# What Fortune Brands' bustup portends for investors

By Joe Cahill February 09, 2013

After a wave of corporate breakups swept through Chicago last year, we're getting the first indication of how well the strategy works.

Some of the biggest names in Chicago business—Abbott Laboratories, Kraft Foods Inc., Sara Lee Corp.—subdivided themselves in hopes that smaller companies with a narrower focus would produce better returns.

Most of the local bust-ups were completed within the past six months, too recently to draw conclusions about the performance of their newly independent halves. But we have an early case study in Fortune Brands Inc., which split its liquor and home-products businesses into separate publicly traded companies more than a year ago, after selling its Acushnet golf business to a South Korean partnership.

So far, the parts are doing better separately. Shares of Fortune Brands Home & Security Inc.—maker of Moen faucets and Master locks, among other things—have soared 166 percent since the split. Beam Inc., known for Jim Beam whiskey and other booze, boasts a 37 percent share-price lift. Both topped the rise of the S&P 500 for the same period, not to mention the 38 percent drop in Fortune Brands shares during the five years preceding the breakup.

Some of the gains stem from Wall Street's preference for one-trick ponies. Both new stocks trade at far higher price-earnings multiples than Fortune Brands got before activist investors started agitating for a breakup in 2010.

Their financial results are better, too. Beam's operating margin climbed to 23 percent in 2012 from 17.1 percent before the split. Revenue grew 6 percent. That's less than the 10.3 percent rise in 2011 but twice the spirits industry's overall growth rate last year.

The home-products company posted 8 percent revenue growth last year, more than double the 3 percent increase in 2011. Operating profit, excluding special items, jumped 40 percent.

These results jibe with research showing that more focused companies generally outpace their diversified peers, says Gregory Milano of Fortuna Advisors LLC in New York, which studied the performance of both types.

Conglomerates tend to “smear” capital across all their divisions rather than target the most promising opportunities, Mr. Milano says. Some initiatives get more funding than they deserve, while others get less. A focused company can concentrate investments on its top prospects.

“Our businesses are no longer competing for investments and resources with other businesses in unrelated industries,” explains Chris Klein, CEO of the Deerfield-based home-products business.

Single-business companies are quicker to seize opportunities, as well. A spokesman for Beam, also based in Deerfield, says, “We're faster on our feet” now that major decisions no longer require approval from the holding company.

Decision-makers closer to the front lines tend to reinvest more in the business, Mr. Milano says. As a result, more focused companies grow faster than diversified firms that spend more on share buybacks and dividends.

Some of this good fortune stems from external factors like the nascent housing recovery and the rising popularity of bourbon (Beam produces Maker's Mark).

But breaking up was the right move for Fortune, a classic conglomerate that sold different products to different customers through different distribution channels. The shortcomings of that business model became clear years ago.

The other local breakups, by contrast, bisected business lines that had more in common. Kraft and Sara Lee were packaged-foods makers, and Abbott sold medical products and drugs. Those deals will test the limits of the smaller-is-better theory. If they produce the kind of results Fortune's breakup has shown so far, expect more corporate divorces.