Case Study - Acquisition of Henkel India Ltd. by Jyothy Laboratories –Will it be Successful?

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ABSTRACT

Mergers and Acquisitions is a strategic move made by a company to achieve inorganic growth. However selecting a right partner for merge requires lot of deliberations. An acquirer should select the target after a thoughtful process. Size of a company, mode of payment, benefits from the acquiring company and post-merger integration are few of the key parameter that should well planned before making a final choice. The present case is about building operational efficiencies by Jyothy Laboratories through acquisition of Henkel Indian operations. Jyothy was depended on it single product "Ujala Supreme" for revenue and had plans for market expansion by increasing its product portfolio. On the other hand Henkel India struggled for survival since the time of its entry into Indian markets. Though Henkel had a strong product portfolio but had failed to take the leverage in Indian markets. Jyothy had a strong presence in semi urban and rural areas parallel to this Henkel had a good hold in urban area. By acquiring Henkel Jyothy will get access to the bunch of products but also get entry in new segment. Since long Jyothy was trying hard to acquire Henkel Indian arm and finally succeeded in March 2011.

The case is developed by referring various secondary sources like newspaper articles, annual reports of the companies and its website.

Keywords: Mergers and Acquisitions, Target Company, Strategic Move.

I THE CASE

"The Henkel deal came at just the right time. This is also the best tax planning they (Jyothy) could have done as they'll be able to get credit for Henkel's losses." **-SubbuSubramaniam, Managing partner, M Cap Fund Advisors**

"We felt comfortable making a loan to them at such short notice as we knew they (Jyothy) were a debt-averse company and had a healthy balance sheet." - **ParitoshKashyap, Executive Vice President, Kotak Mahindra Bank**

"Jyothy needs to see its task for Henkel as that of brand re-creation."**-Santosh Desai,MD&CEO, Future Brands**

"With growth of its flagship products slowing down, and margins under pressure, this acquisition is the best tax planning Jyothy could have done."**-SubbuSubramaniam, Managing partner, M Cap Fund Advisors**

After all hardships, finally UllasKamath, (Kamath) Deputy Managing Director of Jyothy Laboratories was able to strike the deal with Henkel AG to sell its Indian Subsidiary which was making losses since the time of its entry into Indian market.

With the beginning of millennium, Kamath met twice Henkel management to form an alliance or to sell the Indian arm to his company but was not able to crack the deal. In January 2011, things turned into his favor and got the news he was waiting for more than a decade. Henkel parent group was in talk with investment bankers to exit from Indian markets. Without any delay, he flew to Dusseldorf, headquarters of Henkel, with all set to get the Henkel Indian arm under the umbrella of Jyothy.

II ABOUT JYOTHY LABORATORIES – THE ACQUIRER

Mr.M.P. Ramachandran(Ramachandran), in 1983 started the company with an initial capital of Rs. 5000 and the only product – Ujala. With a small factory in a small district with his own formulation, he laid the foundation stone for his little venture.

Since starting, Jyothy has taken the utmost advantages of tax holidays by setting up plants in the backward areas. This was the incident that witnessed the meeting of duo -Kamath and Ramachandaran. He met Ramachandaran in Bangalore when one of his friends was looking for Ujala distributorship. Kamath gave advice to set up plants in areas which was providing tax benefits. This was proven a boon and within a span of three months he was member of Ramchandaran team and became a second in command.

Ramchandaran operated with two principles- reinvest profits into business and never dependent on debt. He was a firm believer of power of advertisement. In early 90s, the era of pre detergent war, he incurred huge advertisement expenses to promote Ujala.

In 1993, Jyothy Laboratories Ltd. (JLL) was incorporated and a factory was established at Tamil Nadu to manufacture Ujala. Later on in 1997 Ujala was roll out nationally and within two years in 1999 it became a Rs. 100 crore brand.

With the beginning of 2000, JLL ventured into households insecticides and utensils care segment. Over a period of time, the company has also forayed into personal care, fabric care services and fragrances.

In 2007, JLL came with IPO and became a listed company. Today (JLL) is having its presence across India with all its brands catering to the needs of the different consumers.

III ABOUT HENKEL INDIA -THE TARGET

Henkel India Ltd. (HIL) was a subsidiary of Henkel AG & Company in Dusseldorf, Germany. To have strong footprints in Indian market, Henkel formed a joint venture with A.C Muttiah'sTamilnadu Petro Products Ltd (TNPL), a Southern Petrochemicals Industries Corporation (SPIC) group company.

Since its inception, Henkel was struggling hard for its survival. It was failed to reap the fruits from its joint venture.

Only plant at Karaikal, Pondicherry to serve the entire country lead to higher transportation cost and ate up the margins. The decision was taken in order to have quality confirmation. While starting up in India, parent group was not in favor of outsourcing because of quality issues so they decided to manufacture the product on their own. This decision was on different lines as compare to Europe where company outsourced the production.

Waiting for approvals from parent group for minor issues affected the operations. Also many of employees in new entity were from SPIC had experience in fertilizers and had no idea about FMCG sectors. As a result, decisions regarding marketing and advertising were taken by the Germany counterpart of Henkel without having a proper understanding of Indian markets.

IV THE NEED FOR SEARCH

The company was highly dependent on single brand "Ujala Supreme" – fabric whitener (Refer Exhibit I – Ujala Losing its Shine). However Jyothy has tried to diversify into detergent, dish wash and mosquito repellents but stiff competition has made a tough ride. Moreover company has its major presence in rural market and with only three brands. The company was facing many challenges to grow more in absence of wide range of product portfolio.

Setting up plants in areas providing tax advantages was no more helpful for the company to improve profits.

JLL was searching for a company that can fill in the gaps in different segments where it was having no presence and at the same time help it to enter into the urban areas.(Refer Exhibit II – Product Wise Market Share)

V SELECTION OF HENKEL

Henkel India had a strong product portfolio but had failed to take the leverage in Indian markets. Its brand like Margo, Fa, Prill and Mr.White had a good recall. The company always focused on technology and was failed in building an emotional connects with the customers.

Although company had never tasted profits, it was having presence across the nation. Majorly in urban sector contrary to Jyothy which has strong hold in semi urban and rural areas. The rural urban mix of Jyothy was 75:25 whereas of Henkel the ratio was 30:70.

The company had sales revenue of Rs. 400 crore and was making loss of Rs. 40 crore a year and has lost money to the tune of 500 crore over the years. This was a huge savings in tax for any profitable company who take over the Henkel India by offsetting the profits against accumulated losses.

Henkel was a perfect fit for Jyothy being a complementary in nature. With the product portfolio of Henkel, Jyothy was able to widen its presence across socio economic categories from premium to niche categories.

With the Henkel acquisition Jyothy was able to expand its reach, leverage the economies of scale and improve the positioning. (Refer Exhibit III – Post Integration Synergies)

VI CRACKING THE DEAL – THE TUG OF WAR

In 2000, the first attempt made by Kamath but was not succeeded.Kamath proposed to join the hands for distribution of Henkel products into different areas other than big cities. Henkel dissented on giving distribution channel to a company which was half of its size.

Within span of 5 years they restarted talk, this time Henkel was also worried about its future in the Indian market. The parent group played a smart game by putting a proposal of taking majority stake in Jyothy Laboratories. Ramchandran rejected the offer being successful he was not in opinion to part with stake.

On one fine morning of January 2011, Kamath came to know from the sources about the Henkel AG looking for a buyer to sell its Indian unit. He flew to the Dusseldorf, the Headquarters of Henkel AG with better preparation this time.

Kamath was aware of the fact that theJyothy's balance sheet size was not fit to get into bidding war. He put another option in front of top management in Germany to send them proposal after consulting his team in India. He made very clear about not participating in bidding process and if they (Henkel) don't like to sell the Indian arm they were free to use his turnaround plan.

By the timeKamath reached India and sent the proposal, the deal took a new turn which was proved to be a game changer in the entire episode.

A C Muttiah of SPIC group, joint venture partnerin Henkel India was unhappy with the Henkel parent group not considering him before selling its share. Through MAPE Advisory, he offered his share in the company to Jyothy. In March 2011, JLL acquired 14.9% in HIL for Rs. 60.73 crore and took the captainship of the company.

Again Kamath visited Dusseldorf and hit the bull's eye. He sealed the deal by giving an option to Henkel parent group of revisiting India after 5 years and can acquire 26% stake in combined entity. In May 2011, he bought 50.97% stake at the cost of Rs. 142.9 crore. He got an unexpected support from Kotak Bank of Rs. 600 crore, which helped to sail the ship with smooth and ease.

On June 30, 2011 JLL acquired 3.97% shares from the open market at the cost of Rs. 18.9 crore.It also acquired 12.05% shares as compare to proposed 20% through open offer at the amount of Rs. 57.8 crore as on Oct. 17, 2011. (Refer Exhibit IV – Acquisition Details)

VII INTEGRATION PROCESS – POST ACQUISITION TASK

Though Kamath was successful to bag the company but the real test was waiting for him. Integration of both the entities in order to derive maximum benefits but this was not a child's play. Ramchandaran and Kamath were aware of the facts that coming days would not be the easy for them.

Soon after the deal, entire Henkel team around 250 people quit as they found difficult to work with Indian company. Jyothy retained selected key functional area's middle manager like operations, distribution, marketing and finance. They also shut down the Henkel's office in Chennai and guest house across countries and shifted the corporate office to Mumbai. Also purchase and supply chain activities were centralized. Jyothy also brought marketing strategies under its purview for Henkel products.

On manufacturing end, they decentralized the production of Henkel products to the 28 units of Jyotyhy Laboratories and outsourced where ever it was economic beneficially unlike centralized production with only a plant that Henkel did in past.

Procurement of raw material was another area. Henkel had compulsion of buying linear alkyl benzene (LAB) a key ingredient in making detergent from its Indian venture partner; Jyothy was able to fetch most competitive prices from its vendors as they have a policy of paying upfront cash. By following Jyothy model, they built the synergy and brought the cost down.

Kamath in one of his interview explained the mantra through which they were saving the distribution cost. He said "We always ask ours supplier to send the raw material when the finished are ready to be delivered". This in turns help them to fetch a better rate unlike most of units where trucks deliver the raw material and goes empty charging for full trip.

To bring in more efficiency, states where Jyothy has its godowns were also put in use for Henkel and the godowns and mother depot of Henkel was used by Jyothy to supply goods. The effect of this integration was saving into cost amounted Rs. 26 crore, which Jyothy was paying to its super stockiest. Jyothy was used to pay 5% margin to its stockiest.

With the addition of seven more products salesmen has more to sell and the pay-off would be dip in operating costs. Also benefits of economies of scale would be harvested. Manufacturing more products (combined entity- Jyothy and Henkel) fixed costs would be mop up by larger turnover.(Refer Exhibit V – Bouquet of Products& Exhibit – VI Segment Wise Products Presence)

Jyothy also instructed its sales team that their costs – salary, travelling expenses, and allowances should not be more than 3% of sales. In distribution Jyothy took over the weak areas and kept regions untouched where Henkel was extremely strong.

Financially also Henkel proved a good proposition for Jyothy. With accumulated losses of Rs. 500 crore, Jyothy was able to reduce its tax liability for three-four years.

Operating model has also witnessed change in post-acquisition scenario. The pipeline inventory came down to Rs. 18 crore from Rs. 70 crore which in turns lead to lesser investment in working capital.

VIII ENTRY OF RAGHUNANDAN

With the acquisition of Henkel the duo-Ramchandaran and Kamath felt the need of change from gurukul to business school. The company never had brand managers, manufacturing or sales head. Advertising agencies was the whole and sole for brand building. With new portfolio of 10 brands in four segments professional team was required to run the business effectively and efficiently.

In May 2012, JLL appointed Raghunandan (Raghu) as CEO of JLL. Raghu also known as "Turnaround Man" had changed the futures of family owned business like Dabur and Paras. According to Raghu, there were many things that required to be changed in Jyothy. The new job was full of challenges. Henkel was not successful because of its investment in brands was low and overheads were high. Jyothy after having a good head start has not invested much. So his task was double folded – minister the Henkel brands and also smooth integration of JLL and Henkel.

Soon after taking the charge, Raghu started charting out the plans for the company growth. He was assigned with a task to build the talent pool at the various categories, supply and other heads that a multinational company should have. With his team of 15 senior managers, he focused on key areas to fuel growth engine. He introduced a second line of management to bring in fresh thinking, leadership and strategy.(Refer Exhibit-VII – The New Structure) The first move he took was shift from company owned sales force and commercial sales agents (CSA) to carry and forward agents. Only top 20% distributors were covered by the company's direct sales force and rest was by distributor's salesman. Also to save costs he replaced turnover based incentives by fixed fee system for the sales team. This results into saving of Rs. 10 crore.

Raghu also reworked on distributor and retailer margins. Jyothy was offering 12-16% margins to its retailer and distributors which were higher than Industry averages. The strategy was good till company had three products as this was a driving factor for a retailer to sell more. But with larger bouquet of products margins need to refine. Jyothy offered margins of 8% and was able to save Rs. 30 crore.(Refer Exhibit- VIII- The New Margins)

The money saved was spent partially on advertising and rest was added to company's bottom line. Apart from it, Raghu also took responsibility to change distributors list. Till now Jyothy worked with smaller ones but with Henkel's products it started on eyeing larger distributors especially who had experience of working with MNCs. This helped them to reach more stores.

Raghu also introduced products in middle in premium segments when company started shifting from regional to national player. Moving forward, he is planning to take seven brands i.e. Henko, Ujala, Fa, Margo, Pril , Maxo and Exo to the next level.

IX LOOKING AHEAD

On July 2012, the name of Henkel India Ltd. was changed to Jyothy Consumer Products Ltd. (JCPL). Within couple of years the Jyothy was able to integrate Henkel in a phase wise manner properly and has introduced structural changes along with new strategies in different segment.

In April 2013, JCPL was merged with JLL. It has been 24 months now; JLL took over the erstwhile Henkel.At this stage analyst view that how this marriage will bring fortune to Jyothy. In span of 730 days, with series of actions the company had brought in operational efficiency, hence making the takeover of Henkel profitable.

Moving further, Jyothy needs to look how to remain competitive in the market place with the diversification adopted 104 weeks back. Till date it seems an ambitious move by JLL -an Indian company acquires multinational – Henkel which is not seen frequently in the Indian markets. However, the time will tell to what extent the merger has been fruitful for Jyothy and was it a wise move to acquire Henkel.

Exhibit-I
Ujala Losing its Shine

Year	Market Share by Volume (%)	Market Share by Value(%)
2009-2010	58	72
2010-2011	58.3	72
2011-2012	60	74
2012-2013	59.06	72.6

Source: Compiled by Authors from JLL Annual Reports

Exhibit-II Product Wise Market Share

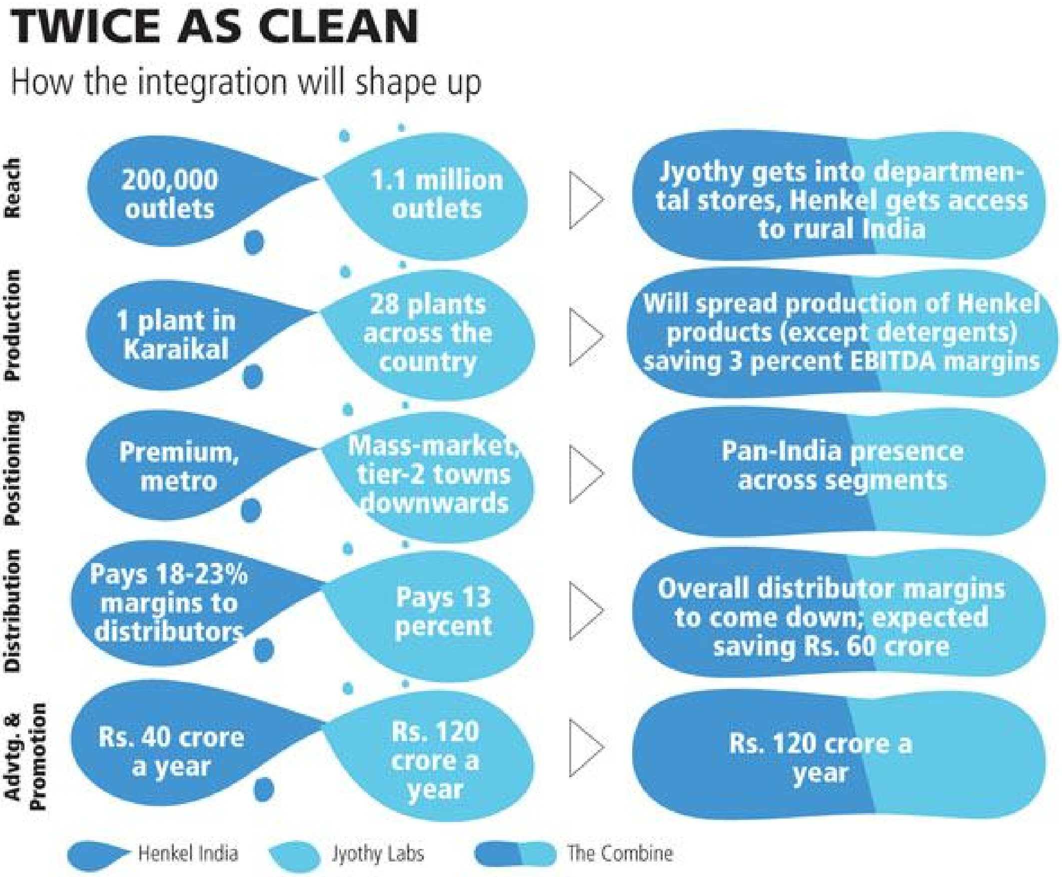
THE BIG PICTURE

CATEGORY	COMPANY	BRANDS	MARKET SHARE	COMPETITORS
Fabric care (Total size: ₹13,000 cr)	Jyothy Labs	Ujala Supreme (fabric whitener)	72% of fabric whitener market (₹250 cr)	Robin Blue (Reckitt Benckiser): 5-8% and balance with regional players
		Ujala Stiff and Shine (fabric conditioner)	3.4%	Comfort (HUL): 5%
		Ujala Technobright (detergent)	Negligible	Surf (HUL): 11%
	Henkel India	Henko (detergent)	1%	Surf (HUL): 11%; Ariel (HUL): 4%
		Mr White (detergent)	Less than 1%	Tide (P&G); Rin and Sunlight (HUL)
		Chek (detergent)	Less than 1%	Wheel (HUL); Ghari; Nirma
Mosquito repellent (coil only) (₹800 cr)	Jyothy Labs	Maxo	22-24%	Goodknight (Godrej): 30%; Mortein (Reckitt Benckiser): 26%; All Out (SC Johnson): 10%
Dishwashing (₹700-800 cr)	Jyothy Labs	Exo (bar)	6-7%	Vim (HUL): 60%; rest fragmented among players like Nip (FENA), Expert (Rohit Surfactants)
	Henkel India	Pril (liquid)	4-5%	
Personal care				
Deodorants (₹1,000 cr)	Henkel India	Fa	4%	Axe, Rexona, Dove (HUL): 25%; Set Wet Zatak (Paras): 9%; balance with other players
Soap (₹10,000 cr)	Henkel India	Margo	1%	Medimix (Cholayil): 2%; Chandrika (Wipro): 1%; Hamam (HUL): 3%
	Jyothy	Jeeva	Negligible	

Source: Industry estimates

Source: The Strategist-July 11 2011, Supplement of Business Standard

Exhibit- III
Post Integration Synergies



Source: Article in The Forbes –June 8,2011

Exhibit-IV
Acquisition Details

Henkel Acquisition

INR Rs. Cr

Seller	% of shares	Value
TPL	16.66	67.9
Henkel AG	50.97	143.0
Open Market	3.97	18.9
Open offer	12.05	57.8
Other Transaction Cost		27.88
Preference Capital		42.6
Loan Repayment		425.0
Total	83.65	783.0

Source: JLL Analyst Presentation – November 09,2011

Exhibit V
Bouquet of Products

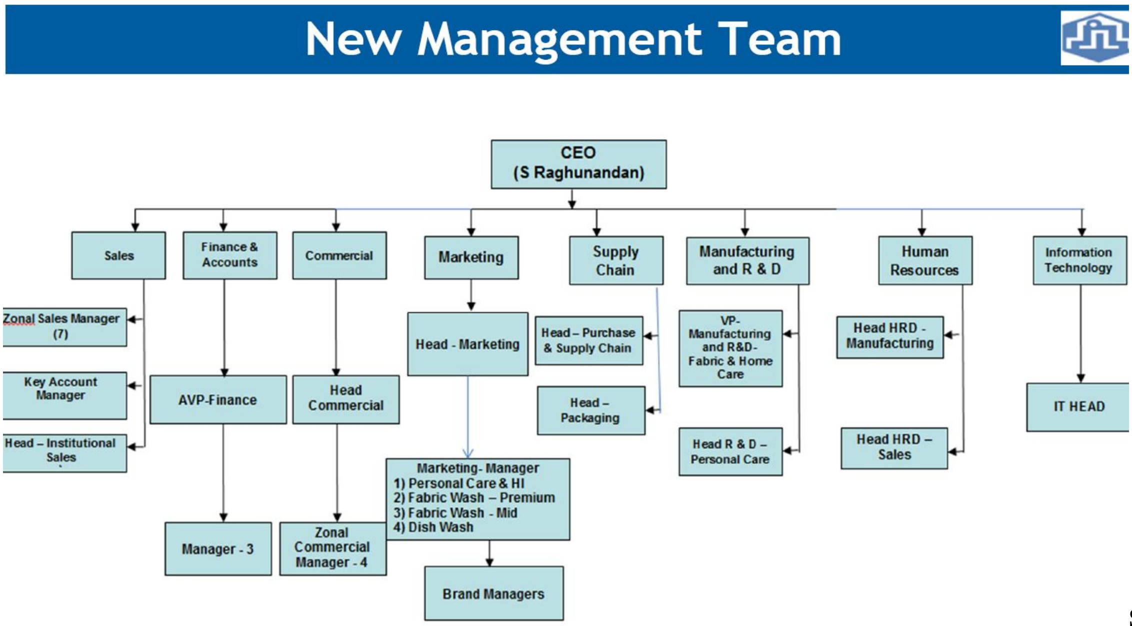
Source: Jyothy Laboratories Ltd. Annual Report 2010-11

Exhibit-VI
Segment Wise Products Prsence

	Value	Mid-Premium	Premium	Niche
Detergents	Check Morelight	Ujala Mr. White	Technobright Henko Champion	Technobright Matic Henko Matic
Other Fabric Care		Ujala Whitener Mr. White Bleach		Ujala Stiff & Shine
Dish wash		Exo Bar, Round Pril Bar	Pril Liquid Exo Liquid	Exo Scrubber
Household Insecticides	Maxo Coil	Maxo Liquid		Maxo Cream Wet Wipe
Personal Care		Jeeva Nikki	Fa Deo Fa Soap	Margo Neem

Source: Jyothy Laboratories Ltd. Annual Report 2010-11

Exhibit – VII
The New Structure



Source: JLL Analyst Presentation – February 07, 2013

Exhibit- VIII
The New Margins

Channel Margin Rationalisation

	Stockist Margin		Retailer Margin	
Brand	Old	Revised	Old	Revised
EXO	6-8	6	8-15	8-10
MAXO	6-8	6	10	10
MAYA	6-8	6	10-20	10-15
MORE LIGHT	6-11	6	10-15	10
UJALA	8	6	10-14	10
INDUSTRY		**4-5**		**8-10**

Source: JLL Analyst Presentation- November 01, 2012

Exhibit- IX
The JCPL Performance

JCPL - Status Update

Rs. In lakhs

Period	Net Sales	EBITDA %
Jan-Mar'11 (3 mths)	11,921	-6.4 %
Apr-Jun'11 (3 mths)	12,311	8.8 %
Jul - Sept'11 (3 mths)	10,746	10.6 %
*Oct - Dec'11 (3 mths)	7,691	1.61 %
Jan-March'12 (3 mths)	11,063	14.2%
Apr-Jun'12 (3 mths)	11,489	10.2%
#July-Sept'12 (3 mths)	8,452	-0.26%

*Oct-Dec'11 - Due to temporary shut down of Karaikal plant on account of Labour unrest from September 26, 2011 to December 26, 2011, 61 days. Sales of Henko Detergent lost 27 Crores and thereby loss of Rs. 7 crores in EBIDTA (10%)

July-Sept'12 - Rationalisation of Henkel distributors done in the month of August/September resulting in temporary loss in primary sales. Integration of JLL and Henkel distribution underway and expected to be completed by December 2012 and sales expected to be normal from coming quarters.

Source: JLL Analyst Presentation- November 01, 2012

Exhibit-X
The Income Statement of JLL

Profit & Loss Account

Particulars	Quarter Ended			Nine Months Ended		Year ended
	31-12-2012	30-09-2012	31-12-2011	31-12-2012	31-12-2011	31-03-2012
Net Sales	20,378	17,783	16,631	59,147	44,395	66,278
Other Income - Operating	74	23	27	121	73	19
Total Income	20,452	17,805	16,658	59,268	44,468	66,297
Cost of Goods Sold	11,117	9,065	8,681	32,489	24,015	37,259
Employee cost	2,269	2,355	2,214	6,867	6,256	7,802
Advertisement and Sales Promotion expense	1,069	1,592	659	4,293	3,270	4,283
Other expenditure	2,346	2,554	2,279	7,238	6,244	8,686
EBITDA	3,651	2,239	2,825	8,380	4,683	8,266
EBITDA % to Net Sales	17.9%	12.6%	17.0%	14.2%	10.5%	12.5%
Depreciation and Impairment	325	330	622	991	1,361	1,703
Finance Cost	1,719	1,648	229	4,853	605	1,943
Other Income - Non Operating	1,725	1,637	1,429	4,987	4,122	5,701
Profit Before Tax	3,332	1,899	3,403	7,523	6,839	10,322
Tax	726	372	495	1,628	1,280	1,970
Profit After Tax	2,606	1,527	2,908	5,895	5,559	8,352
EPS	1.62	0.95	1.80	3.66	3.45	5.18

Source: JLL Analyst Presentation – February 07, 2013

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