



IPO Modeling

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What Is An IPO?

IPO = Initial Public Offering

Private company offers shares to the public

Raises capital to fund company growth

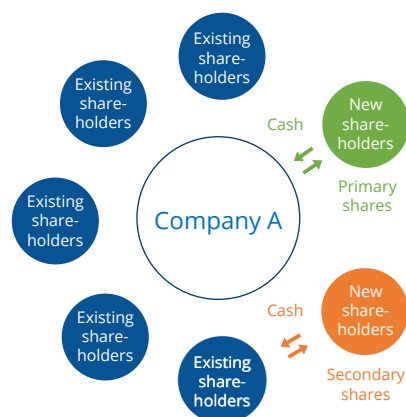
Private investors can exit and realize gains

Allow new shareholders to invest

Potentially millions of new shareholders

Investment banks aid the company in marketing, pricing and selling the new shares

IPO Primary vs Secondary Share Sale



IPO of primary shares

New shares issued to new shareholders

Raises cash for Company A

IPO of secondary shares

Existing shares sold by existing shareholders

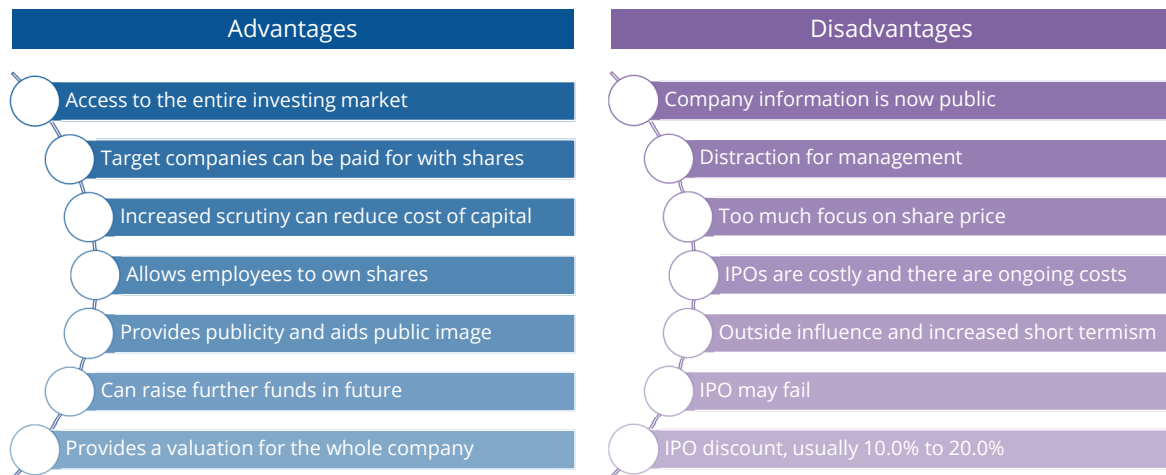
Allows existing shareholders to exit

Allows new shareholders to enter or allows other existing shareholders to increase their investment

Can follow up with block trades

An IPO can include both primary and secondary share sales

Why Do An IPO: Advantages And Disadvantages

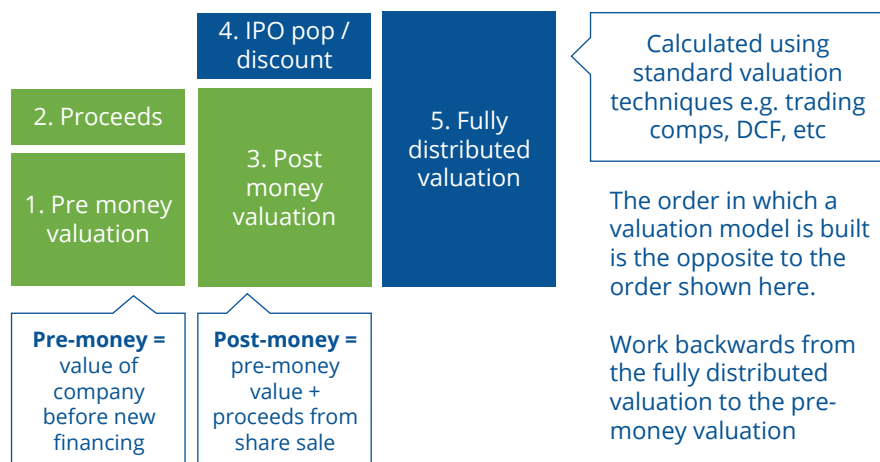


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IPO Pre And Post Money Valuation

There are many valuation terms used in IPOs

- Fully distributed valuation
- Post-money valuation
- Proceeds raised
- Pre-money valuation



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IPO Pre And Post Money Valuation: Order Of Modeling

Use forward multiples and expected earnings of company post IPO (including effect of IPO proceeds invested)

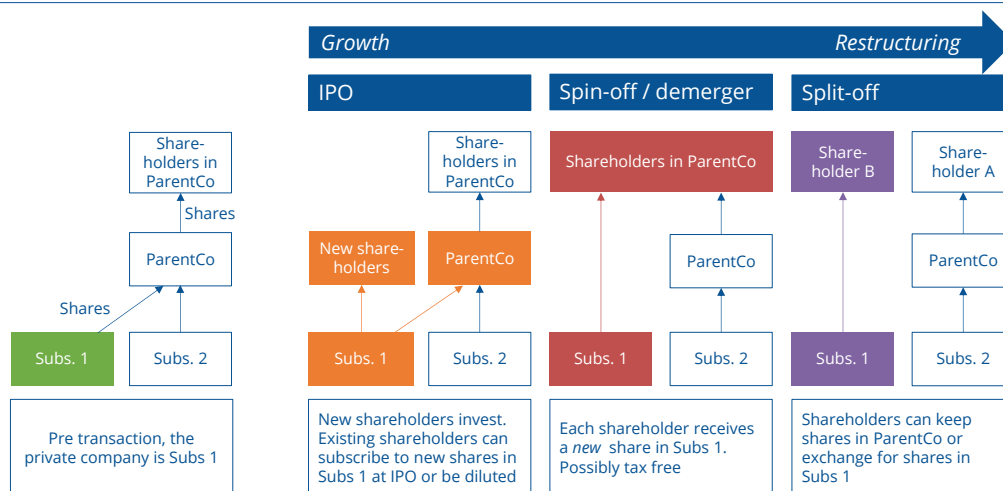
A company is planning its IPO. It has 350.0 existing shares and will issue 50.0 new shares. Work backwards from fully distributed value to pre-money value

1	FY1 PE Multiple	10.0 x	
	FY1 Net income	192.0	
	Fully distributed valuation		1,920.0
2	IPO discount	20.0%	
	Post-money valuation (implied offer price valuation)		1,600.0
3	Shares outstanding post IPO (350.0 + 50.0)	400.0	
	Implied offer price per share (1,600.0 / 400.0)	4.00	
	Primary shares issued	50.0	
	IPO proceeds, gross (4.00 * 50.0)	200.0	
	Fees 5.0% of IPO proceeds (5.0% * 200.0)	(10.0)	
	IPO proceeds, net of fees (200.0 – 10.0)		190.0
4	Implied pre-money valuation (1,600.0 – 190.0)		1,410.0

Discount calculated as % of post-money value, rather than % of fully distributed value

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Different Transactions – IPO, Spin Off And Split Off



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Accounting For An IPO

From the parent company's perspective, an IPO of a subsidiary leads to a minority stake being sold. As the subsidiary remains in the parent company's control, the subsidiary remains consolidated with the parent company, and an NCI is established

ParentCo sells 20.0% of its shares in SubCo in an IPO for 30.0m cash. SubCo has 70.0m of net assets. Assume 30.0% tax rate			
	Group pre IPO	Adjustment to Group	Group post IPO
Assets	500.0	25.0	525.0
Total Assets	500.0		525.0
Liabilities	250.0		250.0
Common stock and APIC	50.0	11.0	61.0
Retained earnings	200.0		200.0
Non-controlling interest	0.0	14.0	14.0
Total liabilities and equity	500.0		525.0
Net assets sold	$20.0\% \times 70.0 =$	14.0	
Gain on sale post-tax	$(30.0 - 14.0) \times (1 - 30.0\%) =$	11.0	
Cash proceeds post-tax	$14.0 + 11.0 =$	25.0	

The mechanics differ slightly depending on whether the IPO involves:

Primary shares issued, meaning new shares are created, *increasing the total share count* and diluting ParentCo ownership

Secondary shares issued by the ParentCo, meaning no new shares are created, and *no increase in the total share count*, but does reduce ParentCo ownership

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EPS Impact Of An IPO

The ultimate EPS impact for ParentCo depends on how it invests the cash proceeds from the sale of shares in SubCo

EPS impacted by:

Return on cash proceeds are added to net income

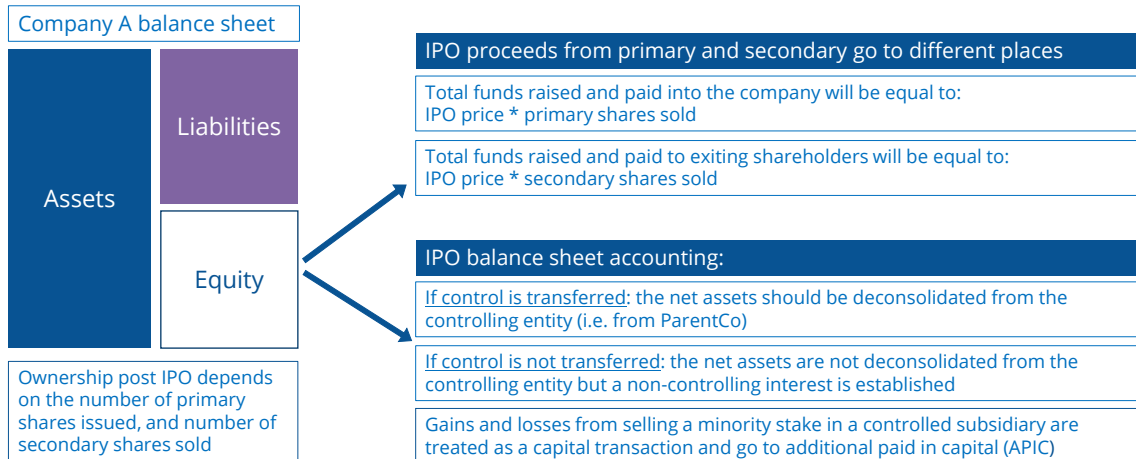
Earnings attributable to NCI are subtracted from net income

Number of shares impacted by new shares issued

If post IPO EPS is accretive, the IPO is a success

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Primary and Secondary Share Issuance Combined



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Appendix: Balance Sheet Accounting Of A 100% Spin-off

Impact on ParentCo. Transfer of full control and ownership of Subs 1 to its shareholders

	Group pre spin-off	Subs. 1	Adjust. to Group	ParentCo post spin-off
Assets	500	100	-100	400
Liabilities	250	30	-30	220
NCI				
Common stock & APIC	50	20	0	50
Retained earnings	200	50	-70	130
Net assets spun off		70		

No non-controlling interest as full control is transferred, leading to full deconsolidation

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Appendix: P/E Ratios

If the Sale P/E > Reinvestment P/E, the equity sale will be accretive:

Sale P/E = Sales proceeds/Net income sold

Reinvestment P/E =
1/% Reinvestment return