



FIN 394 – Private Equity (GSB 3.130)

FALL 2014

Professor: Dr. Audra Boone

Office: CBA 6.250

Phone: 512-471-2822

Email: Audra.Boone@mcombs.utexas.edu

Office Hours: TR 8:00 to 9:15 am and by appointment

TA: Elliott Hendrix: elliott.g.hendrix@gmail.com

1. Overview and Learning Objectives

This course examines the application of advanced corporate finance concepts in the private equity (PE) markets. Private equity is a major source of capital for new and established private and public firms. The size of the organized private equity market has grown dramatically in recent years. For example, assets under management have escalated from under \$1 trillion in 2000 to almost \$3.5 trillion in 2013. The amount of capital that has been committed to traditional private equity funds worldwide, but remains un-invested (dry powder) as of 2013, is estimated to be over \$1 trillion. PE funds have also received increasing scrutiny from both the financial press and regulators in recent years that could affect their ability to raise and deploy capital in the future.

Course objectives are to provide students with an understanding of the nature of the private equity markets, the principal participants in these markets and their activities, and the financial strategies that they employ. Topics covered include: how private equity funds are raised, structured, and financed; contracting in the private equity markets; financing investments; valuation of business interests; M&A and restructuring; and exit strategies.

2. Prerequisites and Preparation

Courses: BA 285T, FIN 286, FIN 397.1, and FIN 394.1

3. Course Materials:

Required:

1. Venture Capital, Private Equity, and the Financing of Entrepreneurship, 2012, Lerner, Leamon, Hardyman, Wiley. (http://www.coursesmart.com/IR/5845697/9780470591437?_hdv=6.8)
2. Course packet, which is available at the University COOP, contains some readings and cases.
3. Course-related information, including the syllabus and class notes, and assignments will be posted on Canvas.

General References Materials:

Corporate Finance by Jonathon Berk and Peter DeMarzo, Pearson/Addison-Wesley.

Private Equity Reference:

Cendrowski, Harry, Louis W. Petro, James P. Martin and Adam A. Wadecki, 2012, *Private Equity: History, Governance, and Operations*, (2nd ed.), John Wiley & Sons, Inc., Hoboken, NJ.

Bartlett, Joseph W., 1995 & 2009, *Equity Finance: Venture Capital, Buyouts, Restructurings, and Reorganizations* (2nd ed., 2009 Cumulative Supplement), Aspen Publishers division of Wolters Kluwer Law & Business, New York, NY.

Levin, Jack S., 2010, *Structuring Venture Capital, Private Equity, and Entrepreneurial Transactions*, Aspen Publishers division of Wolters Kluwer Law & Business, New York, NY.

Metrick, Andrew, 2010, *Venture Capital and the Finance of Innovation*, (2nd ed.) John Wiley & Sons, Inc., Hoboken, NJ.

Valuation and mergers and acquisitions references:

Pignataro, Paul, 2013, *Financial Modeling and Valuation: A Practical Guide to Investment Banking and Private Equity*, (1st ed.), John Wiley & Sons, Inc., Hoboken, NJ.

Koller, Tim, Marc Goedhart, and David Wessels, 2010, *McKinsey Valuation* (5th ed.), John Wiley & Sons, Inc., Hoboken, NJ.

Bruner, Robert F., and Joseph R. Perella, 2004, *Applied Mergers and Acquisitions*, John Wiley & Sons, Inc., Hoboken, NJ.

Gaughan, Patrick A., 2010, *Mergers, Acquisitions, and Corporate Restructurings* (5th ed.), John Wiley & Sons, Inc., Hoboken, NJ.

4. Evaluation and Grading Policies:

Midterm	25%
Final Exam/Case	30%
Case Reports	15%
In-class participation/Peer Evaluation	30%

a. Midterm Exam. There will be an in-class exam on Thursday October 16, 2014. Students will be responsible for all course material covered up through October 14, 2014. Makeup exams are only given to students with documented, university-approved excuses. If an absence is excused, the makeup exam will be scheduled within 3 days of the missed exam. The format of the makeup exam may vary from that of the regular exams and will be at the discretion of the instructor. All exams are comprehensive with emphasis on the newest material presented.

b. Final exam. The final assignment in this course will consist of a written case analysis (individually prepared – no collaboration or discussion with other students). The case will be distributed on the last day of class, December 4, 2014, and the analysis will be due by 10:00 a.m. on Thursday, December 11, 2014. The report will not exceed six pages (including exhibits). More details on the exact parameters and structure will be posted later in the semester.

c. Case Analysis and Reports. Cases are intended to expose the student to more complex and ambiguous analyses than what can be obtained from simple textbook problems. They cover situations that complement class lectures. To properly analyze a case you should: a) browse the provided study questions, b) read the case while noting any particularly relevant information or details, c) conduct any analyses, and d) develop a proposed plan of action and alternative strategies. There is no single correct answer. Some students find the lack of a definitive answer to be frustrating and want to be provided with a solution. Cases are not intended for this purpose. I will be happy to discuss individual analyses, but will not provide a solution set because it fosters the erroneous thinking that only one correct answer exists (moreover, this is often prohibited due by the case publishers).

Case reports will be done in self-formed groups of 4 students. Each group will be responsible for completing short summaries for three cases during the semester. These summaries will be a *maximum* of two pages of text plus one exhibit that outlines the following: 1) defining the issues/problems; 2) discussion of analysis (valuation) with key assumptions and considerations; 3) a proposed solution or strategy and implementation. Teams may deviate from this structure if the case does not follow this outline. These must be in at least 11 point font with 1 inch margins. Provide a cover page with the section time and names.

d. Class participation. This portion of the grade will be based on the contribution of each individual student to the class discussion throughout the term. It will be based on the quality and quantity of class participation. Quality will be the far more important of the two dimensions.

Relatively frequent contributions to the discussion that demonstrate logical and thorough analysis will be required to earn full points. Everyone should have read the case, so merely regurgitating facts covered in the case does not move class discussion forward in a substantive way. For example, instead of noting that the company had profits of \$10 million, it is more useful to discuss trends in sales/costs that reflect industry conditions or strategic decisions by the company being studied. If you are asked about a value for a company, you should be prepared to support your answer by stating what analyses, facts, and assumptions lead you to that conclusion. Moreover, a good question can be worth as much as a good answer. I intend to cold-call one person to start the discussion for each case. I will then either continue to cold-call or ask for volunteers for follow-up questions and discussion.

Some of the points that I will use to grade class discussion are:

- Was the problem or issue clearly defined?
- Did you take a firm stand and back it with evidence?
- Did you outline your assumptions?
- Did you use the frameworks, valuation models and notes discussed in class?
- Did you explore the pros and cons of the strategic alternatives?
- Did you perform both qualitative and quantitative analysis?
- Was a plan of action presented along with implementation steps, timing and costs?
- How did you respond to your peer's questions about your solution?

I will mark participation after each class. Therefore, it is imperative that you display your name card at each and every class session. If you do not display your tag, you may not receive credit. Moreover, missing class, arriving late, or exhibiting any disruptive behavior (talking, using the phone, etc.) will

reduce participation scores. The class will be much more enjoyable and productive for everyone, if there is active debate and consideration of the issues at hand.

d. Peer evaluation. At the end of the semester, I will ask each member of the class to evaluate the contribution of other class members to the quality of the class discussion throughout the semester.

f. Final Grade. The evaluation format is designed to generate meaningful dispersion in measured student performance. The class gpa will be a target of 3.5 but may vary slightly. Grades will also include +/- . Though each assignment is graded separately, final grades will be assessed based on the totality of all work and participation of each individual.

Academic Dishonesty

I have no tolerance for acts of academic dishonesty. Such acts damage the reputation of the school and the degree and demean the honest efforts of the majority of students. The minimum penalty for an act of academic dishonesty will be a zero for that assignment or exam.

The responsibilities for both students and faculty with regard to the Honor System are described on <http://mba.mcombs.utexas.edu/students/academics/honor/index.asp>. As the instructor for this course, I agree to observe all the faculty responsibilities described therein. During Orientation, you signed the Honor Code Pledge. In doing so, you agreed to observe all of the student responsibilities of the Honor Code.

If the application of the Honor System to this class and its assignments is unclear in any way, it is your responsibility to ask me for clarification.

Students with Disabilities

Upon request, the University of Texas at Austin provides appropriate academic accommodations for qualified students with disabilities. Services for Students with Disabilities (SSD) is housed in the Office of the Dean of Students, located on the fourth floor of the Student Services Building. Information on how to register, downloadable forms, including guidelines for documentation, accommodation request letters, and releases of information are available online at <http://deanofstudents.utexas.edu/ssd/index.php>. Please do not hesitate to contact SSD at (512) 471-6259, VP: (512) 232-2937 or via e-mail if you have any questions.

McCombs Classroom Professionalism Policy

The highest professional standards are expected of all members of the McCombs community. The collective class reputation and the value of the Texas MBA experience hinges on this. Faculty are expected to be professional and prepared to deliver value for each and every class session. Students are expected to be professional in all respects. The Texas MBA classroom experience is enhanced when:

Students arrive on time. On time arrival ensures that classes are able to start and finish at the scheduled time. On time arrival shows respect for both fellow students and faculty and it enhances learning by reducing avoidable distractions.

Students display their name cards. This permits fellow students and faculty to learn names, enhancing opportunities for community building and evaluation of in-class contributions.

Students minimize unscheduled personal breaks. The learning environment improves when disruptions are limited.

Students are fully prepared for each class. Much of the learning in the Texas MBA program takes place during classroom discussions. When students are not prepared they cannot contribute to the overall learning process. This affects not only the individual, but their peers who count on them, as well.

Students attend the class section to which they are registered. Learning is enhanced when class sizes are optimized. Limits are set to ensure a quality experience. When section hopping takes place some classes become too large and it becomes difficult to contribute. When they are too small, the breadth of experience and opinion suffers.

Students respect the views and opinions of their colleagues. Disagreement and debate are encouraged. Intolerance for the views of others is unacceptable.

Laptops are closed and put away. When students are surfing the web, responding to e-mail, instant messaging each other, and otherwise not devoting their full attention to the topic at hand they are doing themselves and their peers a major disservice. Those around them face additional distraction. Fellow students cannot benefit from the insights of the students who are not engaged. Faculty office hours are spent going over class material with students who chose not to pay attention, rather than truly adding value by helping students who want a better understanding of the material or want to explore the issues in more depth. Students with real needs may not be able to obtain adequate help if faculty time is spent repeating what was said in class. There are often cases where learning is enhanced by the use of laptops in class. Faculty will let you know when it is appropriate to use them. In such cases, professional behavior is exhibited when misuse does not take place.

Phones and wireless devices are turned off. We've all heard the annoying ringing in the middle of a meeting. Not only is it not professional, it cuts off the flow of discussion when the search for the offender begins. When a true need to communicate with someone outside of class exists (e.g., for some medical need) please inform the professor prior to class. Remember, you are competing for the best faculty McCombs has to offer. Your professionalism and activity in class contributes to your success in attracting the best faculty to this program.

Class Schedule/Readings

Date	Agenda	Reading/Preparation Work
28-Aug	Lecture 1: Course introduction and overview	Textbook Chapter 1
2-Sep	Lecture 2: How private equity funds are raised, structured, and managed	Textbook Chapter 2
4-Sep	Lecture 2: Continued	Textbook Chapter 3
9-Sep	Case 1	Yale University Investments Office: February 2011 (investing in private equity)
11-Sep	Lecture 3: Creating the Deal	Textbook Chapter 3
16-Sep	Case 2	Acme Investment Trust : January 2001 (analyzing an investment in a private equity fund)
18-Sep	Lecture 3: Continued	Textbook Chapter 3
23-Sep	Case 3	Oregon Public Employees Retirement Fund: Push and Pull Over GP/LP Compensation
25-Sep	Lecture 4: Deal Valuation	Textbook Chapter 4
30-Sep	Lecture 4: Continued	Textbook Chapter 4
2-Oct	Case 4	Bidding for Hertz: Leveraged Buyout (LBO valuation)
7-Oct	Case 5	HCA, Inc., (LBO Process)
9-Oct	Lecture 5: Deal Structuring	Coursepack: Company Sale Process Textbook Chapter 5
14-Oct	Lecture 5 : Continued	Textbook Chapter 5
16-Oct	Midterm	Study
21-Oct	Lecture 5 : Continued	Term Sheet Negotiations for Trendsetter, Inc. (Interactions with owners/managers) Coursepack: Note on LBO Capital Structure
23-Oct	Case 7	Auction for Burger King (Sales Process)
28-Oct	Case 8	Berkshire Partners: Bidding for Carter's
30-Oct	Lecture 7: Management after the Investment	Textbook Chapter 6

4-Nov	Lecture 7: Continued	Textbook Chapter 6
6-Nov	Case 9	Between a Rock and a Hard Place: Valuation and Distribution in Private Equity
11-Nov	Case 10	O.M. Scott & Sons Co. Leveraged Buyout (Incentive mechanisms)
13-Nov	Lecture 8: Exit Strategies	Textbook Chapter 7
18-Nov	Lecture 8: Continued	Textbook Chapter 7
20-Nov	Case 11	HCA, Inc. LBO Exit (Exit Strategies)
25-Nov	Case 12	Investing in Sponsor-Backed IPOs: The Case of Hertz (Exit Strategies)
2-Dec	Lecture 9: Restructuring	Handout
4-Dec	Wrap-up	Final Assignment Handed Out

*The exam dates are fixed, but the course schedule may vary depending on the pace of the class.