FNCE 751
THE FINANCE OF BUYOUTS AND ACQUISITIONS
FALL 2021
UPDATED ON AUGUST 24

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Office hours by appointment & on Zoom

COURSE OBJECTIVE

The aim of the course is to provide an understanding of key concepts and institutions involved in corporate buyouts and public company takeovers. Students will develop skills necessary to structure a deal or form an opinion about a proposed transaction.

The course is most suitable for finance majors who are considering careers in corporate finance, investment banking, private equity, or consulting.

PREREQUISITE:

FNCE 611

COURSE WEB PAGE

Course materials including lecture notes, suggested readings, required assignments, deadlines, and other useful information will be available on the Canvas course web page:

https://canvas.upenn.edu/courses/1608062

Please be sure to check the course page regularly for any updates and deadlines. You can set and customize the frequency of course notifications on Canvas by clicking on Account > Notifications and changing the Course Content setting to "Immediately". While these notification preferences apply to all courses, you can also adjust your course-level notifications by clicking the "View Course Notifications" button on the right side of our course home page.

It is **students' responsibility** to be mindful of deadlines and any important developments pertaining to the course.

COURSE MATERIALS

- Lecture notes and non-licensed articles (such as news articles) can be found under Files on the course webpage
- Licensed cases can be found under Study.net materials on the course webpage
- Licensed articles and ebooks can be found under Course Materials @ Penn Libraries on the course webpage
- Recommended (but not required) for background reading:
  - Gaughan, Patrick A., *Mergers, Acquisitions and Corporate Restructurings* 7th ed., Wiley, 2017 (below referred to as Gaughan)

FORMAT

The structure of the course includes lectures, case discussions, and guest speakers. Lectures provide relevant institutional facts, empirical evidence, and analytical methods that support the case analysis. A 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 no single "absolutely right" approach to tackle a case; different assumptions can lead to different solutions**. While there is not one right solution, there are good arguments and bad arguments. The process of this course will help distinguish between sensible and nonsensical arguments. We will be providing our case analyses; however, considering our 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.

Because so much learning occurs through class discussions, it is important that you attend every class. A goal of the course is to provide students with the opportunity to learn how to best contribute to discussions about complex financial issues. Moreover, many students have relevant experience that benefits other students when brought into the classroom.

STUDY GROUPS

There are two projects and one case study that require group work. Students should organize themselves into groups of four or five. All teams should self-register on Canvas by no later than **Wednesday, September 15.** You may use the discussion board on Canvas to post that you are looking for a team member or a group. If a student does not self-register by the deadline, s/he will be randomly assigned to a group. It is the student's responsibility to contact the other team members and arrange meetings. Since group work is a cooperative undertaking, students should ensure that they form groups that are able to work effectively. It is beneficial to have diverse backgrounds within a group. Group members do not need to be in the same section. However, if a group is selected to give a presentation, all members of the team are expected to be present.

GRADING AND EXPECTATIONS

Part I (Q1): 50% of the course grade

Readings
Suggested readings will be published under Assignments > Part I – Suggested Readings. Students are expected to have read these prior to the session.

Exam (15% of the course grade)
The exam will be held in class on **Wednesday, October 6,** between **7:00 pm and 9:00 pm**. A practice exam will be posted on Canvas beforehand. In the exam, you will need a calculator and will be given a cheat sheet. There will not be any makeup exams except when required by the university policy.

Quizzes (5% of the course grade)
There will be two post-class quizzes. The quizzes will be administered through Canvas. They are located under Quizzes. The first quiz will be on PE fundamentals and trends, and will be due at **10:00 am on September 13.** The second quiz will be on leveraged buyout modeling fundamentals and multiples, and will be due at **10:00 am on September 27**. There is no makeup for missed quizzes.

Case Submission (5% of the course grade)
Each group is expected to **submit** a soft copy of their conclusions on HCA case in a 2-3 page long executive

summary. Supporting computations and tables can be included in an appendix. Groups must submit the excel file along with their executive summary. All of the assumptions and mathematical formulas used should be provided (preferably as a footnote). Raw data from the case exhibits in excel format, and hints to help guide the analysis, are available on Canvas.

The write-up must be submitted via Canvas and is due at **10:00 am on Wednesday, September 22**. Submission via email and/or late submissions will not be accepted.

Leveraged Buyout (LBO) Proposal: (23% of the course grade)
Each group must 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 pre-built models that you have used in the past or materials otherwise prepared by professionals. For all submitted assignments, you must start with an Excel spreadsheet which is at most populated with raw data. Furthermore, any existing deal used in a teaching material (e.g., a case study) cannot be chosen as the topic of your proposal.

A written report, the excel file which shows the analyses and a PowerPoint presentation are due at **11:59 pm on Saturday, October 9.** Two selected groups will present their term projects in front of industry professional on **Monday, October 11. Attending the presentation session is required.** The groups can sign up to give the presentation by **11:59 pm on Saturday, October 9**. If slots remain open, I will pick the presenting groups. These groups will be notified the day before the presentation**.** The remaining groups must record and submit their presentation recordings by **11:59 pm on Tuesday, October 12**. Additional details are available in the LBO Proposal Guidelines on Canvas.

Team member evaluation (2% of the course grade)
Each student will anonymously evaluate his/her team members' contribution to the group work via Canvas. Your team members' evaluation of your efforts and your participation in the survey will contribute to your class score. Evaluations for the HCA case are due **Thursday, September 23.** Evaluations for the LBO project are due **Tuesday, October 12.** These evaluations will be confidential and the scores will not be published. Late submissions and/or submissions via email will not be accepted under any circumstances.

Part II (Q2): 50% of the course grade

Class attendance and participation (15% of the course grade)
Starting on October 25, attendance will be recorded within five minutes of the start of each lecture. Missing one class for any reason (illnesses, interviews, religious holidays, case competitions etc.) will not affect your attendance score. Attendance will not be recorded for sessions held outside the regular classtime.

Students are expected to engage and participate actively. I encourage voluntary class participation but will also cold call to ensure that the class enjoys the benefit of every student's contribution. Class participation is an individual effort and is rated in each session on a scale from **1** (minimal participation) to **3** (active and contributing to the flow). We consider the quality of your comments as well as quantity. The overall class participation grade is based on each student's total participation score.

We will cover a case in every session. To facilitate modeling, the case exhibits in excel are posted on Canvas. For some cases, there are hints that help guide you through some facets of the analysis. It is optional to individually submit a case write-up of 3-4 pages addressing the assigned questions. The aim with this report is to allow students who feel disadvantaged in the class discussion to show their case analysis and level of preparedness. You must upload the report on Canvas before class begins.

Each write-up substitutes for class participation and gives a maximum score of 2 (to receive a 3, you need to speak up in class). However, a missed class cannot be replaced with a write-up. The reports will not be returned to you.

Pre- Class Quizzes (10% of the course grade).
For each case discussion, there is a quiz in Canvas. The quiz has five simple questions on case facts that are useful for the analysis of the case. The purpose is to encourage advance preparation and help identify relevant case facts. The quizzes are individual assignments. Students have 30 minutes to take the quiz. It opens two weeks in advance and closes one minute prior to class.

Merger project for part II (25% of the course grade)
Each group should propose a potential takeover transaction, taking the role of an investment bank pitching the deal to the bidder or the target. Using the analytical tools learned during part II, you should select a bidder and a target, and structure the transaction. The analysis should cover different aspects ofthe 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 firmand market data that are publicly available for your analysis. However, you cannot use pre-built models that you have used in the past or materials otherwise prepared by professionals. Exchange of analysis andcalculations across groups is not allowed.

A written report and a power point presentation are due at **11:59pm (EST) on Monday, December 6**. Three to four selected groups will present their term projects on the last day of class (December 8). The remaining groups should record and submit their presentation by **December 9.** Additional details are in the Merger Project Guidelines on Canvas.

Students will evaluate their team members after submitting and presenting the project. Your team members' evaluation of your efforts and contribution to the merger project will contribute to your individual score.

GRADES AND RE-GRADE REQUESTS

Class grades are determined using a class-wide (i.e., across all FNCE 751 sections) curve that respects any constraints imposed by the University or the Wharton School. Note that mandated grade guidelines allow up to 5% failing grades.

If you feel that an item has been incorrectly graded, you may submit a re-grade request to the professor, *not to a TA*. Each re-grade request must include a concise written explanation of the problem accompanied by the original graded assignment and must be submitted **within one week** after the assignment is graded and made available for review. Please note that re-grading applies to the whole assignment, not just the part(s) that are mentioned in your request. If you are submitting a request for a group project, please carbon copy (cc) your team members in your email and include your group number in your request.

CODE OF ETHICS:

Assignments submitted for grading should be your 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.

Students should not in any way rely on the work of prior students or current students who are not on their team. This prohibition extends to prior quizzes, exams, assignments, cases, or projects that are directly relevant to the assignment being completed. When a project requires you to produce a

forecasting/valuation model, the use of a model not created exclusively by the students on the team for the purposes of this class is a violation of the code of academic integrity. **For all submitted assignments, students must start with an Excel spreadsheet which is at most populated with raw data.** Failure to follow this rule will result in an automatic failing grade for the course.

The University of Pennsylvania's Code of Academic Integrity is available at:
[Code of Academic Integrity < University of Pennsylvania (upenn.edu)](#)

TEACHING ASSISTANTS

The teaching assistants (TAs) are responsible for taking attendance and recording class participation in the second part of the class, answering questions about class content, case analyses, projects, holding weekly office hours, and grading items.

Marianne Chin mchinyj@wharton.upenn.edu (will attend to Section I)
Maria Xing mariax@wharton.upenn.edu (will attend to Section II)
Caio Azevedo cazevedo@wharton.upenn.edu (will attend to Section III)
Jia He jiahe1@wharton.upenn.edu

Please see the Canvas homepage for TA office hours and additional information.

COURSE OUTLINE

The course outline below is a preliminary guide as to when the material will be covered. There may be changes with advance notice. Note that guest lectures may be scheduled outside of the regular class slots due to our guests' work schedules. Conditional on our guests' permission, these sessions will be recorded and made available on Canvas.

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TENTATIVE COURSE OUTLINE

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PART I (Q1): BUYOUTS

Session 1: August 30 (Mon)
Introduction and Organization

Session 2: September 1 (Wed)
PE Fundamentals
<u>Reading:</u>
- Gaughan Ch. 8 and 9

Session 3: September 8 (Wed)
PE Trends

Session 4: September 13 (Mon)
LBO Model Fundamentals

Session 5: September 15 (Wed)
LBO Modeling Case

Session 6: September 20 (Mon)
Reduced Form Valuation / Multiples

Session 7: September 22 (Wed)
Case Discussion: HCA

Session 8: September 27 (Mon)
Case Discussion: Realogy and TXU

Session 9: September 29 (Wed)
No class during regular class time. This session is replaced with the session below.

September 30 (Thu) at 10:15 am, location TBA
Impact Investing in PE
Guest speaker: Marc Becker (Senior Partner and Co-Lead of Impact, Apollo)

Session 10: October 4 (Mon)
Growth Equity & Middle Market (Case Discussion: NOH)
Guest speaker: TBA

Session 11: October 6 (Wed)
No class during the regular class time
Exam, 7-9 pm (location TBA)

Session 12: October 11 (Mon)
LBO Deal Proposal Presentations
Note: Attendance is required

Additional Session on October 12 (Tue), time & location TBA
Guest speaker: Jonathan Coslet (CIO, TPG)

PART II (Q2): PUBLIC COMPANY TAKEOVERS

Session 13: October 25 (Mon)
Introduction to M&A: value creation and the merger process
<u>Reading</u>:
- Gaughan Ch. 1 and 2.
- Eckbo, B. Espen, 2009, "Bidding strategies and takeover premiums: A review", Journal of Corporate Finance 15, 149-178.
- Eckbo, B. Espen, 2014, "Corporate takeovers and economic efficiency", Annual Review of Financial Economics 6, 51-74.

Session 14: October 27 (Wed)
Synergy valuation and bid premiums
Case: Monmouth, HBS 4226.
<u>Reading</u>:
- Gaughan Ch. 15.
- Corporate Valuation and Market Multiples, HBS 9-206-039.

Session 15: November 1 (Mon)
Accretion/dilution, method of payment, and exchange ratio
Case: Monmouth, HBS 4226.
<u>Reading</u>:
- 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 16: November 3 (Wed)
Consideration, distribution of synergy gains, and corporate governance issues in M&A
Case: Stanley, Black & Decker, HBS 9-211-067
<u>Reading</u>:
- Gaughan Ch. 4 and 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: November 8 (Mon)
Price protection and risk sharing
Case: General Mills' acquisition of Pillsbury from Diageo Plc., UV0089
<u>Reading</u>:
- 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, 1997, Price protection in stock-swap transactions, Merger & Acquisitions 32, 22- 28.
- Technical note on consideration: floors, caps, and collars, HBS 9-902-056.
- Note on basic option properties, HBS 9-205-105.
- Note on option valuation, HBS 9-205-106.

Session 18: November 10 (Wed)
Hostility, defensive tactics, and antitrust.

Case: Canadian Pacific's bid for Norfolk Southern, HBS 9-216-057
Reading:
- Gaughan Ch. 5
- M&A legal context: Hostile takeovers, HBS 9-904-005.

Session 19: November 15 (Mon)
Expected deal probability, merger arbitrage, and empty voting
Case: Mylan Labs' 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.
- 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.

Session 20: November 17 (Wed)
Interactive role-play focusing on the legal and regulatory issues in M&A transactions
Guest Speaker: Stuart Cable, Partner Goodwin Procter LLP.
Mr. Cable will attend the first two sections in person. The third section will watch a recording.
Reading:
- Gaughan Ch. 3.

Session 21: November 29 (Mon)
Minority buyouts and tender offers
Case: Roche's acquisition of Genentech, HBS 9-210-040.
Reading:
- Gaughan Ch. 6.

Optional session on Zoom: November 30 (Tue) at 8:30am-9:30am
Inside 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 22: December 1 (Wed) at 5:15pm
Structuring the deal.
Guest speaker: Stephen Munger, Managing Director and Chairman, Global M&A, Morgan Stanley
Investment Banking Division

Session 23: December 6 (Mon)
Course review

Session 24: December 8 (Wed)
Merger project presentations
Guest: Luigi Rizzo, Vice Chairman Investment Banking, Morgan Stanley.