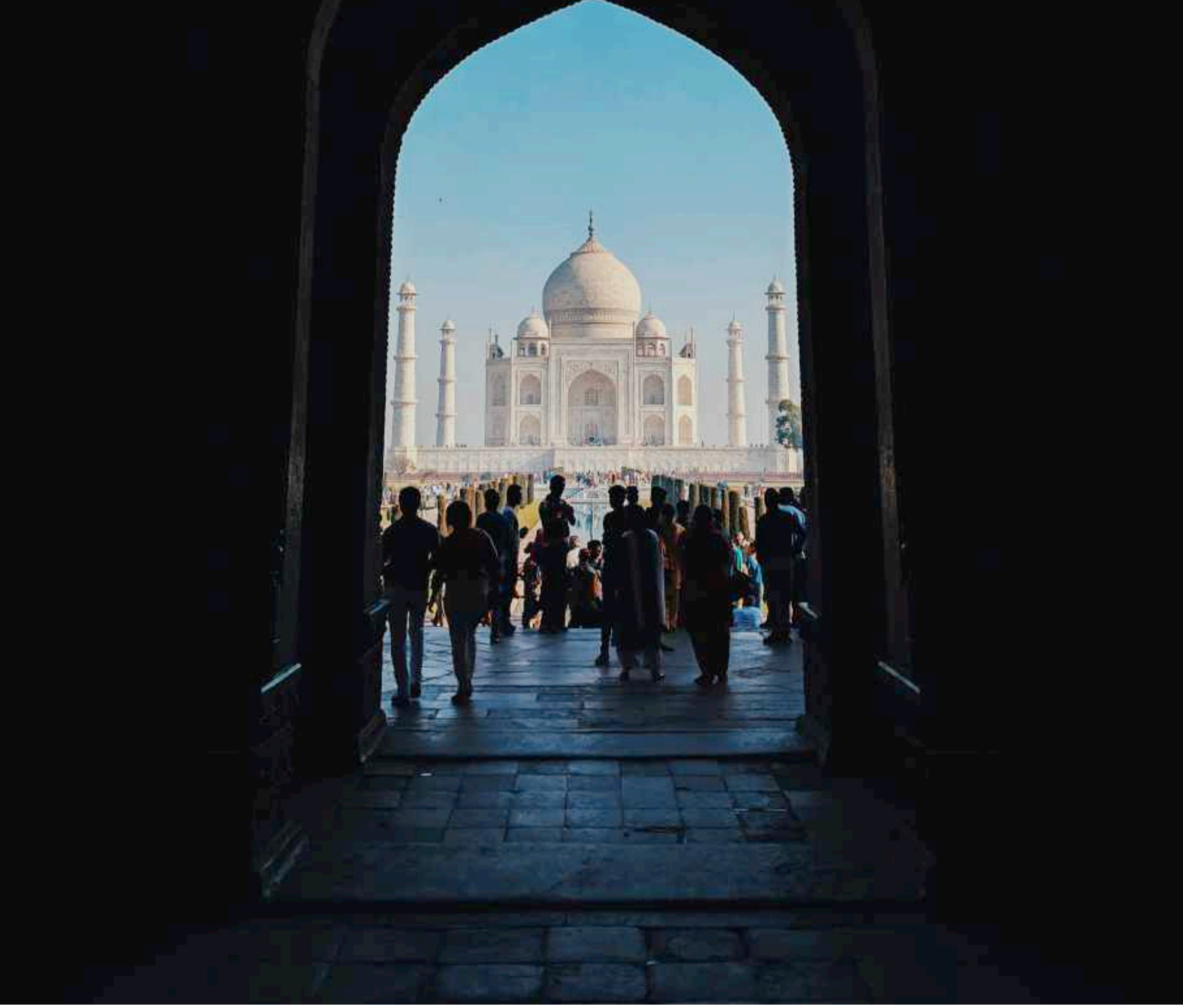
A New Dawn of Acquisitions

Opportunities in Distressed M&As in India

July 2020



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The Covid-19 pandemic is likely to give rise to a wave of distressed companies looking for buyers or investors; with depressed valuations and significant pockets of cash available to investors, there are likely to be many M&A opportunities that might be classed as “distressed M&A”.

Even before the coronavirus pandemic sent shockwaves through global economies, we have seen a surge in Distress M&A post implementation of Insolvency and Bankruptcy Code (IBC) in 2016. The paramount reason being the promoters in financial distress want to encash the opportunity before the insolvency is triggered, since insolvency may not result in any cashflow to promoters.

This article considers the opportunities for investors with a degree of appetite for risk, the options available with investor, and how the sophisticated buyer might address some of them.

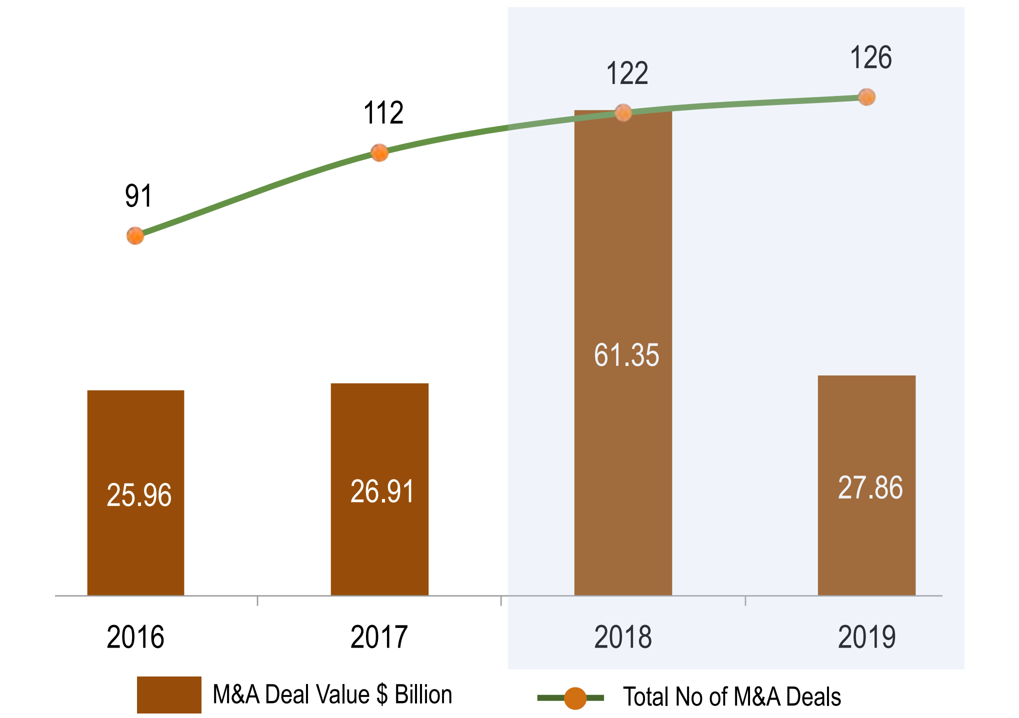
Thank you for reading, and we look forward to your feedback.

Sincerely,
Think Capital

Indian M&A round-up

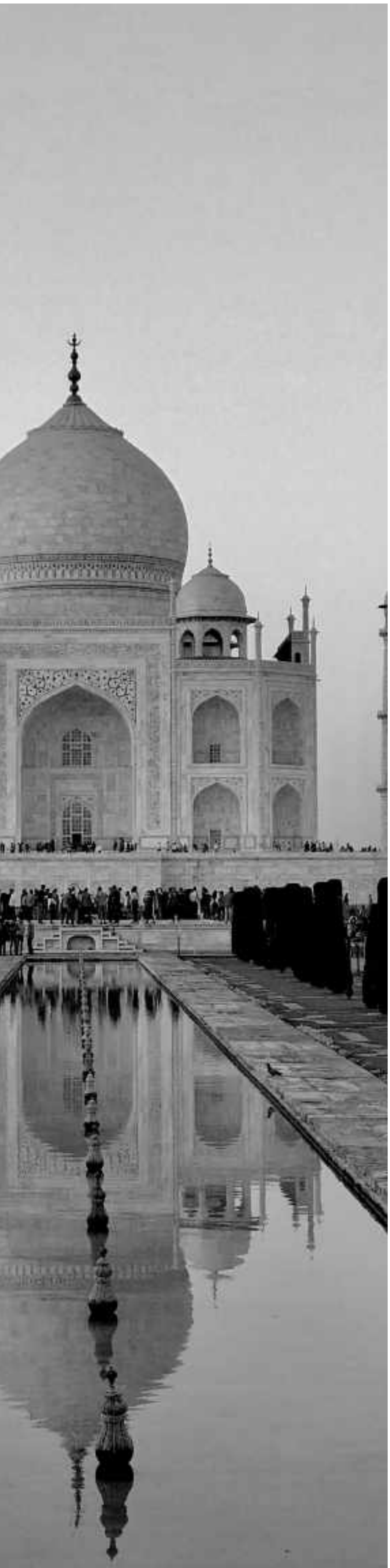
Indian Inbound and Domestic M&A* activity were much lower in aggregate deal value terms in 2019 with $27.86 billion in deal value as compared to $61.35 billion during 2018. The year 2019 witnessed a slight increase in total of 126 deals as compared to 122 deals in 2018. Consolidation across sectors has been a main feature of M&A activity in 2019. India's rapidly evolving distressed asset regime has also contributed significantly to consolidation opportunities. Another key trend was a preference for platform transactions, especially in the infrastructure sector.

Indian Inbound and Domestic M&A Activities in India



Source: VCCEdge Database

* M&A is considered where the total holding of more than 25% is exchanged or transacted of the target entity

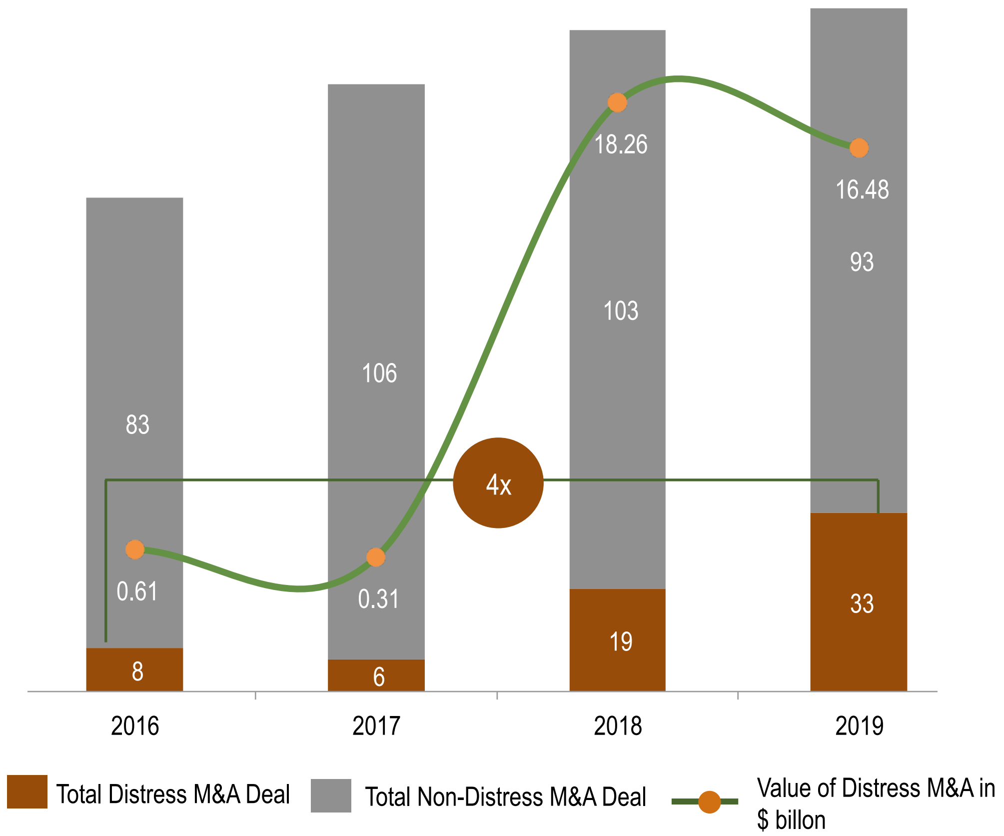


What is distressed M&A?

Distressed M&A differs considerably from non-distressed or “traditional” M&A as we are referring to the acquisition of assets, shares, or businesses where the seller or indeed the company itself being acquired is in financial distress (with the seller or the target having below investment grade rating). The company concerned may have some breathing space or be in early discussions with its lenders based on its view of its own cash needs going forward; towards the other end, the company could be in negotiations concerning a restructuring process or in a formal insolvency proceeding.

Indian Distress M&A* activity has seen a lot of traction during 2018 and 2019 mainly due to the implementation of IBC. During 2019 distress M&A accounted for over 59% of the total M&As with $ 16.48 billion in aggregate deal value terms. During 2018, the Distress M&As was 30% of the total M&As with $ 18.26 billion in aggregate deal value terms.

Distress Inbound and Domestic M&A Activities in India



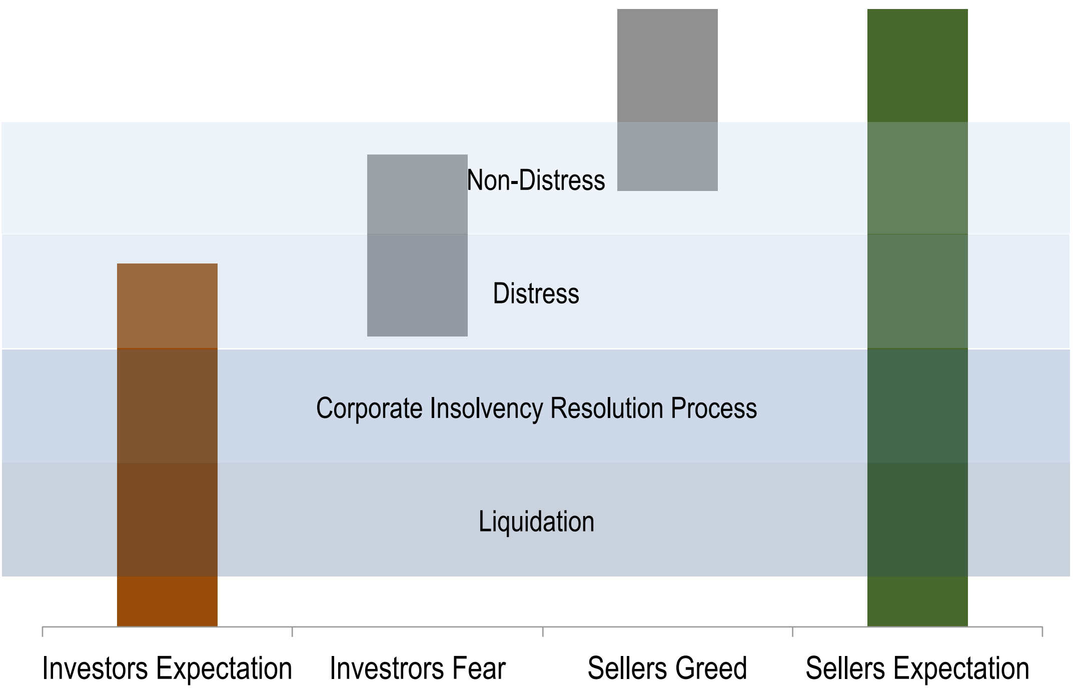
Source: VCCEdge Database and Think Capital Analysis

* Distress M&A is where the Target Company or the Seller is having lower than investment grade credit rating and/or is in financial / liquidity strain.

Sellers Greed and Acquires Fear

There is a massive value mismatch when it comes to distress M&As. Traditionally, distressed M&As command lower valuation in buyers market compared to non-distress M&A. But with the success of IBC, we have seen M&A happening at 3-5 Cents to a Dollar of claim outstanding.

M&A Valuation in various scenario



In the recent transaction, SMC Power Generation acquired steel mill and power plant of Concast Steel and Power Limited in a liquidation process. $ 40 Mn offered as upfront cash to lenders (approx. 3 cents to a dollar of claims), thus making it the largest acquisition in the liquidation process under the Insolvency and Bankruptcy Code, 2016. We estimate more such deal will pick-up its pace in the coming year, where buyers will try to bargain higher under liquidation.

M&A under Insolvency and Bankruptcy Code, 2019

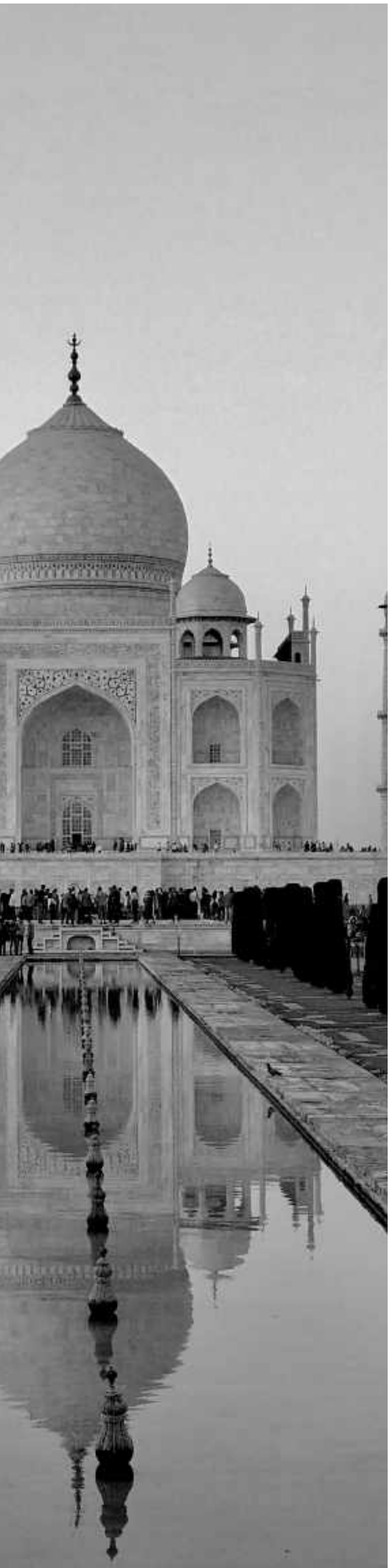
The resolution process under Indian Insolvency and Bankruptcy Code is divided into two parts, a 270 days Resolution Period called Corporate Insolvency Resolution Process (CIRP) and if no resolution is achieved during CIRP within the stipulated timeline of 270 days (extended up to 330 days) liquidation of assets is ordered. Even in the liquidation, the Liquidator has the choice to sell the Company as (a) an asset on a standalone basis; (b) the assets in a slump sale; (c) a set of assets collectively; (d) the assets in parcels; (e) the corporate debtor as a going concern; or (f) the business(s) of the corporate debtor as a going concern.

	Under CIRP	Under Liquidation
Approval of Committee of Creditors / Stakeholders is required to approve of sale as going concern	Yes	No
Insolvency Processional / Liquidators Approval	Limited to oversee the application of law	Authorized to take commercial decision
Transfer of commercial contract	Yes	Maybe
Transfer of licenses	Yes	Maybe
Liabilities prior to Insolvency / Liquidation commencement date	Resolution plan should specify how resolution applicant has dealt with liabilities outstanding as on Insolvency Commencement date	Successful bidder shall fix a price (essentially higher than reserve price). However, Liquidator has power to sell company as Going Concern upto 75% of the liquidation value
Timeline	3-6 Months from date of invitation of expression of interest	2-4 months from the date of invitation of expression of interest

Relaxation in takeover guidelines by Securities and Exchange Board of India (SEBI)

SEBI in its recent amendment has relaxed pricing framework under the preferential route and exempted allottees of preferential issues from open offer obligations. Eligible listed companies having stressed assets will be able to determine pricing of their preferential allotments at not less than the average of the weekly high and low of the volume weighted average prices of the related equity shares during the two weeks preceding the relevant date. At present, the determination of the pricing covers a period of 26 weeks or more for frequently traded shares.

To be eligible for stressed company criteria, an issuer has to disclose all the defaults relating to the payment of interest, repayment of principal amount on loans from banks or financial institutions and such default should have continued for a period of at least 90 calendar days after occurrence of first such default. Also, the credit rating of the listed instruments of the company should have been downgraded to “D” and existence of inter-creditor agreement in terms of RBI (Prudential Framework for Resolution of Stressed Assets).



About Think Capital

Think Capital is a mid market Investment Bank focusing on M&A, Fund Raising, Restructuring and Turnaround Advisory for mid and large companies. We have successfully delivered transactions in a varied of sectors including Financial Services, Food and Beverages, Water Technology, Consumer Goods, Healthcare, Auto Components, Energy (thermal and renewable) and Infrastructure among many others. Our senior management comprises of professionals with deep expertise in Investment Banking and Management expertise, and come from varied fields and backgrounds.

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