Chapter 44
LEVERAGED BUYOUTS (LBOs)

Use management as a lever and lean on it!

A Leveraged Buyout (LBO) is the acquisition of a company by one or several private equity funds which finance their purchase mainly by debt. Most of time, LBOs bring improvement in operating performances as the management is highly motivated (high potential for capital gains) and under pressure to rapidly pay down the debt incurred.

Why are financial investors willing to pay more for a company than a trade buyer investor? Are they miracle workers? Watch out for smoke and mirrors. Value is not always created where you think it will be. Agency theory will be very useful, as the main innovation of LBOs is a new corporate governance which, in certain cases, is more efficient than that of listed or family companies.

In the course of this chapter we will use as an example the leveraged buyout of Elis, the European leader in the rental and maintenance of professional clothing, textile articles, and sanitary equipment, bought by Eurazéo.[1]

1 *We have based this example on publicly available information, and for some of the figures have either simplified the reality or made some estimates. It should be considered as illustrative and does not reflect the reality or the exact state of the company.*

Section 44.1
LBO STRUCTURES

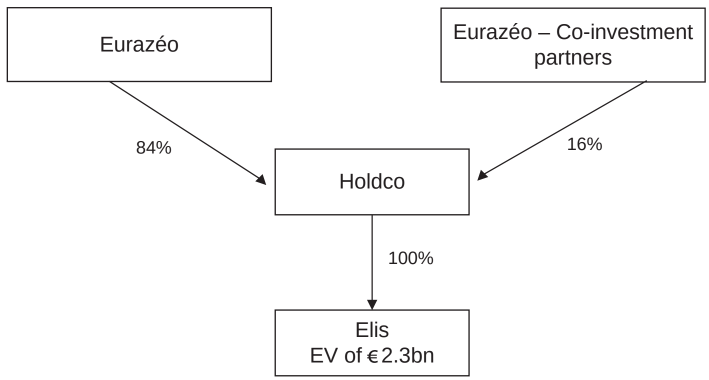
1/ PRINCIPLE

The basic principle is to create a holding company, the sole purpose of which is to hold financial securities. The holding company borrows money to buy another company, often called the "target". The holding company will pay interest on its debt and pay back the principal from the cash flows generated by the target. In LBO jargon, the holding company is often called *NewCo* or *HoldCo*.

Operating assets are the same after the transaction as they were before it. Only the financial structure of the group changes. Equity capital is sharply reduced and the previous shareholders sell part or all of their holding.

From a strictly accounting point of view, this setup makes it possible to benefit from the effect of financial gearing (see Chapter 13).

Now let us take a look at the example of Elis, sold in mid-2007 by the LBO fund PAI for an enterprise value of €2.3bn. Elis generated a 2007 operating profit of €160m for sales of €930m and an EBITDA of €220m.



We assume that the pre-tax cost of debt is 7% (4% plus a 3% margin). The balance sheets are as follows:

Elis's revalued balance sheet		Holdco's unconsolidated balance sheet		Group's consolidated balance sheet	
Operating assets €2276m	Shareholders' equity €2276m	Shares of Elis €2276m	Shareholders' equity €426m	Operating assets €2276m	Shareholders' equity €426m
			Debt €1850m		Debt €1850m

Note that consolidated shareholders' equity, on a revalued basis, is now 81% lower than it was prior to the LBO.

An LBO leads to a massive destruction of equity.

The profit and loss statement, meanwhile, is as follows:

(in €m)	Elis	Holdco	Consolidated
Earnings before interest and tax	160	104[2]	160
– Interest expense	0	130	–130
– Income tax at 35%	–56	0	–10[3]
= Net income	104	–26	20

2 *Assuming 100% payout.*

3 *Assuming tax consolidation treatment.*

2/ TYPES OF LBO TRANSACTIONS

Leveraged Buyout or ***LBO*** is the term for a variety of transactions in which an external financial investor uses leverage to purchase a company. Depending on how management is included in the takeover arrangements, LBOs fall into the following categories:

- a ***(Leveraged) Management Buyout*** or ***(L)MBO***, is a transaction undertaken by the existing management together with some or all of the company's employees;

- when outside managers are brought in, the transaction is called a ***BIMBO***, i.e. a combination of a *buyin* and a management *buyout*. This is the most common type of LBO in the UK;
- finally, the term ***Leveraged Buildup (LBU)*** is used to describe an LBO in which the new group continues to acquire companies in its sector so as to create industrial synergies. These acquisitions are financed primarily with debt;
- an **Owner Buyout** (OBO) is a transaction undertaken by the largest shareholder to gain full control over the company.

3/ TAX ISSUES

Obtaining tax consolidation between the holding company and the target is one of the drivers of the overall structure as it allows financial costs paid by the holding company to be offset against pretax profits of the target company, reducing the overall corporate tax income paid.

In some countries, it is possible to merge the holding company and the target company soon after the completion of the LBO. In other countries this is not the case, as the local tax administration argues it is contrary to the target's interest to bear such a debt load. Provided tax consolidation is possible between the target and Holdco, this has no material consequence except a small increase in red tape. If tax consolidation is not possible because, for example, the Holdco stake in the target company has not reached the required minimum threshold, then a debt push down may be necessary.

The target company pays an extraordinary dividend to Holdco or carries out a share buyback financed by debt, allowing Holdco to transfer part of its debt to the target company where financial expenses can be offset against taxable profits. If the target company is still listed, an independent financial expert is likely to be asked to deliver a solvency opinion testifying that the target debt load does not prevent it from properly operating in the forseeable future.

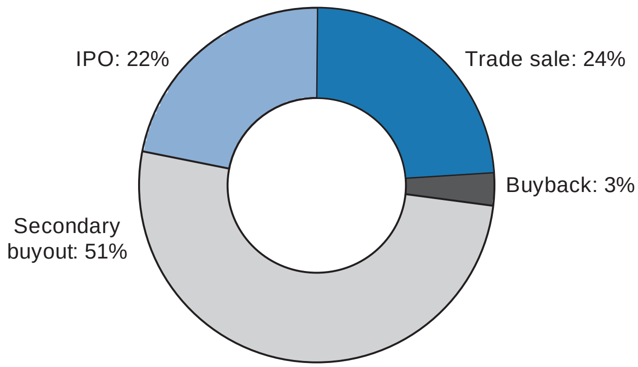
4/ EXIT STRATEGIES

The average LBO lifetime is short. Financial investors generally keep the investment for 2–5 years. There are several exit strategies:

- Sale to a trade buyer. Our general comment here is that in most cases financial investors bought the company because it had not attracted trade buyers at the right price. When time has arrived for the exit of the financial buyer, either the market or the company will have had to change for a trade buyer to be interested. Galbani, the leading Italian cheese company, was sold by BC Partners in 2006 to Lactalis.
- Stock market flotation. This strategy must be implemented in stages, and it does not allow the sellers to obtain a control premium; most of the time they suffer from an IPO discount. It is more attractive for senior management than a trade sale. At end-2006, Hertz was IPOed by Clayton Dubillier & Rice, and Carlyle.
- Sale to another financial investor, who in turn sets up another LBO. These "secondary" LBOs are becoming more and more common. Elis is a tertiary LBO.

- A leveraged recapitalisation. After a few years of debt reduction thanks to cash flows generation, the target takes on additional debt with the purpose of either paying a large dividend or repurchasing shares. The result is a far more financially leveraged company.

VOLUME OF 2007 EXITS FROM €500m+ BY ROUTE



Source: Arbor Square Associates.

If the company has grown or become more profitable on the financial investors' watch, it will be easier for them to exit. Improvement may take the form of a successful redundancy or cost-cutting plan or a series of bolt-on acquisitions in the sector. Size is important if flotation is the goal, because small companies are often undervalued on the stock market, if they manage to get listed at all.

The problem emerges when the target company's profits do not allow a large enough dividend payment to the parent company, which is then unable to pay its bank interest charges or repay its debt in a timely fashion. Apart from recapitalising the company, renegotiating with creditors is the traditional solution (interest rates, covenants, repayment schedule), but in some countries creditors cannot secure their loans with the assets of the subsidiary as long as the loans are extended to the holding company.

Section 44.2
THE PLAYERS

1/ POTENTIAL TARGETS

The transactions we have just examined are feasible only with certain types of target companies. Companies for which income streams are volatile by nature, such as trading companies, do not have access to LBO financing. The same is true for companies requiring heavy capital expenditure, such as certain high-tech companies.

The target company must generate profits and cash flows that are sufficiently large and stable over time to meet the holding company's interest and debt payments. The target must not have burdensome investment needs. Mature companies that are relatively shielded from variations in the business cycle make the best candidates: food, retail, water, building materials, real estate, cinema theatres and yellow pages are all prime candidates.

THE WORLD'S 10 LARGEST LBOs IN 2007 AND 2008

Target	Date	Sector	Equity sponsor	Value ($bn)
TXU	February 2007	Energy	KKR/TPG	45
Equity Office	November 2006	Real Estate	Blackstone	36
HCA	July 2006	Health	Bain/KKR	33
RJR Nabisco	October 1988	Food	KKR	30
Kinder Morgan	August 2006	Energy	Carlyle	27
Harrah's Entertainment	December 2006	Casino	Appolo/TPG	27
First Data	September 2007	Technology	KKR	27
Clear Channel	November 2006	Media	Bain/Thomas Lee	27
Freescale	September 2006	Technology	TPG/Blackstone/ Permira	17
Albersons	January 2006	Retail	Cerberus	17

Source: Thomson Financial.

The group's LBO financing already packs a hefty financial risk, so the industrial risks had better be limited. Targets are usually drawn from sectors with high barriers to entry and minimal substitution risk. Targets are often positioned on niche markets and control a significant portion of them, like Elis.

Traditionally, LBO targets are "cash cows" but, more recently, there has been a movement towards companies exhibiting higher growth or operating in sectors with opportunities for consolidation.

As the risk aversion of investors decreases, some private equity funds have carried out LBOs in more difficult sectors or specialised in heavy turn-around situations (Chrysler). The mid-2007 crisis and the sudden disappearance of LBOs larger than €500m is likely to prompt a return to the basics: targets with high, stable and predictable cash flows able to pay down their debt with a reasonable degree of confidence.

2/ THE SELLERS

Around half of all LBOs are carried out on family-owned companies (the first LBO on Elis). An LBO solves the succession problem as the majority shareholders may be reluctant to sell to a competitor, may prefer to sell to their faithful and dedicated management team, and/or as the stock exchange exit may be close at that time (Thomson Learning). In 20% of cases,[4] a large group wishing to refocus on a core business sells a subsidiary or a division via an LBO. Some sectors are so concentrated that only LBO funds can buy a target as the antitrust authorities would never allow a competitor to buy it or would impose severe disposals making such an acquisition unpalatable to many trade buyers (Pro Sieben

4 *In number, but a larger percentage in amount.*

Sat 1, in German TV).The larger transactions fall into the latter category (Hertz sold by Ford).

But more and more frequently (30%), targets are companies already under an LBO, sold by one private equity investor to another one, for the second, third, or more times, such as Elis.

Finally, some listed companies that are undervalued (often because of liquidity issues or because of lack of attention from the investment community because of their size), sometimes opt for "**public-to-private**" (**P to P**) LBOs. In the process, the company is delisted from the stock exchange. Despite the fact that these transactions are complex to structure and generate high execution risk they are becoming more and more common thanks to the drop in market values. The LBO on Boots Alliance was the largest worldwide P to P in 2007.

3/ LBO FUNDS ARE THE EQUITY INVESTORS

Setting up an LBO requires specific expertise, and certain investment funds specialise in them. These are called *private equity sponsors,* because they invest in the equity capital of unlisted companies.

LBOs are particularly risky because of their high gearing. Investors will therefore undoubtedly require high returns. Indeed, required returns are often in the region of 25% p.a. In addition, in order to eliminate diversifiable risk, these specialised investment funds often invest in several LBOs.

The US and UK LBO markets are more mature than those of Continental Europe. The Asian market is nascent. For this reason, Anglo-Saxon funds such as BC Partners, Blackstone, Candover, Carlyle, Cinven, CVC, Hicks Muse and KKR dominate the market, particularly when it comes to large transactions. In the meantime, the purely European funds, such as Eurazéo, Industrie Kapital and PAI are holding their own, generally specialising in certain sectors or geographic areas.

To reduce their risk, LBO funds also invest alongside another LBO fund (they form a consortium) or an industrial company (sometimes the seller) with a minority stake. In this case, the industrial company contributes its knowledge of the business and the LBO fund its expertise in financial engineering, the legal framework and taxation.

Most of the private equity sponsors contribute equity for between 20% and 40% of the total financing. The Elis LBO was done at the top of the market with only 19% of equity. Post 2007, LBOs are financed with an equity component closer to 40%. Materially, LBO funds are organised in the form of a management company that is held by partners who manage funds raised from institutional investors[5] or high net worth individuals.

When a fund has invested nearly all of the equity it has raised, another fund is launched. Each fund is required to return to investors all of the proceeds of divestments as these are made, and the ultimate aim is for the fund to be liquidated after a given number of years.

The management company, in other words the partners of the LBO funds, is paid on the basis of a percentage of the funds invested and a percentage of the capital gains made,[6] know as **carried interest**.

Some funds decide to list their shares on the stock market, like Blackstone did in June 2007,[7] while others such as Wendel and Eurazéo are listed for historical reasons.

5 *Pension funds, insurance companies, banks, sovereign wealth funds.*

6 *Sometimes above a minimum return rate.*

7 *Just before the LBO market ground to a sudden halt.*

4/ THE LENDERS

For smaller transactions (less than €10m), there is a single bank lender, often the target company's main bank.

For larger transactions, debt financing is more complex. The LBO fund negotiates the debt structure and conditions with a pool of bankers. Most of the time, bankers propose a financing to all candidates (even the one advising the seller). This is staple financing. The high degree of financial gearing requires not only traditional bank financing, but also subordinated lending and **mezzanine debt**, which lie between traditional financing and shareholders' equity. This results in a four-tier structure: traditional, secured loans called **senior debt**, to be repaid first, **subordinated** or **junior debt** to be repaid after the senior debt, mezzanine financing, the repayment of which is subordinated to the repayment of the junior and senior debt and, last in line, shareholders' equity. Sometimes, shareholders of the target grant a vendor loan to the LBO fund (part of the price of which payment is deferred) to help finance the transaction. Assets of the target can also be securitised[8] to raise more financing. Lastly in the halcyon days of LBOs (2005 till mid-2007) other products were created but they have since disappeared.

8 *For more, see Chapter 26.*

(a) Senior debt

Senior debt generally totals 3–5 times the target's EBITDA.[9] It is composed of several tranches, from least to most risky:

9 *Earnings Before Interest, Taxes Depreciation and Amortisation.*

- tranche A is repaid in equal instalments over 3 to 7 years;
- tranches B and C are repaid over a longer period (8 to 9 years) after the A tranche has been amortised.

Each tranche has a specific interest rate, depending on its characteristics (tranche B and C will be more expensive than tranche A because they are repaid after and are therefore more risky). Until mid-2007, the cost of senior LBO financing was 200 to 300 basis points[10] over government bond yields. Since then and because of the subprime crisis, you have to add around 100 basis points to these figures.

10 *100 basis points = 1%*

When the debt amount is high, the loan will be syndicated to several banks (see Chapter 30). Collateralised debt obligation (CDO) funds were created which, until mid-2007, subscribed or bought tranches of LBO debt whose shareholders were mainly insurance companies, hedge funds and pension funds. When the LBO market reached its climax mid-2007, 80% of the senior debt in the USA was subscribed by institutional investors directly or through CDO funds, and 55% in Europe. Since then, these figures have slumped.

(b) Junior or subordinated debt

High-yield bond issues are sometimes used to finance LBOs, but this technique is reserved for the largest transactions so as to ensure sufficient liquidity. In practice the lower limit is around €100m.

An advantage of this type of financing is that it carries a bullet repayment and a maturity of 8–10 years. In accordance with the principle of subordination, the bonds are repaid only after the senior debt is repaid.

Given the associated risk, high-yield LBO debt, as the name suggests, offers investors high interest rates. They were as much as 800 basis points over government bond yields until mid-2007. Since then they have disappeared.

(c) Mezzanine debt

Mezzanine debt also comes under the heading of (deeply) subordinated debt, but is unlisted and provided by specialised funds. Returns on mezzanine debt take three forms: a relatively low interest rate (4–4.5%) paid in cash; a deferred interest or payment in kind (PIK) for 4–5%; and a share in any capital gain when the LBO fund sells its stake.

As we saw in Chapter 29, certain instruments accommodate this financing need admirably. These "hybrid" securities include convertible bonds, mandatory convertibles, warrants, bonds with warrants attached, etc.

Most of the time, mezzanine debt is made of bullet bonds[11] with warrants attached. Mezzanine financing is a true mixture of debt and shareholders' equity. Indeed mezzaniners demand returns more akin to the realm of equity investors, often approaching 15% p.a.

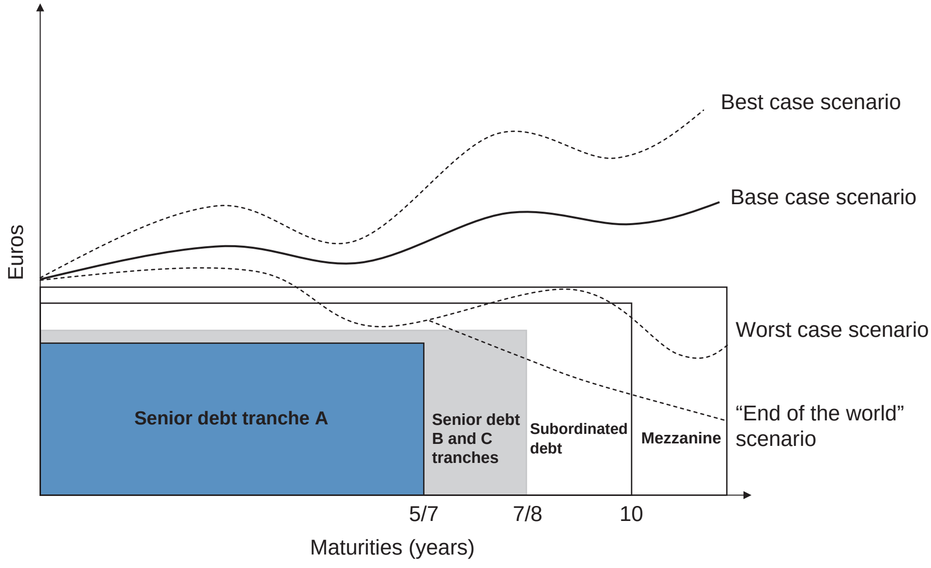
11 *See p. 484.*

Given the associated risk, investors in mezzanine debt – "mezzaniners" – demand not only a high return, but also a say in management. Accordingly, they are sometimes represented on the board of directors.

Subordinated and mezzanine debt offer the following advantages:

- they allow the company to lift gearing beyond the level acceptable for bank lending;
- they are longer term than traditional loans and a portion of the higher interest rate is paid through a potential dilution. The holders of mezzanine debt often benefit from call options or warrants on the shares of the holding company;

LBO financing spreads the risk of the project among several types of instruments, from the least risky (senior debt) to the most risky (common shares). The risk profile of each instrument corresponds to the preferences of a different type of investor.



- they make upstreaming of cash flow from the target company to the holding company more flexible. Mezzanine debt has its own specific terms for repayment, and often for interest payments as well. Payments to holders of mezzanine debt are subordinated to the payments on senior and junior debt;
- they make possible a financing structure that would be impossible by using only equity capital and senior debt.

(d) Securitisation

Increasingly, LBOs are partly financed by securitisation (see Chapter 26). Securitised assets include receivables and/or inventories, when there is a secondary market for them.

A new technique, the securitisation buyout, has arisen in the UK. It is similar to standard securitisation of receivables, but aims to securitise the cash flows from the entire operating cycle.

(e) Other financing

Banks that finance LBOs are extremely inventive: the most complex structures can include, or did up to the summer of 2007, up to 10 types of different debt.

This has led to the development of a tranche of bank debt that falls in between senior debt and mezzanine debt – **second lien debt**, which is first ranking but long-term debt, and **interim facility agreements** which enable the LBO to go ahead even before the legal paperwork (often running to hundreds of pages), has been finalised and fully negotiated. Interim facility agreements are very short-term debts that are refinanced using LBO loans.

The pinnacle of inventiveness was reached with **equity bridge**. The lending banks behind the LBO guarantee a part of the equity used in structuring the buyout, pending a syndication of these shares with other LBO funds. One would be hard pressed to find a more efficient way of increasing the risk of lenders!

The financing of Holdco is generally topped up by financing at the level of the operating company:

- either through a **Revolving Credit Facility** (RCF) which can help the company deal with any seasonal fluctuation in its working capital requirements; or
- an **acquisition facility**, which is a line of credit granted by the bank for small future acquisitions.

(f) The larger context

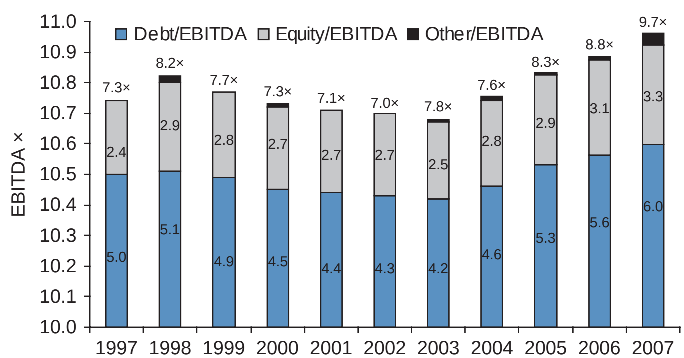
Up until the summer of 2007, investors' increasing appetite for risk meant that they were prepared not only to increase their investments in LBO funds, some of which had funds under management of over $15bn, but also to take out more and more LBO debt, which banks ceded back to them, either directly or indirectly, via CDOs or CLOs. The role of LBO banks had more or less turned into a role of structuring and distributing funds.

This is how a typical LBO structure changed over the eight years running up to 2007:

Late 1990s		Early 2007	
Equity	35%	Equity:	20%
Mezzanine debt	10%	Pik or mezzanine debt:	5%
Senior debt:	55%	High yield bond:	15%
• Tranche A, 7 years amortisable		Second lien:	5%
• Tranche B, 8 years, bullet		Senior debt:	55%
Revolving credit		• Tranche A, 7 years amortisable	
		• Tranche B, 8 years, bullet	
		• Tranche B, 9 years, bullet	
		Revolving credit or securitisation	
		Investment financing credit	

Over the same period, the prices of the target companies acquired under LBOs rose in comparison to their EBITDA.

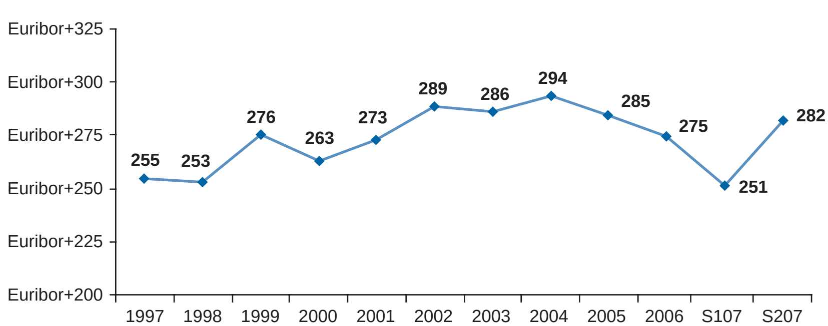
Elis was bought mid-2007 at 10.3 × its EBITDA and the LBO was financed with debt for 81%, representing 8.4 times the EBITDA.



Source: Standard & Poor's.

In a nutshell, the stage was set for a brutal crisis!

WEIGHTED AVERAGE SPREAD ON SENIOR LBO DEBT (IN bps, 1 bp = 0.01%)



Source: Standard & Poor's.

5/ THE MANAGERS OF A COMPANY UNDER AN LBO

The managers of a company under an LBO may be the historical managers of the company or new managers appointed by the LBO fund. Regardless of their background, they are responsible for implementing a clearly defined business plan that was drawn up with the LBO fund when it took over the target. The business plan makes provision for operational improvements, investment plans and/or disposals, with a focus on cash generation because, as the reader is no doubt aware, cash is what is needed for paying back debts!

LBO funds tend to ask managers to invest large amounts of their own cash in the company, and even to take out loans to be able to do so, in order to ensure that management's interests are closely aligned with those of the fund. Investments could be in the form of warrants, convertible bonds or shares, providing managers with a second leverage effect, which, if the business plan bears fruit, will result in a 5- to 10-fold or even greater increase in their investment. On the other hand, if the business plan fails, they will lose everything. So, only in the event of success will the management team get a partial share of the capital gains and a higher IRR on its investment than that of the LBO funds. This arrangement is known as the **management package**.

In some cases, following several successful LBOs, the management team can, as a result of this highly motivating remuneration scheme, take control of the company,[12] having seen its initial stake multiplied several times.

12 *Of small or medium size.*

Section 44.3
LBOs AND FINANCIAL THEORY

LBOs have gained considerable popularity since the mid-1980s, even though the market is cyclical and experienced a dry spell in the early 1990s and a big slump in 2007.

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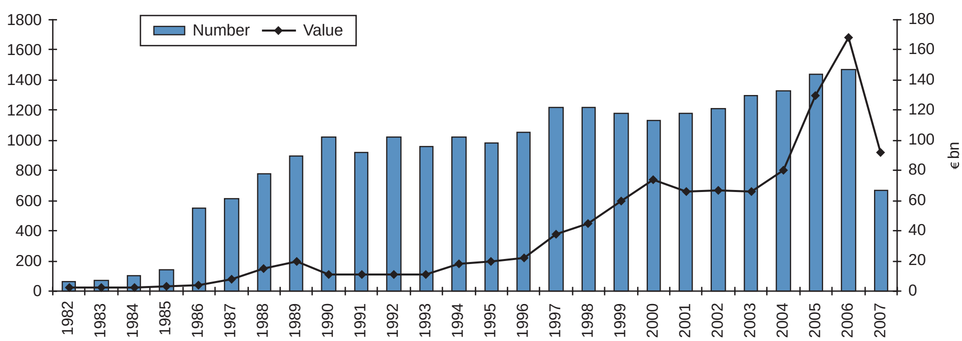
BUYOUTS AND BUYINS IN EUROPE



Source: CMBOR[13] / Barclays Private Equity / Deloitte & Touche.

13 *Centre for Management Buy Out Research.*

Experience has shown that LBOs are often done at the same price or at an even higher price than what a trade buyer would be willing to pay. Yet the trade buyer, assuming he plans to unlock industrial and commercial synergies, should be able to pay more. How can we explain the widespread success of LBOs? Do they create value? How can we explain the difference between the pre-LBO value and the LBO purchase price?

At first, we might be tempted to think that there is value created because increased leverage reduces tax payments. But the efficient markets hypothesis casts serious doubts on this explanation, even though financial markets are not in reality always perfect. To begin with, the present value of the tax savings generated by the new debt service must be reduced by the present value of bankruptcy costs. Secondly, the arguments in Chapter 34 have led us to believe that the savings might not be so great after all. Hence, the attractions of leverage are not enough to explain the success of the LBO.

We might also think that a new, more dynamic management team will not hesitate to restructure the company to achieve productivity gains and that this would justify the premium. But this would not be consistent with the fact that the LBOs that keep the existing management team create as much value as the others.

Agency theory provides a relevant explanation. The high debt level prompts shareholders to keep a close eye on management. Shareholders will closely monitor operating performance and require monthly in-depth reporting. Management is put under pressure by the threat of bankruptcy if the company does not generate enough cash flow to rapidly pay down debt. At the same time, managers systematically become – either directly or potentially – shareholders themselves via their management package, so they have a strong incentive to manage the company to the best of their abilities.

Management, motivated by a potentially big payoff and put under pressure by a heavy debt burden, will manage the company in the most efficient manner possible, increasing cash flows and hence the value of the company. It's the carrot-and-stick approach!

Kaplan has demonstrated through the study of many LBOs that their operating performance, compared with that of peer companies, is much better (cash flow generation return on capital employed) and that they are able to outgrow the average company and create jobs.[14] This is one example where there is a clear interference of financial structure with operating performance.

14 *See interview with Philippe Santini (Managing a company under LBO), The Vernimmen.com Newsletter, June 2007.*

LBO transactions greatly reduce agency problems and in so doing, create value. Their corporate governance policies are different from those of listed groups, family companies, and in many case are more efficient.

LBOs give fluidity to markets helping industrial groups to restructure their portfolio of assets. They play a bigger role than IPOs which are not always possible (equity markets are regularly shut down) or realistic (small- and medium-sized companies in some countries are, in fact, practically banned from the stock exchange).

SUMMARY

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A leveraged buyout is a transaction whereby the purchase of a company is financed primarily with borrowed funds. A holding company contracts the debt and purchases the target company. The company's cash flow is regularly funnelled upstream to the holding company via dividends to enable the latter to pay interest and reimburse the loans.

An LBO is often a solution in a family succession situation or when a large group wants to sell off a division. It can also be a way for a company to delist itself when it is undervalued in the market.

The target company in an LBO may keep the current management in place or hire a new management team. Equity capital is provided by specialised funds, the LBO funds. The structure depends on several layers of debt – senior, junior, mezzanine – with different repayment priorities. As priority declines, risk and expected returns increase.

Increased gearing and the deductibility of interest expense do not satisfactorily explain why value is created in an LBO. Instead, it appears that the heavier debt burden motivates management to do a better job managing the company, of which they are often destined to become shareholders themselves. This is agency theory in action. LBO funds bring different and, most of the time, more efficient corporate governance policies than those of family companies or listed groups: they focus management teams on cash flow generation and value creation. This is why a company can remain under LBO for years, with one LBO fund selling it to another.

QUESTIONS

@ quiz

1/ Explain why an LBO is a type of capital reduction.

2/ What risks are involved in an LBO?

3/ Can mezzanine financing in the context of an LBO be compared with equity or debt?

4/ In the context of an LBO, does the holder of senior debt take more or less risk than the holder of junior debt?

5/ Can an LBO be carried out on a startup company?

6/ In a secondary LBO, can an LBO fund accept that the management team does not reinvest part of the capital gains achieved on the first LBO in the new LBO? Why?

7/ What are the different possible exit routes after an LBO?

8/ How does corporate governance of an LBO differ from that of a listed company with no major shareholder?

9/ How does corporate governance of an LBO differ from that of most unlisted family companies?

ANSWERS

Questions

1/ *Because shareholders' equity is mostly replaced by debt.*
2/ *The risk that debts will outweigh cash flows generated.*
3/ *With debt because sooner or later it has to be repaid.*
4/ *Less risk because the holder of senior debt is repaid before the holder of junior debt.*
5/ *No, because a startup company's cash flows are much too volatile to allow it to carry debt.*

6/ *No, an LBO fund requires around 50% of the capital gains to be reinvested to keep management' s motivation high.*
7/ *IPO, sale to a trade buyer, a secondary buyer, bankruptcy, a recapitalisation.*
8/ *Strong financial incentives for managers, constraint of the debt to be paid down, regular business discussions with shareholders (LBO fund representatives).*
9/ *Meritocraty is the rule of the game, not being member of the family.*

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