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Kellogg's Spinoffs May Create Value Out of Thin Air: ECM Watch

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Spinoffs are meant to unlock unrecognized value, but a plan by Kellogg Co. might be taking that strategy to new levels.

Kellogg's core business -- or what's left of it after a pair of spinoffs announced on Tuesday -- could be worth more than the current value of the combined entity, according to a research firm that specializes in such transactions. The separation plan is just the latest example of large conglomerates addressing the pain of slower growth and higher interest rates that have weighed on stocks all year.

The company's global snacking business could earn a higher valuation that's closer to peer Mondelez International Inc. after separating from Kellogg's North American cereal and plant-based foods units, analysts at The Edge Consulting Group wrote in a note on Tuesday. Based on Mondelez's valuation of 3.5x enterprise value on its 2021 sales, the remaining snacks business would be worth about $40 billion -- at least $10 billion above current levels.

"That is a tremendous value unlock for the RemainCo, with the other two businesses literally to be received for free," according to the note. Others on Wall Street were also positive about the company's outlook after the announcement.

Of course, it's never quite that easy. Kellogg wants to complete the transactions by the end of 2023, meaning there's plenty of time for shares to whipsaw along with the rest of the market. Shares rose 2% Tuesday compared with a 2.5% climb in the S&P 500 Index.

"While investors generally applaud splits, the enthusiasm tends to fade after the knee-jerk rally given the amount of time required to execute the separation and the elevated costs associated with the split," analysts at Vital Knowledge wrote in a note.

General Electric Co. and AT&T Inc. both initially jumped after their spinoff announcements, but those rallies quickly faded, Vital Knowledge noted.

Spinoffs are becoming a more attractive option for highly levered companies as boardrooms adjust to the new more expensive credit environment. Kellogg, which has more than $7 billion of total debt, said on Tuesday that management is committed to maintaining an investment-grade credit rating for the global snacking business after the three-way split.

"Companies will need to spinoff underperforming segments to create value and stay competitive in this slower growth period we are about to experience," The Edge founder Jim Osman said in an interview. "Historically we have seen this happen. Investors should focus on these situations as a means of providing a return to their portfolios as growth and value stall."

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