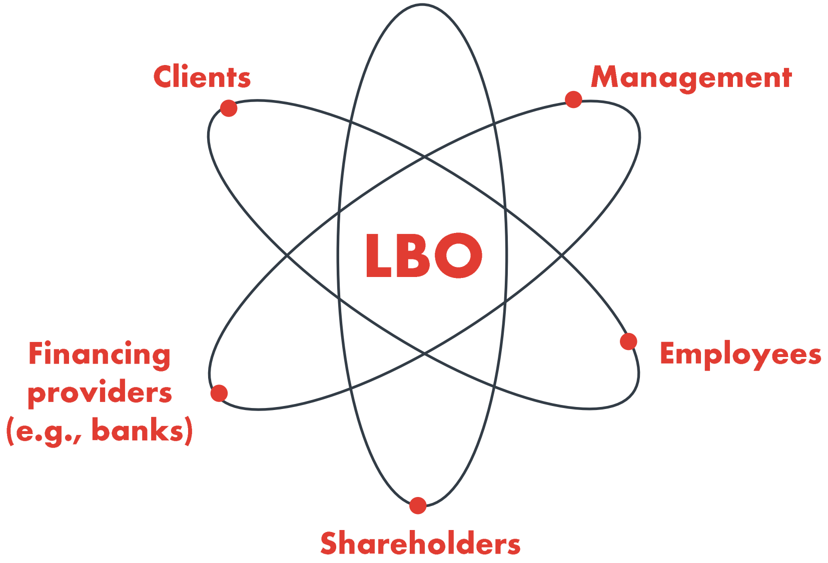
Introduction to Private Equity

ARDIAN

General principles of a Private Equity fund

LBO definition

Generating value supporting high performing companies and implementing long-term strategic vision



THE GOAL IS TO CREATE VALUE FOR ALL STAKEHOLDERS ALIGNING THE INTERESTS OF MANAGERS, EMPLOYEES AND SHAREHOLDERS

- A leveraged buyout (LBO) is the acquisition of a controlling stake in a company by a specialized investment fund, financed by a mix of debt and equity. The LBO funds usually ask managers to invest in the deal to incentivize them: this allows an alignment of interest between shareholders and managers and leads to an improvement or acceleration in the company's operating performance

- The success of a LBO depends on the target management’s ability to implement a sound and long-term strategy, the evolution of the company’s market, and its intrinsic qualities: products / services, positioning, footprint, brand, industrial assets, innovation capabilities, suppliers, clients, distribution network, etc.

- At the same time, the investment fund acts as a sparring partner, supporting the management team by providing access to its network, sharing best practices and technical expertise (in financing, M&A, digital, ESG, treasury management, etc.), as well as providing financial resources to fund both internal, such as opening new sites and industrial Capex, and external growth projects

Key success factors of an LBO

What makes a good LBO target?

Human component

Management team of high quality, with a strong track record, a clear strategy, and motivated employees

Market environement

Identified growth opportunities and fragmentation (presence of potential build-ups)

A mature sector with good visibility, low risks of technological / market disruption and high barriers at entry

Intrinsic characteristics of the target

A strong positioning: brand recognition, quality of its products / services, innovation, high performance on main KPC

Predictable and recurrent revenues (e.g., customer loyalty, low price pressure, revenue model) and high and sustainable margins

Strong cash generation thanks to limited capital intensity (e.g. low Capex or Working Capital requirements)

Entry / Acquisition

What are the key steps of the acquisition process?

LBO

Acquisition

Monitoring

Exit

Sourcing: Types of target

- Sale by a family or a founder
- Carve-out/ divestment by a mjor group of a non-core business activity
- Fund-to-fund/ Secondary LBO
- Take private/ Public-to-private transaction

Sourcing: Types of process

- Proprietary deal (benefits: direct access to management, confidentiality, less pressure in terms of timing, higher likelihood of success thanks to the absence of competition)
- Broad auction process (benefits: Precise, selected and rapidly available information, professional contacts, precise timing)
- Limited auction process (benefits: same as auction process + lower competitiveness)

Process

Phase 1

- Market research (incl. risks and opportunities)
- Study of the strengths and weaknesses of the company (strategy, positioning, offering, past growth and remaining potential, etc.)
- Determination of a preliminary purchase price

→ At the end of this phase, the investment fund decides whether or not to issue an indicative letter of interest to the seller or the intermediary in charge of the sale

Phase 2
(if selected after phase 1)

- In-depth analysis with information provided in data room, management presentations, expert sessions, site visits, interviews or any other relevant research materials
- Appointment of advisors to conduct due diligences/ audits (market, finance, tax, legal, social, ESG, digital/ tech, etc.)
- Determination of the final purchase price (incl. enterprise value to equity value bridge), subject to negotiation with the seller

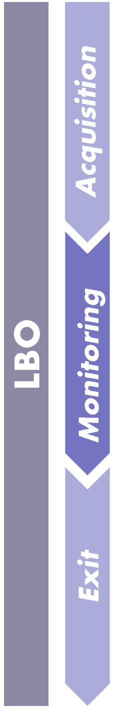
→ This second phase of analysis leads to the submission of a binding offer (generally with the agreement of the banks or private debt lenders to provide debt financing) subject to conditions precedents (CPs – e.g. approval from the anti-trust authorities – waived between signing and closing)

→ After a period of negotiation with the seller (or its representatives), the fund obtains an exclusivity period to finalize some audits/ analysis or directly signs a Sales and Purchasing Agreement (SPA)

Monitoring: the 3 value creation drivers

How does an LBO create value?

Equity Value = Enterprise Value - Net Debt



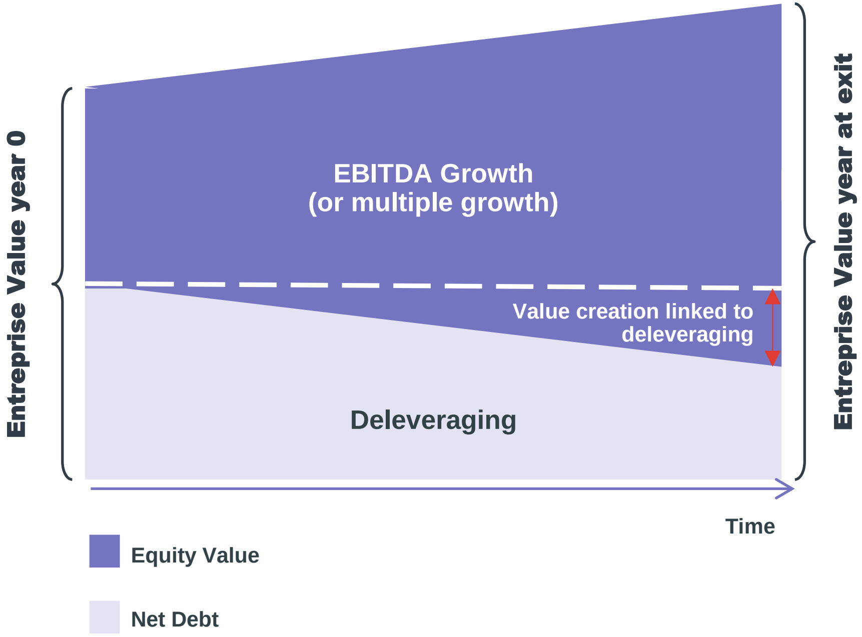
Value creation levers of an LBO

1. **EBITDA GROWTH**
   - Generation of additional organic sales
   - Acquisition of add-ons at a lower multiple than the entry multiple of the Group (ideally) and / or with synergies
   - EBITDA margin improvement

2. **CASH GENERATION / DELEVERAGING**
   - Possible levers : (i) EBITDA generation, (ii) improvement of Working Capital requirements, (iii) Capex optimization or (iv) reduction of the company’s cost of capital

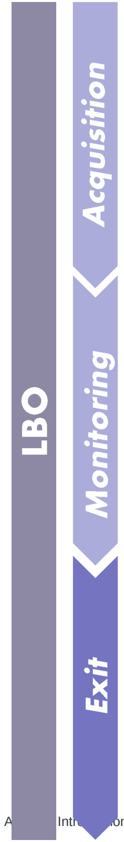
3. **STRATEGIC VALUE / VALUATION MULTIPLE GROWTH AT EXIT**
   - Growth profile, profitability, strategic positioning and market shares of the group leading to the market valuating the asset at a higher/ lower multiple
   - Financial market conditions at exit

Components of the value creation



Exit / liquidity

What are the potential exit routes of an LBO?



- LBO investments usually last for 4 to 5 years, giving companies the opportunity to implement a long-term strategy. It's important to keep in mind that investment funds need to prepare the equity story for the next buyer, so they will be planning a strategy for the next 10 years from the time they enter the company
- Exit strategy is often carefully studied / planned even before the execution of the LBO
- The exit from an LBO can take various forms:

TRADE SALE — Full disposal with a potential to benefit from a price premium as strategic buyers can value synergies

INITIAL PUBLIC OFFERING (IPO) — Existing shareholders can keep a stake in the company

NEW LBO (SECONDARY, TERTIARY) — Full disposal or possibility to reinvest / roll over equity alongside the newcomer (most of the time as a minority or co-controlling shareholder)

CONTINUATION FUND — Ad-hoc fund set up by the existing GP to continue supporting one or more investments over the long-term
Typically a relevant alternative for "trophy" assets that still offer significant potential for value creation

Understanding the mechanics of a Private Equity fund

How does a private equity fund is managed?

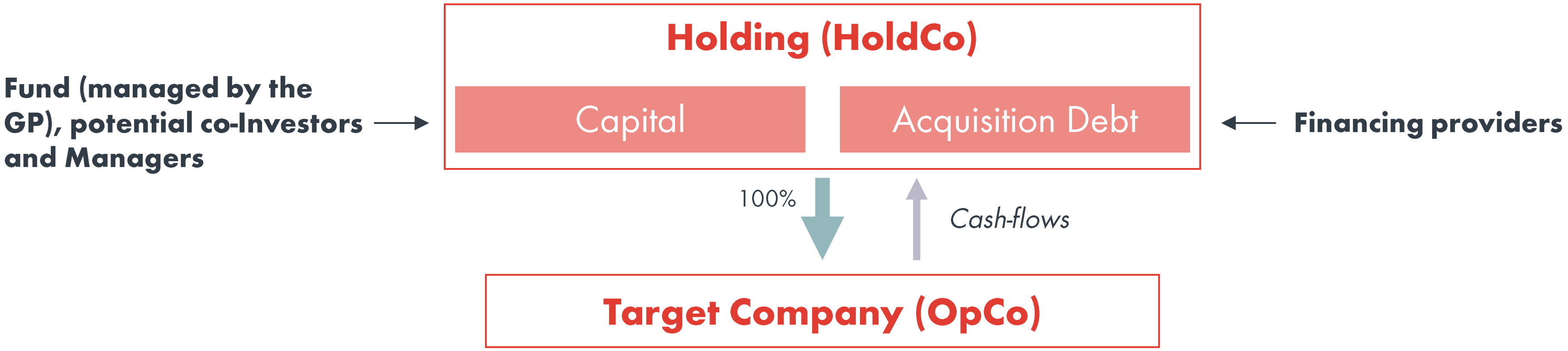
- In the private equity industry, fund managers (General Partners or GPs) and investors (Limited Partners or LPs) have different but interdependent roles. GPs create the investment fund, raise funds from LPs, and manage the fund, including investments, monitoring, reporting, and divestment

- GPs receive compensation through management fees, calculated as a percentage of the fund's committed capital, and through carried interests, representing a share of the fund's capital gains. It is essential to grasp the concept of the hurdle rate, which denotes the minimum return that a fund must attain and deliver to its LPs before the GP and the investment team are eligible to receive carried interests. Typically, the hurdle rate is established at 8% for a buyout fund

- The initial step involves the GP identifying a promising target and preparing to finalize the deal. They secure the amount committed by the LPs in the fund to fund the operation and proceed to establish a holding company (HoldCo). The fund then allocates the capital from the call to HoldCo, which will subsequently acquire the target company (OpCo). Apart from the equity contributed by the fund, managers, and potential co-investors, HoldCo procures debt to finance the acquisition

- Schematically, the OpCo will then upstream cash to the HoldCo (operating cash flows after taxes, etc.) to pay the related financial interests and repay the acquisition debt (which is generally repaid with the proceeds generated at exit). Under certain conditions, this structuring allows tax integration (cf. “régime de l’intégration fiscale” in France), notably resulting in tax deductibility of interests (capped) and a reduction in tax on dividend received by the NewCo (cf. “regime mère-fille” in France)

Simplified structure



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