Incwert Valuation Chronicles
Series 2 I 2023

An insight into **HoldCo Discount**

Holding company or “Conglomerate” discount analysed across major sectors in India

February 2023

Valuation | Research

Foreword

We are pleased to release the third edition of Incwert's holding company discount ("HoldCo Discount") study 2022, based on the analysis of select listed holding companies across major sectors in India.

The study could be of importance to the valuation professionals when dealing with the quantum of discount to be applied for valuing the holding of a minority shareholder in an entity that is essentially an investment vehicle. The empirical evidence based on market data may also be a reference for addressing the holdings in a private conglomerate.

A holding company or conglomerate discount occurs when a holding company's market capitalisation is less than the sum of the investments and other net assets that it holds. The level of discount is the difference between the aggregate value of each investment in the conglomerate and its market capitalisation.

The results indicate that the discounts, influenced by several factors – industry, sector, timing within the economic cycle, multi-layer subsidiaries, reporting complexity and market capitalisation, vary across time and sectors.

We hope you find the results of our study of interest and value.

Key findings of our HoldCo Discount study, 2022 are:

- The median HoldCo discount in FY22 is approximately 71 per cent across the major listed holding entities in India.

What's a HoldCo?

Pyramid holding structure, interlocked ownerships and voting pacts typically characterise an investment holding entity.

These structures allow the ultimate owner to maintain control over a large group of companies through cascades of holding entities coupled with cash flows usually limited to dividends declared by the operating entities.

About Authors

Punit brings with him 19 years of experience in sell-side and buy-side advisory across equity and fixed income. He has worked on several bespoke valuations and lent research support to dozens of asset managers/investment bankers/brokers/consulting firms across the globe.

In the fixed-income segment, he worked as a fundamental analyst across the capital structure: leveraged loans, distressed debt, insolvency/bankruptcy situations and high-yield asset classes. He has also helped sell-side & consulting firms increase their market presence by coming up with thematic and white-label papers.

He started his career as an analyst with Zacks Investment Research, was a part of a UK-based CLO manager's research team, and then moved on to set up research practices for a couple of startups before becoming the Global Head of Research at one of the largest BPO/KPO globally and finally co-founded Incwert.

He won 40 under 40 Alternative Professionals Awards 2020 by AIWMI.

Sunit has an overall experience of over 17 years in valuation advisory, transaction advisory and M&A advisory.

As a valuation professional, Sunit has undertaken valuations of businesses for transactions, fundraising, strategic decision-making, and corporate restructuring. He has also undertaken valuations of intangible assets, financial instruments, option valuation, litigation support, private equity portfolio valuation and valuation for reporting purposes such as purchase price allocation and impairment test under IFRS and Indian GAAP.

In past he has worked with KPMG India (as Associate Director), BDO, Grant Thornton, KPMG UK, and DBDBS a boutique M&A advisory firm.

Sunit has also been an active speaker on valuation at the National Institute of Finance Management (NIFM).

Professor Divya Aggarwal holds a Ph.D. in Finance from XLRI – Xavier School of Management. She has completed The Fellow Programme in Management from XLRI which is a full-time, residential doctoral programme. She is a Company Secretary (the Institute of Company Secretaries of India) and has done her Bachelors in Finance & Investment Analysis from the Delhi University. Her corporate work stints include working in corporate finance roles with McKinsey Knowledge Centre, KPMG, and investing banking roles with Avendus Capital. Before embarking on an academic career, she was working as an AVP in the financial planning team at SwissRe, a leading reinsurance firm.

In 2020 she got featured in the AIWMI list of "India's top 100 women in finance 2020" under the progressing category. She is a recipient of many awards and scholarships including "Peter Drucker essay competition 2014", "The Case Centre scholarship" and best paper awards at several national conferences.

Her research work has been published in international journals like the Journal of Behavioural and Experimental Finance, Research in Economics and Qualitative Research in Financial Markets. She has presented her research work in several national conferences like Pan-IIM, ISDSI, etc. along with international conferences such as biannual meetings of SPUDM.

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- Embedded derivatives
- Hybrid securities
- Forward agreements
- Non-controlling interests
- Loan portfolios
- Swaps
- Right of Use (ROUs)
- Commodities
- Warrants

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ABOUT INCWERT

Incwert focuses on rendering services in the area of valuations and financial research. As a leading valuation advisory firm in India, it supports clients across life cycles (from early-stage to mature) on valuations concerning the transaction, tax and financial reporting. Incwert is trusted by the clients for its incisive research which forms the basis of credible advice. The company also offers offshore valuation support services which include setting up valuation models and report writing.

Incwert's client footprint is across cities & metros in India and globally in the US, UK, Singapore and middle-east. Incwert has offices in Delhi (NCR) and Mumbai, along with Kolkata and Surat where it has affiliate/network partners.

In India, Incwert is registered with The Insolvency and Bankruptcy Board of India as a Registered Valuer Entity.

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DATA SOURCES

For producing the analysis, we have extensively relied on data available as part of the company filings, NSE, BSE, other publicly available information and proprietary database providers.

The information and data presented in the study have been obtained with the greatest of care from sources believed to be reliable but are not guaranteed to be complete, accurate or timely.

Acknowledgements

CA Sunit Khandelwal (Author),
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We thank CA Allen Vincent and Anurag Garg of Incwert for their assistance in assembling the exhibits presented herein and other team members of Incwert for keen insights and assistance in quality check.

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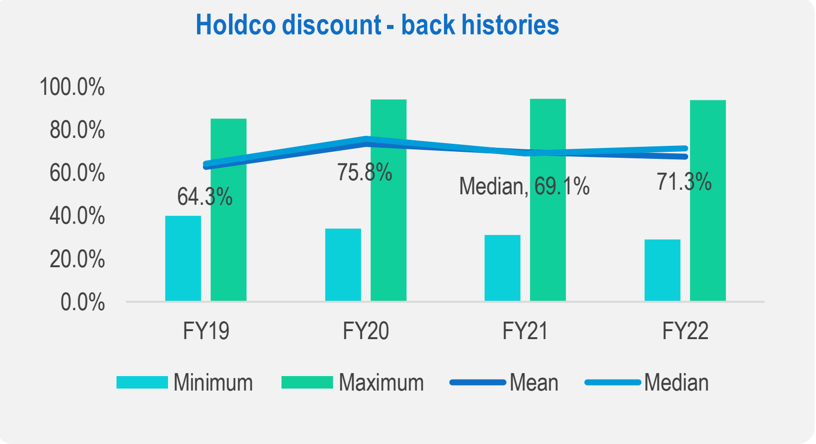
The median HoldCo discount observed in the Indian listed space during FY22 is 71.3 per cent

FY22 Sample size: 27 companies

67% Average	71% Median
29% Minimum	94% Maximum



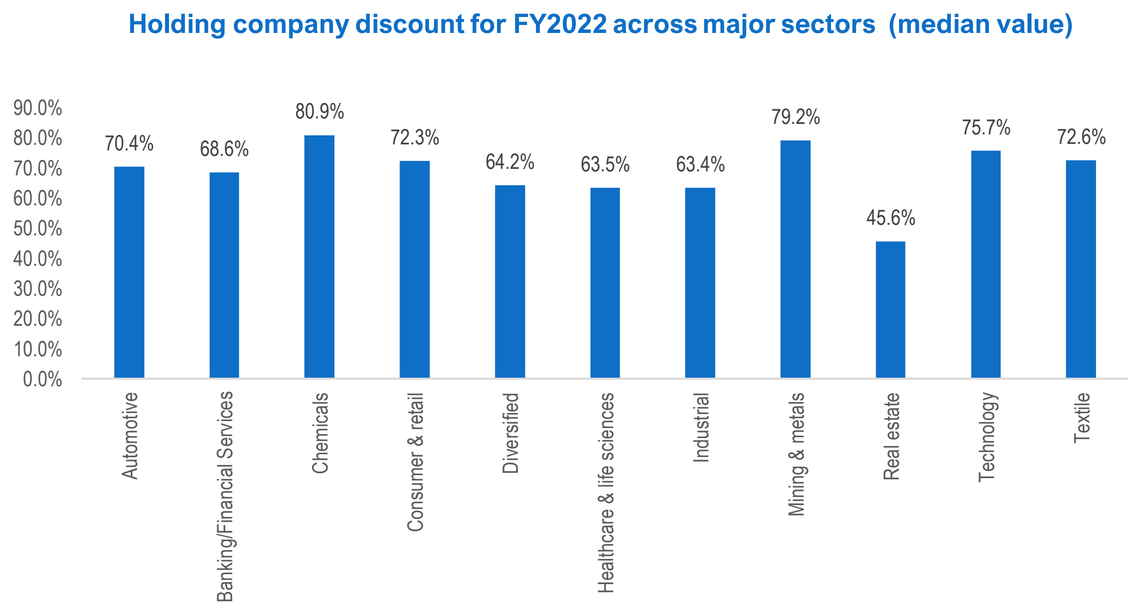
Note: The analysis for FY22 considers a sample size of 27 conglomerates or holding companies listed in the BSE/NSE.
Source: Incwert analysis based on annual reports of companies selected for the study and market price from NSE/BSE.

The range of discounts is driven by:

- Industry, sector and timing within the economic cycle
- Quality of investments held by the HoldCo
- Level of earnings from dividend and interest, and subsequent distribution to shareholders of HoldCo
- The complexity of reporting structure. Minority shareholders tend to discount companies that have complex structures as information on businesses may not be available/accessible on time
- Multi-layer of subsidiaries results in the parking of assets/liabilities in SPVs. Marginal investors at times, do not have relevant information to value such subsidiaries/investments.
- Cross holding in other private companies potentially results in a lack of comprehensibility.
- Cascading effect of dividend distribution tax in a multi-tier structure.

Conglomerate's holding in subsidiaries/associates/JVs, which can be direct, indirect or cross structured, is usually targeted to improve strategic holding of the promoter group. Such structured holdings help in building capital synergies by employing planned procurement, coordination and allocation of resources.
Despite such holding structures showcasing similarities to holdings by private equity funds, the possibility of a planned exit and liquidation event is usually remote. This aspect causes the prices of holding companies to diverge compared to their net asset value ("NAV") for the minority shareholders.
Stocks of holding companies thus mostly tend to yield less value compared to their NAV.

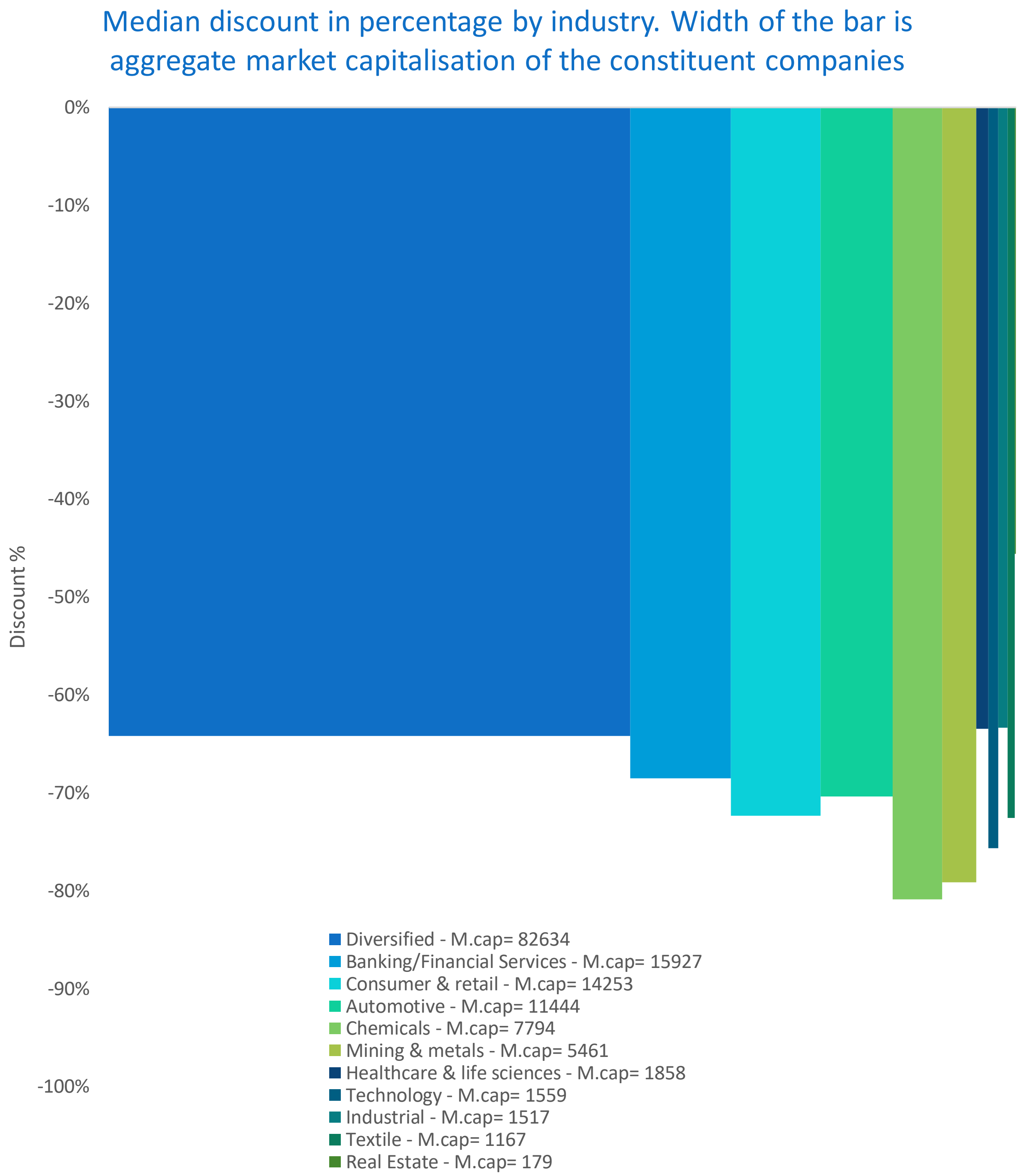
HoldCo discount by sectors



Note: The analysis considers a sample size of 27 conglomerates or holding companies listed in the BSE/NSE.
Source: Incwert analysis based on annual reports of companies selected for the study and market price from NSE/BSE.

Distribution of Holdco discount by select companies

Diversified sector followed by Banking/Financial services sector have the highest weight in the distribution of HoldCo discount



Note: The analysis considers a sample size of 27 conglomerates or holding companies listed in the BSE/NSE.
The total market capitalisation shown in the above chart is in INR crore.

Source: Incwert analysis based on annual reports of companies selected for the study and market price from NSE/BSE.

Methodology deployed

- Listed companies in India that are systemically structured to carry on the business as an investment company or that have a fairly low stand-alone revenue from operations compared to the revenue on a consolidated basis were identified and considered for the analysis.

- The implied holding company discount is calculated by comparing the market value of the listed holding company with its Net Asset Value (NAV).

  Holding company discount (INR) = NAV - Market value of holding company

  $$\text{Holding company discount (\%)} = \frac{\text{Discount amount}}{\text{NAV}}$$

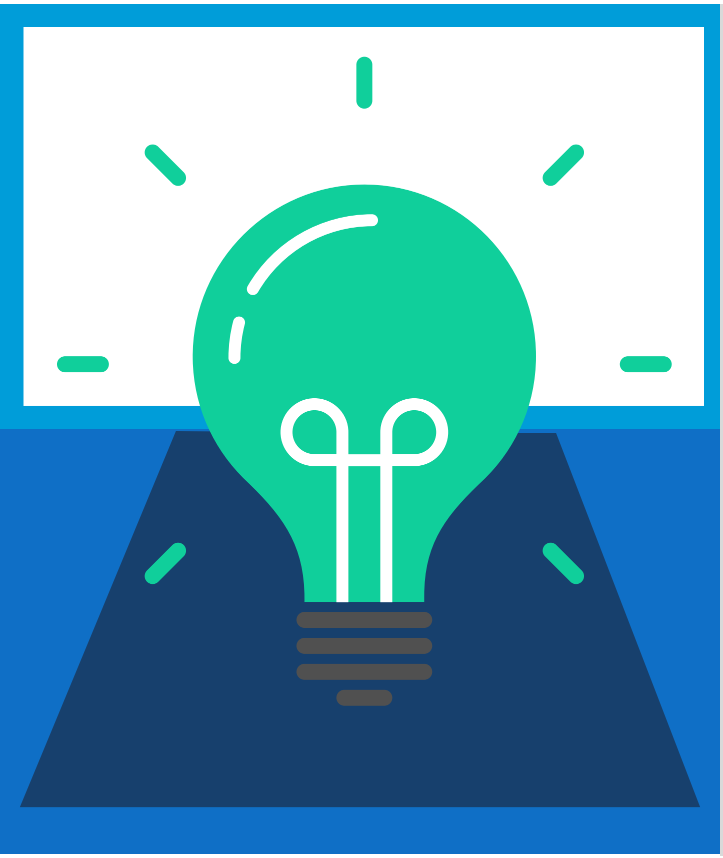
  Net Asset Value = Total value of assets - Total value of liabilities

- Total value of assets include long term and short-term investments in subsidiaries, associates, joint venture and equity shares (quoted and unquoted); gross block; other current assets

- Total value of liabilities includes all current and non-current liabilities.

- Listed investments in subsidiaries, associates and joint ventures are taken at market value and balance investments at book value. Investments in subsidiaries, associates and joint ventures are calculated by multiplying the percentage holding with its market value as of the cut-off date.

- All other assets and liabilities are considered at book value.



Subsidiaries, associates and joint ventures listed on stock exchanges in India have been revalued based on their period-end market price.

Other net assets have been considered at book value.

Understanding the HoldCo study…

1 What is Holding company?

A conglomerate or a holding company typically exhibits the following characteristics:

- does not have any material business operations of its own;
- exists mostly to own assets via holding controlling stock or membership interests in other companies;
- primary revenue is dividend income and interest earnings;
- operating income tends to be consistently less than the value of the assets that it holds.

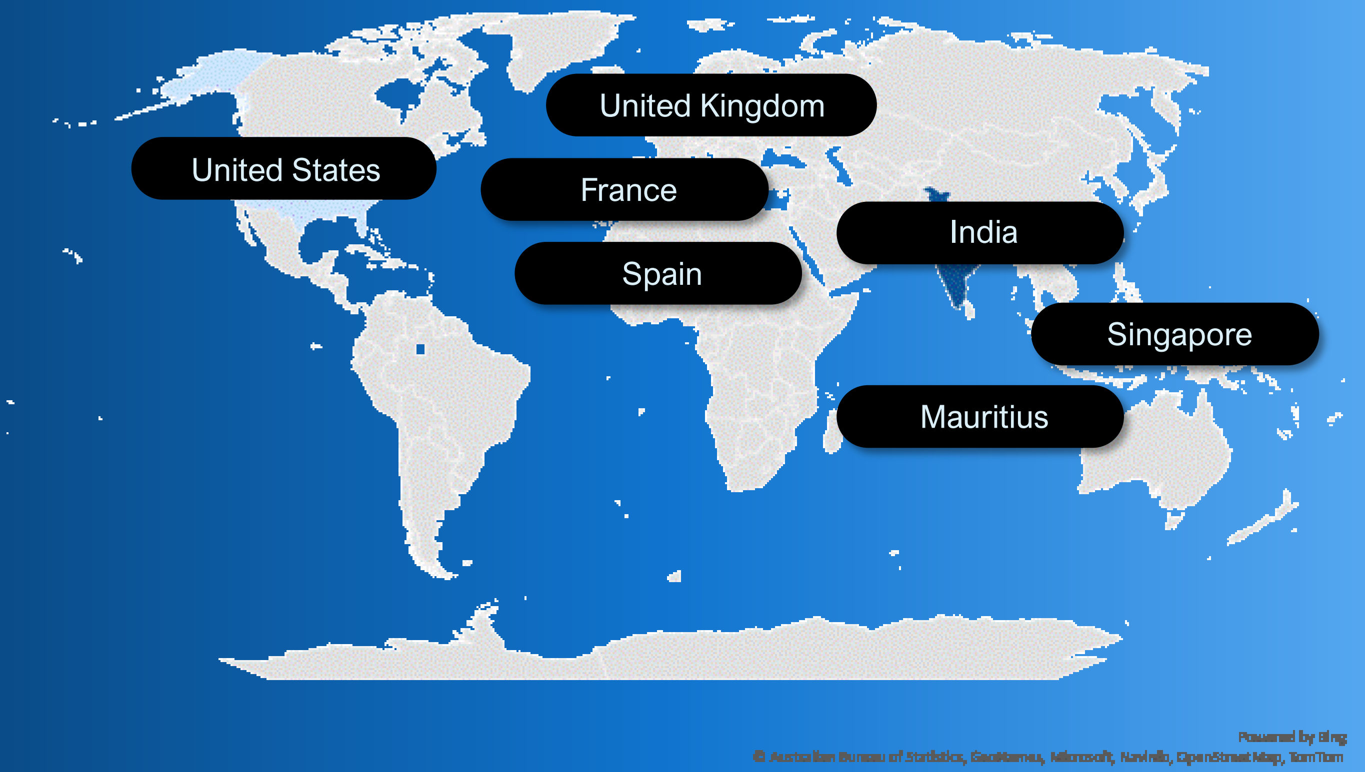
2 Why Holding company discount arises?

- Holding companies are more complex to analyse and determine the true value versus the value of their operating assets
- Holding companies tend to be a sum of disjointed businesses which an investor is forced to buy even though he/she does not like a specific investment of HoldCo
- Holding companies are mostly promoter-driven companies and hence the actions may not suit the return and risk objectives of the minority shareholders
- Holding companies usually are valued based on the liquidation value of the investments. However, such liquidation value may not be realised as the holding company will rarely sell their investments in group companies due to strategic/ synergistic benefits.
- Internal policies could prevent the holding company from realising the value of shares which may also get factored into the discounted pricing.

3 Limitations

- The value of holdings other than quoted investments in subsidiaries/associates is taken at book value.
- Value roll-up has been performed for the first level of holdings. Investments of step-down subsidiaries/associates have not been considered.
- Market prices as at the period end have been considered.
- We have covered only 4 years up to FY2022 under the HoldCo Discount study due to change in the treatment of investments in the books of accounts post-implementation of Ind AS.

Client footprints across India and outside



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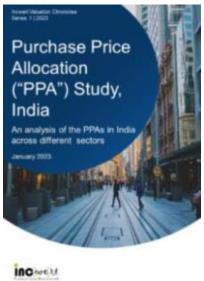

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November 2022

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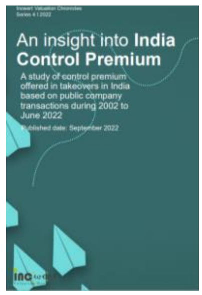

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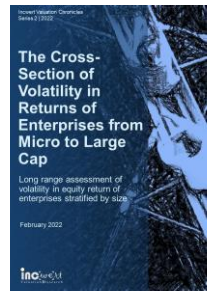

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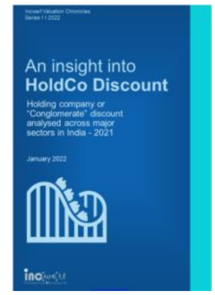

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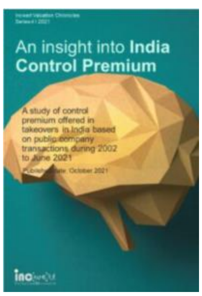

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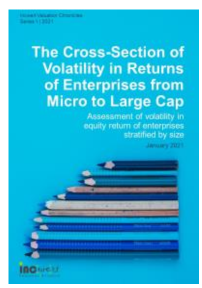

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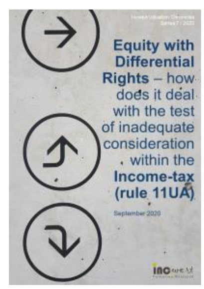

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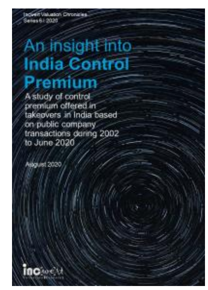

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- July 2020

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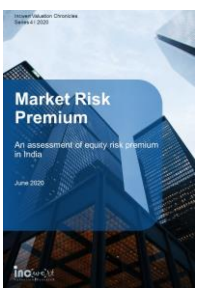

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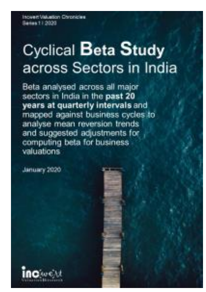

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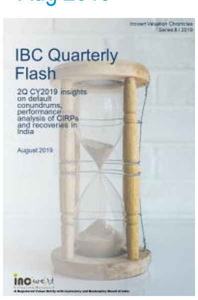

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- Jun 2019

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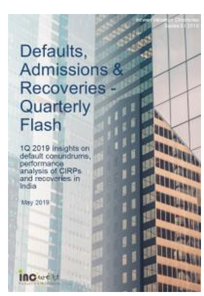

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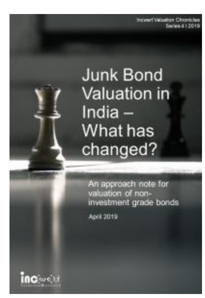

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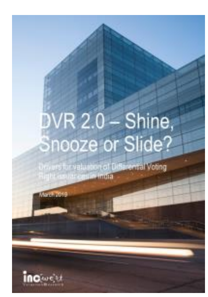
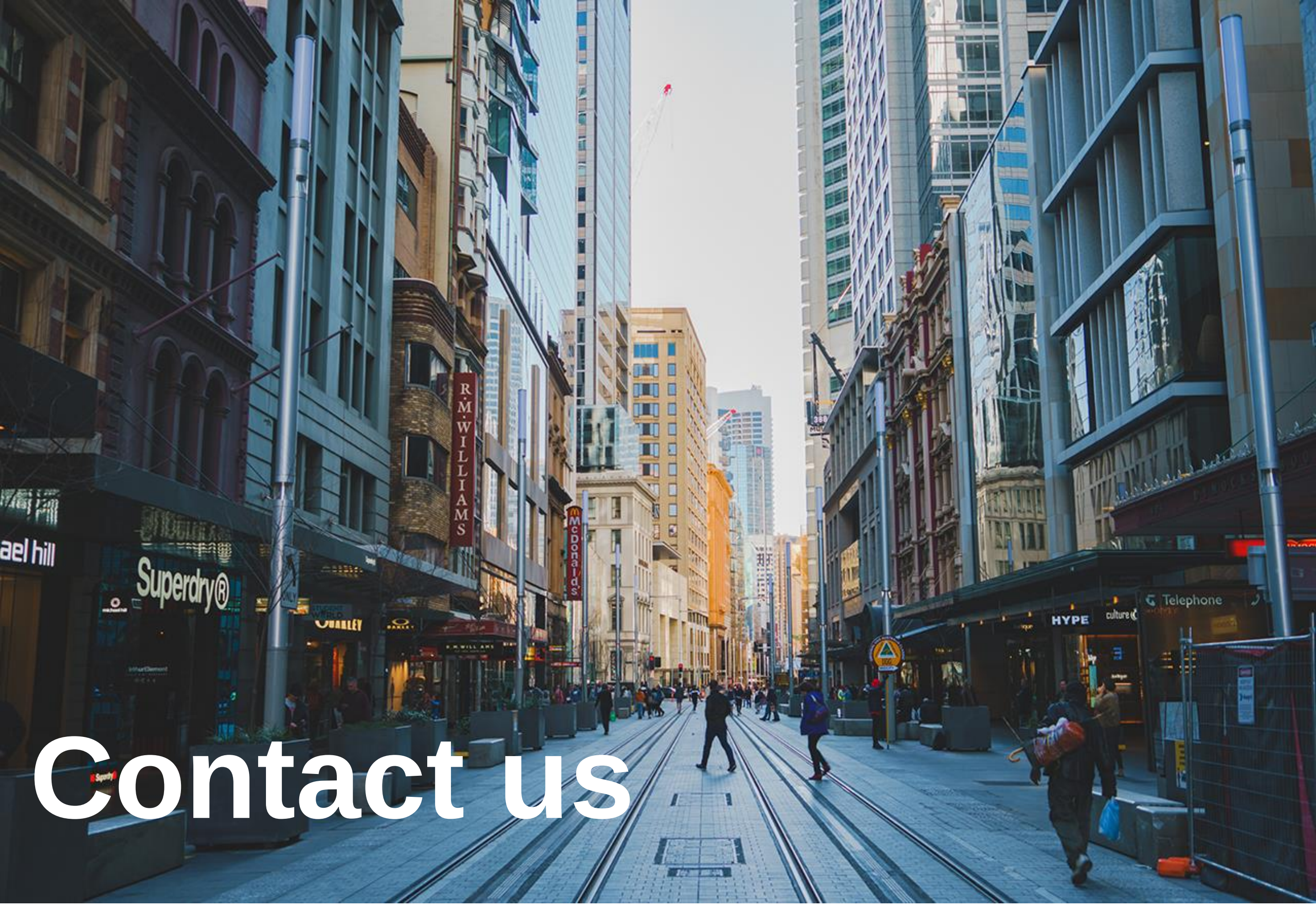
- Mar 2019





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