Mergers & Acquisitions®
The Dealmaker's Journal Jan/Feb 1993 Volume 27/Number 4

The Way Emotional Hang-Ups Can Stymie Deals

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Divestiture Decisions That Make Sense For Troubled Companies

Geoffrey L. Phillips and Jan S. Wolpert

A top-to-bottom analytical process helps ailing firms decide whether to sell for peak value or highest liquidity.

For financially healthy companies, business unit divestitures are common and important tools for reallocating capital and management resources to operations offering the highest returns to shareholders. Decisions on which units to sell generally are reached through a variety of classic strategy techniques. But if the parent is a "troubled company," the approach is altered, because divestitures almost always are a means for management to deal with a crisis situation — usually involving liquidity or forced changed of ownership.

In a distress scenario, the question of which business or which pieces of a business should be sold becomes a much more complex issue. Management must deal with a fundamental trade-off — value versus liquidity.

In a troubled-company environment, management must be willing to sell "stars" as well as "dogs." The underperforming business may be responsible for much of the parent's problems, and its divestiture may eliminate a cash drain. But this hard-sell unit might not generate proceeds capable of alleviating the liquidity crisis. Conversely, the star may fetch the best price, but a sale would mean loss of a business offering significant cash flow and long-term value. Indeed, troubled-company management must focus on "quickly realizable value" — possibly cashing in on long-term potential or potential that can't be achieved because of funding constraints.