



DEAL CHECK FOR RESTRUCTURING CURRENT JV

THE CLIENT

- Large US industrial company
- Majority equity partner in manufacturing and sales joint venture for important product line

THE NEED

- Considering consolidating JV into another business with Partner B
- Business Development team wanted outside view on proposed deal structure and negotiating strategies

OUR SOLUTION

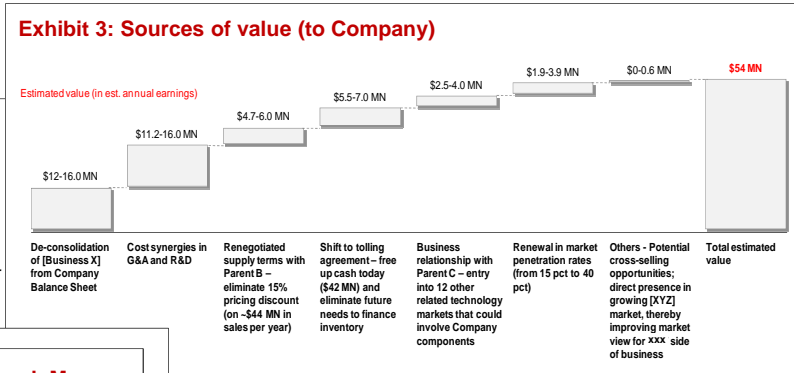
- Reviewed team’s work and key legal agreements
- Facilitated 3 working sessions to understand deal objectives, constraints, team’s underlying assumptions about synergies (and dis-synergies)
- Developed “expert opinion” – 15 page note + 10 exhibits illustrating where proposed deal might be analyzed or structured differently
- Worked with BU President to develop strategy for Round 1 of deal negotiations

Summary memo and exhibits

Exhibit 1: Key deal design principles and implications

Key deal design principles

- Maximize EBITDA of both businesses
- Partners should benefit proportionately from changes – no asymmetric costs or benefits
- Protection of fixed (manufacturing)



Deal Check Memo

Therefore, the sizing of synergy estimates needs to be pressure-tested. Cost synergies on sales-force and R&D also may be challenging to capture in the context of a larger base of customers (Exhibit 2)

- A number of the largest synergies are unique to Company (e.g., renegotiating Partner B supply agreement terms, de-consolidating existing JV from Partner A balance sheet), suggesting that Company may be gaining more than its partners (not necessarily a bad thing, but worth noting).
- Partner C also has significant potential asymmetrical returns in so far as combination creates stronger market position and drives ZZZ contracts
- Likewise, some of the larger synergies (e.g., shift to tolling agreement, renegotiated supply terms with Partner B) do not require Newco JV structure to capture. This suggests that a simpler marketing agreement plus renegotiated supply contract may represent an alternative deal structure or a first phase in a wider set of changes

Key questions to probe in negotiations and deal making

- Revenue-side synergies and new value proposition to customers:
 1. Why is X Business not as successful as its competitors in making second-time/retention sales (50 pct. market share on first sale, 20 pct. on second sale / retention)?
 2. How valuable is bundled offer, given that customers are accustomed to the current setup?
 3. Who are the highest-likelihood, large customers that will switch / add volume on the refill / second sale side? Who do they purchase from today?
 4. How long will it take to penetrate additional customers, given the approximately 3 year cycle and embedded competition?
 5. Will taking share from Axelrod and Athens require price reductions, resulting in lower margins?
 6. Potential approach: Interviews with 8-12 current and non-current customers to understand why X Business second-sale penetration rate is so low, and if, why, and what changes to sales model (including integrating JV and Business Y) will likely affect this penetration rate

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Exhibit 8: Key levers to exercise influence as a minority partner in the Newco JV

Key terms for Company to exercise influence as a minority partner in JV

- Decision rights**
 - Overall governance philosophy: “All Equal” (33x3), despite different equity interests
 - Equal # of Board seats (3 per partner)
 - Certain decisions require unanimous approval, e.g.,
 - Annual operating plan, budget, and sales plan
 - Supply or service contracts with any parent or affiliate
 - Capex decision above \$5M [plus opt-in/opt-out provisions]
 - Changes to sales plan or incentive structure
 - Other decisions require majority approval, e.g., compensation of top 10-15 executives
- Board and decision making**
 - Pre-agreement on Y1 budget and 3-year business plan and capital plan
 - Decisions where Company has casting vote: (see list on next page)
 - Pre-agreement on principles for making key decisions (e.g., sales rules for technology vs. product sales)
 - Appointment of independent member to Newco Board – to promote interests of the JV (rather than on parent)
- Reporting and reviews**
 - Contractual guaranteed Company access to defined Newco financial and operating data – e.g., monthly financial statements, sales data, R&D spending and time allocation, etc.
 - “Open Books” agreement – all partners have same level of access to information
 - External auditors required to annually review JV business, affiliated-party transactions, etc.
 - Company right to lead or participate in annual shareholder audit of Newco (general business and operational review – not a financial audit), or initiate specific functional reviews (e.g., technical services, product development, talent policies)
 - Newco adoption of Company sales/CRM system, IT platform and overall reporting systems (or at least not Partner system)