

# Tata steel



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## **TATA STEEL: ACQUISITION OF CORUS**

### **INTRODUCTION**

Tata acquired Corus, which is four times larger than its size and the largest steel producer in the U. K. The deal, which creates the world's fifth-largest steelmaker, is India's largest ever foreign takeover and follows Mittal Steel's \$31 billion acquisition of rival Arcelor in the same year. Over the past five years, Indian companies had made global acquisitions for over \$10 billion. The Tata bid almost equals this amount. Most of them have averaged \$100 to 200 million.

“ It is a two-way street now,” Kamal Nath (Commerce Minister, India) said. “ Not only India is seeking foreign investment, but Indian companies are emerging investors in other countries.”

Tata acquired Corus on the 2nd of April 2007 for a price of \$12 billion making the Indian company the world's fifth largest steel producer. This acquisition process has started long back in the year 2005. However, Corus was involved in a considerable number of Merger & Acquisition (M&A) deals and joint ventures (JVs) before Tata. This process started in the year 2000 and with Tata it came to an end.

Ratan Tata, Chairman of Tata Steel, said:

“ This proposed acquisition represents a defining moment for Tata Steel and is entirely consistent with our strategy of growth through international expansion. Corus and Tata Steel are companies with long, proud histories. We have compatible cultures of commitment to stakeholders and complementary strengths in technology, efficiency, product mix and

geographical spread. Together we will be even better equipped to remain at the leading edge of the fast changing steel industry.”

## **TATA STEEL**

Established in 1907, Tata steel is materialization of dream of a prosperous & independent India of Jamshetji Tata. It is India’s first and Asia’s largest private sector steel company. Tata Steel is the lowest cost producer of steel in the world.

### **Operations**

Tata Steel’s Jamshedpur (India) Works has a crude steel production capacity of 6.8 MTPA, which is expected to increase to 10 MTPA by 2011. Quality and Yield of raw material unit’s gives competitive advantage and strength to the Indian operation. The security of raw materials provided partial insulation to Tata Steel from the volatility of global market. The company plans to enhance its capacity, manifold through organic as well as inorganic growth.

They have expanded to 11 other countries, Thailand and Vietnam being the latest one. They proposed 3 Greenfield steel projects in the states of Jharkhand, Orissa and Chhattisgarh, which will provide additional capacity of 23 MTPA.

Tata Steel’s products are targeted at the quality conscious auto sector and the promising construction industry. Tata plans to emerge as major global player in the wire business with its wire manufacturing facilities in India, Sri Lanka & Thailand

Tata Steel certainly has one thing going for it as it tries to play in the global steel industry big leagues – that is financial firepower of the entire Tata

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Group. It is one of the India's biggest conglomerates with interest in everything from IT outsourcing to auto manufacturing

## **INDIAN STEEL INDUSTRY**

India's Steel Industry is more than 100 years old. Before the economic reforms of the early 1990s the steel industry was regulated and public sector dominated the industry. Tata Steel was the only major private sector company in the production of steel in India. SAIL and Tata Steel have traditionally been the major steel producers of India. In 1992, the liberalization of the India economy led to the opening up of various industries including the steel industry. This led to the increase in the number of producers, increase in investments in the steel sector and increased production capacity. Since 1991, more than Rs 20000 crores has been invested in the steel industry of India. India's steel industry went through an extremely rough patch between 1997 and 2001 when the overall global steel was facing a downturn and recovered after 2002. The major factors that led to the rebirth and growth of the steel industry in India after 2002 was the rise in global demand for steel and the domestic economic growth in India.

India has now become the eighth largest producer of steel in the world with a production capacity of 35 metric tonnes. Almost all varieties of steel are now produced in India. India has also emerged as an exporter of steel which shows that Indian steel is being increasingly accepted in the global market. The growth of the steel industry in India is also dependent on the level of consumption of steel in the domestic market. Steel consumption is significant in sectors like housing and infrastructure. In recent years the

surge in housing industry and real estate of India has led to increase in the domestic demand for steel.

**Challenges of Indian steel industry:**

- a) Infrastructure
- b) Red tape and corruption
- c) Ever increasing population
- d) Government policies and measures

Growth potential of steel industry:

The two major aspects that are expected to play a significant role in the growth of the steel industry in India are –

- Ø Abundant availability of iron ore in the country
- Ø The country has well established facilities for steel production

The major sectors where consumption of steel is expected to grow in the coming years are –

- Ø Construction
- Ø Housing
- Ø Ground transportation
- Ø Hi-tech engineering industries such as power generation, petrochemicals, fertilizers

## **THE GLOBAL STEEL INDUSTRY**

In global steel industry the consumption of steel has been decreased drastically in 2007, in comparison to 2006. According to International Iron and Steel Institute (IISI) till 2010 the average demand for steel would be 4.9 per cent per year. But during 2010 and 2015 the growth is expected to be 4.2 per cent. In fact IISI forecasts the global steel demand would be 1.32 billion tones by 2010 and 1.62 billion tones by 2015. Much of this demand growth is expected to be generated from countries like China and India. Among the major steel producing countries the production of steel has increased from 2005-2006 except Brazil. China is the highest steel producing country in the world with a production of 355.8 million tons in 2005 and 418.8 million tons in 2006. Growth of the steel industry in China is phenomenal. However, considering that China has a population of 1.4 billion, the per capita steel consumption is less than that of the developed countries. Indeed, while China has been continuously raising steel production for many years, it has also been importing substantial amounts of steel. It is only now that China has become a net exporter of steel. This means that China has also reached a level of saturation and its steel industry is more likely to witness more of consolidation and reorganization in coming years.

## **CORUS**

Merger of two companies, British steel & Koninklijke on 6th October 1999 gave birth to Corus group. Corus is Europe's second largest steel producer with annual reserves of Rs 83674 crores & crude steel production of 18.3 million tonnes in 2006. Corus has presence in nearly 50 countries, including its global network of offices and service centre

**Operations**

Corus main steelmaking operations were located in UK and Netherlands. It produces carbon steel by the basic oxygen steelmaking effort at 3 integrated steelworks in UK and 1 in Netherlands. Engineering steel was produced in UK using electric arc furnace method

There are three divisions of company namely Strip products, Long products and Distribution & building systems. The activities of each division are organized into individual business profit centre, each of which has its own managing director and management team.

**Market focus**

Corus delivers innovative solutions, differentiated products, reliable service and sound technical advice to its customer around the world. Principal end-market for Corus steel products are the construction, automotives, mechanical, packaging and electrical engineering, metal goods and oil and gas industries. Corus plays huge role in commercial and industrial construction and in moving to the residential sector in search of new opportunities. It is leading supplier to automotive sector and stands third in Europe in this sector. European union accounts for 80% of the total turnover in 2006. Within three division, steel division account for the 91% of the total turnover for Corus.

**THE ACQUISITION**

The acquisition process started on September 20, 2006 and completed on July 2, 2007. In the process both the companies have faced many ups and downs. The details and the timeline of the process are given below.

The official declaration of the completed transaction between the two companies was announced to be effective by Court of Justice in England and Wales and consistent with the Scheme of Arrangement of the Tata Steel Scheme on April 2, 2007. The total value of this acquisition amounted to £6.2 billion (US\$12 billion). Tata Steel the winner of the auction for Corus declares a bid of 608 pence per share surpassed the final bid from Brazilian Steel maker Companhia Siderurgica Nacional (CSN) of 603 pence per share.

Prior to the beginning of the deal negotiations, both Tata Steel and Corus were interested in entering into an M&A deal due to several reasons. The official press release issued by both the company states that the combined entity will have a pro forma crude steel production of 27 million tons in 2007, with 84, 000 employees across four continents and a joint presence in 45 countries, which makes it a serious rival to other steel giants.

The deal was a 100% acquisition and was to run by a Tata Steel subsidiary. Tata's had made their motive clear prior to acquisition which was to increase the market share and not the market revenue.

### **Management Structure after acquisition**

The merged entity is known as the 'Tata Steel Group'. It comprises of two entities:

- \* Tata Steel (which includes Tata Steel Thailand and NatSteel Asia)
- \* Corus

Each of the above two entities has an Executive Committee. A Joint Executive Committee sees the overall performance of the Tata Steel Group.



Mr. Ratan Tata chairs the merged entity. The Corus Executive Committee is headed by the CEO Mr. Philippe Varin and its board is chaired by Mr. James Leng. Tata Steel Executive Committee is chaired by its MD Mr. B.

Muthuraman. No major changes were made in the top management of either side after the acquisition. Specifically, the top management of Corus was retained. The boards now share some members from each side. For example, Mr. James Leng acts as the Non-Executive Deputy Chairman of the Board of Directors of Tata Steel.

### **TIMELINE**

The deal went through some twists due to Brazilian Steel maker CSN's counter offers. It finally concluded after an auction in January 2007 and became effective in April 2007.

- \* 2005: Corus board decides on strategic alliance or merger as the best next option. Tata Corus first contact regarding a possible deal.
- \* October 20, 2006: Corus board accepts 455 pence per share takeover offer by Tata Steel, and recommends it to its shareholders
- \* November 17, 2006: Brazilian CSN approaches Corus with a proposal of 475 pence per share
- \* January 31, 2007: Tata Steel wins auction (608 p/share against CSN's last bid of 603 p/share)
- \* April 2, 2007: The deal became effective after shareholder, court approvals

The deal process was otherwise smooth and going by their press statements during the process, the top management of Corus seemed pretty happy and comfortable with the acquisition. It may be remarked here that CSN was involved in a failed merger with Corus in 2002.

**Financing the deal**

Tata financed only \$4 billion of the Corus purchase from internal company resources, meaning that more than two-thirds of the deal had to be financed through loans from major banks. The day after the acquisition was officially announced, Tata Steel's share fell by 10.7 percent on the Bombay stock market. Tata's new debt amounting to \$8 billion due to the acquisition, financed with Corus' cash flows, expected to generate up to \$640 million in annual interest charges (8% annual interest cost). This amount combined with Corus' existing interest debt charges of \$400 million on an annual basis implied that the combined entity's interest obligation would amount to approximately \$725 million after the acquisition.

**AFTER THE DEAL: INTEGRATION PLAN, PERFORMANCE SO FAR**

The deal created world's fifth largest steel producer, adding to the ongoing consolidation of the global steel industry.

**“Light Touch” Integration, Execution plan**

Integration issues are responsible for a relatively high failure of international M&As. Both Corus and Tata knew this from their past experiences. Corus was formed by merger of British Steel and Dutch K. H. N. V. (which was followed by a not so smooth integration), and Tata Group had experienced several international M&A's itself since 2000s (including two recent ones in Tata

Steel). All this experience was used in designing integration plan for Tata-Corus. Tata companies tried to understand the culture of the country where M&A's were to take place, as well as the working environment of that country, for skillful handling of post-merger issues.

A Strategic and Integration Committee (SIC) was set up to facilitate what was envisioned to be "light touch" integration across Corus and Tata Steel. Its goal was to develop common agenda for the group focusing on:

- \* Continuous Improvement
- \* Sharing of best practices
- \* Manufacturing excellence
- \* Cross fertilization of R&D capabilities
- \* Rationalization of costs across the businesses

This would create the foundation on which the group could pursue future growth. The integration was coordinated by a program office formed for the above purpose. Several teams having representation from both companies were set up to handle integration and strategic work streams.

In January 2008, an umbrella management team or "group centre" was created. It consists of senior Corus Group and Tata Steel executives, and is co-chaired by Tata Steel's managing director Mr. B. Muthuraman and Corus CEO Philippe Varin. It was set up to avoid duplication and ensure a common approach across key functions – technology, integration, finance, strategy, corporate relations, communications and global minerals. However, Tata

Steel and Corus will remain two separate brands for some more time. The directors overseeing various functions report both to Muthuraman and Varin. There are more than 20 working groups working on various issues. One of the key steps in integration is integrating raw materials (iron ore, coal). Tata Steel and Corus have already started joint sourcing and purchase of materials. They are also jointly exploring new iron-ore sources in Africa, Australia and Brazil. The idea in most cases is not immediately to fuse the functions but to plan activities in a coordinated manner (e. g. R&D). Mr. Tridibesh Mukherjee, who has been appointed as the group director for technology and integration operates from London. He earlier retired as deputy MD, Tata Steel in October 2007 and was appointed to the board soon after. Tata Steel appointed international consultant Accenture to look at performance issues as part of the integration process. Accenture's plan (Nov 2007) outlined sourcing and talent management as two areas where the two sides could gain the most from synergies. The group targets 40 mn tonne capacity by 2011-12, and a turnover of \$32 bn, with EBITDA of 25%.

**Results: Performance so far**

It is still a bit early to conclusively say whether the acquisition was a success. However, all signs look good and integration seems to have been progressing very well so far. In fact, the integration process has progressed faster than original plans.

\* The combined enterprise now has an aggregate crude steel production capacity of around 28. 1 million tones with approximately 82, 700 employees across four continents.

- \* Corus is leading group's " global safari", for example by planning global network alliances in automotive steel which has been identified as a key focus area for the group.

- \* The benefit from synergies that would be built between Tata Steel and Corus by 2010 was pegged at \$ 450 mn. Tata Steel's annual report (FY 06-07) mentions

" The leveraging of low cost intermediate products from India with further processing at Corus to produce high-end finished products, along with several operation-related initiatives will improve the competitiveness of Corus in the European markets while India will benefit from high-value, sophisticated finished products developed in Corus' R&D facilities. Further, the combined entity will foster cross fertilization of Research & Development personnel, and domain expertise in the automotive, packaging and construction sectors, in addition to the exchange of technology, best practices and expertise. An integration team is in place, which will drive the operations as one single virtual enterprise. The enthusiasm, support and acceptance of the acquisition by employees on both sides have been very heartening".

- \* The group is growing aggressively and targets 50 mn tonne capacity by 2015, adding another 25 mn tonne plus capacity through the acquisition route.

- \* No UK plants have been shut. In fact, new investments (e. g. £74 mn at the Port Talbot plant) have been announced indicating long term commitments. On the other hand, 500 job cuts<sup>7</sup> were announced in ' packaging steel' units

of Corus, and to reduce its capacity from 1.5 to 1.2 mn tonnes by 2008 end. This was however aligned with industry wide move based on overcapacity in Europe's packaging steel market.

## ANALYSIS

### **Why did Tata go for overseas acquisition?**

In early 2000's Indian economy was booming and expected demand for steel was higher than the actual potential of Indian Steel producers. With time, India starts growing at 8 per cent nominal GDP and Indian steel producers are expecting a bright future ahead. They planned to grow organically as well as inorganically to make best out of it.

Initial plan of Tata steel was to achieve a milestone of producing 7 million tonnes in 2007 and 30 million tonnes in 2015. Tata Steel produced about 5 million tonnes of steel the financial year ending March 2006 but with the changing opportunities in the world market they choose to expand inorganically and start evaluating options. There were little chances of mergers and acquisitions between two steel producers from within the country so they planned to expand outside India.

Sensing the need, Tata Steel started scouting for overseas presence through Greenfield or Brownfield projects early this century. The company's journey towards the globalization began with the announcement of its Greenfield Ferro chrome plant in South Africa in 2003 at Richards Bay as the possible location.

Having noticed the success of L N Mittal through overseas mergers and acquisitions, Tata Steel announced its interest in overseas acquisition

especially in Europe and USA. During the same period Corus's officials expressed their interest in China, Brazil and India for cheaper steel. This induced Tata Steel to cash in on the opportunity and decided to offer a bid for Corus. As Corus was also seen interested in setting up a modern steel distribution network in India, Tata Steel wanted to leave no stone unturned to mark its European presence. This led to finalising the deal between Tata and Corus which increased the total capacity of the company to around 23 million tonnes, making it the fifth largest steel producer in the world.

**Target Selection: Rationale**

The acquisition of Corus was an important strategic move by Tata Steel, and marks the further unlocking of its global strategy, in which the first moves were the acquisitions of NatSteel and Millennium Steel. Corus gives Tata Steel access to the developed and demanding markets of Europe in unison with a proven brand name. It was not a decision based on making Tata Steel a much larger company but to exploit the potential for significant synergies between Corus and Tata Steel in manufacturing, R&D, logistics, and sharing best practices.

Tata Steel Managing Director B. Muthuraman has pointed out the economic logic behind the deal. Despite the enormous price tag for Corus, the purchase price per ton amounts to half of what it would cost today to build those same assets from scratch. He said that the acquisition price tag values Corus steel-making capacity at about \$710 per ton which is far cheaper than starting from scratch.

Though Tata Steel was much smaller in terms of capacity, in terms of EBITDA it was almost the same size as Corus. There were also big synergies to be availed by combining two companies which would boost earnings.

This highlights the cost competitiveness of Indian firms in this buoyant sector and many other sectors. Part of this competitiveness comes from the abundant availability of raw material and human resources. Therefore, rather than being an exporter of raw material (iron ore, for example), many Indian firms have been able to integrate forward and access consumers in the foreign markets. Yet there is simply no steel company the size of Corus available in the market, so if a smaller player like Tata had aspirations to become a large player, this was perhaps the only one-stop move that Tata could make to do so.

The acquisition of Corus transformed Tata Steel from a domestic steel producer to an international steel company with global scale. The synergies derived from Tata Steel and Corus coming together were of tremendous strategic value to both organizations. The leveraging of low cost intermediate products from India with further processing at Corus to produce high-end finished products, along with several operation-related initiatives would improve the competitiveness of Corus in the European markets while India would benefit from high -value, sophisticated finished products developed in Corus' R&D facilities. Further, the combined entity would foster cross fertilization packaging and construction sectors, in addition to the exchange of technology, best practices and expertise



**For Tata Steel****Positives****Negatives**

- The acquisition was well aligned with its overall global expansion plan
- The deal would help it achieve global scale from its 56th position in terms of production to 5th in the world. This would translate into significant advantages in terms of price power in the global steel industry.
- Corus offered it a springboard for entry into the European market, and higher value qualities of steel. Though Corus was considered expensive in the short run, it was believed that the deal would be profitable in the long run.
- Corus also offered higher technological knowledge and environmental capabilities. This was a very big incentive.
- In terms of opportunity costs, this investment could prevent Tatas from making investments in India and other (possibly more lucrative) emerging markets. However, some of Tata's investment plans in India were stalled and awaiting political approval.
- Corus was debt ridden with low margins, and still expensive<sup>4</sup>. A downturn would make it highly vulnerable. Many analysts called this investment risky and overpriced, specially the price increased forced after CSN intervention. Tata's share prices fell massively immediately after the deal was made public.

**For Corus****Positives****Negatives**

- A chance to bail out of debt and financial stress, and become part of a winning combination. Corus had been looking for a buyer for two years.
- Access to cheap high quality iron ore
- Access to well established sales network of Tata Steel in developing markets.
- Unions worried that there will be job cuts. But analysts felt that some job cuts were inevitable even if Corus ran alone or with some other partner.
- Fears that UK plants will be shut down and production moved to India.
- Perception among some workers that an Indian entity could be a sub-standard entity.

Cost leadership strategy:

The Tata-Corus acquisition had many motives behind it. One of them was achieving cost leadership strategy. The deal between Tata and Corus was one involving two major steel producers in the world. After the acquisition, the total amount of steel produced by Tata Corus combined allowed Tata-Corus to move up to the 6th rank in terms of global production.

Few of the ways in which Tata-Corus deal allowed a cost leadership strategy are:

**1) Control of production and overhead costs:**

The deal allowed large amounts of production facilities under one entity which allowed Tata-Corus to achieve economies of scale. As a result of which various costs related to production of steel could be reduced.

**2) Minimization of marketing and R&D cost:**

Corus ideally has a good stronghold in Europe especially United Kingdom. Tata steel has a good stronghold in the Indian subcontinent. The deal allowed both the companies to expand their presence geographically. As a result of which marketing costs decreased to a great extent. There also was exchange of technical knowledge related to steel production which further led to a reduction in R&D cost

**Transnational strategy:**

Tata steel followed a transnational strategy by acquiring Corus. As can be explained by the figure below, Tata-Corus is an entity which has focused on global integration as well as catered to local needs.

**Transnational strategy benefits for Tata steel:**

- Increase in market share due to cumulative addition of production capacities
- Return on investment increased due to more than proportionate increase in profits than costs
- Economies of scale or learning
- Competitive advantage through location due to global distribution and presence.

**Benefits of TATA-CORUS merger deal to the stakeholders of TATA Steel****Capital Market shareholders:**

Whenever a strategic move of this scale is made (where a company takes over a global major with nearly four times its capacity and revenues), it is clearly a long-term call on the structural dynamics of the sector. And investors will have to weigh their investment options only over the long run. Over a long time-frame, the management of the combined entity has far greater room to manoeuvre, and on several fronts. If you are a long-term investor in Tata Steel, the key developments that bear a close watch are:

1) Progress on low-cost slabs: Research shows that steel-makers in India and Latin America, endowed with rich iron ore resources, enjoy a 20 per cent cost advantage in slab production over their European peers. Hence, any meaningful gains from this deal will emerge only by 2010, when Tata Steel can start exporting low-cost slabs to Corus. This is unlikely to be a short-term outcome as neither Tata Steel's six-million-tonne greenfield plant in Orissa nor the expansion in Jamshedpur is likely to create the kind of capacity that can lead to surplus slab-making/semi-finished steel capacity on a standalone basis. Second, there may be further constraints to exports as Tata Steel will also be servicing the requirements of NatSteel, Singapore, and Millennium Steel, Thailand, its two recent acquisitions in Asia. However, this dynamic may change if the Tatas can make some acquisitions in low-cost regions such as Latin America, opening up a secure source of slab-making that can be exported to Corus's plants in the UK. Or if the iron ore policy in India undergoes a change over the next couple of years, Tata Steel may be able to explore alternatives in the coming years.

2) Restructuring at Corus: The main reason this deal for Tata Steel is access to the European market and significantly higher value-added presence. In the long run, there is considerable scope to restructure Corus' high-cost plants at Port Talbot, Scunthorpe and the slab-making unit at Teesside. The job cuts that Tata Steel is ruling out at present may become inevitable in the long run. Though it may be premature at this stage, over time, Tata Steel may consider the possibility of divesting or spinning off the engineering steels division at Rotherham with a production capacity of 1 million tonnes. The ability of the Tatas to improve the combined operating profit margins to 25 per cent (from around 14 per cent in 2005) over the next four to five years will hinge on these two aspects. In our view, two factors may soften the risks of dramatic restructuring at the high-cost plants in UK.

**Product Market Shareholders:**

Tata has given name of this combined entities as Tata Group but they have retained the separate working of the both the companies. This will help them retaining their customers and also help Corus to provide the customers with the supplies as committed earlier.

Tata is planning to take advantage of the strong suppliers of Corus to TATA which will help them synergize more and also improve the relation between suppliers and Chorus.

Tata's have announced that there will be no layoffs due to this acquisition which strengthens their relations with the unions of both Corus and Tata.

**Organisation Stakeholders**

As there would be no layoff due to this acquisition so the employees will not be at a disadvantage in any manner but they will prosper as their span of responsibilities increases. Especially managers are going to be benefited most as they will get chance to work on overseas projects and will be able to handle more diverse portfolio.

**Exhibit 1****Long Term Strategy**

- 4 MTPA
- Single Location
- National
- Small & Vulnerable
- Low Cost Production
- World class
- operating practices
- EVA positive

**Exhibit 2****Exhibit 3**

2002

2003

2004

2005

2006

2007

2008

China

182, 366

222, 336

282, 911

353, 240

419, 149

489, 288

500, 312

United States

91, 587

93, 677

99, 681

94, 897

98, 557

98, 102

91, 350

Japan

107, 745

110, 511

112, 718

112, 471

116, 226

120, 203

118, 739

Russia

59, 777

61, 450

65, 583

66, 146



70, 830

72, 387

68, 510

Germany

45, 015

44, 809

46, 374

44, 524

47, 224

48, 550

45, 833

India

28, 814

31, 779

32, 626

45, 780

49, 450

53, 468

57, 791