

## Learning Objectives

- Strategic Negotiations
  - Use of Media for Bargaining
- Preparations before Starting the Strategic Negotiations
- Possible Outcomes of a Strategic Negotiation
- Salvaging a Failed Strategic Negotiation
- Valuation of Partner Contributions
- Pointers to Manage Risk and Increase Chances of Success in Strategic Negotiation

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## Chemical Industry bracing for tough times ahead

- Annual Revenue of Global Chemical Industry at \$3 trillion in 2007
  - Operating profits were up by 12%
  - Growth propelled by Emerging Markets in Asia & Latin America
- However, the future business environment was not encouraging
  - Oil prices were on the rise
  - US growth stunted due to weak housing market
  - Automobile industry expected to fall
- Hence, the Industry was consolidating
  - SABIC & GE Plastics
  - Basell & Lyndell Chemical

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## Dow losing the battle against low-cost competitors in Asia

- Dow Chemical Company was the 2<sup>nd</sup> largest chemical company by sales in 2007, behind BASF.
  - Total revenue \$53 billion; net income \$2.9 billion; 46000 employees in 75 countries; 5000 products
  - Basic chemical business (50%) – low margin/high-volume
  - Performance chemical business (50%) – high margin/low volume
- Andrew Liveris, CEO since 2004
  - Moved away from commodity chemicals due to price-war
  - JVs to reduce capex in basic chemical; redeploy capital in performance chemical



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## KPC suffered from Political Meddling and slow decision making

- Kuwait Petroleum Corporation (KPC) was an integrated state-owned national oil company
  - 7<sup>th</sup> largest oil and gas company by reserves
  - Kuwait controlled 10% of global oil reserves, ranked 5<sup>th</sup> in the world
  - KPC was under the dual control of the Supreme Petroleum Council (SPC) and the National Assembly
- Saad Ali Al-Shuwaib became CEO in 2007
  - Western-educated bureaucrat
  - Tasked with increasing crude production and with a strong focus on upstream to increase Govt revenue
  - JVs to increase international downstream operations



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## Dow & KPC announced plans for a JV worth \$9.5 billion named K-Dow

- **Dec 13, 2007:** 50:50 JV to manage five major chemical businesses
  - As part of its 50% contribution, Dow was to give 50% of its business interest in 5-chemical businesses to the JV
    - KPC was to provide \$9.5 billion cash to Dow for the other 50%
  - Dow would give 90% of its basic chemical business, comprising 22% of revenues, to the JV.
  - JV was expected to have \$11 billion in sales in the first year with 5000 employees.
  - The JV would give Dow access to Kuwait Oil & Gas reserves to produce performance chemicals and reinvest cash.
  - The JV would give KPC access to technology and expertise to diversify.

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## Dow got a sweat deal, but it would take one more year to finalise

- Dow received an attractive asset valuation, which was widely reported in the media.
- JP Morgan advised KPC and Dow on the K-Dow transaction, even though they were long-standing clients of Dow.
- Liveris commented at a press conference that the deal was the “penultimate” step in Dow’s transformation.
- Liveris received an interview invite from Joe Kernan at *Squawk Box* on CNBC.
  - Do you grant the interview? And if so, what are your objectives?
  - Do you have an answer to the inevitable valuation question?

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## Strategic negotiations is the interaction between strategy and negotiations

- Strategic Negotiations are bigger than the bargaining table.
  - Strategic Negotiations in the context of IJVs involve the process of reaching mutually beneficial agreements with potential partners on key aspects of the venture, such as ownership structure, governance mechanisms, resource allocation, and risk-sharing arrangements.
  - Strategic Negotiators must navigate complex issues, address conflicting interests, and find creative solutions to achieve a win-win outcome.
  - Effective strategic negotiation tactics include active listening, relationship-building, problem-solving, and compromise.

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## Steps to consider before going into Strategic negotiations

### 4 Steps of the Negotiation Process

- 1 **PREPARATION:** Preparing in advance can improve your confidence, give you clear goals to work toward, and provide a strategy to base your approach on.
- 2 **BARGAINING:** Bargaining is about creating value for both you and other parties despite your differences.
- 3 **CLOSING:** Closing a negotiation can mean coming to an agreement or ending the discussion without reaching one.
- 4 **LEARNING:** Reflecting on the process and learning from your experiences enables you to become a better negotiator.



### How to Develop a Negotiation Strategy

- 1 Define your role
- 2 Understand your value
- 3 Consider your counterpart's vantage point
- 4 Check in with yourself



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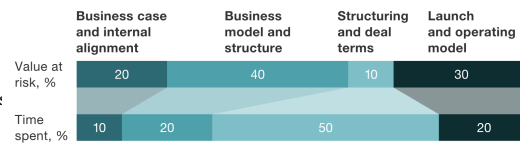
## Preparation before a Strategic negotiation to discover your BATNA is vital

An alliance is a negotiated relationship. It is inherently unstable, as changing the initial conditions renders the initial negotiation obsolete, requiring reconfiguration or termination.

Role play & practice negotiation: to agree on the worst positions that can be conceded.

- This will involve discovering a credible **BATNA** (Best Alternative to Negotiated Position)

Joint-venture planners spend more time on phases of negotiation that create less value.



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## Possible outcomes of Strategic negotiations

In strategic negotiations, two frequently **conflicting** aims must be simultaneously achieved.

- How do we configure the collaborations to achieve the greatest possible competitive advantage for the JV?
- How do we get the best deal for the company?



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## Possible Structures for Ownership and Control that can result from Bargaining

- Dominant Parent:** One parent runs the alliance (most likely in an equity relationship) as a virtual subsidiary.
- Shared Management:** both parents have large and approximately equal influence, often through a joint board structure.
- Split Control:** each parent is responsible for some part of the alliance operations.
- Independent Management:** neither parent is actively involved, and the alliance managers operate largely as an independent organization.
- Rotating Management:** designated management teams from each parent, serve terms and positions of authority.

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## Valuation of Partner Contributions in Collaborations

- This often takes the form of a series of projects, each of which needs to be save separately resourced, and provided with an action plan.
- Thus, the valuation of the partners contribution is never finished.
  - Each new project requires new estimates.
- Royalties and consultancy fees can be used as techniques to reach an accommodation.

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## Valuation of Partner Contributions in Equity Joint Ventures

- If one partner is unable to provide the necessary financing, he may be asked to supply raw materials, provide free consultancy advice or at a per diem, second key personal to the venture and provide blueprints and other proprietor information to the joint venture.
- The new joint venture company is generally allowed to take on loans at rate of interest repayment to be made from joint-venture profit, but with the loan often guaranteed by the joint-venture partners.

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## Contribution of a Conventional Company to the Valuation in an IJV

1. **Trade name:** if it is a new one bought of the shelf, its value will be zero. Else, the market is searched for a trade name of similar reputation that is licensed, and this is used as a guide for royalty level to be applied.
2. **Property:** the factors affecting the valuation will include the cost of the asset, the specificity of the asset, its replacement value and its net present value calculated on the basis of income stream. It is expected to generate.
3. **Inventory:**

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## Contribution of a Conventional Company to the Valuation in an IJV

4. **Working capital:** usually valued at phase value, unless there are reasons for discounting it to some degree as with possible, bad debts that are taken over.
5. **Management:** existing salary levels can be used as a guide guide to contribution value. If new management needs to be recruited, the cost of such recruitment needs to be allocated for an agreement made as to who will be them.
6. **Technology transfer:** time-based valuations, or royalties on subsequence sales using the new technology.

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## Contribution of a Web-Based Company to the Valuation in an IJV

- **Technology:** the fees that would be charged to a third-party.
- **Computer equipment:** valued at market rates after depreciation.
- **Technology, expertise, and research skills:** the valuation should reflect the sun cost of past technology development that had brought the company to its current state of technology strength.
- **Intellectual property, e.g., patents:** this will probably be licensed rather than absolutely contributed, and once more, the cost of such licensing can be treated in a capitalized royalty fashion.
- **Contact network:** although undoubtedly, a major contribution, it is really given a value figure in any valuation.

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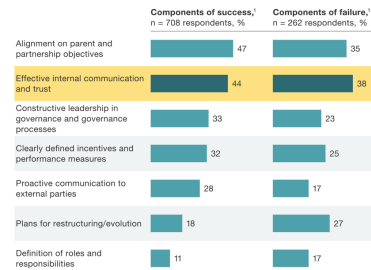
## Salvaging failed or stuck Strategic negotiations using GRIT

Strategic negotiations fail as some firms enter discussions purely to gain competitive intelligence about a technology, specific vendors, or customers and have no serious intent to complete the negotiations.

**GRIT** (graduated reciprocation & tension reduction) needs to be initiated in case of conflict or failure.

- This involves role reversal, keeping the number of issues under control.
- It involves concession exchange aided by problem-solving discussion.

Success and failure in joint ventures often hinge on trust and communication.



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## Key points in strategic negotiations to mitigate risks and increase the chances of success in IJV

### 1. Comprehensive Due Diligence:

- Conduct thorough due diligence on the potential partner and the market.
- Even before negotiations begin, it is important to know your potential JV partner and the expectations of both companies in the venture.
- This also means evaluating how the “pie” could be expanded if the parties decide to form a JV.
- In the case of K-Dow, issues arose due to an inadequate understanding of market conditions and regulatory challenges.

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## Key points in strategic negotiations to mitigate risks and increase the chances of success in IJV

### 2. Alignment of Objectives

- Ensure that both parties have aligned objectives and expectations from the joint venture.
- For both parties, there should be a synergy if operations were combined, as opposed to each of them investing a lot of resources to produce similar results.
- Misalignment in goals can lead to conflicts, as seen in the case of K-Dow, where differences in strategic priorities emerged.

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## Key points in strategic negotiations to mitigate risks and increase the chances of success in IJV

### 3. Legal and Regulatory Compliance

- Understand and adhere to the legal and regulatory frameworks of the countries involved.
- The failure of K-Dow was partially attributed to regulatory hurdles faced in Kuwait.

### 4. Risk Management

- Identify potential risks and develop strategies to mitigate them.
- Factors such as geopolitical instability and economic volatility, which affected K-Dow, should be carefully considered and planned for.

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## Key points in strategic negotiations to mitigate risks and increase the chances of success in IJV

### 5. Clear Governance Structure

- Establish a clear governance structure outlining decision-making processes, roles, and responsibilities.
- The lack of clarity in governance contributed to conflicts within K-Dow, leading to its dissolution.

### 6. Cultural Sensitivity and Communication

- Recognize and respect cultural differences between partners to foster effective communication and collaboration.
- Cultural misunderstandings were cited as a contributing factor to the challenges faced by K-Dow.

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## Key points in strategic negotiations to mitigate risks and increase the chances of success in IJV

### 7. Financial Viability and Funding

- Ensure the financial viability of the joint venture and secure adequate funding.
- Check if potential JV partners have high levels of debt and need deleveraging.
- Knowing a potential JV partner is experiencing tight liquidity is useful information during negotiations, as they would want to sell their assets at a premium.
- Financial considerations, including the global economic downturn, played a role in the failure of K-Dow.

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## Key points in strategic negotiations to mitigate risks and increase the chances of success in IJV

### 7. Flexibility and Adaptability

- Remain flexible and adaptable to changes in market dynamics and business environments.
- Treating potential JV partners as mid- to long-term strategic partners is very important.
- The inability to adapt to changing circumstances was detrimental to the sustainability of K-Dow.

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## Key points in strategic negotiations to mitigate risks and increase the chances of success in IJV

### 9. Conflict Resolution Mechanisms

- Establish mechanisms for resolving conflicts and disputes in a fair and efficient manner.
- The lack of effective conflict resolution mechanisms exacerbated tensions within K-Dow.

### 10. Long-Term Vision and Commitment

- Maintain a long-term vision for the joint venture and demonstrate commitment to its success.
- Short-term thinking and lack of sustained commitment were cited as contributing factors to the failure of K-Dow

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## Recap

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