

FIN31401
ADVANCED PRIVATE EQUITY

Faculty: José Miguel Gaspar (A406)

Objectives

This seminar focuses on themes related to the universe of Private Equity. At the end of the course, participants should:

- Be thoroughly familiar with the private equity industry – its organization and its most important players, as well as the different incentive structures they are subject to
- Understand with how private equity funds raise capital, structure their operations, select their portfolio of deals, and exit their investments
- Understand the structuring of deals and the different types of financial securities employed
- Consolidate their knowledge of valuation and model-building as applied in PE settings
- Be knowledgeable about the theoretical sources of value in private equity deals, as well as the associated empirical evidence about their existence

Background and Prerequisite Courses

There are 4 compulsory pre-requisites to this course: FIN123/124 (Financial Theory), FIN128 (Corporate Financial Management), and FIN253 (Mergers and Acquisitions), and MGT364/5 Introduction to Private Equity.

Organization

The course is composed of:

- *Regular lectures.* The lectures cover the main topics of the course (see “Outline” below). As part of the lectures, students have to prepare a presentation of the case study allocated to each session.
- *Two mini-conference sessions with invited guests.* In each of these sessions, three industry professionals come to present their views and experience on the PE industry. Students are expected to participate actively and professionally in the mini-conferences. The mini-conferences take place at the CNIT, in La Defense.
- *Simulation Game.* In this session, students play the role of members of a PE investment team participating in an auction sale of a company. This year the simulation game takes place in the form of an HBS simulation.

- *Final exam.* The exam lasts three hours. You'll need a calculator.

Readings

There is no textbook that addresses the content of the course. The main book references are:

- [LHL] Lerner, Josh, Felda Hardymon and Ann Leamon, 2008, "Venture Capital and Private Equity: A Casebook" (4th edition), John Wiley and Sons: New Jersey.
- [M] Metrick, Andrew, 2007, "Venture Capital and the Financing of Innovation", John Wiley and Sons: New Jersey.

Grading

The final grade is calculated as follows:

- Denote the participation grade by PART.
- Denote the exam grade by EXAM.
- Denote the simulation game grade by SIM.
- The final grade is equal to the $0.3 \times \text{PART} + 0.5 \times \text{EXAM} + 0.2 \times \text{SIM}$, as long as $\text{EXAM} > 10$ and $\text{SIM} > 10$.

The final grade will be posted online on the Chair's website. Please note that students that fail the Course or miss to fulfill the Chair's requirements (see 'Absences') after the deadlines will not be considered alumni of the Chair.

Absences

Attendance to all meetings is compulsory and all absences must be justified. **More than 3 non-justified absences lead to dismissal from the course.**

Outline of the Lecture Sessions

Session 1

Objectives of investors in private equity. PE fund structuring and the fund raising process. Fees and carry. Protection provisions.

Case: "Pawson Foundation: August 2006" HBS 9-806-042

Readings:

- LHL: chapters 1, 3, 5, 7. M: chapters 1, 2, 4.
- Gompers, P. and Josh Lerner, 2000, "Money chasing deals? The impact of fund inflows on private equity valuations", *Journal of Financial Economics* 55, 281-325.

- Metrick, Andrew, and Ayako Yasuda, 2008, “The Economics of Private Equity Funds”, Yale School of Management mimeo.
- Stromberg, Per, 2008, “The demography of Private Equity”, mimeo.

Session 2

Investment valuation and IRR calculation.

Case: “Butler Capital Partners and AutoDistribution” HBS 9-800-224

Readings:

- LHL: chapters 15, 17. M: chapters 10-13.
- Note “The Company Sale Process” HBS 9-206-108.
- Bank for International Settlements, 2008, “Private equity and leveraged finance markets”, CGFS working paper 30.

Session 3

Acquisition structures. Legal issues in debt structuring: subordination, financial assistance.

Tax issues in debt structuring. Debt in cross-border deals.

Case: “Legrand: A Chance LBO.”

Readings:

- Axelson, Ulf, Tim Jenkinson, Per Strömberg, Michael S. Weisbach, 2008, “Leverage and Pricing in Buyouts: An Empirical Analysis”, mimeo.
- Kaplan, Steven, Jeremy Stein, 1993, “The evolution of buyout pricing and financial structure in the 1980s”, *Quarterly Journal of Economics*, 108 (2), 313-357.

Session 4

Equity securities. Management incentive tools.

“Case: Metapath Software: September 1997” HBS 9-899-160

Readings:

- LHL: chapter 13. M: chapters 7-9, 14-16.
- Kaplan S. and Stromberg, P. (2003), “Financial Contracting Theory Meets the Real World: An Empirical Analysis of Venture Capital Contracts”, *Review of Economic Studies* 70, 281-315.

Session 5

Exit strategies: asset sales, IPOs/reverse LBOs, secondary LBOs, private placements.

“Case: Exxel Group: March 2001” HBS 9-202-053

Readings:

- LHL: chapter 22.
- Brav, Alon and Paul Gompers, 1997, “Myth or reality? The long-run underperformance of Initial Public Offerings: Evidence from venture and non-venture capital-backed companies”, *Journal of Finance* 52, 1791-1821.
- Cao, Jerry, Josh Lerner, 2009, “The performance of reverse leveraged buyouts”, *Journal of Financial Economics* 91 (2) 139-157.

Session 6

Performance measurement in Private Equity. Empirical evidence on performance.

Case: “KKR Private Equity Investors: Private Equity Goes Public”

Readings:

- Conroy, Robert M., Robert S. Harris, 2007, “How good are Private Equity returns?”, *Journal of Applied Corporate Finance* 19 (3), 96-108.
- Kaplan, Steven, Antoinette Schoar (2005), “Private equity performance: Returns, persistence, and capital flows”, *Journal of Finance* 60 (4), 1791-1823.
- Phalippou, Ludovic, Oliver Gottschalg, 2009, “The performance of Private Equity Funds” *The Review of Financial Studies* 22 (4) 1747-1776.

Session 7

Mini-conference 1. Guest speakers: Funds, Banks, Mezzanine.

Session 8

Mini-conference 2. Guest speakers: Secondaries, Venture Capital, Growth Capital.

Session 9

Simulation game: “Blackstone/Celanese.”

Session 10

Final Exam. The exam lasts for 3 hours. You are allowed to bring one A4 sheet of paper written on both sides. Don't forget to bring a calculator. **WARNING: The final exam cannot be replaced by any assignment, project, etc. if you do not attend. BE THERE OR BE SQUARE.**

Contacts

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