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Will you set the divestment pace, or try to keep up with it?

Global Corporate Divestment Study 2019
Spotlight on Advanced manufacturing

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David Gale
EY Global Advanced Manufacturing Transactions Leader

The advanced manufacturing industry faces an immediate and unavoidable challenge: change the business model to embrace new technologies and service offerings or risk a steady decline in growth. Investors are scrutinizing old business models and demanding new sources of value. Companies in the sector need to adjust their thinking to take advantage of the opportunities offered by technology. Divestment will continue to be a fundamental part of this process.

The latest EY *Global Corporate Divestment Study* shows that 81% of advanced manufacturing businesses expect to make a divestment within the next two years, little changed from last year's record of 89%. This reflects a continuation of the transformation we have seen for several years: a focus on the core business and away from conglomeration. That transformation is now moving from the largest companies in the industry and is being embraced by middle-market businesses.

Two-thirds say their recent divestment was part of an effort to streamline the operating model. Looking ahead, this rises to 79%. The trend away from conglomeration, driven in part by activist shareholders, is one element of this story.

At the same time, 77% of advanced manufacturing companies say a unit's weak market position has already triggered a recent divestment, and 83% expect this to impact future divestment decisions.

> "The strategy to focus on core competencies is moving from the biggest companies down to middle-market manufacturers."
>
> **David Gale**
> EY Global Advanced Manufacturing Transactions Leader

Review the portfolio with a focus on technology

Companies in the sector have a keen eye on offering not just products, but technology-driven services that can generate an ongoing revenue stream. Examples include technology that can optimize machine maintenance and consulting services related to a manufacturer's products.

Rapidly changing technology and the opportunities presented by digitalization are expected to continue to drive divestment: 79% in the sector expect a rise in technology-driven divestments, while 70% believe sector convergence will make them more likely to divest in the next year. Funds from divestment can be used to invest not only in new technologies, but in a workforce with skills to employ them effectively.

79% expect a rise in technology-driven divestments in the next 12 months.

Prepare early

Opportunistic deals still account for a third of all divestments in the sector. Advanced manufacturing companies that do not maintain up-to-date valuations of their businesses, and which have never even contemplated how to divest them, may struggle to secure value. It is essential to prepare assets for both planned and opportunistic divestitures.

When they get an offer, how do manufacturing companies know it represents proper value? Once presented with an opportunistic offer, 71% of businesses say they began a competitive auction process to establish whether it represented good value and 54% say they looked back to their most recent portfolio review process.

81% of advanced manufacturing companies expect to initiate their next divestment within the next two years, with 60% expecting to do so in the next 12 months.

Close the valuation gap

While the pool of buyers for divested assets is expected to increase (56% see the number of buyers from outside the sector to increase in the next 12 months), many advanced manufacturing companies are concerned about their ability to secure the valuations they ascribe to their businesses: 63% say buyers are offering at least 20% less than sellers are looking for.

To close that valuation gap, advanced manufacturing companies need to focus on the whole buyer pool, including corporates and private equity acquirers. For the former, building the strongest possible case on synergies is essential, particularly where it is possible to articulate clearly how a buyer will achieve those gains. Right now, however, only 34% of advanced manufacturing companies say they presented the synergy opportunity to each likely buyer.

70% say sector convergence will make them more likely to divest in the next year.

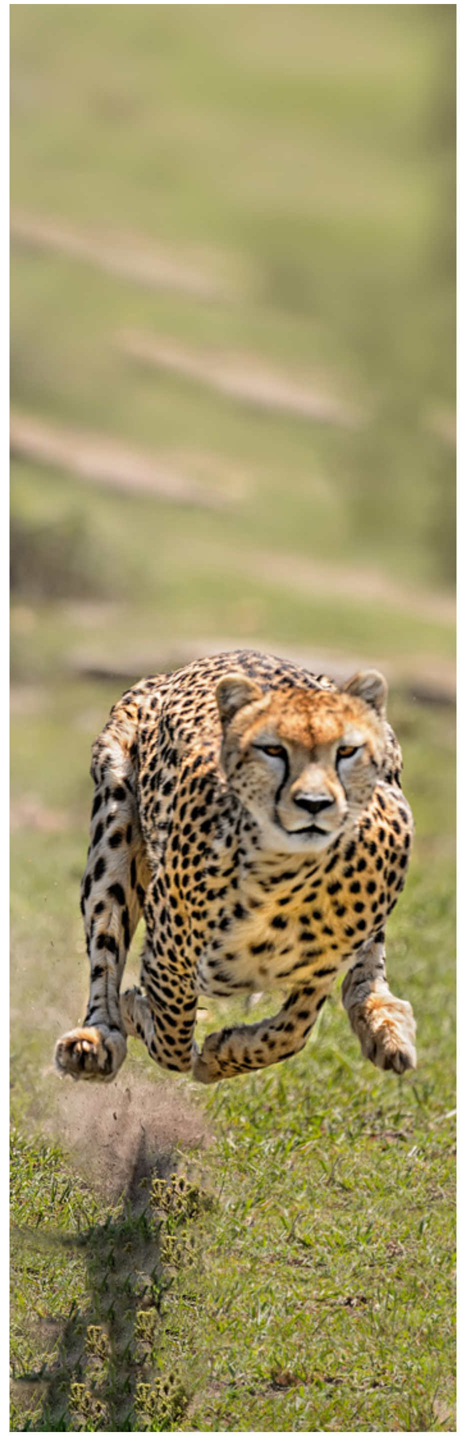
For private equity buyers, preparing a stand-alone operating model is essential to keeping them in a sales process. With record amounts of dry powder (US$703b globally) and favorable deal conditions, keeping PE engaged in the process can be vital to a successful deal. Thirty-seven percent said involving PE in their divestiture led to an increase in purchase price.

Use data to tell the story

Data and analytics tools increasingly offer a way to secure greater value from divestment strategy, but too few advanced manufacturing companies are exploiting the full potential of these technologies. While 70% of businesses use such tools to make divestment decisions in the first place, only 39% do so during negotiations with buyers.

Similarly, only 61% say they provided potential buyers with access to their data and the outputs of their advanced analytics in their latest divestment, but this was considered the initiative that created the most value.

Leveraging these tools to build a stronger case for potential buyers — and even to help buyers build a case themselves — may be a powerful value driver. The key is to identify supportable insight that makes a persuasive argument to the buy side. This will require high-quality data management that generates consistent and accurate outputs.



Conclusion

Advanced manufacturing businesses expect divestment activity to remain elevated over the next 12 months but 57% concede that shortcomings in their portfolio and strategic review process have sometimes resulted in a failure to achieve their expected divestment results.

Later in the deal, it is clear a lack of forward planning too often threatens to erode value, from failing to plan for workstream interdependencies to limited use of data and analytics.

Some of these issues are specific to the advanced manufacturing sector. For example, many companies now need to think of their divestment strategy in the context of the way in which technology is changing their business models. Others are failings that are common across many sectors.

Those advanced manufacturing companies that move fastest to remedy these shortcomings will reshape their portfolios more quickly and effectively — and generate more value than their rivals. As technology transforms their marketplace, these businesses will have a distinct edge.

> “Understanding the needs of specific buyers, and building separate value cases to address those needs, is an important way to maximize value in a divestment.”
>
> **David Gale**
> EY Global Advanced Manufacturing Transactions Leader

About this study

The EY *Global Corporate Divestment Study* focuses on how companies should approach portfolio strategy, improve divestment execution and future-proof their remaining business. The 2019 study results are based on 1,030 interviews with 930 senior corporate executives and 100 private equity executives. The survey was conducted between September and November 2018 by Acuris. Advanced manufacturing highlights are based on interviews with 70 executives in the advanced manufacturing sector (including those from industrial manufacturing and chemicals sectors).

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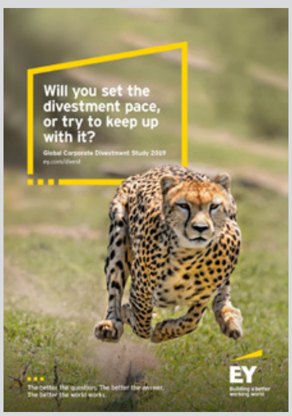

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To learn more and to have a conversation about your divestment strategy, please contact us:

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