Valuation Corner

Abstract

Valuation case studies for mergers & acquisitions – this takes various dimension and well-known for structuring, tax-structuring, strategizing or even swap ratio creation by many. But all are dealing with elephant like a blind man.

Valuation Case Studies under Merger & Acquisitions

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Mergers & acquisitions need conceptual understanding first. It is a wide term encompassing mergers, acquisitions, amalgamation, absorption, demerger, reverse merger, takeover – friendly & hostile, spin-off, consolidation, joint venture, strategic alliance, carve-out, restructuring. Knowing each of them and its ultimate objective can make a valuation job creative. A management accountant can do best justice by analysing spirit of each.

Let us dwell upon some of them. For example, merger generally makes 2 or more companies into 3rd bigger and powerful. In India and worlds history ArcelorMittal is quite famous on this. Having worked in Mittal group I had my share of challenges in same. Steel & mining a composite unit especially in east Europe where progress to democracy was in offing and EU storm was encompassing, posed interesting dilemmas and in many cases, they contributed to 6 to 8% of share of GDP of the economy. The complex clauses of transfer of control as a part of merger agreement are worth publishing in a book forms. But here are few wonders which emerged. Shareholding does not necessarily mean control. Later I learnt this in one of wine client's valuation as well. In that case, wherein power to make decision on rate of interest on loans given by parent alone ensured an acquisition with 0% shares. Now how do you value a share when you have no shares but ability to pull out all the cream is itself a backdoor management. In this case the strategic alliance was made by doing valuation based on power to have risk& reward by way of an agreement which enables a deemed parent to keep hold over wine manufacturing licenses. These licenses otherwise could not have been acquired to laws prohibiting.

That brings light many cases, where two parties did reverse mergers to protect intangible assets. A well-known once are king-fisher & air-deccan, Godrej soaps and Gujrat Godrej and Satyam Mayta (failed case).

So, valuer better know that

Where all he needs valuation of acquiring company rather than acquiree company.

Reasons of reverse mergers are stated below.

a. Loss making company valuing profit making company for loss carry-forward – famous 1st case Kirloskar pneumatics acquiring Prashant Khosla pneumatics

b. Retaining non-transferable intangible assets like landing and flying rights or publication rights. Air-India – Vistara was typically funded by tata sons has shades of reverse merger

c. Save on cost and efforts of tedious listing IPO process – Here private company actually values and acquires public company while on paper public company acquires private company. Yatra online acquired terrapin in USA by which yatra became online public in US market. The reverse merger valuation involved terrapin's valuation

d. Subsidiary acquires holding. Both HDFC and ICICI started banks as subsidiaries and then banking model became so big that the respective subsidiaries acquired parent. Here an acquisition resulted in merging parents' business via reverse merger.

e. Many times, demerger requires valuation of acquiree. For example, a shell company acquires SILO portion of (say one portion of business). Here the bigger company allots portion of wealth of silo to its existing shareholders, by way of shares of shell company which is acquired at pittance and renamed.

That takes us to SILO model. It is possible that a ring-fenced unit is being valued and acquired. But on paper it is shown "rights of management control are sold" in exchange of royalty. A well-known example is Piramal pharma gaining full control over convergence chemical with Navin fluorine retaining rights like perpetual license to use technical know-how for select products and continued supply partnership for key raw material in 2020. Tata tele services now focusing on digital connectivity and selling consumer facing wireless business is typical case of synergy benefit for airtel and spinning off unit as a "SILO" arrangement.

A valuer in all these models is required to think of complex clauses with no loopholes for "no disputes" in future arising out of misinterpretation. Valuer role may not encompass in legal drafting but certainly is there in weighing every word in legal agreement to interpret and factor in valuation. This is an onerous task and it is better that valuer expands its scope in acquiring legal drafting knowledge and learn liberal vs literal interpretation of case studies as enunciated in many cases like Nabha power vs Punjab state power Corp

All in all, M & A valuations are best to test abilities of valuer in its complex sense and also varied possibilities of structuring. MA