

# The Looming Exit Crisis – Finding a Way Out

**APEX'14**  
SUMMIT

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This document presents an overview of the PE/VC investment and exit scenario in India based on analysis of data from Venture Intelligence and inputs from industry participants. The data we have analysed excludes Real Estate deals.

The IRR computations presented in the slides are an aggregate view based on available data for about 60% of the deals. The IRR calculations also do not take into account the interim pay-outs such as dividends and refer only to the initial investment and exit value.

We thank Venture Intelligence for the data support without which this analysis would not have been possible.

## Executive Summary

PE Exits in India have had two distinct Phases in the past decade of investments:

- **"India Shining" Phase from 2004 to 2009** – ~ Rs. 32,000 cr. of invested capital exits characterised by faster exits (mostly <3 years), higher returns (30-60% IRR) and exits mainly through Primary Market Sale or IPO and negligible Buy Back. Investments also had a larger share of PIPE deals during the early part of this Phase with IT/ITES being a large sector both for investments and exits
- **"Melting Pot" Phase from 2010 to 2013** – ~ Rs. 52,000 cr. of invested capital exits characterised by slower exits (mostly > 4 years) and lower returns (~15% IRR), exits mainly through Secondary Sale and a reasonably large share of Buy Back. Investments were more fragmented across sectors and witnessed volatility in line with the economic scenario

Exits are about to enter into a third and most challenging Phase:

- **"Looming Logjam" Phase from 2014 onwards** – ~ Rs. 85,000 cr. of 6+ years invested capital waiting to exit, will be characterised by even slower exits (mostly >6 years) yielding even lower returns mainly through Secondary Sale / Buy Back. Specific sectors IT/ITES, Energy, Engineering Goods and Auto be most impacted

Successful exits will call for a more 'interventionist' approach from PEs – pursuing specific, relevant, time bound and rigorously implemented Value Enhancement initiatives with Management. Several examples of such exits from the past demonstrate the way ahead

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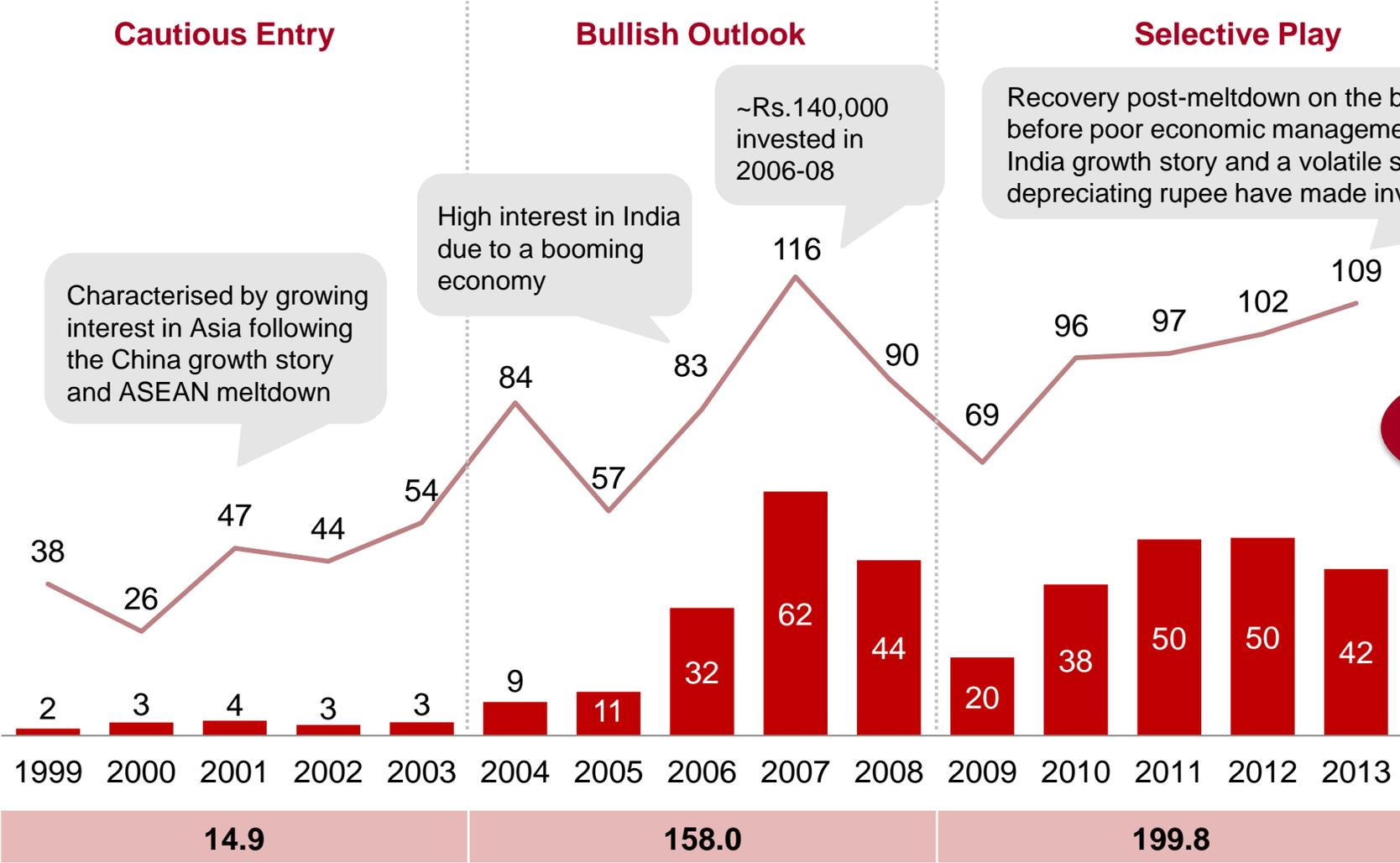
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Successful exits will call for a more 'interventionist' approach from PEs – pursuing specific, relevant, time bound and rigorously implemented Value Enhancement initiatives with Management. Several examples of such exits from the past demonstrate the way ahead

# PE investments in India have seen three 5-year periods since 1999, each unique in their environment and the level of investments which peaked to ~ Rs. 62,000 Cr. in 2007 when India's growth story was at its highest pitch

VC/PE Investments in India (Rs. '000 Cr.) ■ Investments (INR '000 Crore) — Avg size of deals (INR Crore)



**Σ ~Rs. 373,000 Cr.**

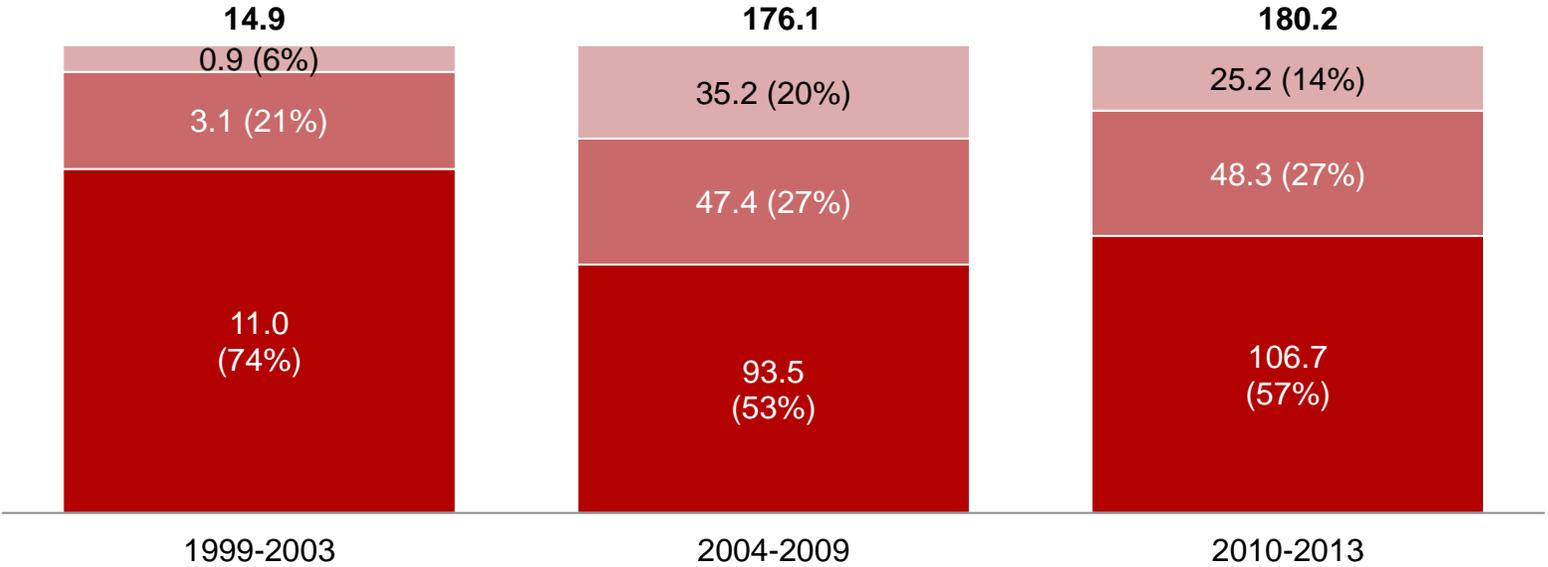
**Cumulative Investments in the Period ('000 cr.)**

Source: Venture Intelligence Data, Avalon Consulting Analysis

# Most of these investments have been raised outside India in foreign currency due to tax advantages. Hence exit returns have to overcome the natural hurdle posed by Rupee depreciation which has been substantial in recent years

VC/PE Investments in India by Source of Funds (Rs. '000 Cr.)

■ Foreign ■ India Dedicated ■ Co-Investment



India dedicated investments have remained relatively steady in absolute terms



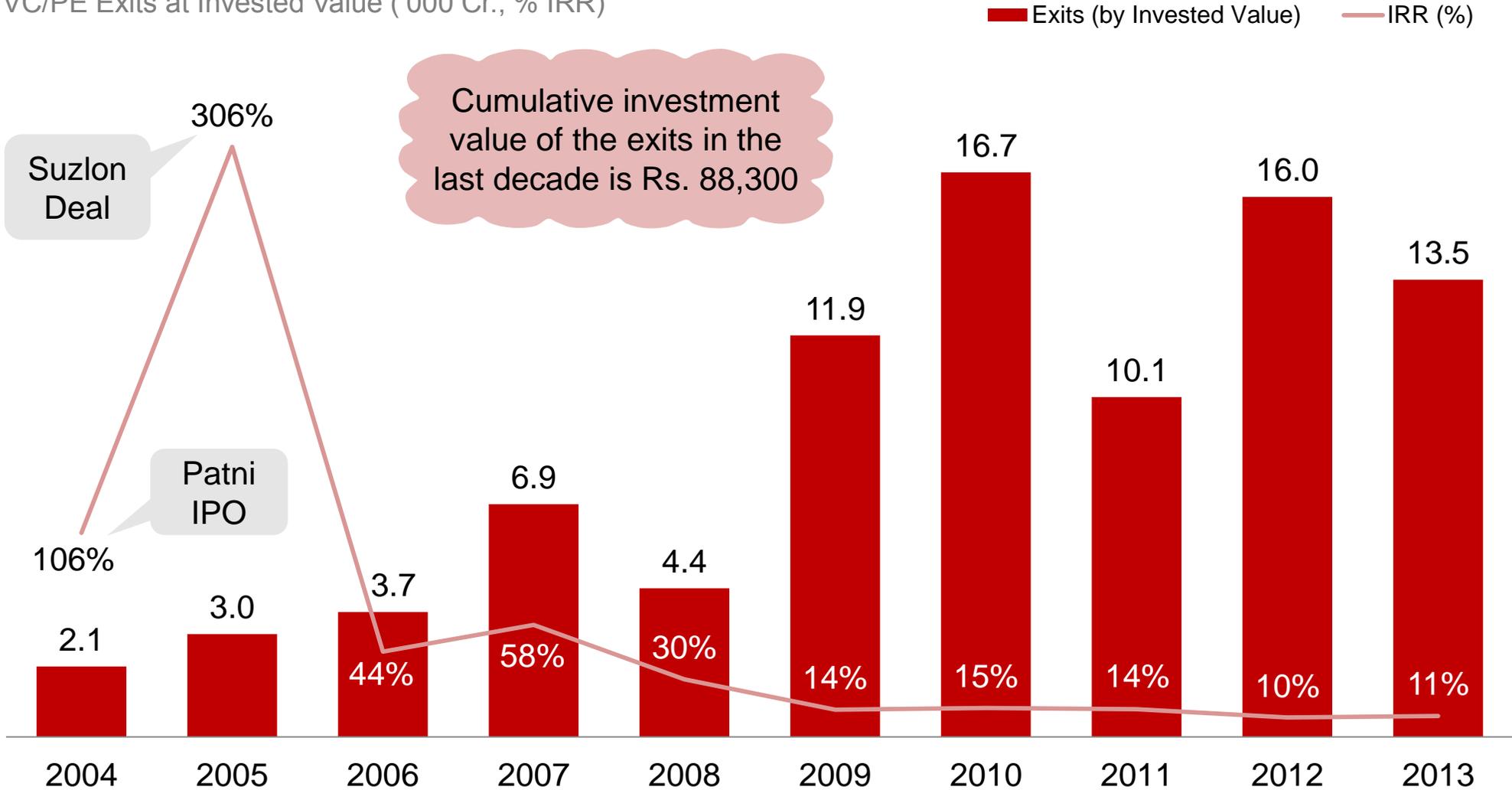
The 2010-13 period was characterised by a highly volatile and depreciating Rupee

Between 2004-07, the Rupee seem to be appreciating, which made India attractive for investments

Source: Venture Intelligence Data, Avalon Consulting Analysis

Over Rs. 88,000 cr. of the invested capital has managed exits from 2004 with reasonably good IRRs till 2008. Exits have increased since 2009 but IRRs have plummeted in recent times

VC/PE Exits at Invested Value ('000 Cr., % IRR)

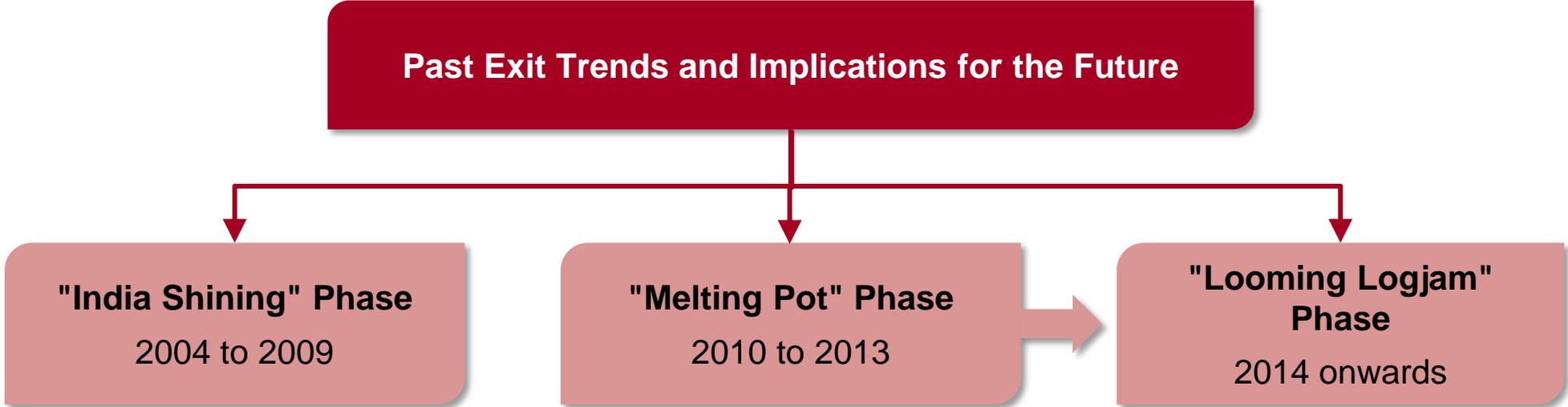


Source: Venture Intelligence Data, Avalon Consulting Analysis

However, this overall scenario masks two distinct Phases of exits in the past and portends a third and most difficult Phase from 2014 onwards

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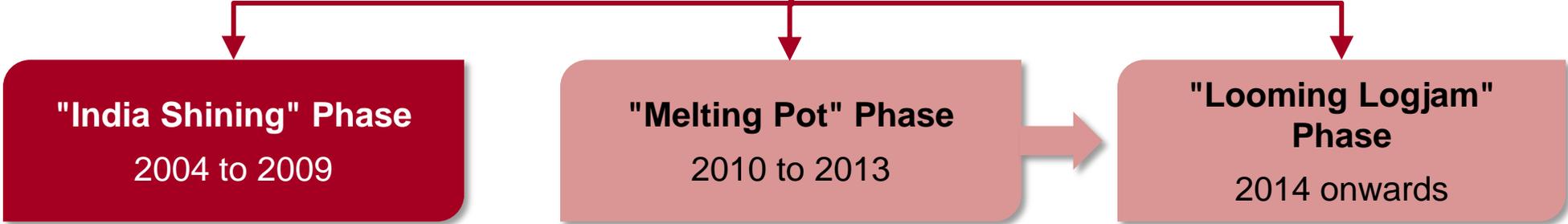
**Past Exit Trends and Implications for the Future**



# Let us look at the India Shining Phase

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## Past Exit Trends and Implications for the Future

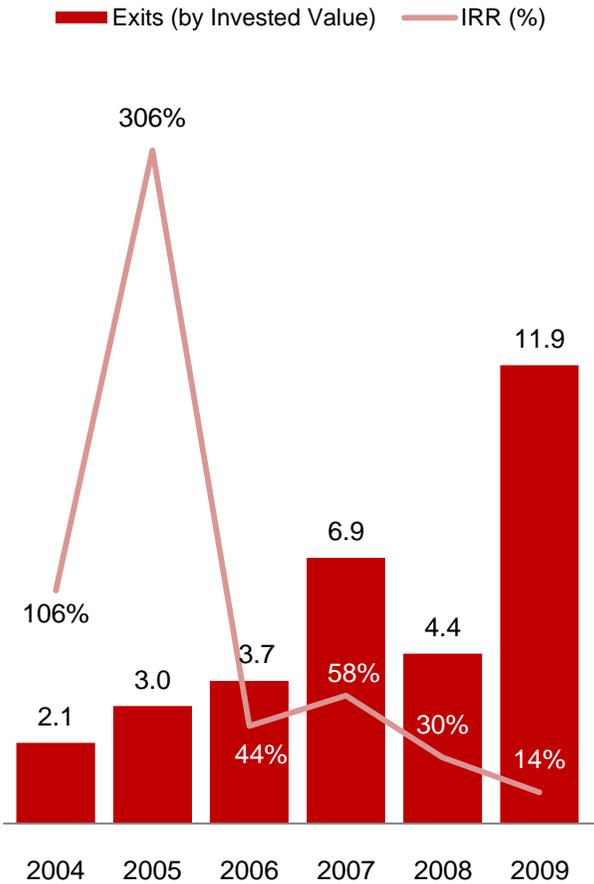


# ~Rs. 32,000 cr. of invested capital exited in the India Shining Phase with a large share of these exits being < 3 years at attractive IRRs irrespective of the years invested

## India Shining Phase Exits and IRR (Rs. '000 Cr. / %)

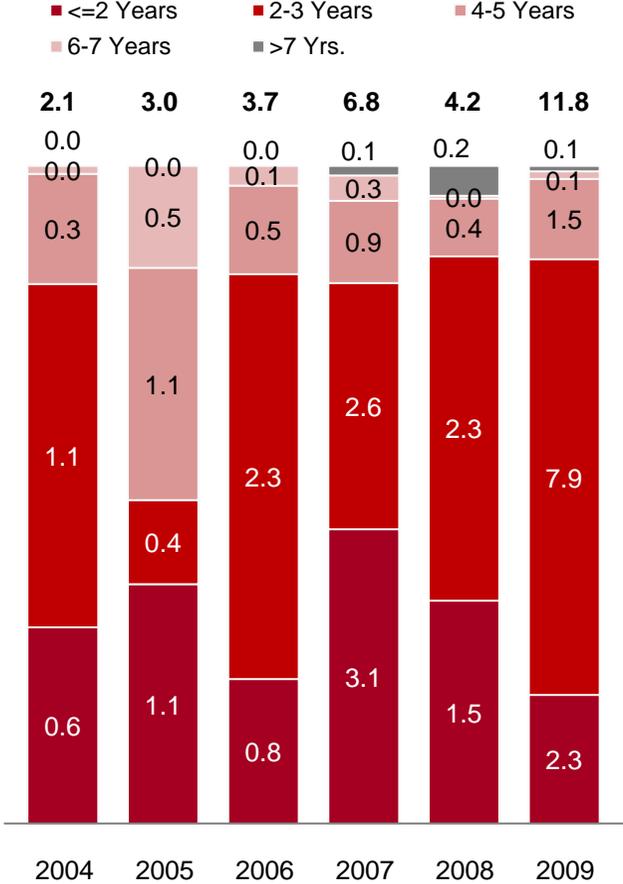
About Rs. 32,000 cr. of invested capital managed exits...

2004-2009 Exits (Rs. '000 Cr.)



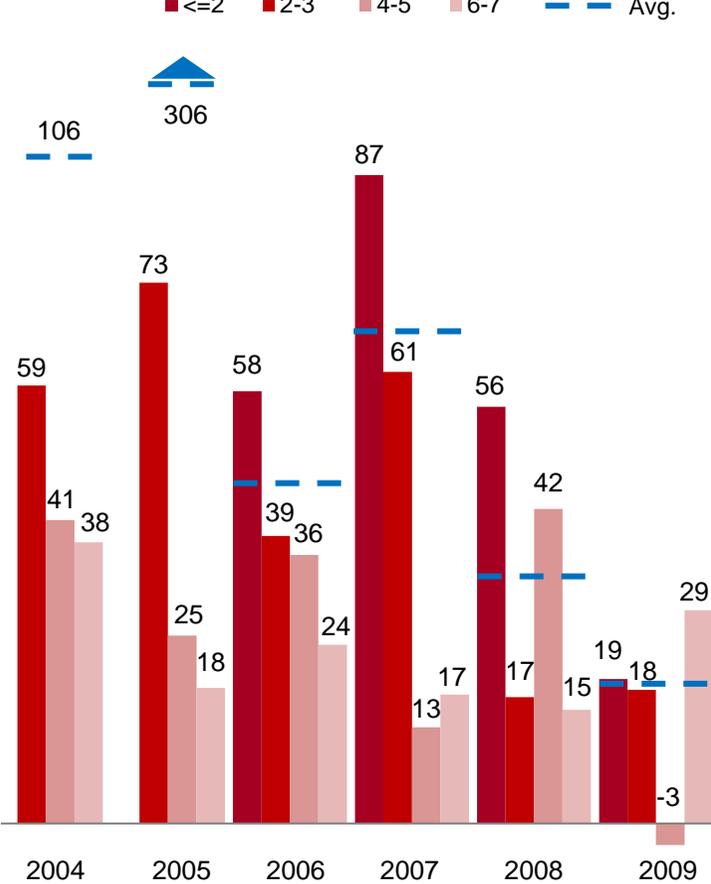
... with most of them being in < 3 years ...

2004-09 Exits at Investment Value (Rs. '000 Cr.)



... and at attractive IRRs irrespective of the holding period

2004-09 IRR by Age at Exit (%)



Source: Venture Intelligence Data, Avalon Consulting Analysis

# A larger share of these exits have been through the Primary Market or IPO on the back of a high share of PIPE deals in the investments and the bull run in the stock markets

India Shining Phase Type of Exits (Rs. '000 Cr. / %)

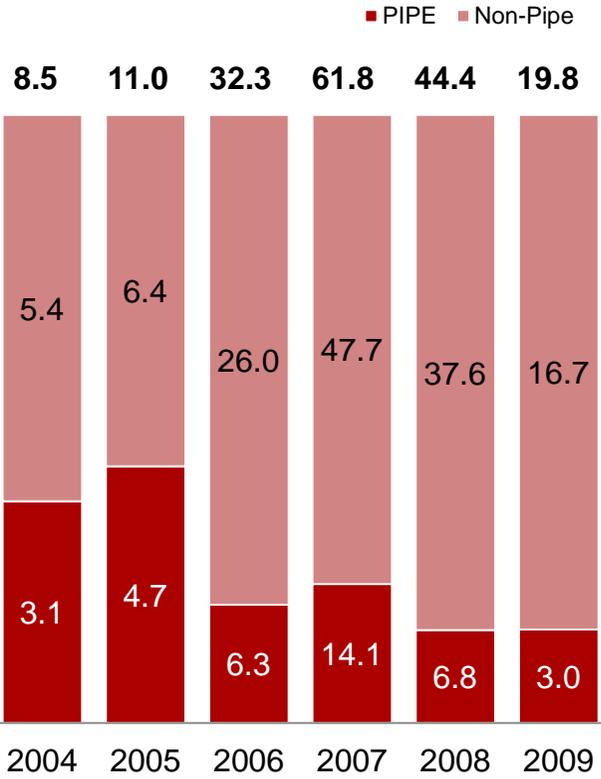
**The 2004-09 period was characterised by a bull run till 2007, followed by volatility in 2008 & 09**

2004-09 Stock Market Trends (BSE Sensex)



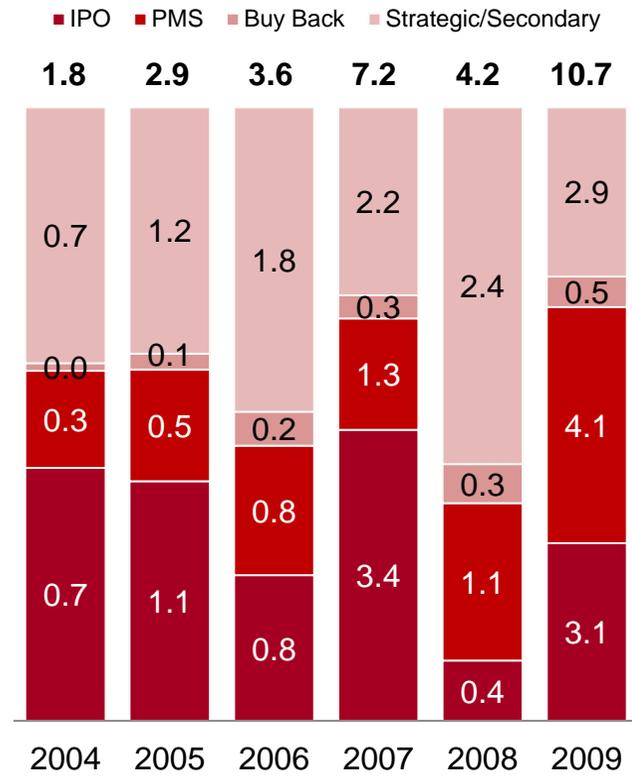
**Investors seem to have sensed the stock market boom given the high share of PIPE deals in the 2004-05 period**

2004-09 Investments by PIPE vs. Non-PIPE (Rs. '000 Cr.)



**Consequently, most of the exits in this period were as IPOs and PMS**

2004-09 Exits by Transaction Type (Rs. '000 Cr.)



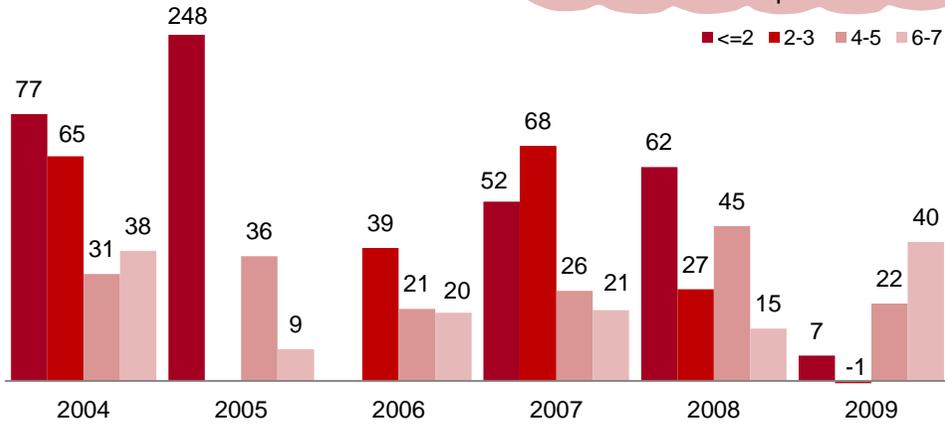
Source: Venture Intelligence Data, Avalon Consulting Analysis



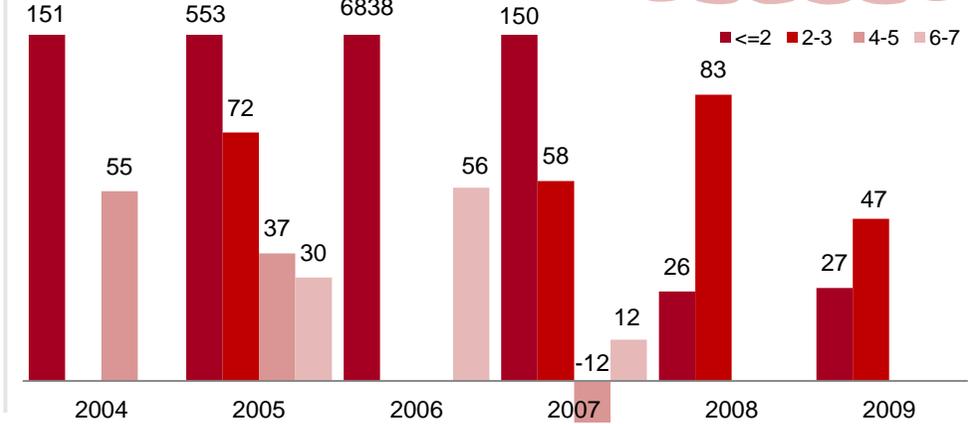
# The IRRs of the these exits and even through secondary sale have been attractive irrespective of the period invested

## IRRs by Exit Type (%)

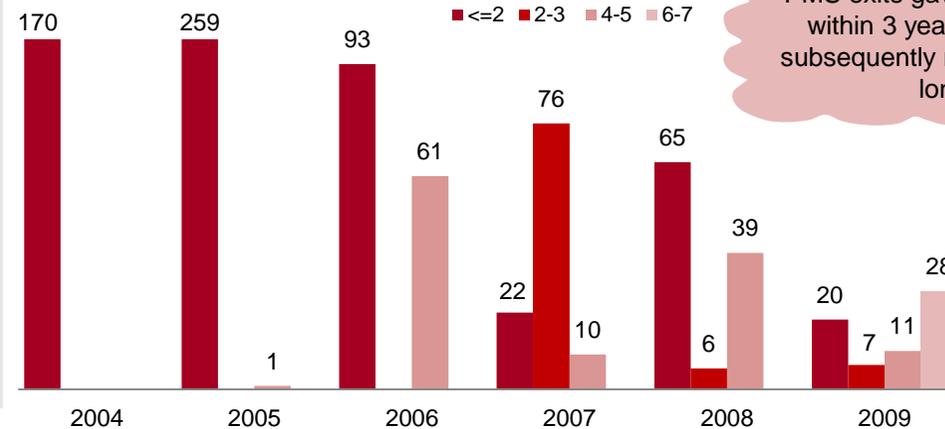
### Strategic/Secondary (%)



### IPO (%)



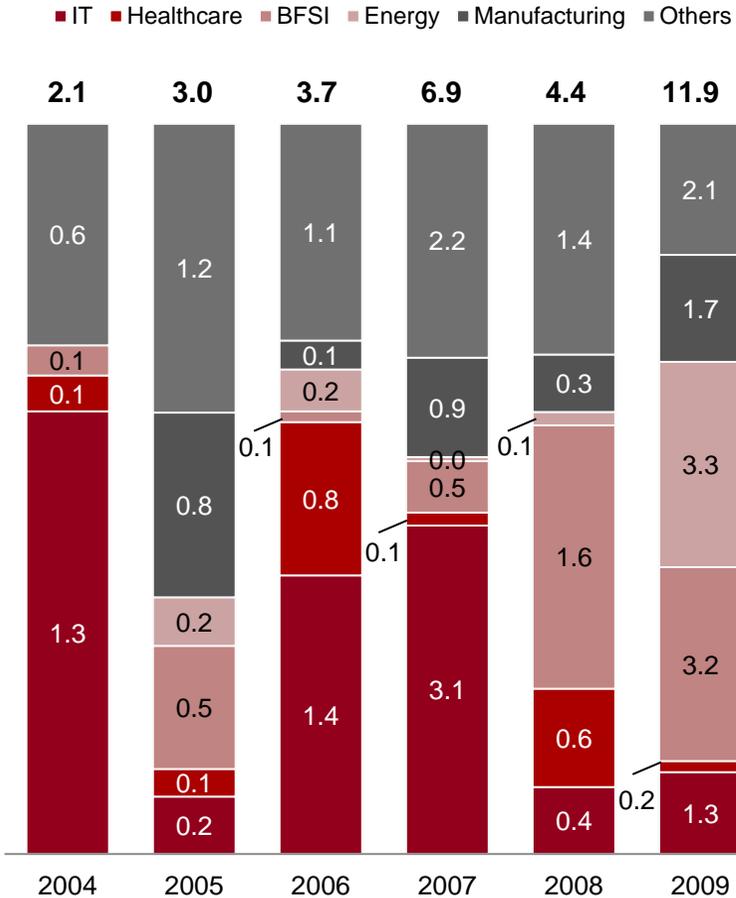
### PMS (%)



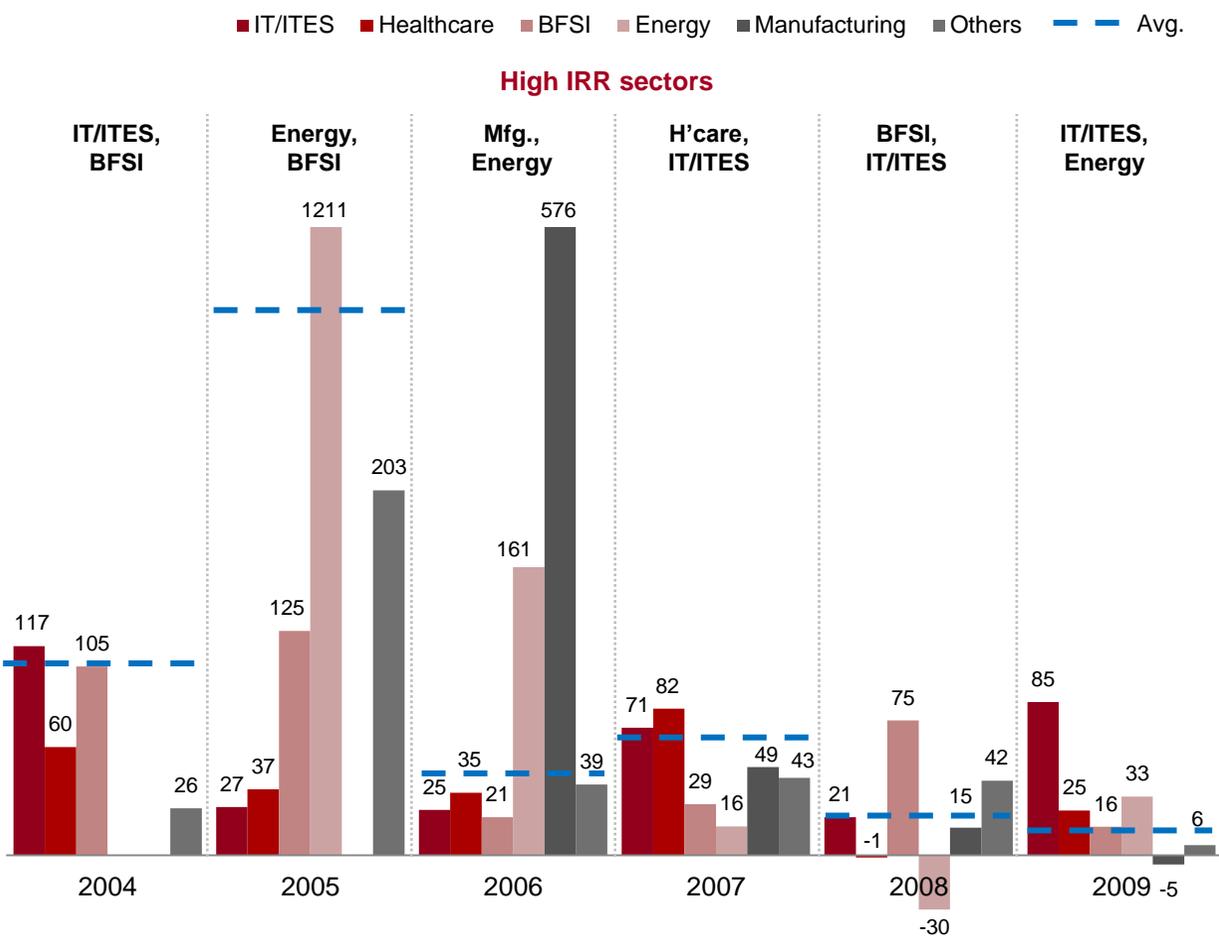
# In the “India Shining” phase, IT/ITES, BFSI and Energy were the key sectors which had exits; these sectors also delivered high IRR on investments across many years in this period

## India Shining Phase Sector Performance

### Exits by Sector at Invested Amount (Rs. '000 Cr.)



### IRR of Exited Investments in the Year (%)



Source: Venture Intelligence Data, Avalon Consulting Analysis

## Thus the India Shining Phase was the dream run for PE exits in India

### Past Exit Trends and Implications for the Future

#### "India Shining" Phase

2004 to 2009

- ~ Rs. 32,000 cr. of invested capital exits characterised by faster exits (mostly <3 years), higher returns (30-60% IRR) and exits mainly through Primary Market Sale or IPO and negligible Buy Back.
- Investments also had a larger share of PIPE deals during the early part of this Phase with IT/ITES being a large sector both for investments and exits

#### "Melting Pot" Phase

2010 to 2013

Let us  
look at  
the Melting  
Pot Phase

#### "Looming Logjam" Phase

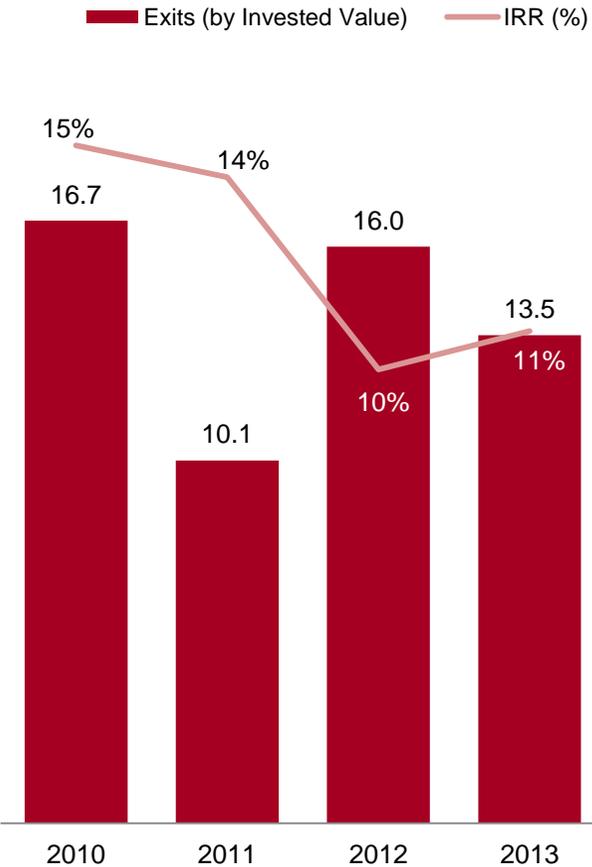
2014 onwards

# ~Rs. 53,000 cr. of invested capital exited in the “Melting Pot” Phase. However most of these exits were in the normative 4-5 years but at more sober IRRs

Melting Pot Phase Exits and IRR (Rs. '000 Cr. / %)

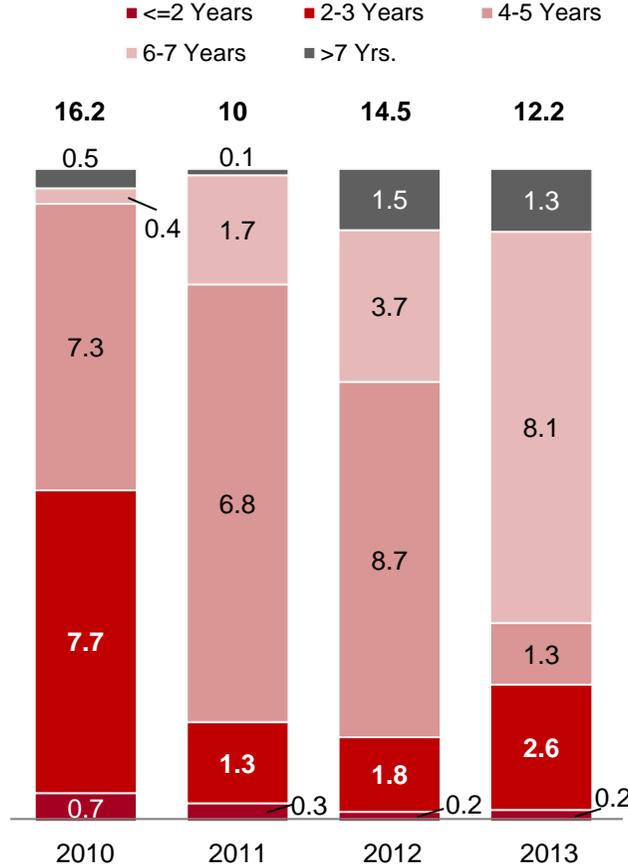
~Rs. 53,000 cr. on invested capital exited with 2010 being a peak...

2010-2013 Investments (Rs. '000 Cr.)



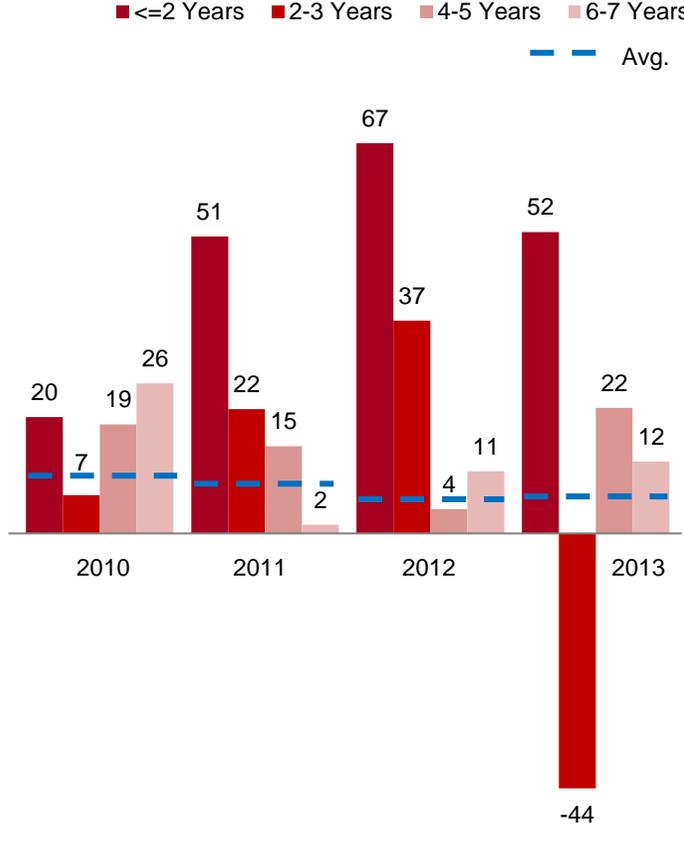
... but most of the exits were >4 years across these years....

2004-09 Exits at Investment Value (Rs. '000 Cr.)



...with IRRs >20% being exceptions only in a few deals with <2 year exits

2004-09 IRR by Age at Exit (%)



Source: Venture Intelligence Data, Avalon Consulting Analysis

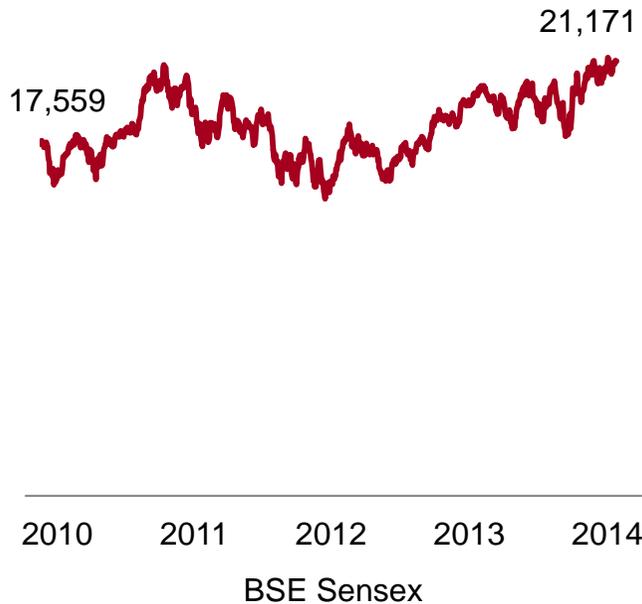


# A larger share of these exits have been through the Primary Market though Buy Backs were also more prominent in this period. Given the volatility in the stock markets, the share of PIPE deals continued to be low

Melting Pot Phase Exit Types (Rs. '000 Cr. / %)

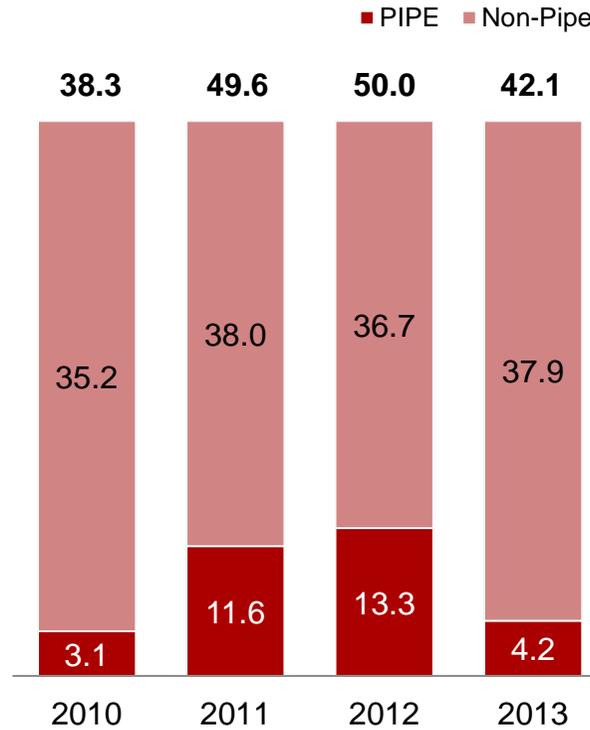
The 2010-14 period was characterized by volatility of stock markets though the markets recorded growth...

2010-2014 Stock Market Trends (BSE Sensex)



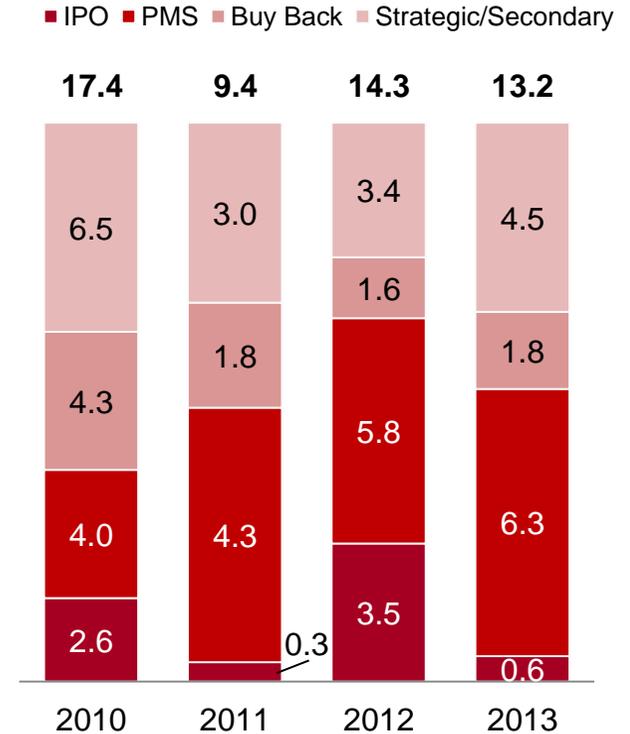
Leading to irregular trends in the PIPE deals, which eventually contributed to drop in overall investments in 2013

2010-14 Investments by PIPE Vs. Non-PIPE (Rs. '000 Cr.)



However primary market exits were still high in this period; the non-PIPE deals on the other hand had difficulty in exits

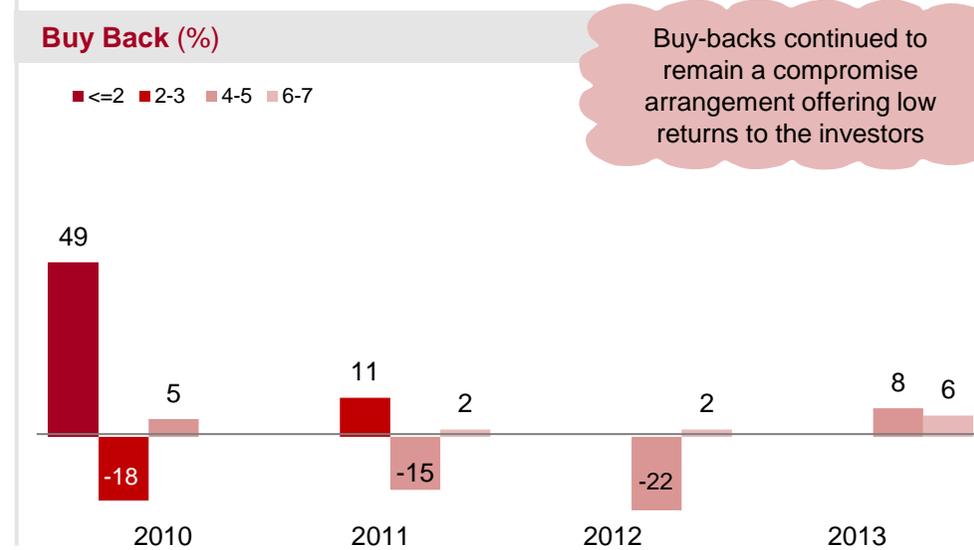
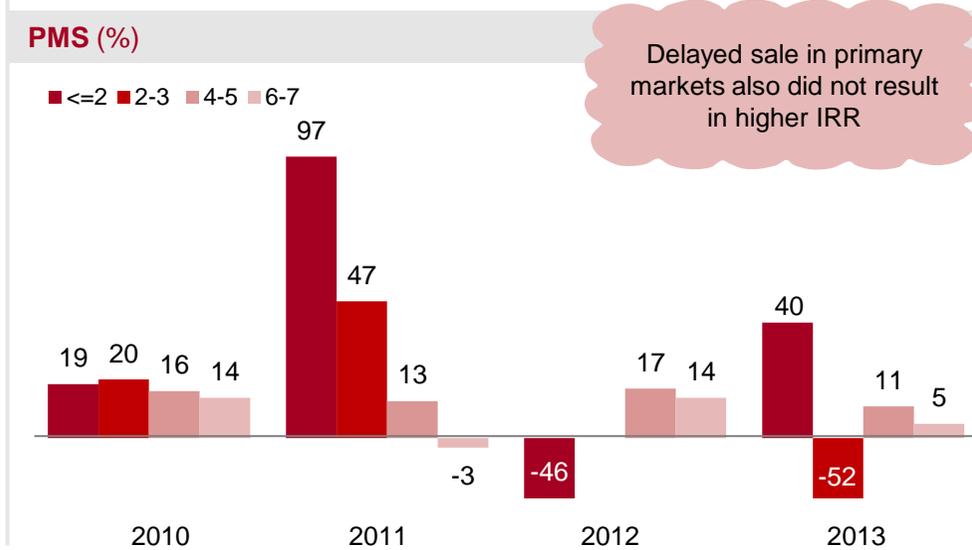
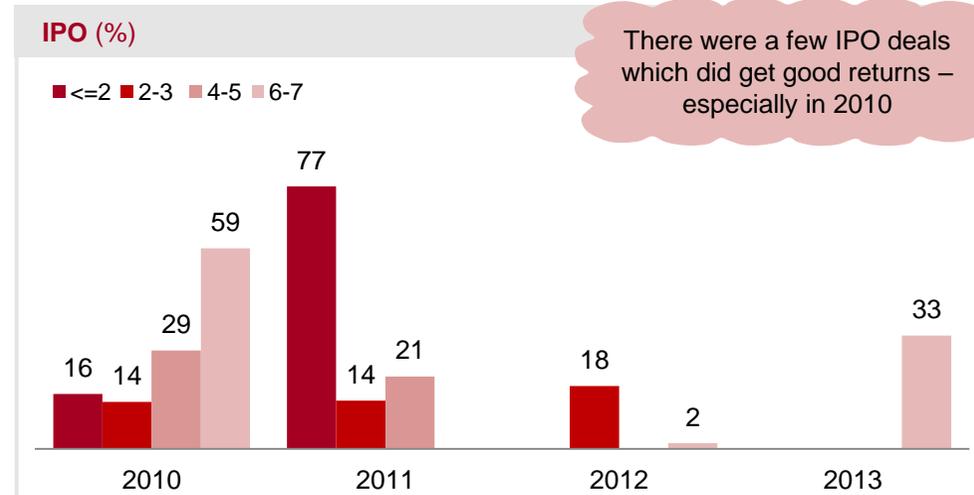
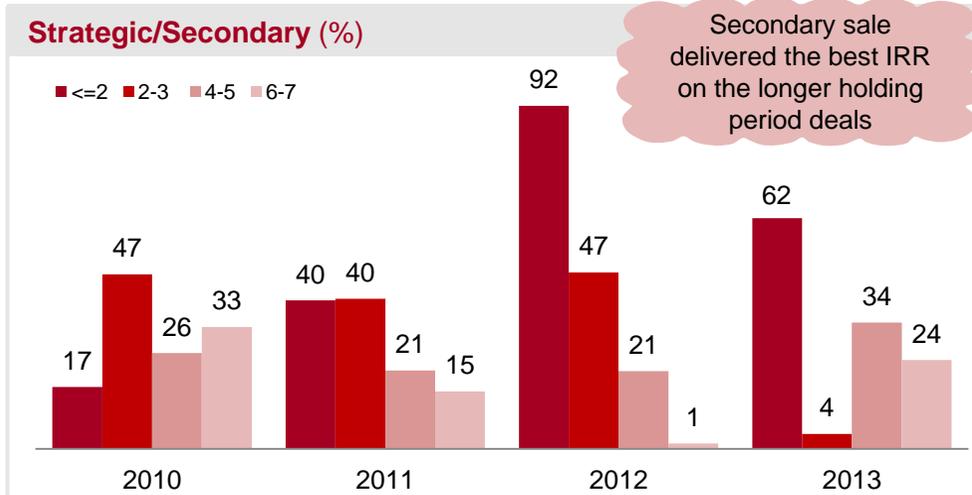
2004-09 Exits by Transaction Type (Rs. '000 Cr.)



Source: Venture Intelligence Data, Avalon Consulting Analysis

# However, most of these PMS of longer periods delivered low IRRs. Buy backs also reflected a poor performance while secondary transactions for longer holding period deals performed credibly

## Melting Pot Phase IRRs by Exit Type (%)

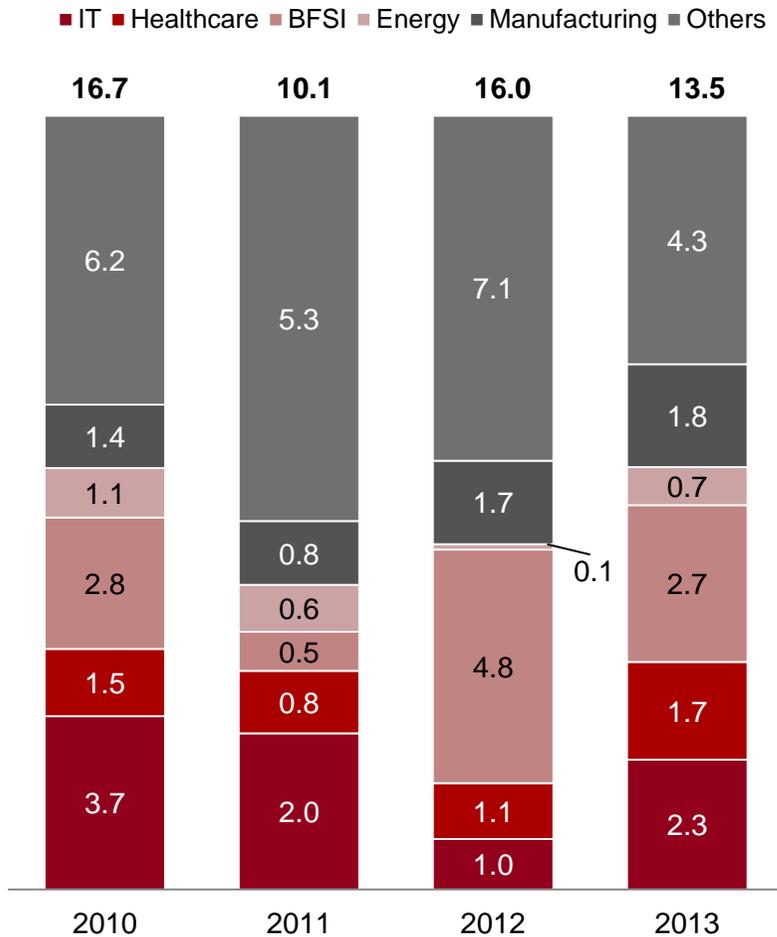


Source: Venture Intelligence Data, Avalon Consulting Analysis

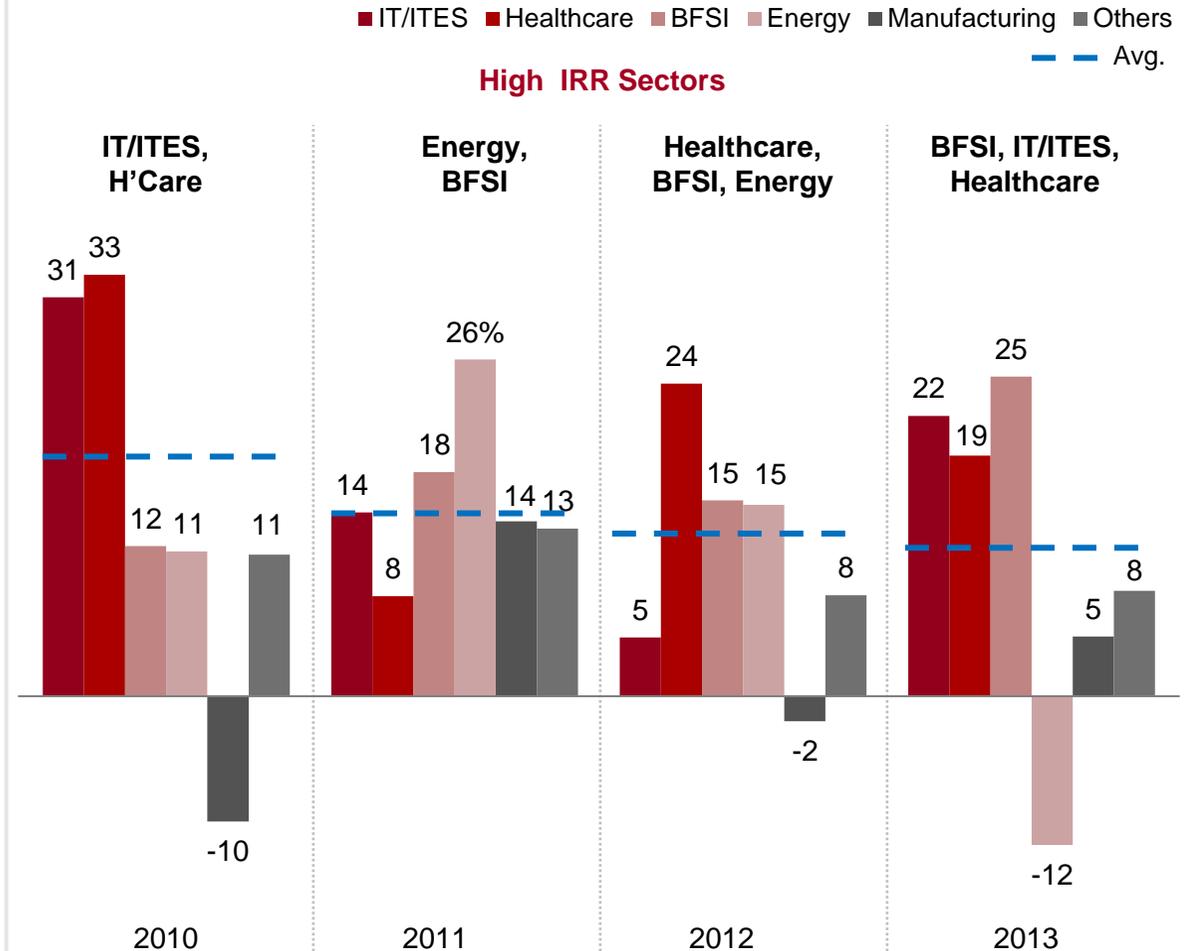
# In the “Melting Pot” phase, the prominence of IT/ITES exits was low, while sectors like BFSI gained share and delivered high IRRs. The fragmented Other sectors underperformed

## Melting Pot Phase Sector Performance

### Exits by Sector at Invested Amount (Rs. '000 Cr.)



### IRR of Exited Investments in the Year (%)



Source: Venture Intelligence Data, Avalon Consulting Analysis

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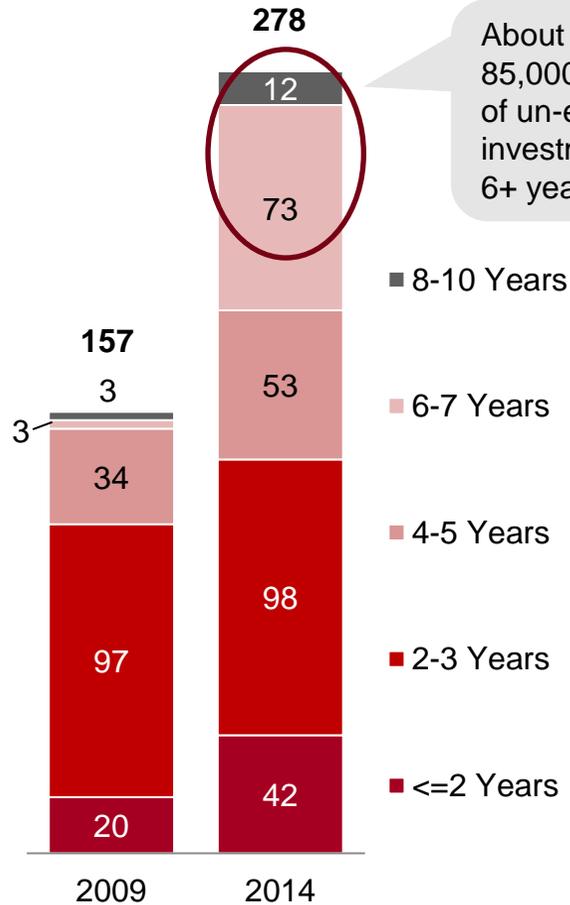
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Successful exits will call for a more 'interventionist' approach from PEs – pursuing specific, relevant, time bound and rigorously implemented Value Enhancement initiatives with Management. Several examples of such exits from the past demonstrate the way ahead

# An unprecedented ~Rs. 85,000 cr. of invested capital of 6+ years is waiting to exit – nearly equal to 10 years' exits, and 5 times the total quantum exited in any year in the recent past

Net (Un-exited) PE/VC Investments at the Beginning of the Year ('000 Cr.)

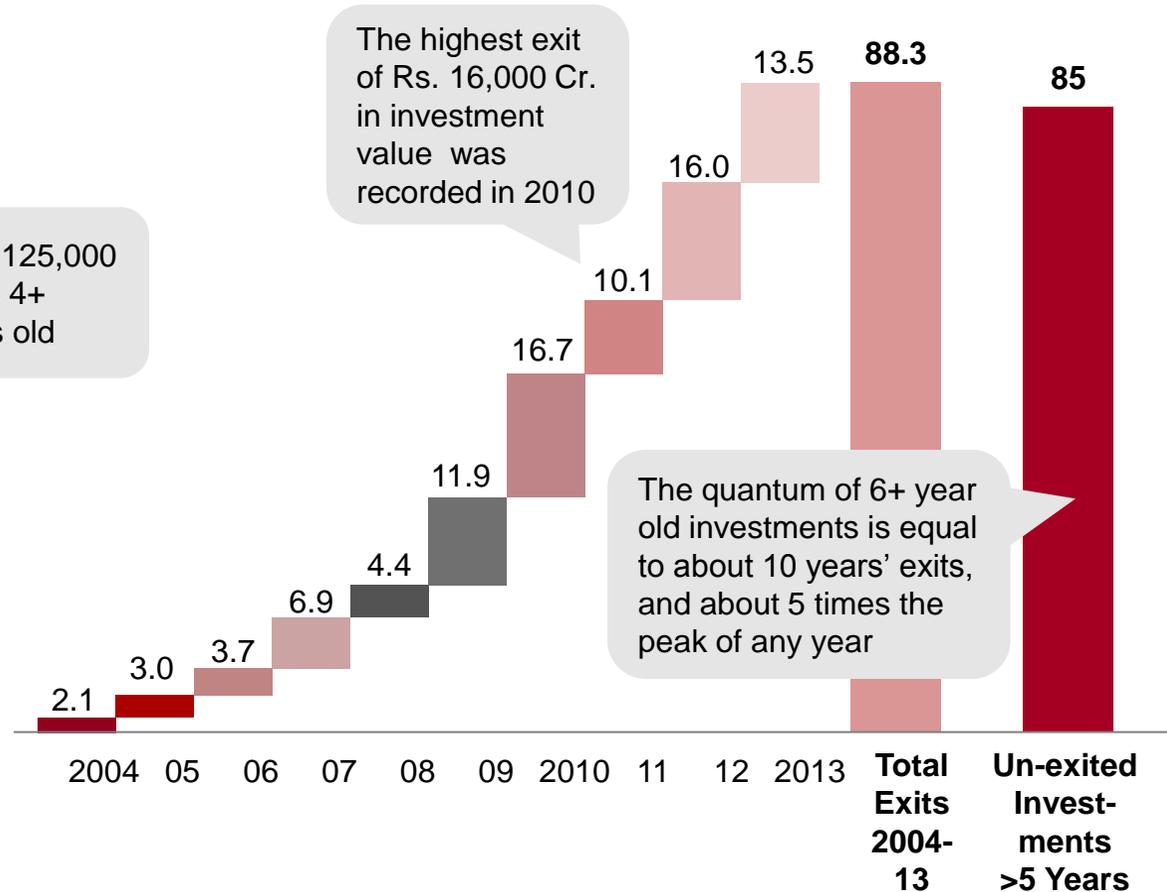
## Un Exited PE Investments ('000 Cr.)



About Rs. 85,000 Cr. of un-exited investments is 6+ years old

~Rs. 125,000 Cr. is 4+ years old

## VC/PE Exits in Investment Value ('Rs. 000 Cr.)

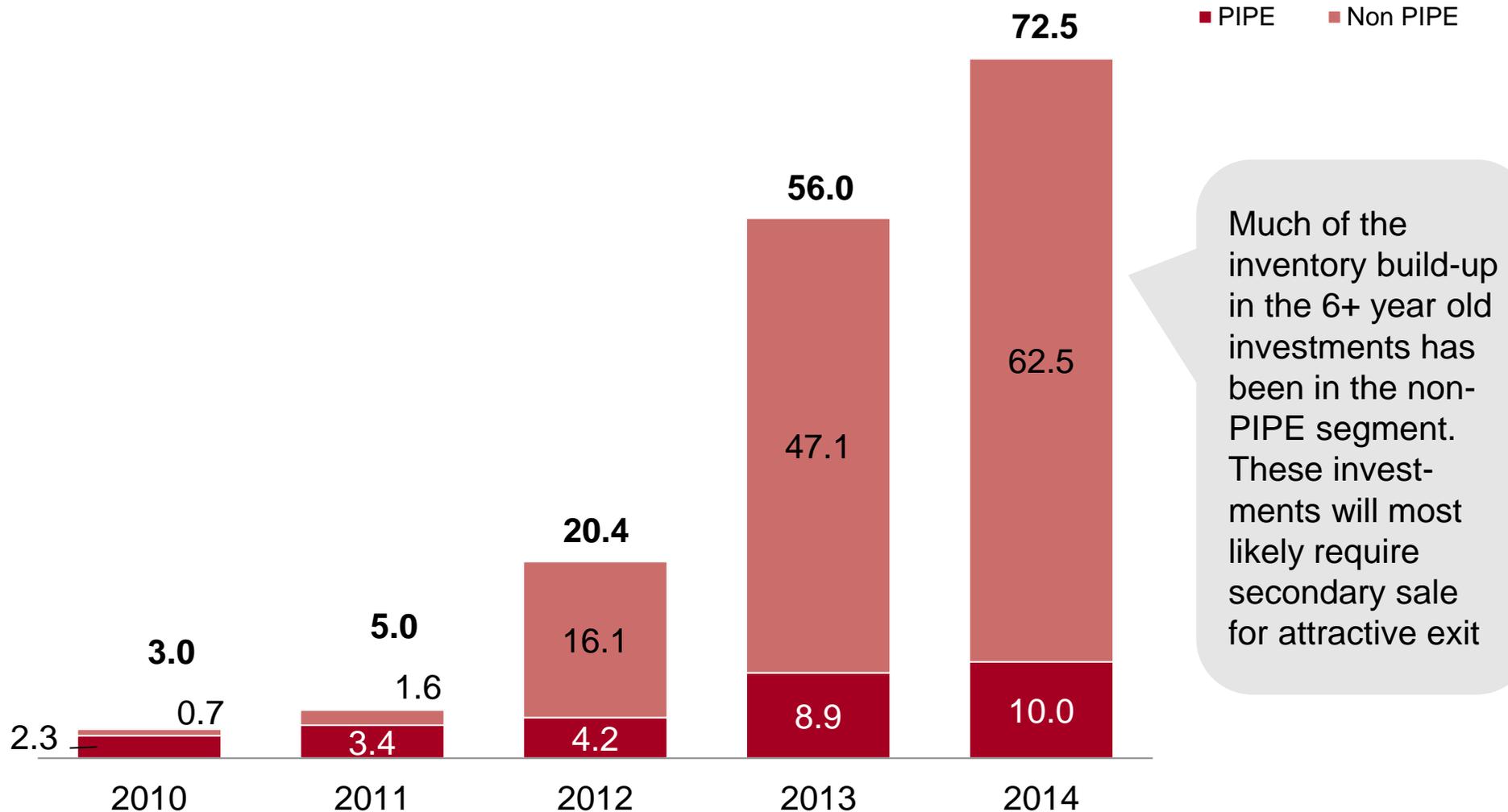


The highest exit of Rs. 16,000 Cr. in investment value was recorded in 2010

The quantum of 6+ year old investments is equal to about 10 years' exits, and about 5 times the peak of any year

# A large share of the invested capital waiting to exit is in non-PIPE transactions, most likely requiring a secondary sale to exit

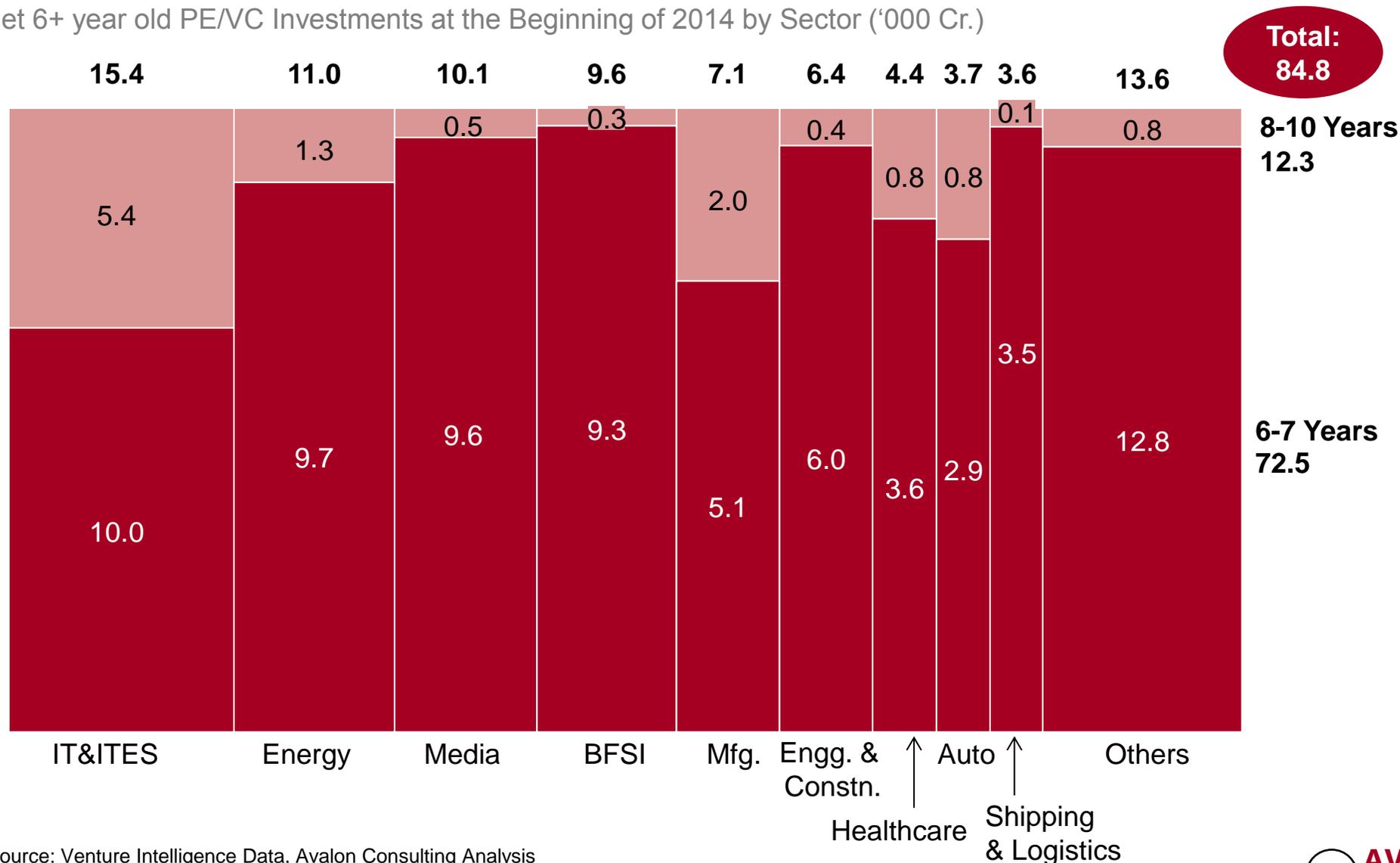
Breakdown of 6+ Year Old Net (Un-Exited) Investments in 2014 by PIPE Vs. Non-PIPE ('000 Cr.)



Source: Venture Intelligence Data, Avalon Consulting Analysis

# These investments are spread across a number of sectors with IT/ITES, Energy, Media, BFSI and Manufacturing having to perform well for the exit scenario to improve

Net 6+ year old PE/VC Investments at the Beginning of 2014 by Sector ('000 Cr.)



Source: Venture Intelligence Data, Avalon Consulting Analysis

# Given the state of the economy and the impending uncertainty, the prospects for most of these sectors in the future look weaker than the past....1

## Key Sectors: Past Growth Trends and Medium-term Outlook

Sector	Growth Rate (% CAGR)			Rationale
	2004 - 2009	2010 -2013	2014 - 18 (E)	
IT/ITeS	20	17	16	<ul style="list-style-type: none"> <li>The depreciation in the rupee and the slow recovery of the US and Europe markets will mean the recent momentum could be maintained and as a sector and exits could be attractive</li> </ul>
Energy	9	10	8	<ul style="list-style-type: none"> <li>Growth will be driven by recovery of the Indian economy which looks tough in the short term</li> <li>Energy pricing in a regulated environment and political uncertainty will remain a dampener for this segment in the medium-term</li> <li>The expectations from this sector was high double-digit growth, which is unlikely</li> </ul>
Media and Entertainment	14	12	8	<ul style="list-style-type: none"> <li>Rise in Ad spends, TV Subscription and movies will drive the growth of the sector in the medium term</li> <li>New delivery models using the internet as a medium will emerge stronger and investments in these new models will find exciting exits</li> </ul>
BFSI	21	17	15-17	<ul style="list-style-type: none"> <li>Short term pain expected with loan restructuring and NPAs. Continued rural expansion through new branches and business correspondent models</li> <li>New banking licenses and increased competition could result in mergers among existing players</li> <li>Insurance penetration will be a major growth driver</li> </ul>

Source: Avalon Consulting Research & Analysis

## Given the state of the economy and the impending uncertainty, the prospects for most of these sectors in the future look weaker than the past....2

### Key Sectors: Past Growth Trends and Medium-term Outlook

Sector	Growth Rate (% CAGR)			Rationale
	2004 - 2009	2010 -2013	2014 - 18 (E)	
Engineering Goods	15	12	8-10	<ul style="list-style-type: none"> <li>Government's increased thrust on infrastructure development and favourable policies for manufacturing should ideally drive the growth of the sector in the long term</li> <li>However, given the state of the economy, short term prospects are tough – exports could be a face saver for some companies</li> </ul>
Construction	15	14	10	<ul style="list-style-type: none"> <li>The growth in the last few years was driven by the projects announced in the previous period. With slowdown in housing, commercial construction and infrastructure spends, the construction growth rate is likely to come down in the short term</li> </ul>
Healthcare	17	15	18	<ul style="list-style-type: none"> <li>Prospects continue to be attractive with deeper penetration of private sector hospitals through specialised models. Pharma companies responding positively to the increased monitoring efforts of USFDA will see greater growth opportunities</li> </ul>
Auto	12	16	8-10	<ul style="list-style-type: none"> <li>Will take a couple of years to recover and short term pain is unavoidable</li> <li>Export growth due to rupee depreciation could benefit some entities</li> </ul>

# Despite unfavourable macro-economic conditions, there have been several successful exits creating substantial value. This will call for active involvement with operating management ...1

## Examples of Successful Exits in Adverse Environment...1

Investee Name	Investor Name	Exit Month & Year	Period Invested (Months)	Return Multiple	Why this example is relevant?	Investor / Investee Speak – What made the deal successful?
 BFSI		May-09	51	8.78	<ul style="list-style-type: none"> <li>Chryscap sold most of the stake, worth Rs 1,250 crore in the markets since February 2009 at a time when sentiment was low</li> <li>The exit sent out a strong revival message to PE community.</li> </ul>	“CEO Thyagarajan built the company through internal accruals and debt over 20 years before accepting any private equity. By then, his processes were rock-solid. Thyagarajan’s <b>approach to business</b> itself, which is a mix of the earth and the pragmatic” <i>– Ashish Dhawan, previously with ChrysCapital</i>
 Healthcare		Jul-09	62	4.38	<ul style="list-style-type: none"> <li>Despite market sentiment, Warburg Pincus felt that the investment was ripe for an exit</li> </ul>	“In addition to being a sounding board, what helped us was the <b>domain expertise that Warburg brought</b> from their international experience“ <i>– Mohit Talwar, Deputy MD, Max India</i>

Source: Venture Intelligence Data, Press Reports, Avalon Consulting Analysis

# Despite unfavourable macro-economic conditions, there have been several successful exits creating substantial value. This will call for active involvement with operating management ...2

## Examples of Successful Exits in Adverse Environment...2

Investee Name	Investor Name	Exit Month & Year	Period Invested (Months)	Return Multiple	Why this example is relevant?	Investor / Investee Speak – What made the deal successful?
 carwale	 <seedfund>	Nov-10	47	8.07	<ul style="list-style-type: none"> <li>The PE played a major role in turning raw startup into market leader</li> </ul>	<p>“Before Carwale, there was no organised auto-classifieds market. We have actually <b>worked to create the sector</b>”</p> <p>– Mahesh Murthy, co-founder, and Partner, Seedfund</p>
 PARAS PHARMACEUTICALS LTD. Healthcare/ FMCG	 Actis The positive power of capital	Dec-10	53	3.21	<ul style="list-style-type: none"> <li>Around the time of purchase of Paras, the environment was one where profit margins in exits from minority investments had shrunk considerably. Hence Actis decided to take a majority stake and influence the management</li> </ul>	<p>"Working in PE-controlled businesses brings in a lot of <b>pace, a sense of urgency</b> as you know that you have only three-four years to play with. Targets are aggressive, and we expect 20 to 25 per cent returns every year, much ahead of the market rate of growth,"</p> <p>– Raghunandan, former CEO of Paras Pharmaceuticals</p>

Source: Venture Intelligence Data, Press Reports, Avalon Consulting Analysis

# Despite unfavourable macro-economic conditions, there have been several successful exits creating substantial value. This will call for active involvement with operating management ...3

## Examples of Successful Exits in Adverse Environment...3

Investee Name	Investor Name	Exit Month & Year	Period Invested (Months)	Return Multiple	Why this example is relevant?	Investor / Investee Speak – What made the deal successful?
 Dairy		Jan-14	44	4.55	<ul style="list-style-type: none"> <li>The deal signified increasing investment activity in Agribusiness in the past 3-4 years</li> </ul>	“Carlyle’s investment in Tirumala exemplifies its ability to <b>partner with entrepreneurs to create value</b> for all stakeholders. During Carlyle’s investment, the company’s revenues grew two and a half times and profits more than quadrupled.” <i>- Shankar Narayanan, Managing Director, Carlyle</i>
 IT/ITES		Jan-11	55	6.64	<ul style="list-style-type: none"> <li>This deal signified that start-up ecosystem was evolving in India and entrepreneurs were able to hone in on viable business models better and faster</li> </ul>	“They (Sequoia, Lightspeed and Silicon Valley Bank) <b>shared our vision and passion</b> and were great partners to have at every step of the way” <i>- K. Ganesh, Founder and CEO of TutorVista.com</i>

Source: Venture Intelligence Data, Press Reports, Avalon Consulting Analysis

# Successful recent examples also indicate that longer holding period can result in exceptional returns if the time is spent productively in value creation...1

## Examples of Successful Exits with Longer Holding Period...1

Investee Name	Investor Name	Exit Month & Year	Period Invested (Months)	Return Multiple	Why this example is relevant?	Investor / Investee Speak – What made the deal successful?
 IT/ITES		Jun-13	71	13.87	<ul style="list-style-type: none"> <li>Since RedBus was a market leader at that time, Seedfund realised better exit returns</li> </ul>	“It was <b>Seedfund’s collaborative</b> spirit that helped build redBus... Not only did Seedfund supply the money in 2007, but Mahesh Murthy, the Seedfund founder-partner, helped redBus redesign its website. The changes were so good that the site remains untouched till date” – <i>Phanindra Sama, Co-founder, redBus</i>
 Manufacturing		Aug-10	93	19.14	<ul style="list-style-type: none"> <li>The exit proved that even social enterprises could give high return multiples</li> </ul>	“Aavishkaar held regular meetings with the CEO, conducted <b>joint reviews</b> of their performance with all stakeholders (investment committee), <b>visits to production sites</b> and <b>fine-tuning of strategies</b> were regularly done. Aavishkaar has contributed to the strong sales growth by introducing ServalS to their network of NGOs” – <i>Case Study on Avishkaar prepared by Dasra, a strategic philanthropy foundation</i>

Source: Venture Intelligence Data, Press Reports, Avalon Consulting Analysis

## Successful recent examples also indicate that longer holding period can result in exceptional returns if the time is spent productively in value creation...2

### Examples of Successful Exits with Longer Holding Period...2

Investee Name	Investor Name	Exit Month & Year	Period Invested (Months)	Return Multiple	Why this example is relevant?	Investor / Investee Speak – What made the deal successful?
 India's No.1 local search engine IT/ITES	SAIFPartners®	May-13	80	12	<ul style="list-style-type: none"> <li>The deal showed that investment play in e-commerce businesses was not a three-to-five years play, but more of a seven-to-10 year cycle</li> </ul>	"“Look at ..... Just Dial...the possibility of making disproportionate (return on) capital is much higher in the early stage,” - Mukul Singhal, Vice-President of SAIF Partners
 ALLIANCE TIRE GROUP Automotive	WARBURG PINCUS	Apr-13	70	4	<ul style="list-style-type: none"> <li>The deal showed huge growth potential in tyre demand from off-highway, agri and mining sectors in emerging countries apart from Europe</li> </ul>	“(Warburg Pincus) helped create and build ATG into the global industry leader that it is today” - Yogesh Mahansaria, Founder of ATG

Source: Venture Intelligence Data, Press Reports, Avalon Consulting Analysis

## Successful recent examples also indicate that longer holding period can result in exceptional returns if the time is spent productively in value creation...3

### Examples of Successful Exits with Longer Holding Period...3

Investee Name	Investor Name	Exit Month & Year	Period Invested (Months)	Return Multiple	Why this example is relevant?	Investor / Investee Speak – What made the deal successful?
 IT/ITES		Aug-12	65	10.76	<ul style="list-style-type: none"> <li>Exceptionally good return multiple in the most ideal investment period of 5-6 years</li> </ul>	“BookMyShow.com caught our attention because it has become synonymous with online entertainment and ticketing. We are constantly striving to invest in businesses that assume a leadership position by <b>driving the definition and growth of their respective categories</b> “ <i>- Accel India Partner Prashanth Prakash</i>
 Retail		Nov-13	80	5.47	<ul style="list-style-type: none"> <li>Relatively longer holding period of about 7 years yielding attractive returns to investors</li> </ul>	“Biyani did not want to control the show or kill the entrepreneurial spirit of the founder. Instead he <b>chose to partner them and together grew the business</b> . He has created value for each one of them and also for his investors.“ <i>- Vishal Mahadevia, MD, Warburg Pincus India</i>

Source: Venture Intelligence Data, Press Reports, Avalon Consulting Analysis

# We would recommend investors to adopt a 5 Step Framework to drive Value Enhancement

## Avalon Consulting 5 Step Value Enhancement Framework

Key Imperative	Rationale	Tools and Tackles
<b>Stay Focused on Delivering A Growth Strategy</b>	<ul style="list-style-type: none"> <li>▪ Growth creates all around value – to the promoter, existing investor and equally, for the secondary investors</li> </ul>	<ul style="list-style-type: none"> <li>▪ Product portfolio rationalisation and New Product Development</li> <li>▪ Customer line profitability</li> <li>▪ Pricing strategy</li> <li>▪ Channel mix optimisation</li> <li>▪ Geographic expansion and Synergistic diversification</li> </ul>
<b>Create Alignment – Promoters and Next Stage Buyers</b>	<ul style="list-style-type: none"> <li>▪ Align with the Promoters on likely secondary investors – strategic or PE, create the buy-in and rationale. Will help to work towards the common goal</li> </ul>	<ul style="list-style-type: none"> <li>▪ Strategic Investor Search – broad buyer category and specific targets</li> <li>▪ Align Strategy where required without compromising key elements</li> <li>▪ Recalibrate and Iterate</li> </ul>
<b>Governance and Organisation Transformation</b>	<ul style="list-style-type: none"> <li>▪ Improved Governance and Organisation aligned with Strategy with Key Personnel in place is a pre-requisite to Strategy Execution</li> </ul>	<ul style="list-style-type: none"> <li>▪ OT through Balanced Scorecard</li> <li>▪ People capability enhancement</li> <li>▪ Good governance and reporting</li> <li>▪ Process / systems (governance, operations, supply chain, sales &amp; marketing, finance, etc.)</li> </ul>
<b>Operational Efficiencies</b>	<ul style="list-style-type: none"> <li>▪ Continuous Operational Improvements to Drive Short and Medium Term Profitability Improvements</li> </ul>	<ul style="list-style-type: none"> <li>▪ Strategic Cost Reduction and Sourcing</li> <li>▪ Supply Chain Efficiency Improvements</li> <li>▪ Cash to Cash Cycle Improvements</li> <li>▪ Sales Force Effectiveness</li> </ul>
<b>Stress Test</b>	<ul style="list-style-type: none"> <li>▪ Key Question – Would the Exiting Investor have invested in the business?</li> </ul>	<ul style="list-style-type: none"> <li>▪ Mini 'VDD' at regular intervals</li> </ul>

Source: Avalon Consulting Research & Analysis

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**Focus Sectors**

	Agri Business		Auto
Chemicals		Consumer Goods & Services	
	Education		Infrastructure & Capital Goods
Metals & Mining		Healthcare & Pharma	

**Service Capabilities**

- Strategy**
  - Corporate Strategy
  - Business Unit Strategy
  - Functional Strategy
- Transformation**
  - Strategy Articulation
  - Organisation Design and Alignment
  - Process Re-engineering
  - Change & Performance Management
  - Post Merger Integration
- Transactions**
  - Deal Origination
  - M&A Support
  - Value Enhancement
  - Exit Strategy

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