



FINC- GB 3365: Private Equity Finance

Spring 2021

Meets: Mondays and Wednesdays 3:30-4:50 PM.

Remote Instruction

Instructor Information:

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Office Hours will be held virtually Monday through Wednesday 5-6 PM and Friday 9-10 AM for students located in Europe or Asia.

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Course Summary

This course will use the cases, lectures and to provide a comprehensive overview of private equity finance. The objective of this course is to survey the private equity industry and to provide an understanding of the origination, valuation, execution, monitoring, and realization of private equity transactions and of the process of investing in private equity funds. The course will include a series of lectures designed to teach specific skills and concepts used in the practice of private equity and in the M&A business more broadly and case discussions through which those skills and concepts will be illustrated and utilized.

Private equity, including venture capital, growth investing, distress, and leveraged buyouts, has grown from less than \$5 billion in assets under management in 1980 to \$3.0 trillion today and is therefore a field worthy of study. Its emergence as a significant global asset class has elevated the industry in the public consciousness and led to a debate about its effect on portfolio companies, contribution to systemic risk, and compensation and taxation practices. The dramatic growth of assets under management by private equity firms has also led to a compression in investment returns, making the tasks of executing successful private equity transactions and selecting private equity funds increasingly challenging.

The first section of this course will examine the industry from the perspective of the private equity firms who invest in and manage portfolio companies (referred to as the general partners or GPs). While this section will address all significant segments of the GP universe, including venture capital, growth investing, distressed investing and leveraged buyouts, the focus will be on the LBO industry. In this section, we will discuss the techniques used by private equity firms to originate, diligence, value and execute transactions as well as how these PE firms seek to add value to their portfolio companies and eventually exit these investments. Through the cases, we will analyze several private equity transactions and situations and apply these concepts and techniques.

The first section of the course will include a lecture on LBO modeling as well as several assignments through which students will learn how to build an LBO model for a SaaS business. These exercises, while **highly time-intensive**, will significantly deepen students' understanding of financial statements and private equity transactions.

The second section of the course will examine the private equity industry from the perspective of the institutions that invest in private equity funds (the limited partners or LPs and their consultants or “gatekeepers”). We will survey the LP universe (pension funds, endowments, fund-of-funds, sovereign wealth funds, and secondary funds). We will analyze the investment track records of GPs, identify the factors that lead to strong performance, and review the process for PE fund raising, due diligence and fund selection. We will also learn about the economic arrangements between LPs and GPs and discuss the terms of fund agreements and the current state of LP/GP relationships.

Instructor Policies

Attendance/Lateness

This course will rely and be heavily graded on active, high quality class participation and on-time attendance. **Students are expected to attend every on-line session synchronously, with cameras turned-on.** The TFs will take attendance based on the Zoom attendance reports after each session.

Any student who is taking the course from a location with a greater than 5-hour difference from NYC will, after clearing this with the instructor, be allowed to attend asynchronously by

watching class recordings. These students will be required to provide a brief one-page summary of each session's content as proof of attendance.

Students who normally would not qualify for asynchronous attendance can do so for individual sessions for the following reasons only: documented illness, family emergency, religious observance, or civic obligation. Recruiting activities are not acceptable reasons for synchronous class absences. **Please notify me of any absence prior to the start of the class.** Unexcused absence and/or tardiness will hurt your grade, potentially materially.

Assignments

All assignments must be submitted electronically through NYU Classes prior to the deadline stated in the syllabus. Late submissions will not be accepted and will be assigned a failing grade.

Honor Code

All students must adhere to the Stern Code of Conduct: <http://www.stern.nyu.edu/uc/codeofconduct>

Students with Disabilities

Students who require academic accommodation during the course should provide me with a letter from the Moses Center for Students with Disabilities (<http://www.nyu.edu/csd>) outlining the accommodations they recommend.

Class Process

In addition to lectures, this class will utilize eleven cases to cover the material. The process for reviewing cases will work as follows:

Each student is required to submit one-page written case summaries for any seven of the eleven assigned cases (the selection is up to the student). These submissions will be assigned a grade of No Submission (if it is functionally incomplete), check, or check plus (if the submission goes the extra mile). These case summaries will be included in the participation portion of the course grade.

The questions for the case summaries can be found in the Assignments tab of the NYU Classes course site

At the beginning of each case discussion, I may cold call an individual student to present their summary of the case. I may continue to cold call students throughout the case discussions and will also call on volunteers. While I expect a robust discussion in which students feel free to disagree with each other (and with me) I would like case discussions to be conducted with utmost civility and respect.

In addition, there will be six individual assignments due throughout the course, each relating to the construction of a different section of the same LBO model: a) quality of earnings analysis, b) the SaaS revenue model, c) the SaaS operating model, d) sources and uses of funds, capital structure and debt schedules, credit statistics and opening balance sheet adjustments, e) valuation, IRR, DCF, and value creation attribution analysis and f) leveraged recapitalization analysis.

There will be an additional, optional assignment (the Waterfall Exercise) which will only count if it brings up the student's grade average. This optional assignment will have a weighting of 12.5% and, if used, will reduce the weightings of all other assignments by 12.5%.

Class participation is an important element of your grade. I will grade participation based on the quality of contributions and insights. Quality comments 1) contribute to moving the discussion forward, 2) offer a unique and relevant perspective on the issue, 3) build on the comments of others, and 4) show evidence of analysis of inherent trade-offs. The class participation assessment will also consider the asking of relevant questions, on-time attendance, posting of questions and relevant materials in the class Forum, the quality of the one-page case write-ups, the quality of the session summaries posted by asynchronous participants, and other evidence of active engagement.

There will be no midterm or final exam.

Use of "Forum" section of NYU Classes Site

Questions of a non-personal nature regarding assignments should be posted in the Forum section of NYU Classes, where they will be answered by me or a TF. This ensures that all students benefit from the Q & A related to that assignment. Students are welcome to answer questions posted on Forum. Comments, questions and answers that are particularly helpful and illuminating will count towards your class participation grade.

Grading

Class Participation:	25%
LBO modelling and other individual assignments:	75%

See the bottom of the syllabus for a break-down of assignment weightings.

I use a 0-5 grading scale for all assignments (except the case write-ups as discussed above). Because the grades are curved, it is difficult to precisely translate this scale to an A through F scale. However, the following is a reasonable general guideline:

- 5 = A
- 4 = B+
- 3 = B/B-
- 2 = C+/C-
- 1 = D
- 0 = F

Grade distribution will follow the Stern finance department grading curve guidelines for MBA non-introductory courses, which suggests the number of A/A- be limited to roughly 35% of the class.

Course Materials

Most course materials are included in the course pack, which is arranged in the order of the course outline below. You may purchase your course pack at the bookstore or online. If you purchase it in-store, the access key code will print on the receipt, so you need to keep the receipt.

If you buy it online, you need to know your course and section numbers, i.e. FINC – UB 32. The website is: shopnyu.com. Once you complete the purchase, the access key code will be emailed to you. You can also purchase a digital copy by clicking the XanEdu Course Pack link on the left-hand drop-down menu in the NYU Classes course site.

Here is a link to the bookstore ordering page:

<http://www.bkstr.com/nyustore/shop/textbooks-and-course-materials>

I will distribute some additional material throughout the semester, which will be posted in the Resources section of the NYU Classes course site.

Course Outline

Class #	Date	Topic	Cases/Lecture	Readings
1	2/1	Overview of Course and Introduction to PE	Lecture	Lerner, "A Note on Private Equity Partnership Agreements".
2	2/3	The Role of PE in Portfolio Construction	Lerner, Rhodes-Kropf, Burbank, "The Canadian Pension Plan Investment Board: October 2012".	
3	2/8	The PE Firm & Deal Origination	Godes, Egawa & Yamazaki, "Carlyle Japan (A), (B), and (C)".	
4	2/10	PE Due Diligence	Lecture	
5	2/17	Due Diligence Analytics: Q of E Debt-like Items, Working Capital and Purchase Price Adjustments	Lecture	
6	2/22	Pre and Post-Money Valuation and Bridging Enterprise Value to	Lecture	

		Equity Value + the SaaS Business Model		
7	2/24	LBO Modeling (1)	Lecture	Schwed, "A Note on Building an LBO Model" Section 1
8	3/1	PE Due Diligence	Roberts, "Summit Partners -- The FleetCor Investment (A)".	
9	3/3	PE Due Diligence	Roberts, "Summit Partners--The FleetCor Investment (B) and (C)".	
10	3/8	Deal Execution: VC Term Sheets	Strebulaev, Gouw Ranzetta & Hoyt, "Evaluating Venture Capital Term Sheets".	Hardymon & Lerner, "A Note on Private Equity Securities" Roberts & Stevenson, "Deal Structure and Deal Terms".
11	3/10	Capital Structure in Leveraged Transactions (1): Overview	Lecture	Schwed, "A Note on Building an LBO Model" Section 2. Gompers, Ivashina & Van Goul, "Note on LBO Capital Structure".
12	3/15	Capital Structure in Leveraged Transactions (2): The Cash Flow Sweep & Equity Structure	Lecture	
13	3/17	Distress Investing: Loan-to-Own	Gilson & Abbott, "Countrywide plc".	Fruhan, "Restructuring Distressed Companies-Cross National Comparisons."
14	3/22	Valuation Techniques in PE	Lecture	Kaplan, "A Note on Discounted Cash Flow Valuation Methods"

				<p>Ivashina & Boe, "Primer on Multiples Valuation and Its Use in Private Equity Industry".</p> <p>Hellmann, "A Note on Valuation of Venture Capital Deals".</p>
15	3/29	LBO Modeling (2)	Lecture	
16	3/31	Value Creation in PE	Lecture	Rogers, Holland & Haas, "Value Acceleration: Lessons from Private Equity Masters".
17	4/5	Deal Execution and Value Creation in PE	Goodson, McGinnis, Zeisberger, "Differentiation Beyond Price: CD&R's Strategy in Acquiring Hussman".	
18	4/7	Deal Execution and Value Creation in PE	Lerner, "Private Equity Transforming TDC"	
19	4/12	PE in Emerging Markets	Weiss, "ofo"	<p>Lerner, Leamon & Vase, "A Note on Private Equity in Developing Countries".</p> <p>Gompers, Ivashina & Dore, "Private Equity Valuation in Emerging Markets".</p>
20	4/14	PE Exits	Lecture	<p>Fruhan, "Company Sale Process"</p> <p>Lerner, "Note on the Initial Public Offering Process".</p>

21	4/21	PE Exits	Lerner & Tuzikov, "The Carlyle Group and Axalta".	
22	4/26	LBO Modeling (3)	Assignment Review	
23	4/28	Investing in PE Funds	Lecture	
24	5/3	Fund Economics and the Distribution Waterfall	Lecture	
25	5/5	The PE Firm as a Public Company	Hardymon, Lerner, Leamon, "The Blackstone Group's IPO".	
26	5/10	Course Recap	Lecture	

Deliverables:

Assignment	Due Date/Time	Grade Weighting
Quality of Earnings	2/26, 11 PM	5.0%
The Revenue Model	3/5, 11 PM	10.0%
The Operating Model	3/19 11 PM	15.0%
The LBO Model	4/9, 11 PM	20.0%
The LBO Model: Valuation, Returns, and Value Creation Attribution	4/23, 11 PM	12.5%
The Dividend Recapitalization	5/6, 11 PM	12.5%
The Waterfall Exercise	5/12, 11 PM	Optional: 12.5%