

Contents

Additional Resources	xv
About the Authors	xvii
Foreword	xxi
Acknowledgments	xxiii
Disclaimer	xxxi
INTRODUCTION	1
Structure of the Book	3
Part One: Valuation (Chapters 1–3)	3
Part Two: Leveraged Buyouts (Chapters 4 & 5)	5
Part Three: Mergers & Acquisitions (Chapters 6 & 7)	6
Part Four: Initial Public Offerings (Chapters 8 & 9)	8
ValueCo Summary Financial Information	9

PART ONE

Valuation	11
CHAPTER 1	
Comparable Companies Analysis	13
Summary of Comparable Companies Analysis Steps	14
Step I. Select the Universe of Comparable Companies	17
Study the Target	17
Identify Key Characteristics of the Target for Comparison Purposes	18
Screen for Comparable Companies	22
Step II. Locate The Necessary Financial Information	23
SEC Filings: 10-K, 10-Q, 8-K, and Proxy Statement	24
Equity Research	25
Press Releases and News Runs	26
Financial Information Services	26
Summary of Financial Data Primary Sources	27
Step III. Spread Key Statistics, Ratios, and Trading Multiples	28
Calculation of Key Financial Statistics and Ratios	28
Supplemental Financial Concepts and Calculations	42
Calculation of Key Trading Multiples	47

Step IV. Benchmark the Comparable Companies	50
Benchmark the Financial Statistics and Ratios	50
Benchmark the Trading Multiples	50
Step V. Determine Valuation	51
Valuation Implied by EV/EBITDA	52
Valuation Implied by P/E	52
Key Pros and Cons	54
Illustrative Comparable Companies Analysis for ValueCo	55
Step I. Select the Universe of Comparable Companies	55
Step II. Locate the Necessary Financial Information	57
Step III. Spread Key Statistics, Ratios, and Trading Multiples	57
Step IV. Benchmark the Comparable Companies	69
Step V. Determine Valuation	74

CHAPTER 2

Precedent Transactions Analysis

	75
Summary of Precedent Transactions Analysis Steps	76
Step I. Select the Universe of Comparable Acquisitions	79
Screen for Comparable Acquisitions	79
Examine Other Considerations	80
Step II. Locate the Necessary Deal-Related and Financial Information	82
Public Targets	82
Private Targets	85
Summary of Primary SEC Filings in M&A Transactions	86
Step III. Spread Key Statistics, Ratios, and Transaction Multiples	88
Calculation of Key Financial Statistics and Ratios	88
Calculation of Key Transaction Multiples	94
Step IV. Benchmark the Comparable Acquisitions	98
Step V. Determine Valuation	98
Key Pros and Cons	99
Illustrative Precedent Transaction Analysis for ValueCo	100
Step I. Select the Universe of Comparable Acquisitions	100
Step II. Locate the Necessary Deal-Related and Financial Information	101
Step III. Spread Key Statistics, Ratios, and Transaction Multiples	103
Step IV. Benchmark the Comparable Acquisitions	111
Step V. Determine Valuation	113

CHAPTER 3

Discounted Cash Flow Analysis

	115
Summary of Discounted Cash Flow Analysis Steps	116
Step I. Study the Target and Determine Key Performance Drivers	120
Study the Target	120
Determine Key Performance Drivers	120
Step II. Project Free Cash Flow	121
Considerations for Projecting Free Cash Flow	121
Projection of Sales, EBITDA, and EBIT	123
Projection of Free Cash Flow	125
Step III. Calculate Weighted Average Cost of Capital	131
Step III(a): Determine Target Capital Structure	132
Step III(b): Estimate Cost of Debt (r_d)	133
Step III(c): Estimate Cost of Equity (r_e)	134
Step III(d): Calculate WACC	138

Step IV. Determine Terminal Value	138
Exit Multiple Method	139
Perpetuity Growth Method	139
Step V. Calculate Present Value and Determine Valuation	141
Calculate Present Value	141
Determine Valuation	143
Perform Sensitivity Analysis	145
Key Pros and Cons	146
Illustrative Discounted Cash Flow Analysis for ValueCo	147
Step I. Study the Target and Determine Key Performance Drivers	147
Step II. Project Free Cash Flow	147
Projection of Sales, EBITDA, and EBIT	149
Step III. Calculate Weighted Average Cost of Capital	154
Step IV. Determine Terminal Value	159
Step V. Calculate Present Value and Determine Valuation	161

PART TWO

Leveraged Buyouts

167

CHAPTER 4

Leveraged Buyouts

169

Key Participants	171
Financial Sponsors	171
Investment Banks	172
Bank and Institutional Lenders	174
Bond Investors	175
Private Credit Funds	176
Target Management	176
Characteristics of a Strong LBO Candidate	177
Strong Cash Flow Generation	178
Leading and Defensible Market Positions	178
Growth Opportunities	178
Efficiency Enhancement Opportunities	179
Low Capex Requirements	179
Strong Asset Base	180
Proven Management Team	180
Economics of LBOs	181
Returns Analysis—Internal Rate of Return	181
Returns Analysis—Cash Return	182
How LBOs Generate Returns	182
How Leverage Is Used to Enhance Returns	184
Primary Exit/Monetization Strategies	187
Sale of Business	187
Initial Public Offering	188
Dividends / Dividend Recapitalization	188
Below Par Debt Repurchase	188

LBO Financing: Structure	189
LBO Financing: Primary Sources	192
Secured Debt	192
High Yield Bonds	196
Mezzanine Debt	198
Equity Contribution	199
LBO Financing: Selected Key Terms	202
Security	202
Seniority	202
Maturity	203
Coupon	204
Call Protection	205
Covenants	206
Term Sheets	209
LBO Financing: Determining Financing Structure	212

CHAPTER 5

LBO Analysis

LBO Analysis	217
Financing Structure	217
Valuation	218
Step I. Locate and Analyze the Necessary Information	220
Step II. Build the Pre-LBO Model	220
Step II(a): Build Historical and Projected Income Statement through EBIT	221
Step II(b): Input Opening Balance Sheet and Project Balance Sheet Items	224
Step II(c): Build Cash Flow Statement through Investing Activities	226
Operating Activities	226
Step III. Input Transaction Structure	229
Step III(a): Enter Purchase Price Assumptions	229
Step III(b): Enter Financing Structure into Sources and Uses	231
Step III(c): Link Sources and Uses to Balance Sheet	232
Adjustments Columns	232
Uses of Funds Links	235
Step IV. Complete the Post-LBO Model	238
Step IV(a): Build Debt Schedule	238
Step IV(b): Complete Pro Forma Income Statement from EBIT to Net Income	247
Step IV(c): Complete Pro Forma Balance Sheet	250
Step IV(d): Complete Pro Forma Cash Flow Statement	252
Step V. Perform LBO Analysis	254
Step V(a): Analyze Financing Structure	254
Step V(b): Perform Returns Analysis	256
Step V(c): Determine Valuation	260
Step V(d): Create Transaction Summary Page	261
Illustrative LBO Analysis for ValueCo	262

PART THREE**Mergers & Acquisitions****273****CHAPTER 6****Sell-Side M&A****275**

Auctions	276
Auction Structure	279
Organization and Preparation	279
Identify Seller Objectives and Determine Appropriate Sale Process	279
Perform Sell-Side Advisor Due Diligence and Preliminary Valuation Analysis	281
Select Buyer Universe	281
Prepare Marketing Materials	282
Prepare Confidentiality Agreement	285
First Round	286
Contact Prospective Buyers	286
Negotiate and Execute Confidentiality Agreement with Interested Parties	286
Distribute Confidential Information Memorandum and Initial Bid Procedures Letter	287
Prepare Management Presentation	288
Set Up Data Room	289
Prepare Stapled Financing Package (if applicable)	291
Receive Initial Bids and Select Buyers to Proceed to Second Round	291
Second Round	293
Conduct Management Presentations	293
Facilitate Site Visits	294
Provide Data Room Access and Respond to Diligence Requests	294
Distribute Final Bid Procedures Letter and Draft Definitive Agreement	295
Receive Final Bids	296
Negotiations	300
Evaluate Final Bids	300
Negotiate with Preferred Buyer(s)	300
Select Winning Bidder	300
Render Fairness Opinion (if required)	301
Receive Board/Owner Approval and Execute Definitive Agreement	301
Closing	302
Obtain Necessary Approvals	302
Shareholder Approval	303
Financing and Closing	305
Negotiated Sale	306

CHAPTER 7**Buy-Side M&A****309**

Buyer Motivation	310
Synergies	311
Cost Synergies	312
Revenue Synergies	312

Acquisition Strategies	313
Horizontal Integration	313
Vertical Integration	313
Conglomeration	314
Form of Financing	315
Cash on Hand	316
Debt Financing	316
Equity Financing	317
Debt vs. Equity Financing Summary—Acquirer Perspective	318
Deal Structure	318
Stock Sale	318
Asset Sale	321
Stock Sales Treated as Asset Sales for Tax Purposes	324
Buy-Side Valuation	327
Football Field	327
Analysis at Various Prices	330
Contribution Analysis	331
Merger Consequences Analysis	333
Purchase Price Assumptions	333
Balance Sheet Effects	338
Accretion/(Dilution) Analysis	343
Acquisition Scenarios—I) 50% Stock/50% Cash; II) 100% Cash; and III) 100% Stock	346
Illustrative Merger Consequences Analysis for the BuyerCo/ValueCo Transaction	351

PART FOUR

Initial Public Offerings

373

CHAPTER 8

Initial Public Offerings

375

Why Do Companies Go Public?	376
Characteristics of a Strong IPO Candidate	378
Attractive Industry	378
Strong Competitive Position	378
Growth Opportunities	379
Moat & Barriers to Entry	380
Healthy Financial Profile	380
Disruptive & Differentiated Solutions	381
Favorable Risk Profile	381
Proven Management Team	382
Key Participants	383
Investment Banks	383
Company Management	386
Current Owners/Investors	387
IPO Investors	387
Lawyers	388
Accountants	388

Exchange Partner	389
IPO Advisors	390
Vendors	390
Selected Key Terms	391
Offering Size	392
Primary/Secondary	393
Overallotment Option, a.k.a. "Greenshoe"	394
Syndicate Structure	395
Lock-up Provision	396
Listing Exchange	396
Gross Spread	397
Dual-Track Process	398
Special Purpose Acquisition Companies (SPACs)	401
Direct Listings	403
Post-IPO Equity Offerings	406
IPO Considerations	407
Nasdaq Appendix	409

CHAPTER 9

The IPO Process

413

Organization and Preparation	415
Select IPO Team, Exchange Partner and Assign Responsibilities	415
Manage Corporate Housekeeping	418
C Corp vs. Up-C Structure	423
Determine IPO Timing	425
Determine Offering Structure and Preliminary IPO Valuation	426
Host Organizational Meeting	429
Due Diligence, Drafting, and Filing	430
Perform Underwriter Due Diligence	430
Draft and File the Registration Statement	431
Prepare Other Key Transaction and Corporate Governance Documents	436
Coordinate with Equity Research	437
Respond to SEC Comments and File Amended Registration Statement	437
Marketing and Roadshow	438
Prepare Marketing Materials	438
Salesforce Teach-in	439
Conduct Roadshow	440
Build Order Book	443
Pricing and Allocation	445
Price the Offering	445
Allocate Shares to Investors	447
Closing	447

Afterword

449

Bibliography and Recommended Reading

451

Index

457