Mergers, Acquisitions and Corporate Restructuring
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Lecture - 37
Alternative Exit and Restructuring Strategies - 2

Hello friends welcome to another session on mergers acquisition and corporate restructuring. In the previous session we talked about alternative exit strategy and alternative expense strategies. Alternative means alternative to mergers and acquisitions there could be several other ways to grow expand or contract the business and will continue with those topics, in this session also.

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So the concept that we have in this session is how to grow through non M and A activities versatile could be business alliances can have and franchising licensing as source of growth.

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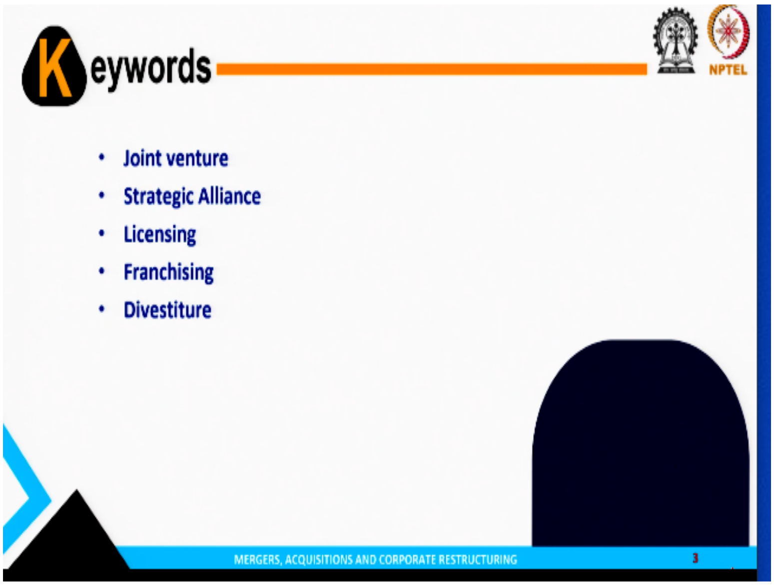

So, these are the keyword that we have joint venture, strategic alliance, licensing, franchising and divestiture as alternative exit strategy or expansion strategies.

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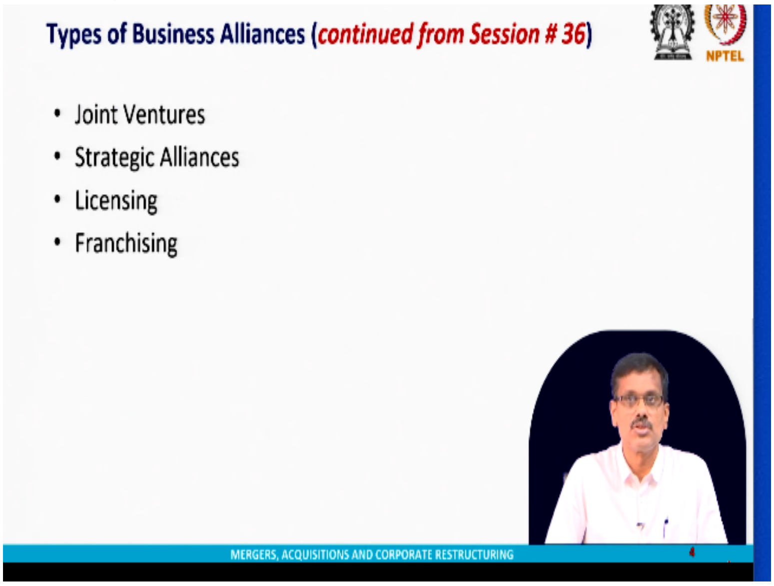

So, we had the last session we discussed in the last slide in the previous session that whatever business alliances could be there that there could be joint ventures, strategic alliances licensing and franchising these are the business alliances. So the subsequent slides we will discuss about each of one of them and at the end we will talk about divestiture as a business strategy.

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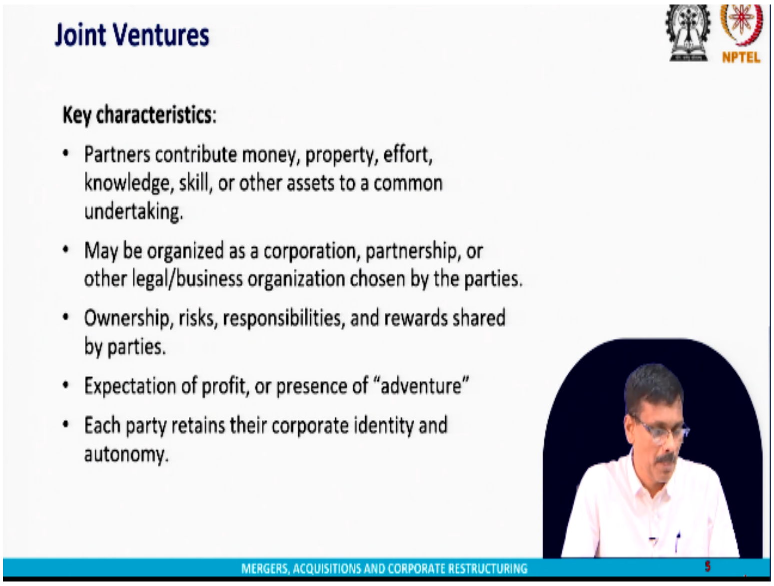

So why need to joint venture it is the word joint itself explains that to more than one party comes together and joint and start a new venture that is the meaning of joint venture and the joint venture parties can participate in terms of money, property, efforts, works, knowledge skill or any other asset and so that a common undertaking is there and a new venture is formed, and also seasonal joint ventures can be there.

Like in case of festival times some 2 3 people will come together and have some seasonal joint signature can be seasonal ventures can be done by jointly. So these are all temporary businesses and this same group of people also can come together and do another business during let us say Diwali then the Dasara something like that during festival season or near during new year but that is joint venture called a temperate joint venture to do some job and get the benefit commercially and then getting close down.

But we are not talking about such joint ventures here we are talking about joint venture where the 2 entities come together and pull their skills different type of skills and form a new venture for the purpose of growth and which is supposed to benefit both the entities which are joint venture partners. It can be a company or corporation it can be a partnership or it can be any other legal business organization setup by the parties.

And the ownership, the risk, the responsibilities and rewards are also shared among the partners there have been agreement between the partners that how those things are to be shared. So unless in otherwise mentioned we can expect that it is equally shared between 2 parties, and there is a expectation profit and also there could be some risk or adventure involved we have got 2 companies coming together under certain understanding common understanding but subsequently there could be some problems also in managing joints venture.

So there is also a risk involved it can be taken in the adventure for the 2 companies which are coming together and setting up new unit and at the same time each party on their own maintain their identity they do not lose that they are corporation there. So company A and company B come together and set up a company C. So company A is having its own identity company B is also having its own identity but company C is form is a new companies form.

As we discussed in the previous class like in initially Maruti limited was set up by, government of India and Suzuki Corporation. So Suzuki Corporation had a joint venture with government of India so for producing and selling cars passenger cars in India that does not mean Suzuki corporation lost its identity. So the corporation in Japan has its own identity but they extended their technology platform, logo, rights etcetera so that these type cars in the name Maruti can be produced and sold.

So that way several companies come together to have several joint ventures likes we also discussed Tata group and Starbucks. So Starbucks is a player in coffee market and Tata group is a player in different activities is conglomerate. So Tata group and Starbucks have come together two half Starbucks outlets and product services given provided in India assets. So Tata group has its own identity Starbucks has his own identity.

But they have found a new identity Tata group Starbucks in India for that matter and they have their own autonomy but joint venture is managed by 2 of these companies and they will be pooling resources and deciding who is doing? Who is going to be doing, what.

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So what are the rational for joint ventures could be strategic planning companies like to grow to different market try to have new technology they have to expand in new market for that matter as an example in the Starbucks will like to expand its operations as an MNC in India for that matter. So it has to start from this cross set up the unit assuming the foreign direct investment guidelines permit them assuming that also.

But they have to start from the scratch and look at where they can set up but if they are having got a tie up with the Tata group. Tata group being local player in this country they will be helpful for the growth of Starbucks in their products and at the same time Tata group also has the advantage of using Starbucks. A famous Starbucks logo or the business and they are also known so for them the growth is also it is mutually beneficial for both the companies to have a mention.

So that could the plan for the company for the growth companies can acquire knowledge. So 2 companies come and share somebody may give technology knowledge somebody may give market knowledge or product knowledge somebody may have very good customer base so those things also can be said and new entity can take advantage of the resources of both the companies and when the skills resources share it is possible that risk is also reduced.

Otherwise, 1 company has to do everything they have to acquire technology process etcetera and that can be more riskier than having a joint venture, where risky also shared and as we discussed earlier there could be several international brands opportunities. So in that case joint venture can be a way to go to that market, or to have the international products in the product portfolio of the domestic company. So, international aspects can also be taken care for the growth purpose.

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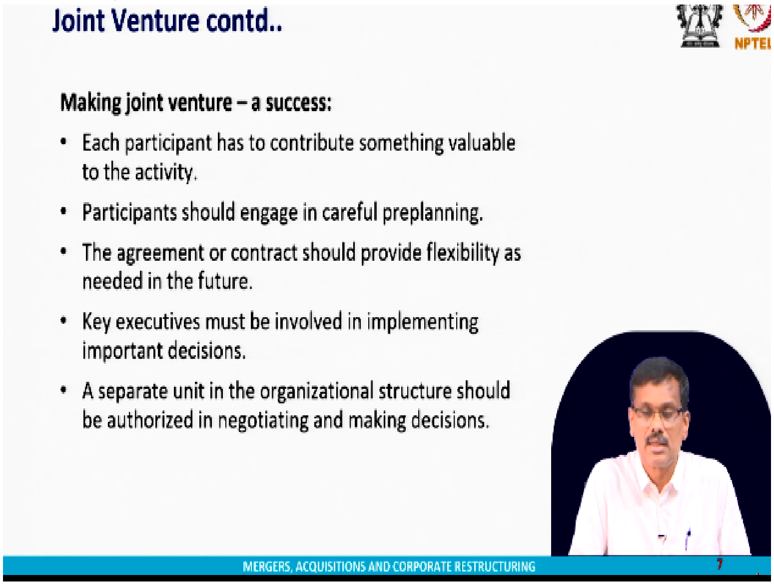

And what can be there so that joint venture becomes a successful venture so each participant has to contribute something valuable to the table. Otherwise it may look like that 1 participant superior another participant superior so that may lead to problems so the equally they should be valuable to the new entity and there should be contributing substantially to the company's growth, plan, technology, strategy etcetera.

Like for example somebody may give a market related information resources somebody may give a product and technology related information. Somebody may have a very large retail network in the country and another country may into new product you can get new product and introduce that product in the already established retail network by company in the domestic market for that matter.

So something somebody has to give some valuable things somebody may go for say we use our logo or and the brand for that matter and expand the business and the azure joint venture and there has to be lot of pre-planning it cannot be done overnight. So pre-planning has to be there in all the aspects starting from like any business plan starting for from the customer needs till execution and customer service between technology set on the plant facilities network etcetera.

So pre-planning has to be there is done very carefully like any other business and its the agreement that is there between 2 parties need not be rigid there should be a scope for changing the agreement if the time requires say the need arises. So instead of some flexibility has to be there. So that in future depending on the changing conditions, changing expectations the agreement can be it rules the conditions can be changed not to have a rigid agreement that is this agreement is there otherwise the business cannot go on change should be possible.

And the joint venture must have support of the key executives, top executives of both the companies, because at the end of the day certain decisions are taken by top management. Top management not in the play. So then it becomes difficult to execute the joint venture assets and it is always better that a separate unit or organization structure is there so that they authorize and the then make the decision.

They should not be a subsidiary of another company rather they should be independent organization having investment from both the parties more than 1 or 2 parties for that matter and there is independent organization should be there instead of being a whole subsidiary as it can be group company but not a subsidiary company where the holding company may have the decision making rights for that matter.

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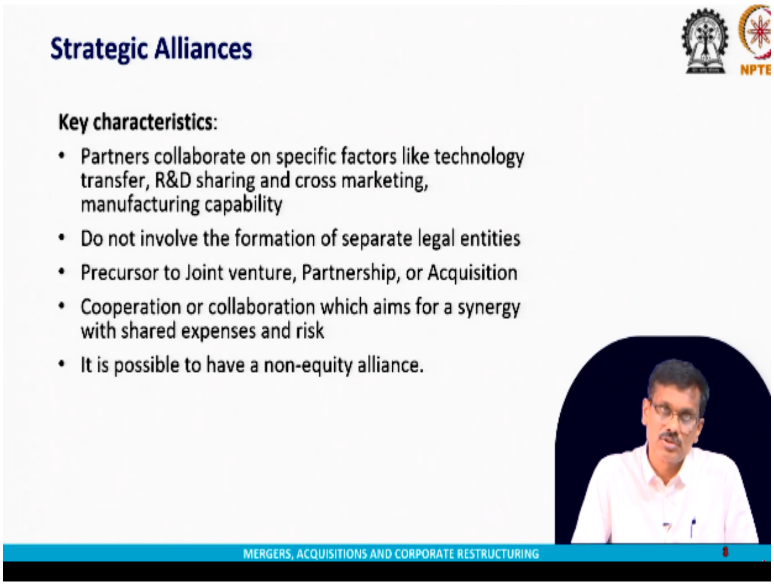

Then we go to another thing that is strategic alliances in joint venture mostly we see that there is equity investment is there that means 2 companies come together they put also the money in that, but you one can also have alliance another partner without having inequity. So strategic alliance can be there for a particular strategy for a particular purpose without having equity investment that means strategic alliance can be non equity as well as equity.

When I say equity means ownership in the entity for that matter strategic alliance can be there with an existing company and the existing company can borrow. The resources of another company of international reputed player and expand its business and its not necessarily it involves the formation of legal entities and but strategic alliance could be taken as a precursor to joint venture partnership or maybe subsequently in acquisition of the company also.

So strategic alliance can be starting point in the growth story of a particular company and it is expected that this cooperation collapse in where 2 parties are there which aims for a synergy with shared expansion shared some expenses can be shared some risk also can be shared. When strategic alliances actually are formed and as you discussed it is possible to have a non equity alliance it is not necessary that both the partners have to put investment equity or ownership the company.

Because new company will be formed and existing company can get the alliance of another entity without having their equity participation in the company also subsequently the companies can think of having a joint venture or having a separate unity setup with participation in equity of both the companies. So, strategic alliances can be precursor for that matter.

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So if you look at certain benefits could be there as in joint venture you have access to knowledge one has access to new technology one has actually intellectual property rights and each partner will focus on their competitive advantage and we have because a new corporate ecosystem is formed and so that you can achieve the desired results and because you are having new technology new processes which possibly helps improve the operations of the company.

So that can possibly reduce the risk or uncertainty and also it can help us enter new market either domestic or international or both for that matter and you can also access the resources also target different markets this could be the benefits of strategic alliance.

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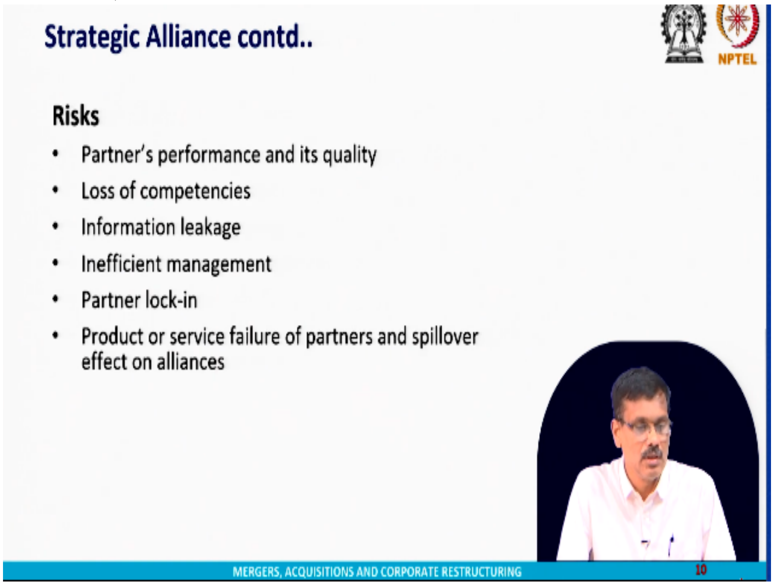

But there could be some risk involved in strategic alliance because partners performance can drive so that they are not doing well. Then the reputation of the alliance partner also is at risk then whatever thinking earlier that particular alliance is giving a new technology. So it helps us grow by the technology may not be now sound or something some other substitute might have come in the meantime and some other companies might be able to use those technologies and out perform this your organization for that matter so that is a risk involved.

Because one may have an agreement to use this particular alliance for certain period of time so till that time changing technology changing that alliance, may be difficult there could be some cost involved if somebody has to break the alliance for that matter. So that risk is always there if computation for which we went for the static alliance that alliance has lost the competence this problem can be there.

Similarly, there could be information leakage somebody may pass the information prior to this the real these things being formed. So that is also another risk involved management may be inefficient to manage the alliance and partner lock-in means if you are going to be with a alliances with us for next 3 or 4 years and n number of years you cannot have another partner. So that is something also if it does that then maybe some compensation may have to be paid to the alliance partner if the alliance has to be broken for that matter.

So that is also this is cost can be involved if somebody has to break their alliances or you have to wait for certain period of time to go to conclude this alliance to be closed and new alliance can be found with the new entities for that matter. Similarly the alliance partners products or services may fail in the market and we have a partnership with the first technology but people know, that you have a partnership with them the customers know about that.

And since alliance partners products are becoming unsuccessful or there is some problem with their product and services so there can be spillover effect of that on this company which is using their technologies for that matter which have formed alliance with them. So that risk is always there whenever there is a problem with a particular brand sonagraph is also have affects the other products of the same company itself.

So that risk is always there so alliances partner has some problem it can affect the company's performance it can also happen both the way that the company which is got the technology as an alliance from some other company. If the company has got the license or the alliance to its advantage if that company does something wrong something bad it can also affect the reputation of the company which has given those technologies for that matter. So both ways it is possible so the partner risk is always there and can have a spillover effect on the other partner.

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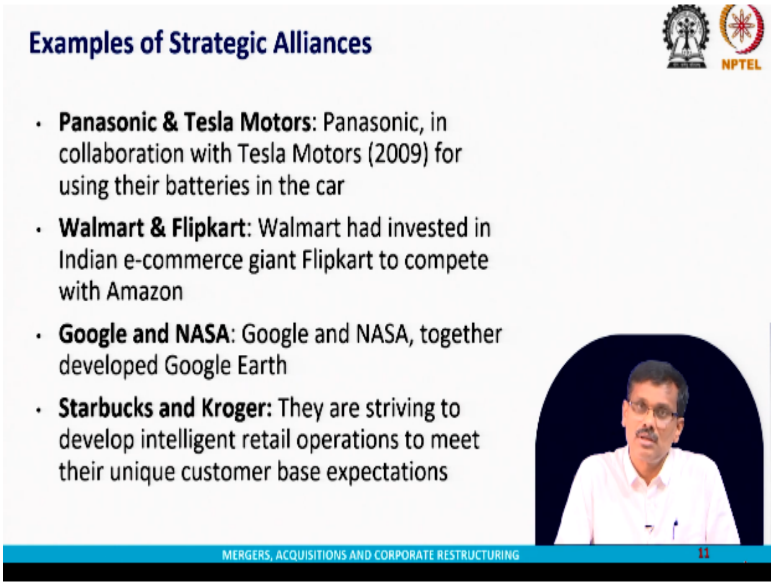

So there are certain example that we have here like Panasonic and Tesla motors they had a collaboration in 2009 for using their batteries in the car tesla, motors could use the batteries of Panasonic for that matter. Walmart and Flipkart came for strategic alliances of course there you had investments by Walmart in Flipkart, so to compete with Amazon retail in India. Amazon is another multinational player which is having operations in India and to compete with them Walmart also want to expand Flipkart has been a Indian market already.

So Walmart to expand to Indian market they thought of coming and joining with Flipkart instead of starting their own company in India for that matter for online ventures. Google and NASA this is called a technology tie up and it is a tie up between a government agency not-for-profit agency and the for-profit agency like Google and NASA. So they came together to have this product called Google Earth.

Starbucks and Kroger, Kroger is a company which is inter retail business in external in developed countries. So Kroger had the Starbucks little so Kroger could have this sale of Starbucks production services its a retail units. So Starbucks also could expand to have and got the access to the customers of Kroger. So it is mutually beneficial for their matters a retail chain called Kroger got the alliance Starbucks. So Starbucks products are sold in Kroger outlets.

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Similarly, if you look at a 1 prominent company in India as reliance industries group that group a conglomerate. So if you look at they have a different strategic alliances like they have a strategic alliance a British petroleum of course this alliance also involves equity investment by British petroleum in reliance group company. So that has helped that is helping them or developing oil and gas fields in exploration, the retail business of petroleum fuel that is in the now it is known as JioBP that BP brand is being used.

The British Petroleum brand is being used so Jio has access to the brand loyalty of British Petroleum they have a technology access to British petroleum and also British petroleum could be expanding to Indian market with having a tie up with reliance industries as in the form of JioBP for this. So it is mutually beneficial for both the companies similar reliance Jio platform has gotten alliance and partnership with Qualcomm US based telecom company and although there that alliance has been there for a very good time.

But recently they have got some more investment so for the purpose of 5G infrastructure service development in reliance Jio that reliance telecom venture for that matter. Similarly, reliance India has purchased a Ambri pilot system which is used for energy storage system which is possibly the future of energy sector and the Ambri is a startup in US which focus on clean energy and in fact Ambri reliance industries already harvest equity in the strategic investor.

So their strategic in which that company and they are also taking the technology for developing the energy storage system in at their end that is a reliance end. So this is some few of the example that you have with respiratory alliance reliance industry has got several other alliances and tie ups with different other companies. If you look at any conglomerate in India be reliance be Tata group and with any other group of big companies for that matter.

We will find that they have got different business they have grown with the help of alliances with other established players that is a very much required assets for the growth of the company.

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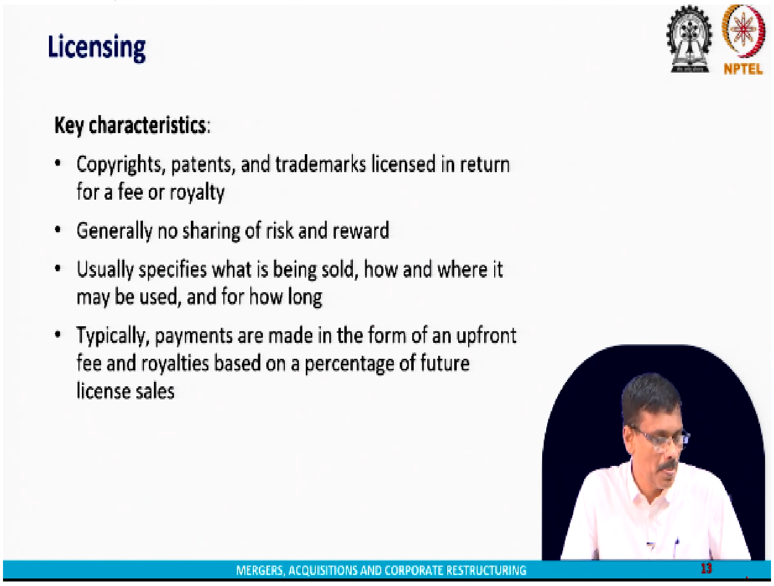

So licensing is another form of alliances so here what happens a company gives the license to use its logo product character of copyrights, patents, trademarks in return of fee or royalty. So we will get the license to use a particular product and for every use or product produced for that matter will be giving a amount per unit product produced for that matter or maybe there is no retainer field also could be there.

Where you give a fixed amount whether you use or do not use plus a variable component depending on the uses, and production of the company for that matter, and after that there is no other sharing of risk there, reward because royalty is paid there is no other risk to be shared or reward shared and it is we have taken the companies taken the license the risk is always them only. That is beneficial nothing like it not beneficial the licensor has does not have any obligation for that.

And but there is a clear cut agreement being what is being sold, how it is being sold, how it is produced, how it is developed, what type of ingredients are used? Everything has to be very much clearly provided by the licensor in terms of an agreement the licensee, because if there is a problem at the end of the licensee and the people come to know that they are using a particular license of another company. So there could be spillover effect on the reputation of the company which has given the license.

They cannot just say that it is their problem what they did with that is not that maybe legally there might be any problem for them, but reputation wise the problem can always be there for the licensure and typically the payments are made in the upfront fee as a fixed amount in the beginning and then subsequently variable component can pay depending on the usage or sales of the company for that matter.

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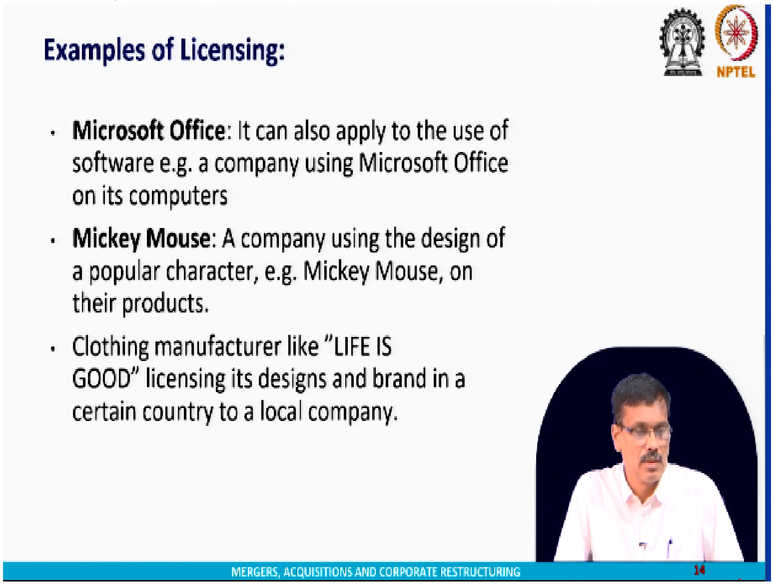

Some examples that we have Microsoft office it has got the license given to use its production services by different companies and the companies can claim that they are using the Microsoft license Microsoft products and they can also use their logo and say that we are using. So a customer a client of company X which uses Microsoft office products or Microsoft products for that matter they rely on the company because they are using Microsoft.

They are more relying on the reputation of the Microsoft products and Microsoft as a company for that matter. Similarly, Mickey Mouse which is popular characters in this different products Mickey Mouse logo is used. So somebody can take the license and use it and sell the products in the other market, but they have to conform to those logos and licenses properly there should not be any problem with that they change the design or they change the logo or something it will be as is basis that logo has to be there.

Then their company life is good as a company which also gives license its designs and brand to certain particular country for a local company. So further manufacturing of the cloth production of cloth and there the life is good can be mentioned, but production is done by another company they have only sold but they can take the advantage of that particular logo life is good for that matter.

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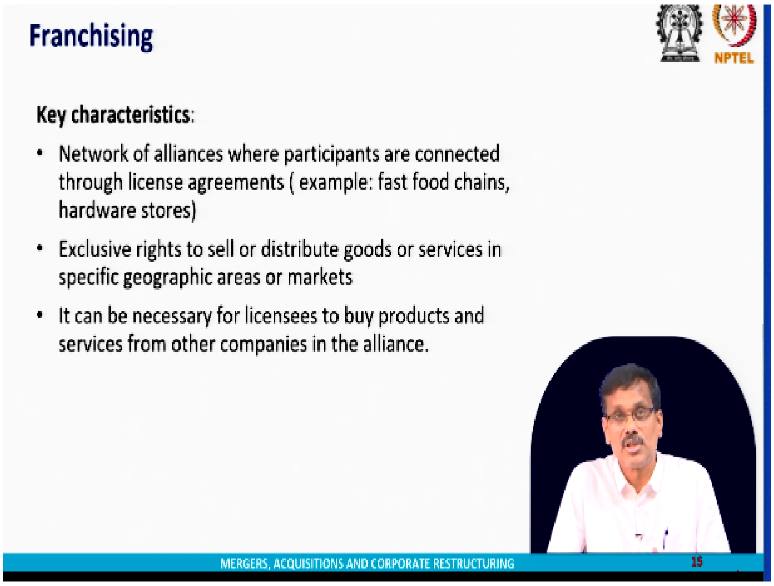

Then another thing that we have in this alliance and joint ventures like tag or strategic alliance type business alliance is that franchising. So franchising what happens where a network alliances where participants are connected through license agreements mostly we find fast food chains we find that in certain hardware stores we can find that. So there is an exclusive rights to sell or distribute the goods and services in a particular area geographic or market for that matter.

So the franchisor gives the franchise to some company to sell the product in a particular location. So nobody can use that franchise in that country no one kills because they only have the exclusive rights to use that particular product and it also necessary that certain times what happens? When you are using the license and using a particular products license particular company's license or franchise for that matter franchise you may have to also use their ingredients.

So besides that, logo or the store etcetera you have to also source the material for them that is possible and they also say how this particular product will be sold, how the products will be the layout will be there in the retail outlet, how the look will be there, what will be the type of leaflet for that matter? All the merchandise material what is there has to be also asked for the specification of the franchisor. So that is something one has to be careful and there is any change in the ingredient they find out so there could be also penalty for the franchise.

So that is what some but the best part is that a customer comes to this particular outlet which is franchise because of the reputation franchise so there could be a particular product, available across the world. So, tourist people tourists come to your country a location so they are bothered about a particular product to be purchased by them or to consume by them. So once they have see that particular logo or the product they will come to that particular outlet and buy them. Because they are very much they are loyal to those particular products for that matter.

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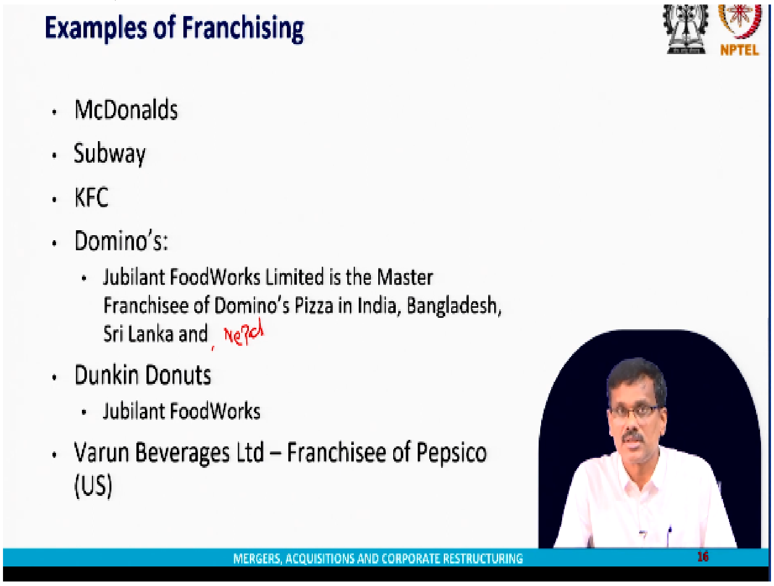

So you can, see the example that we have lender of examples say McDonalds a restaurant chain so all whatever is sale is McDonalds that food products are there. It is if somebody is using that in this country they have to go up to specifies and there could be also possibility that McDonalds may say that whatever ingredients you are using you have to source from us only and your outlets would look like this your display should look like this your employees would observe the norms that we set up for that matter.

The uniform could be something like this all those things are so that a customer who comes to India let us say a looked as a McDonald store that customers should not be finding it different from McDonalds store in other country. At the same time depending on the local requirements local customer requirement there could be some localized products besides those products that is sold across the countries for that particular product brand for that matter.

So, obvious another brand for the work in the sandwich market so you will see that so we look same wherever you go you see the subway logos to be same. Another is KFC brand then we have Domino’s another in the pizza you have also pizza hut for that matter. So Domino’s so Jubilant Food Works that the Indian company has the Master Franchisee of Domino’s Pizza in India, Bangladesh and Sri Lanka and Nepal.

So, these countries only Jubilant Food Works can has the franchise no other company has and Jubilant Food Works give the franchise to other players local players as per the conditions. So they are the master franchise so if you come across a Domino’s pizza outlet it is not necessarily owned by Jubilant Food Works or the Domino’s for that matter, but the owner of that outlet has to use the specifications given by Jubilant Food Works on behalf of Domino’s for that matter.

So, the Domino’s pizzas franchise is used in India, Bangladesh, Sri Lanka and Nepal by Jubilant Food Works India. Similarly, we have Jubilant Food Works also has got the franchisee to use to sell Dunkin Donuts as another food product another company that is there which is very reputed company and lot of growth is like Varun Beverages limited in India. So Varun Beverages limited in India has the Franchisee of Pepsico the US based companies products in India.

So no other company can produce the Pepsico products in India and also Varun Beverages limited has to confirm to the specifications of Pepsico in all its operations, and the typically the formula of let us say the soft drink for that matter or other drinks for the matter. It is the exclusively it used with Pepsico so they will be giving that formula in southern format. So that Varun Beverages cannot use it for some other product with a non Pepsico brand for that matter.

So, those things are taken care any valuation in that can lead to a substantial cost for the company. In fact these are the ways where the companies expand and reach other market. So this is franchises can be a way to start an international operation for a company in other country. Then we go for licensing then strategic alliances then joint venture then subsequently merger acquisition can also take place.

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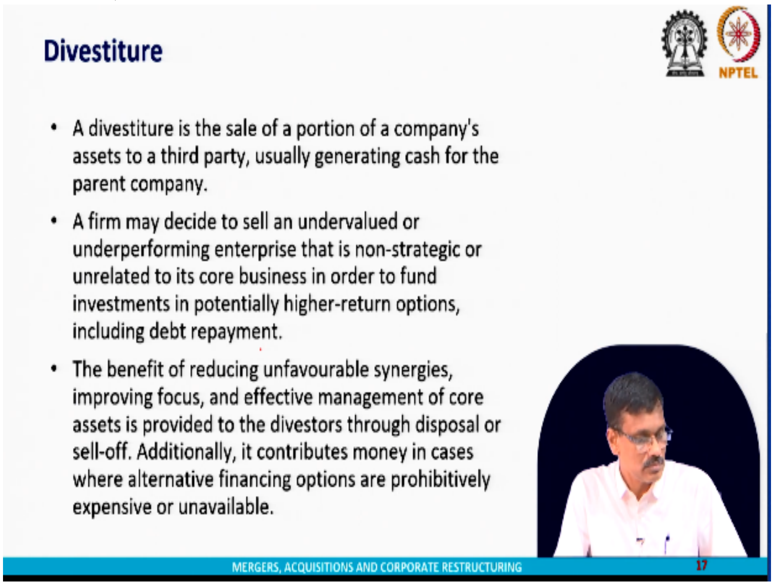

So another thing about restructuring the divestiture so for divestiture something is just other than the it is called reverse of the growth where a particular portion of the company or asset is sold a third party, usually for generating cash for the parent company. So you can sell an undervalued asset or underperforming enterprise to a anticipant also should be non-strategic for the business if that business goes with the core offers is not going to affect ideals possible.

And so that you can you take this money liquidity is created either take that money and use for the rest of the business. So we can possibly have if there is an unfavorable synergy other is opposition is there possible you can reduce that and you can possibly go for more effective manager core operations and so that disposal is done other core is taken care. Additionally, it contributes to money to these companies also and financing can be done, because financing otherwise may be difficult.

So we sell the assets and use that money for the growth of other business for that matter or the company could have been distress it needs money for certain things. So this component does not have any other option but to sell the assets for the time being.

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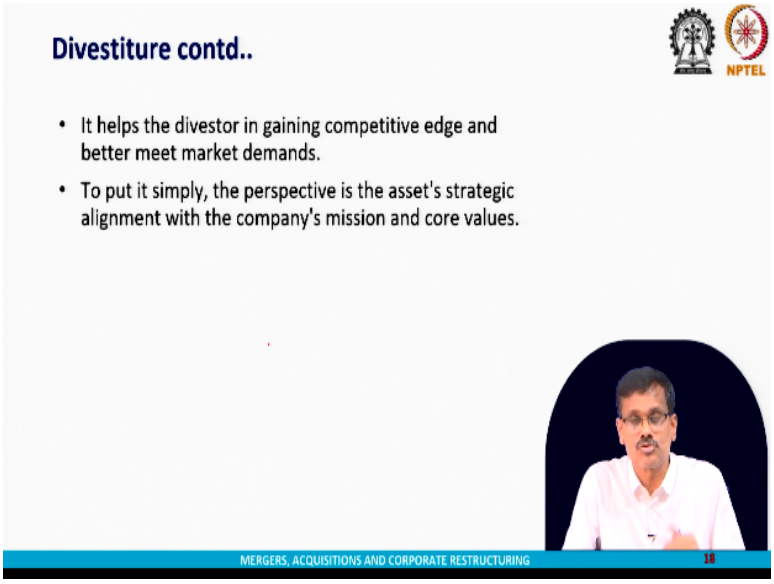

So it helps divestor gaining competitive edge because they will be now not focusing on these products which are not contributing so much and so that if they are in alignment with the company's mission and the core values that should not be diluted.

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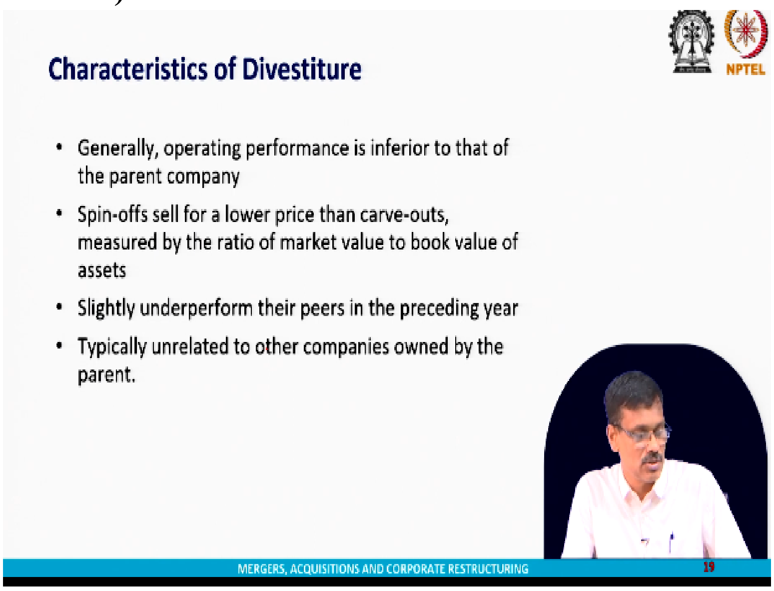

So there are certain characteristics, we feel that the operating performance of the unit diversity is inferior to the parent company their lower return may be and then we can also go for spinoff out of that spin off and split also and we feel that possibly the ratio the market value to book value is 30 percent lower. So that is why it is possible to sell it off and they possibly slightly under perform their peers in the preceding year in the say there could be several other players in other companies.

So they may be doing well but not doing you are not doing in this division so this possibility is that is better to sell it off and maybe it is not related now to the what the company is presently doing. So that could be the characteristics of think going for a divestiture decision.

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Then other reasons could be strategic fit is better for another company, which is buying that particular division because they are selling it even there is a buyer for them is a better strategic fit. Reverse synergy could be there at the repetition we are talking about poor performance could be there for the company for the division which is being divested and by divesting and selling this asset you may give a greater signal to capital market.

Because this company may be a conglomerate doing several things so by divesting certain assets certain businesses the company may give a better signal to the capital market. It becomes less conglomerate in nature, also liquidity in the market is there for the corporate assets company may have some cash flow needs and instead of abandoning also it is possible certain cases core business can be abandoned. If the new things have also come up so not necessary core business is in divested and maybe company proceeds to have another business as the core business.

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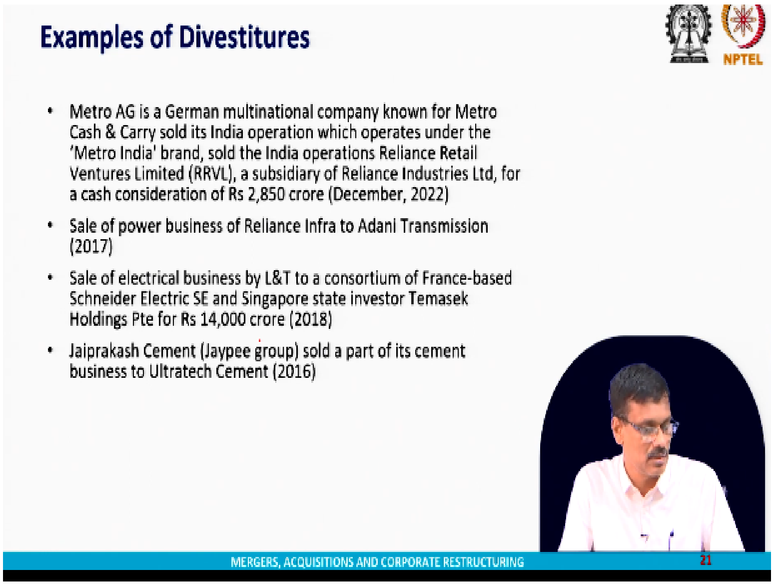

There are certain example that you have letting Metro AG is a cash and carry business a German based multinational company it had its operation in India. Now it has sold its Indian operation to reliance industries in the cash and carry business has been sold that business its episode is a cash and carrying wholesale return market. So from metro point of view they found that possibly divesting it here and getting the cash flow and use it for expansion other countries.

For reliance industries they want their expanding rapidly in retail markets they also wanted wholesale little market retail market so this cash and carry is going to help them their growth also. Reliance infra which is a distressed company sold its power transmission power business to Adani transmission in 2017. It is because of distress and similar L and T to focus on their engineering business they sold their electrical business to a France based Schneider Electric SE and Singapore state invest Temasek.

They came up from in the company they bought the electrical business of L and T and got the in 2018, because L and T wanted to not have focused on this particular electrical business, they want to go for their other construction business. Jaiprakash has cement as a part of Jaypee group has sold its cement business to Ultratech cement it was also Jaiprakash cement had certain liquidity problem that is why they thought of selling the assets to the Ultratech cement.

Ultratech cement was not interested, in buying the Jaiprakash the company they were rather bothered to buy the cement producing assets cement plans for that much. So they did not buy the company they bought the assets of the company for that matter.

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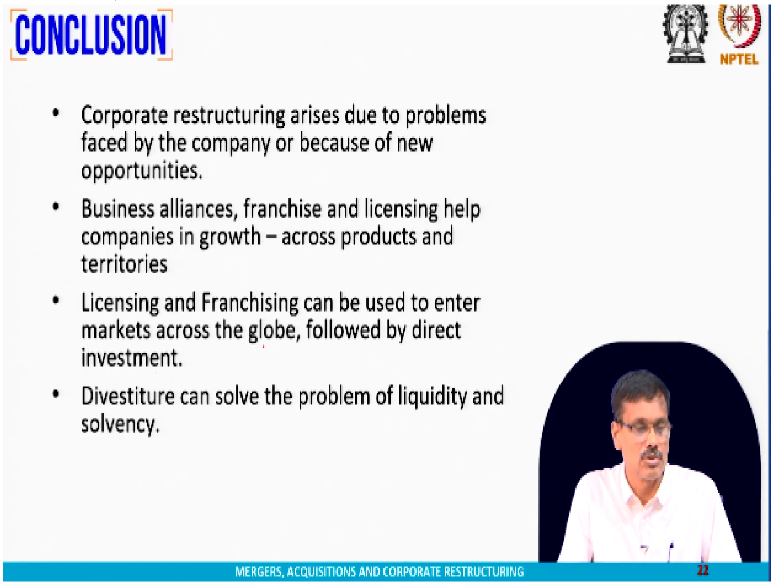

So, in conclusion; corporate restructuring can arise because of problems faced by the company or because the new opportunities. Business alliance and franchise and licenses the help company grow in different products different geography for that matter territories. Licensing and franchise can be used to enter the markets across the globe, followed by a subsequently direct investment that is equity investment and divestiture can also help solve the problem of liquidity and solvency at least the short-term solvency problem of the company.

So we will continue with this alternative corporate restructuring in the subsequent session we will talk more about spin-off split off equity curve out etcetera.

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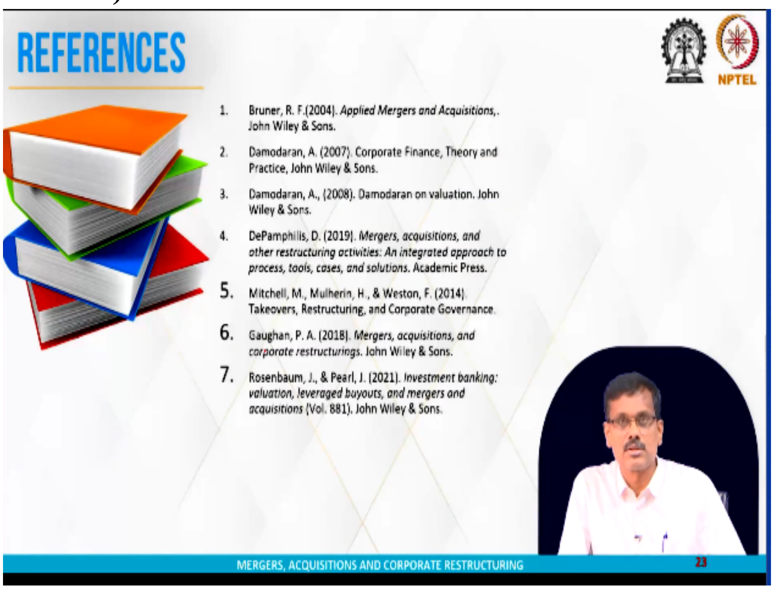

Thank you and happy learning.