Sanjay Jain, Group Chief Financial Officer, Future Group

Creating Shareholder Value: The CFO's Ambit

A CFO's role in any successful turnaround goes well beyond being just a 'super cost-cutter'. When the business context is one of high debt and leverage, it demands a dual focus on expansion, as well as the ability to improve capital structures. One company that has been a stellar 'out performer' on this score is the Future Group. CFO Connect covered Future's dynamic approach to financial re-engineering at length in a 2015 issue. This article, however, reviews the strategy that has made it stronger and leaner, and at the same time, allowed it to create massive shareholder value. In the last three years, revenues have grown at a compounded 33 per cent, its leverage ratio has dropped from 6x to under 2x, and its ratings have moved up two notches. [Strikingly today, market cap has already surged from Rs 36 billion to Rs 500 billion – a whopping CAGR of more than 110 per cent over 3 & ½ years.

In so many ways, Sanjay Jain, Future's Group CFO, and winner of IMA's Tenth India CFO Awards for Restructuring Capital, is a prime example of someone who has successfully created shareholder wealth by using longer-term, lower-cost instruments, and by widening the Group's relations with a spectrum of financial institutions. This issue's cover story provides an in-depth view of his role in restructuring and raising capital to optimise shareholder returns.

FUTURE GROUP: THE JOURNEY TO BECOMING INDIA'S WALMART

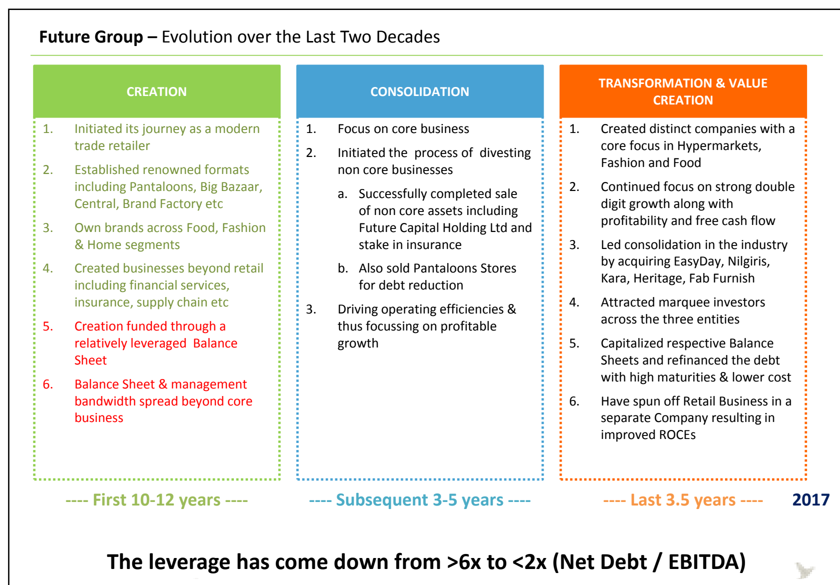
Creation: the First 10-12 Years

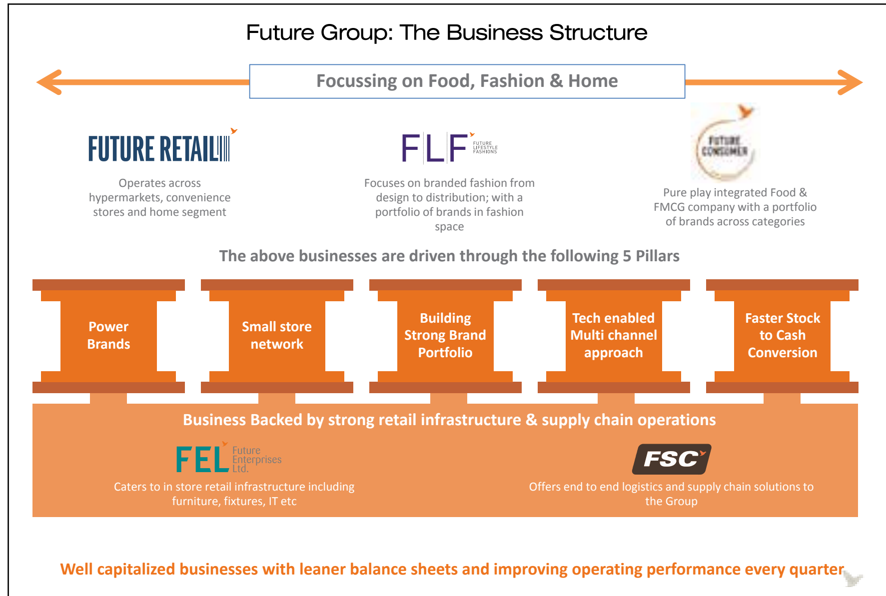
Until 2007, Future Retail was growing rapidly on the back of huge footfalls at its established stores, including Pantaloons, Big Bazaar, Central and Brand Factory, among others. At that point, the company delved into non-retail businesses such as insurance, supply chain, and financial services. The thought of a meltdown never crossed the minds of its first generation of entrepreneurs, as the benign market conditions existent then made them believe that the 'best was yet to come.' With cheap money easily available from banks/financial institutions it soon found itself in a loop, where it was funding its expansion with debt rather than by diluting its equity. The result was an enormous asset-liability mismatch, with substantial debt – pushing its net debt-to-EBITDA ratio to over 6x. Further, it was thinly spread across its many businesses, which meant sub-optimal profitability and operating cash flows.

Multiple sources of funds should be evaluated not just for cost but also for their alignment with the company's long-term plans

Consolidation: the Next 3-5 Years

Faced with slowing growth and mounting debt, the Group decided to capitalise its balance sheet. When he joined the Group in 2014, Mr Jain's five-point agenda involved raising equity, bringing debt down to a third of the existing levels, monetising non-core assets, redesigning the firm's performance-review mechanisms, and – as a core foundation – further strengthening its governance standards. As a first step – and a fitting signal to the markets about Future's commitment to 'righting' itself, the promoters had already sold off their 'crown jewel', Pantaloons, reducing the debt levels by Rs 24 billion. They also divested the NBFC business to a leading private equity firm, raising an additional Rs 5.6 billion. [Next, a plan was drawn up to raise Rs 20 billion through a rights and a preferential issue. Once internally approved, the plan was put into





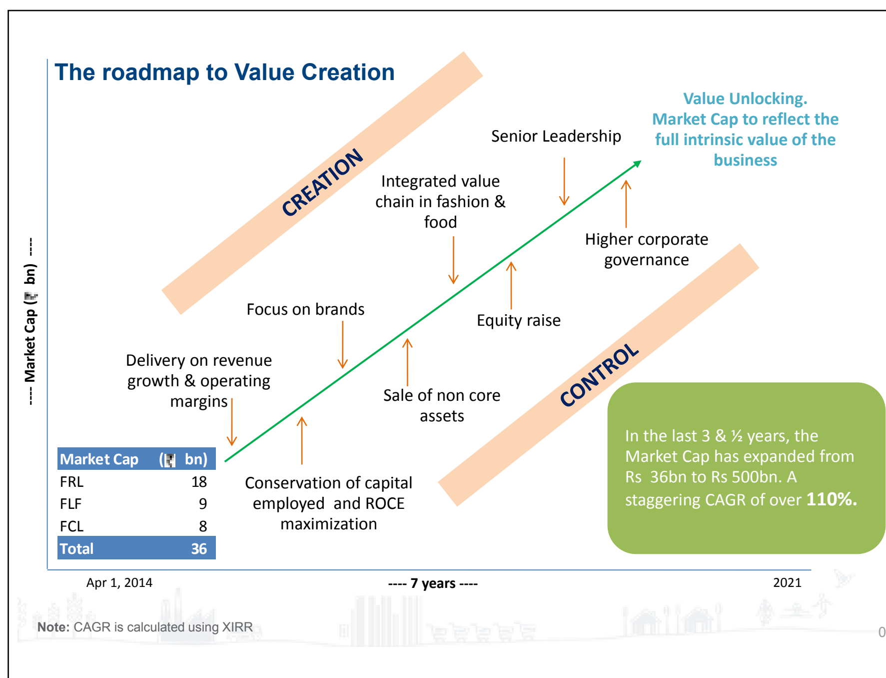
action. Despite tremendous odds, the rights issue proved successful, positively impacting the Group's subsequent rounds of refinancing. [For instance, it was able to secure Rs 1.75 billion through a mezzanine deal involving zero-coupon redeemable preference shares with a 3-year maturity.]

The company also targeted international investors, specifically Indians living abroad, to raise another Rs 6 billion. In parallel, it undertook several initiatives to improve efficiencies and drive up gross margins. The net outcome was that Future Group managed to rehash Rs 80 billion of its total debt, converting 50 per cent into equity, and the balance largely into NCDs with 5-6 year maturities at 2 per cent lower coupon. As part of the Rights & Preferential Issue, the Biyani family decided to fully subscribe to their nearly 50 per cent shareholding. This was a lot for a first generation entrepreneur. A standard holding company (HoldCo) level financing would have meant leverage moving up from the operating company to the HoldCo and that too, with much higher coupon. However, this was very judiciously handled through a suitable quasi equity / long term mezzanine financing. These steps brought down the debt-to-EBITDA ratio to below 2x, and critically, made possible a two-notch rating upgrade, to AA levels.

Transformation and Value Generation: the Last 3.5 Years

Sustainable value creation is Future's long-term strategy, and implementing a high-quality control mechanism is the backbone of this effort. Since 2014, the company has placed much greater emphasis on value creation by delivering on revenue growth and operating margins, creating new brands, and integrating the value-chain in its fashion and foods businesses. Simultaneously, there is now greater control over the Group's leverage profile – made possible by a strict focus on operating cash flows, balance-sheet capitalisation, monetisation of investments, and improved governance standards. These efforts have helped Future emerge stronger, leaner, and more attractive to investors.

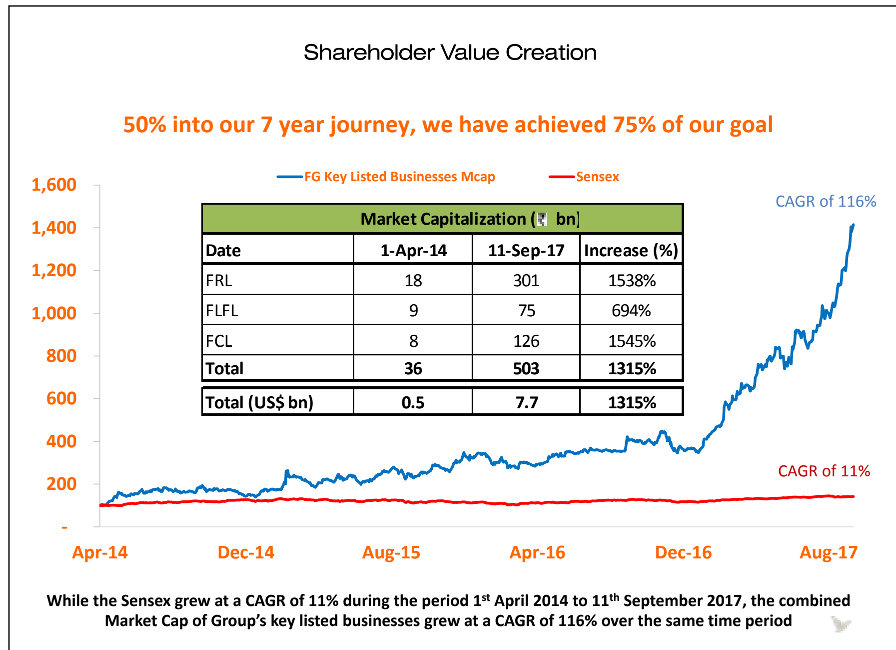
An essential step was the carving-out of four separate, listed entities: Future Retail, Future Consumer, Future



Market Cap (₹ bn)	
FRL	18
FLF	9
FCL	8
Total	36

Lifestyle Fashions, and Future Enterprises. With their core focus on hypermarkets, fashion, and food, separating these companies unlocked huge value and enabled massive capital appreciation.

Future has also been at the forefront of consolidation in the retail industry, acquiring EasyDay, Nilgiris, Kara, Heritage, and Fab Furnish. In terms of outcomes, same-store sales growth has jumped from 5 per cent to 20 per cent, while revenues (currently Rs 280 billion) have risen at a 3-year CAGR of 33 per cent. Its market cap – boosted also by a sectoral re-rating following last year's D-Mart listing – has compounded at 116 per cent. The focus today is on funding growth and expansion while containing the balance sheet to achieve Rs 1 trillion of revenue by 2021. Going forward, Future aims to continuously improve its leverage profile and operating efficiency through a strict focus on operating cash flows, balance sheet capitalisation, and the monetisation of investments. It also plans to leverage any consolidation opportunities that come up. Future firmly believes this would automatically lead to value creation for its stakeholders. The last three and a half years are testimony.



Market Capitalization (₹ bn)			
Date	1-Apr-14	11-Sep-17	Increase (%)
FRL	18	301	1538%
FLFL	9	75	694%
FCL	8	126	1545%
Total	**36**	**503**	**1315%**
Total (US$ bn)	**0.5**	**7.7**	**1315%**

While the Sensex grew at a CAGR of 11% during the period 1st April 2014 to 11th September 2017, the combined Market Cap of Group's key listed businesses grew at a CAGR of 116% over the same time period

ENGINEERING A TURNAROUND

Future successfully overhauled its capital structures using a combination of measures: tapping multiple sources of funds, targeting investors effectively, choosing counter-parties carefully, directly involving its promoters, and leveraging the expertise of bankers. In terms of outcomes, it managed to raise sufficient capital from banks and PE funds, got its ratings upgraded, and built lasting relations with the investor community. In the process, Mr Jain learned some critically-important lessons about shareholder value creation.

Engage investors through storytelling

Essentially, fundraising is an exercise in storytelling. In today's fast-paced, data-driven world, investors have neither the time nor the patience to unpack a company's value proposition, so businesses must effectively communicate their future funding needs. The science of corporate storytelling starts with research. The CFO must have a clear-eyed view of the business from the outside-in, and the inside-out. Further, the story needs to be customised to investors' needs. Those who have a long horizon will be more interested in the company's upside potential in the next 5-10 years, while those who seek mainly to earn dividends will want to know about cash flows. Further, it is important to regularly keep in touch with the existing investor base – which can be a very useful channel for bringing in new investors.

Leverage multiple sources of funds

With myriad types of funding available, from NCDs and PSU banks to private equity and offshore money, choosing the right source is crucial to fulfilling one's growth ambitions. After evaluating different sources, one should settle on sources that are not only relatively cheap, but also aligned to the company's long-

Our global manufacturing and procurement footprint helped us raise low cost capital from sources outside India

term plans. In this respect, Indian businesses remain in a sweet spot, especially because PE and offshore investors see India as a preferred investment destination. In the case of Future Group, owing to India's multi-brand FDI restrictions, it was challenging to solicit foreign investments. Crucially, too, it split its operations into various retail and non-retail subsidiaries, some of which – like the logistics and procurement wings – had no regulatory issues tapping into foreign funds, even for the India operations.

Work closely with the promoters

Mr Jain is fortunate to work with one of India's most progressive first-generation entrepreneurs – many of whom would cringe at having to dilute their personal holdings. Kishore Biyani did not hesitate to sell-off the Group's crown jewel, Pantaloons retail chain. The key to creating a partnership is to regularly engage and communicate with him, as well as the rest of the promoter family – all of whom play an active role in decision-making. The other vital element is to make discussions as numbers-backed as possible. Daily updates on market cap and other stock-performance parameters are important to ensure that the lines of communication remain open. For Future, it also yielded some out-sized results. For example, at one point, Mr Biyani himself suggested diluting the company's stake to raise growth capital, but at an appropriate price. This proved far-sighted: after months of dialogue with investors, the final price was much higher than initially expected.

> Consolidation of the business demanded divestment of non-core assets and simultaneously, a string of acquisitions to enable expansion in the core business of retail. The simultaneous restructuring of business into separate listed entities to enable both funding and focus unlocked huge shareholder value.

Need to be timed right

Rights and NCD issues need to be timed right, which means carefully assessing market conditions and the overall business climate. Further, there should be just enough time for investors to subscribe to the issue. If given extra time, the investor community tends to over-scrutinise, seeking endless clarifications. A too-short deadline, on the other hand, might not create the right 'buzz' within the investor community.

Choosing counter-parties wisely

Before settling on a counter party, it is critical to gauge both the investor's alignment with the company's long-term strategy, and the promoter's comfort level with the investor. Often, promoters will be sceptical about sharing a seat at the table with an outsider who has little knowledge of the business. Therefore, it is essential for the investors and promoters to 'get along'. Also, at times, tactfully refusing an investor actually sends a positive message to the well-knit investor community.

Networking extensively

Targeting investors through personalised meetings is an effective way to build relationships and promote the company's good work. CFOs should regularly address the concerns of current and potential investors openly and honestly. The key is to proactively deal with risks that investors face, and this requires the CFO to prepare accordingly. Critically, CFOs must reach out to investors proactively and regularly, even when there is no immediate-term agenda. 'No agenda' meetings cement bonds and also enable investors to gain ongoing insight into thinking and plans.

Hiring an investment banker

While there is a cost to investment banking, if selected correctly, there are also proven benefits of having outside experts overseeing a funding or acquisition process. Access to the investment bankers' network of investors is another significant advantage when raising capital. Bankers also have extensive industry knowledge which can be helpful in identifying new strategic opportunities, including mergers, partnerships, and acquisitions. Additionally, investment banks provide the resources and expertise needed to structure and implement deals at reasonable price points. Bankers, for instance, guided Future Consumer Limited (the

Group's FMCG arm) to move its convenience stores within the existing Future Retail outlets. This not only helped create a more optimal structure, with clear demarcations between the distribution and the retail business, but also enabled the company to ensure adherence to FDI rules.

Cash how financing

Of Future Retail's annual Rs 120 billion top-line, about half is in the form of credit card receivables. Leveraging this fact, the company worked with banks to restructure its systems such that a select part of the receivables are now routed through a designated account. This enables a more stringent monitoring of funds, but more critically, allowed the Group to move from asset-based to cash flow-based loans. This obviated the need to hold huge inventory, reduced the company's working capital requirements, and improved its return on capital.

Reviewing capital structures regularly

A continual review of capital structures helps arrest undesirable use of cash, and allows the firm to take corrective action early on. Promoter involvement in the review process adds rigour and ensures accountability by business heads. The Future Group's capital structure review process was redesigned to put greater focus on capital efficiency and cash spends. Reviews are now held regularly, taking up as much as 40 per cent of the promoters' time. Mr Jain has ensured a new financial rigour that has, over time, become part of the Group's very DNA, and instrumental in making people conscious of the need for capital efficiency. Resultantly, the quality of corporate governance has also vastly improved.

Balancing ROIC and Growth

The Future Group has always been open to investing in growth prospects, even during times of constraint. Soon after the retail giants Walmart and Bharti parted ways in 2013, Mr Biyani sensed an opportunity and acquired Bharti Retail. Given that Future Retail was still in the process of capital restructuring, the move came as a surprise to most investors. However, Future was so sure about its value-accretive prospects that it went ahead. The deal was structured smartly as an all-stock buy-out that did not impact the company's finances, but actually created shareholder value. It was engineered by splitting both companies vertically to remove the core assets from the non-core ones. The new entity had a strong balance sheet with limited liabilities, and consequently, received a thumbs-up from the stakeholders. Another example is

> **Timing is key in fund raising. The investor community should be given just enough time to subscribe to any fund raising issue. More time might lead to over scrutiny while less time might not create the right buzz.**

Sanjay Jain's Tips

- Adopt a proactive approach
- Manage stakeholders wisely
- Use multiple sources and instruments
- Get stakeholders' expectations right
- Bat on front foot - don't duck risks, talk through them
- Follow a measured pace. Don't start too early
- Select your counter parties wisely
- Look for people who understand your business or who wish to understand your business
- Shop 'globally' not just 'locally'
- Build a funnel (4:1). At the same time don't do carpet bombing
- Engage with investors, be on the road
- Investor community is very small - people exchange notes. So, be sure of what you say
- Hold 'no agenda' meeting with investors
- Write and rehearse your story
- Walk your talk and remember after sales service is the key
- Keep raising equity, as and when it is available
- Be realistic in your negotiations - don't agree to terms and timelines that you can't meet
- Say 'Smart' NO to investors

‘No agenda’ meetings across a CFO’s eco-system are crucial to building continued understanding and strengthening relationships. This effort must be internally (peers, team) as well as externally (investors) focused.

the acquisition of Nilgiris, a South Indian supermarket chain, from Actis, a UK-based PE firm, for Rs 2.7 billion. The deal was initially financed through internal funds, but Future quickly raised equity to restore the capital structure. Nilgiri’s offered strong synergistic value in the form of manufacturing capabilities, the acquisition of a very strong brand and an expansion of Future’s retail footprint. A third instance is Future’s homegrown apparel chain – FBB. After letting go of its Pantaloons stores to the Aditya Birla Group, Mr Biyani built this new business within the framework of the Big Bazaar stores. Today, it is seeing rapid growth,.

In Conversation with Sanjay Jain

CFOs are vested with great powers. Do you ever get carried away to do your own thing?

The role of a CFO comes with great power and responsibility. CFOs are expected to facilitate the growth of business. We are constantly in limelight, but that should not get to our head. At no point should we let arrogance creep into our conduct. We should never forget that the CEO is always in the driver’s seat. In my case, I was expected to facilitate the achievement of an enormous goal set by Mr Biyani - unlocking value and getting the Group to its first milestone of achieving USD 10 billion in market cap. This goal has to be achieved collectively and by working amicably with others. Therefore, as a CFO I proactively avoid any sort of conflict with my peers, take a back seat when required, and constantly remind myself that I am not in the driver’s seat. My aim is not to look for credit, but simply, to get to my goal.

Future Group has made investments in brands. What is the strategy to grow brands?

We have been focused on growing brands organically and inorganically. After selling Pantaloons, Mr Biyani was determined to create strong homegrown brands such as FBB. The focus is also on expanding the brand portfolio by acquiring strong external brands such as Nilgiris, Easy Day, Kara and Heritage. Such moves will help the company be part of a ‘large picture’ retail play and will further boost omni-channel plans of Future.

How do you ensure harmony with promoters?

At their core, entrepreneurs like to do things on their own. To avoid any conflict, it is critical to give enough space while maintaining regular touch-points. A good way to draw promoters’ attention to any important issue is by talking through the correlation between P&L and the balance sheet, ROCE and the cost of capital, and wealth creation and ROCE. It is equally important to speak one’s heart out when the need arises. That helps to build both trust and a strong connect. With Mr Biyani, I was vocal about the challenges of managing legacy relations in my previous organisation. He appreciated my honesty and went out of the way to support me in this regard.

How do you ensure social connectivity among employees within such a large group?

There are nine lakh people directly or indirectly employed by Future Group. We hire talent locally across all our offices. Over time, we have built a strong social interface that helps us engage with not just employees but also suppliers. For instance, we have built a strong farmer connect through our food parks. We have been able to successfully channelize social connect for growth.

What is the role of a mentor; who is yours?

It is crucial to have an impartial mentor who recognises your strengths as much as your weaknesses. In my case, my wife is my best mentor. With no vested interest, she gives me ruthless advice that is really helpful. ■