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Mergers & Aquisitions,
Financing, Business Advisory Services

Joint Ventures

…an attractive strategy for expansion

Sales and market share growth are always challenging either in the national or international markets. As a means to an end, many companies elect for a joint venture approach to obtain their full market potential. Over the years, Cafa has been involved in several joint venture projects both nationally and internationally for several of its clients. We would like to share some key elements for you to consider before contemplating a joint venture.

What is a Joint Venture?

A joint venture is usually formed by two or more partners to undertake a project, compete in a market or establish a new commercial activity. The parties each contribute capital and/or their expertise with the aim to share control, revenues, expenses and profits. A joint venture can be an 'on-off' temporary venture or a permanent entity. Legally, a joint venture can take various forms; from a simple cooperation agreement to a limited partnership or a limited liability company.

Risk sharing, access to markets, economies of scale, know-how and knowledge, accelerated growth and lower capital investments are usually some of the reasons why someone would contemplate entering into a joint venture. Most often, joint ventures are driven by access to market or technical expertise. A joint venture provides leverage and capitalizes on each partner's strengths while minimizing individual capital requirements.

Key Factors to Success or Failure

To be successful the parties involved have to commit to the success of the joint venture over and above their individual interests. Choosing the right partner is essential to success; i.e. do they share the same objectives; are they committed to the success of the venture; what is their reputation, and finally, are their contributions complementary? Most of the time, capital contributions are secondary to market knowledge or technical expertise.

Failure usually occurs when disagreements arise over the objectives of the joint venture, the partners fail to adapt to each other's culture and/or the partners fail to capture the synergies that brought them together in the first place, whether it be in terms of expertise or resources.

Depending on the legal structure used for the joint venture, the partners' intentions must be captured in a legal agreement that can range from a simple joint venture agreement to a full- fledged shareholders' agreement. Regardless of the type of legal agreement that governs the relationship, the agreement must cover, at minimum, the following aspects:

1. Each partner's right to dispose of its interests in the joint venture,
2. Exit or termination clauses,
3. The financing of the joint venture,

Joint ventures are not only used to access new markets, they also allow partners to capitalize on their expertise and know-how while relying on shared resources for the benefits of the group.

The objectives are always the same; i.e. to do more with less risk relative to the financial commitment.

Cafa Corporate Finance
4269 St. Catherine St.West, Suite 200 · Westmount, Quebec H3Z 1P7
PHONE: 514-989-5508 · FAX: 514-989-5941 · www.cafa.ca

Joint Ventures... an attractive strategy for expansion (cont'd)

4. Capital and technical expertise brought to the joint venture,
5. The distribution of profits or dividends, and
6. Non-compete provisions.

> ***Earnouts can be a useful tool in reaching a compromise when the vendor and the purchaser just can't seem to bridge the gap***

Examples

A joint venture for an international expansion

A Quebec-based building products company with a unique technology attracted interest from a central European manufacturer. The European market presented an interesting potential due to growing consumer interest for DIY renovation products. A joint venture was created in the form of a new corporate entity. The Quebec company provided the technology and a good share of the funds by way of share capital and temporary loans. The local partner contributed some technical expertise, its knowledge of the business environment, a local management team and some assets. The initial start-up required more effort than expected and for a time quality control remained an issue. More funds had to be injected but the business eventually became very profitable.

This project has since become one of the Quebec company's most profitable investments. The joint venture continues to perform in large part because the partners still share the same business goals they started out with.

A joint venture for the local market

A Canadian-based public company was seeking to acquire a non-operating manufacturing plant which had been closed for market reasons. Although the acquisition cost was minimal the plant needed over $30 million in modernization to become competitive. Our client approached a Far East industrial customer with the idea of entering into a joint venture for the acquisition and plant refurbishing. The Canadian partner would bring capital, local management and technical expertise and be in charge of raw material supply. The industrial partner would also put up some capital, but more importantly, it provided instant access to Far East markets by way of a bought deal on all of the plant's output.

Once the project was completed, the Canadian partner recovered its capital investment on top of a very attractive return while keeping an equity interest in the plant. This joint venture was successful because the parties' contributions were highly complementary.

Conclusion

Cafa has been involved in several successful projects in the past both in the national and international markets. Our role includes seeking the right partner; negotiating the terms of the joint venture and its financing. We would be pleased to share our experience with you.

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