

Which of the seven prices is this?

Chapters 1 and 2. A deal has one announcement and several prices. Fill all seven before reading the strategic rationale; then say which one the paper quotes, and to which question it is the answer.

Deal		Reviewer	
Paper dated		Date	

Price	Built as	Amount	Times EBITDA	Quoted where in the paper
1. Announced enterprise value				
2. Equity price				
3. Equity after debt-like items				
4. What the seller receives				
5. Cash out at completion				
6. Total expected outlay				
7. Total outlay, full earn-out				

Built as (for column 2)	
2 = 1 less net debt assumed; 3 = 2 less the debt-like items; 4 = 3 plus the earn-out at FAIR VALUE	
5 = 3 plus the buyer's own fees; 6 = 5 plus the earn-out at NOMINAL EXPECTED; 7 = 5 plus the earn-out ceiling	
Multiples only on rows 1 to 4: add net debt and the debt-like items back to 2, 3 and 4. Rows 5 to 7 carry fees: write "not meaningful"	

Question	Answer	Source / note
The tests		
Rows 1 to 3 print the same multiple (if not, it is a transcription error, not a judgement)		
The gap between the multiples that differ, times EBITDA, names an item: earn-out, retention, seller note, completion accounts		
No multiple divides a price from one state of the world by earnings from another (full earn-out over today's EBITDA)		
Fees are inside no numerator of any multiple		
The earn-out is at fair value in the price and at nominal in the funding plan, in every section of the paper		

On the book's deal: 248.4, 209.9 and 194.3 million all print 9.0000 times; 203.9 million prints 9.3496, the third of a turn being the earn-out at fair value; 9.9058 is the hybrid that must not be quoted.

The debt-like items, qualified three times

Chapter 3. "Treated as debt-like" is three decisions, not one. List every item negotiated off the price and answer the three questions separately. Each column feeds a different part of the model.

Deal		Reviewer	
Paper dated		Date	

Item	Amount (price falls by all of it)	Already on the target's balance sheet?	Bears interest after completion?	In the lender's covenant?	Where the expense sits today

Perimeter	Total	Feeds
Price reduction: all items		
Off the balance sheet		
Bearing interest (plus any discounted liability the lender counts)		
Inside the covenant (plus the earn-out at fair value, if the lender counts it)		

Question	Answer	Source / note
Consequences to check		
Off-balance-sheet items reduce the price AND the net assets acquired: neutral to the excess		
On-balance-sheet items reduce the price only: they shrink the excess, the intangibles and the amortisation		
Take each item out of the covenant in turn: does the leverage cross a rung? (On the book's deal, only the leases move anything)		
Any item whose cost is already inside EBITDA carries no interest and enters the leverage numerator only if EBITDA is restated		

Book's deal: 15,600,000 off the price; 11,350,000 off balance sheet; 7,200,000 bearing interest; 11,450,000 in the covenant. Three perimeters, three numbers.

The framework test: where is the expense sitting?

Chapter 4. One phone call before any leverage or interest line is built: which reporting framework does the target use, and is the cost of each liability already inside the EBITDA the deal is priced on?

Deal		Reviewer	
Paper dated		Date	

Question	Answer	Consequence
Target's reporting framework (local GAAP / IFRS)		
Leases: operating (rent in EBITDA) or capitalised?		
Pension: provided or in a note?		
If the rent is in EBITDA: is interest charged on the lease anywhere in the model?		
Is the lease in the covenant numerator? If so, is EBITDA restated by the rent?		
The covenant definition: frozen GAAP, or current?		

Test	Leverage	Rate	Year-one accretion
As the paper models it			
Lease in the covenant only (numerator restated, denominator not)			
Lease in the covenant and bearing interest			
Both sides restated (liability in, rent out of costs)			

Distance from the leverage to the next rung, in turns and in money (times combined EBITDA, divided by the share of target debt that reaches the numerator):

Book's deal: the 4,150,000 lease moved the headline from minus 15.7134 to minus 19.8485 per cent when put in the covenant and charged interest: both sides of the ratio, or neither.

The earn-out: four numbers, three places

Chapter 5. A paper that gives one number for contingent consideration owes you four. Then check that each appearance uses the right one.

Deal		Reviewer	
Paper dated		Date	

The four numbers	Value	Source
Ceiling		
Probability applied (and by whom)		
Discount rate used, and why that rate (cost of debt: the probability has already taken the risk out)		
Where the payment is in the funding table (year, facility)		

Where it appears	Carried at	Amount	Right?
The price and the entry multiple			
Value created			
The leverage covenant			
The purchase price allocation (excess, intangibles)			
The cash forecast and the funding plan			
The income statement before settlement (unwind)			
After settlement: interest, extra EBITDA, extra depreciation			

Question	Answer	Source / note
Tests		
Fair value in every price and value line; nominal in every cash line; never mixed		
Discounted at the cost of capital? The risk is charged twice (8,627,564 against 9,649,087 on the book's deal)		
After settlement all three lines or none: interest on the payment, the EBITDA that triggered it, the depreciation that comes with it		
Value created: is the outperformance that triggers the payment credited anywhere? If not, say which convention is printed		

Book's deal: 25,000,000 at 45 per cent, year three, 5.25 per cent: 9,649,086.71. Symmetric value created minus 10,981,108 against minus 17,530,855.

What the business is worth without you

Chapter 6. Compute this before the multiple. Four lines, then the same instrument on the acquirer, and a yardstick named out loud.

Deal		Reviewer	
Paper dated		Date	

Line	Target	Acquirer (same ratios)
Operating profit (EBITDA less depreciation)		
less tax		
plus depreciation and amortisation		
less capital expenditure		
less increase in working capital		
= normalised cash flow		
Conversion: cash flow over EBITDA		
Next year's flow at growth g		
Intrinsic value = next year's flow / (cost of capital less g)		
Price paid / market enterprise value		
Premium (price less intrinsic), and per cent		

Question	Answer	Source / note
The yardstick		
Which governs the paper: discounted cash flow or trading multiples? Written where?		
If the target is "cheap" on DCF: what does the same DCF say of the acquirer's shares being issued?		
If it is "cheap" on multiples: is the premium page written in multiples too?		
Exceptional items, pension and litigation: in the price or in the flow, never both		

Book's deal: 13,900,000 of cash (50.36 per cent of EBITDA) at 9.25 and 1.75 per cent is 188,576,667; the premium is 59,823,333, larger than every synergy the deal will produce.

The synergy slide, and the coefficient behind it

Chapter 7. Run rate, ramp and bill on one table; then divide the paper's value of the synergies by its run rate and look at the coefficient.

Deal		Reviewer	
Paper dated		Date	

Year	Share of run rate	Gross synergy	Cost to achieve	Net after tax	Discount factor	Present value
1						
2						
3						
4 (perpetuity from here)						
Total						

Ratio	Value
Run rate over target revenue (the one an operating manager can defend)	
Run rate over target EBITDA (the one that gets quoted)	
Cost to achieve over run rate	
Coefficient before the bill (value of one unit of run rate)	
Effective coefficient after the bill (value / run rate)	
The paper's own coefficient (its value / its run rate)	

Question	Answer	Source / note
Reading the coefficient		
Is there a cost to achieve at all, and where in the pack is it classified?		
Coefficient above the instant-and-free one (run rate x $(1-t)(1+g)/(r-g)$, divided by the run rate)? Then the rate or the growth has moved too		
Share of the value beyond year three (on the book's deal, 95.5 per cent)		
Same growth rate here as in the target's own valuation?		

Book's deal: 7,200,000 ramped 30/70/100, 9,400,000 spent 55/30/15: 58,841,565, a coefficient of 9.024135 before the bill and 8.1724 after it. Instant and free: 10.175.

How much synergy it actually takes

Chapter 8. The question the room can settle. Three items, one division, stated in revenue points.

Deal		Reviewer	
Paper dated		Date	

The hurdle	Amount
Premium over intrinsic value	
Transaction fees	
Earn-out at fair value	
Total to be covered	

Basis	Required run rate	Times the announcement	Per cent of target revenue	Per cent of target EBITDA
Integration budget fixed: (hurdle + bill after tax, discounted) / coefficient before the bill				
Budget scaling at the paper's own cost ratio: hurdle / effective coefficient				
With the earn-out outperformance credited (symmetric)				

Three break-evens, three questions	Answer
Value: over the life of the deal (run rate needed)	
Year-one earnings, with the amortisation (share of run rate in year one)	
Year-one earnings, without it	
Hurdle at half a point lower and higher cost of capital	

The operating question the deal turns on, in revenue points: announced ____ % against break-even ____ %. Is the difference available, site by site?

Book's deal: 3.9130 per cent promised; 4.9688 needed at a fixed budget, 5.0789 if the budget scales.

The value bridge: at least five lines

Chapter 9. A value-created figure shown as a two-line subtraction has left lines out. Rebuild the harsh version, set the paper's beside it, and reconcile.

Deal		Reviewer	
Paper dated		Date	

Line	This review	The paper	Difference
Synergies, with ramp and cost to achieve			
Premium over intrinsic value			
Transaction fees			
Earn-out at fair value			
Earn-out outperformance credited (if the symmetric convention is used)			
Value created			

The gap, convention by convention	Amount	Direction
Perpetuity taken today rather than from the year it is reached		
The ramp years, delivered and discounted		
Cost to achieve, after tax and discounted		
Transaction fees		
Earn-out at fair value		
Total (must equal the difference between the two answers)		

How many conventions separate the paper from the harsh version, and do they all point the same way?

Book's deal: the paper's plus 13,436,667 against minus 17,530,855; the gap of 30,967,522 is four conventions and no error.

The funding slide

Chapter 10. It is not plumbing: it sets the group's rate on all its debt. Three perimeters and one missing cheque.

Deal		Reviewer	
Paper dated		Date	

Funding of completion	Amount
Cash out at completion, fees included	
New debt (share ____ %)	
Equity raised	
Issue price (discount ____ % on ____)	
Shares issued, and shares after	
Dilution = new shares / ENLARGED count	
Extra shares caused by the placing discount	

Perimeter	Amount	Used for
Covenant debt (as the credit agreement defines it)		
Interest-bearing debt		
Target's own assumed debt		
Combined EBITDA used by the lender (synergy credit? lease restatement?)		
Leverage, margin, all-in rate		
Standalone rate before the deal, and the repricing of existing debt		

Question	Answer	Source / note
Three questions out loud		
What does the placing discount cost, in shares?		
Which perimeter does the covenant measure, and was the same one (wrongly) used for interest?		
What is paid later and missing from the funding total (earn-out, deferred consideration), and in which year?		

Book's deal: 201.2 million, 60/40; 10,153,283 shares at 7.9265 (dilution 7.9228 per cent); leverage 2.9694, 125 basis points; 466,750 a year of repricing on debt that predates the target.

The ladder and the fixed point

Chapter 11. If anything in the leverage numerator is discounted at the rate the margin grid produces, the model has a fixed point: solve it, report it, and find the band where it has none.

Deal		Reviewer	
Paper dated		Date	

Leverage band	Margin	All-in rate
below ____		
____ to ____		
____ to ____		
____ to ____		
above ____		

Liabilities in the numerator discounted at the grid rate	Carrying value at the low rate	At the high rate	Fall
Deferred or contingent consideration			
Discounted provision			
Pension, discounted at a spread-linked rate			
Lease liability at the incremental borrowing rate			
Total fall (the slack the higher margin creates)			

The band	Value
Leverage now and nearest rung (distance in turns)	
Share of a euro of target net debt that reaches the numerator (1 less the debt share of funding)	
Target net debt at which the rung is reached	
Width of the band with no solution = total fall / that share	
Branch taken inside the band, and who decided	

Book's deal: rung reached at 47,952,283 of target net debt; no solution up to 48,460,708, a band 508,424 wide; the earn-out loses 203,370 between 5.25 and 6.00 per cent. A step is read point by point, never with a ruler.

Allocating the price

Chapter 12. Four inputs, all settled after signing, decide the largest recurring charge the deal creates.

Deal		Reviewer	
Paper dated		Date	

Line	Amount	Note
Consideration transferred: equity after debt-like items plus earn-out at fair value (not EV, not cash out)		
Book equity of the target		
less liabilities recognised on acquisition that the target's balance sheet does not carry		
plus any asset recognised with them (a right-of-use asset comes with a lease liability)		
= net assets acquired		
Excess to allocate		
Identified intangibles (share ____ %)		
Deferred tax liability on them (tax rate x intangibles)		
Goodwill = excess less intangibles PLUS the deferred tax		
Annual amortisation (life ____ years), and per share after tax		
Tax saving the deferred tax liability stops the model collecting		

Question	Answer	Source / note
Before quoting the goodwill		
Which of the seven prices went in? Using the cash out would be wrong by fees in and earn-out out		
Were off-balance-sheet liabilities recognised, and with what assets?		
On-balance-sheet debt-like items: they shrink the excess, the others do not		
Amortisation compared to the synergy run rate: which is larger, and from which year?		

Book's deal: 203,949,087 against 34,950,000: excess 168,999,087; intangibles 64,219,653; deferred tax 16,054,913; goodwill 120,834,347; 7,135,517 a year for nine years, 64,483 short of the synergy run rate.

Four columns and the year-one bridge

Chapters 13 to 15. Print the four conventions; then read the bridge by line, not by total, and sort the lines the deal created from the one it did not.

Deal		Reviewer	
Paper dated		Date	

Year	EPS	Statutory	Adjusted (no fees, no integration)	Cash (no amortisation)	Adjusted cash
1					
2					
3					
4					
5					

Bridge line (after tax, per share)	Amount	Created by the deal?	Cash?	Recurs / stops when
Standalone EPS				
Dilution from the share issue				
Repricing of existing debt				
Target's operating profit				
Synergies, year one				
Integration cost, year one				
Transaction fees				
Amortisation of intangibles				
Interest on the target's assumed debt				
Interest on new debt				
Interest on interest-bearing debt-like items				
Unwind of the earn-out				
Combined EPS (the zero below it proves nothing)				

The test for each line: if the transaction had not happened, would anyone have paid this? The target's own interest: yes. Removing it from an adjusted column is worth 2.8342 points on the book's deal.

Seven questions for Thursday

Chapter 18. Two days, no model. Each question caught something on the book's deal that survived several hostile reviews.

Deal		Reviewer	
Paper dated		Date	

Question	What the paper says	What it should have said
1. Which price is this, and is any fee in the numerator of the multiple?		
2. What was agreed to be debt-like, and was each item qualified three times?		
3. Which column does "accretive" refer to, and where are the other three?		
4. What do the synergies cost, when do they arrive, and what run rate breaks even?		
5. What discount rate produced the value, and what is it half a point either side?		
6. Which charges did the deal create? Is the target's own interest in the adjusted list?		
7. Where are the steps? Is any table smooth across a covenant rung?		

Value created	g low	g base	g high
Cost of capital low			
Cost of capital base			
Cost of capital high			

If the sign changes inside the grid, the paper has reported an opinion about the cost of capital and called it a valuation. On the book's deal value created is nil at 8.77 per cent with 1.75 per cent growth, and at 2.22 per cent growth with 9.25 per cent.