Final Project Handout

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BUS438

Objective

After joining an investment bank you are approached by a client who is interested in acquiring/merging with a target company. Your role is to prepare a professional report on the target company valuation. You will perform a thorough valuation analysis of the target, forecast its cash flows, and make investment recommendations to the board of the client company. Your final report includes a two-page executive summary of your findings, and an appendix containing all your spreadsheets.

Choosing a Firm

The first step for this project is to pick a proper target company based on the following criteria:

- The target must be a publicly traded non-financial US company
- It must NOT be on “List of Companies Chosen by Former Students” on PolyLearn
- The target must be a parent company and not a subsidiary
- It is much easier to work with focused companies than with conglomerates
- It must have at least 10 years of financial statements and stock price data
- To make it more realistic it would be interesting (but not required) if you can find a potential M&A target.

Recommended Resources

1. Part 1 and Part 2 of the recommended book on Valuation (KGW)
2. Chapter 2 and 18 of the course textbook, (BDH).
3. Chapter 2 and 19 of the more advanced version of the textbook, (BD).
4. SEC filings of the target company such as 10-K (annual report), 8-Q, etc.
5. Other resources posted on PolyLearn: Mergent, Morningstar, Yahoo Finance, etc.

Project Format

You need to submit two documents electronically (via PolyLearn) as your final project:

- A two-page executive summary
  - It includes total of 10 paragraphs.
  - The first and the last paragraph are introduction and conclusion.
  - Each of the other 8 paragraphs summarizes the main findings of each workshop.
  - Use plain non-technical language that requires no technical background to understand.
- A spreadsheet
  - It consists of 8 separate sheets; one for each of the workshops listed in the outline section.
  - Your spreadsheet must show the steps you followed in each workshop (e.g., show formulas).
  - Do not include raw data in the main body of the spreadsheet (e.g. time-series of stock price).
  - Tables and graphs should be clearly labeled, and sources should be properly cited.
Outline for the Report

This is a tentative outline for the project. Changes may be made as the course progresses. When you refer to Data Cases mentioned below remember to substitute your company’s data for the proposed company in each case.

1. Company Background and Industry Analysis
   a. Size, Products Range, Geography, Historical Stock Price, etc.
   b. Business Model
   c. Risks and Challenges
   d. Industry Comparisons
2. Financial Statement Analysis (refer to Data Case of Chapter 2)
   a. Ratio Analysis
   b. Horizontal and Vertical Analysis
   c. DuPont Analysis
   d. Comparison to Industry and Rival Firm
3. First Estimate: Valuation Using Comparable Firms
   a. Selecting Comparables
   b. Valuation Multiples
   c. Adjusting for Differences Using Regression Analysis
4. Forecasting Growth
   a. Drivers of Growth
   b. Historical Growth Trend
   c. Revenue, EBIT and EPS Growth
   d. Geometric vs. Arithmetic Averages
5. Capital Budgeting and Pro-forma Analysis (refer to Data Case of Chapter 9)
   a. Follow Chapter 18 of BDH
   b. Forecasting Using Percentage of Sales Method
   c. Graphing IS and BS Items to Detect Jumps and Kinks
   d. Correcting Forecasts
   e. Forecasting Free Cash Flow
6. Estimating the Cost of Capital (refer to Data Case of Chapter 13)
   a. Estimating Cost of Equity Using CAPM
   b. Estimating Cost of Debt
   c. Using Target Weights/Capital Structure
7. Valuation
   a. WACC-based methods:
      i. Discounted Cash Flow (refer to Data Case of Chapter 10)
   b. Non-WACC Models
      i. Adjusted Present Value (APV) Method
      ii. Flow-to-Equity Method
   c. Forecasting Continuing/Terminal Value
8. Sensitivity Analysis and Comparison of Different Valuation Models
   a. Verifying Valuation Results
   b. Analyzing the Effect of Individual and Simultaneous Changes in Assumptions