

UNIVERSITY OF PENNSYLVANIA
The Wharton School
The Finance of Buyouts and Acquisitions: FNCE 251
Professor Burcu Esmer and Professor Bilge Yilmaz
Fall 2017

Course Objective:

The aim of the course is to provide an understanding of key concepts and institutions involved in corporate buyouts and mergers and acquisitions. This course is most suitable for finance majors who are considering careers in corporate finance, investment banking and buyout funds.

Reading Materials:

- Course Reader (cases and articles).
- Further materials and lecture notes on course webpage (Canvas)
- Recommended (but not required) for background reading:
 - i. Robert Bruner, *Applied Mergers and Acquisitions*, Wiley Finance, 2004
 - ii. Thomas Meyer and Pierre-Yves Mathonet, *Beyond the J Curve: Managing a Portfolio of Venture Capital and Private Equity Funds*, the Wiley Finance Series, 2009.
 - iii. Gaughan, Patrick A., *Mergers, Acquisitions and Corporate Restructurings* 6th ed., Wiley, 2015.

Format:

The structure of the course includes lectures, case discussions, and guest speakers. The lectures provide the relevant institutional facts, empirical evidence and analytical methods that will be needed for case discussions.

The major objective of the case method in finance is to **use the logic of financial theory to arrive at sensible conclusions** when faced with real world problems. However, one should **keep in mind that there is not one absolutely right answer to a case; different assumptions can lead to different solutions**. While there are no “right” answers, there are good arguments and bad arguments. The process of this course will help distinguish between sensible and senseless arguments. Considering my analyses as the correct solution defeats the purpose of this course and contributes to the silly notion that in the “real world” there is a single correct recipe to be followed.

Student Responsibilities and Assessment:

- Case Study Assignments: (Approximately 10% of the course grade).

Students will organize themselves into groups of five members to work on case assignments. Groups must be fixed throughout the semester. Diverse background within the group is beneficial. Since group work is a cooperative undertaking, students are urged to ensure that they form groups that are able to work effectively as a group. Although brief discussions across different groups are allowed, exchange of analysis and calculations is not. Most cases in this course involve actual companies.

You may use firm specific or market data that are publicly available for your analysis. You cannot, however, use old notes, handouts, or solutions to the cases from previous years or similar courses elsewhere for your written reports and class discussions. The cases that require write-ups appear in **bold** (see the tentative course outline below). Each group is expected to **hand in** a hard-copy of their conclusions in a one or two page executive summary **prior to any class discussion**. Supporting computations and tables can be included in an appendix. All of the assumptions and formulas used should be provided (preferably as a footnote). The questions that need to be addressed will be posted at the course webpage. The raw data for cases is also available at the course webpage in .xls format.

- Class Participation and Attendance: (Approximately 20% of the course grade)
A goal of this course is to provide students with the opportunity to learn how to best contribute to discussions about complex financial issues. Therefore, this class depends and thrives on class participation. It is an important and essential part of this course. Because so much learning in this course occurs in the classroom, it is important that you attend every class. **Voluntary class participation is encouraged. “Cold calls” will be made as to ensure that the class enjoys the benefit of every student’s contribution.** Inadequate class participation combined with several absences can lead to a failing grade. I will judge performance based on the quality of comments/answers. **Students are expected to prepare for each case and participate actively in class.** I would appreciate it if students keep the same sitting arrangement throughout the semester.
- Examination: (Approximately 40% of the course grade)
You will be tested on both the concepts and the methods studied in this course. You will have access to a calculator and limited amount of information.
- Deal Proposal: (Approximately 30% of the course grade)
Each group is asked to identify a target firm either as a financial or a strategic buyer and prepare a deal proposal. The deal proposal is an active learning tool and allows you to apply many concepts that you have learned at the Wharton School. You may use firm specific or market data that are publicly available for your analysis. However, you cannot use materials prepared by professionals for a deal. Furthermore, any existing deal that is used in a teaching material, e.g., a case study, cannot be chosen as the topic of your proposal. **Each group must identify a deal by October 27, 2017. The final version is due at noon on November 27, 2017.** Each group is required to give 15 minutes presentation in front of a panel.

The deal proposal has two components, a presentation and a written report. Presentation will be 15 minutes (maximum) and you should focus on the deal rationale; why do you want to own the business, what is the investment thesis? You should not get into the details of valuation models during the presentation. There will be additional instructions for the written report.

Code of Ethics:

Submitted assignments for grading should be your own or your team's own work only. Most cases in this course involve actual companies. You may use firm specific or market data that are publicly available for your analysis. You cannot, however, use old notes, handouts, or solutions to the cases from previous or other sections of this course or similar courses elsewhere for your written reports and class discussions. Failure to observe this rule may result in an automatic failing grade for the course.

Office Hours and Contact Information:

Burcu Esmer:

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If you have questions about the material, the best place is the Canvas discussion board. We will try to answer all questions. However, considering the size of the classes we teach, we may not be able to do so especially the night before an exam.

TENTATIVE COURSE OUTLINE

This outline is a rough guide as to when material will be covered. It is highly likely to have a number of changes with advance notice given in class and/or Canvas. Some of the **guest lectures will be held outside regular class location and time**. Furthermore, **the last two weeks of classes may be rescheduled due to our guests' busy schedule**.

Session 1: August 29

Introduction and Organization

Session 2: August 31

Basic Valuation Concepts

Reading:

- “Chapter 2: Using Financial Reporting Information” by Simon Beninga and Oded Sarig
- Bruner Chapter 9

Session 3: September 5

Adjusted Present Value, Costs and Benefits of Debt Financing

Reading:

- Bruner Chapter 13

Session 4: September 7

Case 1: Paradyne

[This case is posted on Canvas.]

Session 5: September 12

Overview of Mergers & Acquisitions

Reading:

- Bruner Chapters 4 and 6
- Gaughan Chapters 1 and 2
- Eckbo, B. Espen, 2014, “Corporate takeovers and economic efficiency”, *Annual Review of Financial Economics* 6, 51-74.
- McConnell, John J., and Valeriy Sibilkov, 2016, “Do investment banks have incentives to help clients make value-creating acquisitions”, *Journal of Applied Corporate Finance* 28, 103-117.

Session 6: September 14

Target valuation, DCF, multiples, and cost of capital

Reading:

- Gaughan Chapter 15

Session 7: September 19

Takeover motives, Form of Payment, Exchange Ratio and Dilution

Reading:

- Bruner Chapters 18, 19, 20, 21 and 26
- Gaughan Chapter 4

Session 8: September 21

Synergy valuation, Contingent Considerations, Risk Sharing and Deal Protection

Reading:

- Bruner Chapters 11,15, 22, and 23
- Caselli, Stefano, Stefano Gatti, and Marco Visconti, 2006, Managing M&A risk with collars, earn-outs and CVRs, *Journal of Applied Corporate Finance* 18 (4), 91-104.
- Amobi, Tuna N., 1997, Price protection in stock-swap transactions, *Merger & Acquisitions* 32, 22-28.

Session 9: September 26

Form of Acquisition and Law and Economics of Market for Corporate Control

Reading:

- Bruner Chapters 32 and 33

Session 10: September 28

CASE 2: Dow's Bid for Rohm and Haas

Session 11: October 3

Private Equity Framework and Industry Overview

Session 12 October 3, 4:30-5:50pm, location TBA

Guest Lecture: Growth Equity (Optional)

Session 13: October 4, time and location TBA

Guest Lecture: Operational Improvements (Optional)

Session 14: October 10

Reduced-Form Valuation Methods

Reading:

- “Chapter 10: Valuation by Multiples” by Simon Beninga and Oded Sarig

Session 15: October 12

Comp Analysis

Session 16: October 17

LBO Model

Session 17: October 19

Incentives and Private Equity Fund Structure

Reading:

- “Note on Private Equity Partnership Agreements” by Josh Lerner
- Meyer and Mathonet: Chapters 2 and 3

Session 18: October 24

Case 3: HCA

[This case is on Canvas.]

Session 19: October 26

Case 3: HCA (cont'd)

Session 20: October 31

Exam, 6:00-7:30pm, location TBA

No Regular Class

Session 21: November 2

Guest Speaker

Session 22: November 7

Case 4: Realogy (Part 1)

[This case is posted on Canvas.]

Session 23: November 9

Case 4: Realogy (Part 2)

Session 24: November 14

Restructuring: Comparative Analysis

Session 25: November 16

Case 5: Middle Market

Session 26: November 21

Deal Proposal Preparation

Session 27-30: November 28 & 30, December 5 & 7

Presentation