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Role of Investment Banks in the M&A Process: Internship at BNP Paribas

Mariana dos Santos Gomes | 27259



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Afonso Eça

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Abstract

This paper is based on an internship at the M&A team of BNP Paribas, and it aims to clarify the role of investment banks in mergers and acquisitions. It explains the organisation of these teams, and includes a detailed explication of the M&A process from the perspective of the investment bank. As valuation is a fundamental part of this process, an example is made on how to value a recent transaction, using different valuation methodologies. The report also contains a description of my personal experience during the internship.

Key words: Mergers and acquisitions, Valuation, Investment Bank, Process, Internship

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1. Introduction

This report was elaborated in the scope of an internship I am currently undertaking at BNP Paribas, in the team of Mergers and Acquisitions. It aims to expose and discuss the role of investment banks in M&A processes, based on my personal experience. Due to confidentiality issues I won't be able to disclose any projects I am involved on, nor possible sensitive information about the bank. I have been working on potential M&A deals, and I will share my experience by explaining the role of M&A teams in transactions, and what are usually their main tasks and responsibilities.

Mergers and acquisitions have a critical role in a dynamic economy, as they facilitate continuous growth of companies, and are often the best way to allocate resources. Their importance to investment banks is also significant, being one of the main services offered within corporate finance and representing a substantial portion of the firm's revenues. This report explores this very important process and details best practices that can guarantee a successful transaction. In addition, M&A is a professional area of interest of many finance students. In that sense, this paper can be very useful as it gives an inside perspective on how it is to work in this field.

The report will clarify how investment banks are relevant for mergers and acquisitions, and how the teams involved in this area of corporate finance are organized. It will detail the process of acquisition (from the sell-side and from the buy-side) from the perspective of the financial advisor, which is something that is not commonly discussed. In this process, valuation plays an important role and is one of the key determinants of the success of a transaction. As so, I'll use some of the most common valuation methods, namely discounted cash flows, trading multiples and precedent transaction multiples, and will give a practical example of how to value a company using the acquisition of Jimmy Choo by Michael Kors earlier this year. The report will also cover my personal experience during the internship, including main responsibilities and challenges.

2. Literature review

Mergers and acquisitions are complex processes, usually with very high stakes that can dictate the future of a business. They have a lot of specificities, and most managers don't have the necessary knowledge to perform a successful transaction by themselves. Plenty of research has been done on this topic, part of which aiming to explain the process and make it easier for companies to complete transactions successfully.

Sherman (2010) walks through every step of the deal process, offering practical advice for keeping deals on track and ensuring post-closing integration success. Reed, Lajoux and Nesvold (2007) give a detailed overview of the M&A process, from planning and finding the right target to valuation and pricing. They aim to provide accurate, practical and up-to-date answers to a very broad set of questions regarding mergers and acquisitions. Miller (2008) provides a legal approach to acquisitions, and his goals are to survey and explain the main legal factors that affects its feasibility and economic consequences, as well as the risks involved in its structure and implementation. All this literature gives guidelines to companies and management teams on how to execute a deal effectively.

Due to its complexity, financial advisors play a very important role in mergers and acquisitions. In many cases, especially in big transactions, it is the financial advisor that organizes the process and coordinates with the other side's advisors. However, there is very little literature about mergers and acquisitions from the investment bank's perspective. Rosenbaum and Pearl (2009) provide the groundwork for M&A in the point of view of the financial advisor, detailing processes, strategies, deal structure and analytics. They also explain how to perform "the valuation work at the core of the financial world", as it is a very big part of the financial advisor's role in a transaction.

Literature on mergers and acquisitions also tries to understand why do acquisitions exist, and what motivates a company to acquire other. According to Berk and DeMarzo (2014), "synergies are the most common justification that bidders give for the premium paid for a target (p.934)". These can be achieved by economies of scale and scope, efficiency gains or tax savings from operating losses. Other justifications for an acquisition might be growth pressure from investors, underutilized resources, or managerial motives. M&A also allow to expand into new geographic markets, diversify into new products/ services, and reduce the numbers of competitors, increasing market share (Sherman, 2010).

There is a very big question in research about M&A, which is whether or not it creates value. According to Koller, Goedhart and Wessels (2010), evidence shows that only a minority of acquisitions are good for the shareholders of the acquirers, because they only create value if the target's performance improves more than the premium paid over its intrinsic value. The work of Rehm and Siverstsen (as cited in Koller et al, 2010) shows that acquisitions collectively do create value for the shareholders of both the acquirer and the acquired company. However, Mark Mitchell and Erik Stafford, 2000 (as cited in Koller et al, 2010) "have found that acquirers

underperform comparable companies on shareholder returns by 5 percent during the three years following the acquisitions.” Koller et al. (2010) sums up research results, defending that “acquisitions that reduce excess capacity or put companies in the hands of better owners or managers typically create substantial value both for the economy as a whole and for investors”, which can be seen on the increase in the combined cash flows of the many companies involved in acquisitions. Even though they overall create value, its distribution tends to be unbalanced. In fact, most empirical research shows that one third or more of acquiring companies destroy value for their shareholders because they transfer all the benefits of the acquisition to the selling companies’ shareholders.

However, it is possible to do acquisitions that are actually beneficial, as long as the acquirers have well-articulated, specific value creation ideas going into each deal. Some of them might be to improve the performance of the target company, consolidate to remove excess capacity from an industry, acquire skills or technologies cheaper and faster than they could be created organically, or pick winners early and help them develop their business (Koller et al., 2010).

Another question that can be further made is if investment banks add value to the M&A process. Fees paid are usually very high and represent a significant part of the costs of acquiring a business, so it makes sense to wonder how much value do investment banks do really add to the transaction. There is no definite answer, but Bao and Edmans (2011) document in their research a significant investment bank fixed effect in the announcement returns of an M&A deal. Their findings suggest that “investment banks matter for M&A outcomes, and contrast earlier studies which show no positive link between various measures of advisor quality and M&A returns. Differences in average returns across banks are also persistent over time and predictable from prior performance. (p.1)”

Overall, recent literature shows that M&A create value as a whole, but many times only for the target company. The acquirer’s shareholders, due to the high premium paid, often lose value in an acquisition, especially if there are no specific value creation ideas. It is very important to know how these ideas will be put in action, and there is a lot of literature that gives companies guidelines and best practices on how to close a successful and value creating acquisition. Research also shows that financial advisors play an important role in a transaction, and that its participation matters for M&A outcome. There is already some literature on the M&A process from the investment bank perspective, but there is definitely room to grow, and in this paper further insights will be given on the financial advisor’s role and practices.

3. Methodology

Mergers and Acquisitions in Investment Banking

Mergers and acquisitions are a major event for all parties involved, from the seller to the buyer, and all their stakeholders. It is a time-consuming, intensive process with high stakes, usually taking several months. As a result, advisors play a very important role in transactions. In that sense, and due to the nature of the transactions, clients need to be advised in both financial and legal streams – lawyer’s offices and investment banks.

Investment bankers are financial and transactional experts who advise corporate clients on transactions such as debt offerings, equity offering, IPOs, acquisitions, divestitures and mergers. In M&A advisory they tend to be advocates for the deal, as the industry works typically with a retainer in the beginning of the transaction – to cover headcount costs – plus a success fee, which is commonly percentage of the deal value. This results in a huge incentive to press for the conclusion of the deal and maximize/minimize (depending on which side you are) its value. On the other hand, these professionals seek to maintain a long-term relationship with their clients, so they will be hesitant to press for an unattractive deal.

Investment bankers try to actually stimulate the decision of making a deal, so a significant part of the time is spent “pitching” client companies on potential transactions. According to Frankel and Forman (2017), the main purpose of the pitch is to encourage a specific transaction in the hope that the bank that bought the idea will be hired to help execute it. However, pitching companies is part of a broader effort to provide general value to the client, as the majority of the material is concerned with providing intelligence, industry insight, transaction ideas, and information on specific targets. All this is part of the constant effort that investment banks put into building and maintaining strong and long lasting relationships with their clients. In fact, client loyalty is essential to Mergers & Acquisitions: on one hand, the constant interactions create trust between the parts; and on the other hand, when the relationship is built, the client discloses not only confidential but sensible information about its activity.

During the actual process, investment bankers have a role in identifying potential targets, brokering initial conversations between parties, conducting valuation, financial structuring, organising financing options, and managing the sale process. They are often also industry experts who have insight into the trends of the sector and among competitors.

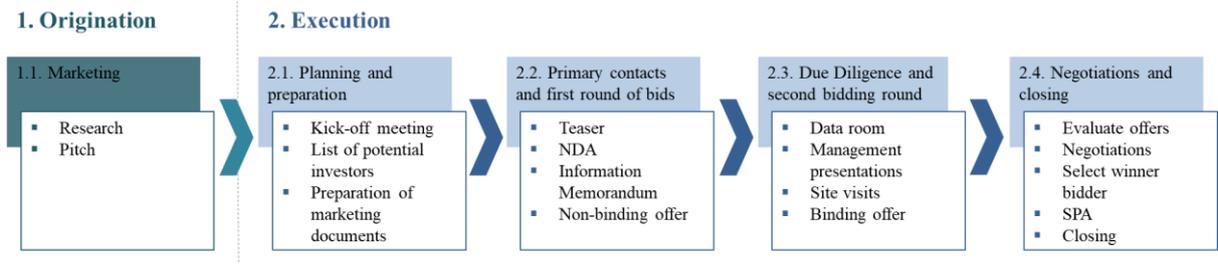
M&A teams have a complex and hierarchical structure, with several roles that vary with seniority. Typical roles include managing directors, directors, vice presidents, associates, analysts and, in some cases, interns.

Starting from the most junior positions, interns and analysts are primarily concerned with basic financial research and the mechanics of building financial models. They are usually out of the university or have very little professional experience. Due to the responsibility and sharpness that the industry requires, more and more investment banks do not hire Analysts without an internship in the area – this reduces the risks of hiring and the certainty that that recruitment is a top talent. Associates are next in terms of seniority, and they are concerned with the drafting of pitch material, more complex financial modelling and management of basic processes. Professionals in these roles have little to none contact with clients, and are commonly responsible for executing pitch ideas of more senior investment bankers. Senior Associates start to have contact to clients and sometimes are pushed into the VPs tasks. Vice presidents manage live deals, develop pitch ideas and are sometimes responsible for pitching clients. Directors focus on pitching clients: they are the main contact point for small and mid-sized clients, and only manage deals at a high-level. The most senior role is the one of the managing directors, whose time is almost entirely dedicated to pitching clients and maintaining client relationships. They are also responsible for managing very-high-level deals.

Mergers and Acquisitions process

In the next section I will go through the M&A process and detail what are the tasks of the financial advisor in all the phases. The process is usually divided in two moments: origination and execution. Consequently, there will be two distinct teams, responsible for each phase, but working with each other. I will give the example of a sell-side and a buy-side mandate.

Sell-side process



1. Origination

Origination teams are typically organized in Industry groups, which consist on professionals specialized in a certain industry and that follow its main players and trends. These teams keep up with everything that happens in a sector and have extensive knowledge about its development. Most of the work that the teams engaged in the origination of deals do is exploratory as their job is to try to provoke some action in the market. These professionals advice their clients on what would be best for them and on possible transaction opportunities.

The main deliverable in this phase is the pitch, which is a marketing presentation with the purpose of securing a mandate. It typically starts with a bank overview making an argument for the capabilities and ‘résumé’ of the investment bank. It includes a market overview, company positioning, some valuation marks and presentation of possible opportunities.

When a mandate is secured, the deal goes into the execution’s team responsibility. However, industry experts may continue to assist in certain aspects of the transaction.

2. Execution

2.1. Planning and Preparation

The primary phase of any mandate is to organize and prepare the transaction. The first step is the **kick-off meeting**, where the financial advisor meets with the board and management of the company for sale. In this meeting, seller objectives are identified and a timeline for the process is defined, including dates of significant steps such as receiving of initial and final bids, contract signing and closing. It is important that this timetable is well-defined and of the knowledge of all the parties involved.

The financial advisor has to have a comprehensive understanding of the business, and this is achieved by having an extensive session with the management team and by performing advisor due diligence. The advisor should understand management’s financial projections and assumptions, and should perform a preliminary valuation analysis, in order to establish a valuation range benchmark that will be used to evaluate buyers’ offers.

It is then important to define the buyer universe. An extensive and detailed **list of potential investors** is compiled, some of which searched by the advisor and others indicated by the company. When compiling this list a decision has to be made regarding the number of prospective buyers. The seller shouldn’t approach only one or two investors, as it may not create the necessary leverage, and there is no way to be sure *at priori* that they will be interested in

paying an interesting price. On the other way, this list shouldn't be too wide because it is more difficult to manage and a lot of confidential information about the target is disseminated. When the list is complete, some information is gathered for each investor, including a company description, the main financials and key people to be contacted.

Another crucial step of the organisation phase is the preparation of marketing documents, namely the *Teaser* and the *Information Memorandum*. Firstly, the **teaser** is assembled, with the purpose of presenting the company and rising interest from potential buyers. It is a brief presentation, and it contains key investment highlights, a market overview, company description and financial data. For confidentiality reasons, the teaser is a summary and general material by nature. Some companies might not even want the market to know that they are for sale, so the teaser can also be constructed as a blind profile. In this case, the name of the company is omitted, as well as some key information that might lead to its identification.

For a more detailed description of the company, the advisor builds the *information memorandum*. This is an extensive dossier to the investors, usually around 100 pages long, that gives an in-depth overview of the company and includes a strong sales pitch. Its content includes a market trend analysis, a corporate overview (history, strategy, products, operations, etc.), competitive analysis, and financial information. The financial section should be detailed and include both historical values and business plan estimates. The sell-side advisor helps to develop projections and supporting assumptions, which will be target of scrutiny. This data forms the basis for the valuation analysis performed by the buyer, so it is essential that all the values are accurate, realistic and can be justified. The information memorandum will only be given to buyers who express serious interest on the transaction.

The management team's input is extremely important in the preparation of these documents, as they are the ones who have an extensive knowledge of the company. Substantial time and resources are spent in order to guarantee that the documents are accurate and comprehensive. Both the teaser and the information memorandum vary in terms of format and content, depending on target, sector or specific circumstances. Once the documents are closed, it is time to start the **marketing of the sale**.

2.2. Primary contacts and first round of bids

A triage of the initial bidders list is made to evaluate if they would be in fact interesting buyers. The resulting list can vary in length, depending on the sector and company for sale.

According to Rosenbaum and Pearl (2009), there is a broad range of criteria to have in consideration when evaluating the buyer, namely its likelihood and ability to acquire the target at an acceptable value. For strategic buyers, strategic fit is an important criteria, including potential synergies. Financial capacity is also important, measured by balance sheet robustness, access to financing and risk appetite. Other factors are M&A track record, cultural fit, market position, and integration plans. When evaluating financial investors, key criteria include sector expertise, investment strategy, fund size, track record, ability to obtain financing and fund life cycle.

After selecting the potential buyers, the advisory team contacts and presents the teaser to every one of them. The ones who are interested in the deal then have to sign a **Non-Disclosing Agreement**. Also referred to as a confidentiality agreement, it is a legally binding contract between the target and prospective buyers that governs the sharing of confidential company information. It basically says that the recipient of the information won't use it for any purpose other than evaluate the target as a possible acquisition. It is drafted by the target's counsel and distributed to potential buyers, and its signing is a condition to the receipt of more detailed information.

After the execution of the agreement, the sell-side advisor distributes the *information memorandum* and the **process letter**. This letter states all the phases of the process, including dates of submission for the non-binding and binding offers and its conditions. Potential buyers are then given several weeks (2-3) to review the information memorandum and to analyse all information before submitting a non-binding offer. This usually mentions an EBITDA ratio rather than an absolute value.

2.3. Due diligence and second bidding round

The financial advisor receives the initial bids and analyses them thoroughly, accessing purchase price and key conditions. The advisor should be able to understand if a bid is real, or if the offered purchase price will decrease in the binding offer. It should also pay attention to those bidders who are just trying to have access to confidential information and have no real intent in pursuing the transaction. The sell-side team then works alongside the company's managers in order to rank and select the potential investors that are going to continue in the process. This is usually a small list, comprising only those investors who are really interested and have a good chance of completing the transaction.

Before the second round of bids, potential buyers conduct comprehensive due diligence and analyse in detail all the possible information regarding the business. This is an opportunity to dig deeper into the business, financial statements and projections. Sell-side advisory team plays a central role in this process, as they coordinate management presentations and facility site visits, monitor the data room and maintain regular dialogue with prospective buyers.

Firstly, prospective buyers are given access to the **data room** (nowadays, Virtual Data Room). This is a platform that has been prepared since the early stages of the process and that contains absolutely all the information regarding the company. This includes financial data, operational and strategic information, legal documents, and tax related info. It is typically online and is designed to provide a comprehensive set of information relevant for buyers to make an informed investment decision about the target. A well-organized data room facilitates buyer due diligence, helps keeping the process on schedule and inspires confidence in bidders. The data room is opened and there is a Q&A in which the investors can clarify whatever questions they have. During this process, the financial advisor helps the company answering all the questions, facilitating an orderly and timely response, and protecting some aspects that shouldn't be disclosed.

Management presentations also take place in this phase, so that the investors get to know the management team and more detailed information on their possible investment. The sell-side advisor prepares the materials, with significant inputs from the management team to determine the speaker line-up for the presentation, as well as key messages and response to likely questions. The presenting team usually consists on the target's CEO, CFO and key division heads, who present a detailed company overview to each potential buyer. The presentation is often the first meeting between buyers and the target's management, presenting a unique opportunity to gain a deeper understanding of the company from the ones who know it best. This consists on an exhaustive discussion of topics ranging from business, industry and financial information to competitive positioning, synergies, growth opportunities and financial projections.

Another important part of buyer due diligence are **site visits**. It provides the buyer with a first view of the target's operations, and it usually involves a guided tour of a key target facility, such as a manufacturing plant, distribution centre or sales office. It is highly interactive as buyer representatives and consultants enjoy the opportunity to ask detailed questions.

After the long and detailed process of due diligence, the interested investors have to submit a **binding offer**. This creates a definite legal obligation upon the bidder to acquire the target in accordance with the terms and conditions. It is the banker’s responsibility to make it look like there is significant interest among multiple parties and try to play them off against each other in order to increase price.

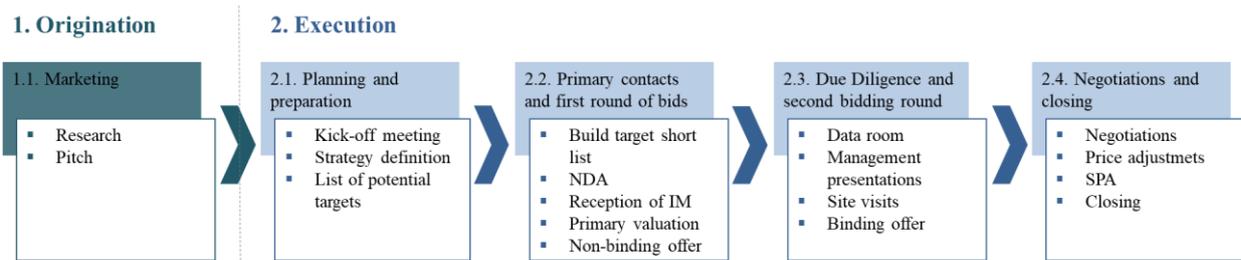
2.4. Negotiations and Closing

The sell-side advisor works with the target management team to conduct a thorough analysis of the price, structure and conditionality of the final bids. The seller then selects a preferred party with whom to negotiate a definite agreement. Any remaining diligence items should be clarified, and key terms of the contract should be confirmed, including the price.

After this, the legal advisors prepare all the documents and the Sales and Purchases Agreement (SPA) is signed. This is a legally binding contract between a buyer and a seller detailing the terms and conditions of the sale transaction.

Before the actual deal closing, there are some approvals that need to be obtained, namely regulatory and shareholders’ approvals, in what can be a relatively long process. An important regulatory approval is from the anti-trust authorities, which prevent companies from gaining too much market share in a given market, and creating potential monopoly effects. Finally, the deal is closed and the ownership of the company is transferred.

Buy-side process



I will now present the process of a buy-side mandate, which will be complementary to the sell side. Many concepts and steps of the process were already explained, so this section will be more succinct.

1. Origination

In the origination phase, the main goal of the buy-side team is to encourage deals, mainly by proposing targets to the client. The advisory team often builds several company profiles that

will be presented to the buyer company in order to trigger a transaction. This profiles often include a company description, main financials, recent M&A activity, and key people. There can also be the case in which the client has some idea of what it wants to acquire (in a certain industry or geography) and the advisor should look for companies that meet the criteria.

2. Execution

2.1. Planning and Preparation

There is a first phase of identification and approach and, as in the sell-side, the process usually starts with a kick-off meeting. In this, the advisory team works along the buyer to figure out exactly what are its goals and how can they be achieved.

It is important that buyer motivation is well-defined and that the advisor fully understands it. The decision of acquiring a company or a business is driven by numerous factors, namely the desire to grow, improve or expand existing capabilities. It is usually a much faster, cheaper and less risky way of growing than by doing so organically. Acquirers often seek value creation opportunities from combining business and creating synergies, such as cost savings and enhanced growth initiatives.

It is also imperative to outline that the acquisition strategy, which can be horizontal or vertical integration, or even conglomeration. Once the buyer motivation and acquisition strategy are defined, the financial advisor has in mind a target industry, or even a specific company, that will be the starting point for the research for potential targets. A detailed investigation takes place, and the buy-side advisor tries to understand the strategic fit of the prospective targets.

2.2. Primary contacts and first round of bids

There is a first contact with the potential targets in order to find out if they have interest in the deal. Based on the output of this contacts a target short list is assembled. The length of that list will depend on the buyer's strategy, but it can consist on only one target.

On a next phase, the financial advisor is going to work alongside its client to evaluate the targets. First of all, the buyer has to sign a NDA so that the target provides some information about its business, namely the information memorandum.

Based on this data, the financial advisor does an organizational and financial characterization of the company, and in collaboration with the buyer's management team, builds a business plan and performs a valuation of the company. This is done from the estimates of the target, and it is important to have in mind that the information provided might not be absolutely complete

and it is only a preliminary valuation. Several methodologies are used in order to achieve the most accurate value for the company, namely comparable companies multiples, transaction multiples and discounted cash flows. With this valuation an initial price is achieved and a non-binding offer is submitted.

The **non-binding offer** should include an indicative purchase price (or price range) and the key assumptions made to achieve it. It should also state the purpose and structure of the transaction, an explanation of the payment terms, information on financing sources, key conditions for signing and closing, timing for negotiations and due diligence, among others.

2.3. Due diligence and second bidding round

Afterwards, the due diligence process takes place. This includes attending management presentations, site visits and analysis of the data room. The buy-side due diligence team includes consultants, investment bankers and lawyers, who work together to analyse all the information regarding the target company. It scrutinizes all the financial, tax, operational and legal aspects of the business, and makes comprehensive questions to the sell-side team. The DD team typically issues reports where it indicates red flags and analyses potential deal breakers. It is the financial advisor's responsibility to coordinate and oversee the entire process.

When all the information is gathered, adjustments to the business plan and valuation need to be made, and the final price offer will often change. The buyer then submits the binding offer that should include the exact amount of the purchase price, evidence of committed financing, confirmation of due diligence completion, required regulatory approvals and timeline for completion, among others. Usually the prices in this phase are adjusted down from the non-binding offer.

2.4. Negotiations and Closing

As explained in the sell-side approach, negotiations to the binding offer are made. After all the negotiations, and if the deal is successful, buyer and target sign the Sales and Purchase Agreement. Both negotiations and contract signing are overseen and assisted by the financial advisor. Again, approvals need to be obtained, and finally the deal is closed.

In a buy-side mandate there is a smaller likelihood of completing the deal, as there are usually several buyers interested in acquiring a certain target. However, these transactions are often more profitable for the investment bank if completed.

Valuation

Valuation is the base for defining the price of a company, which is a determinant factor for the success of a transaction. According to Reed, Lajoux, and Nevold (2007), “no factor counts more than price in closing a transaction, yet very few operating executives know the worth of their own company, much less anyone else’s.” Valuation may be done by the seller prior to entertaining prospective buyers, by a buyer who identifies a specific target, or by all parties during negotiations to resolve a dispute over price. Investment bankers, in their role as financial advisors, perform valuations both for the buy-side and the sell-side.

A sell-side assignment requires the deal team to perform a comprehensive valuation of the target. This analysis is used to frame the seller’s price expectations, select the final buyer list, set guidelines for the range of acceptable bids, evaluate offers received, and ultimately guide negotiations of the final purchase price. (Rosenbaum and Pearl, 2009)

On buy-side assignments, valuation of the target is at the core of the financial advisor’s analytical work. It is important to understand seller’s assumptions and previsions for the future, in order to accurately translate them into a fair price offer. In this kind of assignment, advisors typically also perform a merger consequences analysis, which consists on exploring the impact of a certain transaction on the acquirer.

Valuation is indeed an essential part of the M&A process, but how is it done? The intrinsic value of a business is the present value of all future cash flows generated. In practice, this is very difficult to calculate and both companies and advisors take a more practical approach. Common valuation methodologies include comparable multiples, precedent transactions multiples and discounted cash flows. A combination of the 3 will give us a realistic and approximated value to the company. There are many more valuation methods, but these are the ones I will focus on.

4. Data and empirical results – Valuation

In this section I will give a practical example and use these three methods to value a company that was recently acquired. As it is an academic example and not an in-depth equity research, it will be somehow simplified compared to reality.

In July 2017, Michael Kors announced the acquisition of Jimmy Choo, a UK-based and listed manufacturer of luxury accessories. In the valuation of Jimmy Choo I will use some tools and

approaches that are used by BNP Paribas and that I learned during my internship. However, all the information used is public, and I was in no way involved in the transaction.

Company profile

The first step in performing a valuation is to get to know the company in depth, understanding its business and the market it operates on. Jimmy Choo operates globally in the luxury goods sector, and it has a strong position in the market of luxury shoes, its core product. The company's product range also includes sunglasses, eyewear, fragrance and soft accessories. Jimmy Choo is led by Pierre Denis as CEO, and the design is at the responsibility of the Creative Director Sandra Choi. It has a successful and balanced distribution network, with Directly Owned Stores at its core, providing an expansion opportunity. In 2016 the company achieved £364m in revenues (breakdown in appendix 1), and had 1278 employees.

Comparable companies multiples

Trading multiples analysis is based on the assumption that the market values financial assets efficiently and that the difference in value between two assets is linked to various performance or accounting indicators. So, a company that presents higher profits or EBITDA should trade at a higher level than one with lower results. In this method, similar companies are benchmarked against each other based on key financial statistics and ratios in order to extrapolate a valuation range for the target. It is based on market conditions and sentiment, which can be more valuable than intrinsic valuation.

The first step in this methodology is to select the universe of comparable companies. These are companies within the same sector that share business and financial characteristics, performance drivers and risks. In order to find Jimmy Choo's peers, I started from a universe of 100 top luxury goods companies¹ and selected all the ones that are listed and sell similar products to the company being valued, such as shoes, bags or accessories. I also had in consideration the geographies they operate in, and chose just the ones that are based in Europe or North America and operate globally, compiling the list on appendix 2.

For each of the peers, a financial analysis was made in order to calculate certain multiples' projections. The first step is to calculate Equity Value, which is the share price times the number of outstanding shares. Secondly, one should compute the Enterprise Value, which is the sum of all ownership interests in a company and claims on its assets from both equity and debt holders. The Enterprise Value is calculated by adding to the market capitalization all debt and debt-like

¹ In report "Global Powers of Luxury Goods 2017" by Deloitte

items (such as provisions and unfunded pension liabilities), as well as convertible debt, preferred stock, and minority interests. Cash and cash equivalents (such as investments in associates) should be deducted.

In order to calculate the multiples certain captions from the financial statements are needed. Major items from the income statement, balance sheet and cash flow statement were put together using historical data from Factset. The main items from the income statement used in multiples are Sales, EBITDA, EBIT and Net Income. Other essential captions are Net Debt, Shareholder's equity, Capex, Free Cash Flow and Dividend per share. Once the historical information is known, one has to project all these items for the future. Estimates from broker notes were used to build projections for the next 3 years. Please refer to appendix 3 to find an example for Tapestry, Inc.

As the companies in analysis are in different countries, they disclose their financials and are listed under specific currencies. In order for the outputs to be comparable, they should all be in the same currency, so all the values in the financial analysis were converted to Euros. Also to allow for comparison, the financial statements should all reflect the same period. The companies in analysis report their financial information at different dates, so the information was adjusted in order to reflect the fiscal period.

Using this information, I computed the multiples that will be used in the valuation. With all the financial information collected, one last selection of the true relevant peers of Jimmy Choo was performed. I compared financial ratios, EBITDA margin, revenues growth and multiples results and excluded the companies that were clear outliers. The results are compiled on the table below, where relevant multiples for the year of 2017 are displayed. I also computed multiples for 2018 and 2019, but they yield similar results, so one year should be enough to take conclusions on the valuation while making the analysis simpler.

Table 1 - Trading Multiples Output

Company	Ticker	Equity Value	Enterprise Value	EV/ Sales	EV/ EBITDA	EV/ EBIT	P/E	P/B	Dividend yield	FCF yield
				2017	2017	2017	2017	2017	2017	
Tapestry Inc	TPR-US	11 729	11 376	2,5x	11,5x	14,4x	20,7x	4,3x	2,9%	4,6%
Burberry Group	BRBY-GB	8 310	7 408	2,3x	10,7x	14,2x	23,3x	4,6x	2,4%	6,3%
LVMH Moët Hennessy	MC-FR	112 715	134 978	3,2x	13,2x	16,4x	22,9x	3,9x	2,1%	3,7%
Kering	KER-FR	38 385	43 643	2,9x	13,2x	15,5x	19,8x	3,0x	2,0%	4,2%
Cie Financiere Richemont	CFR-CH	37 555	30 531	2,7x	11,6x	14,8x	22,6x	2,3x	2,6%	4,3%
Tiffany	TIF-US	10 210	10 544	2,2x	9,2x	11,7x	18,2x	2,8x	2,6%	5,5%
Tod's	TOD-IT	1 861	1 914	2,0x	11,7x	16,9x	24,3x	1,7x	2,6%	4,9%
Salvatore Ferragamo	SFER-IT	4 013	4 026	2,8x	14,7x	19,4x	26,0x	4,9x	1,9%	3,9%
Prada	1913-HK	8 034	8 045	2,6x	13,4x	21,5x	30,7x	2,6x	3,4%	3,7%
PVH Corp	PVH-US	7 860	10 035	1,3x	9,2x	6,6x	13,5x	1,5x	0,1%	6,8%
Michael Kors	KORS-US	4 859	4 778	1,2x	5,4x	12,4x	9,3x	3,1x	0,0%	13,2%
Hugo Boss	BOSS-DE	4 323	4 460	1,6x	8,9x	7,0x	17,6x	4,6x	4,4%	6,0%
Ted Baker	TED-GB	1 204	1 336	2,0x	12,2x	6,1x	19,1x	4,7x	2,5%	2,5%
Mean				2,3x	11,2x	13,6x	20,6x	3,4x	2,3%	5,4%
Median				2,3x	11,6x	14,4x	20,7x	3,1x	2,5%	4,6%
High				3,2x	14,7x	21,5x	30,7x	4,9x	4,4%	13,2%
Low				1,2x	5,4x	6,1x	9,3x	1,5x	0,0%	2,5%

Precedent transaction multiples

Precedent transaction analysis employs a multiples-based approach to derive an implied valuation range for a given target. It is premised on multiples paid for similar transactions in the same sector. Comparable acquisitions are deals that have occurred in the same business segment for similar purposes (acquiring a minority or a controlling stake), for companies that are similar to the target on a fundamental level. Generally, the most recent transactions are the most relevant as they took place under similar market conditions. Transaction comps tend to provide a higher multiple than trading comps, because they include in the purchase price a control premium that accounts, among other things, for synergies expected from a strategic investor.

Similarly to the previous method, the first step is to identify comparable transactions that can be used to benchmark a valuation range for Jimmy Choo. I started by searching for transactions in the luxury goods sector, mainly using Mergermarket and press. Transactions over the last 5 years involving companies that offer similar products to Jimmy Choo's (shoes, accessories, bags, apparel and fashion) were then selected.

For each transaction, information about the percentage acquired and the consideration paid were collected in order to compute the Enterprise Value and Equity Value. The difference between these is the Net Debt, information that was gathered from the financial statements of each of the target companies. In these comparable transactions, some companies are relatively small and/or not listed, so they don't disclose financial reports. In this case, information from the press or estimations from Mergermarket were used. In order to compute the multiples, one has to get information on Sales, EBITDA, EBIT and Net Income of the last available twelve months

report before the transaction. For comparison, all the values were converted into euros, using the exchange rate as of the announcement date for the EV and Equity Value and the year-average for the income statement items. All this intelligence was the used to compute the multiples, compiled in the table below. Please refer to appendix 4 for an example of the methodology on the acquisition of Kate Spade by Tapestry Inc.

Table 2 - Transaction multiples output

Date	Target	Country	Acquirer	% acquired	Equity Value	Enterprise Value	EBITDA margin	EV / Sales	EV/ EBITDA	EV/ EBIT	P / E
23/05/2017	Christian Dior Couture	France	LVMH - Moet Hennessy Louis-Vuitton	100%	6000	6500	-	3,2x	15,4x	25,8x	59,4x
08/05/2017	Kate Spade & Company	US	Tapestry Inc	100%	2379	2349	16%	1,7x	10,7x	13,8x	16,8x
25/04/2017	Christian Dior SA	France	Bernard Arnault	26%	46 580	51 903	24%	1,3x	5,5x	7,3x	10,1x
22/06/2016	Balmain SA	France	Mayhoola for Investments S.P.C	100%	-	485	-	4,0x	-	-	-
21/06/2016	Corneliani	Italy	Investcorp	55%	-	88	-	0,8x	-	-	-
01/04/2016	SMCP	France	Shandong Ruyi Technology Group	80%	985	1300	16%	1,9x	12,2x	19,0x	-
14/12/2015	Kurt Geiger	UK	Cinven Partners	100%	329	336	8%	1,1x	13,9x	24,2x	25,8x
06/01/2015	Stuart Weitzman	US	Coach, Inc	100%	-	431	-	1,9x	-	-	-
30/04/2015	Roberto Cavalli SpA	Italy	Varenne	100%	290	390	7%	1,9x	26,4x	-	-
09/02/2015	Hugo BOSS AG	Germany	Zignago Holdings SpA	7%	7 183	7 226	22%	2,8x	12,6x	16,1x	16,0x
17/12/2014	Hermes International	France	LVMH's shareholders	23%	29 229	28 299	36%	7,3x	20,3x	22,5x	35,3x
27/02/2014	Gianni Versace	Italy	Blackstone Group	20%	-	1 050	15%	2,2x	15,0x	36,7x	-
20/12/2013	Nine West Holdings	USA	Sycamore Partners	100%	875	1594	4%	0,7x	17,0x	37,5x	-
08/07/2013	Loro Piana Spa	Italy	LVMH	80%	2 500	2 700	20%	4,3x	21,4x	-	-
20/04/2013	Via Delle Perle	Italy	Argos Soditic	75%	35	33	12%	0,9x	7,0x	7,0x	12,0x
16/11/2012	Cole Haan	US	Apax Partners	100%	447	448	-	1,1x	-	-	-
Average								2,3x	14,8x	21,0x	25,1x
Median								1,9x	14,4x	20,8x	16,8x
High								7,3x	26,4x	37,5x	59,4x
Low								0,7x	5,5x	7,0x	10,1x

Discounted cash flows

The DCF is an intrinsic valuation method with the underlying principle that the value of an asset depends on its ability to generate positive cash flows in the future. Due to the fact that it highly relies upon assumptions about the future of operations, a deep understanding of the business is essential to perform a DCF analysis. In a real-life deal, the investment banking team would have direct contact with the company and its managers, and would have access to all the information needed to execute an informed and detailed valuation. In this paper I don't aim to perform an equity research or an in-depth valuation, the goal is simply to give an overall explanation and example how it is done in an M&A context. In addition, I don't have access to detailed information that would allow to fully understand Jimmy Choo's fundamentals, as I would have in a real-life case. As so, the following will be a simplistic approach that does not reflect the DCF methodology used in a real transaction, and it will mainly based on information from broker notes.

The first step was to gather recent broker notes, and I collected information on the forecasts of the main financial captions from equity reports from HSBC, RBC Capital Markets, Barclays and Liberum.

In the forecast in appendix 5, the values for Revenues, EBITDA and EBIT of the next three years (2017-2019) came directly from the broker notes. After that, I assumed that revenues' growth will tend towards the markets'. According to Euromonitor International², the luxury goods market will stabilize at a 3% growth rate year-on-year, at least until 2021. As so, Jimmy Choo's growth of each year will gradually decline towards 3%. For the remaining captions (gross profit, SG&A expenses, EBITDA and EBIT), margins were calculated and it was possible to conclude that they have been relatively constant in the past. I then assumed that they will continue to be constant and computed margins as the average of the previous three years. Depreciations and amortizations were calculated as the difference between EBITDA and EBIT.

Regarding the forecast of the balance sheet (in appendix 6), intangible assets were assumed to remain constant for the future, based on broker notes estimates. PPE was calculated as a % of sales, which has been constant at around 16% in the past years. It was forecasted to remain at the same levels, and computed for each year as an average of the previous three years. Working Capital captions were computed in days of COGS or sales and assumed to remain constant (average of last three years). I concluded that Jimmy Choo takes on average 50 days to receive from clients and 300 days to pay to suppliers. Inventories are kept for around 200 days and cash only for 15 days. About the financial debt, I assumed it is used to finance investments in PPE and that it will grow at the same pace as this item. Other assets and other long term liabilities were assumed to remain constant over future years.

Table 3 - Free Cash Flow forecast

£m - FY 31/12	2016	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e	2025e
EBIT	39	46	51	57	58	61	64	67	69	71
Taxes	5	6	7	7	7	8	8	9	9	9
NOPLAT	44	52	58	64	66	69	72	75	78	80
Depreciation	20	22	25	28	29	30	32	33	34	35
Gross Free Cash Flow	64	75	83	92	94	99	104	108	112	115
Net Capex	-29	-34	-36	-37	-40	-43	-44	-46	-48	-49
Change in WC	8	-3	3	2	1	2	1	1	1	1
Operating Free Cash Flow	43	38	50	57	54	59	61	63	65	67
Change in other LT assets	17	8	4	5	5	4	4	4	3	3
Change in other LT liabilities	-1	1	1	-1	0	0	0	0	0	0
Total Free Cash Flow	60	47	55	61	59	63	64	66	68	70

After forecasting the financial statements, its captions are used to calculate the Free Cash Flow. Capex for the first three years was forecasted using broker notes, it was calculated as a percentage of sales and assumed to remain constant at around 8.2% in the future. All other captions were taken directly from balance sheet and income statement forecasts.

² in market report "Global Luxury Goods Overview", March 2017, by Euromonitor International

The last step is to discount the Free Cash Flows at an appropriate discount rate. In order to do so, the Weighted Average Cost of Capital should be estimated, reflecting the expected return for equity and debtholders of the company. To calculate the WACC, I estimated the risk-free asset, risk premium and company beta (to compute the cost of equity), as well as the cost of debt.

As a proxy for the risk-free asset, the yield of a 10-year UK government bond was used, which is 1.26%. I considered the risk premium to be the difference between the annualized market return of the S&P 500 Index and the 10-year UK Gilt, corresponding to a market risk premium of 6.97%. To estimate the beta of the cost of equity I started by collecting the raw beta of its peers³ and un-levering them using the respective net debt to equity ratios at market values. I then computed a median, which was later re-levered at Jimmy Choo's debt-to-equity ratio of 16%, achieving an equity beta of 1.12. Using these values, CAPM was applied to get to a cost of equity of 9.8%. Regarding the cost of debt, the interest expense on bank loans was divided by the average total of borrowings of each period, achieving an average cost of debt of 3.8% in the last three years. Assuming that the company is at its target capital structure and that this will remain constant, I calculated the weight of debt and equity at market values (using the share price at the date prior to the acquisition announcement) and computed a WACC of 8.9%.

A big part of the future cash flows of the business will be on the terminal value, which will highly depend on the terminal growth rate. I assumed that in perpetuity Jimmy Choo will grow with the economy, so I computed a weighted average of the GDP growth⁴ on the regions it operates (considering the weight each region has on revenue), and achieved a terminal growth rate of 2.2%.

The sum of all discounted cash flows will then be £868m. As this value vastly depends on assumptions made on the estimation of the WACC and the growth rate, a sensitivity analysis was performed, which can be found on appendix 7.

“Football field”

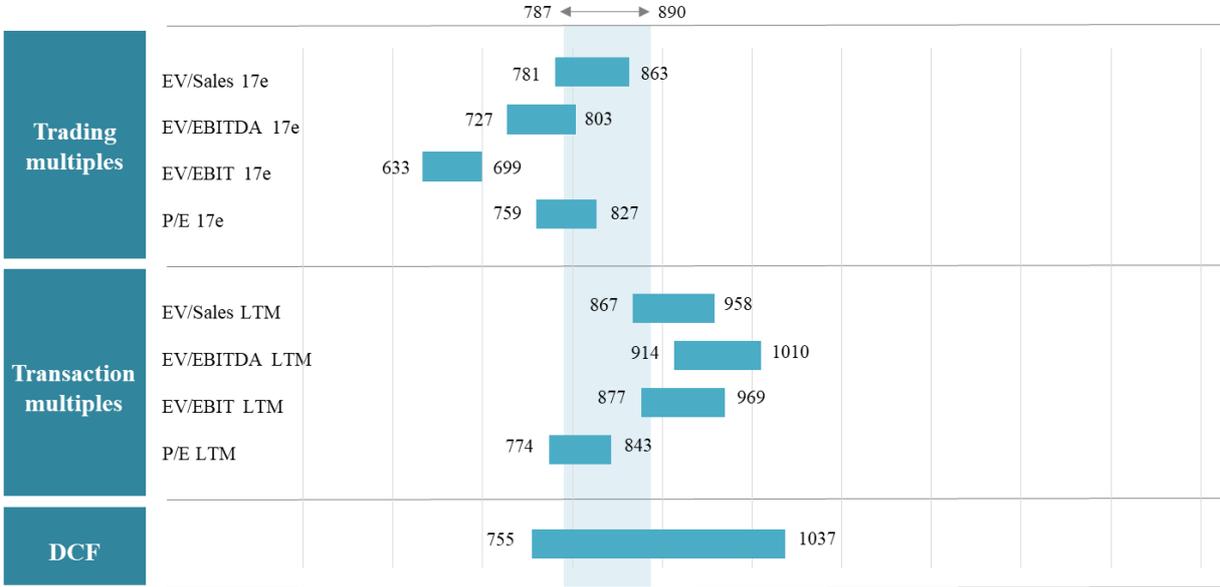
As there is much subjectivity in all of the valuation methodologies, value is usually expressed as range. There are numerous acceptable valuation methods, and in most situations, each will yield a different result. It is important to realize that it is not an exact science, and valuation alone typically won't drive the terms and pricing of the transaction. The actual price will be ultimately determined by what companies are actually willing to pay, which will be a function

³ Using Barra Global Equity Model (GEM3)

⁴ Data from International Monetary Fund

of both economic formulas and market conditions. A common way to present the results of the different methods is to organize them into a football field.

Table 4 - Football field valuation Jimmy Choo



As seen above, the results will largely differ between valuation methodologies, but an average range is possible to infer. According to this valuation, the enterprise value will be between £787m and £890m. In a real-live deal, this valuation elaborated by the investment bank would be brought into the discussion table, and the values compared to those of the client. The discussed valuation range would then be used in negotiations in order to achieve a final price. It is important to mention that synergies between the acquirer and the target should also have to be taken into account, which hasn't been done in this example and would likely improve the bid value.

In fact, Michael Kors has acquired Jimmy Choo for an enterprise value of £890m, which is in line with the results of the valuation performed in this paper.

5. Personal experience – internship at BNP Paribas

This report aims to explain the M&A process from the perspective of an investment bank, on the context of an internship I am currently doing with the M&A team of BNP Paribas. In this section I'll elaborate on my personal experience, contribute to the overall process, and main challenges and learnings.

In the methodology section of this paper there was a detailed explanation of the process that leads to the close of a transaction. This involves many teams and people, and each one has its

own role and responsibilities. I mainly work with the origination teams, preparing pitches for potential clients. Common tasks include targets research, company profiles, and market analysis. It is also occurring to perform financial analysis and valuations, mostly valuations by multiples. Investment banking teams have databases with multiples valuation for different sectors, and it is usually the interns' responsibility to update them so that they are always reflecting the latest information from the market.

The internship has a duration of one year, and I've now been working in the M&A team for six months. BNP Paribas is a global bank, with strong synergies between different locations, and that is really present in the Corporate Finance teams. In Portugal, this team is mainly composed of interns. As there isn't much M&A activity in Portugal, we work directly with teams from other offices (London, Paris, etc.) for clients in diverse geographies, in Europe and around the world. We do most of our work remotely, and mainly contact with analysts (the most junior members), but also with associates and vice presidents. It is very interesting to have this direct contact with senior members, as there is much to be learnt from them. The internship is divided in two parts: during the first six months we are in a general pool, meaning that we work with different teams and in different sectors in short-duration projects or tasks. This gives us the opportunity to gain knowledge on a lot of industries and their players, while also working with different people and teams that have their own procedures. In the following six months, we are allocated to a specific sector and work always with the same people. In this period we gain a deeper knowledge on that sector and are really integrated on the team, being more involved in the projects. During my time at BNP Paribas so far, I have worked in several sectors, among them Consumer Goods, Financial Institutions, Industrials, Transportation, etc. and I will be integrated in a specific sector in the near future.

There is an environment of constant learning, as most of our training is done on-the-job by working with more senior members. We have regular appraisals and feedback on our performance, as well as clear objectives on how to improve and perform a better job.

There are also some challenges to this job, as it is very intensive and involves a lot of pressure due to the high stakes of the deals. M&A is a very intense area, with a heavy workload, even when compared to other areas in Investment Banking. Specifically in the internship, it is sometimes challenging to work remotely, either by phone or email, instead of being personally with the people we are working with. Although technology certainly helps, an extra effort is required to be completely involved in the projects and with the teams. I have also had to learn

how to work with very different people, with distinct approaches and methods. This is sometimes difficult but completely worth it, as I've learnt from all of them and became more flexible.

6. Conclusion

Mergers and acquisitions play an important role in the economy, as they can help to allocate resources efficiently and are a great way for companies to grow. According to Rosenbaum and Pearl (2009), "M&A is a catch-all phrase for the purchase, sale, and combination of companies, their subsidiaries and assets. M&A facilitates a company's ability to continuously grow, evolve, and re-focus in accordance with ever-changing market conditions, industry trends and shareholder demands. M&A advisory assignments are core to investment banking, traditionally representing a substantial portion of the firm's annual corporate finance revenues." As so, the study of the financial advisor's role in this process is of big relevance.

My experience in the internship has mainly consisted on working along origination teams. As explained, most of the work in this phase is exploratory and many times I am not working for a specific deal. The core of my job is to assist in the preparation of pitches, which aim to provide the client with relevant intelligence on the market and to present transaction opportunities. The importance of valuation in the process has been greatly underlined in this paper, however it is not common to perform in-depth valuations in the origination phase. The goal is to secure a mandate and motivate a transaction, so investment banks give clients only a preliminary valuation range. For this, the work performed is very similar to the example given in the report for the acquisition of Jimmy Choo. It is mainly based on market information, multiples are the core of the valuation, and DCF usually relies upon brokers' estimates.

The next phase of the M&A process is the execution, which is already related to a specific transaction. Tasks and responsibilities differ if working on a sell-side or buy-side mandate, but in both the financial advisor plays an important role in managing the entire process and going through all the steps previously explained in this paper. Firstly, there is the planning phase, where the strategy is outlined, a list of potential investors/ targets is put together, and documents are prepared. Next, the primary contacts take place, the teaser and information memorandum are distributed and non-binding offers are submitted. This is followed by the due diligence phase, which includes access to the data room, management presentations and site visits, and culminates with the binding offers. Finally, negotiations are made and the deal is closed. In the execution phase the valuation is much more comprehensive. Whether working on the sell-side

and having to value the client's business, or on the buy-side, where targets need to be valued, the analysis should be exhaustive, detailed and accurate. The main valuation method is discounted cash flows, and the advisor should really know the business and understand its fundamentals in order to make valid assumptions. Multiples are mainly used to cross-check results and compare the company with its peers and the market.

With this paper I attempt to take advantage of my experience to explain the role and organisation of M&A teams in investment banks. Personally, it was useful in the sense that it allowed me to have an overall understanding of the process of M&A. Working in such a big corporation with so many people, it is often difficult to understand exactly how do my tasks and responsibilities have implications to the overall deal. Writing this report definitely helped me to further comprehend my role within the M&A team of BNP Paribas, and to do a better job at it.

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