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LEVERAGED BUY-OUTS : WHEN CASH IS KING

by

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Overview

What is an LBO ? Is the image of financial predators squeezing company assets, as private equity companies are portrayed, justified ? Do LBOs deserve the fiendish reputation that they have as a result of the secrecy surrounding their operations ? Before changing professions to join LBO France, the leading French company in the LBO sector, Noël Goutard was responsible for making Valeo one of the most profitable companies on the stock market. In this talk, he describes a world which is very different from Valeo, one which is dominated by the tyrannical demands for profitability and cash, and orientated towards industrial projects and instant efficiency as well as long-term development strategies of acquired companies. The efficiency of these companies delights both shareholders and managers who are motivated by potential future possibilities.

TALK : Noël Goutard

In 1999, when I was still chairman of Valeo, I realised that I had worked in industry for forty years and I had never worked for myself. So I decided to create my own company, NG Investments. Shortly afterwards, the share-holders of LBO France, one of the first private equity funds to implement LBOs (Leveraged Buy-Outs) in France in 1985, asked me to join them as an associate partner. I was fortunate to work with them at the very beginning of the LBO boom, and thanks to Gilles Cahen-Salvador, the founder of LBO France, and current president of the board of directors, Robert Daussun, this partnership was very successful.

Looking back over the past six years, I am struck by the extraordinary volume of liquid assets which exists. Part of these assets is invested in hedge funds, but a huge amount is also dedicated to LBOs. In 2006, the flood of liquid assets handled by LBO management funds amounted to 204 billion dollars, an increase of 41 % compared to 2005. Among these, ten megafunds including Kohlberg, Kravis, Roberts & Co. (KKR), The Blackstone Group, Texas Pacific Group (TPG) and Carlyle stand out, each fund totalling more than 5 billion dollars. In 2006, 1,500 companies undertook LBOs worth a total value of 750 billion dollars. This shows that liquid capital is present, readily available, and on the increase, because there is ten times the liquid capital now than in 2000.

What underlying factors account for this staggering growth ? Firstly, interest rates are low and therefore it is cheap to borrow money. Secondly, there is a great deal of money generated by the oil industry. Thirdly, pension funds have capital and there are growing profits from international companies which look to invest their liquid assets. Lastly, the world economy is growing at an average rate of 5 % and developing countries are also growing fast which elevates them to the status of international investors. Today, capital is available and cheap, making it possible to take risks. However, sometimes it is difficult to find safe investment opportunities. Are we in a bubble ? At present, experts do not think that the availability of liquid capital will fall in the short term. However, the Bank of England has just raised its interest rates… For how much longer will money be cheap ?

How does an LBO work ?

What is an LBO ? To explain it very simply, I shall take the example of the first LBO I carried out with Actaris. Actaris is a subsidiary of Schlumberger and is the world leader in electricity, gas and water meters : this is not Schlumberger's core business. In 2001, we bought Actaris for 300 million Euros : 100 million Euros came from LBO France investors and 200 million Euros from debt. In 2002, we paid off the debt and the following year, we sold the company for 370 million Euros. Therefore, our investment more than tripled in three years. I should add that we bought this company again in 2005 (this is called a secondary LBO) for 700 million Euros, 500 million Euros of which was debt. I trust that we will be able to double or more our money when we sell it again.

How does an LBO work ? The basis for a good operation is a good relationship between the share-holders of the company managing the funds, the company board, and the bankers.

As investors, we at LBO France want to be the majority share-holder so that we can control the timing of the re-sale, which is essential. In fact, we do not invest in companies on a long-term basis but try to optimise the financial gain rapidly in the expectation of a re-sale which will generate the best possible capital gain on the funds with which we have been entrusted.

To achieve this, it is essential that we have the full support of the management of the acquired company because they are the basis of the business plan. The debt is paid off by the acquired company in the form of dividends payable to a holding company which bears the debt. These dividends are tax deductible. Interest payments also have to be made. This tax lever is an intrinsic part of the structure of an LBO. Therefore, there has to be total consensus between the share-holders and management concerning the viability of the business plan. Furthermore, before the plan is drawn up, there is not only an in-depth financial and legal audit aimed at assessing the company, but also a market study. This is essential in devising a strategy for the period during which the company's shares are owned by the LBO investors. There has to be a social audit, pointing out the dangers and opportunities of a plan which might include a restructuring project.

This common objective of share-holders and management is also important to the bankers who lend the money. More so in the case of mezzanine debt where bankers are paid interest as well as a percentage of the profit made on the initial investment when the company is sold.

This situation is quite different from that of a quoted company where there are scarcely common expectations between the share-holders, the board of directors, the management and the bankers. Management is constantly preoccupied with quarterly accounts and daily fluctuations in share price, as well as the constant interface between the press, analysts and share-holders ! This is in contrast to LBO operations where great emphasis is put on objectives and the degree of efficiency is important. This is a fundamental point which largely explains why the system is efficient. It is interesting to note that an increasing number of managers move jobs from quoted companies to positions in companies controlled by private equity funds.

Managers and self-interest

Close visions in LBOs are strengthened by the fact that managers take a percentage of the capital gain when the company is sold. Managers of quoted companies are generally interested in stock options, in other words in the long-term, and are not as strongly concerned by short-term results because generally they do not have to manage the same level of debt on a short-term basis. This is the opposite to an LBO where the managers know that a minimum amount of capital and a maximum amount of debt mean that when the company is sold there will be a greater capital gain and that a percentage of this will be theirs. When Actaris was a subsidiary of Schlumberger, managers focussed on the budget and the profit and loss account. When we bought Actaris, we asked them to concentrate on cash generation and, where possible, to find the means to pay off the debt in advance. In fact, we were able to do this within a year in 2002.

Managers of quoted companies are not very concerned with the balance sheet, whereas at LBO France, we scrutinise each line of the assets, including land, property and factories. We demonstrated to the managers at Actaris that they could continue to function with just half of their current working capital and fixed assets. They decided to follow our advice and immediately freed up a huge amount of liquid assets. Their previous operating profit of 11 % had been excellent, and they were quite rightly very proud of themselves. However, we managed to convince them that their factories were oversized, their staff underemployed, and their productivity only half of what it could be. In the first six months after our intervention, their results rose from 11 % to 13 %, purely as a result of establishing the same production management methods as those used at Toyota, and the same as I had implemented at Valeo where there is huge pressure on costs. From that moment onwards, we had much better cash-flow, fewer fixed assets and improved performance.

We were also interested in spin-off activities which were not part of their core business and which we sold in favourable conditions. Thanks to rationalisation, optimisation and the disposal of these non-core business assets, we made 200 million Euros and paid off our debt in one year.

The strength of the LBO is its ability to concentrate management's attention on what is essential. LBO companies are often accused of ignoring long-term investments and research. This is not true : LBO companies naturally want the companies which are under their wing to develop R&D (Research & Development) and other necessary investments, because when the time comes to sell the company, this will greatly enhance its value. Therefore, under no circumstances should research and long-term investments be ignored.

LBO France later bought Materis, a subsidiary of Lafarge, and one of the world leaders in specialised chemical products for the building industry. During the three years when we owned Materis, we kept buying Materis' competitors for the Paint division. Our ambition was to create a European-scale business. We sold Materis on excellent terms due to this expansion and because we had exceeded the necessary critical size.

Significant liquid capital but few potential acquisitions

LBOs are capable of altering the minds of managers in an extraordinary way in order to make them more concerned about cash. The LBO has become so popular that acquisition prices are skyrocketting. In 2000, we bought companies at a price amounting to a free cash-flow ratio of one to five (in other words, the cash-flow available after investments and after variations in working capital), whereas today companies are frequently bought on a ratio of one to ten. It is a case of a large amount of liquid capital for a small number of prey.

These ratios are promoted by debt. In 2000 LBOs were funded 50 % by equity, 50 % by debt. Today, the ratios are 20 % equity and 80 % debt. As long as interest rates remain as they are now, the phenomenon is likely to grow. The extraordinary popularity of the LBO can be understood by looking at the annual rates of return on investment for an LBO which are approximately 22 %. Compared with the average interest rate for ten years which is around 3.7 %, or the average performance on the stock exchange which over the last few years has been 6.6 %, investments in an LBO are clearly very good ! Of course, there are hedge funds which have higher returns, but they are much more volatile. There is simply no comparison in terms of risk between hedge funds and LBOs : recently, a hedge fund collapsed leaving behind losses of 25 billion dollars. Therefore, as long as there are favourable borrowing rates and enough liquid capital, it is likely that LBO funds will continue to prosper.

However, the real problem is that there are increasingly fewer good companies for sale. The spotlight is then on secondary and even tertiary LBOs. Let me take the example of Actaris : we bought it for the second time in 2005 for 700 million Euros with the usual strategic expectations, having sold it for the first time in 2003 for 370 million Euros. As I explained, between 2001 and 2003, we rationalised Actaris very successfully and increased its productivity. The managers made substantial amounts of money from the sale. We had agreed that if the rate of return on investment was between 20 % and 40 % in the period between our purchase and our sale of Actaris, we would share the capital gain 50-50 with the management. If these rates were higher, most of the money would go to LBO France and its investors. In general, LBO France asks managers to invest in the operation : this serves to guarantee their involvement. The business plan really has to be devised by them, and represent their convictions. Quite logically, they are substantially rewarded even if their personal investment is small.

From investor to manager

When we bought Actaris for a second time in 2005, the managers who had of course reinvested in the preceding LBO and cashed in a new high capital gain. That allowed them to buy close to 40 % of the equity alongside LBO France.

This time, we devised an expansion strategy for Actaris. We felt that the meter market in which Actaris was involved presented extraordinary expansion possibilities throughout the world in the field of energy in 2005. Therefore, our strategy this time was based on technology and international growth. We can now see that, thanks to investments made, especially in Asia, Actaris is able to benefit from the growth in this sector. It shows that LBO companies are capable of making strategic changes of direction and can be real instruments for growth and a way of helping management to make its decisions.

This example also shows the LBO model is extremely efficient compared to the stock market model. It is therefore easy to understand why there such a huge migration of funds towards private equity companies, and, at the same time, a strong movement of the best managers from quoted companies to private equity companies, and especially those operating LBOs.

It is therefore not simply a case of 'squeezing' liquid assets. Contrary to what the Germans say, LBO companies do not function like a swarm of asset-devouring locusts. Nor are they financial gluttons, as they have sometimes been characterised. Actually, the LBO is an extremely efficient model which highlights new relations between investors and managers to the extent where after a few LBOs, managers often have a greater share of the company than the investors.

What is the future for LBOs ?

One might wonder why this industry seems to feed on itself. What are the options when one owns an LBO company ? Should one sell to a competitor, or float the company on the stock exchange, or sell to other financial interests ? With ever-increasing ratio rates, there appears to be a tendency for fund managers, who are essentially one's colleagues, to buy one's assets. This is acceptable, at least for the time being…

What are the dangers ? With free cash flow ratios of one to ten, the greatest danger would be a recession. The company's cash-flow would then no longer be at the level envisaged by the business plan, and could no longer pay the interest on the debt. Another danger could be the result of a badly designed business plan : there are 4 % to 5 % failures.

The trend is towards LBOs which handle increasingly large sums of money. For example, it was rumoured that KKR wanted to buy Vivendi for 50 billion dollars in November 2006 : this would be the highest ever amount handled in this sector. There are other examples : Cerberus Capital Management bought Absa Bank for 4.2 billion dollars ; PAI Partners sold Vivarte (formerly André, the shoe retailer) to the Canadian fund Charterhouse for 3.5 billion Euros having bought it two years ago for 1.5 billion Euros (including debt). If the market were to slow down now and at the same time interest rates were to rise, there would be bankruptcies and the whole industry would fall apart. As the asking prices increase, the risks taken by investors become greater.

Are LBOs moral ?

There are some who are worried by this situation and raise objections to the amounts which are paid. It is true that everybody is getting richer. The LBO firm can command colossal fees or make the acquired company pay the costs of the bureaucracy for the LBO operation, levying several million Euros. Similarly, partners in the management company receive profit shares which are excessive. In addition, the level of debt of these companies is constantly increasing while the rate of equity contribution is falling. Managers are also paid colossal salaries. Frequently an LBO is accompanied by a restructuring plan, and redundancies are created in order to improve the balance sheet and statement of income ; staff and trade unions can sometimes be hit very hard. Countries such as Korea and Germany have even raised the issue of their national interest in the face of enormous funds taking over assets which are considered to be strategic.

But, at the same time, how should one control the enormous volume of liquid capital which is circulating freely around the world and which, when opportunities arise, can be invested in France, or in a British company, or in China ? How can one possibly oppose a system which ultimately results in improved company management, a sizeable production of wealth, and an impressive return on investment and taxable results ? Furthermore this industry is in the process of spreading to India and China, and it is noticeable, for example, that there are an increasing number of family-run companies in India which are being taken over by Indian private equity funds.

It is therefore difficult to assess the situation. The SEC (Securities and Exchange Commission) and its French equivalent, the COB (*Commission des opérations de Bourse*), are investigating the problems raised by LBOs, especially the extraordinary accumulation of wealth made by investors, managers and banks, but they still have not produced regulations for appropriate intervention.

I shall end this talk on the fundamental characteristics of LBOs with a final example. I mentioned the PAI (PAI Partners : formally Paribas Affaires Industrielles) fund which bought Vivarte for 3.5 billion Euros. Two years after the purchase, having more than doubled the cost price, the fund manager pocketed 20 million Euros when it was sold. The CEO of Terreal received 18 million Euros when his company was sold having been bought eighteen months earlier by a fund. In the case of KKR / Wendel, Wendel floated the Legrand company for 7 billion Euros and the two hundred managers received 350 million Euros, the majority of which was divided between the twelve board members.

From these examples, it is obvious that these situations are quite extraordinary. Let me add that one of the reasons why these LBOs produce such exceptional results is that when one is a manager in an LBO, one is much less resistant to change !

Thus, in the case of Actaris, when this company was bought from Schlumberger and the managers became potential owners, their approach changed radically. We sold a small service subsidiary for 200 million Euros which they had considered as core business when they were at Schlumberger. The day they became manager-owners of the LBO, they told themselves 'After all, if this enables us to pay off a large part of the debt without affecting the core of our business, why not ?' And they made a great sale ! Furthermore, they thought they had wonderful factories and very well managed workshops. We brought over a Japanese team to assess their situation from a different angle : once again, they changed their thinking.

Finally, when trade unions can be shown the potential for improving salaries and bonuses for the management and for the entire staff, thanks to better management, this can be very persuasive in changing their way of thinking.

I hope I have convinced you that LBO companies are not just cost killers which they are accused of being, but that they are important engines for change.

DISCUSSION

The prey, the hunters and the beaters

Question : *How does one spot potential acquisitions and what are the criteria which make a company 'good prey' ?*

Noël Goutard : There are plenty of beaters, such as the Rothschild Bank and many others. Companies which are likely to be the prey include the non-strategic subsidiaries of important groups ; companies which have bad results, but which have the potential to recover ; a quoted company whose shareholders want to withdraw from the financial market ; companies which the share-holder is ready to sell, and whose managers have an ambitious plan but lack the necessary capital ; a family-owned business with a succession problem. In general, these are the categories which are identified by banks which inform us, in return for a commission.

What factors determine the price or the desirability of an acquisition ? Clearly, the capability of the company to make cash available is important, and yet, I have noticed that LBO companies are increasingly employing high-flying managerial teams and analysts. As a result, the search for acquisitions intensifies and their cases are studied with more optimism because the LBO teams are paid on commission. Five years ago, a case followed had an extremely rigorous screening process. Today, one prefers to look at the positive points of the *case*. Management companies take more and more risks, people pay increasing sums of money, and this may contribute to the bubble in this sector. The failure rate, which was 3 % four years ago, is today between 4 and 5 %.

Q. : *In your case, when you launch an LBO, is it because you know the sector well, or because you know the management, or do you launch LBOs in sectors which are unknown to you ?*

N. G. : I ask myself extremely simple questions. Do I understand the industry or the business ? I have invested in clinics as I understood how they worked. Is the management good ? I invested in these clinics not only because the surgeon/manager knew his job but because he also had an exceptional sense of management and finance. Thirdly, is it certain that this venture will produce cash ? These are the three rules which I usually apply, but I remain very selective and very careful in my choices.

Q. : *Is the fact that you are an industrialist an advantage in the way in which the recovery of a company is carried out ?*

N. G. : When you are a partner in a fund management company, as I was at LBO France, you do not manage 'hands on'. My colleagues and I visited only once a month the company because we had a competent management team. This is an essential factor in an acquisition.

Q. : *Why are intermediaries paid so much, and how does one avoid disputes concerning the accuracy of financial contributions ?*

N. G. : There are banks and intermediaries which are very efficient at sifting through information and in finding new opportunities. They are specialists and sources of very accurate information. Every week, we examine various files we receive. If one file catches our eye, and if we are the only LBO company in the deal, it is worthwhile to pay the intermediary substantial fees when the transaction is completed.

Q. : *Does a company whose assets are for sale always find a buyer ?*

N. G. : There is such a wealth of available funds that practically every company will find a potential buyer. One of the attractions of an LBO is to make companies 'liquid', and to encourage the recovery and the improvement of assets which have often been neglected. The cycle of successive improvements means that the companies become remarkably efficient across the world. It results in an exceptional co-operation which explains the spectacular increase in financial performance.

Managing excellence

Q. : *By comparison with other systems which stimulate managers, such as the principle of good governance, the EVA* (*Economic Value Added*), *or stocks options, what is the advantage of the LBO ?*

N. G. : From experience, I know that it is very different. The growth of stock options is linked to the ups and downs of the stock exchange. Unpredictable share prices mean that the end result and the effort involved are not related, whereas with LBOs, the company in question is not quoted on the stock exchange, and thus there is a direct link between the value of its management, the results and the incentive which one draws from this result. It is undeniable, direct and tangible. The LBO is a sprint which lasts four or five years : the length of time until the company is sold is short and the rules of the game are clear and well-known.

Q. : *What is the tax advantage for investors ?*

N. G. : It is complicated ! As far as the investors are concerned, there is, of course, the rather low taxation of capital gains. There is also a specific system which is called tax integration. In this system, the holding company which possesses the shares is transparent with respect to the dividends received from the managed company. The holding company's profits are taxed only after the debt interest is paid.

Q. : *If there are excellent managers making returns on the rate of investment of 22 %, is there not also a place for managers who make returns of 12 % ? How come this market has such a wide range ?*

N. G. : Today, managing a business is difficult. The managers are so well paid because they are a rare commodity as fewer candidates are willing to incur the more and more legal, social, political and security risks in different countries. Secondly, the important issues in company management have become so complex because of technology +and globalisation that there are very few people who are successful in this complicated environment. These factors are magnified in an LBO company which has to win a sprint race and has to make sure it chooses the best runner.

Q. : *Do managers run the risk of favouring their own short term interests by not focussing on the quality of the subcontractors, for example, or by neglecting R&D ?*

N. G. : LBO companies are extremely careful to preserve the long-term interests of the companies they manage because they cannot allow themselves to sell goods which may have lost their value 'on their watch'. One therefore has to make sure that the managers do not sacrifice the long-term essentials such as R&D, investment and globalisation in favour of instant profits.

Q. : *Do the managers play a role in negotiations ?*

N. G. : Managers can act as referees. Often the manager makes the choice between one fund and another. In the Actaris case, the shareholders initially selected an English fund, but the managers preferred LBO France and they prevailed. The first important factor in a negotiation is to be certain that one has the backing of the managers. Negotiations will be more successful with the share-holders of the targeted company if the managers are actively involved. Furthermore, there is nothing a fund hates more than buying a company and having to change the managerial team. One works with managers to establish a credible business plan and so one wants to be able to count on people who get themselves involved. In practical terms, one has little choice but work with the team which is already in place.

Q. : *Do you ever resort to advanced audits to make sure that the company is obeying the rules and that it appreciates the potential opportunities, particularly with respect to R&D, or do you work with the management which already exists ?*

N. G. : When it is an important investment, there is inevitably a strategic audit whose technological assessment is a determining factor. One cannot rely solely on what management says. Obviously it is in management's interest to show you an upward curve for results and a strong growth potential. Hypotheses about the market and technology must be checked. The banks require it as the stakes are so high. Consequently they seek to protect themselves by asking for an audit.

Q. : *There are sometimes negative factors in these operations. You mentioned the pressure from cash. It is an impenetrable world where there are several hundred employees, the same management companies, the same banks, and where information can be manipulated. You also mentioned excessive payments made to certain intermediaries, but it is sometimes difficult to know the precise profitability of the operation.*

Q. : *The society you describe is a bit like a community in which there are villages with farmers and groups of looters who come regularly to take the harvest, sometimes even at the wrong time of year. There is violent fighting between these looting groups about the best moment to come to pillage the harvest. Globally speaking, one may well ask oneself whether this helps productivity.*

N. G. : It is true that private equity companies are compared to locusts which devastate harvests. But in fact this is not the case. World growth is attributable to this substantial volume of liquid assets. These companies stimulate considerable improvement in management and have a very efficient and selective effect. Like any selection, this may include elements which are questionable and there may be outcasts, but I think that this model is more creative than the hedge fund model because money is systematically reinvested. I also think that it is important that managers can become owners of their own company. The LBO is a positive way for important groups to dispose of non core assets. One can also suggest solutions to family-run companies which have problems transferring the business to future generations. Today, practically any company in the world is capable of finding a solution with help of a fund company. Do not forget that not so long ago, France was suffocated by the lack of available liquid assets.

Q. : *Can a company permanently cope with such pressure ? Is the LBO a stimulus to get things moving or is it a long-lasting state ?*

N. G. : It is not a permanently frozen state because a company in an LBO may develop, for example, if its managers become owners or if it is floated. It may also evolve over a series of decades through a succession of LBOs and by remaining under the supervision of the fund company. However, the sprint race – the 100 metres – only lasts four to five years in general.

Q. : *It is not only a different state of mind. I think that the working conditions are much more agreeable even if one works longer hours in a large group.*

N. G. : When I worked for Schlumberger and I managed Actaris in the 1970s, I was asked to impose a budget on the company. Today, the business plan to which the share-holders, managers and bankers agreed is working very well because the managers, who put it into practice, succeed not reluctantly, but because they feel they own it.

Stock exchange or cash ?

Q. : *Is capital risk adjusted more and more profitable given start-ups ?*

N. G. : You cannot ask an investor to go for a drink if he's not thirsty ! Large fortunes tend to share out their funds between capital investment in the form of LBOs, and capital risk, preferring the former.

Q. : *Is it an advantage for an LBO company to be the only company involved in negotiations as well as in payment ?*

N.G. : This is not what happens in practice. The calls for tender take place confidentially : you are handed a file and you are informed that the proposal has been passed to other funds and that at a set date you should send an offer in the form of a letter of intention. Then you are told if you are in the running or not. This is a bid for which essentially you pay nothing ; the opposite might be counter-productive. In this type of bidding, the financial elements are not the only criteria. Several factors enter into the equation including the reaction to the business plan and to the future projects, management's reaction, the nationality of the LBO company, especially when the company in question involves strategic-issues (such as defence contracts), potential personality conflicts, and so on.

Q. : *What is your opinion of LBOs where the debt repayments are based essentially on the transfer of assets ?*

N. G. : You can easily receive a proposal for the purchase of a company where you do not see the operational cash-flow, but where, on the other hand, you can see the possibility of breaking up the assets. This is the case, for example, in property companies where the dismantling of the assets and the resale of their components is more lucrative than their financial performance.

Q. : *How does one seek out, recruit and manage managers when everyone in France knows that very good managers are hard to come by, partly because failure is penalised much more in France than in the United States for example ?*

N. G. : I think that the managerial spirit is taking hold in France. There are more start-ups and more investors who are ready to get themselves involved in these companies. The question is what does one have to do to make managers become good managers. Let us simplify things. Firstly, one has to establish a strategy which is convincing and which is focussed on the market. People from both ends of the hierarchy are extremely attentive and aware of this compatibility with the market. Secondly, the objectives have to be more ambitious ! In France, unless you strongly challenge people, the results can be mediocre. Thirdly, as well as trust, there has to be fairness and discipline. In other words, trust, autonomy and reward. Those who do not adhere to the rules simply do not belong. Everyone understands this and generally conforms. Everyone knows the rules of the game and knows what he has to do : there are no surprises. Managing people by making them fall into traps is a serious mistake.

Q. : *As the image of this activity is sometimes tarnished and judged from its financial angle, should not the LBO be better understood and controlled ?*

N. G. : By definition, it is not possible for governments to intervene as this is private equity, private investments. The day the minutia of the regulations become involved, you lose the strengths inherent in LBOs, in other words, their speed, flexibility and the fluidity of capital. This is the reason for criticism because everything takes place outside the public sphere, in secret. In quoted companies, compulsory and duly regulated publicity accounts for three-quarters of the managers' time. However in France, anything which is private is reason for suspicion !

Q. : *When you were president of Valeo, you were already very interested in cash-flow…*

N. G. : Just that !

Q. (the same) : *… and on the other hand, you were much less interested in debt. Have you changed your mind about debt ?*

N. G. : It is extremely simple : when I was president of Valeo, my eyes were riveted on the stock market, like the share-holders, and I knew that the factor which motivated the stock market price was my financial results. If I was in debt, my financial results were affected by the interest payable on the debt and the share price dropped. Therefore, I avoided debt in order to produce the best financial results possible. My stock market price increased from 20 Euros to 100 Euros and my market capitalisation went from 1 billion to 20 billion Euros. I told myself that this method worked !

I changed jobs and in my new profession in LBOs, the greater my debt, the less tax I pay and the greater capital gain I make ! Therefore, I have changed my way of thinking !

Q. : *This talk is entitled « LBO : when cash is king ». Do you agree with this ?*

N. G. : Cash is the common denominator. When I talk about cash, everyone understands. When you talk about the balance sheet, everyone thinks that you are manipulating the numbers, whether it is trade unions or stock exchange dealers, whereas cash is tangible, it is on the table. There is either credit or debit, debt or no debt ; it is like the family budget : everyone understands it. Cash effectively represents a kind of tyranny which is imposed on management companies by investors who expect cash in return. However, there must also be fun : to enjoy oneself and sleep comfortably at night, you have to devise strategies, move forward and forge ahead.

Presentation of the speaker :

Noël Goutard : currently president of NG Investments (a capital investment company which he created), and administrator of several companies. Between 2000 and 2005, he was a partner at LBO France, a private equity firm which experienced marked growth during this period. From 1987 to 2000, he oversaw development at Valeo as chairman and CEO. He transformed the company into a world force in the automobile equipment market. Prior to this, he was managing director of Compteurs Schlumberger, Chargeurs Group, and Thomson. Having started as a trader on Wall Street, his professional life, spanning forty years, has been marked by a successful career in the world of industry and finance. Author of *L'outsider* (pub. Village Mondial).

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