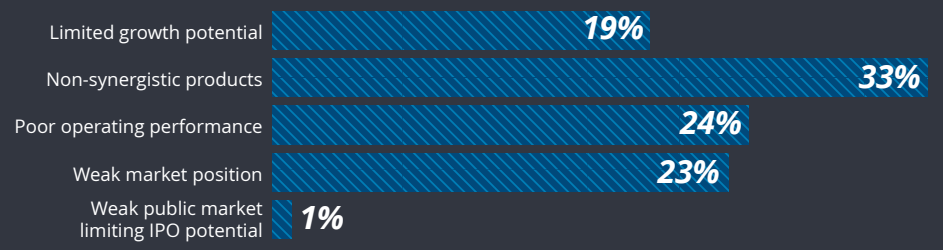
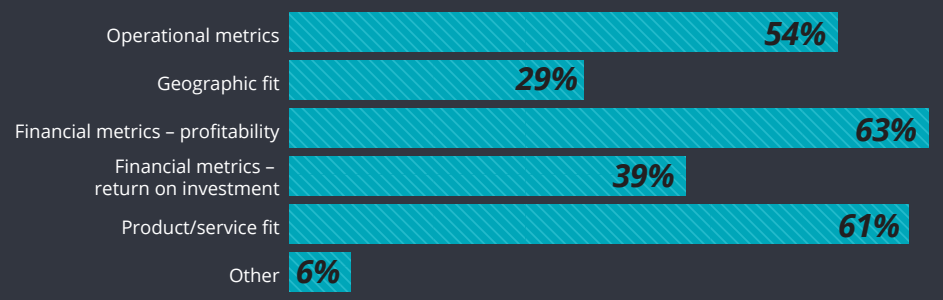


Figure 4. Considering your motivation to dispose of "non-core" assets, what metrics/considerations have you assessed to determine that the asset is no longer core to your business? (Please select all that apply)



Managing the process

Delivering a successful divestment calls for proper planning and skilfully implemented execution. The art of divestment is different from the art of acquisition (even though some of the same executives may be involved) and demands the ability to push through a clean separation without damaging internal morale or external reputation.

According to the separation director at a global banking group, the atmosphere in which divestments take place must be carefully managed.

"Divestments often start from a negative emotion and that becomes pervasive over the course of the transaction," he says. "Separation directors must have a finisher mind-set. You must be able to drive multiple issues in parallel through to resolution usually against almost impossible timescales. The deadlines in divestments are very hard with huge pressures that come from Group management to execute."

- When survey participants were asked to prioritize the tasks they need to perform before bringing a deal to market, 72 percent said **preparing a business valuation is the most important task,** followed by analyzing optimal deal structures and assigning a dedicated deal team (tied at 61 percent).

Many companies concede that business valuation is a challenge because of the difficulty of getting visibility on the standalone performance of an integrated business. "The first challenge is getting solid financials in place to allow bidders to properly understand the business," says the head of M&A at a leading consumer products group. "Our businesses are typically deeply integrated and presenting on a standalone basis can be a challenge."

There is also a second layer of challenge that is related to current uncertainty about the economic and policy environment and the prospects for growth. "First you need a clear understanding of profitability as it stands," says Andrew Robinson. "And then you need to know how much of the price is attributable to growth that has not yet been delivered. The proportion tells you how much of a bet the buyer is taking on the deal, the greater the proportion, the greater the risk of overvaluation."

- The execution challenges of a divestment can be numerous and substantial. Our surveyed organizations say their **biggest issue is managing employee morale,** at 71 percent of respondents. In addition, 40 percent state that a lack of communication with the organization about future plans for the business being sold is a major issue. The two are closely connected—morale is likely to suffer when rumors abound and employees speculate about their future.

Divestments affect internal morale in both the divested business and the retained businesses. But companies can emphasize the positive dimensions of divestment, if they choose to. "An organization needs to position itself, often stepping out of a large group into a smaller organization can drive performance, but the management teams impacted just need to believe this," says the head of divestments at a leading health technology company. "They will ultimately get greater attention and understanding in their new environment as a result of the divestment."

But morale and reputational effects are not entirely in the hands of the vendor, companies point out. Some companies select buyers with this in mind. For example, the separation director at a global banking group says "the impact on people increasingly becomes a powerful factor on choice of buyer. We consciously chose certain buyers over others because they had investment plans for the business rather than high-synergy cases with staff redundancies. We have an ever reducing appetite to go with buyers who would cause us reputational damage with large headcount reductions"

"We have an ever reducing appetite to go with buyers who would cause us reputational damage with large headcount reductions."

Separation Director, global banking group

Leadership and clarity are key, says **leading health technology company**

Leadership is critical to deliver on divestment deals, says the director of divestments at a leading health technology company. “The project lead is the deal captain supported by the disentanglement lead, it is their role to link in the wider business.”

But just as important are clarity and team capabilities. “To deliver a successful divestment you need a clear playbook, and a defined process to give guidance to the deal team and the wider business,” says the director of divestments. “It is also important to have the right capabilities in the team, and that means experience. Divestments differ from acquisitions—in order to successfully disentangle businesses you require operational knowledge. You need to be able to run a standalone business or know what it takes.”

“Time is a crucial factor, and having a clear process and structure is essential,” adds the director. “But in the end you have to remember that you have a responsibility not just to sell, but to deliver the business to a home where it can prosper. It is our responsibility for the business to land well.”

Smart steps

1. Form a dedicated separation team and follow a robust, structured divestment plan to avoid negatively impacting employees' business-as-usual performance.
2. Ensure separation executives have operational knowledge of the business to be divested and are ready to work with very tight deadlines.
3. Conduct thorough sell-side preparation. Deliver clear and consistent financial information that supports the equity story and has forecast assumptions rooted in historical experience. Consider using dedicated tools such as Deloitte's iDeal,[4] designed to create an information resource that allows vendors to see the business through the eyes of potential buyers.
4. Communicate regularly and clearly with employees to keep them motivated and help them manage divestment-related cultural change: work hard to identify the advantages of divestment to an owner that has strong belief in the potential of the business.

"You have to ask how did the company get where it is. Is it by acquisition or by organic growth? Because if you have been through an integration process with an acquisition or you have a heavy reliance on group services that is a very expensive and disruptive thing to unpick."

Dan Beanland, separations partner, Deloitte UK

Figure 5. In your opinion, which of the following are top five priority tasks to perform prior to bringing a deal to market? (Please select all that apply).

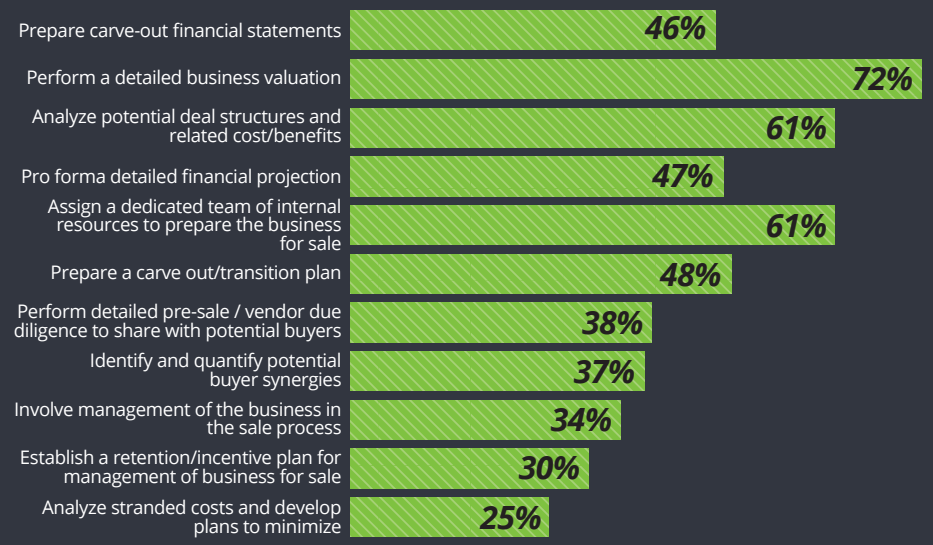
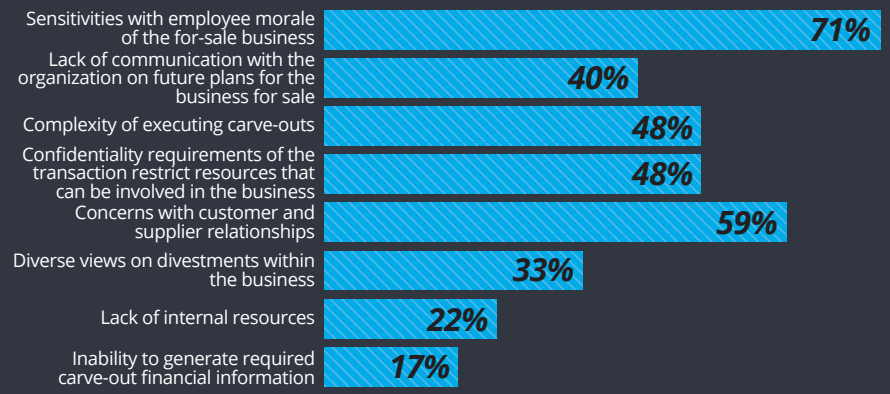


Figure 6. When your company attempts a divestment, where do the challenges lie in pursuing a divestment in your organization? (Please select all that apply)



Finding buyers

Changing external market conditions together with intensifying regulatory intervention are making it more difficult to find the right buyers for corporate assets.

"Choosing buyers can be problematic if the asset for sale is challenged," says the corporate development director of a global banking group. "However, with divestments that have complex separations, you have to remember that you need a buyer that is credible and that regulators will approve."

- The Deloitte Divestment Survey shows that **value depends on the number of bidders**. Half of our surveyed organizations report that having multiple competing bidders is a primary factor in receiving higher-than-expected deal value, and conversely, 50 percent of organizations say that having too few bidders negatively impacts value. The message is clear: Sellers who want to increase an asset's sale price should avoid single-bidder, exclusive deals. And with proper seller preparation, a well-run auction can be more time-effective and produce more deal value than a single bidder transaction, due to the competitive nature of the auction process.

- Widening the buyer universe is one way to maximize a divestment's price, but evidence suggests that **not all companies explore the full range of options**. For example, only 50 percent of surveyed organizations say they marketed their assets to cross-border corporates and only 31 percent marketed to cross-border private equity funds.

The Deloitte Divestment Survey suggests that businesses tend to prefer selling to industry cohorts, when possible, because that is where they have established relationships and therefore, believe that the divestment process will be smoother. It appears that the potential benefits of marketing to private equity groups both at home and abroad are less well understood, even though survey respondents say the main reason for choosing a buyer is ability to deliver the highest sales price, closely followed by speed and certainty to close—factors that are potential benefits of selling to private equity firms.

Smart steps

1. Consider the advantages provided by an auction process instead of a single bidder process. Keep options open and strive to attract multiple bidders. This increases the seller's bargaining position and can increase deal value.
2. Consider intra-industry buyers, as costs related to setting up finance, HR, and other functions can be avoided.
3. Look at PE firms if sale objectives include a high price, deal speed, and certainty to close.

Know your buyer
Consumer products giant

With a large portfolio of consumer brands, this global consumer products group has long experience of divestments as well as acquisitions. Recent divestment deals have ranged from small USD 20 million transactions, to businesses with revenues of USD 2 billion. "For this company the key to success is to understand the buyer," says the senior M&A executive.

"Understanding the buyer helps to maximize transaction value, but we also look beyond this," says the senior M&A executive. "We are well aware of our responsibilities so we will also look at the future of the business in the hands of the buyer and often ask for some form of commitment to the employees."

There are also broader buyer issues to be considered. "We want to know the profile of the buyer," says the executive. "What will be the potential of the business going forward under the ownership of the new buyer? Or in licensing deals, we need to be comfortable with the reputation of the licensee."

This company also looks at a buyer's ability to engage in the deal process and to close the transaction in a timely manner, but more importantly there are competitive implications in the choice of buyer. "We need to know what the dynamics of the sale are in terms of effects on the broader portfolio," says the senior M&A executive. "You have to ask, will the sale make a competitor stronger and have a negative impact on the remaining business?"

Domestic versus cross-border, strategic versus private equity

One striking result of the Deloitte Divestment Survey is that companies are more likely to market divestments to corporate buyers than to private equity, and more likely to market to domestic buyers than to cross-border buyers, yet private equity and cross-border buyers are more likely to complete the deal.

"Everyone prefers to sell to a trade buyer because they can pay a synergy premium," says Mark Pacitti, global leader of Deloitte's Corporate Finance Advisory practice, but he questions whether companies are right to prefer strategic buyers.

"The advantage is the ability to drive performance from a business mentoring and incentivizing management," argues Paul Lupton, head of Deloitte UK's Advisory Corporate Finance practice. "They will look at the debt they can raise and determine what they can pay in the light of that, and that may be more than a trade buyer.

"The speed of transaction in a PE purchase is also very attractive to a corporate buyer. PE does not have so many stakeholders to please, and they can act without worrying about fitting a complex business into an existing corporate system—so they can move faster."

Iain Macmillan, agrees that the advantages of sales to PE are often under-estimated by many vendors. "Companies may be cautious about selling to PE, because PE has a reputation of being very aggressive on the deal and then selling very well after two to three years. But PE has moved on, they are becoming more long-term, and they want to be seen as the preferred buyer and seller of assets."

"The preference for domestic over cross-border buyers should also be re-examined," says Iain Macmillan. "You have to ask why sellers do not market more to emerging market buyers in particular. One reason is that companies may just not be accustomed to putting on a seller's road-show in Asia, and another is that other advisers may tend to take propositions to their known local buyers and indeed may not include any emerging market companies."

Developed economy companies seeking to divest may be unaware of the individual data and analysis needs of emerging-market companies. "Chinese buyers, for example, want very specific things," says Andy Wilson who leads Deloitte's US M&A Seller Services practice. "Often they want very detailed operational information, they are not investors but owners. They want to understand more about things like manufacturing processes, logistics, and which buyers are serviced from which locations. The level of detail they require is very significant. They often need to know a lot about sourcing, because they are interested in whether sourcing can be moved to Asia, and they are more focused on cost than on growth."

Figure 7. Thinking about your company's divestments over the last 36 months, which of the following types of buyers were they marketed to? Please select all that apply.

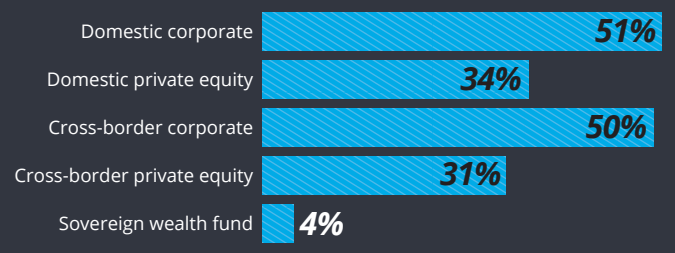
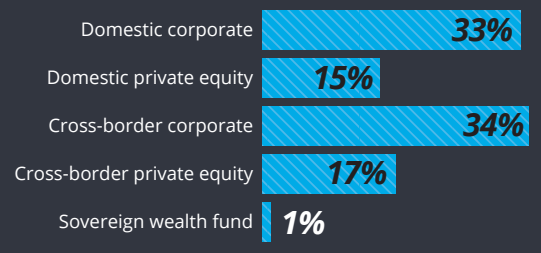


Figure 8. Which of the following represents the typical buyer of the businesses your company divested over the last 36 months?



"The pattern was for PE to buy an unloved subsidiary and improve it. But now PE is just as likely to buy premium assets."

Mark Pacitti, Deloitte

Figure 9. What was the primary determinant/key factor in choosing the buyer?

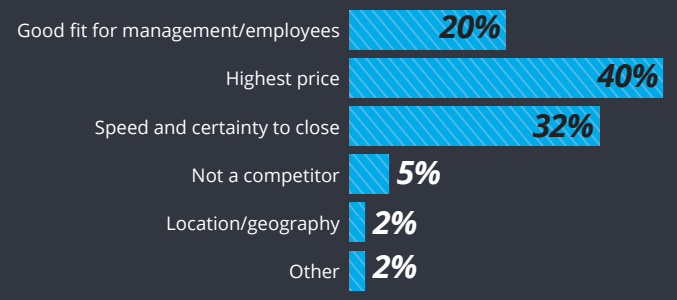


Figure 10. Did any of your recent divestments not end in a closed transaction?

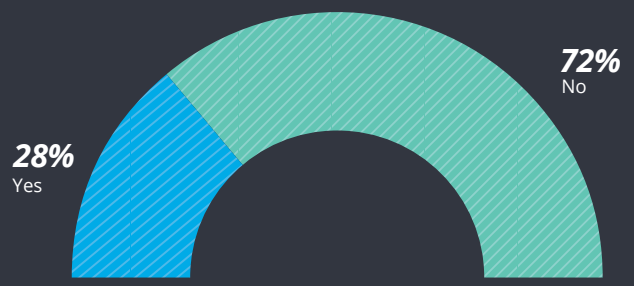
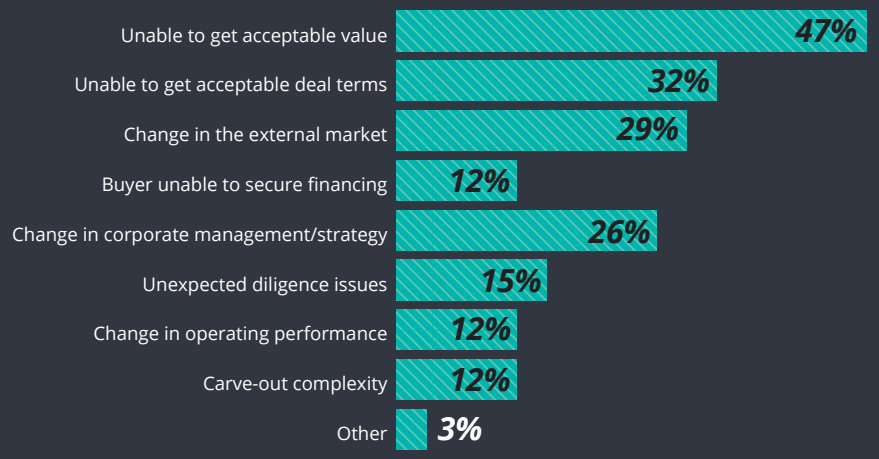


Figure 11. What were the major reasons why some of your company's divestment processes didn't end in a closed transaction in the last 24 months? Please select all that apply.



Data and analytics make the deal

This is the era of data. There are intensifying demands for data and analysis from buyers; at the same time, sellers are coming to the realization that in order to shape the narrative in a divestment, they need more data and more insightful analysis.

"This is a market that is changing rapidly," says Andy Wilson. "There is a huge increase in the amount of relevant information. There is traditional structured data, and there is unstructured data like web reviews or social media. Over the last 12 to 18 months we have seen the more sophisticated buyers looking at kinds of data that were never part of transactions before."

"And for the seller, data is power" says Andy Wilson. "For the seller it is important not to hand over the story of the transaction to the buyer. Most companies tend to say, this is my business, I understand it. But they may not understand it the way the buyer sees it."

- When asked "what would you do differently in your last divestment?" 37 percent of organizations cited the need for **more vendor due diligence** (decreasing the complexity of the divested business was also widely cited).

- Organizations also have seen changes in buyers' needs through the divestment process, with over 50 percent mentioning the need for **more in-depth and "raw" data sources** and 41 percent for greater parent company management team interaction.

- **Use of analytics during the divestment process is becoming widespread,** with buyers demanding greater access to data sources so they can perform detailed, bottom-up modeling. Sellers can add significant value to the asset being divested by providing workforce, commercial, and market data.

"You have to use data to pressure test assumptions, because the people making the assumptions about the value of a divestment don't necessarily really understand the workings of the company," comments Michael Dziczkowski, US Risk & Financial Advisory Divestiture Services leader.

Companies should also focus on customer data, say clients and divestment advisors. "Analysis used to be confined to the top 10 or 20 customers," says Andy Wilson. "Now buyers want to look at the whole customer community. The buyer wants to know what story the data tell, they certainly won't be happy if they find out that all your growth is coming from your bottom 20 percent of customers, but the margins on their business are negative."

Preparation is everything
Global engineering group

A large engineering group says that preparation is the key to successful divestments, but the need for preparation is often underestimated.

"Preparation is the biggest challenge," says the head of M&A. "Good preparation avoids surprises and cuts down the number of challenges you will receive during the due diligence process. You also have to prepare by testing buyer appetite yourself, it's not enough to rely on investment banker pitches for proposed divestments."

"The extent of needed preparation is always underestimated," adds the head of M&A. "Especially the carve-out preparation is crucial, for example deconstructing legal entities in far flung countries. You have to prepare the financial carve-out data to create a standalone EBITDA calculation even before you have the first buyer discussion. You have to invest in preparation upfront otherwise your underlying standalone EBITDA can be challenged and you lose deal dynamic and credibility. The cost and commitment implied is always underestimated, especially where it is a small deal."

"The great advantage in a divestment is that on the sell side you own the process," adds the head of M&A. "But the sell side is more cumbersome for the M&A team, it is a lot more work. The way to deal with that is to control everything that you can control, prepare as much as you can upfront, and minimize the length of the actual auction process."

Smart steps

1. Perform an in-depth, pre-divestment readiness assessment to identify a transaction's key areas of complexity, interdependency, and preparedness, as well as where value can be delivered versus time/cost benefit.
2. Let the data speak for itself: In some cases a full 360-degree pre-sale due diligence can lead the company to decide to market differently, or even not to sell.
3. Focus on the customer: Buyers use data to analyze customer behavior; this will add a lot of value to the asset you plan to divest, since potential buyers will place a premium on this information.
4. Focus on the buyer: Determine what kind of data will satisfy an individual buyer and stay on the front foot by preparing it before it is asked for.

Figure 12. If you could do your company's last divestment/spin-off again, what would you do differently? Please select all that apply.

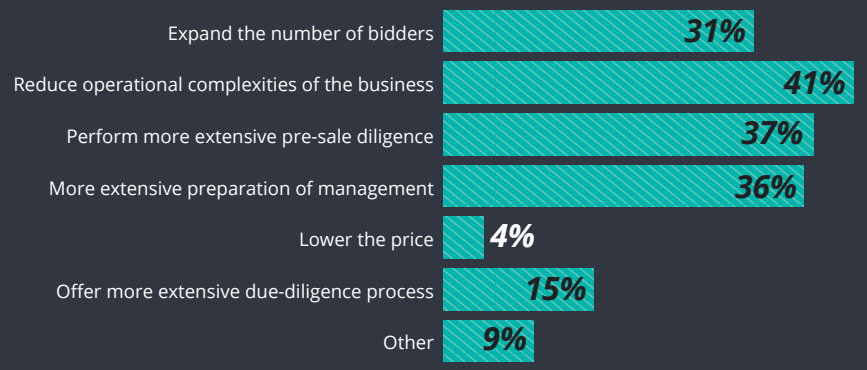


Figure 13. In your experience, have you seen changes to the needs of buyers through a divestment process, namely: (Please select all that apply)

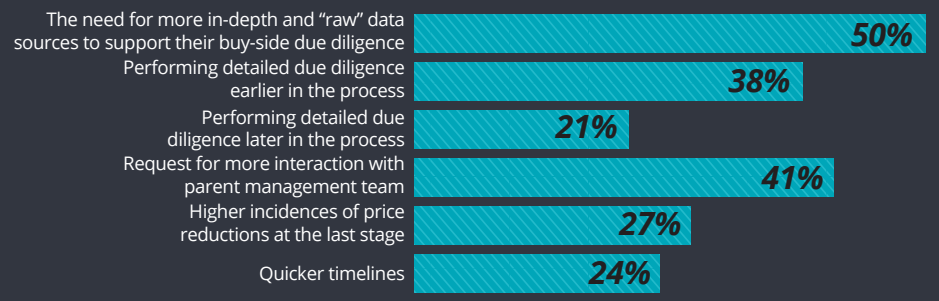
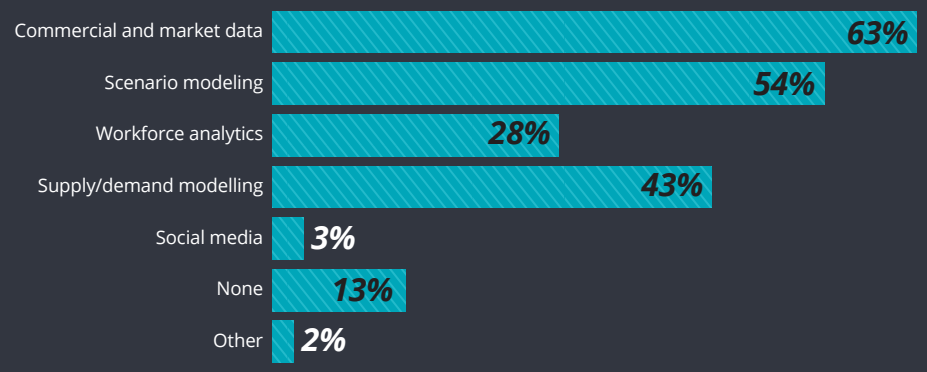


Figure 14. How have you utilized analytics in your recent divestment activity? (Please select all that apply).



"We prepare companies for the diligence that the buyer will require. And it is always better to go out and find your data first rather than sitting on your heels waiting for the buyer to ask."

Natalie Hall, Deloitte

Be prepared for complex transitions

In the textbook scenario, a company is divested, money is exchanged, and buyer and seller quickly part ways with smiles on their faces. In reality, textbook scenarios rarely apply. Many sellers typically have an ongoing relationship with and responsibilities to the divested business that may extend for several months or longer. These are the often complex contractual agreements known as transitional service agreements (TSAs).

The growth of TSAs reflects the trend for diversified corporate groups to run more centralized shared services, and for acquired businesses to be fully integrated in the pursuit of synergies. Unraveling these integrations is complex, time-consuming, and expensive. Often it is impossible fully to disengage a divested business from the original parent's corporate structure within a divestment timeframe.

"The trend over the last 10 to 15 years has been for more companies to be integrated in order to create synergies," says Maxine Saunders, Deloitte UK Head of Transaction Services. "And that creates a challenge when you come to sell. Part of the problem is that vendors may not understand the cost, the more centralized your functions are, the harder it is to see what the costs actually are."

- Survey respondents view TSAs as one of their biggest post-divestment challenges. Of those surveyed companies that provide TSAs, the most frequently offered services are finance and accounting, at 68 percent, followed by IT at 60 percent.
- Survey respondents say that divestments that include TSAs are more attractive to buyers than assets without TSA support. Respondents say that TSAs provide an opportunity to facilitate a divestment and manage costs (37 percent); an additional 28 percent say that providing TSAs is common practice.
- Thirty-six percent of respondents admit that their organization underestimated the costs of providing TSA services. According to our survey, 53 percent of organizations report the typical duration of a TSA is 7-12 months; 22 percent report it is over 12 months.

Our survey results show that 36 percent of respondents say costs were underestimated, compared to only 7 percent who think costs were overestimated.

"Companies make the mistake of thinking it is simple, thinking it involves only two or three functions," says Dan Beanland. "Also, the timeline may be under-estimated, although the vendors may expect and prefer a shorter time, purchasers often want a 12-month TSA with a possible 6-month extension."

Don't be afraid of TSAs
Global banking group

The transitional service agreement (TSA) has proved to be the sting in the tail of divestments for many companies. TSAs are contracts that allow the purchaser to rely on continuing service from the vendor in areas like financing, supply, or logistics during a limited period when the purchaser is building up ability to manage the acquired company—but the cost and complexity of negotiating and maintaining TSAs has often been underestimated.

"Vendors should treat TSAs not as a cost but as a commercial opportunity," argues the corporate development director at a large UK-headquartered banking group.

"There is potentially huge value in TSAs but often corporates fail to secure this," says the director. "The agreed costs of services often under represent the true cost of providing the service, or tail risk isn't sufficiently managed, or TSAs aren't exited when they should be."

The group's separation director agrees that TSAs are often seen as a necessary evil, even though when properly drafted and limited they can secure a sale without increasing risk and cost. "TSAs are about mind-set and too much is made of trying to avoid them, creating increased separation complexity at deal closing," he says. "However, they do keep cost in the selling organization and tie up people on non-core activities. TSAs that are short or low risk to deliver are absolutely fine. It is the large technology and migration services running for longer periods of time that increase risk and can erode transaction value."

"If TSAs are to be treated as a commercial opportunity, they should be prepared early in the deal process," says the corporate development director. "Deal teams need to be much more commercially alert on TSAs. Too often there is not enough thought given to the commercial potential of a TSA. This is usually because the TSA develops late in the transaction process by which point the buyer has had sight of data that limits the seller's ability to maximize value."

"Deal teams and organizations should not fear TSAs," adds the separation director. "If they are for services that have existed before, there is no reason why they should not continue to run as smoothly as before. The processes just carry on."

Smart steps

1. Proactively identify important functions/services that the parent company may need to support through a TSA.
2. Provide sufficient detail about TSA options in separation planning to protect the seller's ongoing business from unnecessary distraction and costs.
3. Structure sales agreements to increase the incentive for the buyer to promptly establish required capabilities and to end the TSA period as quickly as possible.

Figure 15. After closing your company's most recent divestment, what was the biggest continuing challenge?

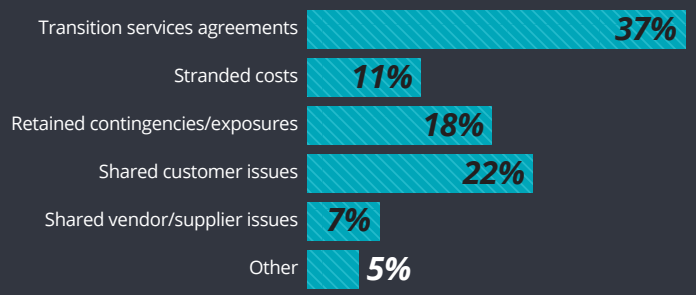


Figure 16. When your company uses a TSA, which functional area does your company typically provide TSA services for? (Please select all that apply)

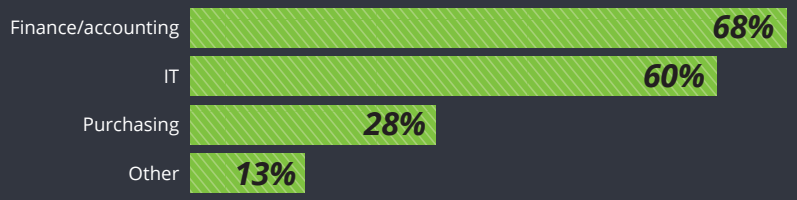


Figure 17. Transition service agreement: What is your organization's practice for providing TSAs?

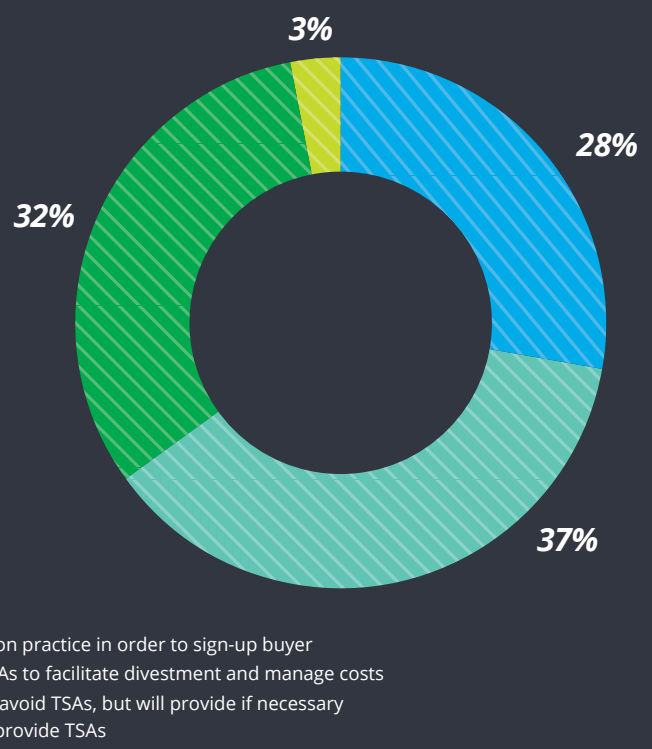


Figure 18. In your company's experience, how has the cost of the services provided through the TSA compared to expectations?

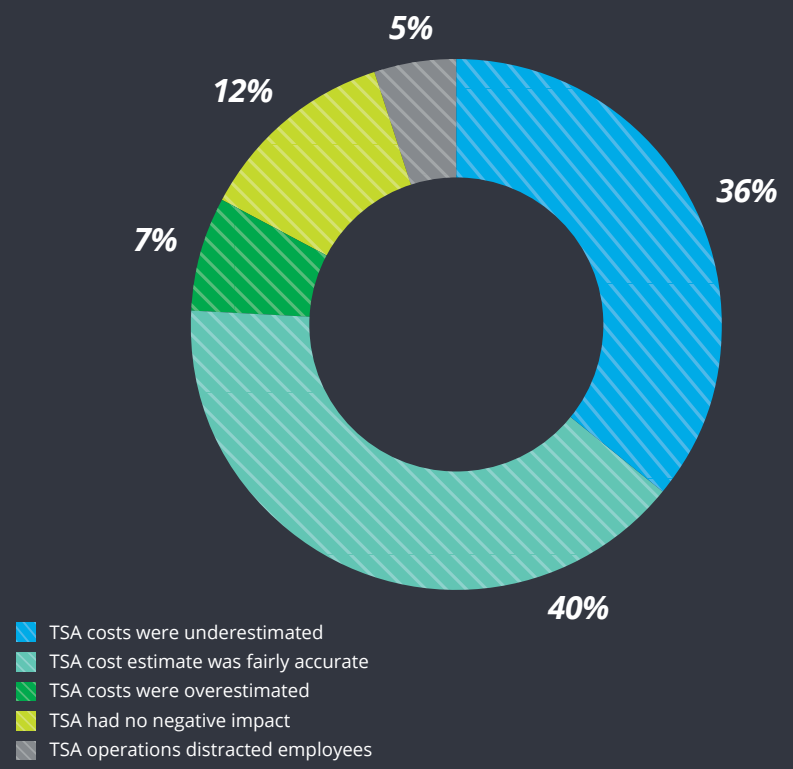


Figure 19. What is the typical duration of your TSAs/reverse TSAs?

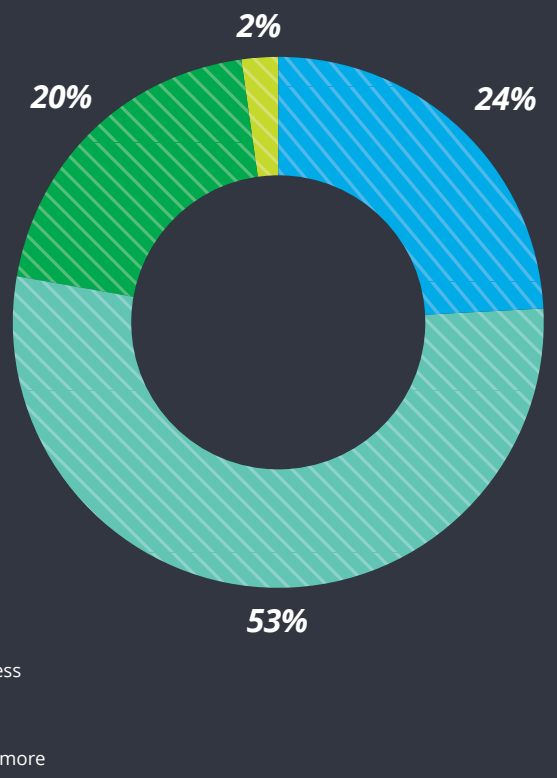
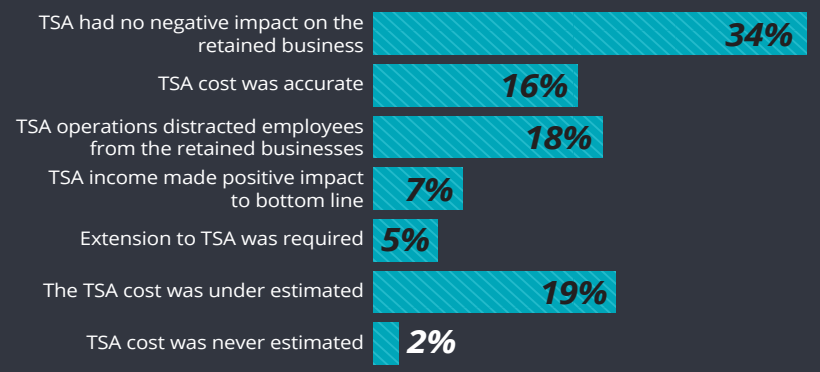


Figure 20. What was the impact on the retained business of the negotiated TSAs with the buyer?



What improves post-divestment share-price performance?

A recent Deloitte study, Creating Value from Divestments, that examined seller and buyer post-divestment share-price performance found that well-executed divestments can create value for both sellers and buyers when:

- They have a clear divestment strategy in place that is aligned to future growth prospects.
- They proactively communicate their growth strategy to the markets. In uncertain times, the market is looking for a clear focus on core business and a well-defined divestment plan.
- They tend to focus on a number of smaller divestments, rather than a single blockbuster.
- They focus on people and cultural changes. Divestments are significant events and leaders must provide clarity of purpose and keep staff motivated throughout the process.

The need for speed

A complex divestment process often can produce unwanted surprises that lead to timeline slippage and operational distractions. Many organizations find it difficult to fully anticipate and plan for a divestment, even where they have previously successfully disposed of assets.

"If you are going to have a successful sale, the first step is speed to market," says Larry Hitchcock, "The longer the deal takes to form, the more uncertainty you build in. You have to recognize that it is difficult to get a deal completed amid uncertainty."

- Among survey respondents, 50 percent say their **divestments took more time than originally expecte**d, due primarily to time spent negotiating the transaction agreements (58 percent) and conducting buyer due diligence (45 percent). One third of respondents said that their divestment took between 6 and 12 months, with 31 percent stating that it took between 12 and 18 months from deciding to sell to executing the purchase agreements.

- Survey respondents report that in **74 percent of their deals, the time between executing the purchase agreements and completing the transaction was over three months.** Nearly seven percent of deals take over 12 months to complete.

"The time to completion can be extended by conflicts between the strategic center and operational units," says the corporate development director at a global banking group. "Big corporates take longer to complete divestments in part because the company thinks they know the business on the basis of analyzing numbers and management packs, when in fact they don't appreciate how the business operates on a day-to-day basis on the ground. There is an arrogance in the head office that divestments can be done quickly and easily, but this runs into trouble the moment you engage local management."

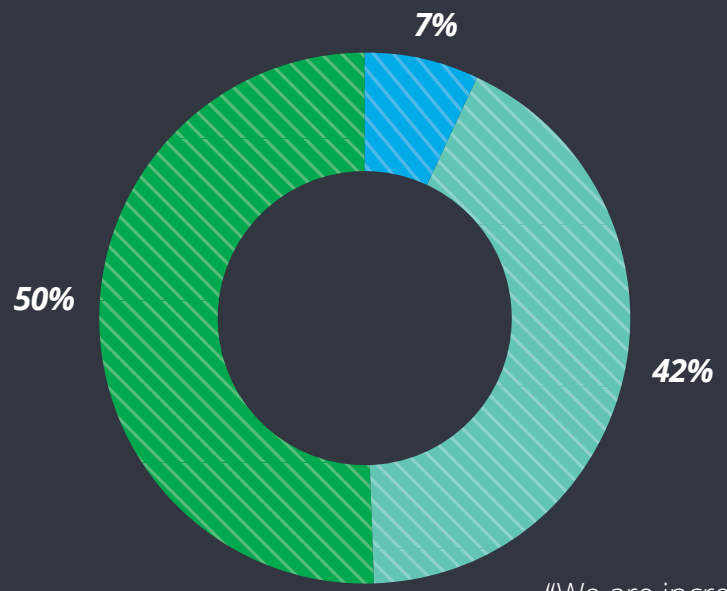
"Employee morale and motivation issues can also be significant when it comes to speeding deals to conclusion," says Anna Lea Doyle, divestiture lead, US M&A services. "There is a question on how do you keep the management team motivated when they don't know if they have a job at the end of the process."

Smart steps

1. Prioritize employee motivation in the business to be divested by demonstrating the growth possibilities of a supportive new ownership.

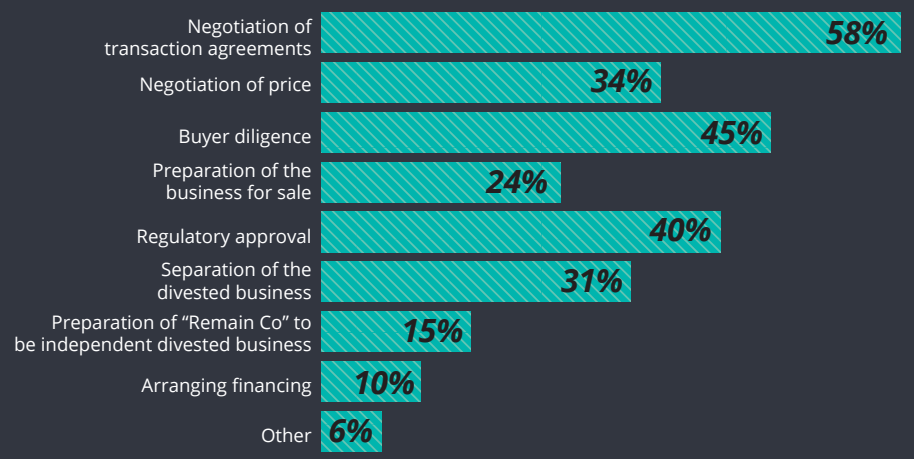
2. Set firm timelines on whether and when to sign and conclude. If deals drift, there is a risk that less-favorable terms may be on offer from a seller's perspective. However, this might not necessarily be the case from a buyer's perspective.

Figure 21. What was the time required to divest compared to expectations?



- Less than expected
- About the amount of time expected
- More time than expected

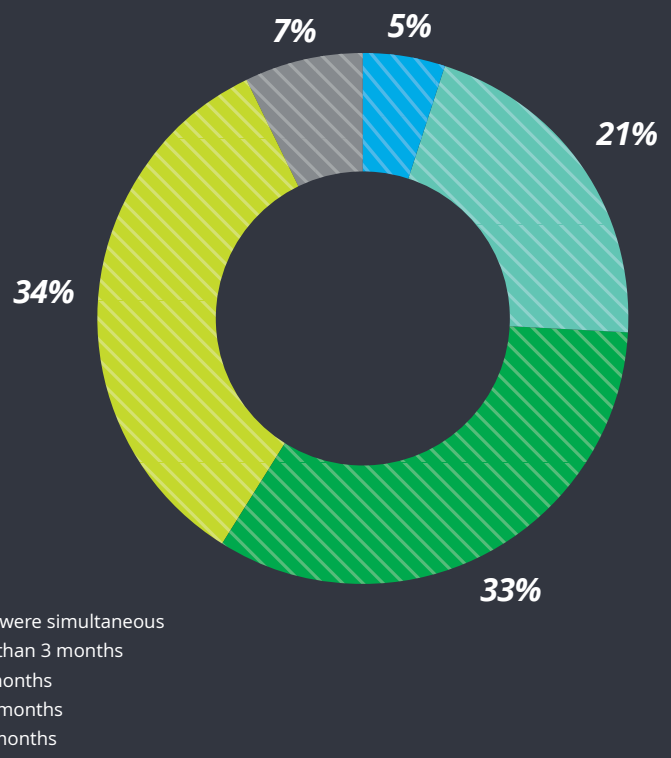
Figure 22. What were the primary reasons that your company's most recent divestment required more time to complete than expected? Please select all that apply.



"We are increasingly seeing complex carve-out perimeters are being established to meet the needs of the sellers. In this seller-friendly market, these rigid parameters are being accepted by buyers, however, it results in lengthy, drawn-out processes, more adviser involvement, and difficulties at negotiation as buyers seek to understand what they actually want to acquire versus what they need to buy to secure the deal."

Maxine Saunders, Deloitte

Figure 23. What was the time period between the execution of the purchase agreements and completion?



"Employee morale and motivation issues can also be significant when it comes to speeding deals to conclusion."

Anna Lea Doyle, Deloitte

Conclusion

The Deloitte Divestment Survey 2017 shows a picture of increased uncertainty over global growth and policy, and increased corporate restructuring in the face of low organic growth expectations. At the same time, the difficulty level of achieving successful divestments is increasing, as the buyer universe becomes more diverse and more demanding.

- Difficulty is increasing, say companies. According to our survey, 54 percent of organizations expect that divestments will be more difficult to deliver in the next 12 months due to external market changes.
- Most divestments are driven by portfolio optimization strategies as companies attempt to refocus on a core of businesses and competencies. Over half of survey respondents say reshaping their portfolio to focus on the core business is their primary motivator for divesting assets.
- Business valuation is the biggest task divesting corporations face as they work to disentangle businesses that may have been intensively integrated in the search for synergies. Over two thirds of respondents say this is their top priority task.
- Execution of a divestment requires planning, leadership, and speed, and the ability to manage morale. Over two thirds of respondents say that managing employee morale is the biggest execution issue.
- Most companies think they should be doing more preparation and providing more analytical data during the divestment process—over half of respondents say this.
- Negotiating TSAs is a critical factor. Over a third of respondents say they underestimated the costs of TSAs, and TSA negotiations contributed to the 50 percent of respondents that say the divestment process took longer than expected.

"Uncertainty is the new normal," says Paul Lupton. "Ten years ago there was growth everywhere, and borrowing was very easy. But now we see new business models that are unproven, we see global disruption, and everywhere you turn there is some sort of turmoil. And all that is making buyers more sensitive to risk."

Endnotes

1. Deloitte M&A Index 2017: Creating Shareholder Value through Divestments
2. Is breaking up hard to do? Deloitte UK Divestment Survey 2012
3. Deloitte US Divestiture survey report 2013: Sharpening your strategy
4. https://www2.deloitte.com/us/en/pages/about-deloitte/articles/press-releases/new-deloitte-mergers-and-acquisitions-analytics-solution-ideal-launches.html

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