
Growth Strategies during Recession through Acquisition

(A Case Study of McLeod Russel India Limited)

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Abstract:

In last few years, the strategy adopted by McLeod Russel (India) Ltd. to grow through acquisitions. This company has become the largest tea plantation company in world through successful acquisitions. For further growth and to mitigate the risk of market it is expanding its horizons in new international market. This paper analyzes McLeod Russel (India) Ltd. strategy to grow and then finds how this strategy helped the company to grow even during the phase of economic slowdown.

Introduction:

Companies, facing economic slowdown, should develop and implement aggressive growth strategies in their core business areas if they are to build solid foundations that will propel them ahead of competitors over the next few years. A thoughtful, managed risk strategy is essential to survive and enjoy the rewards after the recession. Investment in core business is especially valuable when the market is down and competitors, fearful of investing in uncertain times, bury their heads to weather the storm. Amongst the companies that emerge from the downturn, the strongest will be those that use this time of uncertainty to their advantage. They will improve market position through targeted investment in their core business either by adding capacity or capability. They will spend on bargain acquisitions to gain market share and take leadership positions. They will also avoid diversification, because it dilutes focus on strengthening the core business.

By being proactive and remaining focused on their core business they will outperform hesitant and struggling competitors. During this recession period some of the companies were planning for future economic revival. These companies were busy in

adding capacities by acquiring companies which were available at deep discounts to their fair market value. Merger is a transaction where two firms agree to integrate their operations on a relatively equal basis because they have resources and capabilities that together may create a stronger competitive advantage. Acquisition is a transaction where one firm buys another firm with the intent of more effectively using a core competence by making the acquired firm a subsidiary or merging it within its portfolio of businesses.

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Motives behind mergers & acquisitions

- **Manufacturing synergy:** It involves combining the core competencies of the acquirer company and target company in different areas of manufacturing, technology, design and development, procurement etc. It could also mean rationalizing usage of the combined manufacturing capacities. **Ex: Mahindra and Mahindra acquired Jiangling Motors of China:** Objective was to combine M&M design and development strength with low cost manufacturing capabilities of Jiangling. **Tata Motors acquisition of Daewoo's commercial vehicles unit:** Objective was to gain advantage of producing commercial in the 200-400 bhp range. **Daiichi Sankyo and Ranbaxy:** R & D strength of Daiichi being combined with the efficient manufacturing of Ranbaxy.
- **Operations synergy:** It involves rationalizing the combined operations in such a manner that through sharing of facilities such as warehouse, transportation, software and common services such as Accounts and Finance, Tax, HR, Administration etc. duplication is avoided. **Ex: Kingfisher Airlines and Jet Airways acquired Deccan Airways and Sahara Airline.** Objective was to achieve substantial savings through operations synergies such as rationalization of routes, reduction in the combined number of flights on the same routes, sharing of commercial and ground handling staff, reduction in the combined number of airplanes in use. **Oriental bank of Commerce takeover of Global Trust bank:** Operation synergy arose from the fact that OBC had strong branch network in the north but had not explored the western and southern part of India where GTB has a strong network and franchise. **Videsh Sanchar nigram Limited acquired Tyco.**
- **Marketing synergy:** It involves using either the common sales force or distribution channel or media to push the products and brands of both the acquirer and target companies at lower costs than the sum total of costs that they would incur in independent marketing operations. It also involves leveraging on the brand equity of one of the two companies to push the sale of the other

company's products. **Ex: Hindustan lever Limited (HLL) acquired Lakme's brand and business:** Objective was to use its vast distribution network to leverage on the strong brand equity of lakme in the women's cosmetics business. **Dilip piramal acquired Universal Luggage:** objective was to use the common distribution channel and sales force to push both the companies' products which were targeted at the same market segments except for pricing differences and thereby effect a substantial savings in sales force and other marketing costs.

- **Financial synergy:** It involves combining both the acquirer and target companies' balance sheets to achieve either a reduction in the weighted average cost of capital or a better gearing ratio or other improved financial parameters. **Ex: Merger of Reliance Petrochemicals Limited with Reliance Industries Limited and Merger of Reliance Polyethylene Limited with Reliance Polypropylene Limited**
- **Tax synergy:** It involves merging a loss making company with a profitable one so that the profitable company can get tax benefits by writing off accumulated losses of the loss making company against the

McLeod Russel (India) Ltd.

McLeod Russel has been growing tea in India since 1869. McLeod Russel is the world's largest tea plantation company accounting for 8% of India's total tea production and 2% of the world's tea production.

The company owns 55 high quality tea estates spread across 34,000 hectares in Assam and West Bengal. McLeod is able to maintain superior quality and higher yield rates through its replantation policy where in it replants 2% of its bushes every year. Every year they produce over 80 million kilograms of black tea, which is marketed worldwide under the registered Elephant trade mark.

A Brief history

1869 - McLeod Russel has been growing tea in India since 1869. In the beginning, Captain J.H. Williamson and Richard Boycott Magor, two Englishmen based in

Calcutta, formed a partnership firm, Williamson Magor & Company, to service the requirements of tea gardens in Assam.

1954 - It was renamed as Williamson Magor & Co Limited, with the change in its status to a limited company.

1975 - Williamson Magor merged with another company, Macneill and Barry Ltd. The new company was named Macneill and Magor Limited.

1987 - Guthrie family in the UK sold their shareholding in the McLeod Russel group, which included the Makum and Namdang Tea Companies to the Khaitan family, making the Macneill and Magor group.

1992 - Macneill and Magor Limited were renamed Williamson Magor & Co. Limited.

1994 - The group bought 51% of the equity shareholding of Union Carbide India Limited, through McLeod Russel India Limited, and the company was renamed Eveready Industries India Limited. The new company had two divisions, the bulk tea division which managed the tea estates of McLeod Russel and the battery division which marketed the popular Eveready batteries and flashlights.

1998 - The company was originally incorporated as a private limited company on May 5, 1998. **2000** - It became a deemed public limited company on July 6, 2000.

2004 - In April, 2004 Eveready Industries demerged the two divisions into two separate companies, McLeod Russel India Limited and Eveready Industries India Limited. This enabled McLeod Russel to concentrate on its core business of tea production. Eveready, with the second largest retail distribution network in India, enjoys more than 50% market share in their battery and flashlight business.

Major acquisitions by McLeod Russel India Ltd

2005 - In July 2005, the company acquired Borelli Tea Holdings Limited from the Magor family based in England and took over the 17 tea gardens of its Indian subsidiary Williamson Tea Assam Ltd (WTAL). After this acquisition the company became the world's

largest integrated bulk tea company with a production of 62 million kg. For this acquisition company issued 4, 25, 25,000 equity shares of Rs.5 each fully paid up ranking pari paasu with the existing shareholders to the shareholders of WTAL in the ratio of 3 equity shares of the company of Rs. 5 each for every 1 equity share of Rs. 10 fully paid up held in WTAL.

2006 - The company acquired the Doom Dooma Tea Company at a total cost of Rs. 69 crore plus net current assets. Doom Dooma owns seven tea estates in Tinsukia district of Assam with a plantation area of 3,100 hectares and three factories to process tea. The average output from these estates has been approximately 6,000 tonnes. This acquisition of Doom Dooma Company brought in more synergy benefits to MRIL and helped the company to realize better prices for its teas both in domestic and overseas markets.

2007 - McLeod Russel India acquired Moran Tea Company India from Moran Holding Plc for Rs 41.49 crore, consolidating its position as the world's largest tea plantation company. The company paid Rs. 273 for each of the 1,520,000 shares of Moran Tea it acquired from Moran Holding. The shares had a face value of Rs 10.

2008 - McLeod Russel acquired Vietnam-based Phu Ben Tea Company, for about \$7 million. The acquisition increased the tea annual production by the company to 80 million kgs, from about 76 million kgs. The tea produced in Vietnam was for export purposes, as it attracted 100 per cent import duty, if sold in India. Phu Ben owns about 1,000 hectares of land for tea plantation in Vietnam, and has three processing factories in the country as well.

2009 - McLeod Russel India has acquired Uganda's Rwenzori Tea Investments for \$25 million (Rs 117 crore), taking its total annual tea production to 96 million kg. The acquisition is being carried out through Borelli Tea Holdings Ltd of the UK, which is a wholly-owned subsidiary of McLeod Russel India. Rwenzori holds 100 per cent of the equity capital of James Finlay (Uganda) Ltd, or JFUL. The company is engaged in growing, processing and marketing of black tea. It has six estates with annual production of around 15 million kg of black tea. This acquisition would give the company a presence in Uganda, which could lead to possible expansion of production.

Total acquisitions

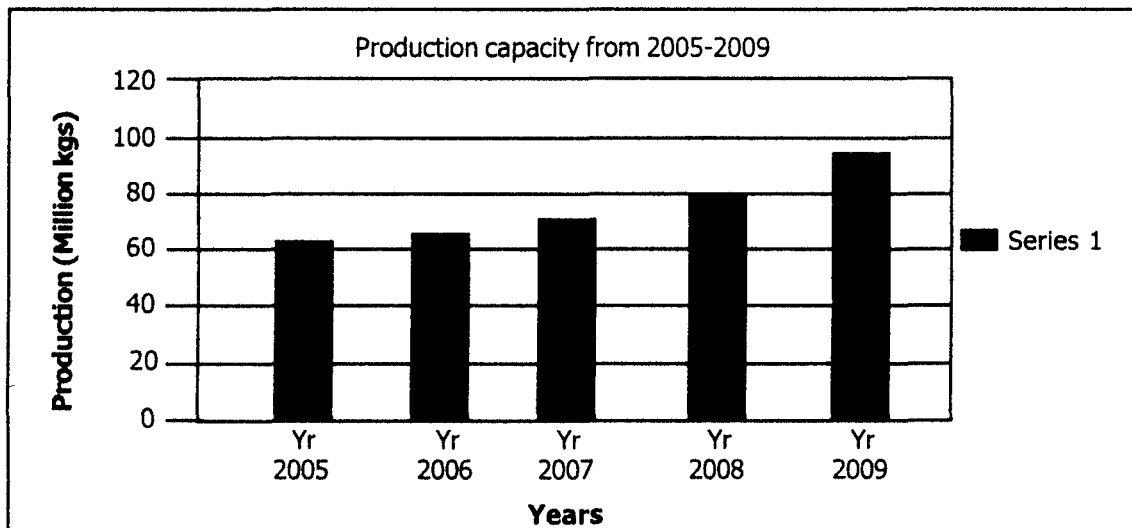
S.No.	Year	Name of the acquired company / country
1.	2005	Borelli Tea Holdings Limited/ India
2.	2006	Doom Dooma Tea Company Limited/ India
3.	2007	Moran Tea Company India Limited / India
4.	2008	Phu Ben Tea Company Limited/ international
5.	2009	Rwenzori Tea Investments Limited/ international

Impact of Acquisitions on company's performance

1. Production capacity

S.No.	Year	Production capacity
1.	2005	62 million kgs
2.	2006	69 million kgs
3.	2007	75 million kgs
4.	2008	80 million kgs
5.	2009	96 million kgs

Source: www.mcleodrusselindia.com



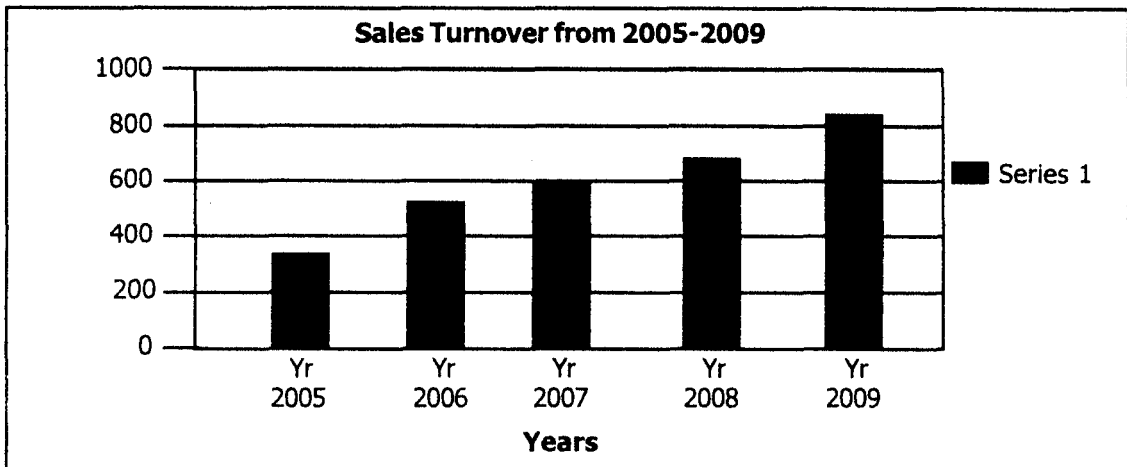
We can see that after acquisition in 2005, company's production capacity increased from 62 million kgs to

96 kgs i.e. 54.84% up to 2009.

2. Sales Turnover

S.No.	Year	Sales Turnover (Rs. In Crores)
1.	2005	322.53
2.	2006	513.70
3.	2007	608.31
4.	2008	667.58
5.	2009	830.83

Source: <http://www.moneycontrol.com/financials/mcleodrusselindia/profit-loss/MRI02>



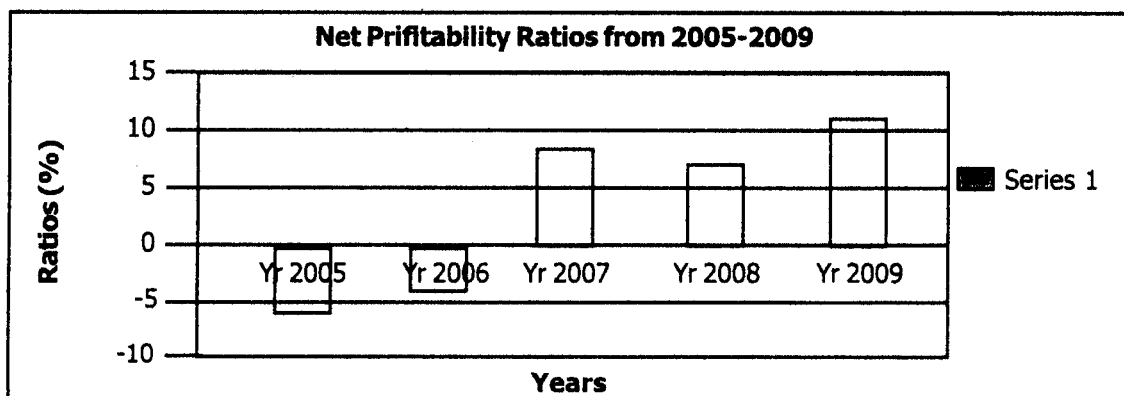
We can see that after acquisition in 2005, company's sales turnover increased from Rs.322.53 crores to

Rs. 830.83 crore i.e. 157.60% more than double up to 2009.

3. Net Profitability Ratios

S.No.	Year	Net Profitability Ratio
1.	2005	(6.00)
2.	2006	(4.43)
3.	2007	7.63
4.	2008	7.06
5.	2009	10.62

Source: <http://www.moneycontrol.com/financials/mcleodrusselindia/ratios/MRI02>

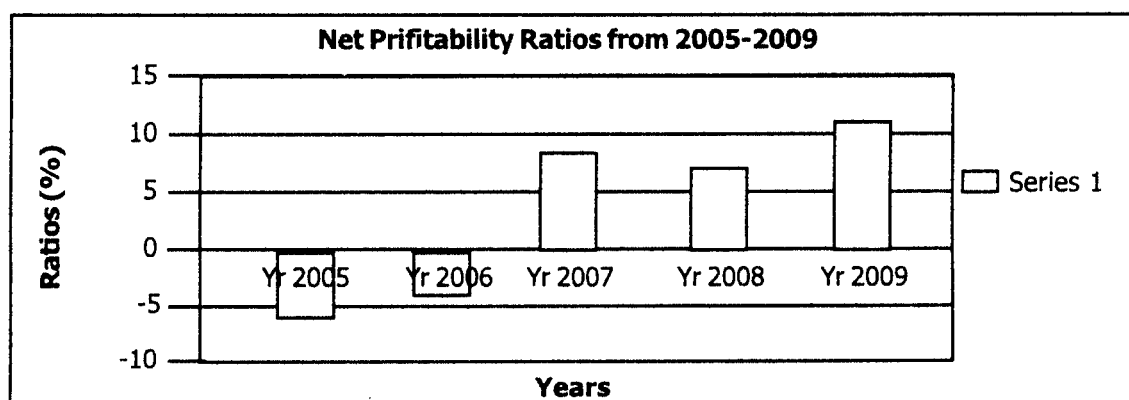


We can see that after acquisition in 2005, company's net profitability ratio increased from -6% to 10.62% i.e. 277% up to 2009.

4. Return on Capital Employed (%)

S.No.	Year	Return On Capital Employed (%)
1.	2005	0.74
2.	2006	1.03
3.	2007	7.47
4.	2008	5.77
5.	2009	16.26

Source: <http://www.moneycontrol.com/financials/mcleodrusselindia/ratios/MRI02>



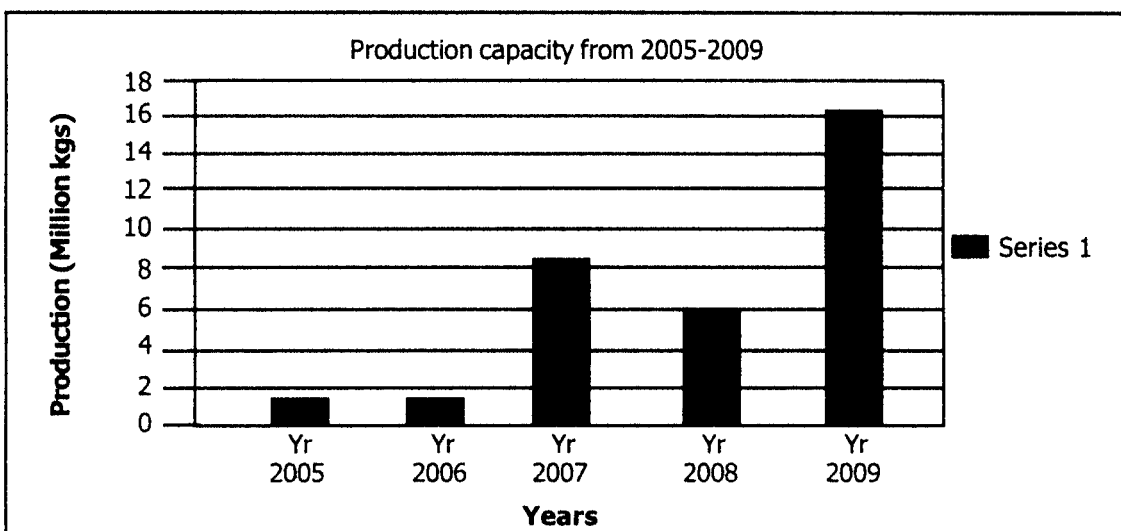
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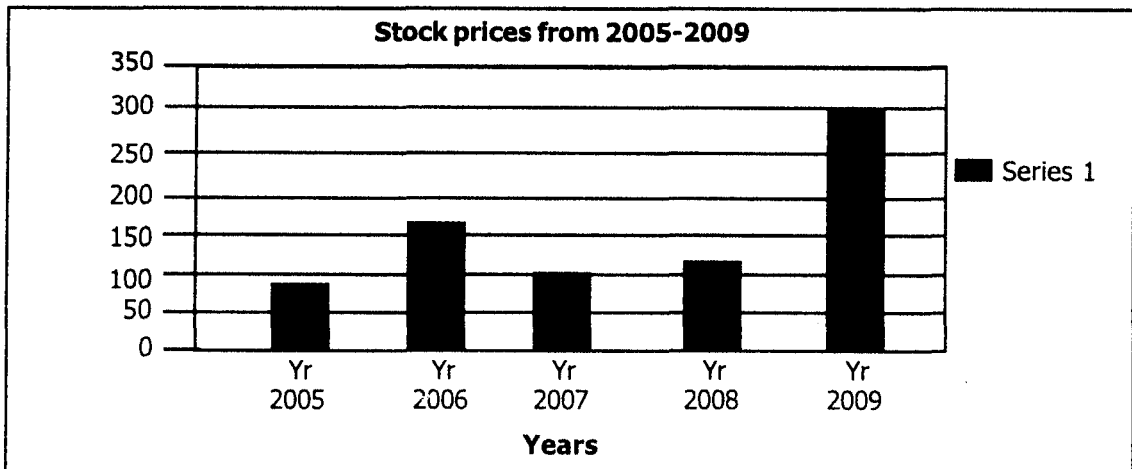
After acquisition in 2005, company's Return On Capital Employed ratio increased from -.74% to 16.26% i.e.

more than 21 times up to 2009. The fruits of acquiring companies can be seen during the performance of last financial year

5. Stock prices

S. No.	Year	Stock price (High price)
1.	2005	92.50
2.	2006	160.45
3.	2007	102.45
4.	2008	118.70
5.	2009	287

Source : <http://www.moneycontrol.com/stocks>



After acquisition in 2005, company's market price per share increased from 92.50 to 287 i.e. more than double up to 2009.

Comparison with peers

S. No.	Company name	Net sales (Rs. in Cr.)	Net profit (Rs. in Cr.)	Market capitalization (Rs. in Cr.)
1.	Tata Tea Ltd.	1,361.53	159.06	5,643.51
2.	McLeod Russel India Ltd.	828.50	88.79	2,509.27
3.	Gillanders Arbuthnot & Co. Ltd.	473.09	16.56	198.27
4.	Jayshree Tea & Industries Ltd.	417.67	13.88	360.43
5.	Goodricke Group Ltd.	293.95	17.59	300.24

Source: <http://www.moneycontrol.com/stocks/marketinfo/marketcap.php?indcode=Plantations - Tea & Coffee&optex=BSE>

If we compare the performance of the company with its peers then also company stood at IInd position in terms of total turnover, profits and market

capitalization. Tata tea stood at number one after successful acquisition of Tetaly in UK

Conclusion: Expansion in the domestic market and export market can be achieved through the strategy of acquisition. In some cases, this merging of firms leaves both entities in a better position, proving that 1 + 1 can sometimes equal 3. Mcleod Russel India Ltd. has a proven track record in this strategic process. The company achieved its position as number one

tea Plantation Company in the world by acquiring companies. During the slowdown in tea industry the company was busy in adding capacity through acquisitions and when the economic conditions improved the company was able to reap the benefit of the strategy.