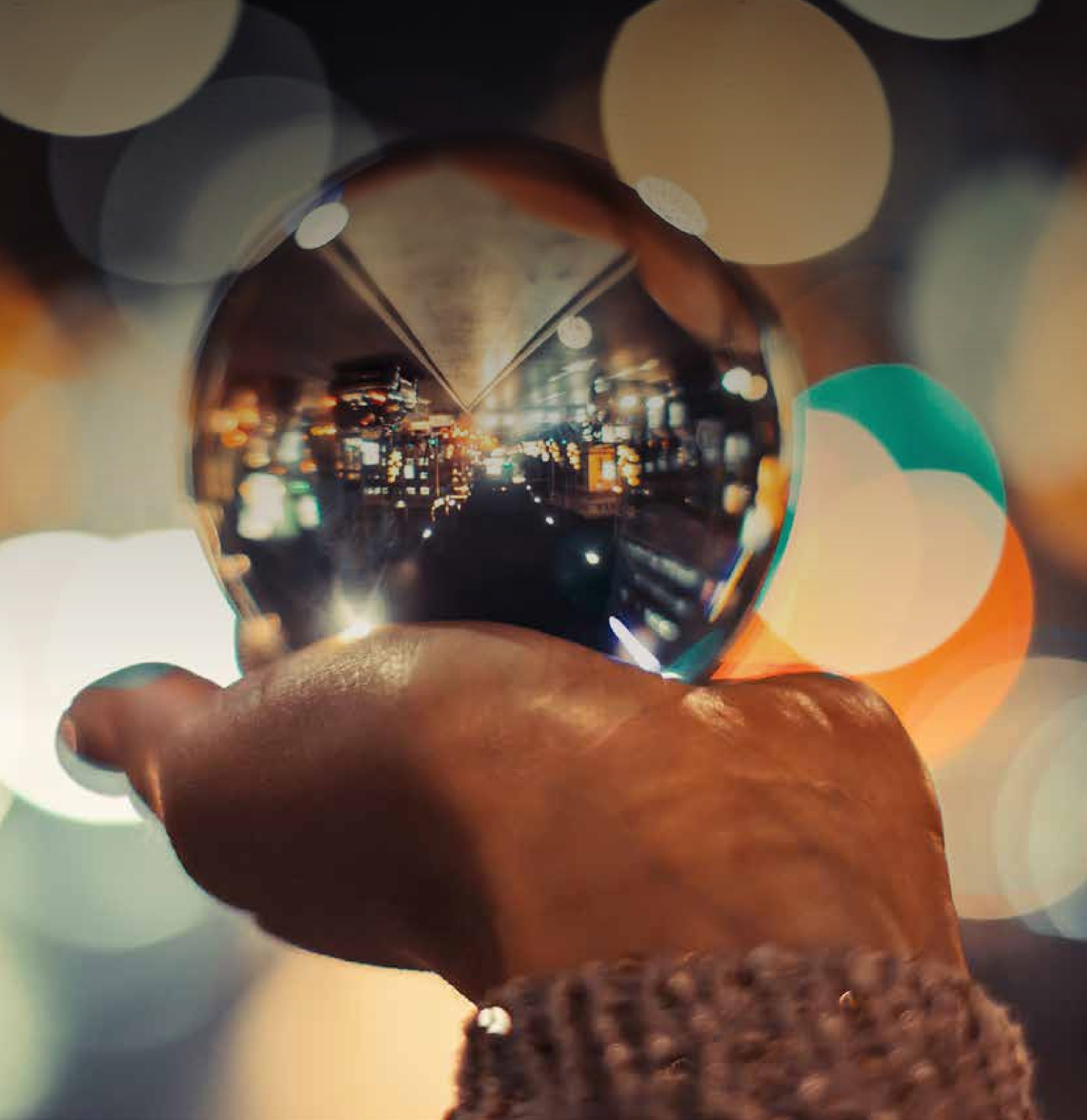
AlixPartners

AUGUST 2020

BE PREPARED TO FOCUS

Introducing AlixPartners Divestment Preparation Programme



Due to the likely long-lasting economic impact of COVID-19, corporates need to focus on their core businesses now more than ever.

Many businesses will be undertaking a ruthless review of their portfolios to understand the returns on their invested capital. This will enable management teams to focus on key growth areas and prioritise capital allocation to core, value generating assets and conclude on appropriate strategies for non-core assets, which may well result in disposals.

However, the current M&A market is also facing challenges. COVID-19 has hit deal volumes and investor confidence hard and there is an added increase in conservatism, partly due to memories of the 2008 financial crisis. Given the challenges with forecasting and delivering against business plan targets, buyers are behaving more cautiously, valuations are being suppressed and debt providers are wary of lending.

FACING A CHALLENGING M&A LANDSCAPE

A year-on-year comparison of European M&A activity in Q2 2020 is a sobering read. There has been a 40% volume decline on Q2 2019 and a staggering 87% decline in total deal values from £173bn to £23bn, while the average deal size has fallen from £310m to £81m [Source: Capital IQ].

Further analysis has shown a similar downward trend in sectors that have historically been the most active from a M&A perspective (see Fig A).

Unsurprisingly, this backdrop has fuelled caution among buyers. Some are sitting on the sidelines waiting for the market to stabilise; others are taking a more prudent approach to deal assessment. The latter has resulted in increased levels of due diligence, sensitivity analysis, rigorous commercial and market assessments, as well as careful assessments of potential digital, cyber and technological risks.

This approach is not only leading to lower valuations, but it is also extending the timelines on sales processes. A recent survey conducted by IHS Markit and Mergermarket in North America reported that 93% of sellers felt longer due diligence processes have become more common, along with greater challenges in agreeing warranties and indemnities (87%), more concerns over digital and technology issues (77%) and a growing valuation gap between buyers and sellers (70%).

As a result, it is not surprising to see a growing number of sale processes stagnate, with data from Mergermarket suggesting an increase in approximately 50% of transaction processes slowing in 2019 compared to the previous year. We would not be surprised if this increases in 2020.

Additionally, the more time spent on preparation, including addressing a buyer's concerns, means corporates are finding the excessive time and resource unwelcome distractions from their core business activity.

TYPICAL LENGTH OF SELL-SIDE PROCESSES	
Between 4 and 6 months	30%
Between 6 and 9 months	43%
More than 9 months	27%

Source: IHS Markit and Mergermarket

FIG A: EUROPEAN M&A ACTIVITY IN Q2 2020 VS Q2 2019

	Europe	Consumer	Industrials	IT & Communications
Deal volume	-40%	-45%	-47%	-35%
Total deal value	-87%	-84%	-69%	-80%
Average deal size	-74%	-71%	-27%	-65%

Source: Capital IQ

All signs point to the fact that, unless divestments are needed to urgently raise liquidity or reduce the cash burn of a lossmaking business, now is a difficult time for corporates to bring assets to market.

At present, corporates are faced not only with a buyer's market but also with the need for increased active portfolio management to ensure scarce resources are focused on the most likely future stars of the business. So, in this landscape, what should boards and management teams be doing while they wait for the M&A market to recover?

REVIEWING PORTFOLIOS

Whilst the M&A market is subdued, now is a logical time for businesses to focus on reviewing their portfolios to determine whether operations continue to fit their core strategies.

Our accelerated approach to portfolio review will help companies answer key questions in formulating their capital allocation strategies and identifying possible divestment opportunities, such as:

- How does a division or segment fit within the company's overall strategy?
- Does it form part of the 'core' operations of the business?
- Is the division or segment generating the required levels of return and/or does it provide a competitive advantage to the core business?
- Would it be more valuable to allocate capital to another core division or segment?
- What is the outlook for the division or segment considering future market dynamics (e.g. has the market fundamentally changed given COVID-19)?
- If a division or segment is considered non-core, what would be the operational and financial implications for the remaining business were the division or segment to be sold?

Determining whether a divestment of a non-core business is the right course of action can be challenging. It requires a deep understanding of the value of the non-core business in its current state and the potential value on its disposal, taking into consideration factors such as any lost synergies, disentanglement, and stranded costs.

WHAT TO DO WITH NON-CORE ASSETS IN AN UNFAVOURABLE MARKET

In our experience, once a business has been identified as non-core, it tends to be neglected. It receives minimal further investment or management attention and as a result, the performance, attractiveness and overall value of the business starts to further erode before it is even brought to market.

This neglect can result in lower valuations, or in some instances the sale failing altogether, costing the seller time and money. And those who resort to dissolution will find themselves with additional costs through redundancies, management and administration.

Rather than businesses ignoring non-core assets, there needs to be a switch of focus from strategic attention to value protection.

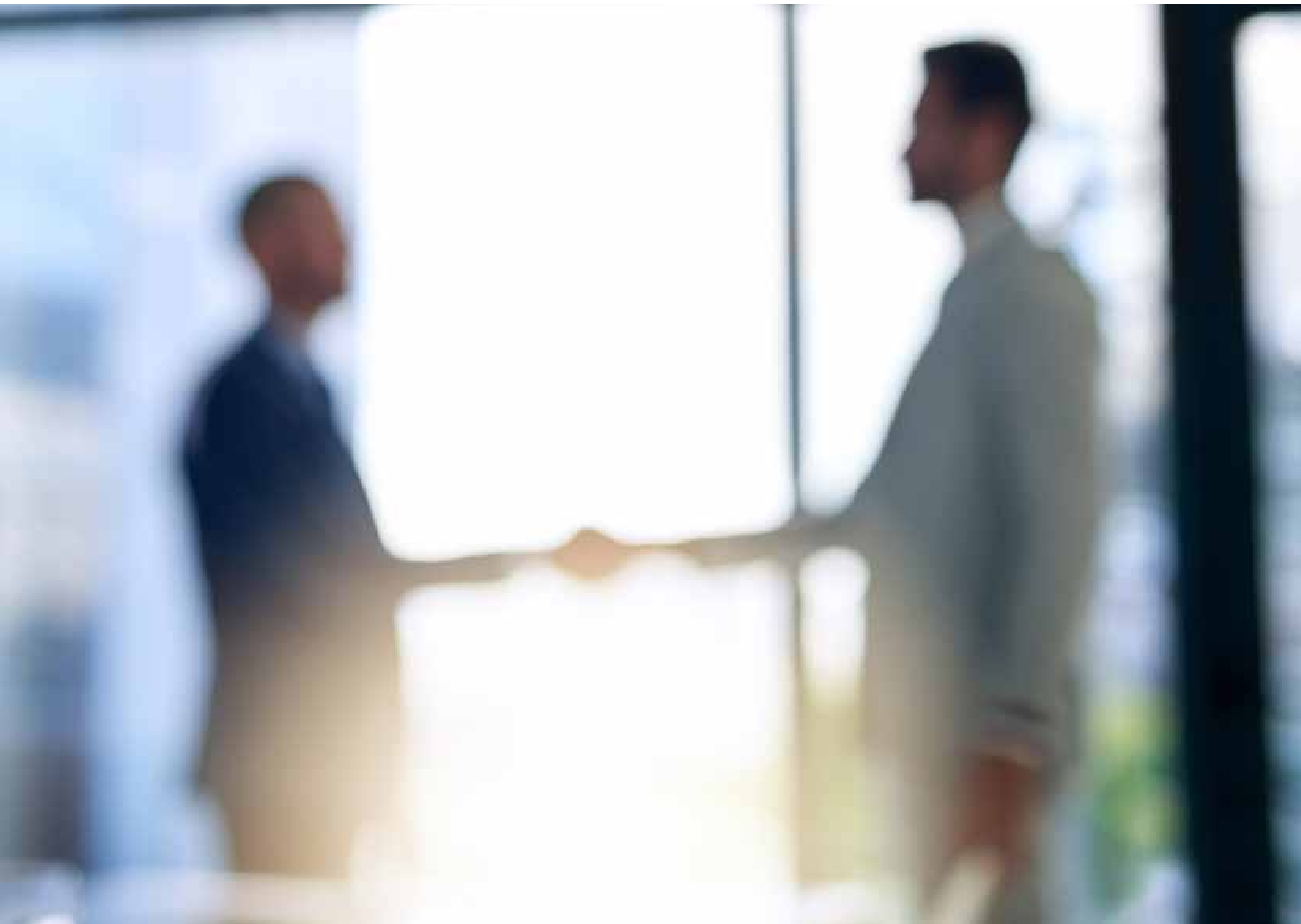
To help clients achieve this and realise maximum value from non-core divestment processes, we have implemented our Divestment Preparation Programme.

DEPLOYING THE DIVESTMENT PREPARATION PROGRAMME – HOW WE CAN HELP

In a volatile and uncertain M&A environment, all too often the outcome of business divestment processes can be uncertain. To reduce this uncertainty, ensure value is not left on the table and increase certainty of a positive outcome, we recommend thorough preparation prior to divestment.

In a recent survey by IHS Markit and Mergermarket, it was confirmed that clients feel the same. When asked what actions could have been taken to make their most recent divestment deal go more smoothly, 87% wished they had organised the company for a sale well in advance of the process beginning, while 77% believed they should have developed a more in-depth insight into potential issues with specific business units.

In response to these observations, we have developed the AlixPartners Divestment Preparation Programme (DPP) – a highly structured, focused approach, designed to maximise value on the sale of non-core businesses and provide greater certainty on delivering a transaction.



MAXIMISING VALUE AND PROVIDING GREATER CERTAINTY ON DELIVERING A TRANSACTION

The Divestment Preparation Programme consists of four core phases: a business assessment or QuickStrike©; performance improvement and carve-out assessment; exit readiness; and divestment execution.

Key workstreams

PHASE I	PHASE II	PHASE III	PHASE IV
Initial business assessment	(a) Performance Improvement (b) Carve-out planning & implementation	Exit Readiness	Launch sale process

BUSINESS ASSESSMENT (QUICKSTRIKE©) AND INDUSTRIAL LOGIC

- Detailed financial, commercial and operational review
- Identification of performance improvement opportunities
- A commercial and M&A assessment to develop the 'industrial logic' of a proposed exit

PERFORMANCE IMPROVEMENT

- Performance improvement opportunities defined, road mapped and implemented
- Development of a robust business plan
- Carve-out assessment to formulate a detailed plan to de-couple the target from the group

EXIT READINESS

- Pre-sale financial, legal, tax and HR review
- Identify and address any gaps to ensure surprises are avoided
- Develop sale process strategy, potential buyers and deal timetable

DIVESTMENT

- Execute sales process
- Build momentum, maintain flexibility

PHASE I – BUSINESS ASSESSMENT OR QUICKSTRIKE©

Once a business has been identified as non-core, an initial 'QuickStrike©' evaluation will be carried out. QuickStrike© is a fast and thorough stocktake of the target business's performance, core value proposition and strategy. This will focus on key questions such as:

1. Does the value proposition of the business remain valid?
2. Is there a clear growth story?
3. What performance and strategic improvement opportunities exist in the short- and long-term?
4. What issues exist that could hinder or delay a sale?

Finally, we will make a full assessment of the level of sector M&A activity and the competitive landscape in order to validate the industrial logic for a sale and determine how best to maximise value.

PHASE II – PERFORMANCE IMPROVEMENT AND CARVE-OUT ASSESSMENT

Building on the insight developed in Phase One and the industrial logic validated, detailed performance improvement plans will be created. Readily identified 'quick-win' improvements can be implemented immediately, bolstering the value of the business prior to the launch of a sale process.

For longer term improvement opportunities that require more management attention, a road map to delivering the improvements can be developed. These can either be implemented prior to sale or incorporated into management business plans and sold as part of the upside to the new owner of the business, making the asset a more attractive prospect and the process smoother and quicker.

In conjunction with the value creation activities, a carve-out assessment will be carried out to identify group dependencies, potential standalone costs and formulate a detailed action plan to de-couple the target from the group.

PHASE III & IV – EXIT READINESS AND DIVESTMENT

Finally, before launching the sale process, a full review of financial, legal tax and HR related items will be undertaken. This will identify and address any gaps, avoid surprises and ensure momentum is maintained throughout the sale process.

The sale process strategy will then be confirmed, including assessment of potential buyers and deal timetable, followed by the launch of the sale process.

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HOW WE CAN HELP

Through our Divestment Preparation Programme we have helped numerous clients increase the value of their businesses and build confidence in delivering successful, faster and more outcome-certain divestment processes.

Should you be undergoing or considering a portfolio review and wish to learn more about how our Divestment Preparation Programme can deliver value, please do not hesitate to get in touch. Please find contact details of our senior corporate team below.

FOR MORE INFORMATION, PLEASE GET IN TOUCH:

Nick Wood
Managing Director, London
M: +44 7976 851 379
E: nwood@alixpartners.com

Graeme Smith
Managing Director, London
M: +44 7932 158 222
E: gsmith@alixpartners.com

Michael Wabnitz
Managing Director, Munich
M +49 172 8 55 59 66
E: mwabnitz@alixpartners.com

Tom Paterson
Director, London
M: +44 7584 149 328
E: tpaterson@alixpartners.com

Azeem Ahmed
Director, London
M +44 7920 156 936
E: aahmed@alixpartners.com

Craig Rachel
Director, London
M +44 7919128328
E: crachel@alixpartners.com

Utsav Patel
Senior Vice President, London
M: +44 7823 402 535
E: upatel@alixpartners.com

ABOUT US

For nearly forty years, AlixPartners has helped businesses around the world respond quickly and decisively to their most critical challenges – circumstances as diverse as urgent performance improvement, accelerated transformation, complex restructuring and risk mitigation.
These are the moments when everything is on the line – a sudden shift in the market, an unexpected performance decline, a time-sensitive deal, a fork-in-the-road decision. But it's not what we do that makes a difference, it's how we do it.
Tackling situations when time is of the essence is part of our DNA – so we adopt an action-oriented approach at all times. We work in small, highly qualified teams with specific industry and functional expertise, and we operate at pace, moving quickly from analysis to implementation. We stand shoulder to shoulder with our clients until the job is done, and only measure our success in terms of the results we deliver.
Our approach enables us to help our clients confront and overcome truly future-defining challenges.
We partner with you to make the right decisions and take the right actions. And we are right by your side. When it really matters.