



# The art of strategic divestment

By Patricia Anslinger, Justin Jenk and Ravi Chanmugam

Divestiture makes sense only as part of a sound, long-term strategy. Before shedding business units, companies must consider all the options, then be willing to constantly review, replenish and trim portfolios as markets change and evolve.

In a punishing economic climate, many companies turn to restructuring as a way to weather the storm. One way to do this, of course, is to slash costs and reduce capital expenditure. A more dramatic step is to sell off business units. This approach is not without risk, however, and in the past, many companies shrank themselves to a level that made them uncompetitive when the economy rebounded. Because 2001 was a record year for corporate divestitures, there is cause for concern that some companies may be making this same mistake.

Companies shed business units for a variety of reasons. For example, Wall Street's demands to improve near-term earnings are relentless, and the temptation to divest as a way to raise cash, to maintain dividends, fund critical capital expenditure and pay down debt is hard to resist.

However, divestiture makes sense only as part of a sound, long-term strategy in which the company constantly reviews, replenishes and trims its portfolio as its markets change and evolve. That is very different from selling a poorly performing unit at an unattractive valuation, which is what happens most commonly in difficult economic times.

Is there a smarter way to approach restructuring? Accenture believes there are a number of alternative options. What is required, first and foremost, is a willingness to consider all the

possibilities: to look at ways to radically redesign a business without divesting; to put all of the business units—including what seems to be the core business—on the table as possible candidates for divestiture; and, finally, when the decision is made to shed a particular business unit, to think of innovative ways to prepare it for sale. By examining all of the alternatives to selling the obvious candidates outright, a company can increase not only its options but its chances of success as well.

### Asking the right questions

Companies thinking about a restructuring plan that might include divestiture would do well to keep the following questions in mind.

*Rather than getting rid of an entire business unit, can you disassemble its operations and outsource the costly or cumbersome functions?*

This approach goes beyond traditional subcontracting, asset disposal and conventional outsourcing. It means changing the way you do business, from top to bottom, perhaps outsourcing core functions that traditionally have been considered far too important to be performed out of house. But a company doesn't necessarily need to own an asset to control it.

In the spring of 2000, J Sainsbury, the second largest grocery retailer in the United Kingdom, found its premier position slipping as several forces chipped away at its performance. Costs were substantially out of line with those of industry leaders, and profits had dropped 40 percent over the three previous years.

Sainsbury embarked on a business transformation program that included extending and refurbishing the store network and reinventing the company's supply chain. It also involved outsourcing all of the company's IT

with a view to immediate cost reductions of nearly 20 percent and the replatforming of all existing IT systems to support the program. Two years into the program, the group has announced the fourth consecutive half-year of improved underlying profits. The annual IT operational savings have been fully realized, and the replatforming program remains firmly on track and within budget.

No aspect of a company's operations is more important than customer relations, a function so sensitive that organizations generally want to keep it under their own watchful eyes. Nonetheless, in early 2002, AT&T Consumer turned to an outside partner to help transform its sales and customer care unit, including telemarketing.

The arrangement is an example of what's known as "co-sourcing," to distinguish it from outsourcing. In this case, the partner provides AT&T with technology to increase self-service, as well as innovative customer relationship management expertise.

Unlike most outsourcing arrangements, under this contract, AT&T employees will continue to perform key functions and will remain AT&T employees, while working side by side with the partner's staff and management team to implement the technology and process changes that will improve service and reduce costs. Within five years, AT&T expects to cut customer service costs in half.

*Have you pushed technology as far as you can, or are there still new ways it can cut costs, increase productivity and improve operations?*

Cost cutting has been so aggressive and pervasive at times that it is difficult to imagine that more savings can be realized. But emerging technology may offer new ways to shrink costs even further.

Consider the case of one of the world's largest oil producers, which used reverse auctions to push down its procurement costs. In the past, the purchasing department had solicited bids from a group of suppliers. To increase competition and reduce the prices it had to pay, the department started using a software program that enabled it to put out its procurement specifications to qualified suppliers over the Internet. The company set a deadline for bids. Because the system was transparent, all of the suppliers could see and study their competitors' bids during the bidding process. Generally, a rush of very low bids appeared at the end of the time period, and the company got its materials for 20 percent less than it had been accustomed to paying.

*Do you have all the candidates on the table, not just the dogs?*

Too often, companies consider only the lame and the scruffy when thinking about which units to dispose of. Instead, they should put all of their businesses up for consideration and subject them to a couple of tests.

- If you didn't already own this business, would you buy it at the current market price? If the answer is no, why are you still in this business?
- Is this business so essential to your other businesses that you can't eliminate it without damage to the bottom line?

Like many other brewing companies, Canada's Labatt owned an entertainment business—in this case, a baseball team, the Toronto Blue Jays. Labatt and its partners bought the team for \$7 million in 1976, because among other things, ball teams and ballparks are useful tools for selling beer. But in 2000, when the value of baseball teams had soared into the hundreds of millions of dollars, Labatt, which by

then had merged with Belgium's Interbrew, decided that the time was right to sell its controlling interest in the team. So it sold the Blue Jays to Rogers Communications for \$112 million, a capital gain of 1,600 percent. Labatt retained a 20 percent interest in the franchise, along with marketing rights. This includes pouring rights at the team's home field and title sponsorship of Blue Jays broadcasts.

AT&T went through an agonizing reappraisal of its wireless operations (along with its broadband, consumer and business divisions). Despite the initial conviction of many in the company that there were essential synergies between AT&T Wireless and the rest of AT&T, it turned out that Wireless was, in fact, separable. It was not significantly absorbed into the company's other operations, such as long distance and business services.

Moreover, it turned out that customers didn't always value getting all their communications services—wireless and wired—from one provider, as the company had assumed. While many have questioned AT&T's overall strategy during the past several years, the company nonetheless made a tough and rational decision when it decided to spin off its wireless division, which became a separate company in July 2001. Both AT&T and AT&T Wireless retain some of the strategic benefits they had when they were parts of the same company, such as the marketing and brand relationships. In addition, agents for each company refer customers to the other, and the two companies share support services.

*Is it possible that the business you thought of as core is your least important one?*

This is such a radical thought that it naturally meets a lot of resistance. But

a company's greatest asset may not, in fact, be the obvious one. Indeed, there may be a hidden asset that could be the foundation on which a stronger business could be built. The evolution of Centrica illustrates the point dramatically. In 1997, the venerable British Gas was split into two entities: BG, an energy company, and Centrica, which retained the British Gas brand and the business of selling natural gas to 67 percent of the homes in the United Kingdom.

Dominating the UK natural gas business has a couple of drawbacks, however. Keeping millions of houses connected through thousands of miles of pipeline and in order is enormously expensive. What's more, the business is mature, growing no faster than its customers' minimally increasing need for home heating and cooking fuel.

Centrica recognized that it had a valuable hidden asset, albeit one much softer than plants and pipelines: the names, addresses, demographic profiles and credit records of the millions of British households served by its pipelines.

For the past five years, Centrica has built and acquired the capability to meet various needs of these households. The company has concentrated on selling to those households services for which demand is booming, such as financial services (through its Goldfish subsidiary) and roadside assistance (through The Automobile Association). By logging on to a single website, [house.co.uk](http://house.co.uk), customers connect to suppliers of household maintenance and repair services, ranging from plumbing needs to less expensive mortgages.

As a result, Centrica's profits rose from £175 million (\$287 million) in

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1997 to £679 million (\$987 million) in 2001. During the same, period its stock price outperformed the FTSE index by 183 percent.

*If you do decide to get out of a business, what's the best way to exit?*

There are a number of options that a company should consider. Spinning off all or part of the business as an IPO or selling all or part of the business to someone else are the most common approaches. However, a company alternatively can create a joint venture with a competitor, swap assets with another industry player or even find an unconventional buyer.

Consider the example of two giant pharmaceutical companies: Novartis and AstraZeneca. Both are leaders in research and boast a range of profitable drugs. Although they were eager to divest their agribusiness and agrochemical divisions, respectively, and concentrate on their core businesses, they decided not to dispose of these units separately. Instead, they agreed in 1999 to spin these divisions off simultaneously into a single entity named Syngenta, which would have the size and growth potential to attract institutional investors, go public and compete with the likes of Monsanto.

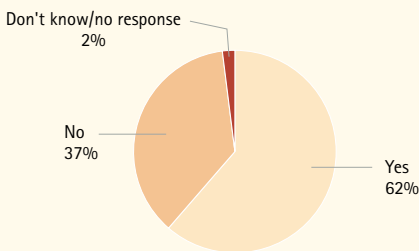
By 2001, Syngenta had established itself as the world's leading maker of agricultural pesticides and anti-fungal products to protect crops and the No. 3 producer of high-value seeds. The company recorded sales of \$6.3 billion that year and a net income of \$223 million. As the Syngenta experience illustrates, individual divisions may be worth more when they are spun off and recombined with other groups.

Siemens and Motorola are considering (as of the time we went to press) attempting a similar leap in value

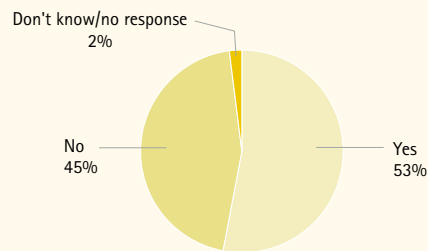
## From the executive suite

In a study conducted with 100 senior-level executives at US Fortune 1,000 companies, we found that more than half of the companies surveyed have been active in divestments in the last 18 months. Although there are a number of drivers that lead companies to divest, the primary success factor that they are seeking is to realize some strategic objective, such as reducing debt and minimizing any disruption to the current business.

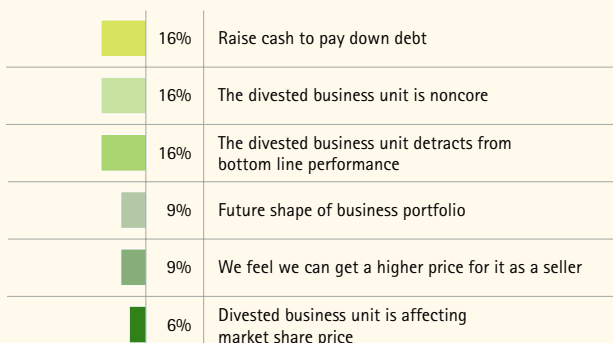
Does your company engage in divestments?



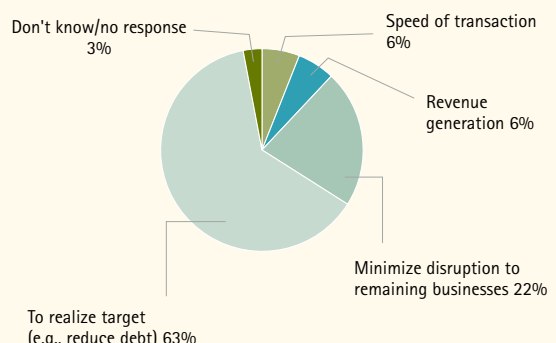
Have you sold any business units over the last 18 months?



What are your primary reasons for conducting your current divestments? (Multiple responses were accepted.)



What is the most important success factor for your divestitures?



SOURCE: ACCENTURE/WIRTHLIN WORLDWIDE SURVEY

through a swap. Although Siemens is a leader in telephony networks and switching, it is not as strong in the consumer side of the mobile telephone business. It has therefore proposed giving its handset manufacturing business to Motorola in exchange for access to Motorola's valuable wireless network infrastructure. Motorola would gain as well, boosting its share of the handset market to 25 percent, second to industry leader Nokia's 37 percent.

Divestiture that creates a joint venture is another possibility. Strategic assets are spun off from each partner to form a jointly owned company that is in a stronger, more competitive position. This is a particularly appealing approach in the fast-paced industries that have constant technology innovations, because the venture will have the autonomy to make decisions quickly, the ability to move more nimbly and the freedom to pursue new ideas that will not put the core business at risk.

#### **A creative choice**

When a divestiture is forced upon the owner—when it is mandated for antitrust reasons, for example—it pays to be creative in choosing a potential buyer. It is often possible to get a good valuation without strengthening a competitor's hand. Belgium's Interbrew, the owner of Beck's, Labatt and Stella Artois, among other beers, found itself in a difficult position in the UK market in 2000. To avoid possible antitrust action, Interbrew had to divest itself of its Carling brand.

A number of European rivals were eager to buy Carling, but the purchase would have strengthened their relative position in the English beer market, which was clearly worrisome from Interbrew's perspective.

So Interbrew sold Carling to Coors, a power in the United States but a neophyte in Europe and therefore less of a competitive threat.

Once a business unit is tagged for possible sale, the temptation is to starve it of capital that is needed elsewhere, cut its marketing budget, reassign its best managers to other divisions and, in general, treat it like a poor relative. The problem with that strategy, of course, is that it is likely to reduce the divestment candidate's market value. Instead, the company should build the unit up the way a private equity firm prepares a company for sale: invest capital to grow its market share, offer management strong incentives tied to the right metrics and separate the business from the other business units. In short, keep it growing and keep it strong for the short to medium term.

For the next few years, many companies will give far more thought to divestitures than they did in the late 1990s. Disposing of a business unit is not always the answer. Sometimes a troubled, costly subsidiary can be restored to health with emerging technology. Often, it is not an entire business that has to be divested but simply one or more of its functions.

When divestiture of an entire business is necessary, it can take many forms. Wise companies will avoid the knee-jerk reaction of disposing of the "obvious" candidates before considering all the possibilities.

In the end, divestiture need not be cause for depression, an admission of defeat. Indeed, a well-done restructuring that includes divestiture can be as great a victory for management and shareholders as a well-done acquisition. ■

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