Financial Modeling and Due-Diligence for
Corporate Acquisitions, Greenfield and Brownfield Projects

Corporate management is often focused on short-term revenue growth and on "making things happen", more than on carefully evaluating future cash flows, debt service and returns to shareholders. Corporate lenders and equity fund managers are often more focused on transactions booked during the current performance evaluation cycle, than on the medium term risks of those transactions.

The success or failure of corporate acquisitions, Greenfield or Brownfield projects depends on many interactive factors. One of the key factors is timing. Is the acquisition or project launched at the top of an economic cycle, at the bottom, or somewhere in-between? Is the price or cost too high? Will revenues grow or stagnate? Other key success or failure factors include:

Projected Revenues and Operating Margins:

What are the projected revenues and operating profit margins to be generated from each business segment? What are the trends in each business segment, and how will they affect the overall cash flow over time? What can or will be done pro-actively to affect them? Is the business mature and broad-based, or is it rapidly evolving, trendy, or soon to be obsolete?

Leverage:

How is the acquisition or project financed? Is there too much debt to service, or will there be insufficient net cash flow returned to shareholders? Will it be possible for the business or project to generate a sufficient Internal Rate of Return (IRR) on the equity invested? What are the potential impacts of a downturn or an upturn on debt service and on IRR?

Further Considerations:

There are a myriad of other financial and operational considerations that can affect success or failure of acquisitions or projects. Among those that will directly affect financial performance, some of the key factors include:

- Working capital requirements to support account growth.
- New or maintenance capital expenditure requirements.
- Known or unknown liabilities assumed.
- Changes in tax or other regulatory requirements.

Contingency and Risk Management:

During the life-cycle of an acquisition or project, there will always be unforeseen events. Even if revenues and margins are "locked in" by long-term contracts, changes will occur. What contingency factors are built into the financial forecasts? What risk management practices are implemented to identify, mitigate, react to and compensate for risks?

Conclusions:

- Better acquisition or project investment decisions can be made with thoughtful financial modeling, with significant emphasis on contingency and risk planning and management.
- It can be better to decline a marginal acquisition or project than to rush into an opportunity to make this year's compensation targets.
- It can be helpful to have an objective third-party review and model a proposed transaction at an early stage, before committing to a full due-diligence effort, negotiations, legal reviews, documentation and funding.

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