INTRODUCTION

Announced spinoffs continue to proliferate, with the list of recent and imminent deals increasing to 55 (see below). Safe and cheap ones remain hard to come by, though the short-term performance of most spinoffs has continued to outperform the market.

As you know, in addition to the spinoff calendar, we suggest one specific new idea each month, typically a spinoff, rights offering or other reorganization. As of today, our average return on all ideas since inception is 20.5% in the 6 months following each publication, i.e. 45% annualized. To maintain this performance, we tend to be pretty picky about price ratios. While spinoffs have reliably generated supernormal returns for decades, and continue to do so now, it's also true that prevailing prices are high for just about everything today. Spinoffs may start lofty and still go up – in fact, that's exactly what they're doing today – but when we find some other type of reorganization or other special situation, attractively priced at the outset, we'll write our in-depth section about that.

As a result, among the crop of spinoffs completed in the past several months, we've suggested Discovery Holding Company and Omega Flex, and passed on the rest for a variety of reasons, including but not limited to the following: net losses (Proliance/Modine, GSE/GP Strategies), P/E ratio exceeding 20 (WebMD, Treehouse, Expedia), or unpredictable industry outlook (Fidelity National Title). Many of these have worked out very well; we don't mind missing some good ones as long as we successfully avoid bad ones.

With some reluctance, we declined to propose Ameriprise, though it is profitable and reasonably priced. The reasoning had to do with visibility (market cap over $10 billion, as well as a huge consumer advertising blitz), which makes bargain pricing less likely. There were also concerns about declining business attractiveness, for two reasons. First, Ameriprise in recent years abandoned its practice of aggressively marketing proprietary mutual funds to individuals through a high-pressure sales force. Its clients may now choose from listed mutual funds, most of which have higher returns and lower fees than the captive Ameriprise funds, so there exists new pricing pressure. Second, aside from the profitable captive funds, Ameriprise's key business advantage was the American Express brand. This unfair advantage is now gone. To lose one of the world's most recognizable brands is so earthshaking a change that we didn't see a meaningful way to assess its impact, and as a result, we didn't cover it.

It should be stated here that skeptics of our position on Ameriprise would be in very good company. The stock is up 25% in the two months since it floated. Moreover, Warren Buffett, Oracle of Omaha, greatest living investor, et cetera, has not sold the Ameriprise shares Berkshire Hathaway inherited in the spinoff. We think it's because his basis is so low, but you may conclude differently.

A NOTE ON CANADIAN INCOME TRUSTS

For several years, and accelerating in the past year, various Canadian firms have been spinning subsidiaries into income trusts, which are pass-through entities, similar to REITs, but with fewer operating restrictions. The effect of conversion from corporation to income trust is to instantly increase share value by eliminating corporate tax. The Canadian government has confirmed recently that firms have broad latitude to set up such trusts, and that the current friendly regulatory environment will not change soon.

Does a passive investor benefit from this? Yes, but generally only if you already happen to own shares in the parent prior to the announcement. The Canadian market is so eager for these events, and visibility so high, that the increased value is more or less instantly captured in the parent's price upon announcement of a new income trust spinoff.

There is an additional risk, warned of with considerable prescience in a 1997 article from Burgundy Asset Management of Toronto. Because of the excitement for these vehicles, an IPO gold rush has sprung up around them, with all the attendant dangers. The biggest is the incentive to underestimate future required capital expenditures, driving higher current payouts and thus a better IPO valuation. One can find Canadian income trusts right now with a P/E ratio of 30 and dividend payout ratio of 10%. That can't work for long.

A retired Barclays Global Investors executive we know once chuckled about a disappointing investment in 1999, saying, "It was just too early. But 'early' and 'wrong' are pretty much the same thing." For Canadian income trusts, Burgundy's call, though years early, may yet turn out right. And at that point, a few investment opportunities may appear north of the border.

For now, the biggest opportunity is apparently in private equity: acquire control of a Canadian firm, convert some portion of it to an income trust, and pocket the increased value through an IPO or other sale.

NEENAH PAPER – STILL AVAILABLE

You may remember our January 2005 suggestion, Neenah Paper, which spun off from Kimberly-Clark in December 2004. Those who invested (such as the author, we disclaim) have watched NP decline 8% and then sit there, held down by a higher dollar and lower pulp prices. We don't dredge up this disappointment to wallow in grief: the point is that we think it's still a bargain. The attractive hidden asset remains the company's roughly 1 million acres of Nova Scotia timberland, held on the books at $5 per acre but worth over 100 times that, based on certain public statements to the Canadian government by Kimberly-Clark prior to the spinoff. This puts adjusted book value at well over the current price of about 29. The company's Canadian holdings and operations remain a good dollar hedge for those who think deficits matter.

MORE INSIDER TRADING

Large-scale insider buying is a relatively reliable signal of potential value. This month's idea, **American Eagle Outfitters** (NYSE: AEOS), offers an example. More information on American Eagle follows the spinoff list below.

While we usually only mention one specific idea per issue, this month we wanted to offer as an aside one other potentially interesting situation: micro cap **Lynch Corporation** (Amex: LGL). It closed today at $7.90, which is within a stone's throw of the 52-week low, approximately equal to the company's tangible net worth, and only 6 times its past 9 months' earnings. This company is simultaneously deploying a number of tactics we find interesting:

- *Going dark*. The firm is voluntarily deregistering to eliminate SEC reporting requirements, and delisting from the American Stock Exchange. Elimination of the expensive Sarbanes-Oxley compliance regime will make Lynch more profitable, yet its retreat to the Pink Sheets causes institutions to sell indiscriminately in anticipation of lower liquidity. The result can be a window in which intrinsic value is rising as price is falling – a potential buying opportunity.
- *Insider buying above current price*. In October, chairman Marc Gabelli – son of veteran value investor Mario Gabelli – indirectly purchased $1.8 million in LGL at over $13 per share, a significant premium to the current price, to fund a recent LGL acquisition.
- *Tradable rights offering with oversubscription privilege*. Expiring this Friday, the Lynch rights (symbol: LGL-R) currently trade at 30 cents. 3 rights may be converted to one share of LGL common at $7.25 per share. That makes it sound like the rights are selling at a premium, but this may not turn out to be the case, due to the oversubscription privilege. After Friday, unexercised rights will be given free, pro rata, to whoever exercised his rights.

Among these events, the tradable rights are probably least interesting, because 28% of the rights would have to go unexercised for an arbitrage to work out, and no one can reasonably predict this outcome. The insider purchase could potentially be attributable to reasons other than direct value, but with this particular manager, it seems unlikely. The going-dark transactions are most interesting because it implies management believes the business is intrinsically strong enough to finance itself with diminished access to the equity markets.

The initial signals are certainly intriguing. For those with a tolerance for illiquidity, this one might be worth further research.

SPINOFF CALENDAR

Company	Parent	Type	Nation	Date
Treehouse Foods (NYSE: THS)	Dean Foods (NYSE: DF)	Distrib	USA	Jun-05
Discovery Holding Company (Nasdaq: DISCA)	Liberty Media (NYSE: L)	Distrib	USA	Jun-05
Expedia (Nasdaq: EXPE)	InterActive Corp. (Nasdaq: IACI)	IPO	USA	Jul-05
Proliance (AMEX: PLI)	Modine (NYSE: MOD)	Distrib	USA	Jul-05
GSE Systems (Amex: GVP)	GP Strategies (NYSE: GPX)	Distrib	USA	Sep-05
WebMD Health (Nasdaq: WBMD)	WebMD (Nasdaq: HLTH)	IPO	USA	Sep-05
Ameriprise (NYSE: AMP)	American Express (NYSE: AXP)	Distrib	USA	Sep-05
Alinta Infrastructure Holdings (Sydney: AIHCA)	Alinta (Sydney: ALN)	IPO	Australia	Oct-05
Fidelity National Title (NYSE: FNT)	Fidelity National Financial (NYSE: FNF)	Distrib	USA	Oct-05
Clear Channel Outdoor Holdings (NYSE: CCO)	Clear Channel Comm. (NYSE: CCU)	IPO	USA	11/11/2005
Tronox (NYSE: TRX)	Kerr-McGee (NYSE: KMG)	IPO	USA	11/28/2005
SK Petrochemicals	SK Chemicals	TBA	S. Korea	12/1/2005
Burberry (LSE: BRBY)	GUS plc (LSE: GUS)	Distrib	UK	12/13/2005
Spansion (Nasdaq: SPSN)	AMD (NYSE: AMD)	IPO	USA	12/15/2005
Goodman Fielder	Burns Philp (Sydney: BPC)	IPO	Australia	12/19/2005
CCE Spinco	Clear Channel Comm. (NYSE: CCU)	Distrib	USA	12/21/2005
Triple Crown Media (Nasdaq: TCMI)	Gray Television (NYSE: GTN)	Distrib	USA	12/30/2005
Delia's (Nasdaq: DLIA)	Alloy (Nasdaq: ALOY)	Distrib	USA	Dec-05
Charity Tunes Inc.	Sound Revolution Inc. (OTCBB: SRVN)	Distrib	USA	Q4 2005
CBS Corporation	Viacom (NYSE: VIA)	Distrib	USA	1/3/2006
Southland Health Services	Bad Toys Inc. (OTCBB: BTYH)	Distrib	USA	1/12/2006
Polyus Gold	Norilsk (Pink Sheets: NILSY)	Distrib	Russia	3/3/2006
Chipotle	McDonalds (NYSE: MCD)	IPO	USA	Q1 2006
Wholesale candle unit -- name TBA	Blyth Inc. (NYSE: BTH)	Distrib	USA	Q1 2006
Real estate unit -- name TBA	Cendant (NYSE: CD)	Distrib	USA	Q2 2006
Motels unit -- name TBA	Cendant (NYSE: CD)	Distrib	USA	Q2 2006
Travel bookings unit -- name TBA	Cendant (NYSE: CD)	Distrib	USA	Q2 2006
Rental car unit -- name TBA	Cendant (NYSE: CD)	Distrib	USA	Q2 2006
Local Telecoms Division -- name TBA	Sprint Nextel (NYSE: S)	TBA	NYSE	Q2 2006
Ansaldo Trasporti Sistemi Ferroviari	Finmeccanica (Milan: FNC)	IPO	Italy	Q2 2006
Tronox (NYSE: TRX)	Kerr-McGee (NYSE: KMG)	distrib	USA	Q2 2006
Capital Services	Pitney Bowes (NYSE: PBI)	Distrib	USA	Q2 2006
Drug wholesaling -- name TBA	Orion Corporation	Distrib	Finland	Q2 2006
Memory chip business -- name TBA	Infineon Technologies	Distrib	USA	Q2 2006
Verichip	Applied Digital Solutions (Nasdaq: ADSX)	IPO	USA	Q2 2006
Greenvest Technologies Inc.	Mass Megawatts Wind Power (OTCBB: MMGW)	Distrib	USA	Q2 2006
Valor (NYSE: VCG) - reverse merger	Alltel (NYSE: AT)	Distrib	USA	Q2 2006
Hanesbrands	Sara Lee	Distrib	USA	Q3 2006
Chemical division -- name TBA	Altana AG (NYSE: AAA)	TBA	Germany	2006
Avago	Agilent (NYSE: A)	IPO	USA	2006
Praxis Automation SA	Intracom: (Berlin: INT)	Distrib	Greece	2006
Ilida Hellas SA	Intracom: (Berlin: INT)	Distrib	Greece	2006
Crystaal Pharmaceuticals	Biovail (Toronto: BVF)	Distrib	Canada	2006
FTS Wireless	FTS Group (OTCBB: FLIP)	Distrib	USA	TBA
Gedas AG	Volkswagen AG	IPO	Germany	TBA

UK Thames Water and American Water Works	RWE (Pink Sheets: RWEOY)	IPO	Germany	TBA
Heartstitch	Sutura (OTCBB: SUTU)	Distrib	USA	TBA
Lottery Corporation	Games, Inc. (OTCBB: GMSI)	Distrib	USA	TBA
Water Products unit -- name TBA	Walter Industries (NYSE: WLT)	Distrib	USA	TBA
Uranium assets -- name TBA	Crescent Gold (Sydney: CRE)	Distrib	Australia	TBA
Rosetta Resources	Calpine (NYSE: CPN)	IPO	USA	TBA
Aquacell Water	Aquacell Technologies (AMEX: AQA)	Distrib	USA	TBA
Mariner Energy Resources	Forest Oil (NYSE: FST)	Distrib	USA	TBA
G2	IMSA (Mexico: IMSAUBC)	Distrib	Mexico	TBA
Targeted immunotherapy assets -- name TBA	Inex Pharmaceuticals (Toronto: IEX)	Distrib	Canada	TBA

LISTING CRITERIA

Spinoffs are listed when announced by management as certain to occur. They are included only if intended to be available to outside passive minority shareholders. The list does not include private equity deals.

The date shown is generally the record date for distributions or the initial trade date for IPOs. Trading symbols are provided where available.

There are no quality requirements for the above list. As a result, while most of the above are legitimate businesses, several are highly speculative concept companies, almost always located in sunny climes, with little or no revenue – for example, Aquacell, Sound Revolution, Games Inc., Sutura and FTS Group. (The latter sports the unfortunate OTC ticker "FLIP.")

Multiple events result in multiple listings. For example, this month, Tronox is listed twice. Its A shares were floated by IPO this year, and Kerr-McGee will distribute Tronox B shares to its stockholders sometime in 2006.

Items are included for some time after the record date, because the opportunity is often best several months after the fact.

Announcements of possible spinoffs, which appear frequently in the press, are not included here, because possibilities are generally not as investable as facts.

FEEDBACK

If you find we're routinely leaving out information you would find relevant to your research, please email bmitchell@spinoffprofiles.com with your suggestions. When we receive a preponderance of sensible requests for a particular element, we'll include it in future issues.

ABOUT THE AUTHOR

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INSIDER PURCHASE / BUYBACK

STRUCTURE

BACKGROUND

About ten weeks ago, Jay Schottenstein, chairman of American Eagle Outfitters (NASDAQ: AEOS), bought a million shares of AEOS. Around the same time, the company bought back 4.4% of its own stock, and announced it would buy more.

TERMS

On September 22, American Eagle's chairman reported open market purchases of one million shares at a blended price above $21 per share. In November, the company reported it had repurchased 6 million shares in Q3 2005, and intended to buy back another 4.5 million in the current quarter.

RECENT PRICE HISTORY

American Eagle Outfitters has apparently fallen out of favor with growth investors, yet its merits haven't yet been noticed by cooler heads – except in the company's own management.

The price has been falling, off and on, since July, and is now off about 35% from its peak. The stock tanked in the third week of September, falling 20% in a matter of days. Why? Because the company reported it expected earnings *growth* of 13% (very close to its 5-year average) instead of 17%. The stock fell sharply again after Thanksgiving, when the company reported it expected fourth quarter earnings to come in just 2.7% below analyst estimates, touching a 52-week low last Tuesday, December 6.

AUTHOR OWNERSHIP

Author does not own AEOS.

American Eagle Outfitters

Company Information

BUSINESS

American Eagle Outfitters is an apparel retailer with 866 outlets in the U.S. and Canada. It is positioned as a low-cost competitor to Abercrombie & Fitch.

American Eagle recently generated a 13% net margin and 24% return on equity, with essentially no debt. Earnings have grown at a compounded 14% for the past 5 years, and appear likely to come in near that rate for the current fiscal year. Compared to its industry, the company's financials are unusually attractive in most dimensions, especially inventory turnover.

VALUATION

Does the collapse in share price (see left) make sense here? P/E is now 11.8, and the dividend yield 1.4%. The company is still profitable, growing, and shows no hint of inventory buildup. Qualitatively, the stores are still full of teenagers with their wallets out (we stopped by for a peek), and above all, knowledgeable insiders are buying.

Indeed, management is feasting on AEOS. Chairman Schottenstein grabbed 0.7% of the company within a few days after the September decline. By the end of the year, the company will have repurchased nearly 7% of its own stock in two quarters. Yet today's close of $21.28 is about what Schottenstein paid in September.

Whether AEOS is a good buy is not so much a guessing game about Christmas as a question of whether American Eagle is a stable, well financed, profitable, inexpensive enterprise that would thrive in an upturn and survive a slow season.

Look first at the downside: if this Christmas were an unmitigated disaster – and current evidence points to nothing so extreme – aggregate sales might be down 5%. How much lower could AEOS go? P/E is already only half the industry norm, and the company's unusually low inventory leaves the business less exposed to a poor season. On the other hand, look at the upside: if sales are flat or better, it would be reasonable to see AEOS eventually regress to at least the long-term pan-market mean PE of 16, implying a price of 23.

RISKS

A worst-case Christmas would turn this into a waiting game or a dollar cost averaging game, but would not necessarily spell failure. There are no sure things, but when a profitable, established, low-debt business is selling this cheap, with some growth as a bonus, the deck is certainly stacked toward success.

Moreover, in considering risk of ownership, look at the risk your chairman faces: his basis is 21 and change, the same as yours. Like sharing the captain's lifeboat, this alignment of exposure can be motivational to management and beneficial to your own results.

PROPOSED TACTIC

Buy and hold.