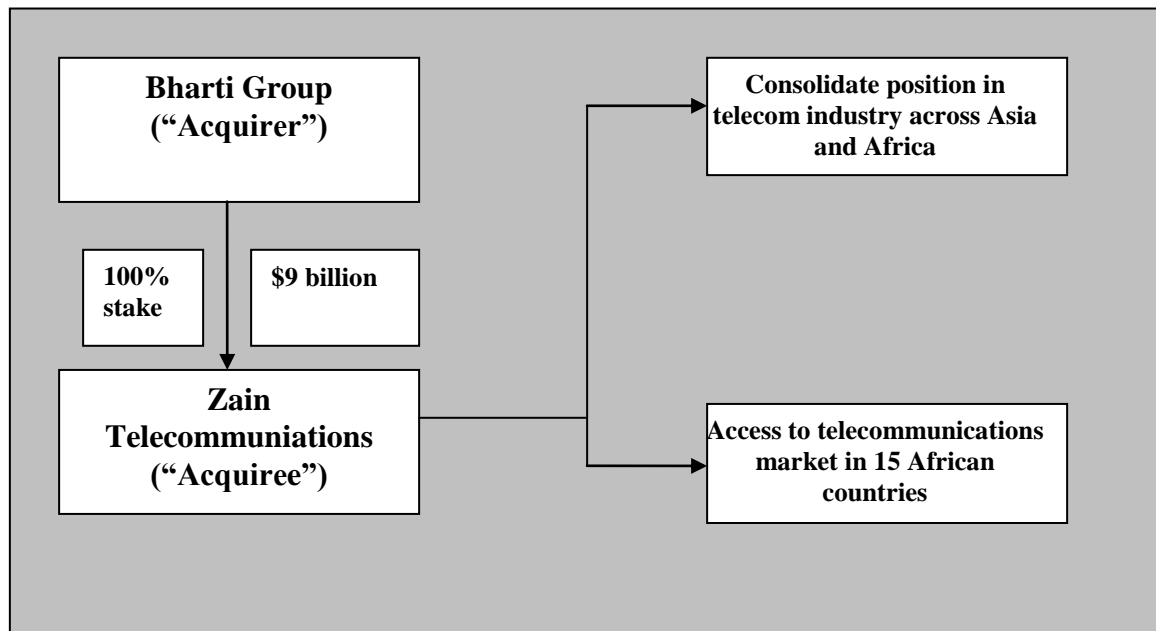


1. Identifying the M&A Candidates

Be it a buyer or a seller, the first move towards M&A is to take a firm decision regarding the company. Having decided to follow the M&A route, it is important for a firm to decide on the candidates it would like to have on the other side of the negotiation table. There are several criteria based on which a firm may decide on the acquiring or the merging partner. For example, in view of Mr. Kelly Porter, an M&A strategist, Google should acquire Roku, a digital set-top box maker. This is in view of the offerings made by Google through YouTube. According to Mr. Porter, though YouTube delivers almost about 38% of the digital video content on the internet, its average viewership compared to a television is only 15 minutes compared to 5 hours of the television. Thus, acquisition of Roku would serve as a channel of delivering content of YouTube on television.

In another example, the US-based pharmaceutical research firm Charles River acquired the Chinese pharmaceutical outsourcing firm WuiXi Pharma Tech to foray into outsourcing services to other pharmaceutical, biotechnological, and medical device companies. Charles River believes that the acquisition shall increase their gamut of their offerings. In yet another deal, the most talked acquisition of Zain telecom by Bharti Group is an example of an acquisition to broaden the geographical reach to 15 countries across Africa.

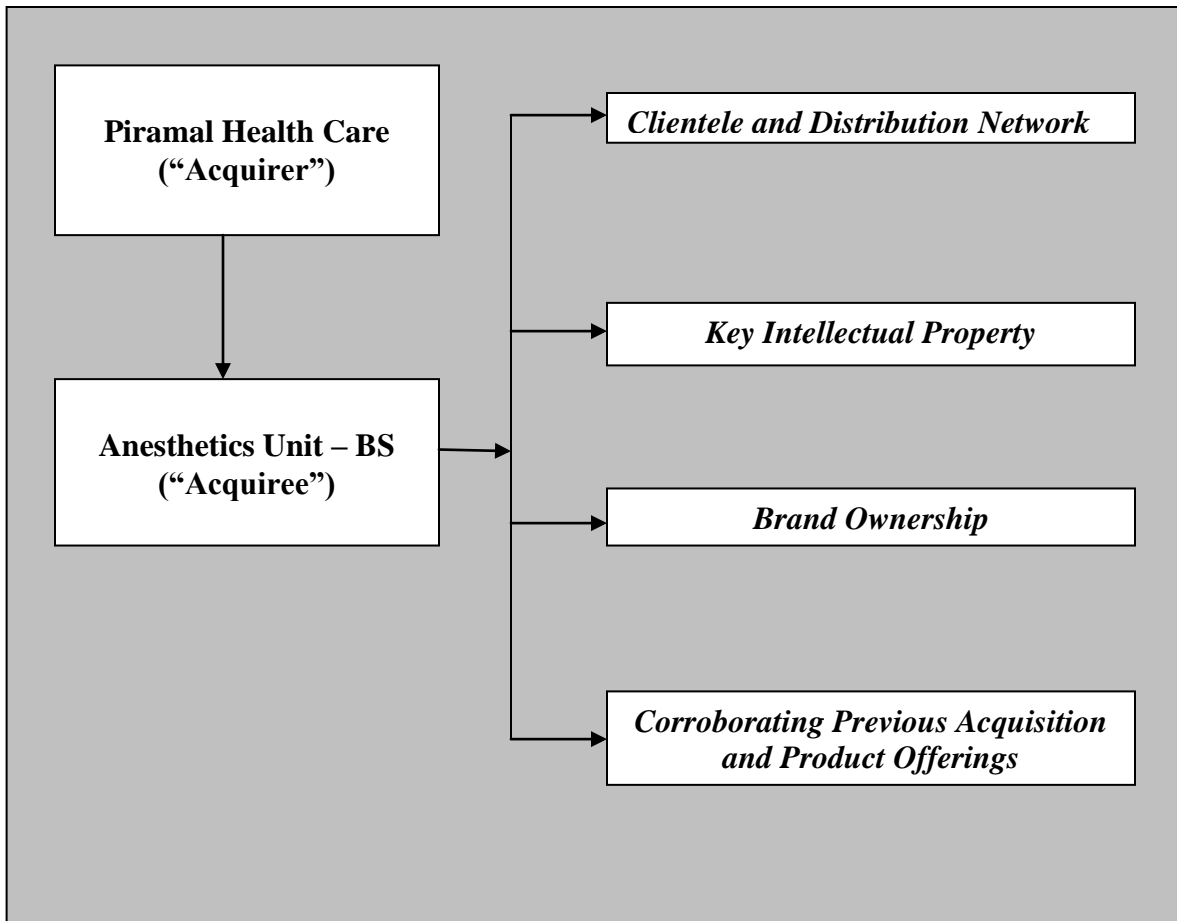


Thus, in each of these M&A deals we observe that the seller has some value to offer in form of products, services, or skills or accessibility, while the buyer views these as a “value-add” rather than just a “value” to its existing business. The “value-add” combines original ideas, precedent transaction knowledge, knowing where to get the deal and “tie up” the ends. The value-add may be in form of acquiring new clients, enhancing the distribution network, capitalizing on the existing brands, consolidating share in a specific market segment, or accessing the intellectual property of the acquiree. This forms the basis of M&A deal. The following snippet on acquisition highlights the importance of these features of acquisition.

Case Study- Deal Motivation

In an acquisition deal in the healthcare sector in India, Piramal Healthcare Ltd acquired the anesthetics unit of Bharat Serum (“BS”).

The following chart summarizes the rationale for such acquisition:



Clientele and Distribution Network:

With the acquisition, Piramal Healthcare shall have access to about 30 countries in which BS had sold its anesthetic drugs worth about 10 crore in 2009

Intellectual Property: The acquisition shall enroute access to the key intellectual property developed by BS in the domain of anesthetics

Brand Ownership: It shall also own reputed brands such as Propofol, Bupivacaine and Atracurium Besylate that were previously owned by BS

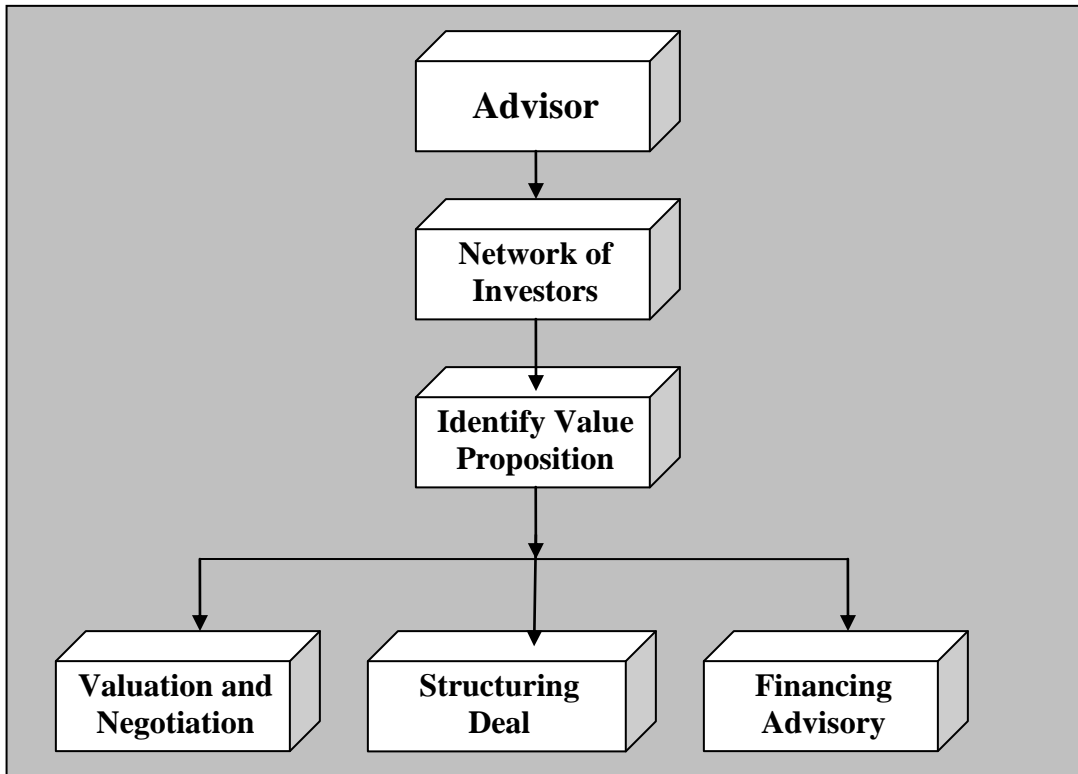
Corroborating Previous Acquisition

Piramal Healthcare expected BS's portfolio to complement its hospital-based product business and strengthen its hold on the anesthetics business by complementing its previous acquisition of anesthetics business of Minrad International Inc.

Having decided on the parties or the candidates whom you would like to see on the other side of the table, the question arises – Who would negotiate better to get the best deal? Can a firm negotiate (the owner of the firm) or should a broker or an investment banker (“IB”) get involved? In case of a small firm or acquisition, the firm itself can negotiate or a broker may do so. But in case of large deals, an investment bank is the most preferred option as it represents an array of valuation experts and has a wider reach to the potential buyers than the owner himself or the broker. Often, the IB is aware of the profile of the buyer in terms of the cash it possesses or its ability to raise the money from the market to finance the deal, or the strengths of the acquirer that could be leveraged through the deal. The owner himself is often unaware of such details and hence may not be the best negotiator. In addition, the difference between the broker and an investment banker is that an IB is a registered party that can integrate the different sections of a deal, whereas in case of a broker, it may be a party that is not registered with any regulatory authority and may not possess the skill for integration of the components of deal and take it through. Thus, in most of the cases, the large deals are effectively handled, packaged and presented through investment banks and not through brokers or by the owners themselves. The broker or an IB can put across a deal along with their track record for past 6-12 months, or refer to its sectoral expertise to instate the confidence of the parties involved in the deal.

2. The Role of an Advisor

In an M&A deal; the advisor in form of a broker or an investment bank plays an important role in taking the deal through. It is expected of an advisor to address the following:

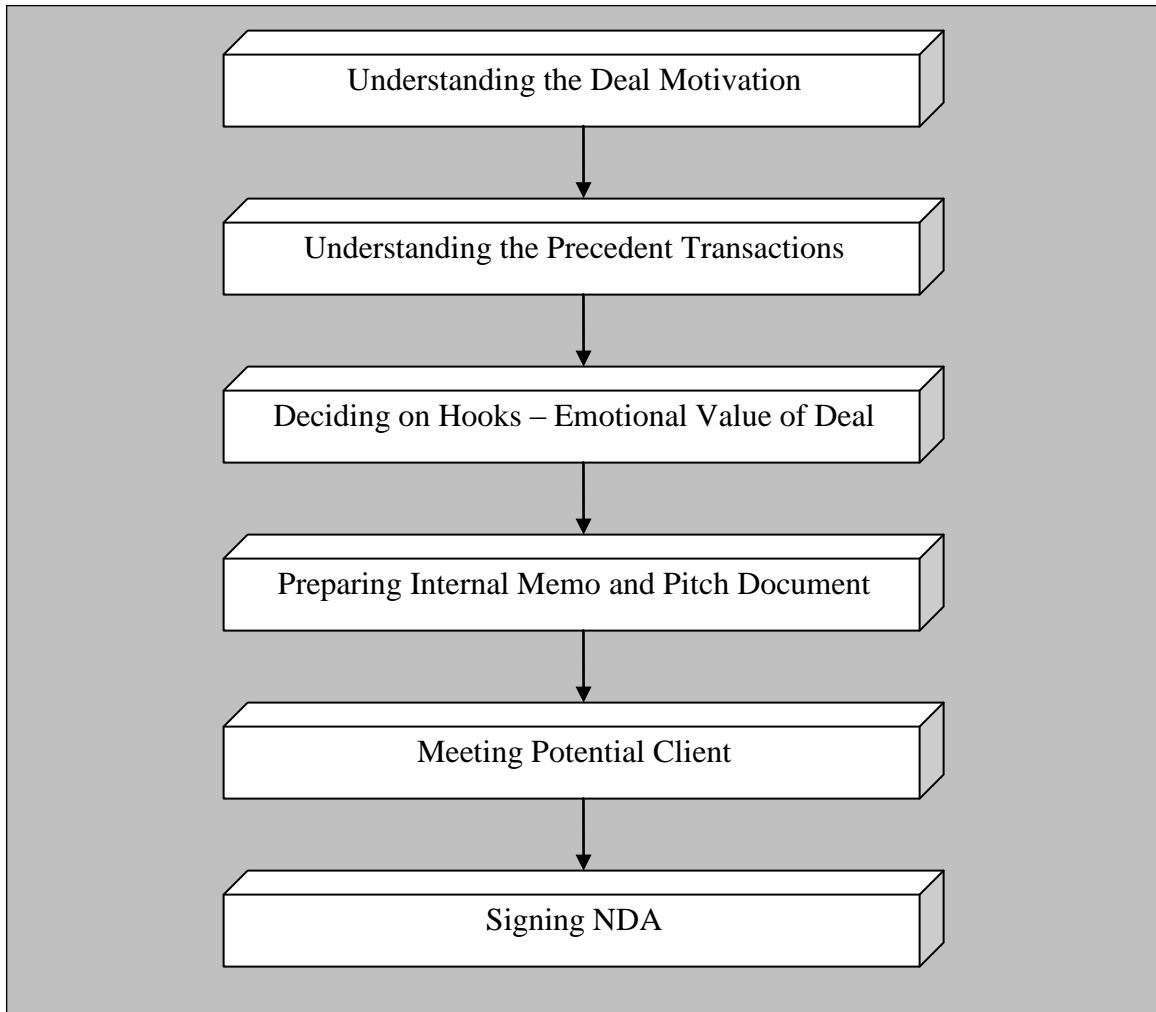


It is the advisor's responsibility to identify the right investors to whom the deal can be offered. The value proposition identification is done in view of the selected investors who are likely to be involved in the deal. In the above diagram, the elements at the bottom of the structure, which includes valuation structuring and advisory, are the parameters that clearly distinguish an investment bank from a broker. A broker may be able to present a proposition to a prospective buyer, but he may not be able to propose a structure of the deal or provide adequate financing. Having decided on the parties, it is important to know what goes into an M&A process which is discussed in the next chapter.

3. Pitching for an M&A Deal

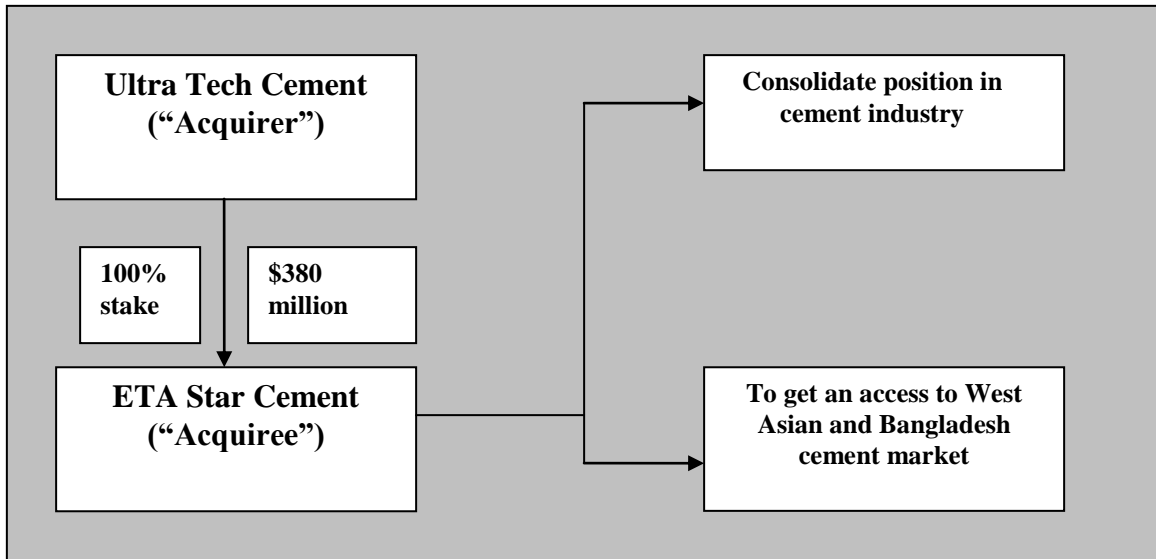
The understanding of the motivation to enter into an M&A deal forms the stepping stone to take the deal forward.

The following flowchart enlists the steps involved in pitching for an M&A deal:

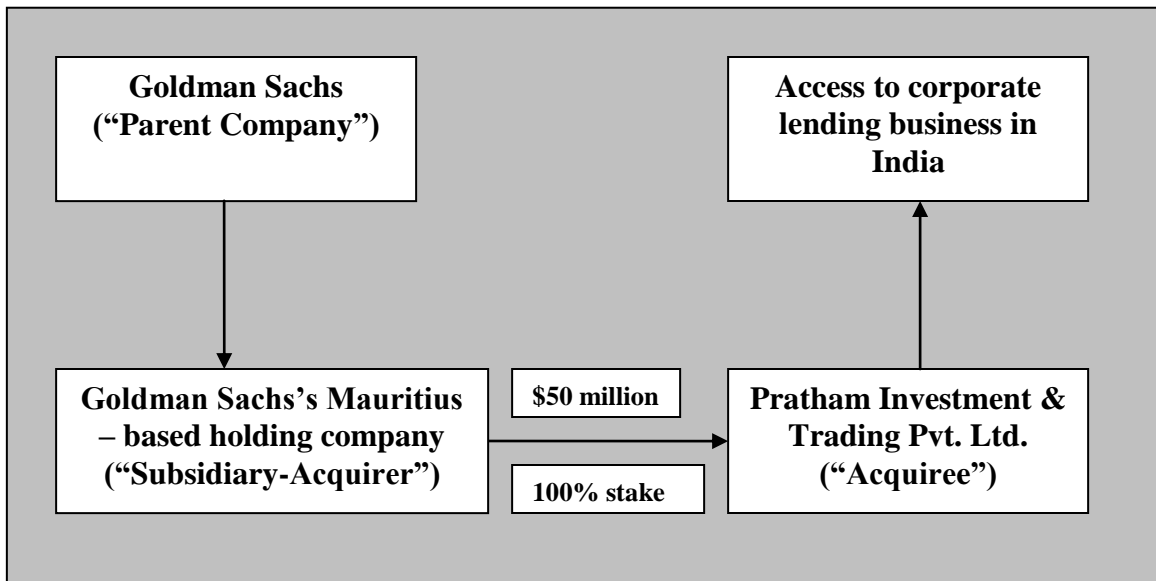


Understanding the Deal Motivation

Be it buyers' perspective or sellers' perspective, the understanding of the motivation for a party to be involved in an M&A deal is essential. Such information empowers the party to negotiate better. For instance, the UltraTech Cement, an Aditya Birla Group company, acquired Dubai-based ETA Star Cement for \$380 million. The motivation for cement major - UltraTech to enter into such an acquisition was to have access to West Asian and Bangladeshi cement markets.

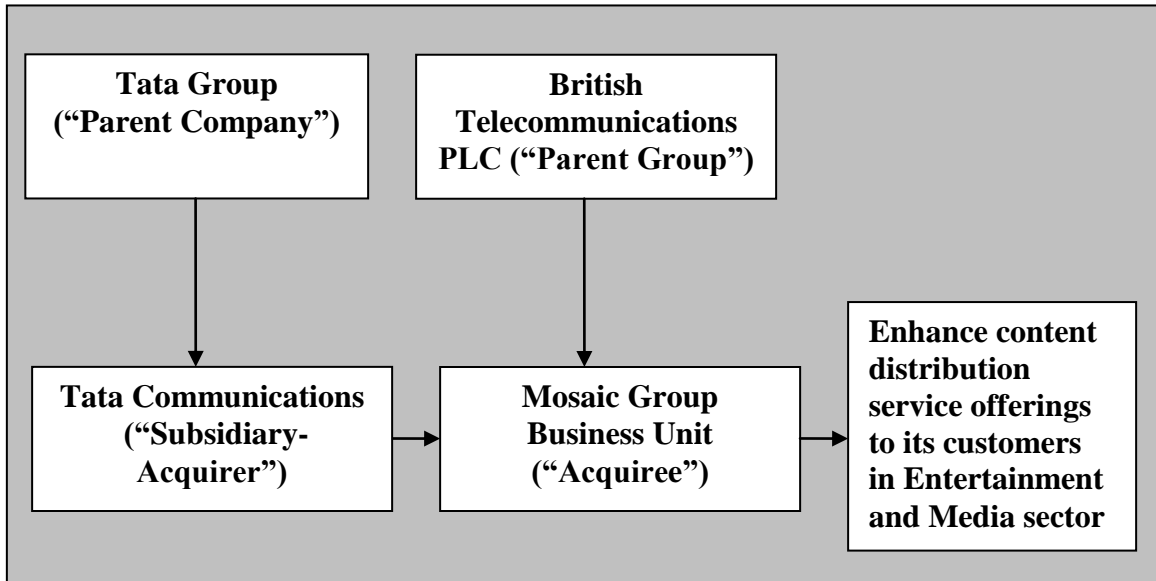


Similarly, Goldman Sachs paid \$50 million for acquiring 100% stake in a Mumbai-based investment and trading company- Pratham Investment & Trading Pvt. Ltd. through its Mauritius-based holding company. The acquisition marked the entry of Goldman Sachs into corporate lending business in India.

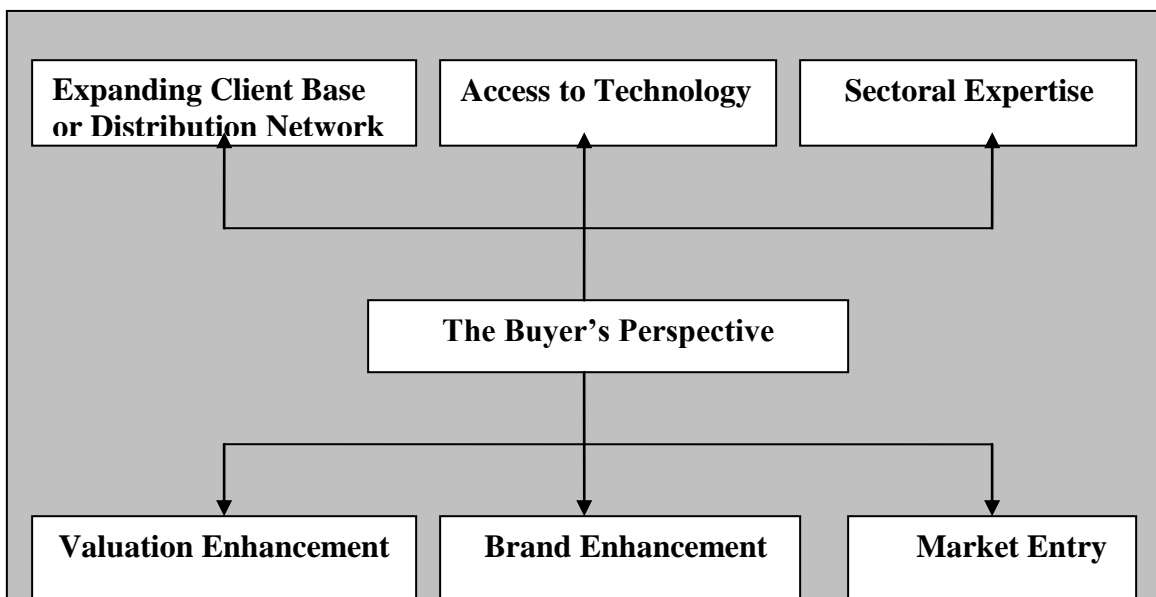


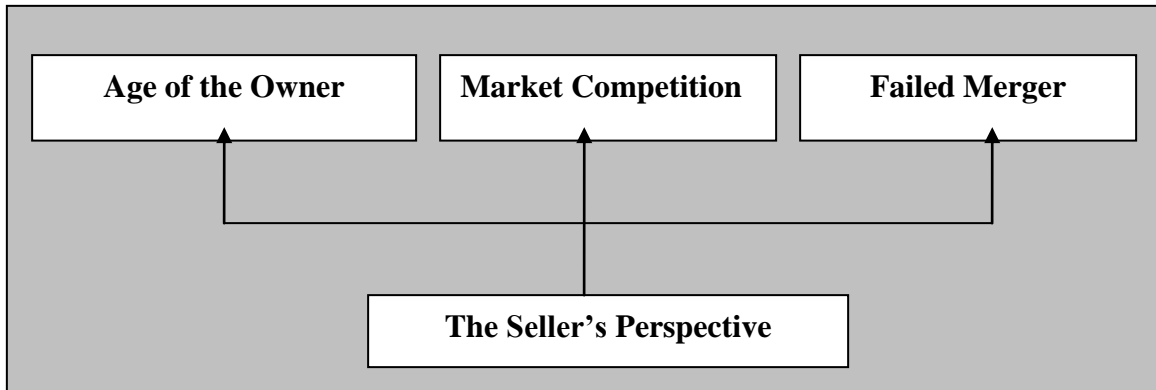
India based Tata communication acquired British Telecommunication PLC's Mosaic business that offers an on-demand digital media management platform to manage content and

workflow from production to distribution across collaborative market ecosystems. This acquisition was in view of enhancing the content distribution services offered by Tata to its customers in the entertainment and media sector.



To summarize, the deal motivation on the buyer side and the seller side may involve the following reasons:



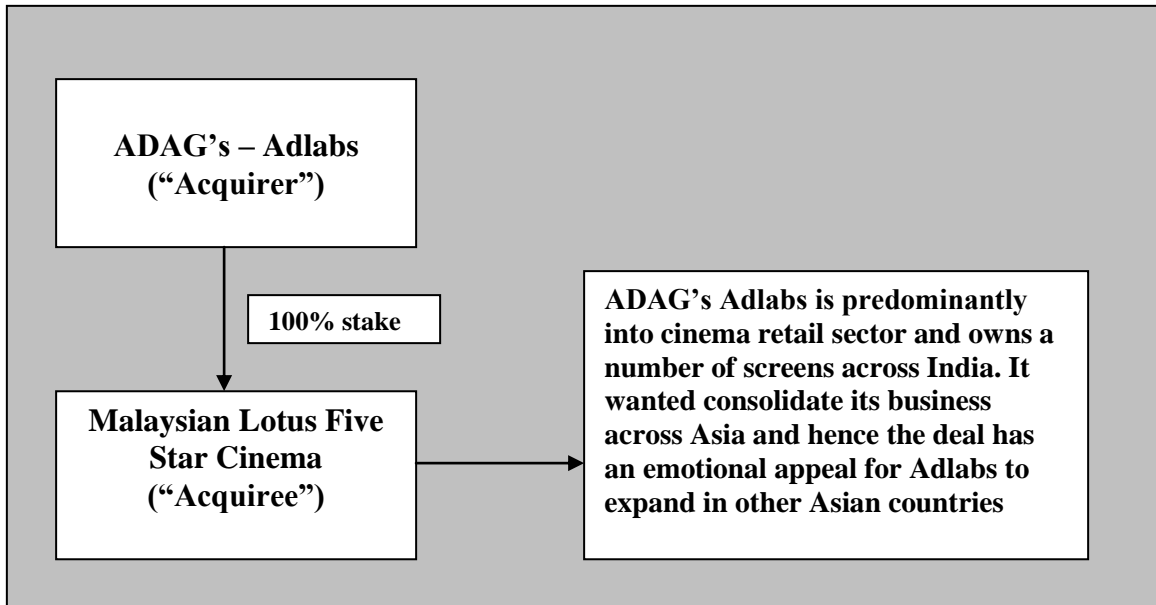


The Role of Precedent Transactions

The precedent transactions form the overall frame work of an M&A deal. It takes into account the buyer profile, the type of deals and valuations in the market, etc. It forms a benchmark or a threshold on which an M&A deal is based. For instance, PeopleSupport, a NYSE listed company which is a largest BPO in the Philippines, rejected the bid from IPVG Corp. and American Online Capital Partners Ltd. The buyers had offered \$15 per share. PeopleSupport believed that the buyers were either unwilling or were unable to provide details on their ability to fund the transaction and the price offered did not take into consideration PeopleSupport's strategic value and hence rejected the bid. The bid was then revised to \$17 per share, but based on the experience of the precedent transaction, PeopleSoft again denied the offer.

Deciding on Hooks

The term "deciding on hooks" refers to understanding the emotional value of the deal to a potential client before evaluating the rationale. It is about evaluating whether the deal represents an area where the client has been unable to get into. For instance, an Adlabs film, which is an entertainment firm, acquired a controlling stake in Malaysian Lotus Five Star Cinemas for an undisclosed amount to foray into Malaysian cinema where Lotus had about 50 screens. This shows some emotional value of acquisitions in the domain of cinema for Adlabs.



Preparing the Internal Memo and a Pitch Document

The internal memo is a consolidation of the above mentioned points into a single document and it reflects a rough sketch of the deal. It also addresses the issues that need to be addressed by the management, and how to take the deal forward.

Meeting the Potential Client

The in-person meeting with the potential client is a step involving preliminary negotiations. Several issues such as price of the deal or its structure, the financing considerations may be discussed during the deal. This step helps filter out some of the unsuitable potential buyers.

Signing the NDA

This forms a critical step while involving a third party or a broker in the deal. This is because the broker has sensitive information regarding the deal and the standpoint of its client on the deal. It would be horrendous if such sensitive details are leaked. The Non-Disclosure Agreement (“NDA”) is a step to prevent such practices. The client also has the right to review what information the broker would present to the other party with reference to the deal.

4. The Pitch Document

Following the identification of the potential clients and the appointment of the advisor, the several parameters associated with the deal are documented, which we refer as “The Pitch Document.” Though the document details on the seller’s offering or proposition, the document is prepared in view of the buyer’s perspective. One may also put himself in the buyer’s shoes and view the deal. If the deal then does not appear profitable to the seller himself, it may be difficult to take the deal forward in actual sense. The following are the contents of the document:

Company Formation, History and Business Overview

This section of the document presents a brief history about the company and its formation. It further details about the key business lines of the company, its competitors, its client base, and the profiles of the management executives associated with it. This section also provides details on the company’s existing product/service portfolio, its liabilities, the distribution network and the risks related to its businesses.

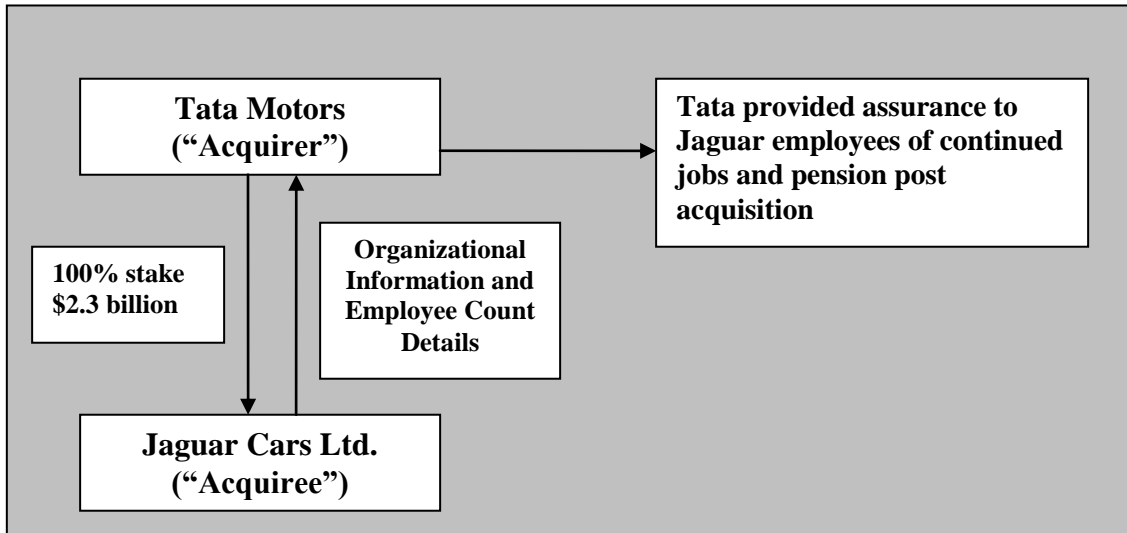
Opportunity and Offerings

This section of the document contains the offering that is made as per the buyer’s perspective of an opportunity to invest. Thus, a company may have a diverse portfolio of hotels, but it may not be an “opportunity” for a buyer to invest in all the portfolio hotels. However, a selected few hotels among the portfolio, with specific criteria or geography would be an appealing strategic investment to the potential buyer. Detailed information of these specific hotels is presented in this section of the report, unlike the introductory section of the report wherein the overall portfolio is referred.

Corporate Hierarchy and Organizational Structure

This section of the report includes details on the organizational structure (department, divisions, etc.) and reflects the hierarchy in the organization. For instance, in the Tata – Jaguar deal, the employees of the acquiree-Jaguar were assured of continued jobs and

pension. Such assurance was possible only when the acquirer-Tata was informed about the organizational structure and the employee count. This section also highlights the human aspect of the acquisition deal.



Summary Financials and Transaction Terms

As referred in the beginning of the section, though this report contains offerings from a seller’s standpoint, the data is presented from the buyer’s point of view. Referring the Tata-Jaguar deal which was worth \$2.3 billion, the seller - Ford Motor Credit Company had agreed to provide financing for Jaguar and Land Rover dealers and customers for 12 months during the transition. Such a provision in a deal enhances the value proposition offered by the seller. The financial summary also takes into account the rate of return (IRR) on the project and the internal targets set by the company.

Next Steps and Q&A

This section deals with consolidating the data into actions by selecting the lead investors, the marketing strategy in view of the deal, the financial and regulatory norms verification. It also contains the details of the terms of the investment which is termed as “terms sheet.” It comprises of a collective draft of the shareholders of the company and details on eventually how the deal shall be sealed.

5. Structuring the Deal

The structuring of the deal involves shaping the terms and conditions and the offerings in a deal in such a manner that the buyer and seller both see a value in the deal. It involves creating different presentations for the buyer and the seller on the same deal. Referring to the section 1 of this document that emphasizes on the “value” and “value-add,” these presentations make a different appeal to the buyer and the seller in the deal. The deal should be structured keeping in view of the regulatory norms such as foreign holding limitations, etc. Having decided upon the parties to the deal, the structure of financing is decided. This involves structuring of the proportion of the debt and the equity components. Another trend which is often observed is that the buyer company may not wish to leverage or expose itself to such deals completely. In such cases it is vital to evaluate the credentials or the backing-up of the Special Purpose Vehicle (SPV) that is created specifically to enter the M&A process. Following the Enron Scandal in 2001, the SPV’s have been often criticized as shell-units that are used to siphon money or hide liabilities, but on the other hand these SPV’s reduce the risk exposure of the overall entity in case if the M&A does not bring in the desired results for the entity.

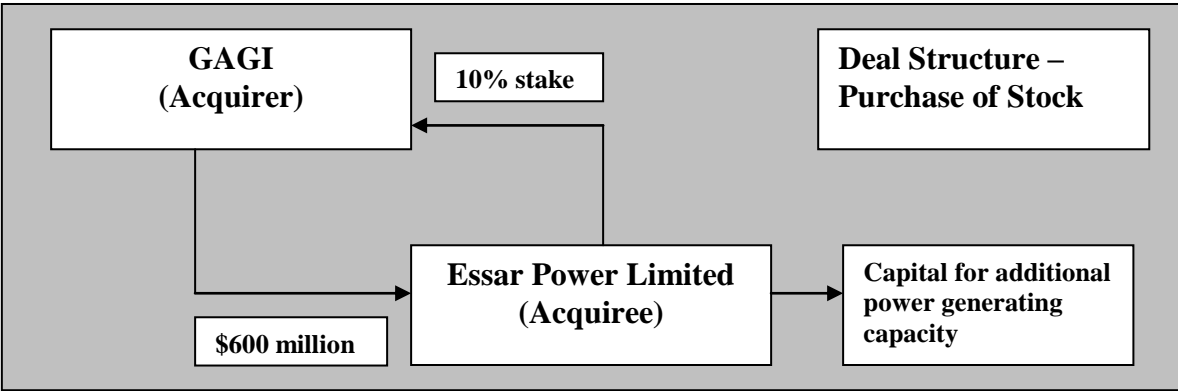
Besides these, there are three ways to structure a deal:

- Purchase of company’s assets
- Purchase of stock
- A statutory merger or a reorganization

Case Study- Purchase of Stock

| | |
|----------------------------------|--|
| Year | 2008 |
| Deal Type | Entity Level |
| Acquiree | Essar Power Limited (“EPL”) |
| Acquirer | General Atlantic Global Investments (“GAGI”) |
| Stake to be Acquired | 10% |
| Deal Value | \$600 million |
| Deal Financial Structure | Debt :Equity – 3:1 |
| Deal Proposition for GAGI | GAGI had invested around \$250 million in India in |

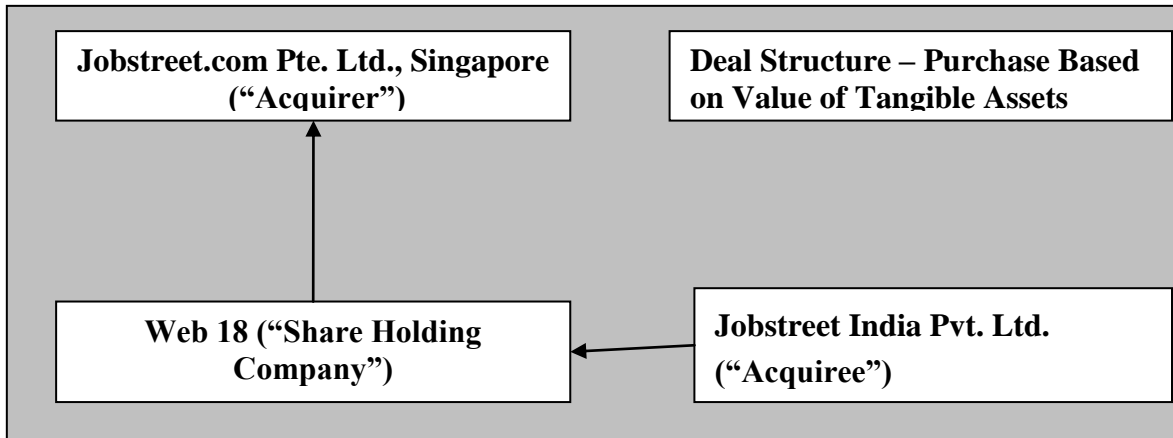
| | |
|---------------------------------|---|
| | 2007 and wanted to extend its portfolio to growing sectors that includes the power sector |
| Deal Proposition for EPL | EPL had been generating 515 MW of power, it wanted expand its power generating capacity to 6,000 MW with the infusion of capital obtained through selling the stake |



In another example, the deal can be structured on basis of the value of the net assets of the acquiree company.

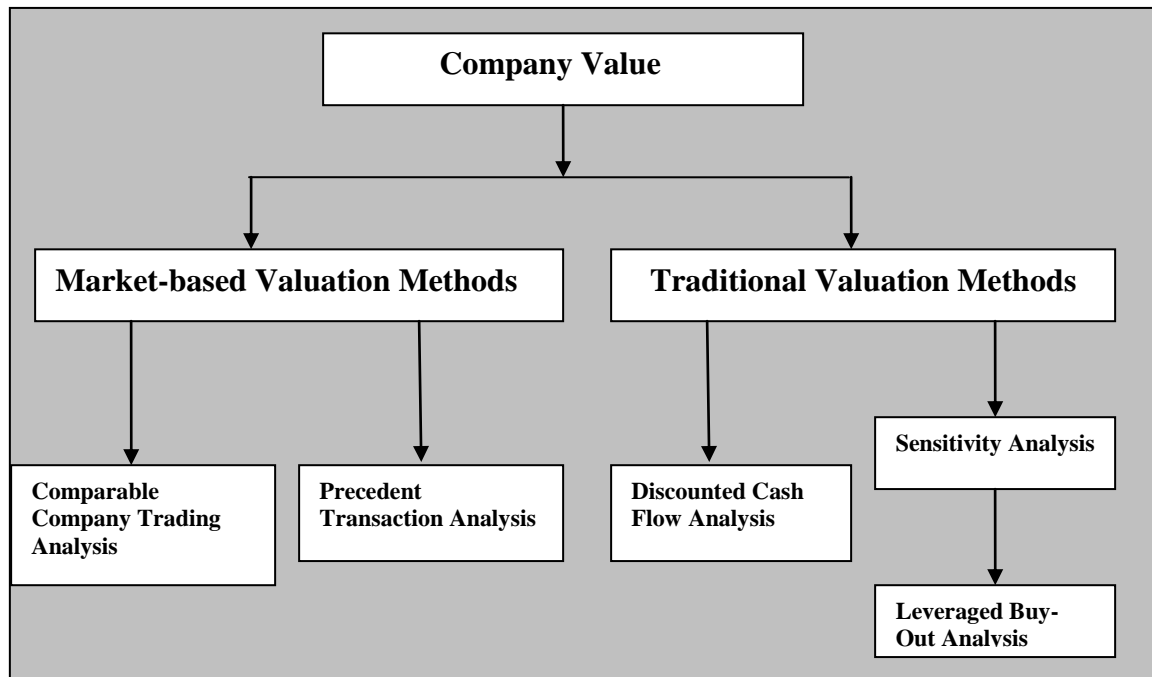
Case Study – Purchase based on Net Value of Tangible Assets

| | |
|---------------------------------|---|
| Year | 2010 |
| Deal Type | Entity Level |
| Acquiree | Jobstreet India Pvt. Ltd. |
| Acquirer | Jobstreet.com Pte. Ltd., Singapore |
| Stake to be Acquired | 50% |
| Deal Financial Structure | Valuation based on the net tangible assets value of Jobstreet.com India |



6. The Valuation Methods

The traditional methods and the market-based methods are the major valuation models in case of M&A. These can be represented by the following diagram:



The M&A Valuation process involves quantifying the proposed deal. The selection of the methods listed in the diagram above for the valuation depends on the following:

- a) The market conditions, especially the transactions that involve stock transfer. It depends whether the market sentiment is bullish or bearish

- b) The acquirer preference for a particular valuation model or a method
- c) The sector in which the acquiree operates
- d) The stage of the market growth or structural shift in the market, and hence the change in the preferred valuation method

7. Comparable Company Analysis Method

In the traditional methods such as Comparable Company Trading Analysis, multiples of publicly traded companies are used to value the target business which may be public or private. This method is usually used in the bull market where the “market value” of the reference company can be established. The comparability depends on the industry, products profile, revenue, growth and profitability. The parameters that are compared include market capitalization, financial performance, and the credit profiles. By this method, an evaluator can determine the threshold value of the investment. A valuation done by this method reflects the status of the company if it were to be listed. It is also a benchmark of financial and operating performance of a company in that sector and provides a brief idea on the future prospects of the acquired company in the given business sector.

The following table summarizes the steps involved in Comparable Company Analysis valuation:

| Step No. | Title | Criteria for Analysis and Identification |
|----------|-------------------------------|--|
| I | Identify Comparable Companies | <ul style="list-style-type: none"> ○ Business characteristics ○ Products & product Mix ○ Geographical markets ○ Customers ○ Financial characteristics ○ Size (revenues, operating income) ○ Profitability (operating margins) ○ Leverage |
| II | Identify Valuation Benchmarks | <ul style="list-style-type: none"> ○ Financial benchmarks based on industry and growth rates ○ Industry-specific benchmark ○ Mean and median values and where does the company fall |

| Step No. | Title | Criteria for Analysis and Identification |
|----------|------------------|--|
| III | Compile the Data | <ul style="list-style-type: none"> ○ Industry databases ○ Research reports |

The compiled data can then be used for the following:

- Identify the acquiree company's competitiveness
- Identify the industry trends, cyclicalities in the acquiree company's business sector
- Identify post acquisition improvement areas

To derive to the above mentioned information using the Company Comparable Analysis, the following analysis is performed and the below listed multiples are evaluated and compared:

| S. No. | Title | Contents (Multiples for Evaluation) |
|--------|-------------------------------|--|
| 1 | Market Analysis | <ul style="list-style-type: none"> ○ Identify undervalued companies ○ Identify key industry players ○ Identify acquisition targets |
| 2 | Operating Parameters Analysis | <ul style="list-style-type: none"> ○ Analyze companies' past and projected financial performance ○ Identify the correlation between trading and operating statistics e.g. high growth rates can be equated to high trading multiples ○ Relative measure of companies' operating efficiency |
| 3 | Credit Analysis | <ul style="list-style-type: none"> ○ Credit profile and implied credit rating ○ Capital structure ○ Amount of leverage ○ Typical Ratios: <ul style="list-style-type: none"> ● Debt/Book Capitalization ● Debt/Market Capitalization ● Debt/EBITDA ● EBITDA/Interest ● Cash Flow/Total Debt |
| 4 | Equity Value Analysis | <ul style="list-style-type: none"> ○ Equity Value = Outstanding shares x Current Share Price ○ Equity value/Net Income (P/E) ○ Equity value/After-tax Cash Flow ○ Equity value/Book Value of Equity (P/BV) ○ Total Shares Outstanding (TSO) = Total Shares + |

| S. No. | Title | Contents (Multiples for Evaluation) |
|--------|--------------------------|---|
| | | Underlying Options <ul style="list-style-type: none"> ○ Equity Value = (TSO x current stock price) - Option Proceeds ○ Option Proceeds = Total Options x Average Strike Price |
| 5 | Aggregate Value Analysis | It represents value available to service claims of all investors, including holders of both debt and equity securities <ul style="list-style-type: none"> ○ Equity Value + Net Debt ○ Net Debt = Short-term Debt + Long-term Debt + Minority Interest + Preferred Stock + Capitalized Leases - Cash and Cash Equivalents ○ Typical aggregate value multiples: <ul style="list-style-type: none"> ● Aggregate Value/Revenue ● Aggregate Value/EBITDA ● Aggregate Value/Free Cash Flow |

The following are the advantages of use of Comparable Company Trading Analysis Method:

- a) Since the value is established based on similar companies, the price arrived at is an acceptable benchmark for buyer/seller
- b) It is a valuable tool to deliver “maximum value” if you represent the seller in a bull market
- c) It takes into account the role of debt and equity in valuing a deal

The following are some of the disadvantages of the use of Comparable Company Trading Method:

- a) It is often difficult to find companies in the same sector that are strictly comparable
- b) The valuations are likely to be influenced by the bull/bear phase of the market and may not reflect the real value
- c) The comparable companies may have low liquidity or smaller capitalization or may not have a good enough “float”
- d) The stock prices may be higher or lower because of factors not related to the company like investor interest, regulatory, issues etc

- e) It does not take into account previous deals or management quality

Besides the disadvantages, there are several other issues that challenge the applicability of the method for valuations in an M&A deal. The following are some of the major issues:

- a) Different industries trade on different multiples and hence the multiples across which the comparison is may differ in each industry
- b) In case of some companies, their presence is spanned across several sectors or “bridge” sectors which make distinctions blur
- c) Even within the industry, the multiples are often inconsistent at times
- d) The relative value of the company compared to relevant industry multiple range
- e) It is important to evaluate whether the reference company itself is trading at a discount or a premium before valuations