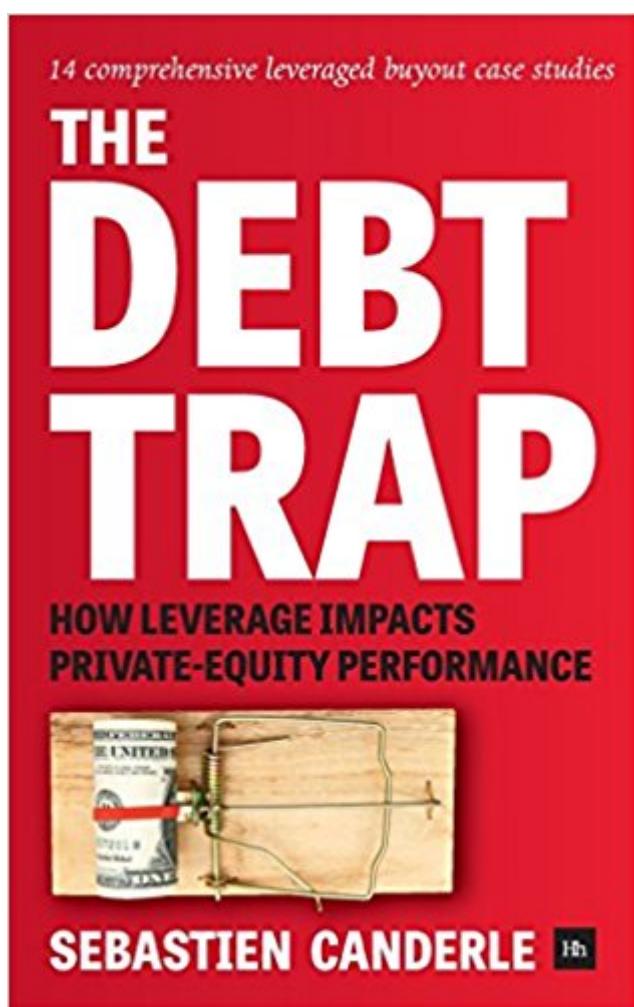


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The Debt Trap: How Leverage Impacts Private-equity Performance



Synopsis

This is the inside story of private equity dealmaking. Over the last 40 years, LBO fund managers have demonstrated that they are good at making money for themselves and their investors. But when one looks beneath the surface of the transactions they engineer, it is apparent that these deals can, at times, go spectacularly wrong. Through 14 business stories, all emanating from the noughties' credit bubble and including headline-grabbing names like Caesars, Debenhams, EMI, Hertz, Seat Pagine Gialle and TXU, *The Debt Trap* shows how, via controversial practices like quick flips, repeat dividend recaps, heavy cost-cutting and asset-stripping, leveraged buyouts changed, for better or for worse, the way private companies are financed and managed today. From technological disruption in the worlds of music recording and business-directory publishing to economic turbulence in the gambling, real estate and energy sectors, highly levered corporations are often incapable of handling market corrections when debt commitments start piling up. Behind the historical events and the financial empires erected by some of the elite private equity specialists, these 14 in-depth case studies examine how value-maximising techniques and a short-cut mentality can impact investment returns and portfolio assets. Whether you are a PE practitioner, investor, business manager, academic or business student, you will find *The Debt Trap* to be an authoritative and fascinating account.

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Customer Reviews

"...The Debt Trap is a very valuable addition to the inordinately small body of literature on the

subject of private equity...By breaking down the asset class's methods through relatable examples, Canderle has opened the door for further investigation into the opaque world of private equity." --A Darragh Riordan, *Real Deals*"Written for an audience with a working knowledge of finance, *The Debt Trap* dissects the dealmaking that undergirds leveraged buyouts and provides an essential road map to the many ways that this has changed since the 2008 financial crisis. Detailed examinations of high-profile buyouts demystify the excessively risky and opaque means - new and old - that private equity firms use to acquire companies. *The Debt Trap* should be required reading for the staff and trustees of institutional investors, and for professionals working at lending institutions, but the clear writing and compelling case studies make it appealing to a much wider audience." --- Eileen Appelbaum, Senior Economist at the Center for Economic and Policy Research, and author of *Private Equity at Work*"Sebastien Canderle has written a genuinely compelling book that raises crucial questions about modern-day PE investment practices. *The Debt Trap* is a thoughtful and stimulating work that helps to frame the debate on value creation in the world of alternative finance." --- Pablo Fernandez, Professor of Financial Management and PricewaterhouseCoopers Chair of Corporate Finance at IESE Business School"Sebastien Canderle's book should be at the top of recommended reading lists for every finance course. It is a skilful critique of the fast-paced private equity industry. Drawing on a vast amount of research, *The Debt Trap* gives fascinating insights into some of the most illustrious leveraged buyouts, which will help to improve our teaching of finance and contribute to a sounder financial industry. For that reason it deserves to be read." --- Jacques Regniez, Professor of Economics and Finance at the State University of New York"Private equity has thrived on debt. Excessive debt can harm companies. This important book shows how and why thanks to a rich set of in-depth case studies. It is essential reading for practitioners and students of private equity." --- Francois Degeorge, Senior Chair of the Swiss Finance Institute and Professor of Finance at the Universita della Svizzera italiana"Private equity plays a crucial role in modern economies. What Sebastien Canderle explains is that the sector's performance depends on a very specific set of value triggers, first among them the optimal use of leverage. Get the mix wrong, however, and as the book's well-researched case studies demonstrate, even the most experienced fund managers can come to regret their foray into leveraged buyouts. *The Debt Trap* is filled with grounded analysis and is an authoritative book for PE practitioners and scholars alike." --- Franklin Allen, Nippon Life Professor of Finance and Economics at the Wharton School of the University of Pennsylvania, and Brevan Howard Centre director at Imperial College in London"A valuable contribution to the literature on private equity, *The Debt Trap* is an absorbing study of why leverage is a two-edged sword and should be used with

utmost caution. The book is an important read for anyone involved in the private equity world or even the finance world at large." --- Jacob Wolinsky, CEO of ValueWalk "Call it 'the art of the leveraged buyout'...Canderle explores some of the more controversial business strategies such as quick flips, repeat dividend recaps, heavy cost cutting, and asset stripping as related to leveraged buyouts...the author brings these investment strategies to life through real-world application--offering an up-close view of private equity deal-making. The text is a great resource for PE fund managers and business people alike." --- Wharton Magazine "Not only does the book offer plenty of warning for private investors about investing in IPOs (Initial Public Offerings) where the company floating is backed by a Private Equity (PE) house, but also offers institutional investors plenty of evidence of what can go wrong with companies saddled with the exorbitant debt an LBO can bring. We're also taken on a tour of the most favoured practices of PE owners when trying to extract the maximum return on their investment. What I most like about this book is its broad scope in explaining the social effects of this kind of financial engineering." --- Owen Jones, Fidelity

Sebastien Canderle has more than 20 years of experience in the consulting and financial sectors in New York and London, including as an investor for various private equity firms. He is also the author of 'Private Equity's Public Distress', a book covering the impact of the financial crisis of 2008 on the buyout industry, and has been a contributor to several financial blogs as well as a business school lecturer in private equity.

Barbarians at the Plate: Batter Up! As does fire the body warm and bread help to bake, so, too, is it capable of engulfing and destroying all around it. Such it is with debt which inflates the balance sheet, but, applied to excess, can impair or even cripple it, exacting much for the few, and little for the many. This is the central theme of Sebastian Canderle's *The Debt Trap*, an examination of private equity deals through the prism of fourteen case studies taken from recent financial history. Perhaps they should be acts in a long running drama. Written for the MBA student, but equally suited to the laity without too much effort on the part of the latter, the author's narrative is at once instructive and cautionary. It is a worthwhile contribution to the study of an oft touted and controversial asset class. Canderle lets the facts and circumstances do the talking. In his estimation, the reader will need to draw her own conclusions as to the merits and demerits of the discipline. At the very least, it would seem that the truth about private equity's intentions lies somewhere between opprobrium and encomium, though the author at times is unsparing in his criticism of the industry's shortcomings. Private equity is as much an investment strategy as it is an asset

class. As such, it is multifaceted, often subject to the whims of human emotion, something that the case studies bring out with a high degree of granularity. The book assumes knowledge of the rudiments of finance, but is not completely inaccessible to those who lack it. On the contrary, it encourages the reader to learn more. Academics and financial writers could take a page from Canderle's book...literally. On the surface, the objective of private equity is simple. Borrow money, buy a company, manage it to be more efficient and profitable, then sell it. Repeat. While it endeavors to deliver value, it can destroy it as well. Private equity often appears to be an extractive industry, taking as much value out of the business as quickly as possible with little regard for the longer-term viability of the enterprise. A surfeit of leverage can lead to zombie companies kept alive through loan forbearance and poor regulation. Market driven regulation may be better. Private equity claims ingenuity, yet as the book narrates in exhaustive detail, it often runs riot. Indeed, leverage often induces moral hazard with fund operators working outside the lines and just beyond regulatory remit. Solve for maximum greed as it were. At once surprising and disturbing is the all too common lack of formal training amongst fund managers who seem to learn the business on the fly. Avarice, it seems, is good or, at the very least, alive and well. In truth, malfeasance often operates with impunity. Managers exact their cut, pawns in the leverage game, CEOs and top brass get sacked. Shadow capitalism runs amok for the benefit of the few in the land of the fee. Its nefarious reverberations on companies and the economy notwithstanding, the practice is far more nuanced as the case studies in *The Debt Trap* make clear. One would not think a book on the arcana of balance sheets and capital structure as they relate to firm buyouts to be a particularly interesting read, yet Sebastian Canderle makes it so. The table of contents alone reads as much like a series of movie trailers as it does introductions to a complex investment process. The chapters enumerate LBO techniques, yet often appear to be as much a taxonomy of bad deeds. The text elucidates investment legerdemain that general partners often employ to gussy up their performance and close deals. It equally informs the reader that private equity is more variegated than black and white. A primer for those not completely current on leverage, the first chapter foretells the remainder of the book without giving the plots away. Worked examples of private equity math introduce the reader to the basics of leverage's effect on returns. A brief lexicon is useful particularly for the uninitiated. Indeed, Canderle entices the reader, encouraging her to read on. The author's style is erudite, yet he felicitously phrases the narrative to make what could otherwise be a dry volume into an engaging read. Private equity is dynamic. Enjoy this series of financial short stories. Perhaps truth is at times stranger than fiction.

As a hedge fund manager, I am used to press criticism regarding my industry's uneven performance. But private equity also has issues, judging from this book's case studies. The cases cover many companies across geographies (the US and European markets), industries (leisure, media, retail, real estate, chemicals, industrials, business services) and transaction types (secondaries, take-privates, PE-backed IPOs, PIPEs, repurchases). I found the issue of technological disruption in the EMI scenario compelling. Albeit quite technical in parts, the book is easy to understand. We forget how prevalent private equity has become. These investors have their hands in so many parts of the financial sector, including in credit, property and turnaround situations that we can all benefit from learning more about them. Only problem with this book is that it is pricey. I managed to get myself a cheaper copy straight from the publisher.

It is hard to go through this book and to feel that PE fund managers actually know what they are doing. Even though the author points out that we should not reach conclusions from just reviewing the 14 case studies he covers, I can't quite understand why regulators are not all over this industry and its major participants. If KKR, TPG and Apollo behave that way and can get away with it, what hope is there to ever get the sector to behave ethically? The chapter on Caesars is edifying. To call that asset-stripping is an understatement. The court proceedings are still ongoing, eighteen months after the business declared bankruptcy! No one can actually make sense of what went on during Apollo and TPG's period of ownership. This book is a good summary of what capitalism has become: a free-for-all feast that only benefits the rich and powerful.

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