3.
Alternate deal structures and private equity

For many corporates, divestiture used to mean just one thing – the outright sale of a company or division. But corporates in Asia Pacific are increasingly taking a more sophisticated approach to divestiture and considering a range of options when a business's place in a portfolio is no longer secure. Among these options are joint ventures (JVs), partnerships, and alliances. In fact, in our portfolio rebalancing survey, the number of organisations considering the use of JVs as an exit route has increased significantly, from 47% in 2022 to 96%; for partnerships it rose from 64% to 96%; and for strategic alliances it climbed from 67% to 95%.

It seems that corporates are increasingly alive to the idea that different structures can help them achieve different objectives more effectively than a one-size-fits-all, complete divestment. They recognise that there can be merits in retaining a stake in businesses that may have become non-core but for which there remains an enduring interest or strategic relevance, or bringing in outside capital to fund growth in a business division needing investment but for which internal funding is not available.

Simply put, divestiture comes in many forms, and rather than defaulting to a sale, it should be a company's strategic objectives that drive the divestiture approach and structure.

For example, if a corporate wants or needs to unlock capital to put to work elsewhere in the business, an outright sale of a non-core asset may be the best option. But, if it is looking to inject capital, leverage new relationships, or reinvigorate management, a JV might be a better option. If the goal is to add new or complimentary offerings, a partnership may be right, but if the goal is to reduce geopolitical exposure or simplify the global footprint, it may be worth exploring a structural separation with a partial sale that prepares the business for potential full separation, but which retains desired exposure to growth and profits.

Different structures, different partners

Critically, when corporate divestors start looking at alternatives to outright exits, they also unlock a different buyer or investor universe, one in which private capital – be it from private equity, pension funds, or sovereign wealth funds – can be especially attractive, both for financing and operational support to help achieve corporate objectives.

The scale and diversity of private capital – different investment models, rules and timeframes – mean that divestors have the opportunity to find the best-fit partner in any set of circumstances. For example:

- A sovereign wealth fund that does not have a limited investment horizon might be a good solution if long-term stability in ownership is key
- Local or regional private equity funds would be beneficial if local relationships or management are important, or where insulating the asset from geopolitical tensions is desirable
- A specialist fund or one with substantial investment track record in the industry could make sense if specific industry knowledge or network is required.

Ignoring or excluding private capital will limit a divestor's options, potentially impacting competitive tension in a sale process as well as valuation. In our survey, some respondents reported that a failure to include private equity bidders in the sale process had been a contributing factor in them achieving a lower-than-expected value.

Why private capital now?

A combination of circumstances mean that private capital is in the spotlight in Asia Pacific, perhaps as never before, and particularly for corporates with an eye on divestiture. From corporates' perspective, a range of factors including geopolitical crises, the high cost of capital, and localisation or competition from local brands as Asian markets mature are leading companies to review their portfolios and consider strategies to rebalance.

At the same time, the demand for investment opportunities for private capital has rarely been higher. In fact, corporate divestiture as a percentage of all private equity buyouts has reached a five-year high within Asia Pacific (and globally).[4] With sponsor-backed sale volumes down, private funds have accumulated record levels of dry powder – estimated at around US$630 billion[5] in Asia alone – and are under pressure to deploy it. Opportunity-hungry funds have a growing interest in corporate divestiture, recognising that their financial, operational, and managerial focus make them potentially ideal standalone owners for businesses that are unloved – non-core or under-resourced – by their corporate owners. They may also have local knowledge and relationships in market that enable them to achieve growth in ways that would be more difficult as part of a larger multi-national. A good example of this strategy – leveraging local partners to manage brands in different geographies – is Restaurant Brands International (Burger King, Tim Hortons, and Popeyes), which has partnered with nearly a dozen private equity funds to grow its brands in different parts of Asia.

Private capital can be a great partner

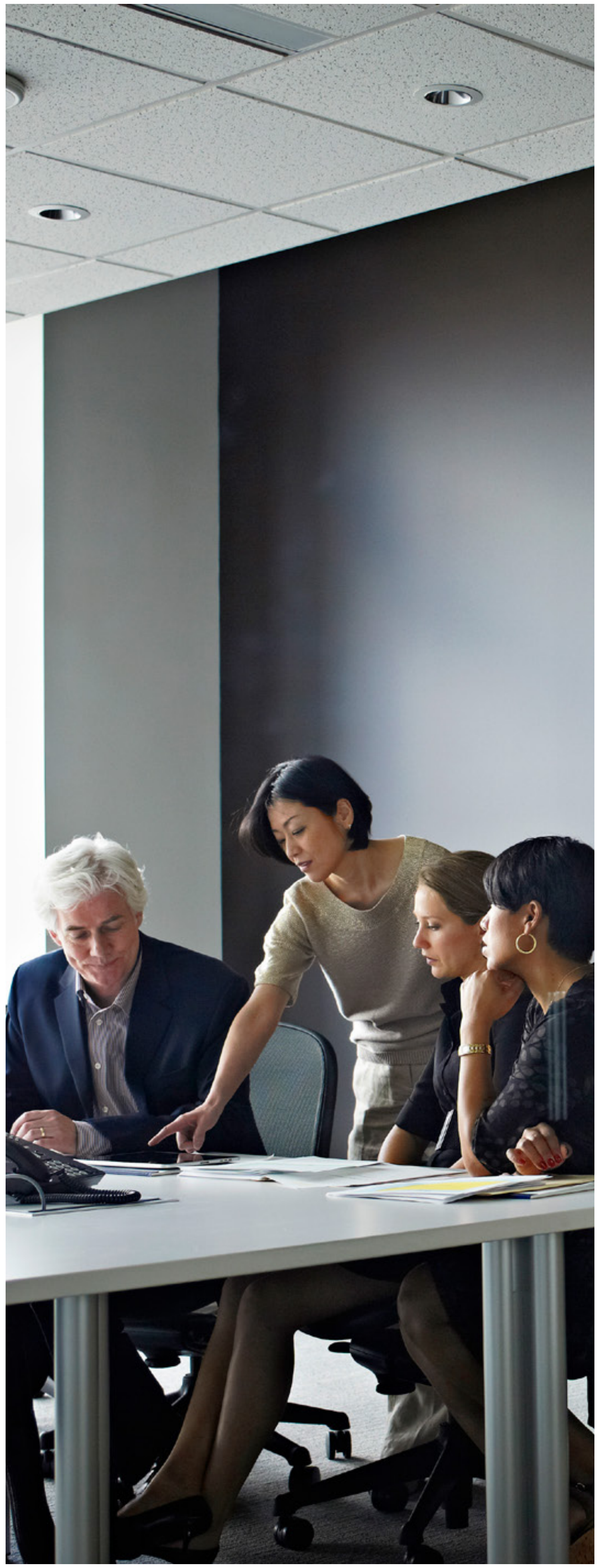
Depending on the company's reasons for divesting – and its timeframe – private capital can be a great partner for portfolio rebalancing, offering a number of potential advantages over corporate buyers:

- **Flexibility:** one of the immediate advantages of working with sources of private capital is that financial investors, depending on their own rules, can do things that corporate entities cannot; they can be more creative and work within a wider range of potential structures, giving the seller a broader set of options to achieve their goals. While these might still include a conventional whole sale, they can also include JVs and partnerships, partial sales and contingent sales, giving divesting companies options to 'retain a say' post-transaction through, for example, call options or the right of first offer to buy the asset back, restrictions on potential buyers (white list or black list), or limitations on brand or IP use.
- **Domain and regional expertise:** financial investors may have experience through current or past portfolio companies that bring strategic knowledge and deep networks within the industry. They may be able to draw on local expertise and insight to create value, for example by adapting marketing and communication to leverage locally effective channels or tweaking services and products to better-suit local tastes and behaviours. They may also be able to draw on synergies across their global portfolio of investees, such as customers or suppliers, which can be beneficial to the asset in question.
- **Not a competitor:** selling to private capital means the company is not selling to a peer or competitor in this or other markets, potentially adding strategic benefit to the divestment, and avoiding the loss of face that can sometimes accompany a sale to a direct competitor.

Not all divestments are non-core

While divesting is often used as a means of shedding non-core or underperforming operations, it can also be used as a strategy for restructuring or revitalising strong assets and in these cases, private capital can be the ideal solution. Bringing in a partner can mean the asset gets additional and specialist attention that it might lack as a business unit. Equally, a corporate might benefit from structurally separating an asset but retaining some financial upside, giving it the flexibility to make a final decision – sale, IPO or repurchase – at a later date. Partnering with a private fund can solve for a number of unique strategic objectives, for example:

- Investment for rapid growth: If a corporate wants to quickly scale or improve an asset, PE's limited investment timeframe makes for closely aligned goals. This is even more impactful for assets that require significant capital to fund growth. For example, many telecom operators have partnered with financial investors to fund rapid growth in their data centre assets, such as KKR committing S$1.1 billion for a 20% stake in Singtel's regional data centre business (September 2023).[6]
- Turnaround or significant reorganisation: private equity funds specialise in turnarounds, operational improvements, and planning for growth – it is their bread and butter. Companies can effectively outsource these activities to specialists while retaining the option to buy back the asset when it is in better shape. There are numerous cases where private equity fund ownership has substantially improved an asset before it was sold back to the corporate parent, notably: McDonald's buy back of Carlyle's stake in McDonalds China after the fund had overseen a 50% expansion in just five years (November 2023); and, Anheuser-Busch's exercising of its call option on Oriental Brewing five years after private equity funds KKR and Affinity Equity Partners acquired the Korean brewer and drove an 80% increase in revenue, 108% increase in EBITDA and 20% rise in market share (January 2014).[7,8,9]
- Full or partial structural separation: There may also be cases where structurally separating a business from its corporate owners, perhaps to deconsolidate financial reporting or to separate across two geographies, can be a way of protecting or insulating it from potential regulatory or geopolitical risks.



Many early conversations: the way to engage with private capital

Private capital is all about flexibility and agility – identifying opportunities and deriving a strategy to make a significant difference to a business within a specific timeframe. That means financial investors need to be involved early. They will explore potential portfolio company synergies, value creation angles that leverage their operational capabilities and domain expertise, or propose different structuring options to best fit the corporate and their own objectives. It is also important to note that private capital funds vary widely; they each have their own approach and focus – and put a lot of faith in their 'secret sauce'. Preliminary conversations, before any portfolio rebalancing decisions are made, afford the corporate time to assess potential private capital partners and better understand the unique contributions each could bring to the table.

Early engagement with multiple funds is the best way for companies to maximise the chances of finding the right 'fit'. Companies that come to market with a fixed idea of what they are offering have probably missed the boat when it comes to private capital, because financial investors will want to shape the perimeter and scope of the transaction – geographies, products, MSAs, brand licensing, etc. Structuring that makes managing and exiting the investment difficult is unlikely to garner much enthusiasm from funds that need clear visibility of their eventual exit. Equally, if the corporate owners approach the portfolio rebalancing with a narrow set of target buyers in mind – often excluding financial buyers at the outset of a process –they may struggle to get private capital interested later in the process, should strategic buyers not materialise.

Waiting too long to divest, potentially eroding value, can also be a problem for private funds. Asian operations often provide a large portion of growth for global businesses, and this can create a reluctance to divest, even when the assets are underinvested, suffering from slowing growth, facing increased local competition, or lack sufficient localisation to reach their full potential. In these instances, a partial divestment of a strong asset to reinvigorate the local strategy is likely to appeal to a financial investor much more than waiting until the asset is crying out for more attention and starting from a weaker competitive position. Leaving it too long risks not only losing the interest of a potential partner, but also of seeing the asset fetch a lower valuation as the potential to achieve significant gains dwindles.

Deal or no deal, conversations add value

Early and confidential dialogue with selected funds through a trusted advisor is a good way to gauge interest and explore potential deal parameters before making any decisions; understanding what is possible, and perhaps uncovering unique opportunities and angles that would not be discovered without those conversations. If the right 'fit' in terms of deal structure, culture and timings, is identified, companies can then rapidly progress to bilateral discussions, saving the time, resources, and pressure associated with running a sale process with multiple participants.

It is also true that any financial investor interested in a particular divestment is likely to be already active in that industry. Establishing a relationship with them, even if it does not lead to a deal immediately, may still benefit the corporate's business development function in the future, for example to explore JV, partnership and alliance opportunities with a fund's portfolio companies.

In our survey, 50% of respondents indicated that a domestic private equity was a typical buyer for businesses divested in the last two years, and for 22% it was a cross-border PE. There can be little doubt that private equity will play a significant and growing role in Asia Pacific portfolio rebalancings in the next few years. Corporates that fail to adapt their portfolio rebalancing strategies to engage a different class of buyer or to consider different types of divestments are effectively turning their backs on the most active, agile buyers in the market.