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Reforms: The Way To Revive Deal Street

by Salil Panchal | Oct 1, 2014

With the new government, there is optimism in the market. But, India Inc believes, big-ticket mergers and acquisitions will take another couple of years

Image: Vikas Khot
From left): Vishal Tulsyan, Michael Surface, Tarang Jain, R Jagannathan and Anil Singhvi

Market sentiment and business mood have been buoyant since the Narendra Modi-led government took charge in May 2014. Deal Street has been abuzz with optimism as big-ticket acquisitions hit the headlines. In July, Reliance Power said it would buy the hydropower business of Jaiprakash Power Ventures for an undisclosed sum. Last month, Adani Power, controlled by billionaire Gautam Adani, announced that it will acquire Lanco Infratech's power plant in Karnataka for Rs 6,000 crore. Earlier, India's largest e-tailer Flipkart acquired leading fashion portal Myntra for Rs 2,000 crore.

A recent KPMG study found India to be one of the strongest performers globally. The country's mergers and acquisitions (M&A) activity rose by an impressive 10 percent between January and June 2014. But do the recent deals indicate a smooth road ahead for the corporate world? What do promoters and acquirers need to understand before taking crucial decisions in these highly competitive times?

For the third session of the Forbes India CEO Dialogues: The Leadership Agenda, we invited top business leaders to discuss the path ahead for India Inc in the M&A space. Anil Singhvi, chairman of iCAN Advisors and former CEO of Ambuja Cements, Tarang Jain, managing director of auto component maker Varroc Group, Michael J Surface, advisory leader with PricewaterhouseCoopers and Vishal Tulsyan, CEO at Motilal Oswal Private Equity Advisors, gave insights into the ways of boosting deal activity.

Excerpts from the discussion, moderated by R Jagannathan, editor-in-chief, Forbes India:

R Jagannathan: Is it a good time for business?
Anil Singhvi: A lot has been spoken about policy paralysis previously, so from that point of view, things are easing up a bit. But that's only in terms of mindset... change is yet to be seen on the ground. Also, on the M&A front, there are only acquisitions in India, not mergers. There should be more mergers.

Jagannathan: Is there a climate developing for more M&As, divestitures?
Michael Surface: We are doing better than last year in the deal business, but significant headwinds still remain. India is among the more difficult countries to do business with. There is a lot of trepidation among clients and companies about whether the government can bring about a change. Things are definitely getting positive, but we are only 100 days into the new government.

Jagannathan: Mr Jain, when you make an acquisition, do you do it when times are good or when they are bad?
Tarang Jain: When times are bad. Valuations are important going forward but, from our experience, they [acquisitions] are better during bad times. You also have to consider other factors such as global customer base, technology and talent. We got into a cycle when valuations were good and that helped us turn around companies faster than we could have otherwise.

Jagannathan: Mr Tulsyan, do you find the same attitude in India? That people are more willing to sell when in distress? In India, I think people have always waited for better days to sell.
Vishal Tulsyan: Indians have largely been value buyers. When they want to buy, they want to do it at one cent to a dollar. But while selling, they expect a dollar to a cent. That's why we have not seen more of domestic M&As in India. I have rarely seen two Indian entrepreneurs coming together and agreeing on a valuation. This is because the buyer wants to pay less and the seller wants more. In India, historically, the owner and manager of the business are the same, unlike much of the developed world. That could be the reason why we do not see many mergers in India... because both parties want to

run the business.

Singhvi: India is a difficult place. Period. In such a situation, it will always be challenging to look at an M&A.

(L-R) Vishal Tulsyan, CEO, Motilal Oswal Private Equity Advisors and Anil Singhvi, chairman, iCAN Advisors

Jagannathan: But recently, we saw the willingness to sell when Myntra agreed to sell to Flipkart.

Singhvi: The younger generation has lesser baggage to carry than the older generation.

Tulsyan: Even in traditional businesses where second or third generation [entrepreneurs] have come in, they are quite open to selling their business and starting something else. When we started our PE venture eight years ago, our initial thesis was that the most exits would be from initial public offerings [IPOs]. But now we realise that many are open about selling their companies.

Jagannathan: Mr Surface, you spoke about some quickening in the pace of M&As. Can you expand on that?

Surface: We have a lot more inquiries and mandates from companies. And it's largely cross-border, where Indian companies are looking to expand overseas through acquisitions. Look at Starbucks… it is not an acquisition, but it's moving very quickly in India. Companies that have the wherewithal will continue to look at India.

Tulsyan: Lack of funding is the reason why domestic acquisitions have been few in India. Most acquisitions made by Indian companies overseas have been through LBOs [leveraged buyouts where a firm is bought using borrowed money]. That would be tough to do in India.

Singhvi: I don't agree. In 1999, Ambuja, which was way smaller than ACC [formerly The Associated Cement Companies], acquired the company with entire leverage in 24 hours. If you can demonstrate that you are acquiring the asset for growth [and not seeking funds only to acquire shares], it is possible. Most people in India don't have that mindset. We are inward-looking as a society. I often compare it to running away with your neighbour's wife, which is not looked at kindly in India. M&A has to be viewed in that context: That you can woo your neighbour's wife. Nothing wrong if she likes you and you like her.

Jagannathan: Mr Jain, are you always on the lookout for acquisitions?
Jain: We have articulated a strategy till 2020. We want our global turnover to touch Rs 20,000 crore by then from the current Rs 8,000 crore. Visteon [American automotive supplier] and we thought we got into a good deal. We will look at buys everywhere, but it will be a strategic call. We may also look to divest some of our product groups.

Jagannathan: Mr Surface, do Indians approach acquisitions differently? Do they think more as a win-lose rather than a win-win situation [like in Varroc-Visteon]?
Surface: Absolutely. There are a lot more emotions attached to the business. Overseas, they will look at the price and if they see a good deal, they will go for it.

Jain: Ultimately, business families should not destroy their wealth. They have to be professional in their thinking. The Godrejs are more professional; they believe more in education and training before taking charge.

Singhvi: When I look at the Holcim Ambuja-ACC and Ranbaxy-Daiichi deals and Mr Ajay Piramal selling his domestic health care formulations business, I know they must have been caught up by emotion. But eventually they took a strong decision. In hindsight, they all sold at fabulous valuations. Whether you have somebody in the family who can take the business to the next level is a very myopic way of looking at the venture. We should all become history at some point; what should survive is the institution, not one's personal fiefdom. Indian entrepreneurship should study what made Malvinder Singh [former Ranbaxy CEO] sell his family business and why Mr Piramal and Mr Sekhsaria did the same.

(L-R) Michael J Surface, advisory leader, PricewaterhouseCoopers and Tarang Jain, MD, Varroc Group

Jagannathan: Will we see the big deals again?
Jain: The valuations will not be the same, but such type of deals will happen. It will take a couple of years. For M&As to happen, reforms have to take place and Modi has to execute that.

Jagannathan: Mr Surface, the interest towards M&A deals is across the board?
Surface: There is interest in technology and pharma. Some clients are pessimistic and assume there won't be progress in India for two years. How far does it push India back then? India could be dead in the water for 10 years.

Jagannathan: So how long will the patience last?
Surface: I think two years.

Jagannathan: If you had to see a positive change in the M&A space, what are the three pre-conditions for things to change?
Tulsyan: It has to start with sentiment, which is turning positive now. We need to see three years of sustained economic growth with improving profits and balance sheets getting deleveraged for the M&A hunger to return.

Surface: I agree. We also need to take away the uncertainty about how the government would act on certain regulations. It needs to simplify norms and make them consistent, not ad-hoc.

Jagannathan: Do you see banks playing a catalytic role in boosting deals?

Singhvi: That will happen. The banking industry has to change its mindset. Look at the power sector, which is struggling and has little M&A activity. It needs to be consolidated in a big way. The country has invested heavily in this sector. Banks have to be proactive… we cannot have unproductive assets. Assets must move into stronger hands.

Sourav Majumdar (Editor, Forbes India): Mr Tulsyan, how much of M&A activity do you see driven by private equity for investors who are stuck?
Tulsyan: Between 2006 and 2013, $32-35 billion was invested by PE players. If one expects 5 to 6 percent dollar returns, we need $50-55 billion worth of exits which must take place in 3 to 5 years. In recent years, however, exits have dried up. If exits don't happen, it will impact foreign direct investment into India.

Singhvi: Power, telecom, banking and pharma sectors are hugely crowded and could see huge M&A activity. Power, telecom and banking deals could be driven by banks while pharma M&A would be driven by size.

Jain: There will be consolidation in the auto component sector, but this could happen over 5 to 10 years due to lack of technology.

Jagannathan: Mr Jain, how do you see the M&A space and when do you see things accelerating?
Jain: Sentiments have turned positive for Indian entrepreneurs. I see an increase in M&A, but no big deals happening before the next couple of years. Reforms have to take place steadily.

Surface: There will be some big deals, but they will not be of the volume that we need [them to be]. It will take a fair amount of time.

Tulysan: We need a couple of good years before we see M&A activity.

Singhvi: I think large-ticket M&As will happen in 18 to 24 months. If they don't happen within this period, it will be difficult for deals to take place as valuations will be so challenging that the buyer will not write a cheque. Right now, we have some stress levels [on balance sheets], a little bit of proactiveness is needed. If we believe that the next five years will be good for the economy, this is the time for M&As.

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