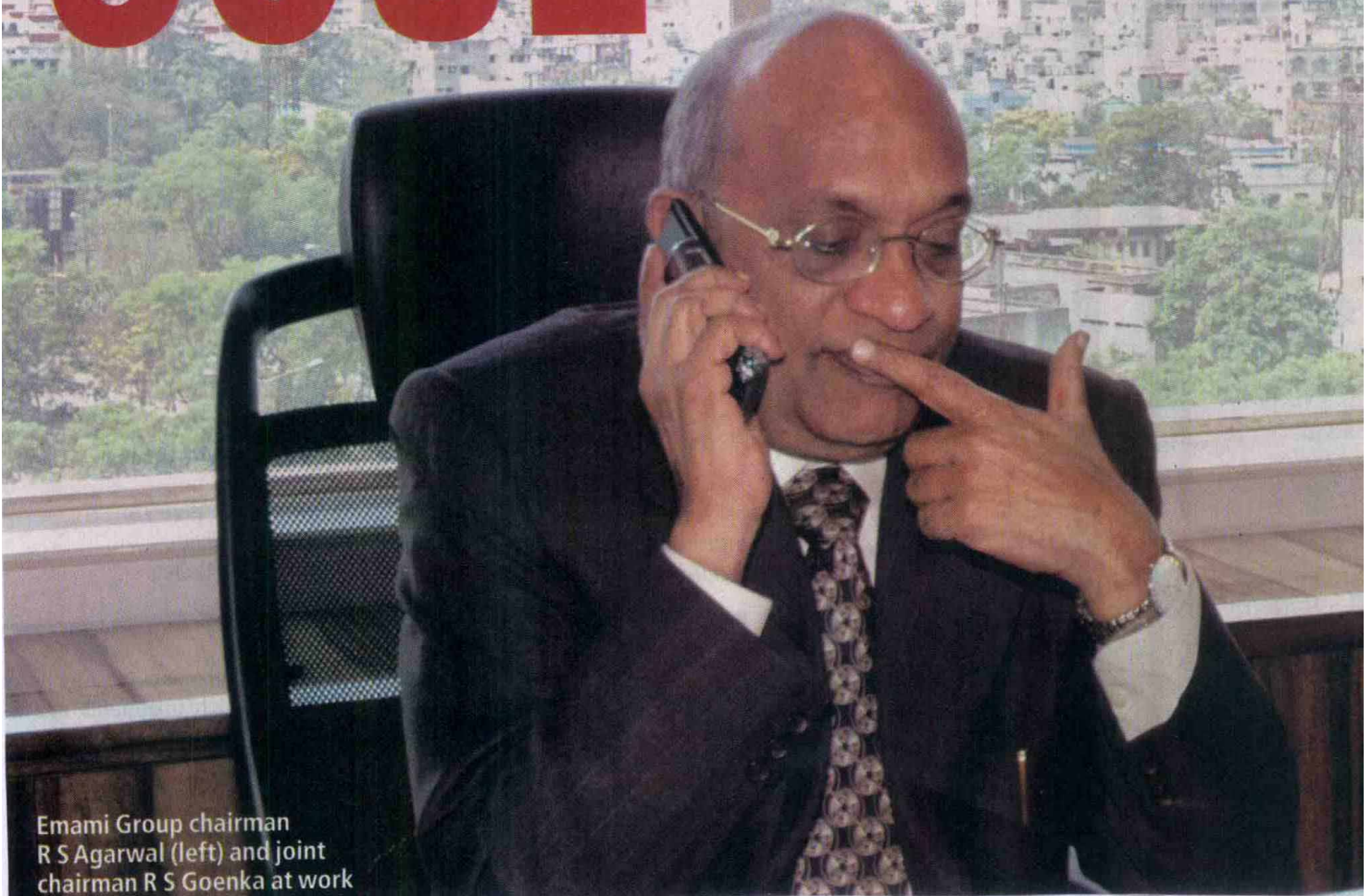


**Emami needs more to be
a major FMCG player**
The Strategist, Separate section

BALM for the SOUL

Emami's old-school promoters were nimble enough to acquire Zandu. They need many more manoeuvres to become a major FMCG player

Aanand Pandey & Pradipta Mukherjee



Emami Group chairman
R S Agarwal (left) and joint
chairman R S Goenka at work

Radhey Shyam Goenka, 61, the joint chairman of the Emami group, loves to take an occasional dig at the group chairman and his friend of over 40 years, Radhey Shyam Agarwal. Like most old-school entrepreneurs, Agarwal has a habit of scribbling down numbers on a piece of paper during meetings. When Goenka and Agarwal sit with the next-generation directors from the two families, at times Goenka snatches the scribbled note from Agarwal's hand, gives it to one of the directors and asks him to check the final figure. Surprisingly, every time Goenka has done this, Agarwal's final figure has turned out to be incorrect. "Our children laugh at this," says Agarwal.

Goenka is the cool one, known for his meticulous planning, while Agarwal is the galloping warhorse, whose business instincts appear incredible at times, but, according to Goenka, "turn out, amazingly, to be prophetic". Sure enough, most of the promoters' decisions bear the stamp of Goenka's diligence and Agarwal's foresight.

They characterised their first life-altering decision. In 1974, the duo left cushy jobs at one of the Birla companies to sell "beauty and cosmetic products priced 30 per cent higher than the competing brands, piled on the back of a hand-pulled rickshaw", according to Agarwal's younger son and Emami's executive-director, Harsh Vardhan. One could hardly predict that the duo will take the business, started with a seed capital of Rs 20,000, to where it is today: Rs 1,700 crore flowing in from fast-moving consumer goods, newsprint, edible oil, real estate and health care. It again came into play four years later when they took over a sick unit named Himani Ltd and pressed on to make it work for eight years.

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Balm for the soul

In 1984, Himani gave them Boroplus, a blockbuster product that rejuvenated their FMCG business.

As Emami acquired Zandu Pharmaceutical Works recently — the culmination of a six-month battle — it fought with precision and planning. The mark of foresight, however, is yet to be seen.

To seal a deal

To acquire an Indian listed company, one needs a Teflon exterior, which would prevent things from sticking. Mumbai-based Rs 140-crore Zandu is a 100-year-old company that manufactures more than 300 herbal and ayurvedic products. A zero-debt company with a strong brand name, Zandu has always been an attractive target for both Indian as well as multinational FMCG companies.

In May this year, when Emami picked up 23.6 per cent stake in an off-market deal from the Vaidyas, one of the two promoter groups of Zandu, it looked a smart, albeit expensive, move. According to reports, Emami paid Rs 130 crore to the Vaidyas at an offer price of Rs 6,900 a share (including Rs 100 a share as non-compete fee).

Immediately after Emami's announcement of the mandatory open offer of 20 per cent to Zandu shareholders at Rs 7,135 a share, Zandu sought to stave off what it saw as a hostile takeover bid by taking recourse to a popular and effective tactic known in M&A parlance as the Shark Repellent manoeuvre. It sent a notice to Bombay Stock Exchange saying the company intended to issue preference shares to the company's promoters and directors. This was aimed at fortifying Zandu's second promoter group, the Parikh family. Emami got wind of the note and sent a legal notice to Zandu the next day, which forced the Parikhs to withdraw the plan. "The independent directors on the Zandu board were kind enough to understand our point of view," says Harsh Agarwal.

Meanwhile, Zandu's shares at BSE stayed around Rs 10,000 a share in anticipation that Emami will raise the offer price. Emami's promoters remained unfazed. "We think we have done a fair evaluation keeping in mind the industry standards," said a press statement issued shortly after-

wards. Meanwhile, the stock market soared in July, when Emami's open offer opened.

By that time, the expected had happened. The Parikhs, anticipating Emami's next step, had raised their stake in Zandu from 18 per cent to 22 per cent. They owned another 20 per cent, said industry sources, through family members and associates. At the same time, the Parikhs had gone about knocking on all possible doors — Securities & Exchange Board of India, the Company Law Board (CLB) and the Bombay High Court — but by the end of August, it was clear that as far as the Parikhs were concerned, Zandu was a lost cause.

By mid-September, Zandu's shares

gence may have given way to adventure.

Experts say the deal holds lessons for future buyers. KPMG's corporate finance director, Nandini Chopra, who also heads the firm's valuations practice, says: "Acquirers in future would possibly seek to be more in control of their pursuits by ensuring that they are negotiating, from the outset, with majority blocks of shareholders." This would help mitigate the risk of another shareholder block perceiving it as a potentially hostile situation. "This will also prevent the target company's remaining shareholders from putting up bid defence strategies, which would ultimately increase the cost of acquisition,

quisition brand consolidation, sounded even more optimistic. "We expect our sales and profitability to grow by two to three times in the next couple of years," he said.

According to Associated Chambers of Commerce and Industry, FMCG sales have not been affected by the current slowdown and the sector is expected to touch \$25 billion by the end of 2008, as against \$20 billion in 2007.

A positive industry outlook and Emami's compounded annual growth rate at an impressive 25 per cent for the last three years, the anticipation is soaring in the region of 34-35 per cent. However, the steep takeover price and historically low growth of the Zandu franchise (10 per cent CAAGR) indicate that there is more to Emami's enthusiasm than meets the eye.

Analysts say the intent is not only to unleash the untapped potential of the strong Zandu brand — deploying a mix of marketing, distribution and operational strategies — but also to prepare the ground for



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HARSH AGARWAL
Director, Emami

had fallen below Rs 16,700 and that was when Emami doubled its offer to Rs 15,000 a share. Zandu ran out of options when CLB asked the two companies to try and settle out of court.

On October 3, Emami revised the offer to Rs 16,500 a share and, according to sources, this was when some of the Parikh family members evinced interest in quitting the company, saying they would not get a better price. Trade reports were released soon after, stating that Emami had entered into a share-purchase agreement with Zandu. Looking at the price that Emami paid for the deal — Rs 800 crore for a Rs-160 crore entity — it appears that dili-

or, worse still, thwart it," she adds.

Emami's persistence with the deal says something about what it expects from the acquired company. "At almost 5.5 times the sales multiple and almost 30 times EBIDTA (earning before interest, depreciation, tax and amortization) multiple, Emami is expecting stupendous growth from the Zandu franchise," says C Ravishankar, manager-strategic and commercial intelligence, transaction services, KPMG India.

Speaking to *the strategist* after the acquisition, R S Agarwal indicated that he expected Emami's FMCG business to touch Rs 1,100 crore by 2009-10. Harsh Agarwal, who has been overseeing the post-ac-

Emami to play a bigger role in the consumer goods market. Earlier this month, R S Agarwal and R S Goenka issued a statement saying that the company plans to position itself as a "food products and personal care major". Food products and personal care comprise the biggest slices of India's Rs 96,000 crore FMCG pie, accounting for 43 per cent and 22 per cent, respectively.

Marked markets

Emami has not yet announced the final product strategy but careful analysis seen in the light of recent announcements shows that its product portfolio is changing in

terms of the market size of each product category. Before Zandu came into the fold, Emami was the market leader in two niche categories: Boroplus cream, with 70 per cent, led the Rs 190 crore antiseptic creams market, and Navratna, with over 50 per cent, headed the Rs 397 crore cooling oil category. "Now, with the Rs 120 crore Zandu Balm in its fold," says Harsh Agarwal, "Emami leads the 'rubificient' (local pain ointment) category with a combined market share of more than 25 per cent... Zandu balm is the market leader and Mentholplus the strong third player, so both can continue without competing with each other. They can play complementary roles."

Similarly, the Rs 170 crore Cyawanprash category, dominated by Dabur Chyawanprash with 61 per cent share of the market, will see a bigger Emami footprint paved with Zandu Special, Sona Chandi and Kesari Jeevan, ayurvedic medicine, antiseptic creams

Harsh Agrawal sees Emami's consolidation in the classical ayurvedic medicine category as the biggest advantage of the deal. Indian over-the-counter herbal and ayurvedic medicine segment is estimated at Rs 7,500 crore. Dabur leads this segment with 10 per cent market share.

Emami and Zandu's combined product portfolio does not give Emami enough to stand up to the might of the Rs 2,360 crore Dabur, Rs 2,290 crore Marico or Rs 1,267 crore Glaxo Smithkline Consumer Healthcare India — much bigger FMCG players. Experts say Emami will take its first big step to becoming a serious player in the FMCG segment when it comes up with defined product architecture. AT Kearney India principal Debashish Mukherjee says an evolved product architecture, displaying a much bigger scope than its present "ayurvedic proxy" positioning will be the first critical step if Emami aspires to be an FMCG major. "Merely changing or rearranging the existing product categories will not put Emami into the big league," he adds.

Mukherjee adds that unless herbal or ayurvedic consumer goods players hit mass retailing, they can't hope to challenge serious FMCG players such as Hindustan Unilever or Procter and Gamble. Smaller players, such as, Emami will have to think of ways to gain access to product categories they can't reach. Product improvisation, customisation, even price variations can help. Emami's Chyawanprash product range, for instance, could see price variations with the inclusion of Kesari Jeevan, which is in the premium consumer segment. Similarly, the rubificient range can see price differentiations.

The market is in the villages

Categories such as health supplements and cooling oil have a huge untapped potential in the urban and rural markets. The Rs 600 crore health supplement market has a surprisingly low penetration level of 0.2 per cent in rural and 1 per cent in the urban markets. Similarly, cooling oil has a huge potential in the rural market. With the increased media reach, Emami has a big market waiting to be explored, and it can only be reached through a wide and efficient distribution network.

The cooling oil category has few rivals, all of them local players (Dabur Super Thanda, Himange, Himtaj). Emami's substantial advertising and promotions spending — more than 20 per cent of sales every year, much higher than the FMCG industry average of 11-12 per cent — can provide the beachhead.

Emami has a strong sales network of 2,800 distributors with direct supply to 400,000 retail outlets and a product reach of 2.6 million outlets across India. Urban distribution channels cover modern format outlets and retail stores and rural sales channels include Emami mobile traders and Emami small village shops.

Emami has also tied up with ITC e-Chaupals, Indian Oil Corporation petrol pumps and the India Post network. Moreover, it has five sales channels divided into rural and urban areas. Unlike Zandu's distribution channels, which were strong in the West and South, Emami's network is evenly spread out in all regions of the country.

Third Eyesight chief executive Devangshu Dutta says growth in the smaller towns and rural markets can still be driven by penetration and improved availability levels of stock-keeping units. There are still vast swathes of consumers in India whose consumption of packaged skin and personal care products is negligible. The main causes of optimism about continued growth would stem from this aspect of untapped markets and unfulfilled demand."

An AC Nielsen report for April-September 2008 showed that value and volume growth across a range of products, such as, skin creams, lotions and hair oils, was much higher in the rural markets than in urban markets.

Citing Hindustan Lever's Shakti Amma initiative, Dutta says if Emami can map the two portfolios (of Emami and Zandu) on each other's distribution channels, sales could rise quickly. Is the promoter duo ready for the new journey? 