

Spin Offs Back in Style

It seems as though throughout the history of Wall Street, there has been a continuous cycle where companies merge to form 'synergies,' and then years later spin off assets to 'unlock' value. In the late 1990s, the merger of Salomon Smith Barney and Citigroup was lauded as a monumental merger whose synergies would lead to huge cost savings and cross selling that would benefit shareholders of the combined company. We all know what happened in the ensuing years following that merger. Citigroup, as the combined company is now a shell of its former self in terms of divisions and market cap.

These days the market seems to be in the unlocking phase where several companies are spinning off units in an effort to boost share prices. In the last quarter of 2011 alone, there were eight spinoffs of \$100 million or more.

Company Spinoffs: Q4 2011

Ann'd	Completed	Child Company (Ticker)	Parent Company (Ticker)	Child Performance			Parent Performance			
				1 Week	1 Month	3 Month	Ann to Spin Date	1 Week	1 Month	3 Month
12/13/10	10/3/11	Lone Pine Resources (LPR)	Forest Oil (FST)	4.5	31.2	22.1	-66.1	21.9	31.2	52.4
12/8/10	10/4/11	Fortune Brands (FBHS)	Beam (BEAM)	1.5	19.3	36.7	-6.3	5.2	8.6	13.9
8/29/11	10/31/11	Genie Energy (GNE)	IDT (IDT)	-9.3	-17.1	23.6	-3.7	15.4	1.7	-20.3
12/8/10	11/1/11	Lumos Networks (LMOS)	NTELOS Holdings (NTLS)	7.9	-6.2	1.1	-3.5	-11.9	-23.5	-8.9
1/12/11	11/1/11	Exelis (XLS)	ITT (ITT)	-7.3	-22.3	-14.6	-7.8	5.0	4.3	15.6
1/12/11	11/1/11	Xylem (XYL)	ITT (ITT)	-8.7	-14.8	-5.1	-7.8	5.0	4.3	15.6
2/14/11	11/22/11	Marriott Vacations (VAC)	Marriott In'l (MAR)	-10.2	2.9		-25.3	1.5	-0.8	
4/7/11	12/21/11	TripAdvisor (TRIP)	Expedia (EXPE)	-6.9	4.9		32.4	6.0		
		Average		-3.5	-0.3	10.6	-11.0	6.0	3.7	11.4

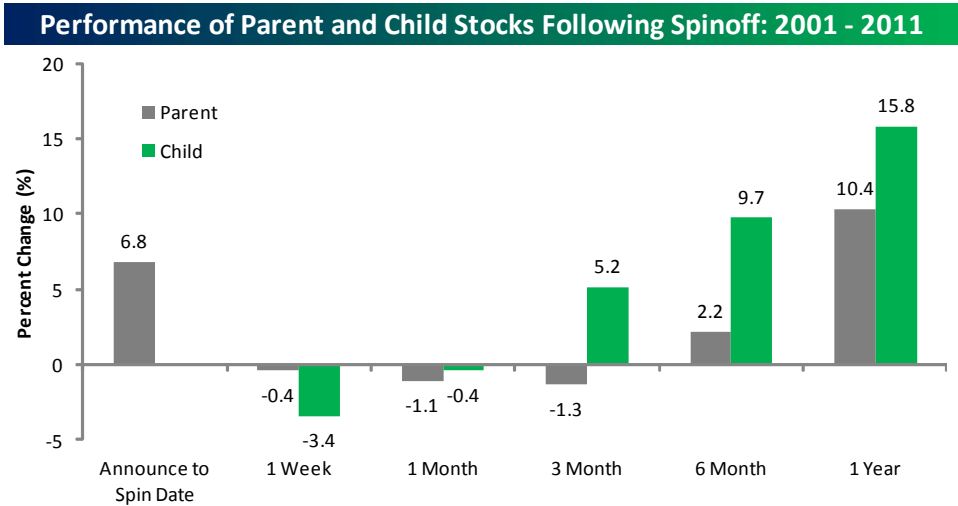
So far this year the trend has continued as Expedia (EXPE) completed the spin off of TripAdvisor (TRIP), and Ralcorp (RAH) spun off its Post Cereal (POST) unit. As the year progresses, we will certainly see this trend continue as bankers, hungry for fees, will no doubt be touting the windfalls from spinning off assets that would command higher multiples as a separately traded entity.

So with the pace of spinoffs on the rise, what is an investor to do? When a company splits in two, or in some cases three, separately traded stocks, should investors buy the parent company, the child stock, or just stay away? In order to answer this question, we conducted an analysis of all US companies who have completed spin offs of \$100 million or more in the form of a publicly traded US stock since 2001. *Continued on page two.*

From 2001 through 2011, there were 132 spinoffs that fit the above criteria. For each spinoff, we calculated the performance of the parent company from the time of the announcement through the completion of the spinoff, and then compared the performance of the parent and child stocks over the next week, month, three months, six months, and one year.

As shown in the chart below, when a company announces a spinoff, its stock has averaged a rally of 6.8% from the time of the announcement to the completion of the spin off. Once the spin off is completed, both the parent and child tend to see negative returns in the near term. The declines seen in the child stock are especially noteworthy as they average a decline of 3.4% in the span of just a week. One possible explanation for this decline is that in most cases, the child stock does not fit into the same style as the parent company, so many managers will immediately sell the new stock to avoid deviating from there predominant style.

After the initial week, however, the child stock’s performance improves substantially. Three months after the spin off is completed, the child stock averages a gain of 5.2% compared to a 1.3% decline for the parent company. Six months after the spin off is completed, the child stock’s performance improves to an average of 9.7% versus 2.2% for the parent stocks. Finally, one year after the spinoff is completed, the parent company’s performance (10.4%) starts to catch up to the child (15.8%), but the average return of the child stocks is still considerably greater.



Turning our attention back to the recent spinoffs shown on page one, as well as the ones that have been and will be completed this year, it appears as though the best way to play the ongoing wave of corporate spinoffs is to avoid the parent stocks. Instead, investors should focus on possibly buying the child stocks a month or so after the spin off is completed. By waiting, investors will not be subject to the initial selling that inevitably takes place as existing shareholders sell shares of the child stocks that may not fit in with their investment criteria or guidelines.