



*The ability to see into the future – a decent skill if you have it...*

"I have seen various sell-side reports that claim to analyze this space, but I have not come across anything as consistent in approach across geographies as The Edge."

*- Chand Sooran, Value Investor, New York City*

## THE INVESTOR'S EDGE

Biweekly Education Saving You Time & Money in Investing

### What is a Spinoff?

I used to say to people, "I don't know what is going to happen. I don't have a crystal ball." It was probably the right thing to say 10 years ago, but today, our client partners and your investors (if you have any) are essentially paying you to have that skill and expect it! Quite a feat. We will return to this a little later.

In the meantime, this newsletter goes out to tens of thousands of people, and to be honest, I don't really know who most of you are. However, my last newsletter touched on why you need Spinoffs in your portfolio. On the back of that, I received many emails asking if I could concisely explain what a Spinoff is, so I'd thought I'd lead this week with exactly that.

***A Spinoff is the creation of an independent company through the distribution of new shares of an existing business or division of a parent company.***

"Nice one, Jim," I hear you say, "but what does that really mean to me as an investor?" Well, there are many angles to consider. Here are three of the most important.

- 1. Definition** – This is the basis of getting these situations right. I will tell you what a Spinoff is not. It's not a sale, it's not an IPO and it's not a divestiture within a business. A true Spinoff occurs when you, as the shareholder of the company, receive shares of another company by holding that parent company. A true Spinoff occurs by distribution. Just a side note: the press has forever got the definition wrong. Just look a little closer when they write about it. In my opinion, it is essential that it happens this way as a means for starting an investigation into a potential investment. **Receiving shares in a stock whether you want them or not throws up all sorts of issues to think about.** I will save the rest of the reasons why Spinoffs can be good sources of investments for another time, but this is one of the most important that people rarely mention. Also remember, it can go by the name of breakup and divestiture, but a "true" Spinoff is what has been described. It must be by distribution.



*Erm... incorrect breakup...*

- 2. Dates** – This is key. **When a Spinoff is announced, it can take up to 18 months for the event to materialise.** Interesting to note, our 14-year Spinoff Study with Deloitte ([available for purchase](#)) shows that companies who prepare more than six months ahead of the Spinoff produce 2x better returns. Post-announcement it will often go very quiet. Unless you closely track that Spinoff, or alternatively have someone to track it for you, you will more than likely miss it. Along the journey, you should be watching for new Form 10 filings, updates in earnings about performance and continually updating your model with the financials produced. If you have managed to do all that, then make sure you hold the parent shares before that important “record date.” That will ensure you get the Spinoff entity. Miss that and you maybe be able to pick up the shares in the when-issued market or when it goes regular trading. I’ve always been a fan of pre-spin. You never know what happens.
- 3. Investable Opportunity** – This is the area where you should be doing your homework. Here is my best tip: **Find out first why the company is doing the Spinoff.** This is the part most analysts miss. They decide to jump on the numbers. The real key to starting any analysis is this precise point. You will get the signposts on where to go to lead your investigation. It’s what we do here. Sometimes the reason is quite generic. Common generic reasons include, “We believe the companies will function better on their own,” and “Independence is needed to realise each individual company value.” Again, read between the lines and you will discover more. You will need to analyse pre-and post-spin companies to see if there is any value. Should you buy the stock before it spins or after? Furthermore, consider the shareholders and management. Who are the major shareholders and why do they hold the stock? Who are the management specifically and how are they incentivised? Have they been buying any shares recently? Depending on their amount and how much they already own, buying could be a good sign. Finally, consider the index that the names are about to go in or come out of. Many larger index funds cannot hold small names and they will need to be sold, putting pressure on many Spinoffs in their early days. Consequently, when companies are big enough to go into indices, the opposite happens. Quantify all of this.

Lastly, back to the crystal ball thing. Look, the more I do this, the more I try to look at clues in companies which will give me the insight into what they will become. They can and usually are hidden within the numbers and transcripts. Spinoffs are great hunting grounds and they are unlike IPOs because no investment bank needs to push the stock. This makes it more interesting for me, anyway. Ultimately, you will gather a picture of what can develop. Remember, most if not all the information you need is out there. Just do the digging to find it.

I trust this has given you good insight about Spinoffs. There is much more to it and, again, it’s what we do. There are about 35-40 larger Spinoffs per year. If you feel like you are missing out on this niche part of the market that is difficult to analyse and follow, fill out the webform and let’s talk. We have products for the small and large investor. I would love to hear from you. Alternatively, send me a direct email below.

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THE EDGE INVESTMENT IDEAS YOU CAN TRUST						
SPINOFF REPORT		SPECIAL SITUATIONS		STRESSED CREDIT		
	2014 Q3 AEO	2014 Q4 AMZN	2015 Q1 INDV	2015 Q2 PYPL	2015 Q3 ADS	2015 Q4 HPE
Ticker	AEO US Equity	AMZN US Equity	INDV US Equity	PYPL US Equity	ADS GT Equity	HPE US Equity
Company Logo						
What Was the Situation?	The arrival of retail turnaround specialist Jay Schottenstein and an accumulation of 22.5% of insider buying gave confidence to a promising redirection of a significantly underperforming company.	The Edge saw hidden value in the potential Spinoff of Amazon Web Services (AWS) when the market was quiet. The segment continued to be the primary driver for consistent revenue growth.	A Spinoff from fleckit: Benchmark in Dec. 2014. The Edge urged investors to ignore the Parent and focus on INDV for its insider buying ahead of the Spin, strong management, new products, and likelihood of a takeover.	The Edge highlighted the benefits of eBay's move to Spinoff its digital payments arm PayPal in July 2015 to clean its portfolio of services and create a more focused marketplace business.	ADS reshuffled its management, introduced a new product line, performed a strategic review, and had activist investors backing a strong balance sheet in its multi-catalyst turnaround story.	Following its Spinoff from HP, Inc. in Oct. 2015, HPE went on to perform two Reverse Merger Trust Splits of the Software (DIX) and Enterprise (IMGP) segments in 2017.
Portfolio Return (%)	37%	93%	55%	36%	26%	48%
Index Return (%)	-4%	-7%	-5%	-1%	-7%	25%

  

THE EDGE INVESTMENT IDEAS YOU CAN TRUST						
SPINOFF REPORT		SPECIAL SITUATIONS		STRESSED CREDIT		
	2016 Q1 RR <th>2016 Q2 BCO <th>2016 Q3 MET <th>2016 Q4 ARIC <th>2017 Q1 DATA <th>2017 Q2 SCAB </th></th></th></th></th>	2016 Q2 BCO <th>2016 Q3 MET <th>2016 Q4 ARIC <th>2017 Q1 DATA <th>2017 Q2 SCAB </th></th></th></th>	2016 Q3 MET <th>2016 Q4 ARIC <th>2017 Q1 DATA <th>2017 Q2 SCAB </th></th></th>	2016 Q4 ARIC <th>2017 Q1 DATA <th>2017 Q2 SCAB </th></th>	2017 Q1 DATA <th>2017 Q2 SCAB </th>	2017 Q2 SCAB
Ticker	RR/ US Equity	BCO US Equity	MET US Equity	ARIC US Equity	DATA US Equity	SCAB US Equity
Company Logo						
What Was the Situation?	A management restructuring coupled with activist involvement and potential Spinoffs, Rolls Royce already had negatives priced in and a strong position for a turnaround in the European automotive space.	A strong management, led by turnaround specialist and new (as of June 2016) CEO Doug Pertz, is focused on improving operational efficiencies and expanding its high value and technology driven services.	A Special Situation turned Spinoff. The Edge highlighted the potential benefits of separating its US retail unit in April 2016. The Spinoff of BrightHouse Financial was subsequently announced that following July.	The market struggled to follow the split, as Alcoa (Parent) transformed into Arconic while the Spinoff took the Parent's name and ticker. Heavy insider buying coupled with strong fundamentals produced a solid investment.	CEO Adam Selipsky (who grew ZOWI from scratch) took over the undervalued tech company in Sep. 2016, and set to improving DATA's business model, cloud subscription system, and long-term takeover potential.	Europe's largest private forest owner is a strong takeover target due to its high margin profile, diverse timber product range, and wide geographic reach. The new management is led by Forest segment veteran Ulf Larsson.
Portfolio Return (%)	22%	87%	41%	49%	68%	50%
Index Return (%)	14%	13%	39%	10%	29%	3%

"Being clients for over 5 years and given we've over \$25bn AUM and 20 analysts, [The Edge is] in an extremely rare position of being the only external advisor we trust."  
- Portfolio Manager, \$25bn NYC Investment Management Firm

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"I am a big fan of the Spinoff Report and The Edge team. I like their work because of their differentiated research – they quantify the impact of technical selling with the Spinoff, which I greatly appreciate."

- Madan Gopal, Former Analyst, \$7bn NYC Investment Fund

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