

UNIVERSITY OF PENNSYLVANIA
The Wharton School
The Finance of Buyouts and Acquisitions: FNCE 751
Part I: Professor Bilge Yilmaz
Part II: Professor Karin Thorburn
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 (below referred to as Gaughan).

Format:

The structure of the course includes lectures, case discussions, and guest speakers. 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 the professor’s 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 30% 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. Performance will be judged based on the quality of comments/answers. **Students are expected to prepare for each case and participate actively in class.** To facilitate recording of class participation, please keep the same sitting arrangement throughout the semester.
- Examination: (Approximately 30% 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 for Part I: (Optional)
Each group is encouraged to identify a target firm as a financial 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. **The final version is due at 5pm on Tuesday, October 17, 2017.** Each group will have a chance to give 15 minutes presentation in front of an “investment committee.”

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.

- Merger Project for Part II: (Approximately 30% of the course grade)
Each group is asked to propose a potential takeover transaction, taking the role of an investment banker pitching the deal to the bidder or the target. Using the analytical

tools learned during the course, you should select a bidder and a target, and structure the transaction. The analysis should cover different aspects of the deal, such as the strategic and economic benefits, target and synergy valuation, method of payment, bidding strategy, target management reaction, and corporate governance issues. You should rely on firm and market data that are publicly available for your analysis. However, as for the deal proposal in Part I, you cannot use materials prepared by professionals.

Each group is required to give a 10-15 minute presentation in class on December 4 and 6. Moreover, a **written report is due at 5pm on Sunday, December 3, 2017**. Additional details are in the Merger Project Guidelines on Canvas.

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:

Bilge Yilmaz:

Office Hours: Wednesday noon-1:00pm, SHDH 2333

Email: yilmaz@wharton.upenn.edu

Karin Thorburn

Office Hours: TBA

Email: karinsi@wharton.upenn.edu

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 deal proposal presentations will take place outside regular classes**.

PART I (Q1)

Session 1: August 30

Introduction and Organization

Session 2: September 6

Private Equity - A Framework

Session 3: September 11

Incentives and Private Equity Fund Structure

Reading:

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

Session 4: September 13

Reduced-Form Valuation Methods

Session 5: September 18

Comp Analysis

Session 6: September 20

LBO Model

Session 7: September 25

Case 1: HCA

[This case is posted on Canvas.]

Session 8: September 27

Case 1: HCA (cont'd)

Session 9: October 2

Exam, 6pm, location TBA

No Regular Class

Session 10: October 4, time and location TBA

Guest Lecture: Debt Financing (Optional)

Session 11: October 4, time and location TBA

Guest Lecture: Operational Improvements (Optional)

Session 12: October 9

CASE 2: Realogy (Part 1)

[This case is posted on Canvas.]

Session 13: October 11

CASE 3: Realogy (Part 2)

[This case is posted on Canvas.]

Session 14: October 16

Case 4: Middle Market

[This case is posted on Canvas.]

Optional Session: October 18, time and location TBA

Investment Committee Presentation

PART II (Q4)

Session 15: October 23

Introduction. Value creation in mergers and acquisitions.

Reading:

- Gaughan Ch. 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 16: October 25

Premiums, exchange rates, and post-takeover ownership. Severance agreements.

CASE 5: Stanley, Black & Decker, HBS 9-211-067.

Reading:

- Gaughan Ch. 13.
- M&A legal context: Basic framework for corporate governance, HBS 9-803-200.
- Standards related to the sale or purchase of a company, HBS 9-904-004.

Session 17: October 30

Target valuation, DCF, multiples, and cost of capital.

CASE 6: Monmouth, HBS 4226.

Reading:

- Gaughan Ch. 15.
- Corporate Valuation and Market Multiples, HBS 9-206-039.

October 30 at 6pm: Optional review session

Review of spreadsheets, calculations and concepts covered in class.

Session 18: November 1

Takeover motives. Accretion and dilution. Choice of payment method.

CASE 7: Monmouth, HBS 4226.

Reading:

- Gaughan Ch. 4.
- Evaluating M&A Deals: Accretion vs. Dilution of Earnings-per-share, HBS 9-208-059.
- Evaluating M&A Deals—Equity Consideration, HBS 9-208-077.
- Rappaport, Alfred, and Mark L. Sirower, 1999, Stock or cash? The Trade-Offs for Buyers and Sellers in Mergers and Acquisitions, *Harvard Business Review* (Nov-Dec), reprint 99611.

Session 19: November 6 at 6pm (note the time)

Interactive role-play focusing on the legal and regulatory issues in M&A transactions.

Guest Speaker: Stuart Cable, Partner Goodwin Procter LLP.

Reading: Gaughan Ch. 3.

Session 20: November 8

Synergy valuation. Contingent value rights, risk sharing and deal protection.

CASE 8: General Mills' acquisition of Pillsbury from Diageo Plc., UV0089.

Reading:

- 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.
- Technical note on consideration: floors, caps, and collars, HBS 9-902-056.

Session 21: November 13

Minority buyouts, tender offers, hostility

CASE 9: Roche's acquisition of Genentech, HBS 9-210-040.

Reading:

- Gaughan Ch. 5 and 6.
- M&A legal context: Hostile takeovers, HBS 9-904-005.

Session 22: November 13 at 6pm (note the time)

Roche's acquisition of Genentech

Guest speaker: Stephen Krognes, CFO of Denali Therapeutics.

Head of Roche's global M&A team, 2004-2009. CFO of Genentech, 2009-2015.

Session 23: November 15

Empty voting. Merger arbitrage and investor activism.

CASE 10: Mylan Laboratories' proposed merger with King Pharmaceutical, HBS 9-214-078.

Reading:

- Gaughan Ch. 7.

- Wyser-Pratte Guy P., Merger Arbitrage, *Merger & Acquisition Handbook*, 2nd ed. by Rock-Rock-Sikora, 1987.

November 20: NO CLASS (Thanksgiving week)

Session 24: November 27

Conditional deal financing, investor activism, appraisal rights.

CASE 11: AXA MONY, HBS 9-208-062.

Reading:

- Gillan, Stuart L. and Laura T. Starks, 2007, “The Evolution of Shareholder Activism in the United States”, *Journal of Applied Corporate Finance* 19, 55-73.
- Liu, Baixiao, and John J. McConnell, 2015, “CEOs, abandoned acquisitions, and the media”, *Journal of Applied Corporate Finance* 27, 113-121.

November 27 at 6pm: Optional review session

Review of spreadsheets, calculations and concepts covered in class.

Session 25: November 28 at 6pm (note day and time)

Structuring the deal: Selling Guidant.

Guest speaker: Stephen Munger, Managing Director and Chairman, Global M&A Morgan Stanley Investment Banking Division

Session 26: November 29

Bidding tactics: markups and toeholds.

Reading:

- Eckbo, B. Espen, 2009, “Bidding strategies and takeover premiums: A review”, *Journal of Corporate Finance* 15, 149-178.

Session 27: December 4

Term project presentations.

Session 28: December 6

Term project presentations.

December 11: NO CLASS