KPMG THE EDGE

Dissecting public carve-outs:

What are the dynamics of a successful transaction?

KPMG International

home.kpmg/carveouts

October 2020

The Edge was established to provide actionable investments in public markets not normally seen by the mainstream. The company analyzes investment opportunities due to corporate change and produces research for global Money Managers and Activists.

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Preface

As markets begin to recover following the COVID-19 in all instances crisis, many businesses will be considering new strategies for structuring their operations and their portfolios. Their focus will be on efforts to reinforce their balance sheets against future market disruptions and economic anomalies, reduce costs and optimize their operational efficiency. With economic trends and regulatory changes evolving rapidly, and product lifecycles increasingly shortened, leaders will need to aim for agility in their strategic portfolios. In addition, the ESG agenda is increasingly causing businesses to reconsider their portfolios by focusing more strongly on sustainability. A carve-out — in which a company either floats part of the business on the public market or divests it in a sale — may be an attractive option for companies that want to restructure, refocus on core competencies, or adjust to major regulatory policy changes in certain sectors of the economy.

In this paper, KPMG and the Edge professionals have undertaken detailed empirical analysis of the results of 45 public capital market carve-outs that have taken place in jurisdictions, including the US, Europe, UK and Australia over the past 5 years. This report's focus is on public carve-outs rather than private divestments or trade sales. Many published studies discuss the technical, accounting and regulatory requirements of carve-outs, but few have analyzed the potential financial and performance outcomes and other aspects of these transactions.

The results of our joint analysis reveal five key considerations that management and boards need to think about carefully if they are considering a carve-out within their own business. We hope you find this information useful as you plan your own company's future.

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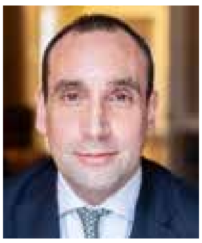

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Carve-out transactions in a more volatile environment

Carve-out types and approaches in a world full of risk

Before the 2020 coronavirus outbreak, the increase of carve-outs had become a notable development in the corporate transaction landscape. Some of these transactions were private divestitures, but many created new public companies, involving some of the world's foremost corporate groups across business sectors.

Several factors drove this growth. The global economy had been showing signs of a potential slow-down, while the business environment had become more uncertain and volatile amid the threat of potential trade wars, especially between the US and China. Meanwhile, the prospect of Brexit introduced significant unpredictability into operations and supply chains in the UK and EU.

Then came the COVID-19 crisis. Product markets effectively shut down as businesses looked for survival strategies. As countries and companies begin to reopen, profound economic impacts are ongoing and may prove long-lasting. Consequently, as economies gradually recover and business returns to a more familiar footing, organizations will be more focused than ever on achieving optimal corporate structures that inject cash, drive sustainable cost efficiencies, improve risk profiles and refocus on core competencies.

Digital transformation is also prompting organizations to focus considerable effort on optimizing their core business with the help of artificial intelligence (AI), intelligent agents (i.e. chatbots), robotics and advanced analytics. With less capital available to invest in non-core functions, the strategic argument to separate from them only grows stronger.

In addition, in recent years, activist investors have been quick to pressure organizations to maximize value creation over other goals. Often these investors encourage a parent group to spin off a part of its business, creating a new, independent entity with its own corporate rationale.

As a result of all these circumstances working together, carve-outs will remain an important business strategy for many companies in the coming months and years.

Spin-offs vs. IPOs vs. Hybrid

Public carve-outs generally take two principal forms — spin-offs and Initial Public Offerings (IPOs). Some transactions, described as 'Hybrids', combine elements of spin-offs and IPOs (e.g. a spin-off with a capital increase at listing date or an IPO immediately subsequent to a non-public spin-off).

In a spin-off, shares in the carve-out entity ('Listco') are distributed to current shareholders of the parent on a pro-rata basis as a 'dividend in kind.' A spin-off does not generate new capital for the business; instead, it redistributes capital to the parent company's existing shareholders by issuing shares in Listco with the potential to create new value. The listing process and requirements for the newly distributed shares correspond to those of a traditional IPO. One of the chief attractions of spin-offs is that they offer certainty, given they are not subject to market risk. Once approved by shareholders, Listco will have its own leadership and can proceed independently.

On the date of spin-off, the parent company's shareholder structure will be unaltered. Shareholders retain their shares in the parent company and receive newly issued shares in Listco on a previously determined share exchange ratio. At the spin-off date, shareholders may decide either to keep the newly issued shares in Listco or divest them. The immediate divesture of the newly issued shares is commonly referred to as a 'flowback'.

Though a spin-off does not generate cash for the parent company, it does subject the parent company as well as its existing shareholders and potential new investors to flowback risk. Without a strong investor demand to take up the shares, high flowbacks result in a decrease in value of the newly issued public stocks at the expense of the shareholders. Thus, throughout the going-public process, conveying a successful equity story as part of communications to the capital markets is as important for spin-offs as it is for traditional IPOs.

Carve-out IPOs, by contrast, create a potentially significant capital injection for Listco or its parent entity. IPOs' potentially large returns are balanced by their dependence on prevailing market conditions. Depending on the transaction objectives and capital structure objectives, IPOs consist of primary and/or secondary offerings.

With primary offerings, the proceeds are directed to the carve-out business — that is, Listco, which is selling its own shares. In this, the classic IPO case, Listco uses the capital market to generate cash and put equity on its balance sheet. Primary offer IPOs result in an overall capital increase with the original parent retaining its existing equity ownership in Listco, albeit diluted by the issue of additional shares to new investors.

"Carve-outs like IPOs and spin-offs follow the idea of creating an even more successful company in a separated set-up. Carve-outs allow companies to sharpen their business strategy in terms of customers, markets, regions and products as well as to optimize their processes and cost position. If done properly, carve-outs will add value to customers, employees and owners."

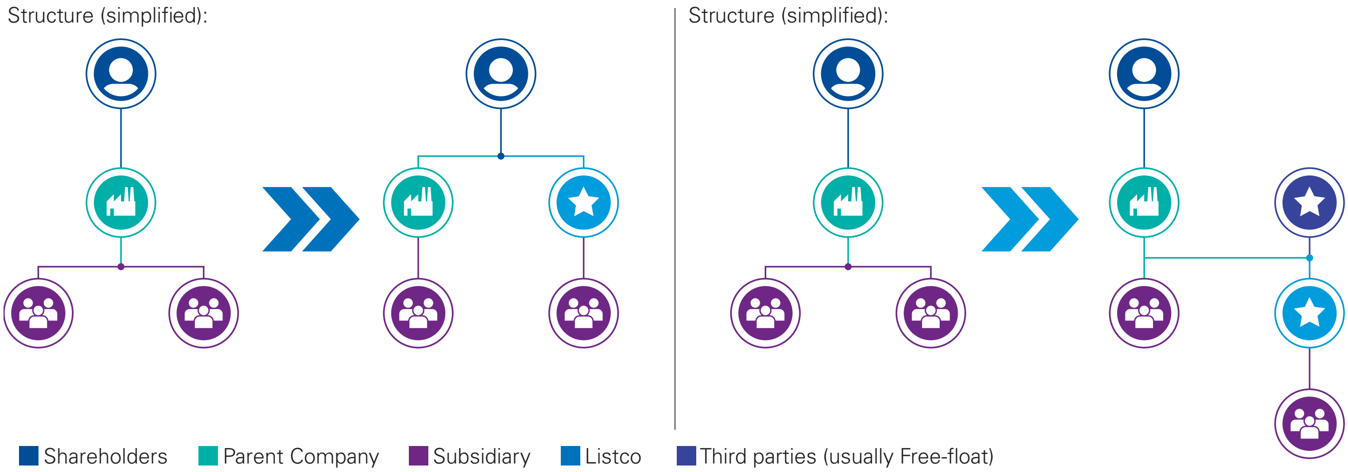
— Dr. Jürgen M. Wagner,
Siemens AG, Head of Accounting, Reporting and Controlling

In contrast, secondary offerings constitute a sale of (a majority or minority of) newly listed shares of Listco by the parent company with the parent receiving cash in return. Secondary offerings — in which the parent company sells a majority of its shares (up to 100 percent) or a minority stake (below 50 percent) in the carve-out business — are thus a divesture of the carve-out business in much the same way as a spin-off. The majority of carve-out IPOs on global capital markets are usually conducted as secondary transactions, reflecting the divesting nature of strategic portfolio realignments as triggers for the carve-out.

To maximize proceeds, selling parent companies often conduct 'dual track processes' by weighing expected capital market proceeds against potential M&A volume gains for the carve-out business. A sound equity story, value-driving capital market communications through roadshows, and stakeholder management in alignment with the corresponding underwriters are all essential to maximize investor demand for the newly issued shares.

The basic structural distinction between a spin-off and a carve-out IPO is illustrated below:

Spin-off	Carve-out IPO



Spin-off

- Shareholders of a parent company receive shares of a subsidiary company by way of a **spin-off** ('dividend in-kind')
- The newly created shares in Listco are virtually 'deposited in the securities account' for the shareholders

Carve-out IPO

- Shares (majority or minority stake) of a subsidiary company are sold **to new investors** through an initial public offering (IPO)
- The parent company (secondary offering) and/or Listco (primary offering) generate IPO proceeds

Complex accounting and auditing requirements

Whether resulting from an IPO or a spin-off, the carve-out business must include its financial track record in the prospectus — and pulling the required financial statements together is often a complex undertaking. Pre-transaction, the proposed carve-out business is not a legal group or even a stand-alone division. Its operations, revenues and costs depend on a host of shared services and service level agreements with parent — provided functions, such as IT, HR, legal, procurement and marketing. Unbundling these relationships and defining the parameters of a transaction requires significant judgment. To make matters more complex, some services may need to continue under a Transitional Service Agreement (TSA) for a defined period post-transaction.

Historical financial information about the legal entity (i.e. NewCo) or the existing group is unlikely to be an adequate representation of the economic activities of the carve-out business. In these circumstances, financial statements that essentially reflect the carve-out's historic cost of doing business are needed. What's more, determining the carve-out parameters is a critical early stage in the preparation of the required financial information. The objective is to present aggregated financial information of components that have not in the past represented a reporting entity; rather, they reflect a true and fair view of the historic economic situation of the carve-out business in accordance with the Accounting GAAP of the relevant jurisdiction.

For public market transactions, carve-out financial statements covering a minimum period prescribed by regulation must be published in the prospectus. These financial statements must be accompanied by a full audit opinion (confirming true and fair view) and be compliant with specific accounting standards in the jurisdiction of the placement (i.e. IFRS within the European Union).

A simpler private 'basis of preparation' audit opinion, where an auditor gives a limited opinion based on accounting principles for a special purpose, is usually sufficient for private carve-out transactions in M&A markets.

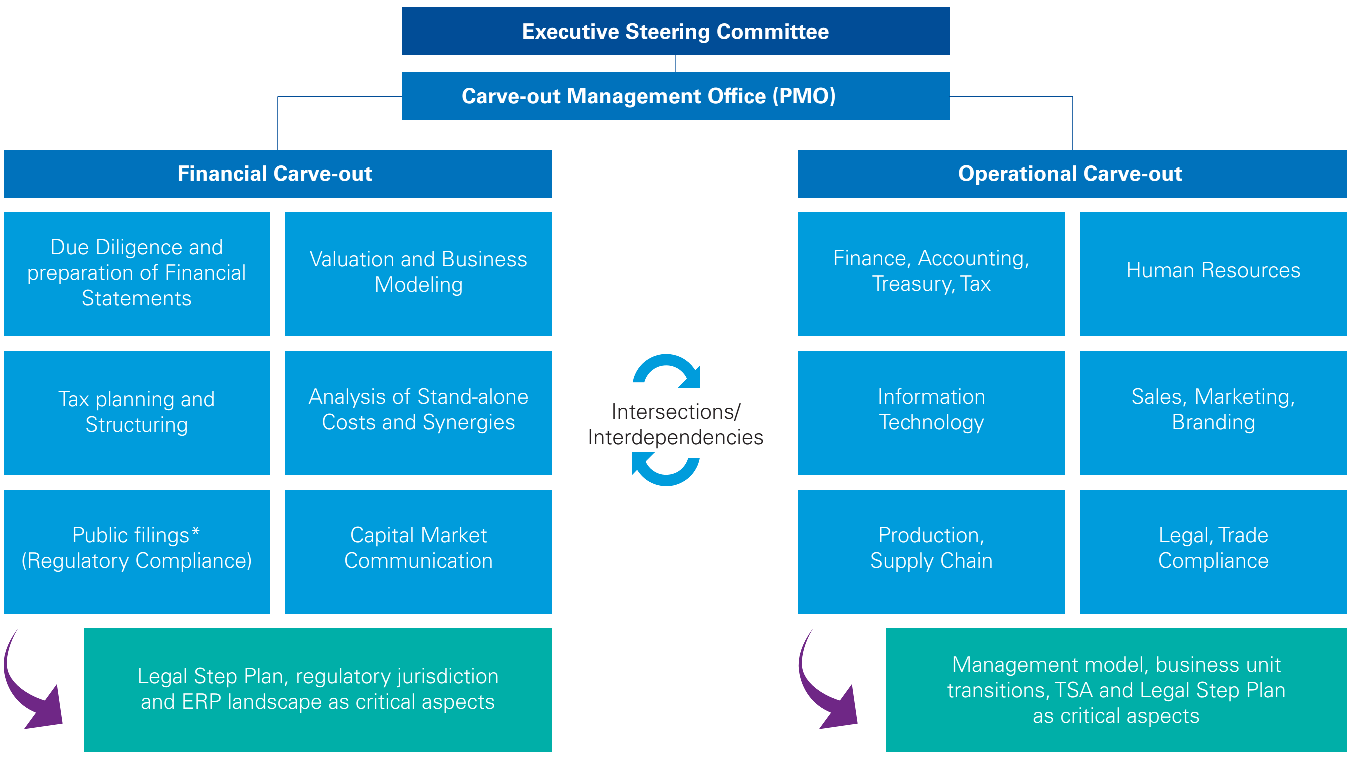
Multitude of stakeholders and project management challenges

Carve-out projects are usually large scale, highly complicated projects to manage. Several interdependent workstreams are in play, as illustrated in the graphic below. The first major workstream is the operational carve-out, where the focus is to disentangle the carve-out business and appropriate administrative functions. A sound separation process ensures the highest degree of operational and functional stand-alone readiness, which is an important measure for investors and the market.

Transaction financials, another major workstream, should accurately reflect the historical financial position of the carve-out business and meet all reporting requirements, both for the listing process as well as for equity story purposes. Both pillars are highly interdependent and together form the foundation of the restructuring. Towards the end of the process they are usually linked via a legal step plan, to ensure a proper cutover from a legal and tax perspective. Stakeholders across these major pillars, or workstreams, include companies' managements and functional boards as well as their lawyers; investment banks serving as underwriters; underwriters' counsels; auditors; experts in accounting, capital markets, and valuations; management consultants; IT consultants; public relations professionals; regulatory approval bodies; and the relevant stock exchanges.

These complexities and interdependencies make a compelling case for a comprehensive project management office that steers, monitors, and manages the overall process. Specific IPO advisors can guide the company's leaders in addressing project management challenges across the lifecycle.

The following illustration highlights the basic structure of an effective carve-out management, for both spin-offs and IPOs:



Depending on the scale and entanglements of the carve-out business, the PMO structure encompasses multi-level project and steering groups that include all operational and administrative functions. These interdependencies highlight the organizational challenge, scrutiny and stamina needed across the lifecycle of the spin-off or IPO.

Carve-out transaction outcomes: What does the data show?

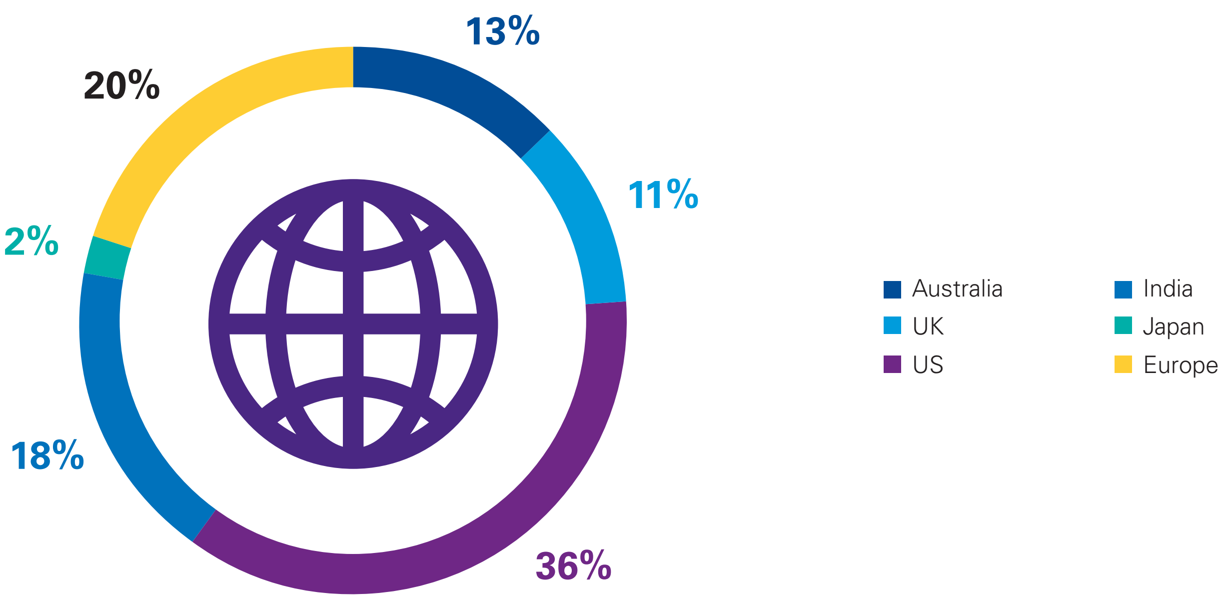
What transactions did we include in our analysis?

Professionals from KPMG and the Edge analyzed 45 public carve-outs that took place in major markets, including the US, Europe, UK, India, Japan and Australia from 2015 to March 2020. About a third of the transactions occurred in the United States. Mainland Europe (mostly Germany and the Netherlands) and India follow with nine and eight transactions, respectively. Selected Australian, UK and Japanese transactions were also considered.

We identified 'significant' transactions based on their revenues or relevance within a jurisdiction or business sector. Consequently, the population in scope mainly covers large-cap transactions, but a few lower and mid-market deals are also included.

The following illustration reflects the geographical breakdown of study participants:

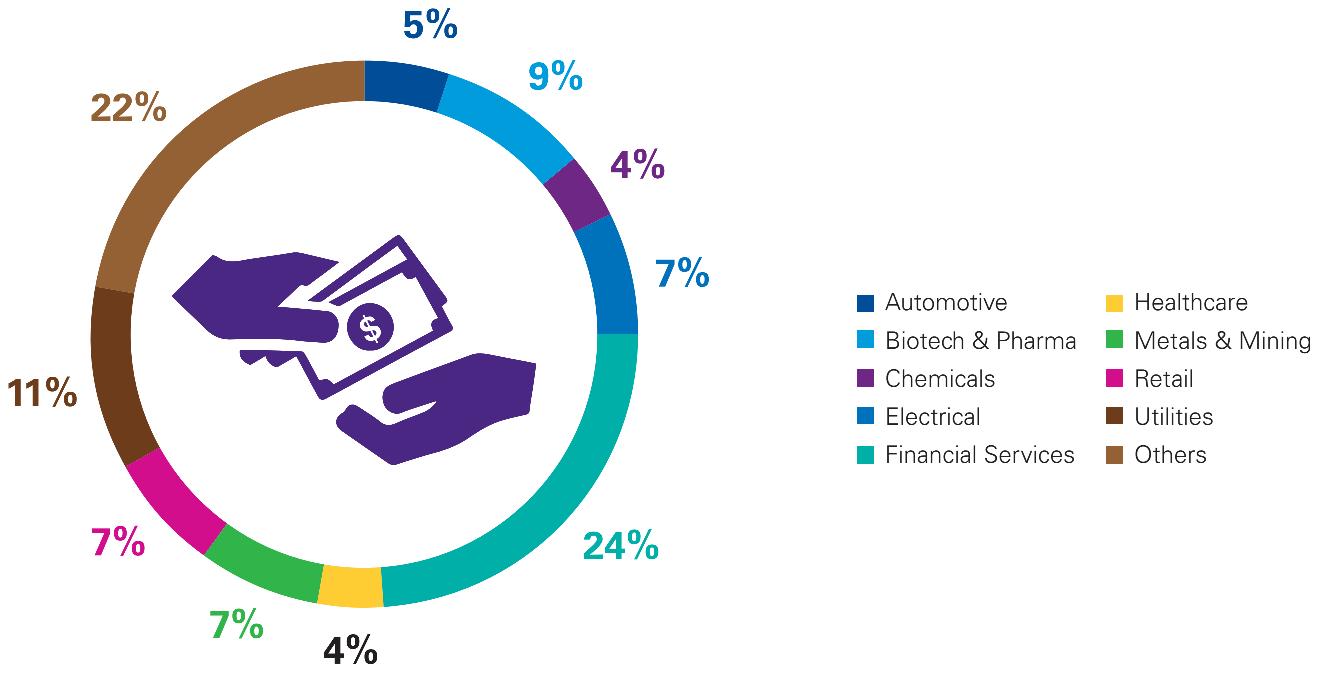
Carve-out transactions in scope of analysis per region



Source: Dissecting public carve-outs, KPMG International, October 2020

The following breakdown portrays the industries covered within our sample population:

Carve-out transactions in scope of analysis per industry



Source: Dissecting public carve-outs, KPMG International, October 2020

The most frequent transactions in our study took place in financial services; however, carve-out transactions are not limited to certain sectors. Indeed, their prevalence across industries points to their macroeconomic relevance as industries become more intertwined, regulatory efforts adjust or increase, and market disruptions and product lifecycles become more fast-paced and dynamic. The interrelationships among these circumstances are prompting an increase of strategic portfolio restructuring for companies across industries.

What transaction characteristics have we studied, and how?

Our joint analysis considered several stand-alone criteria as well as the interrelationships among these criteria, resulting in a picture of how each carve-out has performed. Univariate empirical findings regarding these criteria are reported in section 3; multivariate results are covered in section 4.

Criteria analyzed include:

Transaction type:
IPO vs. spin-off vs. hybrid.

Duration of process:
Time between first announcement of the transaction (i.e. within a press release or other public statement) and listing of the shares on a stock exchange.

Use of proceeds:
In the case of proceeds generated, we have analyzed the principal purpose of the cash received (i.e. financing of further growth, repayment of debt, etc.).

Post-listing control:
For each transaction, we have identified the size of the ultimate parent's stake after the transaction. Does the ultimate parent still have control (generally meaning that they own > 50 percent of the shares) or does the parent retain only a minority stake (generally < 50 percent) or none?

Timing of legal reorganization:
Time between finalization of legal reorganization and listing of the shares on the stock exchange.

TSA coverage:
The areas of usage covered by Transitional Service Agreements between the ultimate parent and the carved-out company. These might include administrative support functions (such as IT, HR and accounting services) and/or operational activities (such as technical services and R&D).

TSA duration:
The maximum term of any services provided under Transitional Service Agreements between the ultimate parent and the carved-out company or group.

Leverage:
We calculated leverage profiles of the carve-out entities by dividing net debt by the 1-year forward EBITDA (where net debt is total debt less cash, short-term investments, and marketable securities).

Share price development:
We analyzed the carved-out businesses' share price movements by comparing the opening share price as of the listing date with the post-transaction share price after 1, 2 and 3 years, respectively.

Univariate empirical analysis: What patterns do our empirical findings show?

We considered questions including:

— How have the carve-out transactions in scope of analysis been conducted, and how did they perform regarding these specified transaction characteristics?

— How long do carve-out processes usually take?

— What are typical uses of proceeds?

— When is the process of legal reorganization typically completed?

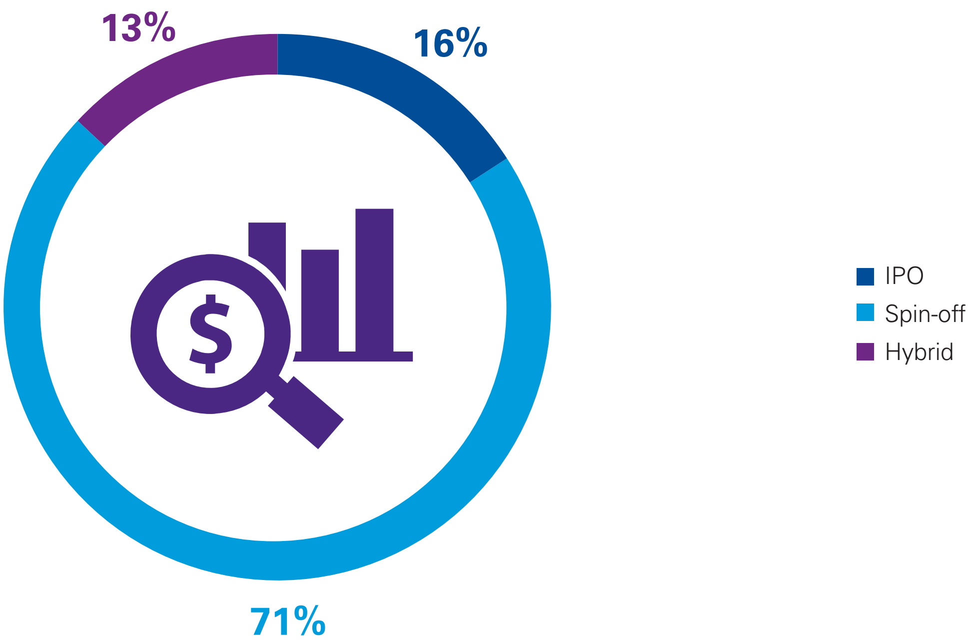
— What services are usually included in TSAs and what time horizons do they cover?

— What leverage profiles do carve-out entities usually have?

Transaction type

The majority of carve-outs in our analysis are spin-offs:

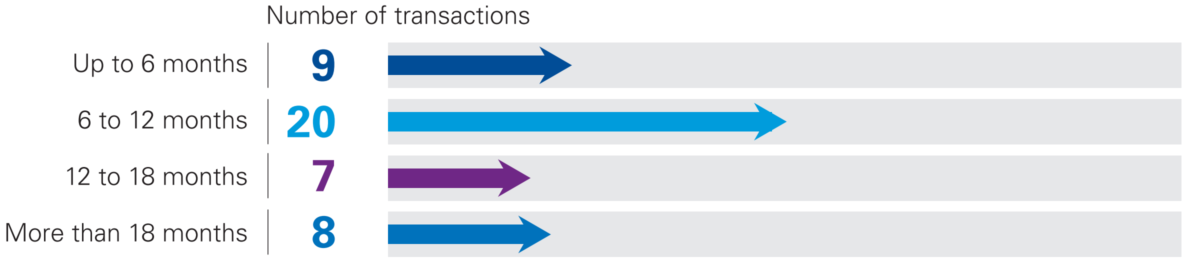
Carve-out transactions in scope of analysis per transaction type



Source: Dissecting public carve-outs, KPMG International, October 2020

Duration of process

Duration of process from first announcement until listing on the stock exchange



Source: Dissecting public carve-outs, KPMG International, October 2020

The path from announcement of the planned carve-out until its listing on the stock exchange ranges from 2 months to 27 months, with an average duration of about 1 year.

"The complexity and as such duration of carve-out processes is mainly driven by setting up the new legal structure for the carved out business as well as preparation and audit of various financial and legal reports whilst continuously maintaining the customer focus as the overarching priority during the whole process. Especially in light of the constant customer focus, the carve out process should be executed as quickly as possible. Moreover customers should be provided with both, information on the carve-out process as well as confidence that they continue to be in the gravity center of entrepreneurial activities.

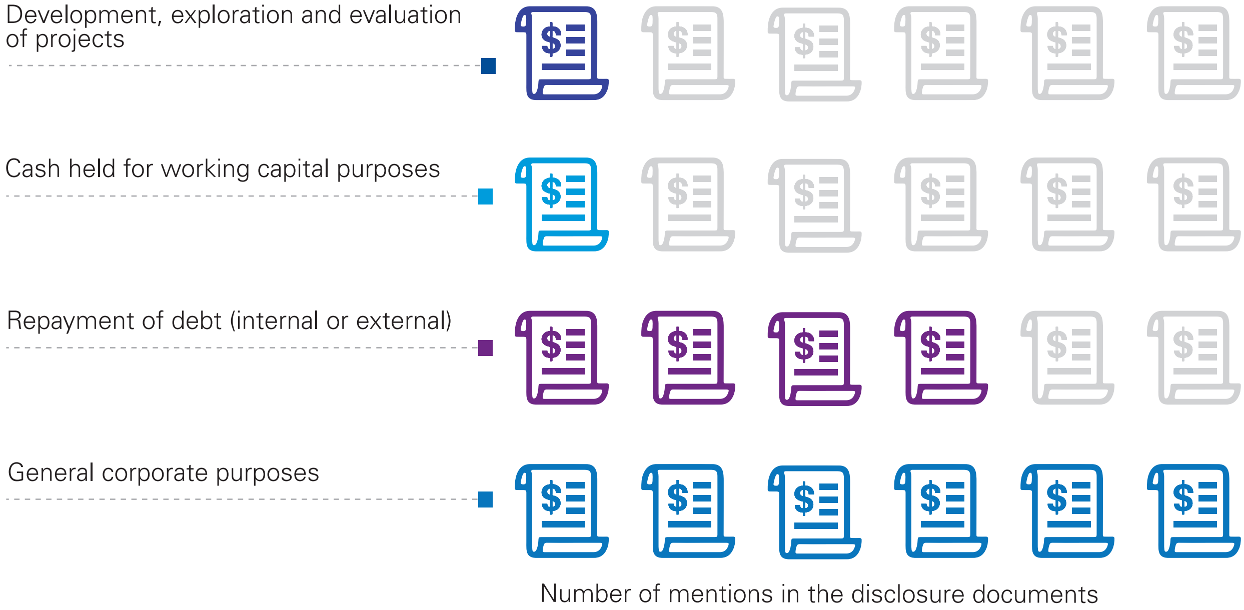
One prerequisite at the beginning of such a complex separation process is a precisely defined business and regional scope. This allows the highly interrelated global carve-out workstreams to jointly identify the best set-up for the future company. A legally and tax-optimized set-up will often be an important decision criteria, yet there is no one-fits-all blueprint for each and every local business to be separated. Similar, a stable scope is inevitable for an in time preparation of external legal and financial disclosure. Effective and efficient project execution based on professional expertise of the involved teams and a constant team collaboration are prerequisites. A capable, convinced and success committed leadership team of the carved-out sub-group is key!"

— Dr. Jürgen M. Wagner,
Siemens AG, Head of Accounting, Reporting and Controlling

Use of proceeds

IPO and hybrid transactions can generate significant cash injections, which, in our study, companies use mostly for general corporate purposes (i.e. financing future growth and development of the company), followed by repayment of debt (internal, external, or both).

Use of proceeds in case of primary shares being offered

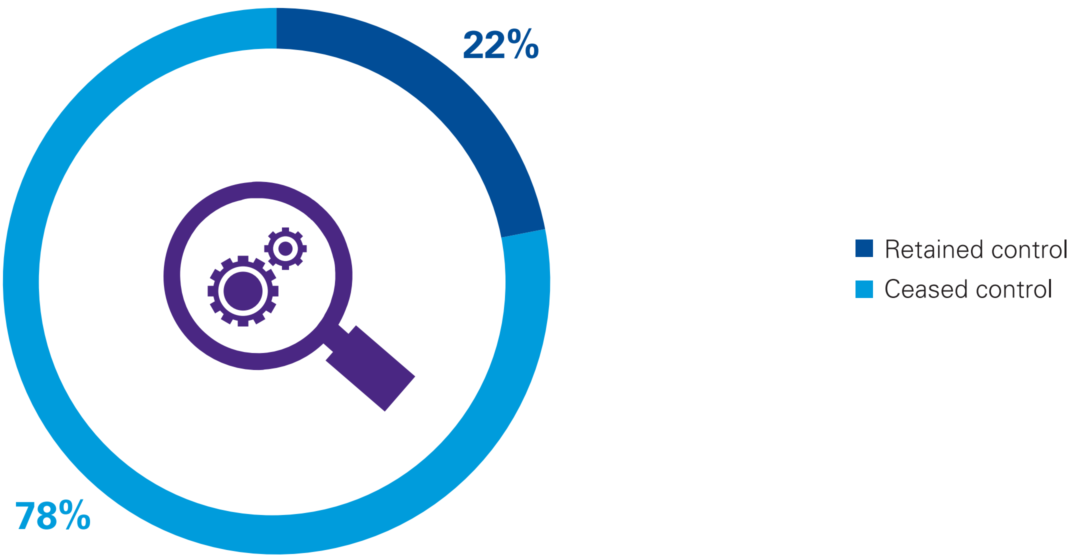


Source: Dissecting public carve-outs, KPMG International, October 2020

Often, however, the disclosure documents indicate that the proceeds are intended for more than one use. Typically, a specified amount may be used for debt repayment and the remainder to support the future development of the company.

Post-listing control

Post-listing control of ultimate parent



Source: Dissecting public carve-outs, KPMG International, October 2020

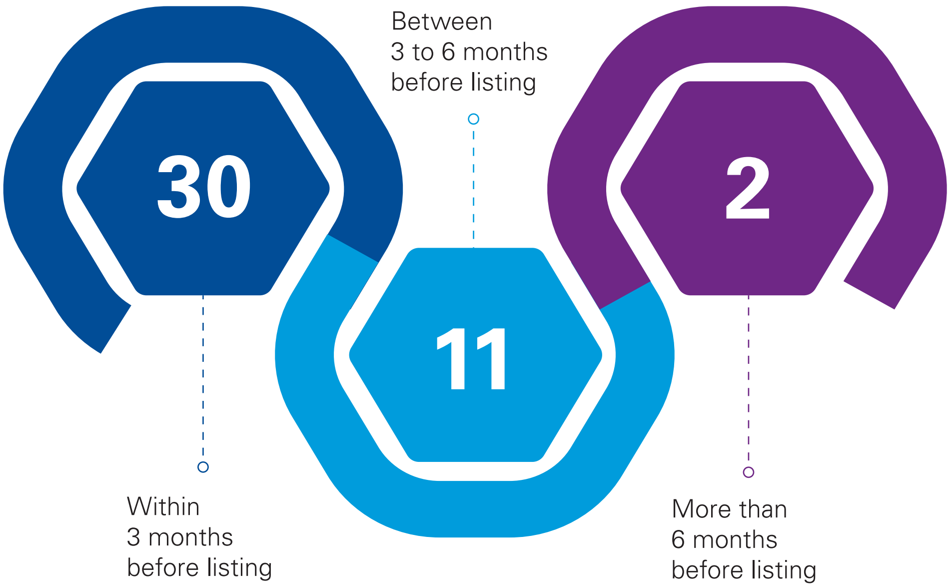
Most of the transactions in our analysis are spin-offs, and, as we expected, the parent did not retain a majority stake in the carved-out company (or retain control by other means). With spin-offs, the shareholders of the former parent company typically receive a majority shareholding in the carved-out company, via a 'dividend in kind.' When the former parent company divests the majority of its holdings in the carved-out company, control ceases.

Timing of legal reorganization

Carved-out businesses are usually not separate legal entities before the carve-out process but are reorganized as such with the implementation of a transition step plan. The following chart illustrates the timing of the finalization of the legal reorganization process:

Timing of finalization of legal reorganization

Number of transactions



Source: Dissecting public carve-outs, KPMG International, October 2020

Our empirical analysis shows that legal reorganizations are usually finalized not long before the listing date on the stock exchange. This finding is not surprising since the process of legal reorganization is usually somewhat complex, as can be seen in companies' legal step plans.

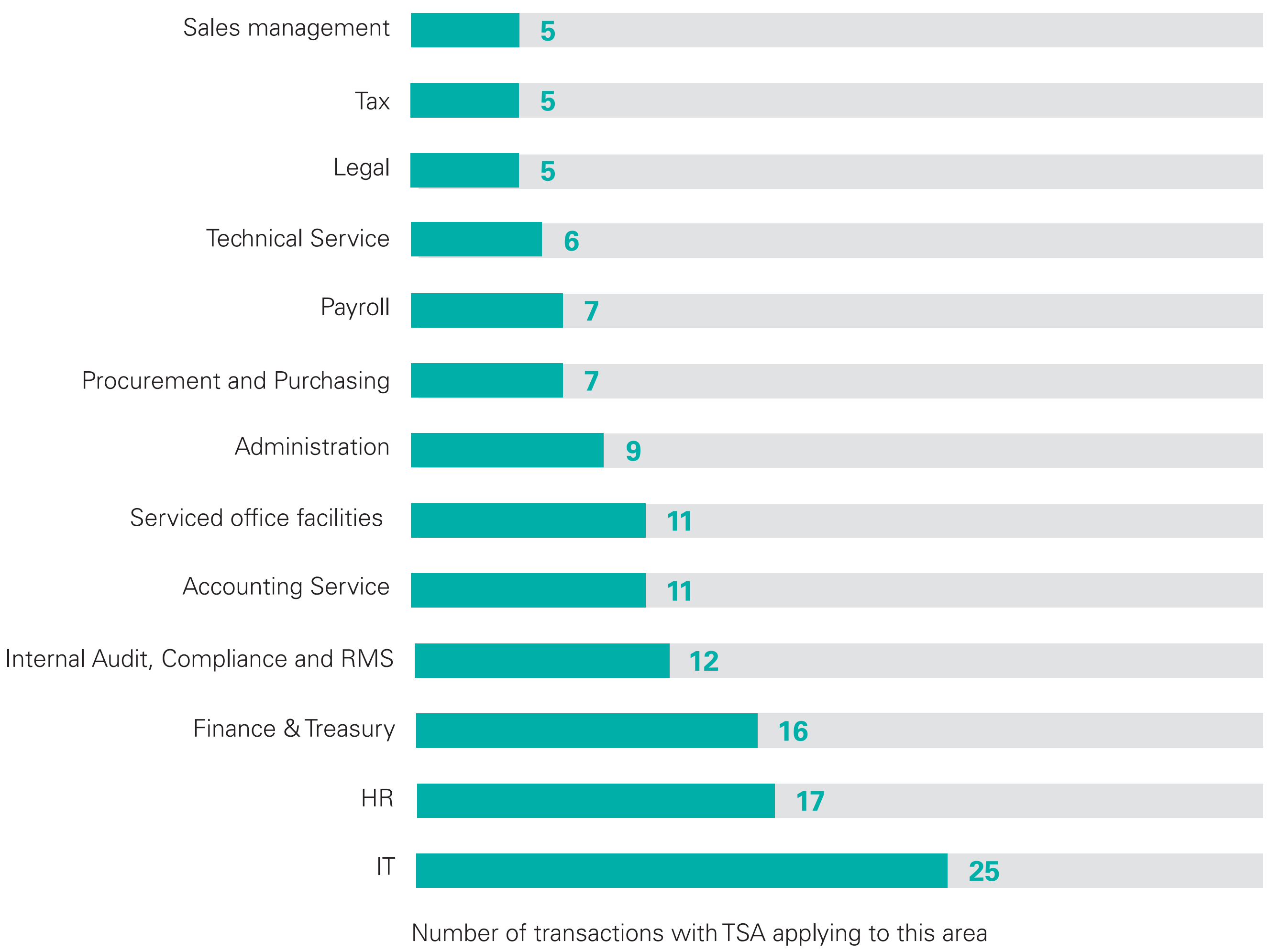
TSA coverage

Transitional Service Agreements (TSAs) specify the services provided by the parent company to the carved-out company (or vice versa) and the fees required for a specified time period, including the terms of possible cancellation or extension options. Parent companies and their carve-outs enter into TSAs to facilitate and smooth both parties' operations and processes post-transaction.

During the term of the TSA, the newly listed company can build up its own resources, capabilities, structures, and capacities. Nonetheless, TSAs delay the carved-out company in becoming truly independent, which may raise questions by regulators. They can also lead to conflicts between the parties if they are not sufficiently specific (i.e. regarding scope and depth of services provided, fee structure, duration, and extension or cancellation options).

The following chart identifies the most frequent areas of usage of TSAs:

Most frequent areas of usage of Transitional Service Agreements (TSAs)

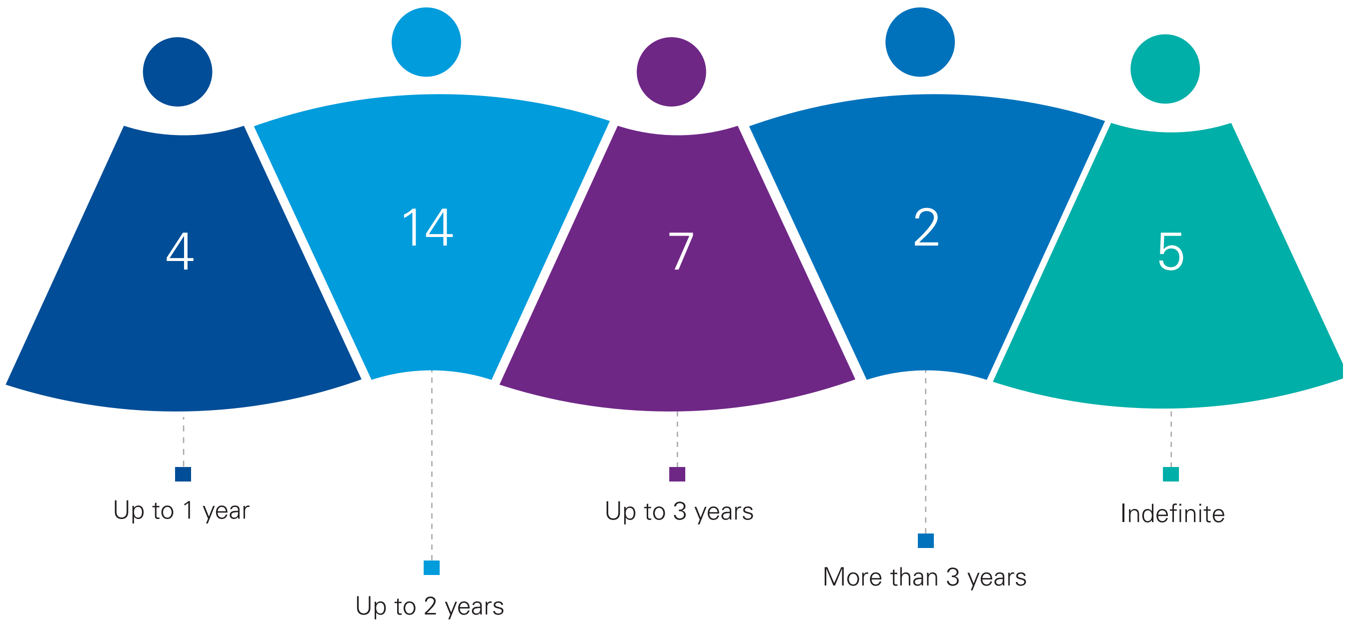


Source: Dissecting public carve-outs, KPMG International, October 2020

Services provided under TSAs can be supplied by the ultimate parent and received by the carved-out company and/or vice versa. Our analysis focuses on the 'standard' case, in which the parent company is the larger, more experienced and more knowledgeable party and the carved-out company is the recipient. TSA disclosures indicate that carve-outs provide services to the (former) parent company infrequently.

TSA duration

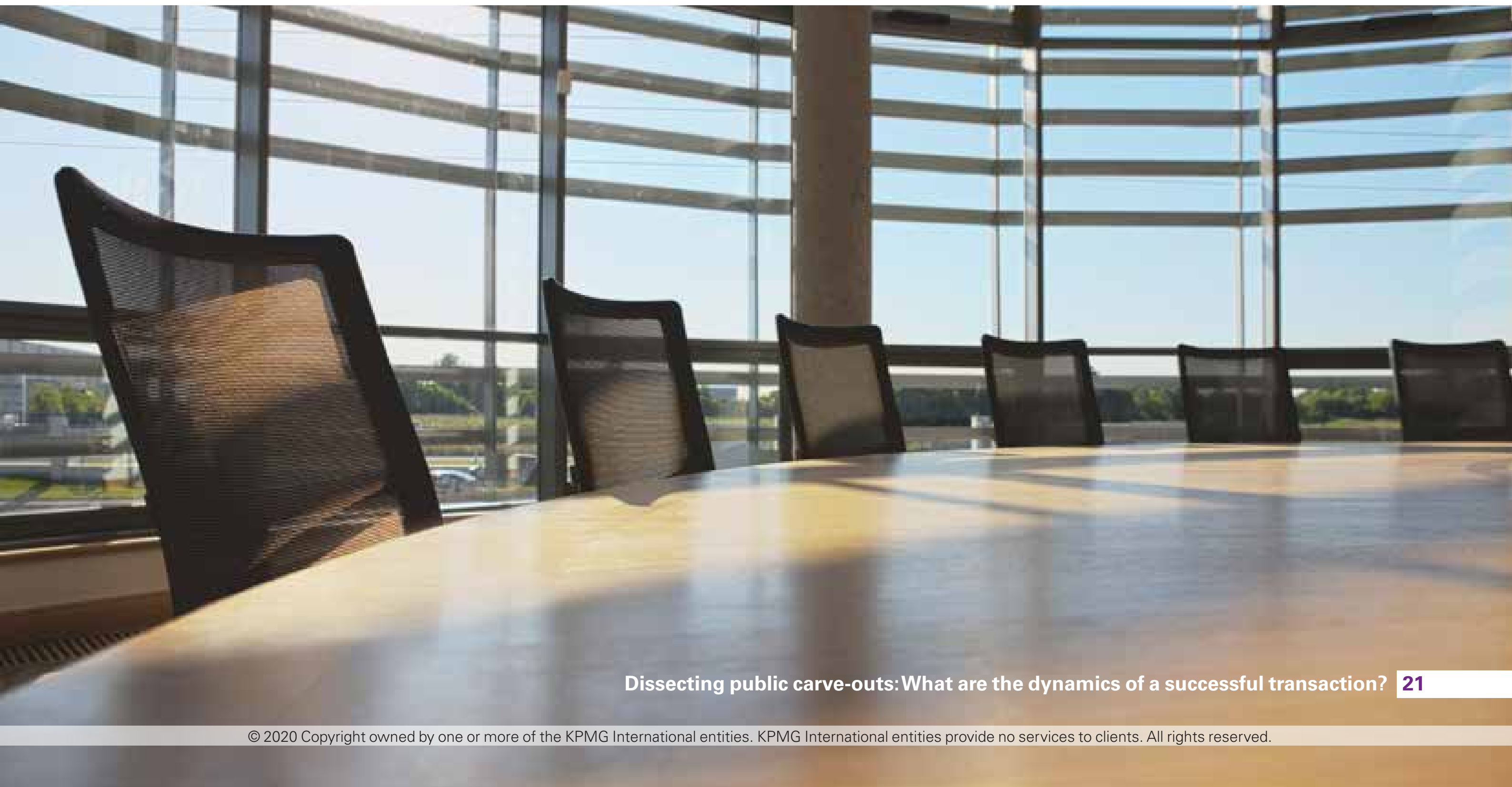
Maximum duration of TSAs



Occurance

Source: Dissecting public carve-outs, KPMG International, October 2020

Most TSAs have a maximum duration of 2 years. In our sample, the shortest duration was 6 months and the longest was 10 years. Some services included in TSAs have inherent options to extend their duration, if necessary; in other cases, no maximum term is specified. In these cases, the recipient cancels the services when the business is ready to run the activities independently. Even though some variance in maximum duration of TSAs is given, a mid-term horizon of 2 years can be considered a characteristic feature of TSAs.

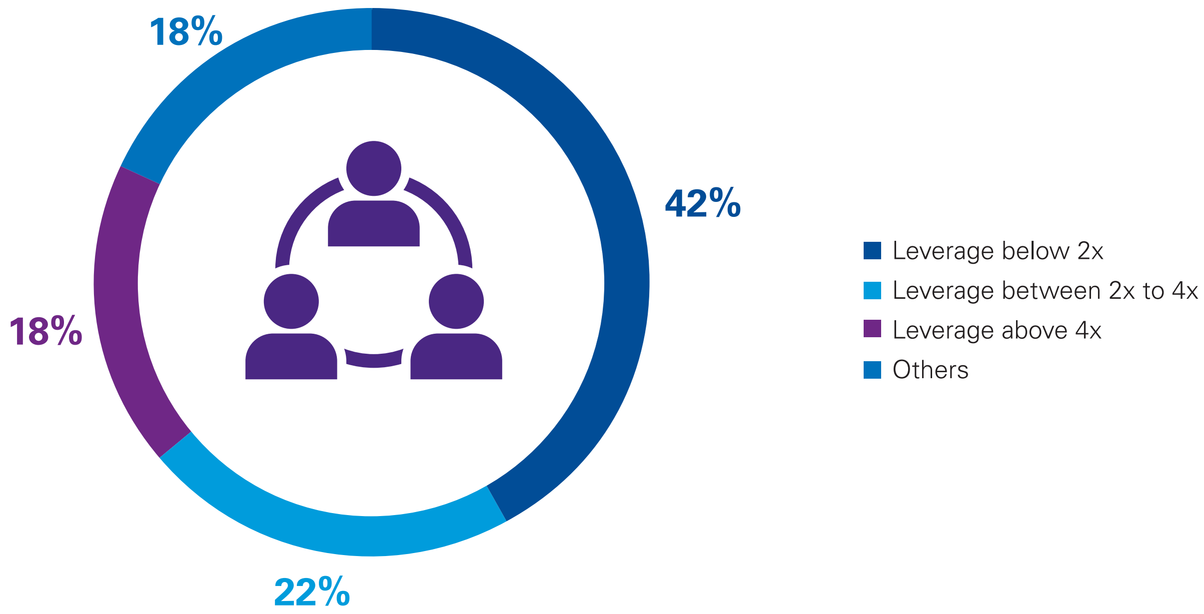


Leverage

As part of the carve-out transactions, the ultimate parent companies usually transfer to the carve-out entity certain amounts of debt and cash that tend to weigh heavily on how the newly formed carve-out formulates its strategy and sets goals.

Usually the debt and cash transfer to the carve-out entity declared not long before its potential listing date on the exchange. Depending on the size of carve out, the debt and cash transfer plays an important role in deciding potential equity valuation of the carve-out entity.

Current leverage profile of carve-out companies



Source: Dissecting public carve-outs, KPMG International, October 2020

Multivariate empirical analysis: What relations can be found between selected transaction characteristics?

Significant relationships between selected variables analyzed in our study include:

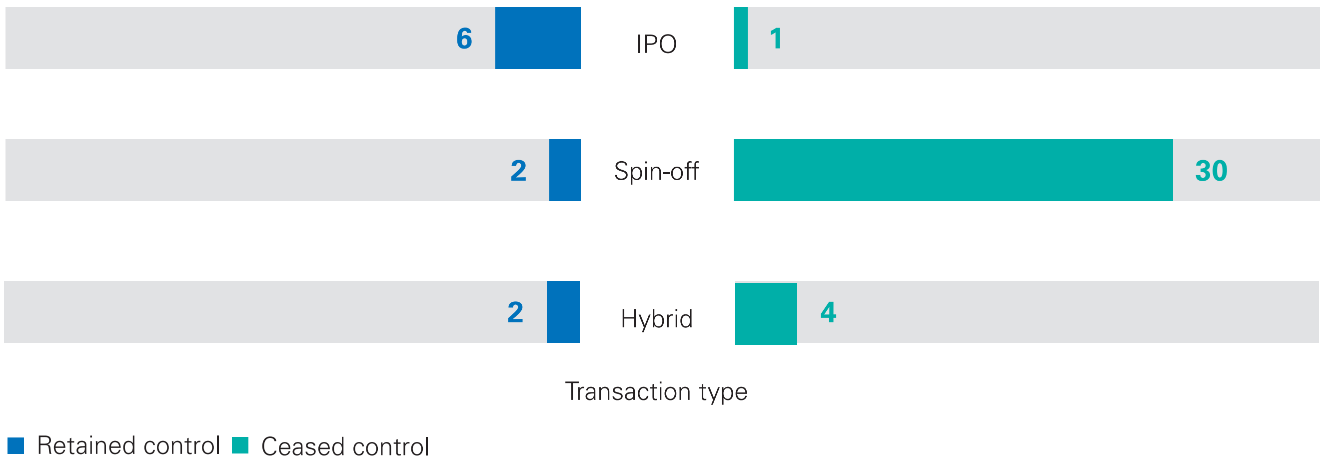
- Correlations between transaction type (i.e. IPO vs. spin-off vs. hybrid) and transaction characteristics, such as post-listing control, duration of process, and share price performance post-transaction
- Transaction characteristics and features that tend to correlate with favorable subsequent share-price performance.

How does the transaction type correlate with selected transaction characteristics?

Transaction type and post-listing control

While parent companies in spin-off transactions usually relinquish control in the carved-out business, parent companies in IPO transactions tend to retain control, usually by holding more than 50 percent of the shares of the newly listed company. We therefore expected a strong correlation between transaction type and post-listing control of the parent, and the study results confirmed this expectation.

Transaction type and post-listing control of ultimate parent



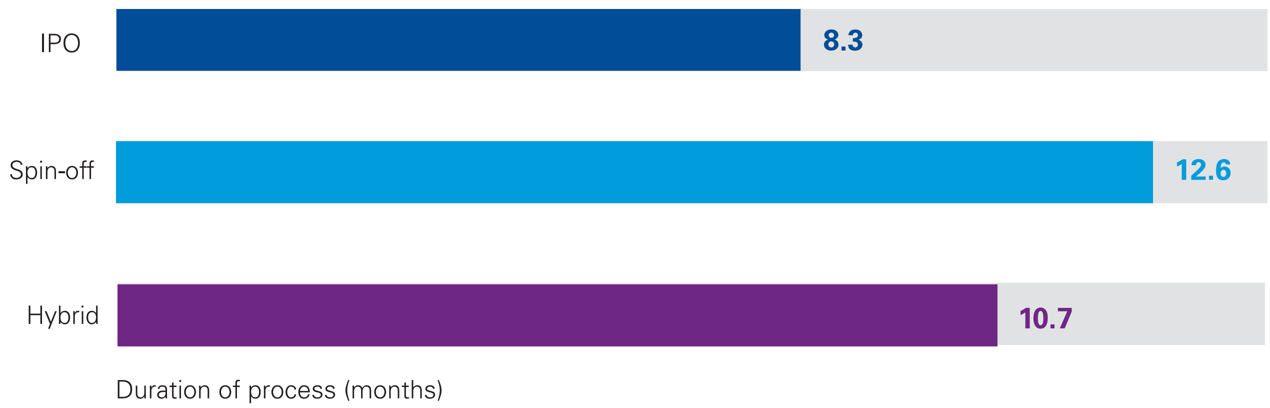
Source: Dissecting public carve-outs, KPMG International, October 2020

In addition, we found that hybrid transactions are sometimes associated with ceased control, and other times with retained control, by the ultimate parent.

Transaction type and duration of process

As discussed, the time between the announcement of the planned carve-out until its listing on the stock exchange is usually 1 year, but the length of the process depends on transaction type. We calculated the mean duration of the carve-out process based on the three transaction types.

Mean duration of process per transaction type



Source: Dissecting public carve-outs, KPMG International, October 2020

In our sample, spin-off transactions are correlated with longer time spans between announcement and listing. Here the mean duration of the entire process exceeds 1 year. Hybrid transactions follow with an average time span of 10.7 months, while classical IPO transactions are correlated with the shortest carve-out processes. Hybrid transactions combining attributes of both IPOs and spin-offs do not take longer than 'pure' spin-offs.

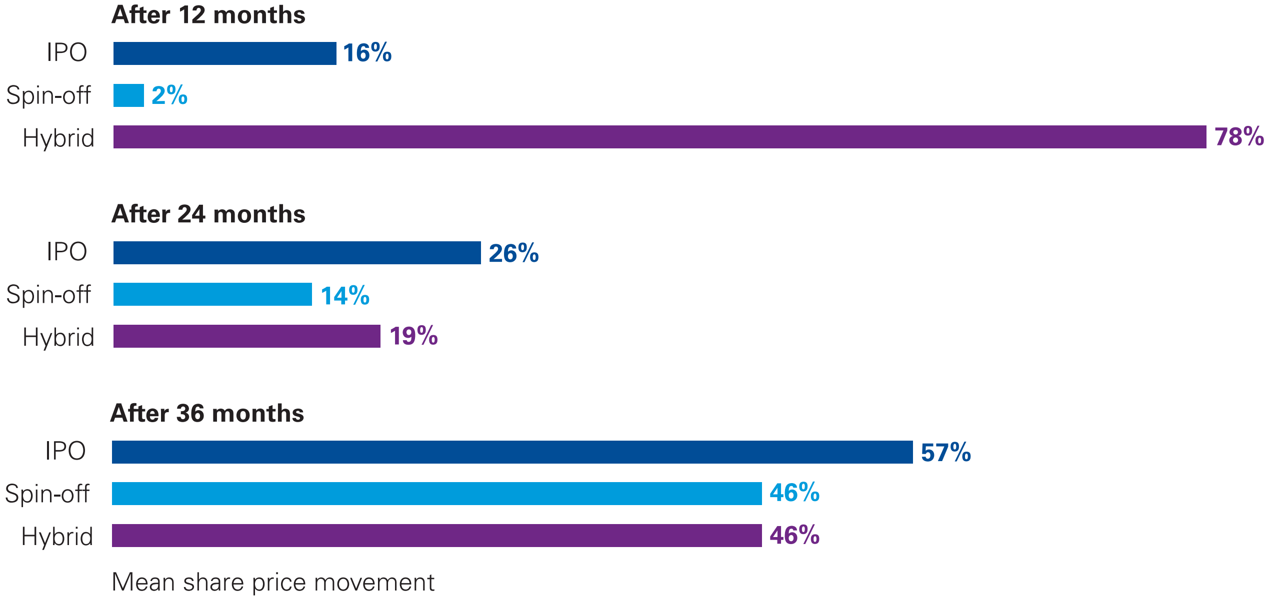
Transaction type and share price performance post carve-out

Carve-out transactions are intended to maximize shareholder value by allowing the carved-out business to be run independently of the ultimate parent company. The parent can better focus on its core business when the carve-out can set its own goals, formulate its own strategies, and implement its own structures, processes and management systems.

Assuming these conditions hold true, post-transaction share prices of both parent and carve-out should rise.

We examined whether the carve-out transactions in our analysis achieved this result. We also looked at whether post-transaction share price performance varied depending on whether companies were divested via a spin-off, an IPO, or a hybrid transaction.

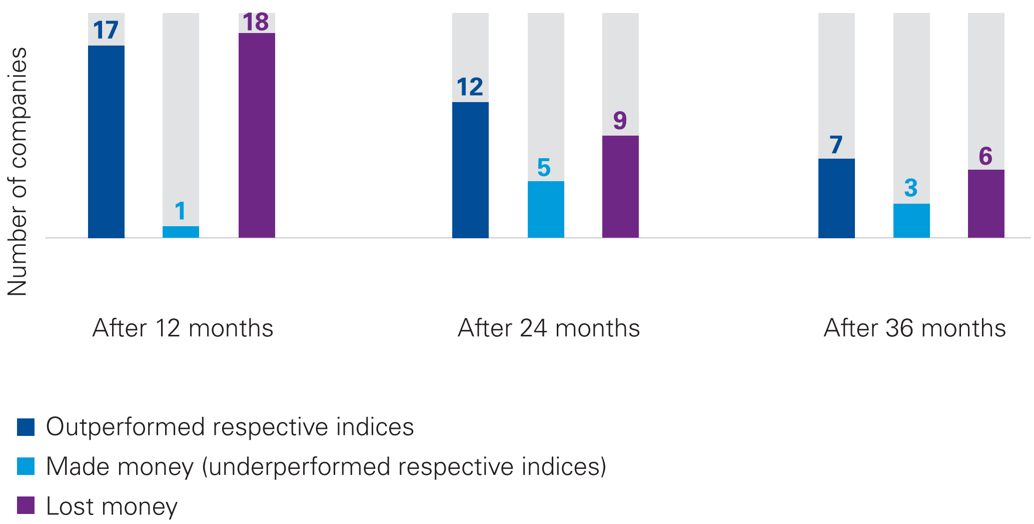
Mean share price movement per transaction type



Source: Dissecting public carve-outs, KPMG International, October 2020

We also examined how these companies' performance fared with respective indices for 3 years following the date of listing.

Mean share price performance vs. respective indices



Source: Dissecting public carve-outs, KPMG International, October 2020

Overall, the carve-out companies' share prices seem to develop favorably, especially after 3 years, supporting our expectation that such transactions increase shareholder value.[1]

[1] The outstanding performance of hybrid transactions 12 months after listing is due to an outlier in our sample with an extremely positive share price movement. This result should not be interpreted as characteristic of hybrid transactions.

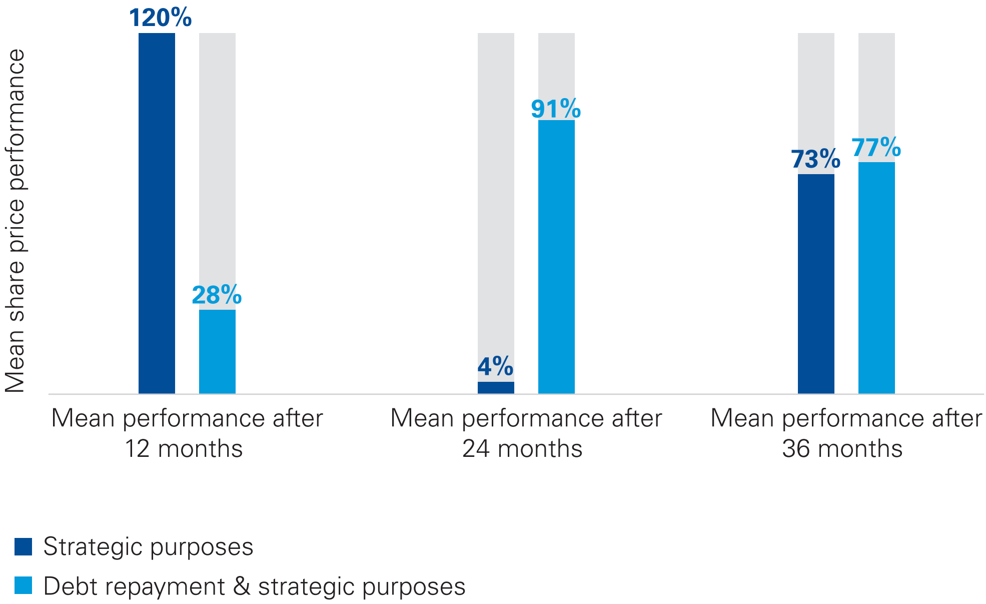
How do selected transaction characteristics correlate with share price performance?

Use of proceeds and share price performance post carve-out

When carve-out proceeds are used for strategic or 'general corporate purposes' they serve to catalyze and enable the company's future development and growth. Should there be a correlation between the use of proceeds and the post-transaction share price performance?

Based on our sample population, we were able to analyze share price development where proceeds were used for strategic purposes only. We predicted [2] that some time would be needed for the share price to show strong positive developments, and our expectations were largely borne out over time.[3] It is fair to say, however, that when strategic goals are prevailing, a longer time horizon and a certain degree of patience are needed to evaluate the success of a carve-out transaction.

Use of proceeds and share price performance



Source: Dissecting public carve-outs, KPMG International, October 2020

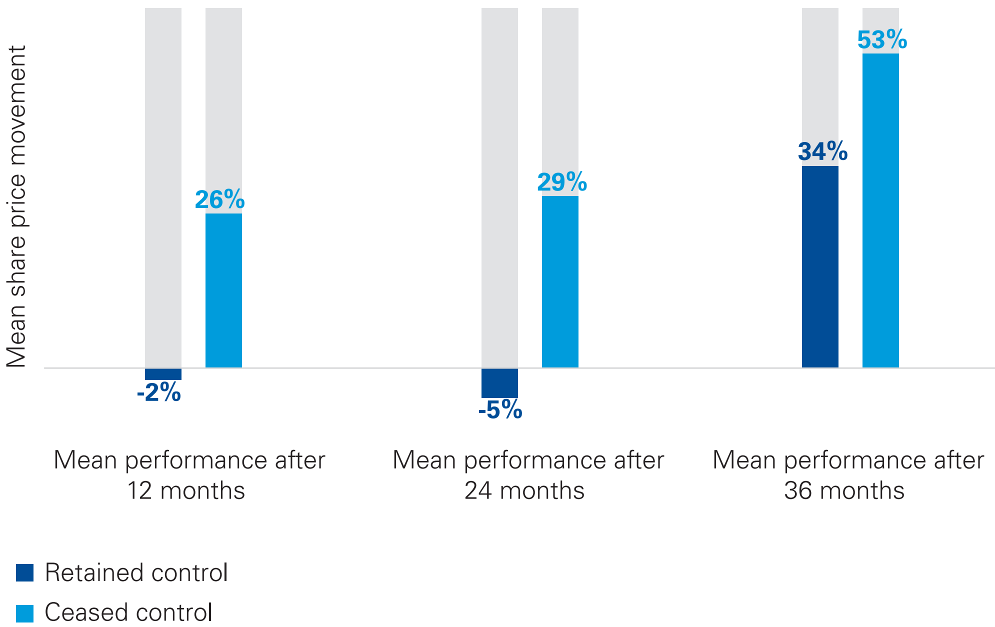
Post-listing control and share price performance post carve-out

Should the share price performance of the carved-out company be different depending on whether the ultimate parent retains or ceases control? Since the advantage of retained control (i.e. access to shared resources and capabilities) can also be achieved using TSAs, we predicted that share price performance would improve when the carved-out business could operate truly independently from the former parent company.

[2] Our analysis shows that this prediction is true, although the chart displayed above does not directly indicate as much due to an outlier that drove up mean share price performance after 12 months. Without this outlier, mean share price performance after 1 year is negative when proceeds are used for strategic purposes only. It becomes slightly positive after 2 years and strongly positive thereafter.

[3] Interpretations or generalizations should be made with caution. There are no transactions in our data where proceeds generated served only for repaying debt. Instead, there are some cases where proceeds served only strategic purposes and some where they were used for both debt repayment and strategic purposes. The majority of transactions we analyzed were spin-offs with no proceeds being generated, so the number of transactions in each category (strategic purposes vs. debt repayment and strategic purposes) is also small.

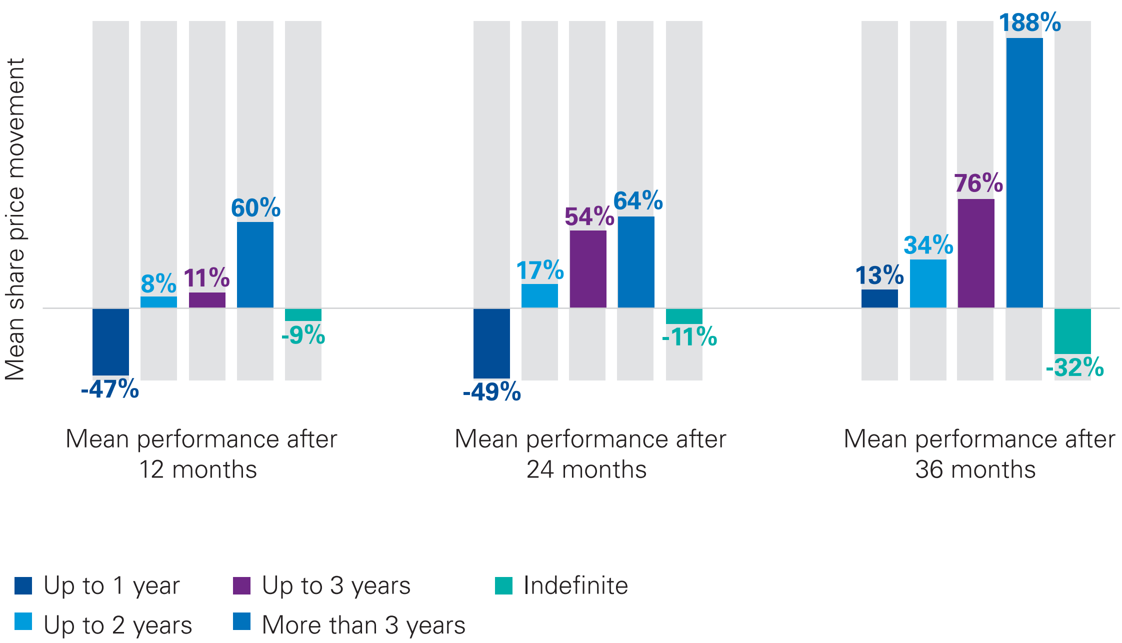
Mean share price movement and post-listing control of ultimate parent



Source: Dissecting public carve-outs, KPMG International, October 2020

The chart above illustrates that our prediction holds true. After even 1 year, mean share price performance for transactions where the ultimate parent does not retain control is significantly higher than for cases where control is retained. To build shareholder value, carved-out businesses need to be able to achieve true independence.

Duration of TSAs and share price performance



Source: Dissecting public carve-outs, KPMG International, October 2020

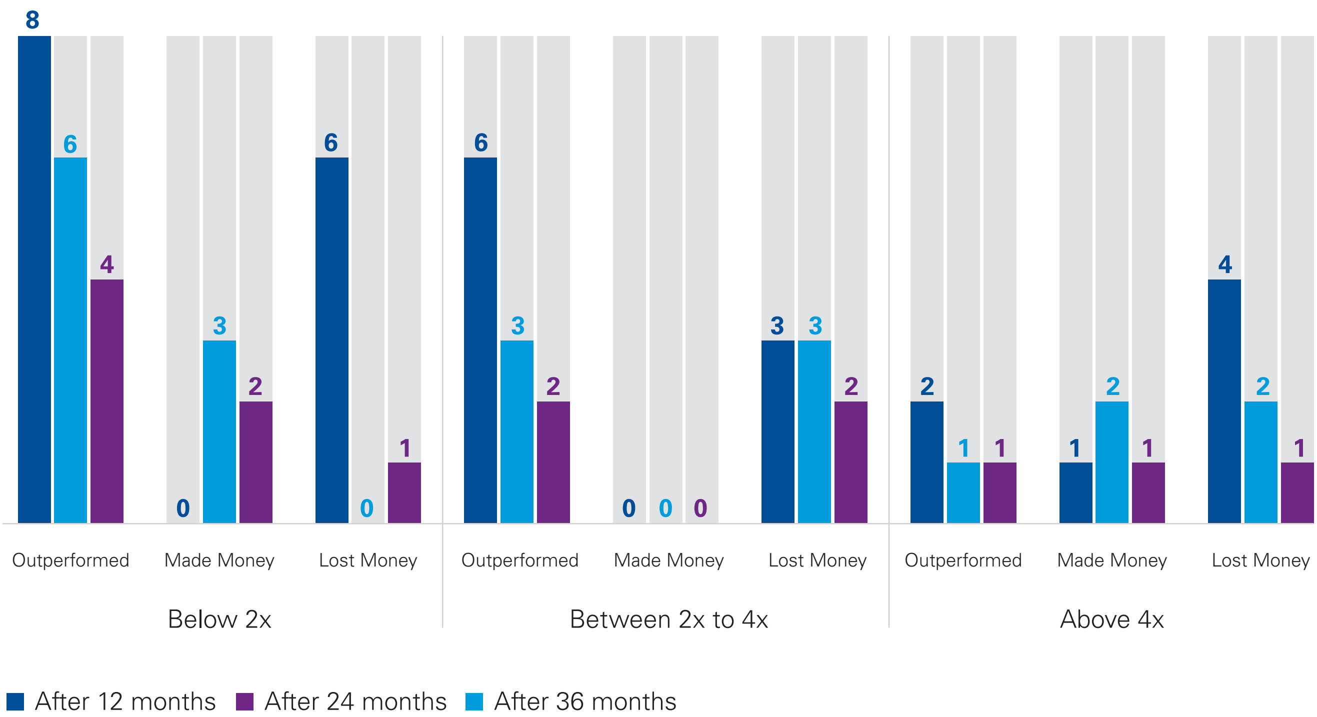
The results point to a positive correlation between TSA duration and share price performance. TSAs can contribute to a smooth transition post-transaction if they allow sufficient time for carved-out companies to set up their own structures.

Furthermore, the results underscore the importance of sufficiently specifying the terms of services provided by a TSA, which can be an important and useful tool if defined unambiguously. In cases where the maximum duration of TSA services is not specified ('indefinite'), share price performance remains negative. Additionally, TSAs tend to be inconsistently defined: one disclosure document may allude to 'accounting, reporting, finance and treasury services,' while another could mean the same thing but refer simply to 'administrative services.'

Leverage and share price performance post carve-out:

We examined how different levels of leverage impact companies' share price performance in the years following the listing of the carve-out entity. We classified carve-out companies' performance into three categories i) Outperformed (respective indices since listing), ii) Made Money (underperformed respective indices but yielded positive returns), and iii) Lost Money (yielded negative returns).

Performance classification by leverage



Source: Dissecting public carve-outs, KPMG International, October 2020

We found that below 4x leverage carve-outs tend to perform better compared to above 4x leverage carve-outs.[4]

[4] Above 4x, outperformance is skewed due to an outlier driving share price performance up after 24 months. Eliminating this, our conclusion holds true.

Summary of key insights (Top 5)

Share price development of carve-out businesses is favorable overall:
The goal of maximizing shareholder value by establishing an independent entity with its own corporate rationale seems to work well in many cases. Most carve-out entities outperform the respective indices.

Public carve-out processes take time and require thorough advance planning:
A time span of 1 year between first announcing the transaction and listing the carve-out business on a stock exchange is an appropriate rule of thumb.

Carve-outs need a PMO to manage multiple workstreams:
These transactions' inherent complexities and interdependencies require a comprehensive project management office that steers, monitors and manages the process.

Regulatory requirements are quite complex:
Combined and/or carve-out financial statements must often be prepared because standard historical financial information may not appropriately reflect the economic activities of the carve-out business.

Transitional Service Agreements (TSAs) play a crucial role in the carve-out process:
TSAs usually cover multiple areas, especially administrative functions. Carefully defining all relevant terms is critical to avoid future conflicts and share-price impacts.

Appendix 1: Summary of regulatory requirements

	Major regulatory documents	Trigger events for the preparation of FS	Scope of disclosure requirements	Further comments
Europe	— EU Prospectus Regulation 2017/1129; — Delegated Regulation to the Prospectus Regulation 2017/1129; — ESMA Guidances and Recommendations.	— Making an offer to the public of shares; — Issuing other transferable securities equivalent to shares or other securities that can be converted; — Exchanging transferable equivalent securities into shares under certain circumstances; — Asking for the admission of securities to trading on a regulated market.	— Present FS for the last 3 fiscal years; — For carve-out businesses with a "complex financial history", combined and/or carve-out FS are to be prepared for the historical years.	— "Complex financial history" refers to the common case where the legal form is being established along the road to the IPO date.
United States	— SEC Regulation S-X-3-05; — Other SEC pronouncements.	— Certain capital market transactions, such as: — Put-together IPO transactions (two or more parties transfer net assets to a Newco in exchange for shares in that entity); — Roll-up IPO transactions (an investor acquires two or more smaller business from the same sector and merges them into a Newco).	— Combined and/ or carve-out FS according to the specific scenario; — In case of ad hoc reporting in conjuction with significant acquisitions by SEC registrants: Combined and/or carve-out FS on the basis of IFRS.	— In roll-up transactions, the investor is usually from the private equity or alternative investment sector.
United Kingdom	— Prospectus Regulation Rules and Listing Rules; — European documents have also been adopted in the UK.	— Issuers seeking a premium main market listing.	— Components held under common control: Historical FI presented on a combined basis; — Components not held under common control: Separate historical FI up to the point of coming under common control.	— Historical financial information shall represent at least 75% of the issuer´s business for the track record period.

	Major regulatory documents	Trigger events for the preparation of FS	Scope of disclosure requirements	Further comments
Japan	— Financial Instruments and Exchange Act.	— Split-off type company splits where a listed company reorganizes to a certain degree; — Stock distributions, if the spin-off company is listed; — Stock distributions, if the spin-off company is not listed, but the number of shareholders exceeds 1,000.	— If the spin-off source company is a listed company, etc., there is the need to prepare a securities registration statement or a prospectus.	— Stock distributions without monetary distribution claim rights: No need to submit a securities registration statement or prepare a prospectus.
India	— Guidance note for preparing combined and/or carve-out FS from the Institute of Chartered Accountants of India.	— Amalgamations/ mergers/demergers of listed entities; — Acquisitions/ reorganizations within a proposed entity before listing; — Proposed acquisitions of one or more material businesses from proceeds received from a listing.	— Public demergers: Carve-out FS for the last 3 years; — Acquisition of one or more material businesses not representing a whole entity: Carve-out FS for the last 3 years and the stub period.	— Acquisition or demerger before the date of filing the offer document: Pro-forma FS for the last year and the stub period.
Australia	— Part 5.1 of the Corporations Act (for schemes of arrangement); — Standard on Assurance Engagements ASAE 3450.	— IPOs; — Demergers involving a capital reduction; — Demergers involving a scheme of arrangement (a procedure that allows a company to reconstruct its capital, assets or liabilities with the approval of its shareholders and the court); — Transactions including both IPO and demerger elements.	— Historical and pro-forma historical and forecast FI disclosures in both a scheme of arrangement and prospectus are typically supported by a limited assurance Investigating Accountants Report.	— Processes around demergers and IPOs are very legalistic and controlled by lawyers.

Appendix 2: List of transactions included in our analysis

Company name	Country	Listing date	Stock exchange
South 32 (demerger from BHP)	Australia	May 2015	Australian Securities Exchange (ASX)
Tilt Renewables Limited (demerger from Trustpower Limited)	Australia	Oct 2016	New Zealand Exchange (NZX)
Westgold Resources Limited (demerger from Metals X Limited)	Australia	Dec 2016	Australian Securities Exchange (ASX)
Ardea Resources Limited (demerger from Heron Resources Limited)	Australia	Feb 2017	Australian Securities Exchange (ASX)
Domain Holdings Australia Limited (demerger from Fairfax Media Limited)	Australia	Nov 2017	Australian Securities Exchange (ASX)
Coles (demerger from Wesfarmers)	Australia	Nov 2018	Australian Securities Exchange (ASX)
Sixt Leasing (demerger from Sixt)	Germany	May 2015	Frankfurt (Prime Standard)
Covestro (demerger from Bayer)	Germany	Oct 2015	Frankfurt (Prime Standard)
Uniper (demerger from E.ON)	Germany	Sep 2016	Frankfurt (Prime Standard)
Innogy (demerger from RWE)	Germany	Oct 2016	Frankfurt (Prime Standard)
Metro (demerger from Ceconomy)	Germany	Jul 2017	Frankfurt (Prime Standard)
DWS (demerger from Deutsche Bank)	Germany	Mar 2018	Frankfurt (Prime Standard)
Healthineers (demerger from Siemens)	Germany	Mar 2018	Frankfurt (Prime Standard)
Traton (demerger from VW)	Germany	Jun 2019	Frankfurt (Prime Standard)
Reliance Home Finance Ltd. (demerger from Reliance Capital)	India	Sep 2017	Bombay Stock Exchange (BSE) and National Stock Exchange (NSE)
Praxis Home Retail (demerger from Future Retail)	India	Jan 2018	Bombay Stock Exchange (BSE) and National Stock Exchange (NSE)
Adani Green Energy (demerger from Adani Enterprises)	India	Jun 2018	Bombay Stock Exchange (BSE) and National Stock Exchange (NSE)
Adani Gas (demerger from Adani Enterprises)	India	Nov 2018	Bombay Stock Exchange (BSE) and National Stock Exchange (NSE)
Arvind Fashions Limited (demerger from Arvind Ltd.)	India	Mar 2019	Bombay Stock Exchange (BSE) and National Stock Exchange (NSE)
IIFL Wealth Management (demerger from IIFL Holdings)	India	Sep 2019	Bombay Stock Exchange (BSE) and National Stock Exchange (NSE)
IIFL Securities (demerger from IIFL Holdings)	India	Sep 2019	Bombay Stock Exchange (BSE) and National Stock Exchange (NSE)

Company name	Country	Listing date	Stock exchange
ABB Power Products and Systems India Ltd. (demerger from ABB India)	India	Mar 2020	Bombay Stock Exchange (BSE) and National Stock Exchange (NSE)
Curves Holdings (demerger from Koshidaka Holdings)	Japan	Mar 2020	Tokyo Stock Exchange (Prime Standard)
Signify (demerger of Philips Lighting from Philips N.V.)	Netherlands	May 2016	Euronext Amsterdam
CYBG (demerger from National Australia Bank)	UK	Feb 2016	London (Premium Listing)
Quilter (demerger from Old Mutual)	UK	Jun 2018	London (Premium Listing)
M&G (demerger from Prudential)	UK	Oct 2019	London (Premium Listing)
Ninety One (demerger from Investec)	UK	Mar 2020	London (Premium Listing)
Galliford Try (sold off its housebuilding business)	UK	N/A	London (Premium Listing)
PayPal (demerger from ebay)	US	Jul 2015	NASDAQ
Baxalta (demerger from Baxter)	US	Jul 2015	New York Stock Exchange (NYSE)
Chemours (demerger from Dupont)	US	Jul 2015	New York Stock Exchange (NYSE)
CSRA Inc. (demerger from Computer Sciences Corp.)	US	Nov 2015	New York Stock Exchange (NYSE)
Aptevo Therapeutics (demerger from Emergent BioSolutions)	US	Aug 2016	NASDAQ
Adient (demerger from Johnson Controls)	US	Oct 2016	New York Stock Exchange (NYSE)
Yum China Holdings (demerger from YUM! Brands)	US	Nov 2016	New York Stock Exchange (NYSE)
BioVerativ (demerger from BioGen Inc)	US	Feb 2017	NASDAQ
Brighthouse Financial (demerger from MetLife)	US	Aug 2017	NASDAQ
nVent Electric (demerger from Pentair plc)	US	May 2018	New York Stock Exchange (NYSE)
Arlo Technologies (demerger from Netgear Inc.)	US	Aug 2018	New York Stock Exchange (NYSE)
Elanco (demerger from Eli Lily)	US	Sep 2018	New York Stock Exchange (NYSE)
Resideo Technologies (demerger from Honeywell International)	US	Oct 2018	New York Stock Exchange (NYSE)
Arcosa (demerger from Trinity Industries)	US	Nov 2018	New York Stock Exchange (NYSE)
Covetrus (demerger from Henry Schein)	US	Feb 2019	NASDAQ
Diamond S Shipping (demerger from Capital Product Partners LP)	US	Mar 2019	New York Stock Exchange (NYSE)

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