

LBO Case Study [WIP]

BabyBurgers LLC – A Completely Fictional Company

ASimpleModel.com

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INTRODUCTION

DISCLAIMER: All of the information contained in this exercise is entirely fictional. The company described is hypothetical. Any similarity between the business description and financial information provided and an actual company is purely coincidental. ASimpleModel.com does not provide investment, accounting or tax advice. Everything is intended for educational purposes only.

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SPECIAL THANKS TO FRIENDS THAT SUPPORT MY INTERNET TENDENCIES:

Mark Plunkett, Chief Investment Officer, Hilltop Opportunity Partners: Mr. Plunkett has reviewed countless documents published on ASimpleModel.com.

Adam Rodman, Founder, Segra Capital: Mr. Rodman came up with the concept for BabyBurgers LLC.

Yalun Tu, Goldman Sachs investment banker who gave it all up to be a successful writer in Los Angeles: Mr. Tu graciously edited the BabyBurgers CIM. It would be a lot funnier if I had accepted all of his edits. It would also be even less appropriate in an academic setting.

Jon Gattman, Founder, Cloverdale Capital: Mr. Gattman has long considered starting a blog called Ben Bersnacky and was polite enough to let me borrow the clever name for this narrative.

INSTRUCTIONS

LBO Case Study Instructions:

In this exercise you are to assume the role of an independent sponsor. You will be provided with the information and documents outlined below, and asked to build a financial model that can be used to communicate returns to your investors:

- a. Confidential Information Memorandum
- b. Financial Statements and Historical Financial Model
- c. Summary Term Sheet from the Subordinated Lender
- d. Summary Term Sheet from the Senior Lender
- e. Letter of Intent

You will need to incorporate information contained in the two term sheets for the debt schedules in your model. You will also need to include the management fee detailed in the Letter of Intent. Otherwise the information required to complete this case study is contained in the Excel file associated with this exercise.

This is *not* a guided exercise. No solution will be provided. If you forget any step of the process you can revisit the examples provided in the Leveraged Buyout Model video series.

Task: Use the information provided to build an LBO model of BabyBurgers LLC with a 5-year projection. As you will see when you download the Excel file referenced, you will need to develop all of your own assumptions.

The process of building a model without a template will expose areas of weakness in your skill set. I would encourage you to attempt this exercise without downloading templates available on ASimpleModel.com. I would even avoid cutting and pasting line items for the financial statements. Typing them will improve retention and cause you to think through the structure of the financial statements. It also provides an opportunity to display information in your own format, which becomes increasingly important as you look at opportunities in different industries.

Legal Documents:

For this exercise we are including some of the legal documents you would typically encounter working towards a Letter of Intent. It has been my observation that analysts are too frequently focused on the financial modeling exercise without realizing the significance of the legal documents that consummate the transaction. It is a critical process, and early exposure may help accelerate your career.

Confidentiality Agreement (“CA”): The investment bank representing the transaction will require that anyone interested in reviewing the opportunity execute a confidentiality agreement. This holds you responsible for the confidential information shared as part of the process.

Confidentiality Agreement with Non-Circumvent Language: As an independent sponsor you will also want to share the information you prepare with the sources of capital you intend to work with. For this purpose, you require a confidentiality agreement with non-circumvent language to prevent the parties you share information with from completing the transaction without you.

Indication of Interest (“IOI”) [Link to File]: This is typically a short document that states the valuation range at which you would be interested proceeding with the transaction described in the Teaser.

Letter of Intent (“LOI”) [Link to File]: A letter of intent is essentially an elaborate indication of interest. The valuation range previously provided will be reduced to the precise value at which you are interested, and you will be asked to include information about capital structure, employment agreements, non-compete agreements and high-level representations and warranties, among other things.

Subordinated Lender Term Sheet [Link to File]: A document summarizing the terms and conditions at which the subordinated lender is willing to finance the transaction.

Senior Lender Term Sheet [Link to File]: A document summarizing the terms and conditions at which the senior lender is willing to finance the transaction.

To mirror how this process typically unfolds, we have described the sequence as it would occur if you were in fact pursuing this transaction in real life. I have included the names used in this case study for the purposes of the explanation.

Sequence:

1. You receive a teaser (a one- or two-page document that anonymously describes the business) and a confidentiality agreement for Project Ben Bersnacky from Banker Brothers Investment Banking (“Banker Brothers”).
2. Once you have executed the confidentiality agreement and returned it to Banker Brothers, they will follow up with a copy of the confidential information memorandum (“CIM”) describing the target company. A CIM is typically a 25- to 50-page document that describes the business in detail. In this exercise we have reduced the CIM to two pages.

LEGAL DOCUMENTS

3. Using the information contained in the CIM, you then do some initial due diligence to determine the valuation range at which you are interested. If you decide to move forward with the process you will provide the investment bankers with an Indication of Interest (“IOI”) to communicate this range.
4. If the valuation range provided is appealing to the selling shareholders, you would then be asked to provide a Letter of Intent. Preparing a Letter of Intent requires substantially more work than an Indication of Interest (please see the description and example document available above).
5. At this stage you would reach out to potential lenders to determine their level of interest in financing this transaction. Lenders generally indicate their level interest and the terms on which they would like to participate in the transaction as a summary of terms or in a term sheet.
6. As part of this process you would also start communicating with your potential equity investors. You would likely develop your own CIM and financial model to communicate the returns you believe are achievable with the investment you are proposing.
7. The final step is to submit the completed letter of intent. If this document is executed, you will have an exclusivity period (typically somewhere in the range of 60 to 120 days) to consummate the transaction.

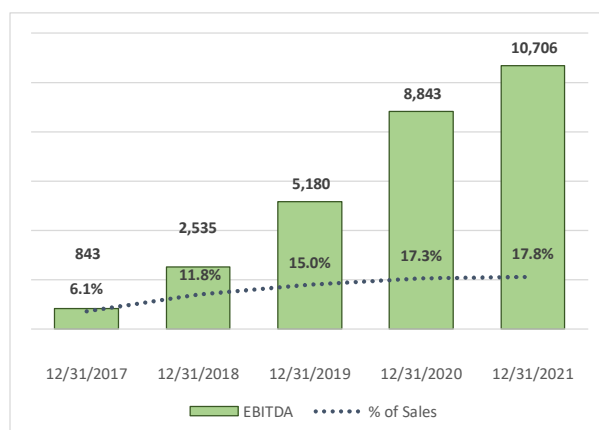
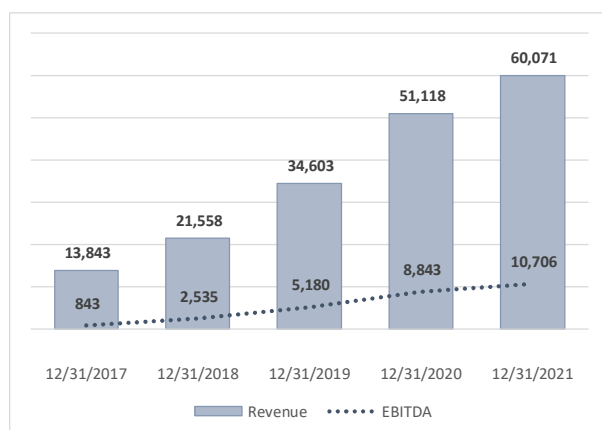
This case study is intended to focus you on the financial modeling exercise required to complete step 6 above, and provide the confidence required to submit a letter of intent.

Project Ben Bersnacky

Banker Brothers Investment Banking is pleased to introduce Project Ben Bersnacky (“Bersnacky” or the “Company”), a high-growth company in the infant organic food industry.

The Company uses a proprietary recipe to develop a novel product currently unmatched in the marketplace. The Company sells its products direct to consumer and through select retailers.

Select Financial Data (all figures in 000s)



Investment Highlights

- **Recognized Brand:** Though the Company is young relative to its competition, it has developed an enthusiastic following.
- **Proprietary Process and Recipe:** The company has developed a proprietary process and recipe that allows it to offer high quality organic infant food that visually sets itself apart from the competition.
- **Direct-to-Consumer Model:** One of the few companies in the space that has managed to develop a strong direct-to-consumer model while simultaneously growing its wholesale footprint.
- **Benefiting from Trends:** The organic food trend is expected to continue for the foreseeable future. The company also benefits from the ongoing food-photography trend.

At this time the Company has elected to release limited information. If this opportunity is of interest please execute the attached NDA, and Banker Brothers Investment Banking will follow up with a Confidential Information Memorandum detailing the business.

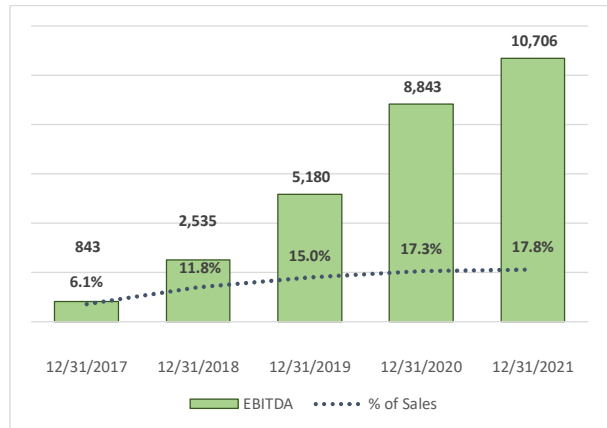
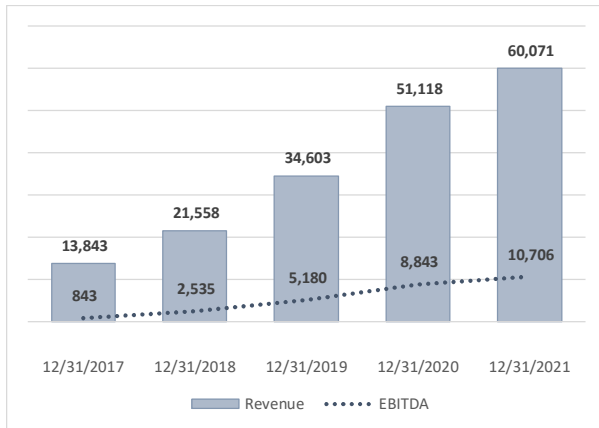
BabyBurgers LLC: Confidential Information Memorandum (“CIM”)

1. Company Overview
2. Company History
3. Product & Pricing
4. Competition
5. Financial Information

Company Overview

BabyBurgers LLC (“BabyBurgers” or the “Company”) uses a proprietary recipe to produce baby food shaped like favorite fast food dishes, BabyBurgers™, BabyNuggets™, and BabyShakes™ in miniature. This food technology immediately dissolves into semi-nutritious foodstuffs when it encounters the precise combination of heat and moisture found in a baby’s mouth. As CEO Madison English explains, BabyBurgers “melt in your mouth, not in your hand, a phrase I definitely invented.”

BabyBurgers sells its products direct to consumer and through select retailers. Select financial data provided below (*all figures in 000s*):



Company History

BabyBurgers was founded by the former chef of five-star restaurant Fifteen Gramercy Park, Madison English. Ms. English was appalled at the lack of infant diners at one of New York City’s best restaurants. The problem, she concluded, could be solved by providing infants, who are otherwise forced to consume food in liquid format, a solid option that would not create a choking hazard.

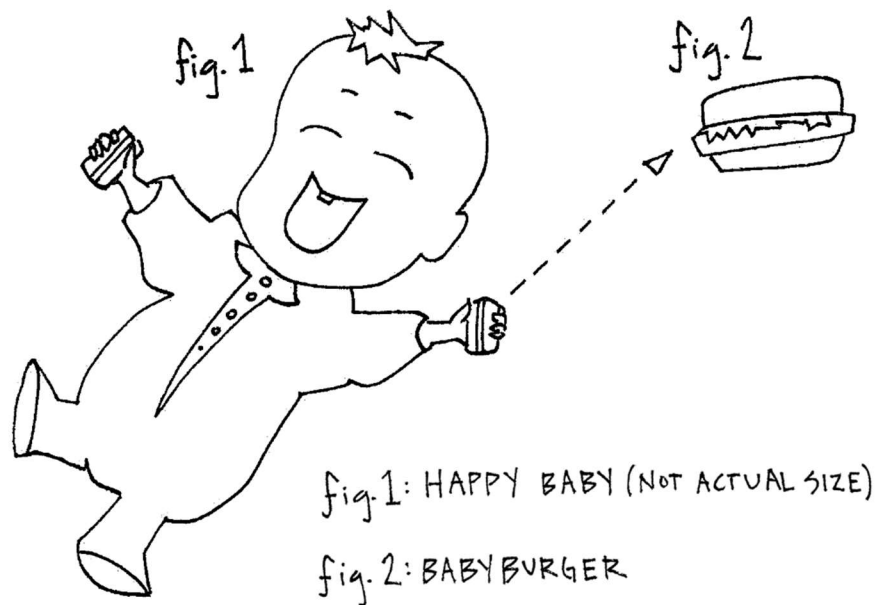
To the menu she one day quietly added BabyFoieGras and BabyPorterhouse using her new proprietary recipe that immediately dissolved in the appropriate environment (i.e. a baby’s mouth). Critics were aghast and Ms. English was banished from New York City’s culinary scene.

Mrs. English took her recipe and moved to Dallas, Texas where she temporarily worked at a day-care center to make ends meet. Having never really watched babies and toddlers eat before, she

was astounded by how sloppy they all were. “Why should babies eat sloppy soups?!” she demanded.

The following week she returned to work with a new prototype. This time her recipe was in the shape of a tiny burger. At lunch each child was provided three mouth-sized burger-shaped food objects made of hearty organic baby-growing nutrients. A mother that had arrived late noticed, gushed, and immediately produced her phone to photograph her child eating a delectable “burger” in one hand. The photograph was uploaded to Instagram with the caption “Let them eat like adults!!! *heart-eyed emoji*” It was an immediate sensation. BabyBurgers was born.

Today, BabyBurgers satisfies thousands of social media savvy parents tired of meal-time photographs ruined by liquid food.



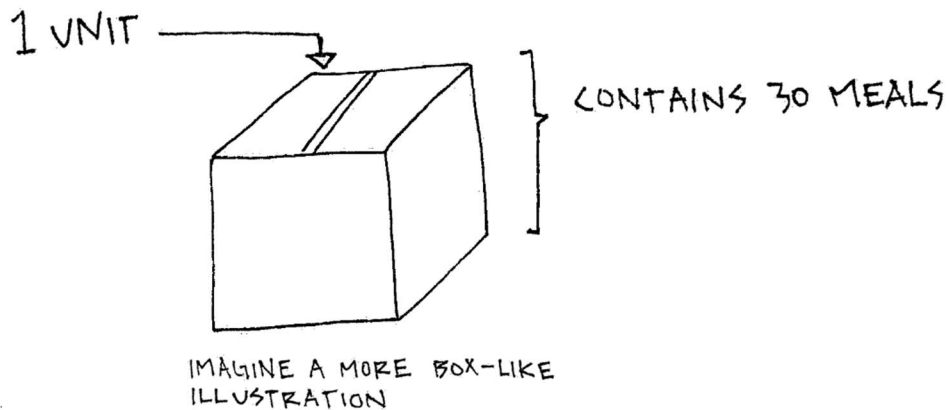
Note: Banker Brothers Investment Banking could not find a baby model that fit the budget for this CIM. So we had one of our analysts draw the baby at 2am after pulling an all-nighter the previous night.

Product & Pricing

BabyBurgers sells its product direct-to-consumer and through wholesale channels. Regardless of point of sale, the product is always sold in the same packaging with 30 meals available per unit sold. Each box has five tiers of six units.

The management team believes additional sales could be achieved in the direct-to-consumer segment if more lower volume options were made available. The Company has not yet elected to take this on because of the additional cost associated with fulfillment, packaging and logistics.

Initially the product was priced at \$125 per unit, which translates to \$4.17 per meal. Since then the company has implemented two price increases, and currently the product sells for \$145 per unit or \$4.83 per meal. These price increases can be seen in the financial model provided by the Company.



Competition

BabyBurger's CEO would argue that the company does not have any "real" competition because the product does not have an equal in quality and presentation. It is, however, the highest priced item in its category of high-quality, organic infant food.

Competitor Honestlé Foods Inc. ("Honestlé") makes a liquid product of equivalent nutritional value with similar high-quality ingredients that is sold in a pouch format at an average price of approximately \$3.75 per meal.

CONFIDENTIAL INFORMATION MEMORANDUM

Financial Information

Income Statement	12/31/2017	12/31/2018	12/31/2019	12/31/2020	12/31/2021
Revenue	13,842,500	21,558,250	34,602,910	51,118,010	60,070,683
<i>Growth %</i>	39.6%	55.7%	60.5%	47.7%	17.5%
Cost of Goods Sold	10,436,441	15,691,667	24,913,852	36,534,048	43,014,284
Gross Margin	3,406,059	5,866,583	9,689,058	14,583,962	17,056,399
<i>% of Sales</i>	24.6%	27.2%	28.0%	28.5%	28.4%
Total SG&A	2,999,525	3,811,160	5,067,858	6,423,441	7,139,655
EBIT	406,534	2,055,423	4,621,200	8,160,522	9,916,744
<i>% of Sales</i>	2.9%	9.5%	13.4%	16.0%	16.5%
EBITDA	842,963	2,534,887	5,179,533	8,842,664	10,706,030
<i>% of Sales</i>	6.1%	11.8%	15.0%	17.3%	17.8%
Balance Sheet	12/31/2017	12/31/2018	12/31/2019	12/31/2020	12/31/2021
Cash	515,041	1,640,099	2,952,138	6,813,814	12,771,242
Accounts Receivable	1,365,000	2,209,815	3,506,100	4,934,785	5,481,000
Inventory	1,147,850	1,859,490	2,936,540	3,977,060	5,000,000
Current Assets	3,027,891	5,709,404	9,394,778	15,725,659	23,252,242
PP&E	1,958,333	2,153,869	2,395,536	2,763,393	3,224,107
Total Assets	4,986,224	7,863,273	11,790,314	18,489,052	26,476,349
Accounts Payable	583,500	945,324	1,490,484	1,991,372	2,500,000
Accrued Compensation	875,208	1,047,125	1,336,917	1,630,813	1,802,313
Current Liabilities	1,458,708	1,992,449	2,827,401	3,622,185	4,302,313
Revolving Line of Credit	-	-	-	-	-
Term Debt	3,600,000	4,200,000	3,800,000	3,400,000	3,000,000
Total Liabilities	5,058,708	6,192,449	6,627,401	7,022,185	7,302,313
Common Stock	750,000	750,000	750,000	750,000	750,000
Retained Earnings	(822,484)	920,824	4,412,913	10,716,867	18,424,037
Total Equity	(72,484)	1,670,824	5,162,913	11,466,867	19,174,037
Total Liabilities & Equity	4,986,224	7,863,273	11,790,314	18,489,052	26,476,349
<i>Check</i>	-	-	-	-	-
Investments	12/31/2017	12/31/2018	12/31/2019	12/31/2020	12/31/2021
Capital Expenditures	600,000	675,000	800,000	1,050,000	1,250,000
<i>% of Sales</i>	4.3%	3.1%	2.3%	2.1%	2.1%

TRANSACTION ASSUMPTIONS

Transaction Assumptions:

In this exercise we are leaving most of the assumptions about the future to you. In a real-world exercise you must develop your own assumptions and evaluate any projections provided with extreme skepticism.

As it relates to revenue growth, think through your customer base. How do you measure demand for this product? Because this is a fictional company you could develop your own thesis. For example, assume you believe only Instagram obsessed parents are willing to pay a premium for photo-friendly baby food. And to take it a step further, you might conclude that only parents that can broadcast this purchase widely will be consistent customers. You might then try to go through the exercise of determining how many of Instagram's users are parents with more than X,000 followers. Alternatively, if you are just trying to test your understanding of LBO mechanics, you can simply use historical averages to project the future.

We are also leaving the purchase price to you. We have included the sources of financing in the Term Sheets linked in this document. As you will see in the Sources & Uses table provided in the model, the amount of equity raised will be left to you as the independent sponsor driving the transaction.

Transaction:		12/31/2021
		EBITDA
EBITDA at 12/31/2021		10,706
Sources		Multiple
Senior Term Debt	25,000	2.3x
Subordinated Debt	17,000	1.6x
Equity		0.0x
TOTAL	42,000	3.9x
Uses		Multiple
Seller Proceeds		0.0x
OldCo Debt		0.0x
Transaction Expenses		0.0x
Financing Fees		0.0x
TOTAL	-	0.0x

Remember, ultimately the objective is to build a model that allows you to demonstrate the returns achievable in the event of a successful exit. If at the conclusion of the exercise you do not believe the returns are attractive, revisit the capital structure you created to make adjustments. After all, the best way to control risk is with price. Good luck!