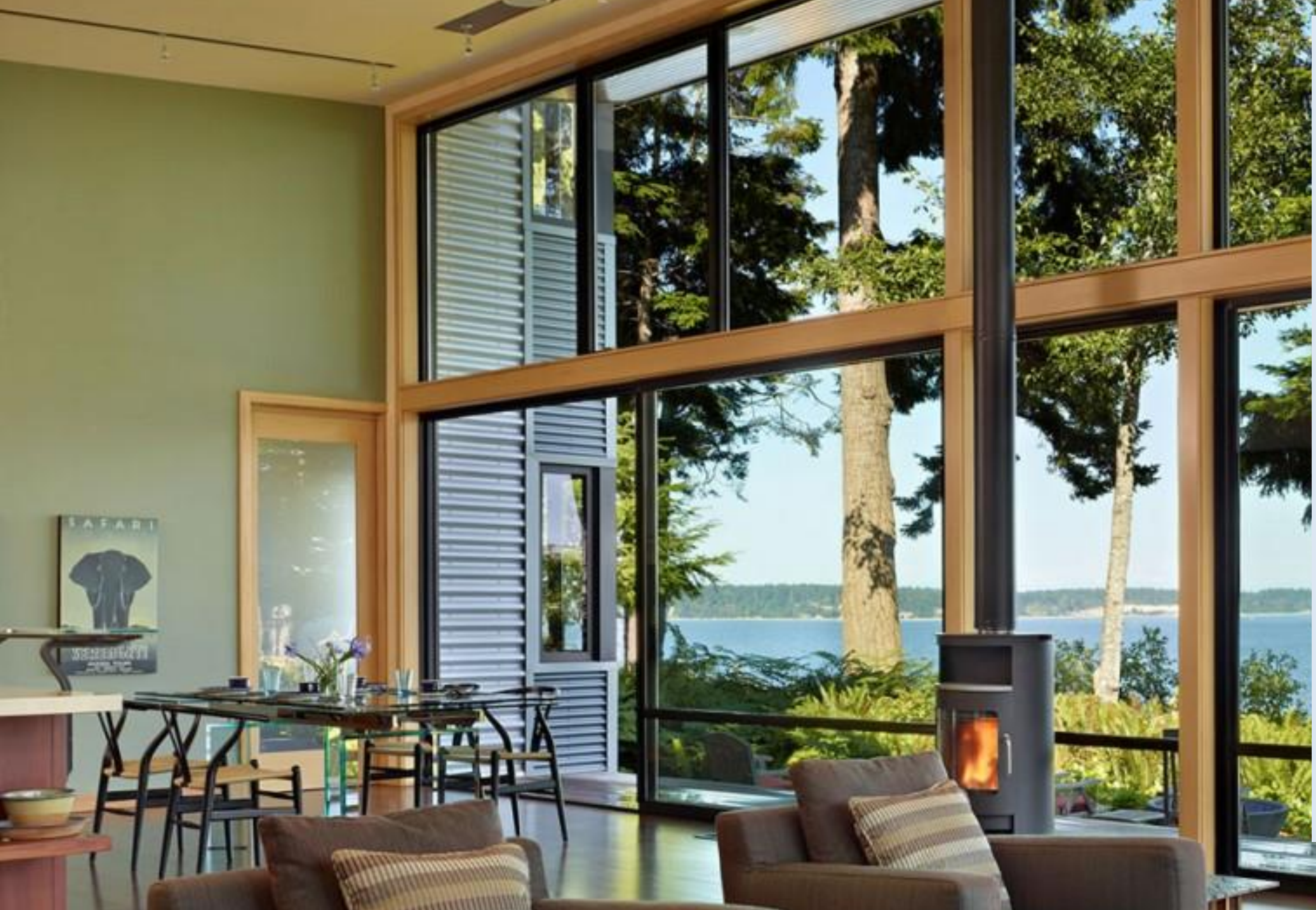
Guidance Document

Frametastic
Window and Door Frames



About Frametastic

- Frametastic manufactures and distributes window and door frames in Germany.
- Over the last 5 year’s Frametastic revenue growth was close to 4% per year.
- Global Markets Insights estimates the annual growth rate for sales in the German door and window frame market to be 3% in the foreseeable future.
- The demand for eco-friendly window and door frames is rapidly growing and companies that are not transitioning to eco-friendly solutions are expected to fall behind.
- Reported EBITDA margin was close to 16% with a dip last year.
- The company was bought by a financial sponsor 5 years ago for €800 million. At the time, the deal included a €440 million Term Loan B.
- Inflation expectation is 1.5%.

Transaction

- Frametastic is owned by a Private Equity (PE) firm which has initiated the sell side process (i.e., has started the process of selling Frametastic).
- Your team's Debt Capital Markets (DCM) department will provide debt financing services.
- You are a Private Equity client and will evaluate the (i) the Enterprise Value (EV) bid to acquire Frametastic and (ii) the choice of the debt package.
- Note that the sell side team has private information about the company. You should reach out to the sell side team for data/intelligence you require for your analysis.

Financials

Profit & Loss	Frametastic				
	Historical				
(in € million)	*2018*	*2019*	*2020*	*2021*	*2022*
Revenue	**612**	**662**	**708**	**723**	**740**
Cost of Goods Sold	339	372	390	391	394
Direct Labour	127	134	151	157	165
SG&A	32	32	36	41	74
Product Development	15	16	16	16	17
EBITDA	**99**	**108**	**115**	**118**	**90**
EBITDA margin	*16.2%*	*16.3%*	*16.2%*	*16.3%*	*12.2%*

Working Capital & Capex	Frametastic				
	Historical				
(in € million)	*2018*	*2019*	*2020*	*2021*	*2022*
Inventory	70	71	72	74	76
Accounts Receivable	45	45	46	47	47
Accounts Payable	28	28	29	29	29
Working Capital	87	88	89	92	94
Change in Working Capital	**3**	**-1**	**-1**	**-3**	**-2**
Capex	**-15**	**-17**	**-18**	**-36**	**-36**

Debt Capital Markets (DCM)

- **Debt Amount:** This is the amount that you are willing to underwrite. In the construction and building material sector, a debt amount of 5.5x EBITDA is considered average in the leveraged loan market. A debt amount as high as 6x EBITDA would be considered highly aggressive. For example, if you decide to use a 5.5x leverage, you have to multiply EBITDA by 5.5 in order to calculate your Debt Amount. The higher your Debt Amount, the higher the chances of your debt package being selected as the lender and hence to win the business. However, be careful not to be too aggressive as you, as an investment bank, want to syndicate (sell) the Loan to debt investors within 3 months after you have underwritten it; ie. if the leverage is too high, they will find the Loan unattractive.
- **Interest Rate:** Think of the interest rate as Euribor base rate + premium. Euribor is currently 2.6%. A normal premium is around 3.75% in the sector. You could go lower if you are keen to win the business. Typically, an interest rate of 6.20% would be considered highly aggressive.
- **Leverage Covenant:** Legally binding for the borrower to maintain a leverage ratio below this level. They warn the lender when debts of a company are disproportionate with the company's EBITDA base. Typically set with at least a 25% headroom at initiation. If you choose a leverage of 5.5x, the Leverage Covenant value could be 7x. Borrowers do not prefer to have a tight headroom but having too ample headroom makes syndication of the loan more difficult.
- **Maturity:** The date when the outstanding principal on the debt is due. Typically, between 3 to 5 years. Borrowers tend to prefer a longer horizon assuming a prepayment option exists.
- **Amortization:** With a term loan that is amortizing (TLA), the principal is paid back over the term of the loan rather than having one bullet at the maturity date. Most deals do not have amortization schedules and principal repayments are done via prepayment options.
- **Prepayment Option:** Optional prepayment (all or partial) of principal by the borrower. Gives the borrower the option to reduce indebtedness before it is due, this typically involves a break cost. Providing this option is likely to increase chances of your debt package being selected, however, it will be viewed unfavorably by other lenders (which might make syndication of the loan more difficult). Most deals include prepayment options.
- **Guarantees**: In private lending, lenders prefer to have a guarantee on the loan interest and principal payment. However, Frametastic does not have a parent company that could act as a guarantor; thus, a guarantee would have to be provided by the equity owner.
- **Security**: Consider if the company has suitable assets that can be used as collateral. If there are no assets that could be used, the company can use share pledge as collateral. Most Term Loans in Leveraged Buyouts are secured. Collateral is viewed favorably by other lenders (which will aid syndication) but unfavorably by equity holders.

Note:

- Enter your DCM input variables as quickly as possible and start your Buy-Side analysis.
- You can adjust your DCM inputs during your Buy-Side work. For example, you might want to offer more attractive debt terms if the company is stable or has a high cash conversion ratio (EBITDA to Free Cash Flow).

Buy-Side

Company Name: Frametastic   Team Number:

1a. Project P&L:

(in € million)	Units:	Historical 2018	2019	2020	2021	2022	Projected 2023	2024	2025	2026	2027
Revenue	€	**612**	**662**	**708**	**723**	**740**	**740**	**740**	**740**	**740**	**740**
% growth	*%*		*8.2%*	*6.9%*	*2.1%*	*2.4%*					
Cost of Goods Sold (COGS)	€	339	372	390	391	394	0	0	0	0	0
% of revenue	*%*		*56.2%*	*55.1%*	*54.1%*	*53.2%*					
Direct Labour	€	127	134	151	157	165	0	0	0	0	0
% revenue	*%*		*20.2%*	*21.3%*	*21.7%*	*22.3%*					
Gross Profit	€	**146**	**156**	**167**	**175**	**181**	**740**	**740**	**740**	**740**	**740**
% of revenue	*%*	*23.9%*	*23.6%*	*23.6%*	*24.2%*	*24.5%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*
SG&A	€	32	32	36	41	74	0	0	0	0	0
% revenue	*%*		*4.8%*	*5.1%*	*5.7%*	*10.0%*					
Product Development	€	15	16	16	16	17	0	0	0	0	0
% revenue	*%*		*2.4%*	*2.3%*	*2.2%*	*2.3%*					
EBITDA	€	**99**	**108**	**115**	**118**	**90**	**740**	**740**	**740**	**740**	**740**
EBITDA margin	*%*	*16.2%*	*16.3%*	*16.2%*	*16.3%*	*12.2%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*
Depreciation & Amortization	€	12	15	17	18	19					
EBIT	€	**87**	**93**	**98**	**100**	**71**	**740**	**740**	**740**	**740**	**740**
EBIT margin	*%*						*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*
Interest Expense - TLB	€						0	0	0	0	0
EBT	€	**87**	**93**	**98**	**100**	**71**	**740**	**740**	**740**	**740**	**740**
(Enter German Corporate Tax Rate) Tax @	€						0	0	0	0	0
Net Income	€	**87**	**93**	**98**	**100**	**71**	**740**	**740**	**740**	**740**	**740**
Net Income Margin	*%*						*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*

1b. DCM Table:

Debt (Term Loan B) Amount	
TLB Interest Rate	

For your buy-side mandate, you must evaluate 2 input variables: (i) the most attractive debt financing package, which can be selected once all teams have submitted their DCM Inputs and (ii) the EV of Frametastic, which should be based on the information in here and the sell-side information you will receive.

- **Revenue:** Use all available information and apply your judgement when making forecasts.
- **EBITDA*:*** Some expense items may be best modelled as moving in line with revenue, use your judgement. Note that the average EBITDA margin is 8%-14% in the manufacturing sector *(source: S&P Ratings).*
- **Interest**: Enter the Debt Amount and Interest Rate in the blue cells in the DCM Table.
- **Depreciation and Amortization (D&A)**: You may use some sort of average of past Capex figures to help you estimate D&A.
- **Tax**: Assume 15% for the Germany Corporate Tax Rate.

Table 2: Working Capital and Capex

2. Project Working Capital Changes & Capex:

(in € million)	Historical 2018	2019	2020	2021	2022	Projected 2023	2024	2025	2026	2027
Inventory	70	71	72	74	76					
Accounts Receivable	45	45	46	47	47					
Accounts Payable	28	28	29	29	29					
Working Capital	87	88	89	92	94	0	0	0	0	0
Change in Working Capital	**3**	**-1**	**-1**	**-3**	**-2**	**94**	**0**	**0**	**0**	**0**
Capex	-15	-17	-18	-36	-36					

- Working Capital: Use the historicals to question whether the company's planned WC optimization is realistic.
- Capex: Use the historicals as a guide and consider whether you think the company's future plans are likely to require additional capital expenditure.

Table 3: Free Cash Flow to Equity

3. Calculate Free Cash Flow:

(in € million)	Actual 2022	Projected 2023	2024	2025	2026	2027
(+) EBITDA						
(-) Interest Expense						
(-) Taxes						
(-/+) Change in Working Capital						
(-) Capex						
Free Cash Flow to Equity (FCFE)		**0**	**0**	**0**	**0**	**0**

The Free Cash Flow to Equity is the projected future cash flow. The work to calculate Free Cash Flow to Equity is already done hence, you do not have to carry out any work in this section.

Table 4: DCF Valuation

4. Discounted Cash Flow Valuation (DCF):

(in € million)	Actual 2022	Projected 2023	2024	2025	2026	2027
FCFE						
PV of FCFE						
Terminal Value					=	
PV of Terminal Value					=	
Discount Rate (IRR)						
Terminal Growth Rate						
Equity Value	-					
(+) Net Debt						
Enterprise Value	-					

In Section 4, you are using the FCFE figures that you calculated in the earlier tabs to complete your valuation. The PV (Present Value) of FCFE is today's value of the projected future cash flows.

The required rate of return for a private equity firm is currently close to 15% (IRR target). Ideally, you should not submit an EV bid which implies an IRR of less than 15%. Hence, your Discount Rate (IRR) should be 15%. You can use the Inflation Rate as the Terminal Growth Rate.

Note: The discount rate is the rate at which you discount the projected future cash flows.