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Company Spinoffs Help Fill U.S. Market's IPO Void: ECM Watch

By Yiqin Shen / Bloomberg News / March 22, 2022

A flow of corporate spinoffs is providing some much-needed activity in U.S. equity capital markets, as companies look to slim down or unlock value in parts of their businesses.

XPO Logistics, Inc. (XPO) said this month that it plans to split its freight brokerage and North American trucking operations into two publicly traded companies. It's one of at least three companies that have announced similar initiatives this year, building on a burgeoning move toward corporate breakups. The trend emerged late in 2021, underpinned by deals from conglomerates including **General Electric Co. (GE)** and **Johnson & Johnson (JNJ)**.

The prospective transactions are shaping up as a rare source of new share sales in the U.S. An extended stretch of market volatility is quashing companies' appetite for initial public listings, leading to the longest drought in more than a decade.

The trend also comes against a backdrop of soaring long-term interest rates, with Federal Reserve officials signaling they could start tightening policy more aggressively to battle elevated inflation. So for companies, the rising cost of capital is a major part of the decision-making process that is making spinoffs more appealing.

"Separated companies get independence to tap capital markets to raise funds on their own terms, leveraging on their own capabilities, without requiring rationing for capital raised by parents," said Jim Osman, chief executive officer of The Edge Consulting Group. "Further, pure-play companies receive higher premiums over conglomerates."

Of course, as with other types of corporate transactions, not all carve-out businesses will take off in the stock market.

The Bloomberg U.S. Spin-off Index , which tracks 19 equities that were spun off from larger corporations within the past three years, has trailed the S&P 500 Index since May 2019.

Among those deals, **Concentrix Corp. (CNXC)** led gainers over the past year, advancing about 50%. Meanwhile, **Vimeo, Inc. (VMEO)** led decliners, losing around 75%.

But the performance of XPO shares shows how the market can embrace a streamlined corporate story: The stock surged the past two weeks and is trading at the highest since early December.

Analysts have touted the company's move as helping it focus on operational efficiency and capital allocation. XPO could be valued at least 65% to 67% higher if management successfully creates two companies that trade closer to pure-play peers, according to Bloomberg Intelligence.

Meanwhile, activist investors are also advocating for corporate breakups in candidates they consider ripe for such transactions. In one example, Alta Fox Capital Management has urged toymaker **Hasbro, Inc. (HAS)** to spin off its Wizards of the Coast playing card and digital-gaming business.

The investor called the unit a "hidden gem" and said a spinoff would simplify Hasbro's corporate structure and unlock additional value in the firm's shares. Hasbro's shares have declined about 12% this year, outpacing the roughly 5% drop in the S&P 500.

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