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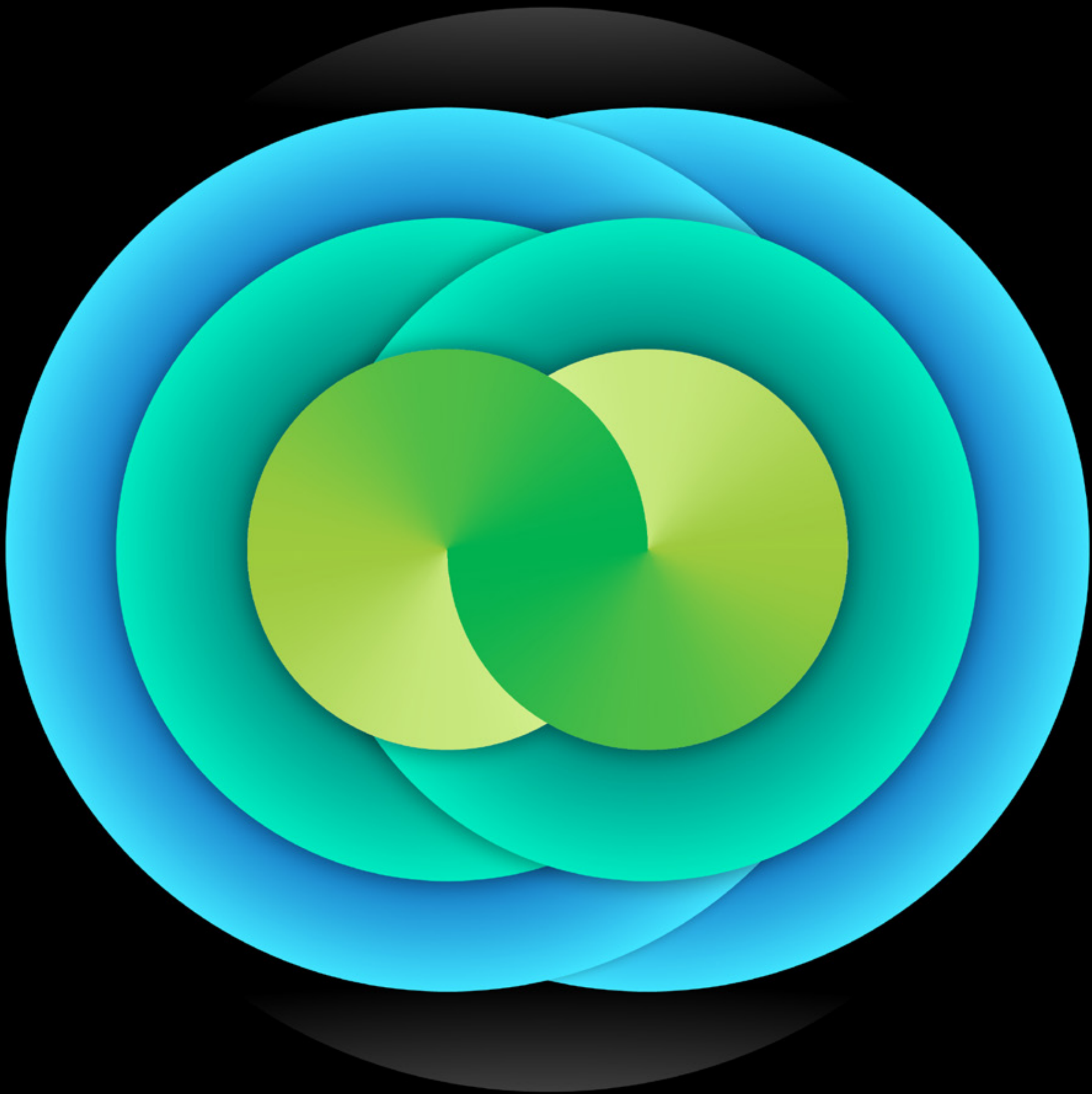


Rebalancing your portfolio to fuel growth

July 2024

Contents

Insight in brief

In the post-COVID economy, across the Asia Pacific region, many companies across all industry sectors are facing an urgent need to intensify their scrutiny of portfolio holdings and future capital allocation strategies, as they seek to rebalance, look for growth opportunities and divest assets that no longer fit. Alongside evolving strategic goals and the relentless, and sometimes disruptive, march of technology, this need to rebalance is driven by five powerful forces:

1. **Navigating geo-political tension** causing dislocation of marketplaces, supply chains and trade partners.
2. **Capital efficiency regulation** (Japan, Korea and likely the rest of Asia) forcing companies to disclose if capital returns are below threshold.
3. **The rise of investor activism** in Asia putting pressure on companies to address underperforming assets and divest non-core businesses.
4. **ESG and the road to net zero** triggering Boards and Executives to undertake deals and divestments to transition to a 'green portfolio'.
5. **Private equity's increasing role as an investor and potential partner** in asset portfolio optimisation choices.

We have seen these forces intensifying over the last few years and wanted to quantify their influence on business opinion and behaviour in Asia Pacific. For this reason, we conducted a survey of 250 executives across Asia Pacific representing private or public companies, most with revenues in excess of US$1 billion.[1]

The survey found that active portfolio management plays an increasingly important role in the way that executives and boards are adjusting to the forces outlined above. Our report strongly advocates a move towards an active portfolio management mindset, and the development of two key qualities: *resilience* – to protect companies from the negative impacts of these forces; and *transformative growth* – to be able to capitalise on growth opportunities and synergies as and when they arise.

These portfolio reviews often lead to companies shedding assets to release growth capital and increasingly focus on their cores. Our survey found that almost four in five (79%) executives are expecting to make two or more divestments in the next 18 months. Interestingly, the feedback from the surveyed executives also found that most (95%) have abandoned a sale in the last 12 months, suggesting a need to do more to be divestment ready.

1

Chapter 1
Active portfolio management and capital efficiency

To be truly agile and able to respond to the above external forces, companies should be moving to an 'always-on' mindset when it comes to portfolio review, dedicating resources and board-level bandwidth to ensuring that assets are aligned with the overall strategic direction. And, where they are not, being willing and able to move quickly to divest or engage with partners who can create value.

Our portfolio rebalancing survey reveals that 59% of corporates are now assessing their portfolio performance at least twice a year, up from 46% in 2022. While this is an encouraging development, active portfolio management is a continuous process, so we have provided an initial roadmap to help company leaders frame their approach and build their capacity to achieve transformational growth while remaining resilient.

2

Chapter 2
Protect value by being divestment ready

With so much attention now focused on portfolio rebalancing, it is increasingly important to understand how to both preserve and maximise the value achieved from any asset deemed to be a poor fit. Essentially, this boils down to planning and preparation. Value can be eroded at any and every stage of the portfolio rebalancing process and once it has gone, it is very hard to claw it back.

Our survey found that deal-ready sellers – those that are ready and able to move fast – are three times more likely to exceed deal-value expectations. Respondents also said that developing a compelling value story and track record for the asset would be one of their top priorities if they could revisit their most recent transaction.

3

Chapter 3
Alternate deal structures and private equity

Private capital, and in particular private equity, is playing a growing role as a buyer or strategic partner in divesting or restructuring businesses that are deemed to be non-core, underperforming or under-resourced. The record volume of dry powder amassed by private equity firms means they are hungry for investment opportunities. But, in order to engage them effectively, companies need to adapt their portfolio rebalancing approaches by initiating dialogues earlier and being open to alternative strategies and structures – whole sale is not the only option for businesses that no longer fit.

More than 80% of the respondents in our survey say they are now considering alternative exit strategies – partial sales with buy-back options, joint ventures (JVs), strategic partnerships etc.

4

Chapter 4
ESG is a critical driver of deal value

More than half of our survey respondents report that ESG (environmental, social and governance) considerations were discussed frequently during their most recent divestiture. ESG has definitively moved from the margins into the mainstream and now plays a central role in companies' strategic decision making, including shaping the criteria by which they assess their portfolios and the rebalancing activities that result.

Precisely how ESG impacts individual companies varies widely by sector and market position but impact it does and companies need to be alert both to the risks (headwinds), and the growth and value opportunities (tailwinds) that the evolving ESG picture brings. This is true of both the sell and the buy-side and is much more nuanced than simply divesting 'dirty' assets.

However, our survey clearly points to the fact that sellers with a clear ESG story are six times more likely to receive higher-than-expected deal value.

5

Chapter 5
How tax impacts deal success and values

Tax rules vary widely across the Asia Pacific region but, in every jurisdiction, there is value to be preserved and maximised through close attention and careful structuring of portfolio-rebalancing transactions. In our survey, 31% of respondents said that the availability of tax attributes or other tax benefits had played a significant role in them achieving a higher-than-expected valuation in their most recent divestment.

From deal structuring and pricing to managing divestment cost, the potential tax implications, and opportunities, should not be overlooked in portfolio rebalancing, even though they may be subservient to the strategic and commercial considerations.

Where to next?

This report combines the key insights from our survey with reflection and comment from experts around Deloitte Asia Pacific, to provide both an overview of the market dynamics and some practical insights into how company leaders can best respond.

You will also find first-hand experience from BHP, one of the world's leaders in mining and mineral extraction, on what good looks like when it comes to rebalancing a portfolio through divestments.

As corporate leaders seek to prepare their organisations to adapt and thrive in a new era, the capacity to balance resilience and transformative growth through active portfolio management will be one of the defining benchmarks for success.

Jiak See Ng
Deloitte Asia Pacific Strategy, Risk & Transactions Leader

Survey highlights

Deloitte's survey of 250 Asia Pacific executives reveals that active portfolio management is crucial for Executives and Boards to adapt to the five external forces we have identified. Our report strongly advocates a move towards an active portfolio management mindset.

59%

of corporates are assessing their portfolio performance at least

2x per year

up from 46% in 2022

Most companies are now needing to increase their scrutiny of portfolio holdings to rebalance to ensure resilience and growth. This need to rebalance is driven by five external forces:

1. Navigating geo-political tension
2. Capital efficiency regulation
3. The rise of investor activism
4. ESG and the road to net zero
5. Private equity's increasing role as an investor and potential partner.

60%

of respondents reported completing at least three divestitures in the last 36 months with motivations including:

- Change in market/ competitive landscape
- Lack of internal talent to grow business
- Business are no longer part of the core business
- Need to raise additional funds

95%

of respondents have experienced abandoned sales in the last 12-18 months, with multiple factors including:

- Change in internal strategy
- Competition
- Regulatory challenges
- Buyer interest

79%

of business leaders say they are expecting to make at least two divestments in the next 18 months, motivations include:

	Asia Pacific	Global
Business are no longer part of the core business	38%	35%
Change in market / competitive landscape	37%	39%
Opportunistic approach from an interested party	36%	34%
Lack of internal talent to grow business	34%	32%
Response to shareholder activism pressure/concerns	34%	35%
Regulatory environment or tax structuring	32%	40%
Need to raise additional funds	28%	32%

Asia Pacific Global

Readness

88%

of companies had to spend at least 4% of the divested company's revenue on preparing for divestiture

Alternate deal structure

99%

of respondents are considering at least one strategic alternative compared to more typical divestiture deal types (JV 96%, Partnership 96%, Strategic Alliance 95%)

ESG

52%

of respondents report that ESG considerations were frequently or very frequently discussed for their company's most recent divestiture

Tax

68%

of respondents say that Tax law changes have had at least a moderate impact on their divestiture strategies with 10% saying the impact has been high

54%

of survey respondents reported receiving a higher-than-expected valuation in their most recent successful divestiture. The top reasons sighted for these higher-than-expected valuations were:

- 39% Preparation/ optimisation execution at the divested business prior to deal
- 36% Value creation opportunity execution at the divested business prior to deal
- 31% Tailoring of the sale process to different bidders prior to engaging them
- 31% Availability of tax attributes and/or other tax-related benefits
- 27% Strength or preparation of management team
- 26% Availability of financial and tax information and analysis
- 24% Ability to present and execute a clear separation approach and framework
- 23% Inclusion of private equity bidders in the sale of the business
- 21% Exit/separation readiness assessment prior to engaging market

Asked what they would prioritise if they could execute their company's most recent portfolio rebalancing/spin-off again prior to bringing a deal to market, respondents cited:

40% Plan customer, supplier, other partner change management and communications

37% Have a compelling value story and track record for the divested business

35% Analyse potential deal structures and related cost / benefits

1.
Active portfolio management and capital efficiency

Looking around the post-COVID world, it is clear that we are in very different territory than before. Dislocation of marketplaces and trade lanes; rebalancing of energy markets in response to ongoing global conflicts; the rising cost of capital; economic patriotism impacting investment in critical sectors; the recalibration of the Chinese growth story – all these factors and more are profoundly impacting economies and sectors in ways that companies cannot ignore. Globally, and in Asia Pacific in particular, these forces are exerting significant and intensifying pressure on companies to review and adjust their portfolios.

Thriving – and, in many cases, simply surviving – in these new conditions will be defined by companies' ability to develop two key capabilities: resilience, through which they secure their foundations; and transformative growth, where they are able to reinvent their businesses to drive market leadership to ultimately create long term shareholder value. Central to developing these capabilities is the adoption of a more active portfolio-review mindset, where assets are regularly assessed for their fit, cost and contribution to the company's overall strategy. Those that are likely to deliver a competitive advantage are retained, while those that are deemed non-core to future growth or generate marginal returns on capital should be lined up for some form of portfolio rebalancing.

Regardless of approach, it is most important that companies make decisions and act on rebalancing, to prioritise capital to where they can generate greatest returns, as not acting can lead to a spectrum of unfavourable outcomes including missed opportunities that can go unnoticed, through to shareholder activism or takeover where value is transferred away form existing shareholders to the acquirer.

Our portfolio rebalancing survey reveals that 59% of companies in Asia Pacific now review their portfolio holdings at least twice a year, up from 46% globally in 2022. As well as being good corporate practice, active portfolio management is a valuable strategy for addressing the new pressures now facing companies in the region:

Creating or preserving shareholder value

There is always an opportunity cost for companies that have capital tied up in underperforming or non-core businesses they are holding and continue to hold in the hope that they will turn them around. When the 'repair' cost (the investment required to achieve that turnaround) is greater than the price they can achieve by selling it, then it is better to let it go. Persisting with a business as if it is still a good fit, or worse, investing valuable resources to rectify it, leads to value depletion and erosion of shareholder value.

Navigating geo-political realities

While geo-political tensions are always a factor, we are experiencing a period of unusual volatility and this is inevitably impacting board rooms; forcing companies to make portfolio rebalancing decisions at short notice. In the last few years, we have seen upheaval in the energy markets and a mass exodus of Western brands from Russia, following significant political and public pressure over the Russia's invasion of Ukraine, while ongoing tensions between the US and China are leading many brands to consider rebuilding their supply chains in other Asian markets. Companies with an active approach to portfolio review are significantly better prepared to manage the cost and impact of any sudden strategic adjustments driven by geo-political pressures.

Adjusting to regulatory pressures

Corporate governance in Asia Pacific companies lags behind best-in-class practices and, in a bid to drive improvement, many governments are introducing new regulations. For example, authorities in Japan and Korea are targeting listed companies with a price-to-book ratio of less than one (i.e. with a valuation that is less than sum of company's parts). This may lead to a wave of portfolio rationalisation and rebalancing or shutdown of underperforming businesses. This effect may be further amplified by the attention of activist funds piling on additional pressure on such companies to divest assets, and deliver greater shareholder value.

At the same time, competition regulators across the major regions are raising the bar for the approval of mergers and acquisition (M&A) deals, forcing buyers to divest assets in order to secure approval for a deal. For example, Asiana Airlines had to sell its cargo business to win approval from 'the European Union (EU) to acquire Korean Airlines.

Disruption from exponential technologies

The march of technology disruption is relentless. In the previous wave, the digital revolution upended the business models of many traditional companies, particularly in the traditional media and retail sectors, leading to many fire sales of assets. We are facing a new revolution, this time driven by the emergence and rapid proliferation of Gen AI and similar AI-enabled technologies. Companies need to consider the impact of such disruptions on their business models and take measures to realign their portfolios to embrace change. Again, those with an active portfolio review mindset will be best placed to achieve this efficiently and gain any first-mover advantages.

Engaging private equity

Private equity (PE) firms have long been a major force in the M&A market in Europe and the US, and they are now playing an increasingly important role in the Asia Pacific markets. Together with private debt capital, private equity firms are sitting on an estimated US$4 trillion of dry powder – capital that they are under pressure to deploy. Private equity firms are now actively on the hunt for carve-out assets across Asia Pacific. Our survey revealed that 26% of respondents divested to private equity in their most recent divestiture.

In chapter 3 *'Alternate deal structures and private equity'*, we explore in detail the evolving role of private equity firms in the region but suffice to say that their cash on hand, relative agility and non-competitor status makes a compelling proposition for companies in a hurry to divest non-core assets. For Asian companies reluctant to close the book on once-cherished businesses or unwilling to accept the reputational hit associated with divestment, private equity firms also offer the tantalising prospect of alternative exits.

While private equity firms are typically buyout engines, in Asia Pacific, they are adopting innovative strategies including JVs and partnerships in which they are willing to take a minority stake alongside the parent company and use their distinctive skills to create value from non-core business divisions and share the benefits. Blackstone recently took a majority stake in Sony Payments from Sony Bank and will partner with Sony Bank to co-invest and drive growth in the payments business. Companies should take note of this trend and consider such opportunities, preferably as early as possible.

The rise of activism in Asia

As we've already mentioned, companies also need to factor in the rise of activism in Asia – a feature that now looks set to stay. Activist funds often target cash-rich low-profit businesses, those with weak governance structures and those with conglomerate discount and then agitate for the break-up or divestment of certain portfolios. HSBC was part of a long-running campaign by Ping An to break up and even though the HSBC board won, it came at the compromise of divesting its Canadian retail business.

ESG and the road to net zero

Many companies are already re-examining their existing businesses through an ESG lens and identifying problematic assets to divest or wind down. Those that are not will have to step in line soon; the investor, workforce and media pressure to decarbonise, to tread lightly and employ well, is intensifying around the world, including in Asia Pacific. This is particularly the case in the energy sector, where many are divesting fossil fuel dependent assets to release capital for investment in renewables and clean energy. BP sold its global petrochemicals business to INEOS. In chapter 4, *'ESG is a critical driver of deal value'* we explore the growing importance of ESG considerations in detail, but it's already clear that the days of ESG as a 'nice-to-have' story are over. ESG is now central to the way stakeholders of all kinds view businesses.

The emergence and intensification of all these pressures is undoubtedly going to drive companies in Asia Pacific to increase their scrutiny of portfolio holdings, as they seek to rebalance and ensure they are both resilient and equipped to deliver transformative growth. In some Asia Pacific markets, portfolio management is still a relatively new concept – companies have typically held on to assets even when they have underperformed. That is clearly changing and active portfolio review, already widely used by western multinationals, seems likely to become much more widely accepted as a strategy for optimising portfolio holdings in this altered landscape.

Moving towards active portfolio management

As we noted earlier, the fact that companies in Asia Pacific are already reviewing their portfolios at least twice a year is encouraging. However, in order to be truly agile and able to course correct, companies should be moving to an 'always on' mindset when it comes to portfolio review, dedicating resources and board-level bandwidth to ensuring that assets are aligned with the overall strategic direction and, where they are not, being willing and able to move quickly to divest or engage with partners who can create value.

And when we say 'mindset' we mean it: developing both resilience and the potential for transformative growth means embracing the constantly shifting nature of markets and geopolitics and developing a state of readiness. If a metaphor is useful, it is akin to steering a sailing yacht – setting a course while simultaneously and continuously responding and adapting to the wind, waves and tide.

In advising companies on how best to achieve the required state of resilience and growth readiness, Deloitte Monitor's Advantaged Portfolio framework[2,3] outlines four broad characteristics that a successful portfolio needs to display:

1. Strategic strength

- Does the portfolio align to and advance the company's enterprise strategy? Without this alignment, while it may deliver reasonable financial return, and in the short term it is unlikely to create sustainable competitive advantages that are shared across portfolio businesses.
- Are the businesses competitively positioned in industries and markets that effectively capture evolving customer demands? Active assessment and action to carve-out businesses that are not attractive and have a limited ability to win will enable the reallocation of resources to attractive sectors with greater ability to win.

2. Value creation

- Are there synergies between businesses that ensure the value of the portfolio is greater than the sum of the parts? Identifying and exploiting intra-company synergies is one of the most powerful ways to capture a portfolio premium.
- Has capital been deployed in the most attractive areas or is there an opportunity to recycle capital to optimise returns?

3. Resilience

- Does the portfolio have the flexibility to survive multiple strategic scenarios in uncertain times? Effective portfolio management should articulate multiple growth paths to achieve future state portfolio and their related trade-offs, including anticipating potential changes within the enterprise portfolio.

4. Sustainability

- Does the portfolio create social, environmental and economic value and deliver positive social impact to the communities that it operates in? Society now expects that business think beyond profits and should play a positive role in these addressing these requirements.

The main goals

Ultimately, the main goals of an active portfolio management approach are: to put the company in a better position to achieve its strategic objectives and withstand the impact of market developments and factors beyond its control. Moving towards active portfolio management is, however, a significant change; requiring structured thinking and senior-level buy-in and commitment. This initial roadmap towards active portfolio management provides a useful framework to begin that process:

1. Strategic alignment and competitive positioning

- Analyse key forces that could influence the portfolio, including technological advances, market shifts, regulatory changes, and economic conditions
- Connect that analysis with enterprise strategy and chart the current and future competitive positioning, identifying the capabilities that will be required to succeed

2. Financial and operational controls

- Identify the financial and operational levers that will maximise return and achieve wider goals, particularly relating to ESG considerations

3. Scenario planning

- Develop multiple plausible future scenarios based on the intersection of critical uncertainties identified in the industry analysis

4. Optionality and risk adjustment

- Develop strategic options ranging from 'no-regret' moves that are beneficial in all scenarios to more speculative 'big bets' that could pay off in specific scenarios
- Establish a dynamic strategy that can evolve as new information becomes available or as specific scenarios or risks begin to materialise
- Leverage advances in AI to develop an active monitoring system that maps against the scenarios.

Case Study

BHP's divestiture of its Blackwater and Daunia mines

Deal summary

BHP Mitsubishi Alliance (BMA), a metallurgical coal joint venture in Queensland, Australia between BHP Group Limited (BHP) and Mitsubishi Development Pty Ltd (MDP), divested two of its operating mines, Blackwater and Daunia, in April 2024 for AU$6.4 billion.

Background

The decision to divest the Blackwater and Daunia mines stemmed from BMA's strategic imperative to optimise its portfolio composition as part of its proactive strategy to upgrade its portfolio of higher-quality metallurgical coal. BHP stated that, as a result of the divestment, more than 85% of BMA's production is now premium hard coking coal, which is sought after by global steelmakers to help increase production efficiency and lower emissions. Additionally, the divestiture created a strategic opportunity for BHP to realign its resources from an ESG perspective. This strategic shift enabled BHP to focus on future-facing commodities, such as copper, and environmental responsibility.

The transaction is one of the most operationally complex transactions that BHP has completed with the asset sale structure, change in rail and port arrangements and the preference to complete the transaction without a Transitional Services Agreement (TSA); all presenting significant challenges during the completion process.

Because the two operating mines were part of a highly integrated portfolio of assets, the separation at divestment also required the disentangling of co-mingled data and personnel. In addition, the transaction meant running two sales processes concurrently, allowing for the possibility of the mines being sold to different parties.

Supporting success with Deloitte

Deloitte's role as lead separation adviser encompassed strategic planning, execution, and readiness activities, with a focus on achieving separation objectives while maintaining safety, operational continuity and deal value.

This transaction marked BHP's second significant separation in the region and BHP incorporated valuable insights from the first, embedding practices such as involving separation advisers in the transaction structure sooner and assigning dedicated roles to key capabilities within the critical workstreams. This proactive approach ultimately led to a more favourable outcome. Integrating separation processes and establishing centralised governance early in the separation lifecycle, enabled and de-risked the 'no TSA' option, provided clear direction of the separation process in the transaction documents, and facilitated the concurrent running of two sales processes.

Positive outcomes

BHP successfully navigated complex challenges and executed the divestment with minimal disruptions to operations and ensured a safe and stable operational environment throughout the transaction period.

The divestiture of the Blackwater and Daunia mines marked a significant achievement for BHP. By safely separating the operational coal mines within the envisaged transaction timeline, BHP was able to realise its strategic objectives while optimising portfolio value.

The transaction enabled BHP to reallocate resources towards core growth areas that reflect ESG concerns.

Ultimately, the successful divestment reinforced BHP's commitment to proactive portfolio management and value creation in a dynamic market environment.

> Working collaboratively with Deloitte was pivotal in structuring our separation approach and execution. Establishing centralised governance early in the separation lifecycle, enabled and de-risked the 'no TSA' option and provided clear direction for the separation requirements in the transaction documents. This approach enabled the concurrent running of two sales processes, ensuring a smooth and efficient transition.
>
> **Andrew Larder**
> BHP Separation Lead

2.
Protect value by being divestment ready

In the rapidly changing global and regional corporate landscape, portfolio rebalancing remains an essential tool for organisations seeking to refine their strategic direction, allocate resources efficiently, build resilience and grow. Alongside delivering on these goals, an important measure of rebalancing success is the preservation or enhancement of value through the divestiture process itself; has the parent company maximised the value it realises by selling and, critically, ensured that the divested company is in the best position to succeed in the future with its new owners?

While an increase in deal activity or opportunities appears likely (see *'Survey highlights'*), sellers should also anticipate an environment where prospective buyers are increasingly vigilant, subjecting deal narratives to intense scrutiny and ensuring that value propositions are not merely presented but are fortified against challenge. In these conditions, robust preparation and strategic foresight are the best way to secure favourable outcomes and protect against the risk of value erosion.

Creating and preserving value throughout a divestiture is an exercise in strategic acumen, meticulous planning, and strong execution. The objective is to not only present the business in its best light, and thus increase its value, but also to ensure that its intrinsic worth is maintained and protected from value loss, from the initial stages of the portfolio evaluation through to the transfer of ownership and completion.

From strategy to sale

Value creation or erosion can occur at every stage of the divestiture lifecycle. Where it is lost at one stage, it is rare to see it recovered further along. This fact alone underlines the necessity for a proactive approach to preparation, where each phase of the divestiture process is thoughtfully planned and diligently executed to enhance value and to protect against its loss.

Value loss can occur at any stage with examples including:

- Incorrect valuation leading to pricing the asset too low or too high, which then impacts buyer interest
- Inadequate preparation and presentation of the asset diminishing its attractiveness
- Due diligence revealing unanticipated issues and hidden liabilities that reduce the asset's value
- Poor management presentations and negotiation resulting in unfavourable terms
- Operational disruptions impacting the overall performance of the asset.

However, while these issues are all too common, they are not inevitable and there are a number of practical steps a company can take to avoid value erosion.

A seller that is prepared is in a better position to establish value prior to the deal and protect against value loss throughout the divestiture process

Enhancing seller readiness: a blueprint for success

In chapter 1, *'Active portfolio management and capital efficiency'*, we looked at the benefit of an active portfolio review mindset. Regular and rigorous portfolio assessment puts companies in a strong position to build resilience and grow, enabling them to move swiftly when the time demands. And when an asset has been chosen for divestment, it is important that the focus switches to planning and preparedness. The principles laid out here provide a blueprint for companies to fortify their exit strategies, ensuring that every operational step contributes positively to the transaction's end value.

Strategic planning and a robust value story

In our Asia Pacific survey, more than a third (36%) of respondents said that the execution of value creation initiatives prior to the transaction was a significant factor in them achieving a higher-than-expected deal value. They also said that having a compelling value story and track record for the divested business would be one of their top priorities if they could revisit their most recent divestiture.

These findings underline the significance of strategic planning and developing a compelling value story, supported by robust separation financials and data. Together they help to frame the asset within a narrative that reflects market trends and investor interests while showcasing its unique potential.

- **Value proposition development:** The cornerstone of a compelling transaction narrative is a value proposition that resonates with potential buyers or investors. It should feature a detailed explanation of the divested entity's growth trajectory, highlight any synergistic opportunities for buyers, and provide a clear demonstration of its standalone viability.
- **Bidder analysis:** Preparing a detailed bidder list and analysis is key in a divestiture to target the right potential buyers (e.g. corporate versus private equity), stimulate competitive bids, and align the sales approach to their preferences.
- **Go-to-market plan and clear exit strategy:** A well-articulated exit strategy tailored to the right buyer group(s) should identify divestment options and how to take the entity to market, and also feature a thorough valuation impact analysis that highlights how divestiture pathways – sale, spin-off, or IPO – align with the company's overarching objectives and prevailing market dynamics.
- **Detailed separation financials and robust data:** Detailed robust financial and operational data build credibility in a divestiture, providing transparency on the health and potential of the business and the integrity of the deal. They give buyers the empirical evidence they require for valuation, allowing for informed bidding that reflects the true worth of the entity. They can also help to avert post-deal disputes and adjustments, streamline due diligence, and improve buyer confidence, all of which contribute to preserving and even enhancing the value of the deal. By contrast, the absence of detailed, credible financials leaves room for uncertainty, scepticism and discord, eroding value and ultimately deterring investment.
- **ESG consideration:** Incorporating ESG considerations into a divestiture strategy and value story (see chapter 4, *'ESG is a critical driver of deal value'*) not only aligns with ethical business practices but can also help to mitigate risks and enhance the overall value proposition of the deal for buyers who, like everyone else, are under increasing pressure to present strong ESG stories themselves. Interestingly, in our survey, there was substantially greater overlap between companies that frequently discuss ESG considerations and those that report receiving a significantly higher deal value than expected, than there was with companies that only occasionally discuss ESG.

Operational capability and independence

In our survey, when respondents were asked for the most significant reasons for their companies receiving a higher-than-expected value, the top-ranked answer was 'preparation and optimisation execution at the divested business prior to the sale' (39%).

Planning for operational and technological independence in a divestiture is crucial. It ensures that the entity being sold can function autonomously, without relying on the selling company's resources or systems or cumbersome transitional services. This independence can enhance the entity's appeal to buyers: it promises a seamless transition and the potential for uninterrupted business operations post-sale. It also mitigates integration risks and allows for clearer valuation since the entity's performance is not entangled with the seller's infrastructure.

Technology capability and decoupling

Given the extensive role technology plays in business, ensuring the divested entity has an independent and robust IT infrastructure is paramount. Technological preparedness involves a comprehensive review and restructuring of IT systems, data management protocols, and digital assets to ensure continuity and efficiency post-divestiture.

The vast majority of Asia Pacific survey respondents (84%) say that improving their tech savviness and maturity would help to improve their divestiture outcomes. In fact, respondents in our survey that describe themselves as tech-savvy (45%) report faster-than-expected time to divest; are more likely to identify and mitigate stranded costs; are more confident of achieving favourable transaction outcomes when approached opportunistically by bidders; and, have better internal M&A stakeholder alignment (E2E) than companies who aren't tech savvy.

As part of building divestiture preparedness from a technology perspective, companies can take a number of steps:

- Ensuring tech-foundations are sound (e.g. data availability and robustness)
- Understanding the impacts of technology across each stage of the divestiture lifecycle
- Deploying technology throughout the bidder process (e.g. VDR, visualisation for key financial and operational data)
- Considering alternate software solutions such as pre-configured SaaS platforms to avoid any significant costs to disentangle existing platforms and improve ability to scale.

Operational streamlining

Beyond technology, operational readiness involves a critical assessment of supply chain dependencies, internal processes, and customer relationships. Establishing operational independence ensures the divested entity can function effectively without the parent company's support, enhancing its attractiveness and value.

Tax structuring

In a divestiture, effective tax structuring can play a pivotal role by optimising the transaction's tax impact, thereby maximising after-tax returns. Strategic planning to minimise tax liabilities, leveraging incentives, and addressing potential exposures and opportunities should all be considered within the context of the tax laws of the relevant jurisdiction (see chapter 5, *'How tax impacts deal success and values')*. This can serve not just to preserve but enhance the deal's value and make the asset more attractive.

Compliance infrastructure

For our survey respondents, the time required for regulatory approvals was the top external factor (20%) influencing the one-time cost for planning and execution of the most recent divestiture. Building a compliance framework that can withstand regulatory and investor scrutiny means going beyond addressing current regulations and issues such as ESG requirements and anticipating future legislative or social changes. A forward-looking approach can help to minimise risks of compliance-related disruptions that could stall or derail divestiture processes.

Consideration of the remaining organisation

Value protection is not only critical for the assets being divested but is also for the remaining core-business. Keeping the remaining organisation front of mind throughout the divestiture process helps to improve continuity, stability, and positive relationships, ultimately contributing to the overall success of the divestiture. To prepare the remaining organisation for risks post-divestiture, it is crucial to undertake a rapid assessment of the shared elements between the seller and the business to be divested across products, processes, people, technology, and assets. A clear end-state vision and carveout strategy should be developed across all geographies and functions to minimise the chance of dis-synergies or stranded costs slipping through unnoticed. In addition, defining a target cost structure for the post-divestiture organisation allows for swift adjustment, shortening the duration of change and facilitating a smoother transition to the desired end-state. These actions collectively aim to mitigate risks and ensure the organisation can adapt effectively to the new landscape.

Stakeholder engagement

Asked what they would prioritise if they could revisit their most recent divestiture, the top-ranked response among Asia Pacific sellers was 'planning customer, supplier, other partner change management and communications.'

Portfolio rebalancing is, in essence, a form of corporate change and it's hard to overstate the importance of communication in managing change effectively. Keeping stakeholders informed and involved enables companies to better navigate the complexities of divestitures, including tight timelines. It also means they can address any concerns proactively and foster an environment that is supportive of, rather than resistant to change.

A strategic approach to stakeholder management helps preserve the value of the business being divested, accelerates the transaction process, and secures buy-in from key parties, ultimately contributing to the success of the divestiture. In our survey, there is significant alignment between sellers with strong internal collaboration and positive divestiture experiences, including higher-than-expected transaction values, faster times to execute, and better identification and mitigation of stranded costs post completion. So, what does good stakeholder engagement mean?

- **Proactive regulatory engagement:** Anticipating and navigating the regulatory and industrial relations landscape requires early engagement with regulatory bodies, unions, and the State; understanding potential hurdles such as foreign investment requirements and developing a clear compliance roadmap. This strategic focus is especially relevant in industries where regulatory scrutiny is intense, such as financial services.
- **Customer and supplier engagement:** An effective communication plan and alignment with customers and suppliers is vital for retaining confidence and loyalty, ensuring the continuity of business relationships, supply and revenue streams. It mitigates the risk of customer attrition triggered by uncertainties surrounding the transaction and can prevent disruptions to supply and dis-synergies created by a loss in purchasing power.
- **Management preparation:** A significant amount of value can be lost if management are unprepared and fail to make a compelling value story to prospective bidders. By adequately preparing management and engaging them throughout the divestiture process, companies can inspire confidence in bidders, mitigate risks and help protect against the loss of value throughout the divestiture process. Unsurprisingly, when asked what respondents would do differently if they could complete their most recent divestiture again, the most common response was more-extensive preparation of management.
- **Workforce engagement:** During a portfolio rebalancing, a wide range of workforce challenges can arise. Uncertainty about the future within the business being divested can result in the erosion of morale and productivity, the loss of key talent, cultural misalignments and miscommunication. Legal and regulatory compliance, integration complexities, discrepancies in compensation, and the need for effective change management can also present significant hurdles. By proactively addressing these issues through transparent communication, strategic planning and offering reassurances, companies can mitigate risks, ease the transition for employees, and help to preserve the value of the divestment.

Prepare and plan to preserve value

In any divestiture, successfully executing across multiple dimensions within a compressed timeframe while maintaining business as usual is essential if value is to be preserved and created, both for the divested asset and remaining organisation. Achieving this demands strategic planning and meticulous preparation at every stage of the transaction and with consideration of every stakeholder in the process.

As a bare minimum, divesting companies should take the following steps to ensure they are positioned to preserve value throughout the portfolio rebalancing lifecycle:

1. Develop a plan to maximise deal value and options, supported by a value-creation story
2. Develop a comprehensive buyer list to inform the design of the portfolio rebalancing process and any supporting materials
3. Develop detailed separation financials supported by robust data
4. Develop a clear separation strategy and blueprints
5. Anticipate alternative divestiture scenarios and be prepared to react
6. Streamline and separate technology and operations where possible
7. Develop rapid and clear TSA entry and exit plans where entanglements remain
8. Develop a detailed stakeholder management plan for both internal and external stakeholders.

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.

Rebalancing your portfolio to fuel growth

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.

Rebalancing your portfolio to fuel growth

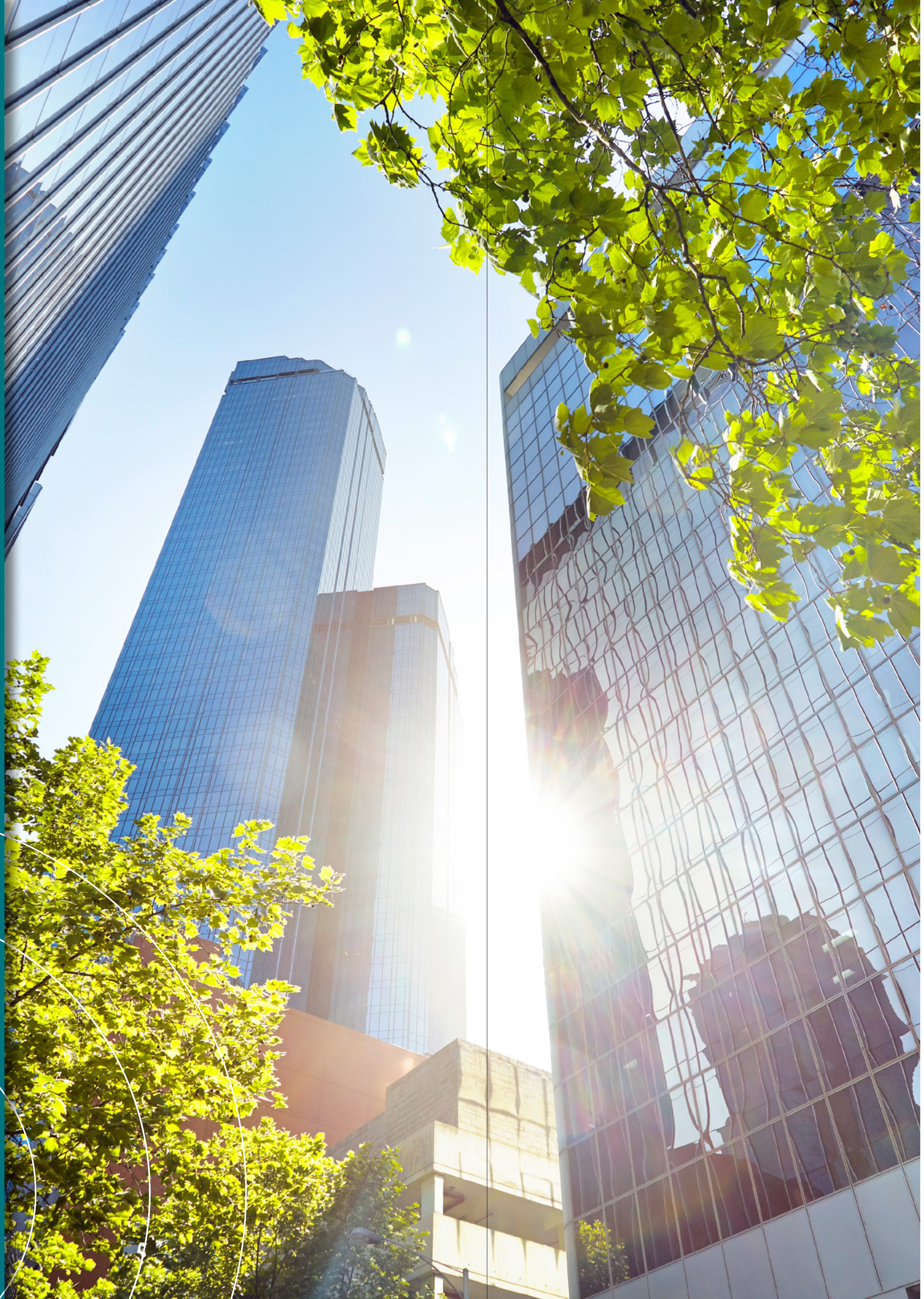
Deal or no deal, conversations add value

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.

4.
ESG is a critical driver of deal value



Not long ago, companies regarded ESG (environmental, social and governance factors) as a 'nice-to-have' component of their wider strategic narrative – something that reassured investors and stakeholders but wasn't considered essential. Now, investors and stakeholders increasingly focus on the credibility of a company's ESG story to understand its risk and return profile in a changing world. Companies that demonstrate a mix of ESG-related growth opportunities and a sustainable business model may attract higher valuations from an expanded potential buyers.[10]

Across the entire spectrum of the economy, companies are considering the transition to a sustainable, low-carbon economy in all aspects of their portfolio and value chains. This was initially driven by regulatory and investor pressures focused on addressing climate-related risks, such as the need to decarbonise emissions-intensive sectors and the risks posed by the changing physical climate. However, the focus is now equally on the growth opportunities that the energy transition, circular economy, and shifting customer preferences for sustainable solutions are creating. This is evidenced by the level of capital being deployed in sectors that seek to harness strengthening ESG tailwinds, with US$30.3 trillion invested globally in sustainable investing assets (2022).[11] In Q1 2024 alone, US$900 million of net new money flowed into sustainable funds.[12]

These shifts are occurring across the globe, even in jurisdictions such as the USA, where there has been some pushback in recent years regarding the term 'ESG'. In fact, some US-based asset managers are increasingly focusing on building a credible narrative around ESG and demonstrating quantifiable commercial and sustainable impact.[13] For example, CalPERS, the largest US public pension fund, has acknowledged that a fundamental shift in the economy is underway and is looking at ESG to generate alpha, aiming to expand its low-carbon assets portfolio to US$100 billion by 2030.[14] This may signal further ESG investments from funds with a member-first philosophy.

The role of government policy and subsidies to incentivise private capital investment in nascent industries and technologies, such as green hydrogen and ammonia, sustainable aviation fuels, and low-carbon transport options for heavy industries has also increased significantly in recent years. The US Inflation Reduction Act (US$370 billion clean energy investments, the EU Green Deal (US$1.1 trillion), the Future Made in Australia (US$15 billion), Singapore Green Plan 2030 (US$26 billion green bonds) and Singapore Future Energy Fund (US$3.8 billion) are prime examples of this.[15,16,17,18,19]

Individual ESG-related topics, such as carbon footprints, resource consumption, and human rights in operations and supply chains, are increasingly considered as measures of performance and risk by investors and stakeholders.

The combination of all these factors means that ESG has now become intertwined with commercial considerations. It is therefore important for companies, particularly those looking to review their portfolio and divest non-core assets, to align their approach to ESG with their corporate strategy to provide a compelling story around risk and return.

Decision makers need to explore the implications of a sustainable low-carbon future on their current business (core and non-core) and understand how factors such as revenue, cost base, customer and market preferences, and regulation can be strategically leveraged and changed to demonstrate their companies' existing and future ESG credentials and maturity.

Positioning by ESG personas

How companies and financial investors are choosing to respond to this changing environment is being shaped by their differing motivations, sector experience, investor mandates and risk-return requirements. These factors inform their understanding of their underlying assets, business model and strategies, ultimately driving decisions about what is core and non-core in their portfolios. They also highlight where new sources of growth can be found and where growth may be constrained in the future.

In analysing how companies are responding to the growing significance of ESG factors in their portfolio assessment, we can see three distinct personas emerging:

Persona 1:
Drivers and pioneers

Understand the game-changing nature of the transition to sustainable low-carbon future and are looking to grow their market share, technological and capability advantage, and brand in existing and emerging ESG-aligned industries. This might include companies focused on renewable energy generation and all the supporting infrastructure to enable this; companies focused on the decarbonisation of the transport sector (rail, road, aviation, etc.); or companies focused on decarbonising and reducing waste in the food and agricultural sectors.

Persona 2:
Transformers and pivoters

Recognise the shifts taking place and the need to transform existing business models, revenue streams, R&D and brand/competitive positioning and are looking to uplift, expand or pivot these assets to align more closely with broader market and industry trends, and improve the sustainability of the business model to deliver longevity. Examples might include a technology company expanding its software offering to support carbon-reporting requirements; an auto manufacturer purchasing a critical-minerals company to provide the raw materials needed for EV production; or an energy company divesting its fossil-fuel assets and pivoting its business model to focus on renewable energy.

Persona 3:
Residual value players

Understand the world is changing and are looking to capture the residual value of assets that are facing strong headwinds, are undervalued and have limited life. They are continuing to support these sectors as the economy transitions and are considering opportunities for an asset's next stage of life following the assets terminal value becoming zero. Examples of this might include coal and gas assets.

Optimising portfolio rebalancing outcomes through ESG

Historically, ESG has either been overlooked or considered implicitly during portfolio rebalancing. However, organisations are now increasingly considering the opportunities inherent to ESG and are looking to extract value from both the buy- and the sell-side.

ESG value creation

There is growing awareness of how ESG can be a source of competitive advantage when harnessed as an engine for innovation and growth. It challenges companies to rethink their internal and external approaches to their products, services, and processes, and to consider how they are facing into ESG trends.

ESG value creation focuses on identifying revenue-accretive opportunities that can deliver positive environmental and social impact while enhancing reputation and brand, including solutions that meet customer goals such as their sustainability agendas. Ultimately, ESG value creation can support revenue growth for both the buy- and the sell-side, with the following key drivers:

Revenue per customer

- Green premium, with higher prices driven by a compelling customer proposition, for example positive branding, meeting public decarbonisation commitments, and protection against reputational, financial and competitive positioning risks from not being sustainable.
- Expansion of existing revenue streams and creation of new revenue streams, with green and/or sustainable solutions providing greater cross-sell and up-sell opportunities among the existing customer base and serving to attract new customers.

Number of customers

- Attract ESG-conscious customers, particularly those who have started on their sustainability journey and are considering solutions that enable their decarbonisation for example. They will have some knowledge and understanding of their ESG procurement criteria.
- Customers who have not yet started to consider sustainability. Customers who have not yet started to consider sustainability may be looking to uplift their capability rapidly, and may decide who they procure from based on their understanding of the ESG positioning and the supplier's brand.'

Rebalancing your portfolio to fuel growth

Other ESG-linked synergies

There are additional benefits that strong ESG practices can provide to the buy-side or sell-side beyond cost savings:

Reputation and branding	• Improved reputation and branding in market. Having a strong ESG proposition is important to both the buy- and sell-side to foster trust, build goodwill and communicate the company's ethos such that it resonates with stakeholders including customers, employees and regulators. ESG can be a lever for companies who are looking to shift their brand identity, particularly from a neutral or 'dirty' sector. • Opportunity for buyers to take on the green branding of the target. While this can appear attractive, it is fraught with danger given uncertainty of investor and customer response. For example, the initial announcement following Shell's acquisition of Powershop Australia resulted in customer uproar.[20] If a buyer wishes to pursue this, extensive change and stakeholder management will be key to navigate and rationalise the benefits of the deal.
Operational efficiency, improvement and resilience	• Buyers can achieve rapid ESG capability uplift from acquiring the initiatives, learnings, and knowledge of the target, including their sustainability team if they have one. This can accelerate understanding of how the buyer can generate value from ESG and embed it within the organisation, but also highlight areas of risk. Proactively addressing and mitigating these risks allows for strong operational resilience, for example through the strategic placement of assets to minimise impacts of physical climate risk. • Improved operational efficiency can provide time and material savings and improve output. For example, improving the operational efficiency across the value chain can minimise raw material usage, save time in production and distribution, and increase productivity. This may be supported by the tracking of qualitative and quantitative metrics such as raw-material usage, energy consumption and carbon emissions attributed to transport.
Talent attraction, engagement and retention	• Drive competitive advantage through best-in-class talent proposition by meeting the needs and values of employees. This resonance can drive employee advocacy of the business, for example on public rating sites such as Glassdoor and LinkedIn, and higher rates of engagement and retention. This is crucial in industries where there is a shortage of talent, the technology industry is an example of this.
Lower cost of capital	• Building ESG credentials can provide access to green financing. It represents an opportunity to lower the cost of capital, particularly since green and sustainable loans lower the lending rate based off progress against ESG measures. • Having strong ESG credentials can support business longevity due to lower perceived risk and higher resilience.[21,22] A lower risk profile makes a company more attractive, particularly for financial investors who are concerned about how the changing external environment might impact the long-term viability of their investment.
Regulatory compliance	• Companies that can develop a fit-for-purpose approach to dealing with emerging and existing regulatory concerns will be attractive to potential investors, and their ability to future-proof their operations by leveraging their information advantage to inform better decision making.

Responsible divestment: an emerging concept

The intensifying focus on ESG as a driver of portfolio rebalancing activity is also now leading to consideration of the ESG profile of prospective buyers and what might happen to divested assets and the people employed within them. This is especially relevant in areas such as mineral extraction, where highly prized resources are often found in territories with historically weak environmental and employment regulation. Companies divesting mining assets, for example, may be forced to consider whether the prospective buyers are likely to be motivated to manage them responsibly, particularly if the buyer does not have the expertise, knowledge or focus on sustainable business practices.

Already we are seeing these kinds of issues being surfaced. If a luxury car manufacturer switches the sourcing of minerals essential to the electrification of its products to jurisdictions that have lower inherent ESG risk exposure, such as Australia and Canada, rather than locations which historically have been associated with labour exploitation, what happens to those abandoned resources? Is there a risk that a business with less concern for environmental or labour standards will acquire them? What responsibility does the divesting company have to ensure that divested assets go to 'good homes'?

ESG in portfolio rebalancing

The energy sector has a well-established approach to leaning into the energy transition to drive growth. However, the relevance of ESG goes across multiple, less-obvious sectors. Below, we have outlined how different ESG themes have driven portfolio rebalancing in different sectors and for different ESG personas (see page 31).

Climate

The physical impact of climate change is a risk to many companies, with the severity varying based on sector according to its impact on business operations, employee and customer safety, and the wider economy.

For example, extreme weather events can damage property and increase the number of claims, which may result in the unaffordability or unavailability of insurance in high-risk regions.[23] Similarly, climate change can impact the supply and quality of crops and livestock through reduced crop yield over time or loss of land to rising sea levels, which is an existential crisis for the agricultural sector.[24]

Solutions that aim to solve these challenges are emerging, with examples including:

Example	Persona	Description
Technology platform	Drivers and pioneers	CORE Markets, formed from the merger between Renewable Energy Hub and TFS Green APAC in 2022, provides climate software and services. The merger rationale was to bring together the carbon and energy commodity-market expertise of TFS with Renewable Energy Hub's existing carbon marketplace platform and net zero services.[25]
Agriculture	Drivers and pioneers	In 2023, Belgian sustainable crop-management provider Biobest Group acquired an 85% stake of Brazilian Biotrop, an Agtech that is similarly focused on sustainable solutions for agriculture. The acquisition rationale was to expand Biobest's footprint in the high-growth and favourable regulatory environment of the Brazilian markets and combine both firms' sustainability strengths.[26]
Climate insurance	Drivers and pioneers	In 2013, US agrochemical and agricultural biotechnology company Monsanto paid US$930 million for The Climate Corporation, which underwrites weather insurance for farmers. The deal rationale was to strategically expand Monsanto's revenue stream into the US$20 billion opportunity of services and data.[27]
Professional services	Drivers and pioneers	There have been many acquisitions to date in professional services, with a focus on building capability to expand into net zero-climate consulting. As a snapshot, in 2023, Schneider Electric acquired climate consultancy EcoAct, ERM acquired climate, energy and water advisor Coho, and Accenture acquired sustainability consultancy Green Domus. In 2022, Accenture also acquired carbon and climate-change-strategy consultancy Carbon Intelligence.

Rebalancing your portfolio to fuel growth

Changing consumer preferences and laws

Consumer preference for sustainable goods and services, alongside broader trends of health and wellness, has resulted in the emergence of new product categories, such as plant-based alternatives to meat and dairy, and natural paints. There is growing emphasis on sustainable practices including biodegradable and eco-friendly products and circular economy, which is supported by laws such as the Australian Recycling and Waste Reduction Act and Singapore's Resource Sustainability Act.[28,29]

Example	Persona	Description
Sustainable packaging	Transformers and pivoters	In 2023, Amcor, a global packaging company, announced it had entered agreement to acquire Phoenix Flexibles, a flexible packaging manufacturer in India. The deal rationale was to expand Amcor's capacity in the high-growth Indian market but to also acquire advanced film technology that can enable local production of more sustainable packaging solutions.[30]
E-Waste	Drivers and pioneers	In 2024, Australian e-waste company Sircel wholly acquired the assets of e-waste processor Scipher Technologies. The acquisition rationale was to increase processing capability, deepen specialist expertise and acquire Scipher's customer base.[31]
Media	Transformers and pivoters	Rainmaker Group, an Australian researcher and media publisher, later bought by Institutional Shareholder Services in 2021, acquired sustainable investment publication The Sustainability Report and Audacious Investing in 2019. The acquisition rationale was to tap into the growing investment interest in ESG from both companies and consumers.[32]

Human rights in supply chains

There is increased focus on human rights in supply chains across many sectors. Some companies are seeking to source raw materials and components from suppliers and geographies with higher standards, while others are looking for vertical integration opportunities to gain greater control over the supply of raw materials and labour conditions.

Example	Persona	Description
Automotive	Transformers and pivoters	In 2023, Volkswagen's battery unit PowerGo, Dutch automotive company Stellantis and mining company Glencore agreed to back a US$1 billion deal to purchase two Brazilian mines (Nickel Sulphide and Copper) by UK-listed SPAC ACG Acquisition Company. The acquisition rationale was to guarantee critical mineral supply for use in their EV battery manufacturing.[33]
Cocoa	Drivers and pioneers	In 2019, global food and agri-business, Olam International Limited, acquired 85% of BT Cocoa, Indonesia's largest cocoa processor. The acquisition rationale was to ensure Olam could continue to be a world leader in traceable cocoa sourcing and processing by gaining ownership of a major processor in its supply chain, and meet growing demand for products requiring sustainable cocoa powder.[34]
Cotton	Transformers and pivoters	Both Singapore-based Olam Agri and France-based Louis Dreyfus Company are currently bidding for Namoi Cotton, an Australian cotton ginner. An ongoing transaction, the acquisition rationale for both is to leverage Namoi's focus on sustainable cotton, long-standing reputation and assets to complement their existing operations.[35]

Becoming ESG prepared

The transition to a sustainable low-carbon future is inevitable and will impact every sector. It will create challenges for companies in Asia Pacific that will need to wrestle with changing operating parameters and business environments. The result will, inevitably, be a rebalancing of portfolios as companies seek to strategically refocus and divest assets that no longer fit or align with their positioning in a sustainable low-carbon future.

ESG preparedness will become a distinct advantage, with companies that can demonstrate a compelling ESG story around risk and return and strong ethical positioning, likely to be significantly more attractive to prospective buyers. There is potential for higher trading multiples. In fact, in our portfolio rebalancing survey, companies that very frequently discuss ESG considerations are nearly six times more likely to report receiving a significantly higher deal value than expected compared to those companies that have these conversations only occasionally. Having strong ESG credentials will also be key to building trust with a company's investor base, particularly activist investors, and the broader market.

To achieve ESG preparedness, business leaders need to first understand what ESG means for their company and sector, particularly the implications of a sustainable low-carbon future on their current business (core and non-core). They will need to align ESG with corporate strategy, with strategic considerations including factors such as revenue, cost base, customer and market preferences, and regulation. However, the baseline is that business leaders need to show stakeholders that they are actively meeting and embracing the fundamental shift in the economy.

By embedding ESG into an organisations' DNA, there is an opportunity to drive growth through ESG value creation and realise other ESG-linked synergies, such as business longevity. This can be articulated into a credible narrative around how ESG can generate quantifiable commercial and sustainable impact, particularly as it relates to divestitures. In one way or another, ESG has become a consideration in the M&A process and is here to stay.

5. How tax impacts deal success and values

Alongside the strategic and commercial considerations of any prospective divestiture, sellers should be cognisant of their tax implications so that they realise the full value of the transaction – and that means taking a holistic view that goes beyond looking at the asset itself.

Tax structuring and close attention to changing tax laws can help to manage tax costs associated with divestments, mitigate any adverse tax risks and exposure, and deliver tax efficiencies for the seller or buyer both during and post-divestment. In our survey, 68% of respondents said that tax law changes have had at least a moderate impact on their divestiture strategies, with 10% saying the impact has been high. We have surveyed some of the major jurisdictions across Asia Pacific to identify the key tax issues and considerations for companies reviewing potential divestitures.

Structures and modes of divestment

Divestments are typically undertaken through share sales, asset sales or a combination of the two. In share sales, it is usually the selling shareholders who receive payment, while in asset sales, the consideration will be received by the selling entity. So, where a divestment is undertaken through an asset sale, but the shareholders want to receive funds from the transaction, it will be necessary to devise a way of upstreaming the sale proceeds and this may then entail additional tax costs and planning.

Individual Asia Pacific markets display widely differing characteristics when it comes to the typical forms of portfolio rebalancings, including:

India

Alongside conventional asset and share sales, slump sales (i.e. the sale of a business for a lump sum consideration without attribution of specific values to assets and liabilities) of itemised assets, and tax-neutral demergers are common types of asset sales often used in an India divestiture transaction.

Singapore and Malaysia

In Singapore, any gains from the sale of shares or assets, which are considered as capital in nature, are generally not subject to tax. However, gains arising from the sale of foreign assets (as defined) may be deemed taxable upon receipt in Singapore to the extent they take place on or after 1 January 2024, subject to certain exclusions and economic substance requirements. In addition, stamp duty generally applies to sale of shares in unlisted Singapore companies. Effective from 1 March 2024, Malaysia has introduced a capital gains tax (CGT) regime which taxes disposal of Malaysia unlisted shares, while similar to the Singapore regime gains from disposal of foreign assets are taxable effective from 1 January 2024 subject to certain exclusions. Real property gains tax may also apply for share transfers of companies which are real property companies, in addition to stamp duty.

Indonesia, Philippines and Vietnam

Indonesia, Philippines and Vietnam generally impose capital gains taxes on the sale of unlisted shares in these markets. In the Philippines, donor's taxes can also be imposed on the excess of fair market value over the selling price of unlisted shares in certain instances. Vietnam, however, also imposes capital gains tax on indirect share transfers, and that is something that sellers should be aware of as returns may be impacted.

Japan

Alongside conventional asset and share sales, divestments in Japan are typically structured as demergers, reverse-demergers, or business transfers in combination with share transfers. Demergers can be used to defer the recognition of capital gains in some cases provided that certain requirements are met. These techniques are commonly used in an internal group reorganisation scenario, where some degree of capital relationship is expected to continue between the entity housing the divested business and its original contributor/shareholders. Maintaining such capital relationship is intended to generally restrict the preferential tax treatment of deferring capital gains to internal group reorganisations.

Korea

A combination of share and asset sale transactions would typically be undertaken in a carve-out situation using a two-step process: first, by establishing a company (NewCo) to absorb assets and businesses through an in-kind contribution from the transferor entity; and second, through the subsequent spin-off of such NewCo via a share sale. There are certain tax concessions in Korea that can minimise the tax costs associated with these steps, subject to certain conditions being satisfied.

China

The sale of assets in a Chinese company, can be achieved through sale of shares, spin-offs, reverse carve-outs and indirect share transfers (e.g., via selling an offshore entity that holds a Chinese company). For indirect share transfers, it should be noted that there could still be a reporting and capital gain exposure, subject to the factual circumstances.

New Zealand

Since there is no comprehensive capital tax gains regime, nor stamp duties or other transfer taxes, share sales are the most common mode of divestment. Asset sales are typically undertaken for carve-outs, where the seller has available tax shelter to mitigate any adverse tax costs associated with such asset sales.

Australia

Share sales are the most common mode of divestment since share sales, unless the relevant target is land-rich are typically not subject to stamp duty. However, in a carve-out where a share sale is not possible for commercial reasons and depending on the specific tax profile of the seller and the assets being carved out, either of these scenarios are possible: the seller transfers the relevant assets to a newly incorporated entity (NewCo) and then disposes of them, or the seller disposes of the relevant assets directly by way of an asset sale.

Managing portfolio rebalancing tax costs

Divestments will often carry capital gains and transfer-tax implications which may impact transaction pricing. However, there are ways to manage these tax costs. Some jurisdictions provide a relevant tax framework that allows business restructurings to be treated as tax-free or tax-deferred, provided certain conditions are satisfied. However, these tax-deferral schemes typically only apply in an intra-group transactions. Hence, to help mitigate taxes, early planning and restructuring of the target assets to be disposed of, such as moving target assets into a separate holding vehicle and selling shares in that holding vehicle some time later, could be considered to avail to such schemes. Alternatively, a reverse-carve out where the seller carves out the assets to be retained could also be considered.

Warranty and indemnity (W&I) insurance is increasingly used to better manage tax risks and exposure in the target group, where they exist in jurisdictions across Asia Pacific. For example, this can be done in private equity and privately (family) held exits by transferring to an insurer, material legacy tax risks in the target group which might otherwise be a deal breaker.

Tax efficiencies and deal pricing

While portfolio rebalancing is largely driven by commercial considerations there can be associated tax considerations too. Sellers seeking to attract investors into their profit-making businesses may want to segregate or dispose of loss-making business segments. However, these loss-making businesses may also have accumulated tax losses over the years, which can represent value if they can be applied to reduce future taxable profits and therefore future taxes payable. In certain cases, these entities may recognise deferred tax assets on these losses.

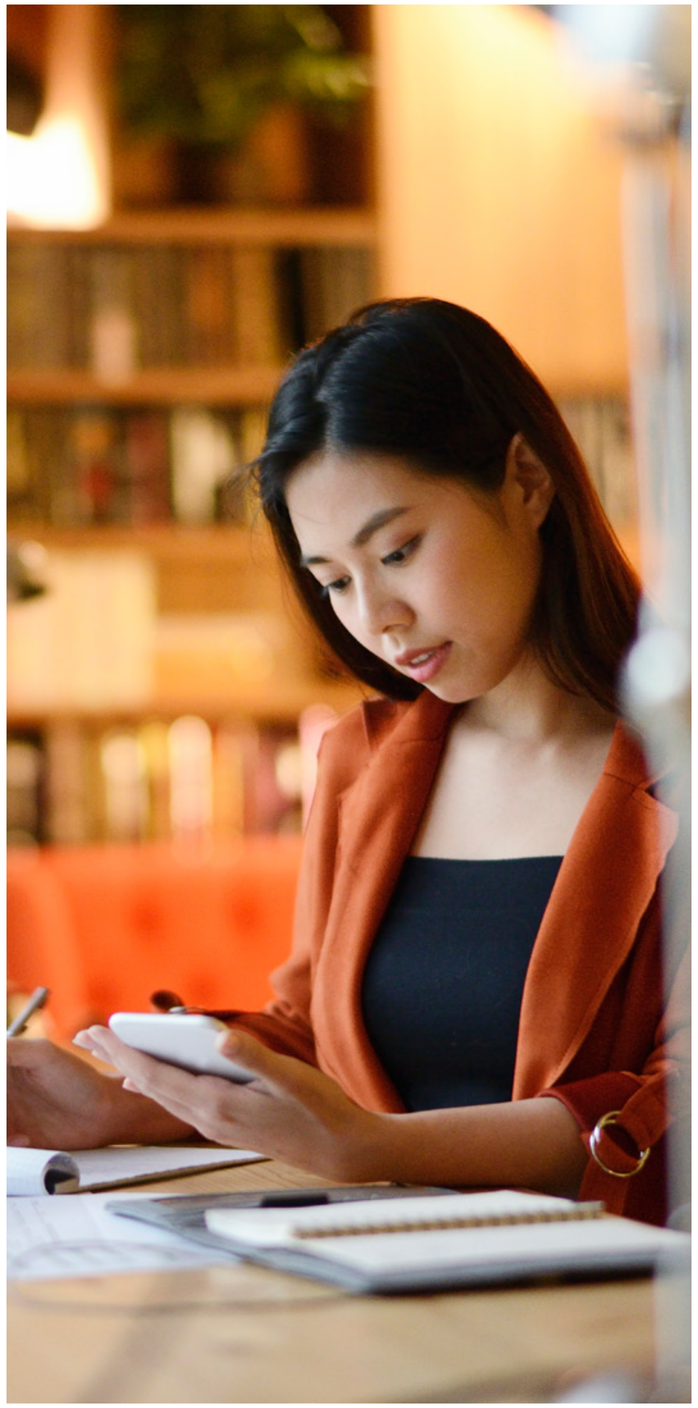
In our survey, 31% of respondents said that the availability of tax attributes and/or other tax-related benefits were among the most significant reasons for them achieving a higher-than-expected value on their most recent divestiture.

However, while sellers may want to price in certain tax attributes to derive maximum value out of a portfolio rebalancing, they should be aware that the practices of different jurisdictions in Asia Pacific vary significantly. In the case of India and New Zealand, tax costs are typically not explicitly priced into the deal. Specifically, in Korea, the tax value does not directly affect the deal price unless the tax value is very likely to be realised. In China, the buyer and seller can reach an agreement on how tax attributes may be priced into the sale consideration, so long as the deal price is commercially justifiable by the parties.

In other cases, tax attributes may be disregarded and not priced into the purchase consideration, particularly when the availability of the tax attributes post-divestment is uncertain. It is also possible to implicitly price certain tax attributes or costs into the overall transaction, though these may not be expressly presented in sale transaction documents. These tax items can include Net Operating Losses (NOLs) and the tax cost of asset sales, as well as additional costs of cash upstreaming, where the portfolio rebalancing was achieved through an asset sale and shareholders are keen to access the divestment proceeds. More importantly, in an asset sale, typically there is a step up of asset value to transaction price. This benefits the buyer, who would otherwise be buying shares and inheriting the underlying assets at book cost. However, asset sales are often more difficult or take longer to execute owing to the need to transfer contracts and licenses.

Sellers may also want to look at the impact of the divestitures on their effective tax rates (ETR), specifically on the adjusted Global Base Erosion (GloBE) ETR per jurisdiction. The impact on GloBE ETR would be especially relevant where the seller wants to manage the ETRs in the group for the purposes of minimising any top-up taxes, which may need to be paid by the relevant group in accordance with global tax regime changes brought about by OECD's Base Erosion Profits Shifting (BEPS) Project 2.0, Pillar Two.[36] For example, a multinational group that is in-scope for Pillar Two may want to consider the impact on the GloBE ETR of an asset sale as compared to a share sale. While a non-portfolio share sale may not have an immediate impact on a company's GloBE ETR, an asset sale could significantly alter the company's adjusted tax expenses and income, and consequently its GloBE ETR. This would especially be the case if the company sells high-value assets. Strategic planning and knowledge of the BEPS rules are therefore essential in either scenario to effectively manage the multinational group's global tax liabilities.

As ever, the tax component of a prospective divestiture is both complex and nuanced. But it also cannot be ignored. While the specific tax rules that apply differ widely across the Asia Pacific region, the cost of not fully understanding the tax implications of a divestiture transaction is potentially the same regardless of the specific jurisdiction: that is potentially a failure to realise the full value of the deal.



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Rebalancing your portfolio to fuel growth

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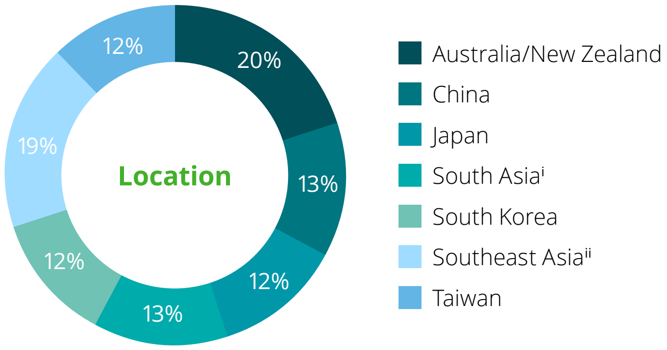
About this survey

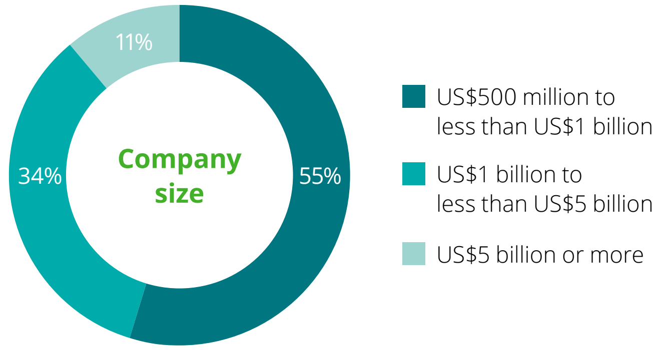
Methodology

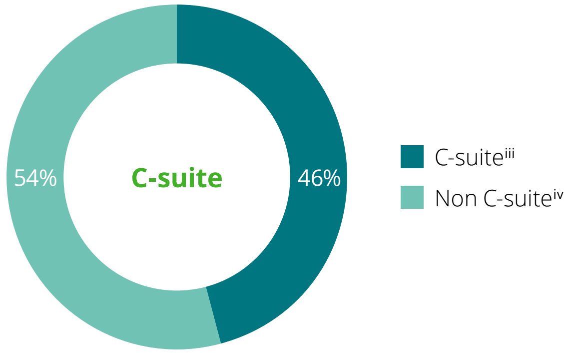
Between 21 March and 5 April 2024, a Deloitte survey conducted by market research firm OnResearch, polled 250 executives who had been part of a divestiture within the preceding 36 months to understand their thoughts about divestiture activity in the next 12–18 months, as well as their experiences with recent divestitures.

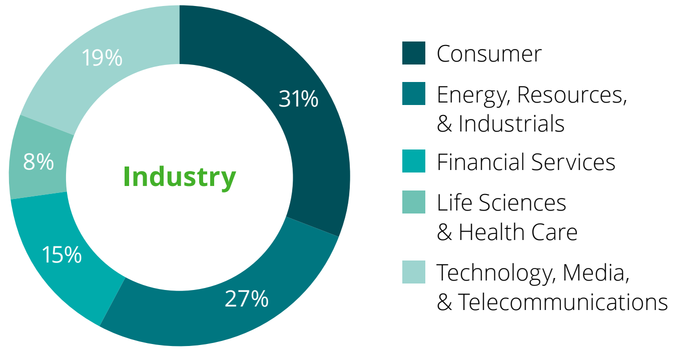
All survey participants work either for private or public companies with revenues in excess of US$500 million. Two thirds (67%) of respondents represented firms with more than US$1 billion in revenue. The participants hold senior ranks (senior director or above at the corporations). Most of the respondents (80%) sit within the C-suite. Respondents' companies are headquartered in eight Asia Pacific locations (Australia, New Zealand, Japan, Korea, China, Taiwan (China), India and Southeast Asia) and each location is represented by a statistically viable sample of responses.

250
companies surveyed:









i. India, Sri Lanka
ii. Singapore, Indonesia, Malaysia, Thailand, Vietnam, Philippines
iii. Board member, CEO, CFO, CMO, COO, CTO/CIO, Other C-level executive, Owner/Operating Partner
iv. Head of business unit or department, Senior Director/Director, Senior Managing Director/Managing Director, Senior Vice President/Vice President, Controller

Endnotes

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8. Anheuser-Busch InBev buys back South Korea's Oriental Brewery (ft.com) – https://www.ft.com/content/6f8ba754-817f-11e3-b3d5-00144feab7de
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