Joint Venture & Partnering InSight

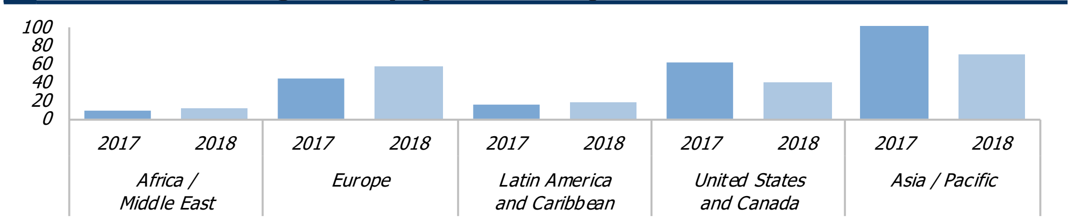
April 2018

Key Topics

Europe Overtakes the US...

Q1 JV & Partnering activity shows 2018 has got off to a slower start than 2017. Many geographies show an increase in joint venture activity year on year, although Q1 this year has lacked the major deals of 2017 in the US and Asia Pacific regions.

JV and Partnering Activity Q1 2017 vs. Q1 2018



Source: CapIQ

Geographies

European JV and partnering activity was up 31% on the same quarter last year and continues to accelerate, finishing Q1 higher than the US for the first time since 2015. Most of this momentum comes from the Industrials and Energy sectors, reflecting similar conversations the Lincoln JV&P team has been having recently with clients.

Despite the Q1 decline, Asia Pacific continues to dominate in terms of volume, with over 35% of the total deals announced.

Sectors

JV and partnering in most sectors was stable or a little down on the same quarter in 2017, except for Consumer Staples, up 60% (mainly driven by activity in the Automotive space) and Utilities, up 10%.

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Lincoln International is pleased to publish its fifth issue of JV&P InSight.

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How Partnering to Exit Can Unlock Value

Joint ventures (JVs) can provide a viable alternative to an outright sale, particularly where complex systems need to be untangled or where many of the assets being sold are intangible. JVs are an unusual solution – most investment banks / M&A teams think in terms of a traditional sale to realise value. However, if well-structured and tightly managed, JVs can be a powerful medium-term solution to exit, creating and unlocking value.

Using a JV as a mechanism to buy / sell a business, e.g. where the buyer commits to a stake in the business in return for an option to purchase all the remaining shares within a specified period, is far from simple and requires specialist advice.

Sample Benefits and Potential Downsides of Using a JV to Buy / Sell a Business Over Time

Sample Benefits	Potential Downsides
Employee engagement ▪ A JV can be positioned as a "good news story", signalling investment into the business, thereby helping to retain and motivate talent"	**Ongoing management burden** ▪ Unlike a sale, a JV needs continued attention after the deal – to monitor performance, protect value and manage both timing and process of exit
"Business as usual" stability ▪ A JV often enables pre-existing knowledge, technology, and skills to be shared during business transition / rejuvenation / streamlining"	**Legacy culture / infrastructure issues** ▪ A JV usually works best when it creates its own culture and behaviours; this can be harder if people / location / systems and processes remain as before the deal
A clear, milestone-linked timetable for exit ▪ A timetable and performance milestones together help avoid the risk of one partner seeking to suppress growth, accelerate investment or hold back profits	**Unforeseen issues and valuation disputes** ▪ Exit mechanisms and options which take no account of potential changes in economic / market conditions can lead to time-consuming and destructive conflict on exit

Case Study: Phased Exit via JV

Situation:

Our client wanted to divest a non-core business to focus on its chosen strategic products and markets. However, buyers were put off by:

- Its complex internal structure, which made separation look difficult and lengthy
- A powerful unionised workforce that appeared very resistant to an outright sale

Result:

Our client was planning to abandon the sale but we came up with an alternative:

- Presented the JV as an investment vehicle, whilst building an agreed plan to exit the business
- Brokered a strong working relationship with the incoming partner, openly agreeing the exit plan, timetable and process up front

When it May be Wise to Consider This Approach

- A separate JV entity can help when disentangling a business from complex systems / structures, e.g. where several businesses share facilities, IT, or personnel
- If many of the JVs assets are intangibles, e.g. a consumer franchise, distribution relationships or intellectual property; the phased sell-down agreement provides more flexibility, while enabling the initial deal to go ahead at a manageable price

Just as "traditional" JVs and partnerships need careful planning – not just legally, but operationally – so do acquisitions and disposals using a JV. That is why it is important to seek the advice of genuine specialists. Lincoln International's JV and partnering advisory team is ready to help you explore the potential of using a JV to exit, and how to negotiate and structure it successfully.

How to Succeed at Partnering: Some Initial Pointers

Identify the potential challenges – internal as well as market-related

- Often easier said than done; few organisations can see themselves as others do

Think through the value proposition – to the customer and the prospective partner

- In a market with lots of competition for talent and the "best" technology, this is vital to attract the best partners
- To avoid later pitfalls, all parties should see the same opportunity / have similar goals

Understand what you need from a partner

- Not only to build the proposition and attract customers, but also in terms of resources, speed of decision-making, behaviors, "look and feel"
- Again, this demands corporate "self-knowledge"; an objective view often provides valuable additional insights

Where Next for Tech Partnerships in Financial Services?

Joint ventures and partnerships between technology companies and start-ups, and their larger, traditional counterparts have been growing steadily, especially in banking. The opportunities to benefit from, and the need to combat, disruption have proved compelling drivers.

We believe this trend is set to continue across insurance, asset management and traditional "financial advisors". However, as partnering becomes more accepted, competition for partners will increase.

Banking Disruption: Payments Just the Tip of the Iceberg?

We are all familiar with the rise of Peer-to-Peer (P2P) payments disruptors (PayPal, Snapcash, Google Wallet, Venmo). In 2017, Venmo transferred payments totalling ~$35bn. We also saw a major response from Zelle, a consortium of 50+ traditional US banks, including Wells Fargo and Bank of America. After reportedly six years of "development", Zelle has "caught up" – processing transactions worth ~$75bn in its first year.

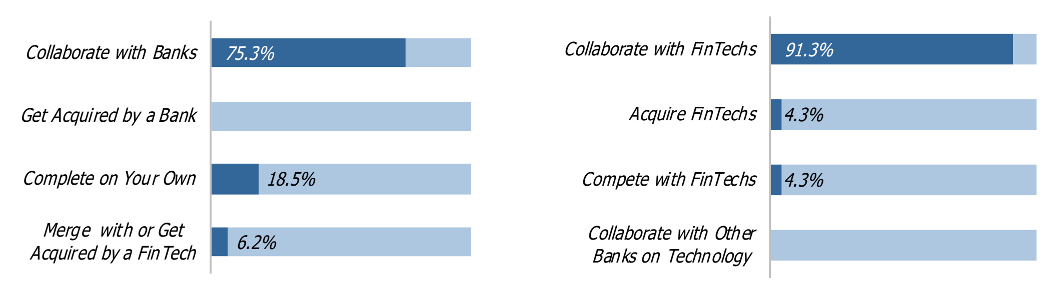
According to Citibank's recent report, "banks of the future" will need to adjust fundamentally, learning "to co-exist with e-commerce and social media-based companies"[1].

We believe such change – at a time of increasing regulation, cyber and other forms of fraud – can only be achieved and afforded through intelligent, well-planned partnering. According to a 2017 Financial Services Banking review (see Fig. 2.2 below), banks and FinTech companies agree.

[1]Source: "Bank of the Future", The ABCs of Digital Disruption in Finance, Citibank, March 2018

Figure 2.2: Future Strategy of FinTechs and Banks (%), 2017

Future Strategy of FinTechs (%), 2017 | **Future Strategy of Banks (%), 2017**



Note: The percentage represents the FinTech/banking executives who have chosen the particular option
Source: Capgemini Financial Services Analysis, 2017 Retail Banking Executive Interview Survey, Capgemini Global Financial Services

Big Insurance Brands Continue to Dominate the Industry, But for How Much Longer?

In January 2018, a joint venture (JV) was announced combining:

- Amazon's expert technical capabilities;
- JPMorgan's ability to leverage its technology; and
- Berkshire Hathaway's access to multiple industries, from insurance to utilities and manufacturing.

On the day of the announcement, the US's five biggest health insurers – UnitedHealth, Anthem, Aetna, Humana and Cigna **–** suffered losses of 3 to 7.2%. But how will the world of insurance itself respond? According to survey many are thinking of partnering:

- Over 80% of insurance CEOs believe their companies have a shortage of digital skills
- 49% of these CEOs are planning a strategic alliance / JV over the next year[2]

[2]Source: 21st Global CEO Survey, PwC, March 2018

How to Succeed at Partnering: Common Challenges to Overcome

Many industries in which we work, notably Automotive and Retail, are also facing radical disruption to the status quo, and incumbents' response often involves partnering with tech firms and start-ups. Similar themes to those occurring in Financial Services include:

Decision-makers often don't understand the technology or the speed of change

- This can be a big hindrance when seeking to woo a "hot" potential fintech partner

Perceptions and concerns on exit options vary enormously

- A fintech entrepreneur will be concerned about potential constraints imposed by a bureaucratic and risk-averse partner
- A traditional partner will wish to protect its investment (time and brand as well as cash) and lock in key talent to transfer skills and know-how

Limited experience of partnering delays progress and can harm developing relationships

- Most internal legal and M&A departments have limited experience of partnering
- Business people also lack this expertise, but often put relationships (which are critical) before process, leading to mixed results

Partnerships Are Also Emerging in Asset Management

Robotic process automation (RPA), blockchain, and cognitive systems are changing the provision of asset management services. We believe such innovation can drive efficiency, reduce risk, and improve service quality.

Examples in the US…

Many early "robo-advisor" firms (those using algorithms to provide financial advice) favoured "going it alone". However, partnership announcements, such as Citizens Financial and SigFig, and the larger link-up between Betterment, Goldman Sachs and BlackRock, suggest the appeal / reach of incumbent partners is attractive in asset and wealth management too.

…And in Europe

The largest German independent financial advisor, Deutsche Vermogensberatung AG (DVAG), announced a JV with fintech company builder FinLeap in early April 2018. The goal of the JV is "*… To combine the empathy and expertise of financial advisors with artificial intelligence and put the results at the service of customers.*"

Successful Partnerships Need a Rare Combination of Skills

At Lincoln, we work in close cooperation with our industry counterparts, including searches for the right partnering and structures to incentivise the desired behavior on both sides.

In the Financial Services market, we work with Alex Ring and the Lincoln Financial Institutions team to design and build sustainably successful partnerships.

Global Industry Groups

Business Services

Consumer

Energy, Power & Infrastructure

Healthcare

Industrials

Technology, Media & Telecom

Global Locations

Amsterdam

Beijing

Chicago

Dallas

Frankfurt

London

Los Angeles

Madrid

Milan

Moscow

Mumbai

Munich

New York

Paris

San Francisco

São Paulo

Stockholm

Tokyo

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Debt Advisory

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Valuations & Opinions

Special Situations

About Lincoln International

Lincoln International specializes in merger and acquisition advisory services, debt advisory services, private capital raising and restructuring advice on mid-market transactions. Lincoln International also provides fairness opinions, valuations and joint venture and partnering advisory services on a wide range of transaction sizes. With twenty offices in the Americas, Asia and Europe, Lincoln International has strong local knowledge and contacts in key global economies. The firm provides clients with senior-level attention, in-depth industry expertise and integrated resources. By being focused and independent, Lincoln International serves its clients without conflicts of interest. More information about Lincoln International can be obtained at www.lincolninternational.com.

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