BG Consulting Financial Modelling Training Example
Construction and Interpretation of LBO Models

Overview

This programme provides participants with a working knowledge and practical understanding of the construction and interpretation of complex LBO models. The programme is highly interactive with participants working on a case model throughout the programme. The key focus is on understanding the key financial and commercial sensitivities around executing an LBO and not on mechanical modelling skills, although of course modelling good practice, Excel tips and techniques will be communicated throughout the course. At the end of the programme, participants will be able to:

■ Understand the key dynamics that drive the LBO – vendor price, sponsor IRR and creditor risk/reward

■ Create intelligent assumption sets for operating scenarios and build models that allow easy switching between different scenarios

■ Build models that accommodate different financing scenarios and understand the drivers that determine the design of the debt and equity components

■ Analyse the returns to the Sponsor under a range of entry, exit and intermediate distribution scenarios and relate these results to the price that the Sponsor can afford to pay to acquire the business

This programme will be largely be taught 'through the spreadsheet' – the issues raised and material covered will be linked to its application in transaction models.

'Embedded Learning'

Excel functionality, Excel 'power user' tricks and shortcuts and principles of good model design and good modelling practice will be embedded throughout the material rather than being delivered as a separate topic. Particular emphasis will be put on building models with user friendly input and output that assists in scenario modelling and interpretation of the results. We will also stress audit and error trapping techniques to ensure model integrity and quality.

The kinds of embedded topics that we will build into the programme will include:

User Friendly Input and Output

■ Where should we put the assumptions?

■ Adding analytical features to the model

■ Grouping key outputs in a user-friendly summary

■ Data tables to show sensitivity to key variables

■ Applications for Excel's financial, bond and interest rate maths functions in corporate finance models

Auditing the Model

- Sanity checking and integrity checking
- Issues around over optimistic or unrealistic forecasting – assumptions around future capital structure and leverage
- Techniques in Excel to identify coding errors and trap mistakes

LBO Modelling Skills (1½ Days)

Understanding the Key Dynamics

Leveraged Buyouts – The Triangular Tension

- Balancing three opposing sets of objectives

Operating Scenario Modelling

Case Company Model

- Participants will build a fully balancing LBO model for the case company, starting from a completed financial forecast model that provides a base case forecast from a simplified assumption set

Developing Intelligent Assumptions and Projecting Cash Flows

- Garbage in, garbage out – why actually building the Excel model is not the most important part of the task
- The case company model will require interactive discussion of both assumptions and how to interpret the disclosure in the case company's public information pack – it tests both analytical and Excel skills
- Populating the operating model
- Different cash flow measures
- Estimating cash flow generation – growth and margin assumptions
- Estimating cash flow generation – capex, working capital, D&A
- Estimating financing requirements consistent with growth assumptions

Scenario Modelling

- What cases do we want to model?
- Dangers of straight-line adjustments
- Sanity checking scenarios for internal consistency

Valuation

- What valuation range should the Sponsor consider?
- What is driving the Sponsor's ability to pay a premium to last night's close? - Potential for value creation through:

Financial Scenario Modelling

Structuring the Financing Package

- Structuring the transaction
- Free cash flow for debt paydown
- Layering debt
- The equity component
- Debt modelling

Debt Capacity – How Much Debt Can Be Raised in the Capital Structure

- What are the banks looking for?
- Protecting the lender – seniority and security:
- Designing covenant packages
- Key ratios used by rating agencies and banks
- Peer group analysis and sector/comparable transaction benchmarking
- Mapping the LBO to a Rating Methodology – where does the proposed structure come out and is that position 'bankable'
- Retaining flexibility – estimating future borrowing requirements
- Liquidity and refinancing risks

Measuring Returns to the Sponsor(s)

Establishing the Returns

- Exit and returns analysis
- Assessing IRRs

How Much Should the Sponsor Pay?

- Scenario and sensitivity analysis – analysing the deal at different assumed entry and exit prices
- Establishing the take-out valuation

This outline has been abridged, to find out more about our approach to financial modelling training please contact us at info@bgconsulting.com