Research Paper Management

Corporate Restructuring in India with Special Reference to Reliance Industries Limited (RIL)

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ABSTRACT

The increase in Competition, rapid advances in technology, more demanding shareholders, more flexible workforces and rising complexity of the business conditions have increased the burden on managers to deliver superior performance and value for their shareholders. Corporate restructuring helps companies to address poor performance pursue new strategic opportunities and attain credibility in the capital market. In this modern "winners take all" economy, companies have to take a timely responsive action to save their organizations. At this point of time, company executives may ask whether it is time to restructure the company. However, before considering any action, they must first answer the questions: "Will restructuring work?" and "When does restructuring improve economic performance?"

During the past decade, corporate restructuring has increasingly become a staple of business and a common phenomenon around the world. Unprecedented number of companies across the world have reorganized their divisions, restructured their assets and streamlined their operations in a bid to spur the company performance. Corporate Restructuring generally includes a diverse array of company actions, from selling business lines to acquiring new business lines, from downsizing workforces to the addition of new business units and from stock repurchase to debt elimination. It has enabled numerous organizations to respond quickly and more effectively to new opportunities and unexpected pressures so as to re-establish their competitive advantage.

Keywords : Corporate Restructuring, Strategic Opportunity, Competitive Advantage

Introduction

Restructuring refers to a multidimensional process. However, the term corporate restructuring is used in the context of operational restructuring as a long term strategy of business. Operational restructuring is an ongoing process, which includes improvement in efficiency and management, reduction in staff and wages, sales of assets (for example, reduction in subsidiaries), enhanced marketing efforts, and so on with the expectation of higher profitability and cash flow. Rising competition, breakthrough technological and other changes, rising stock market volatility, major corporate accounting aspects have increased the responsibility to managers in order to deliver superior performance and enhance market value to shareholders. The companies which fail to deal with the above successfully may lose their independence, if not face extinction. Increasing competition, rapid advances in technology, more demanding shareholders and rising complexity of the business conditions have increased the burden on managers to deliver superior performance and value for their shareholders. Corporate restructuring helps companies address poor performance, pursue new strategic opportunities, and attain credibility in the capital market. It can also have a huge impact on a company's market value, often in terms of billions of dollars. But how does a corporate restructuring actually get done? How do the related bankruptcies, mergers and acquisitions, spin-offs, and buyouts affect creditors, shareholders, and employees? What are the options, issues, trade-offs, and conflicts?

During the past decade, corporate restructuring has increasingly become a staple of business and a common phenomenon around the world. Unprecedented number of companies across the world have reorganized their divisions, restructured their assets and streamlined their operations in a bid to spur the company performance. It has enabled numerous organizations to respond quickly and more effectively to new opportunities and unexpected pressures so as to re-establish their competitive advantage. The suppliers, customers and competitors also have an equally profound impact while working with a restructured company.

Review of Literature

- According to Peter.F.Drucker, (International Conference on Technology and Business Management, March 26-28,2012) the management guru, the greatest change in corporate culture and the way business is being conducted, is the strategic intervention and relationship based not on ownership, but on partnership. He also observed that there is not just a surge in alliances but a worldwide restructuring of companies in the shape of alliance and partnerships.
- According to a recent survey by the global consulting major, Booz, Allen and Hamilton, corporate restructuring in the form of strategic alliance is spreading in every industry and is becoming an essential driver of superior growth. The corporate restructuring in terms of number of strategic alliances in the world is surging. For instance more than 20,000 new alliances were formed in the U.S between 1987 and 1992, compared with 5100 between 1980 and 1987 and 750 during the 1970s. The firm also predicts that within the next five years, the value of alliances is projected to range between $30 trillion to $50 trillion. The survey also reveals that more than 20% of the revenue generated from the top 2,000 US and European companies now comes from alliances, with much more predicted in the near future.
- According to a study by the Harvard Business School (2011), corporate restructuring has enabled thousands of organizations around the world to respond more quickly and effectively to new opportunities and unexpected pressures, thereby re-establishing their competitive advantage.
- According to the 2008 Boston Consulting Group (BCG) New Global Challengers report, top companies from rapidly developing economies (RDEs) such as India, China, Russia, Mexico

and Brazil, are changing the world and challenging the dominance of establishing multinational players across the world. In 2006, they completed 72 outbound acquisitions, up from 21 in 2000. The average size of these transactions grew from $156 million in 2001 to $981 million in 2006. Of the 100 companies on BCG's list, 41 are from China, 20 from India and 13 from Brazil, with the rest coming from other Rapidly Developing Economies.

- Ashwani Puri (2008) opined that Business Restructuring in India has been slow and expensive. due to lack of conducive regulatory environment, a complex tax framework, court processes and an endless list of compliance issues impede the process and impair efficient and effective realignment of resources through restructuring.
- Corporate restructuring in India through Mergers and Acquisitions is facilitated by the Supreme Court of India which in the land mark judgement of HLL–TOMCO merger has said, "In this era of hyper competitive capitalism and technological change, industrialists have realized that mergers/acquisitions are perhaps the best route to reach a size comparable to global companies so as to effectively compete with them. The harsh reality of globalization has dawned that companies which cannot compete globally must sell out as an inevitable alternative."
- Prashant Kale and Harbir Singh (2004) in their articles on M&A between 1982 and 2002 concluded that in the initial years of economic liberalization, Indian companies failed to create sufficient value from acquisition, as compared to Multi National Companies.

Objectives of the Study

- To Study and Analyze Corporate Restructuring with reference to Reliance Industries Limited (RIL), India.
- To Study the Various issues related to the process of Corporate Restructuring.
- To understand the general framework of corporate restructuring and reorganization.
- To analyze how Corporate Restructuring can be used as a tool of Competitive Advantage.
- To provide Suggestions to alleviate the problems of Corporate Restructuring in India.

Corporate Restructuring:

A Boon For Competitive Advantage Crum and Goldberg define restructuring of a company as "a set of discrete decisive measures taken in order to increase the competitiveness of the enterprise and thereby to enhance its value." It generally includes a diverse array of company actions, from selling business lines to acquiring new business lines, from downsizing workforces to the addition of new business units and from stock repurchase to debt elimination

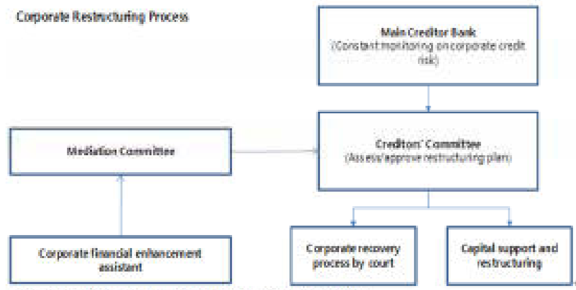
The general framework for corporate restructuring and reorganisation consists of the following:

1) Reorganisation of assets.
2) Creating new ownership relationships.
3) Reorganising financial claims.
4) Corporate Strategies.

It has enabled numerous organizations to respond quickly and more effectively to new opportunities and unexpected pressures so as to re-establish their competitive advantage. The suppliers, customers and competitors also have an equally profound impact while working with a restructured company. In India, corporate houses have recently witnessed an increase of restructuring in different organizations. The main reasons for the sudden impetus to restructure in India are as follows:

a) Implementing of strict MRTP provisions and new government policy of relicensing. b) Increased competition is another key element for giving rise to corporate restructuring. c) Mounting pressure on margins have necessitated higher volume of business, resulting in mergers and acquisitions or the grand concentration of strategy has led to demergers of non profitable businesses, and d) All round resource optimization in existing businesses to streamline operational profit and to stay fit in competition. However, some organizations have done their restructuring through acquisition and mergers and some through demergers.

A framework of corporate restructuring shown in the Figure below explains all about corporate restructuring.



(Source: Financial Service Committee/ Financial Supervisory Service)

Corporate restructuring is carried out through changes in corporate structure and optimization of resources including financial structuring. When the market prices of shares are rising, the companies like to use their shares to acquire other companies. Acquisition is a process of taking over companies and merging with the entity in order to improve the margin. Here the advisors of the company may suggest and encourage mergers after taking over the other company. Demerger is a process of corporate restructuring in which single or multiple business units are spun off as a new entity. Demerger is just the opposite of merger. In a market of falling prices, mergers and initial public offers are less popular and the merchant banks, who normally earn their fees from corporate activity, start to look at demerger possibilities of their clients. In this modern "winners take all"economy, companies have to take a timely responsive action to save their organizations. At this point of time, company executives may ask whether it is time to restructure the company. However, before considering any action, they must first answer the questions: "Will restructuring work?" and "When does restructuring improve economic performance?

The general framework for corporate restructuring and reorganization consists of the following:

1) Reorganisation of assets.
a) Acquisitions
b) Sell-offs or divestitures

2) Creating new ownership relationships.
a) Spin-offs
b) Split-ups
c) Equity carve-outs

3) Reorganising financial claims.
a) Exchange offers
b) Dual-class recapitalisations
c) Leverage recapitalisations (bankruptcy)
d) Financial reorganisation
e) Liquidation

4) Corporate Strategies.
a) Joint ventures
b) ESOPs and MLPs
c) Going-private transactions (LBOs)
d) Using international markets
e) Share repurchase programs.

When one company purchases another company and clearly establishes itself as the new owner, the purchase is called an acquisition. Divestiture, on the other hand, involves sale of a unit or a segment of company to a third party. The company's assets, product lines, subsidiaries or divisions are sold for cash or securities or a combination of these. In spin-offs, a company distributes all its shares in a subsidiary to their shareholders on a pro rata basis. As a result, a new public corporation is formed with the same ownership pattern as that of the parent organisation. There is no money exchange and revaluation of subsidiary's assets. The transaction is treated as a stock dividend and a tax-free exchange. On the other hand, in a split-up, two or more new companies are formed in place of the parent company. The parent company is liquidated after exchanging the stocks of two or more subsidiary companies for all the parent company's stock. They are usually a result of spin-offs. In equity carve-outs, some of the shares of a subsidiary are offered for sale to the general public as a means to generate cash for the parent organisation without losing its control. In split offs, the parent company issues its subsidiary's shares to the parent company's shareholders in return for a specified number of parent company's shares.

Capital structure and leverage decisions represent potentials for value enhancement, for acquiring other firms or to defend against being acquired by others. Leverage recapitalisation involves a relatively large issue of debt that is used for the payment of a relatively large cash dividend to non-management shareholders or for the repurchase of common shares, or a combination of both, thereby increasing the ownership share of the management. On the other hand, in a dual-class stock recapitalisation, firms establishes a second class of common stock that has limited voting rights but usually with a preferential claim to the firm's cash flows. An exchange offer provides one or more classes of securities, the right or option to exchange part or their entire holding for a different class of securities of the firm. Financial reengineering is used by the firms to limit their financial exposure and also to facilitate merger transactions. If the firm is worth more "dead than alive", creditors will force the firm to liquidate. In liquidation, the firm can be sold in parts or as a whole for an amount that exceeds the pre- liquidation market values of the firms' securities. Voluntary liquidations are used when there is a threat of a "bust-up" takeover.

Joint ventures are used to acquire complementary technological or management resources at lower cost, or to benefit from economies of scale, critical mass and learning curve effect. They are often used to provide countervailing power among rivals in a product market and among rivals for a scarce resource. Employee Stock Ownership Plan (ESOP) is a type of stock bonus plan that invests primarily in the securities of the sponsoring employer firm. They are designed to promote employee stock ownership and to facilitate raising of capital by employers. On the other hand, Master Limited Partnership (MLP) is a type of limited partnership whose shares are traded publicly. The limited partnership interests are divided into units that trade as shares of common stock. MLPs offer investors liquidity via an organised secondary market for trading of partnership interests. Both ESOPs and MLPs have tax advantage and both have been involved in takeover and takeover defence activities. Going private refers to the transformation of a public corporation into a privately held firm. A Leverage Buyout (LBO) is a general form of restructuring wherein the managers, with the help of some outside agencies, replace the public stockholdings with closely held equity. Sometimes, the stocks and assets are purchased by a small group of investors especially buyout specialists or investment bankers or commercial bankers. Usually, the incumbent management is included in the buying group. The buyout process varies with few managers preferring the acquisition of the entire company, while few preferring the acquisition of a division or subsidiary. When the company's key executives are involved in the buyout process, it is termed management buyouts (MBOs). Share repurchase program generally deals with the cash offers for outstanding shares of common stock thereby helping in changing the capital structure of the firm. It also helps in reducing the common stock so that the debt/equity ratio or leverage ratio is increased. There are four major types of share repurchase programs – Fixed Price Tender Offers (FPTs), Dutch Auctions (DAs), Transferable Put Rights (TPRs) and Open Market Repurchases (OMRs).

The selection of the restructuring initiative varies with the type of organisation, the management and the challenges faced by the organisation. However, generally, specialists distinguish three modes of restructuring – Portfolio Restructuring, Financial Restructuring and Organisational Restructuring.

Portfolio Restructuring:
It involves changes in the asset mix of the organisation, i.e. addition or disposal of assets from the organisation's business. It includes acquisitions, asset sales, divestitures, liquidations, spin-offs or a combination thereof. It is cited that spin-offs generate higher performance gains than sell-offs and acquisitions and divestitures. Better strategic focus, strong control of multiple business units and superior economies of scope can be the intermediate effects of portfolio restructuring.

Financial Restructuring:
It involves changes in the capital structure of an organisation which includes leveraged buyouts, leveraged recapitalisation and debt for equity swaps. The largest returns in financial restructuring come from leveraged and management buyouts. Increased emphasis on cash flows and changes in managerial incentives can be the intermediate effects of financial restructuring.

Organisational Restructuring:
It involves changes in the organisational structure which include divisional redesign, reducing the hierarchical level, reduction in product diversification, compensation revision, improving governance and workforce reductions. However, it is more dependent upon the circumstances in which it is initiated and has the least impact on performance. An increase in operating efficiencies, greater employee satisfaction, reduced turnovers and better communications can be the intermediate effects of an organisational restructuring.

These intermediate effects, directly or indirectly, influence the financial performance of the organisation. However, this ultimate effect might be visible within a few years or might take a longer time period. To measure the impact of restructuring, the organisation can study the impact on market performance through the movement in the organisation's stock prices after the announcement of the restructuring or through the impact on accounting performance by analysing the changes in earnings (like return on equity and return on investment) before and after the restructuring.

Restructuring of Reliance Industries Limited (RIL)
Background
There were various corporate restructurings in India during the last few years. However, this paper deals with successful corporate restructuring of one Indian company which immensely enhanced the shareholders' market value and strengthened their competitive edge in recent times i.e Reliance Industries Limited (RIL).For example, the acquisition, merger, and demerger of Reliance Industries Ltd. like their acquisition of IPCL mergers of Reliance Petrochemicals Ltd., and the recent demergers of four entities like Reliance Communication Ventures Ltd., Reliance Energy Ventures Ltd., Reliance Natural Resources Ventures Ltd., and Reliance Capital Ventures Ltd. which spun off from Reliance Industries Ltd. (RIL), and were perhaps the most prominent restructurings in recent times.RIL entered into the telecom segment in the year 2000. The company also submitted open offers to take control of BSES stocks and took over BSES in 2002. It also planned to merge its finance company with another subsidiary Reliance Petrochemicals Ltd. (RPL). In March 2002, RPL merged with RIL. In the same year, RIL bagged a 25 percent share of IPCL. On July 6, 2002 the great Reliance patriarch Dhirubhai Ambani passed away.Mukesh Ambani, elder son of Dhirubhai Ambani, was elected as chairman of RIL on July 31st 2002. RIL diversified further into the areas of biotech, life sciences, mining, and insurance.

Reliance Empire Split

RIL, one of India's largest private sectors groups, was split in June 2005 due to differences between two successor brothers. The RIL struggle was not only a clash of egos between estranged brothers, but it was also about big money in the area of Rs.1000 billion which was not easy to share. Also not easy to understand were the complexities involved in running such an empire with two power centers. On January 17th 2006, a unique trading and investment era was over. As per the demerger approved by RIL board in August 2005, both brothers, Mukesh and Anil – headed different businesses and five listed companies emerged as potential investment opportunities for investors by March 2006. Among the group companies of RIL, Reliance Energy and Reliance Capital, were already listed at the exchanges. The remaining four companies were listed by the end of March 2006.

New Structure

The new RIL structure gave Mukesh complete independent control in the business of oil exploration, refining, petrochemicals, and textile businesses through a stand alone entity in RIL along with IPCL. His shares also included biotech firm Reliance Life Sciences and Trevira, a company in Europe which manufactures polyester fibers. Anil got control over power, communication, and financial businesses through four companies which came under Anil Dhirubhai Ambani Enterprise (ADAE) as part of the Reliance group. These four companies were named as Reliance Capital Ventures Ltd. (proposed to be merged with another listed company Reliance Capital Ltd.), Reliance Energy Ventures Ltd. (proposed to be merged with existing company Reliance Energy Ltd.), Reliance Communication Ventures Ltd.(these include both Reliance Infocomm and Reliance Telecom) and Reliance Natural Resources Ltd. (which includes businesses in gas based energy undertakings).

Outcome of Demerger

After the demerger, share prices of the listed five companies were quoted differently at the Bombay Stock Exchange and National Stock Exchange. Prior to the demerger, RIL's share was traded around Rs 978 per share, but after the demerger the combined demerged share values of five companies came to around Rs. 1235. This is a gain of almost 26 percent for every shareholder. This overall gain has to be seen from long-term perspectives when the demerged entities will be further merged with the running businesses of Reliance.

Suggestions

Corporate restructuring in a developing country like India is potentially one of the most challenging tasks faced by economic policymakers. The Following Measures will help to alleviate the problems of Corporate Restructuring in India

- The federal structure of India with hostile political environment makes it inevitable for government and leadership to take lead in establishing restructuring priorities, addressing market failures, reforming the legal and tax systems especially in the wake of financial crises when corporate distress is pervasive.
- Corporate governance must be brought up to international standards to provide incentives for viable firms to restructure their balance sheets and maximize their value.
- A supportive legal, regulatory, and accounting environment is to be created for successful corporate restructuring. Important legal aspects of restructuring include foreclosure standards, foreign investment rules and mergers and acquisition policies.
- Restructuring should be based on a holistic and transparent strategy encompassing corporate and financial restructuring.
- Restructuring planning should include conducting proper due diligence, effective communication during the integration, committed and competent leadership; speed with which the integration plan is integrated facilitates the success of Corporate Restructuring.
- Effective measures should be taken quickly to offset the social costs of crises and restructuring. Government should be prepared to take on a large role as soon as a crisis is judged to be systemic.
- Prior to Restructuring, it is necessary not only to analyze the financial aspects of the acquiring firm but also the cultural and people issues of both the concerns for proper post-acquisition integration.

Conclusion

Corporate Restructuring has become very popular over the years especially during the last two decades owing to rapid changes that have taken place in the business environment. Business firms now have to face increased competition not only from firms within the country but also from international business giants thanks to globalization, liberalization, technological changes, etc. Generally the objective of Corporate Restructuring is wealth maximization of shareholders by seeking gains in terms of synergy, economies of scale, better financial and marketing advantages, diversification and reduced earnings volatility, improved inventory management, increase in domestic market share and also to capture fast growing international markets abroad. But astonishingly, though the number and value of Corporate Restructuring are growing rapidly, the results of the studies on the impact of mergers on the performance from the acquirers' shareholders perspective have been highly disappointing. Making the restructuring work successfully is not that easy as here we are not only just putting the two organizations together but also integrating people of two organizations with different cultures, attitudes and mindsets. Meticulous restructuring planning including conducting proper due diligence, effective communication during the integration, committed and competent leadership, speed with which the integration plan is integrated all this pave for the success of Corporate Restructuring. While making the Restructuring deals, it is necessary not only to make analysis of the financial aspects of the acquiring firm but also the cultural and people issues of both the concerns for proper post-acquisition integration.

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