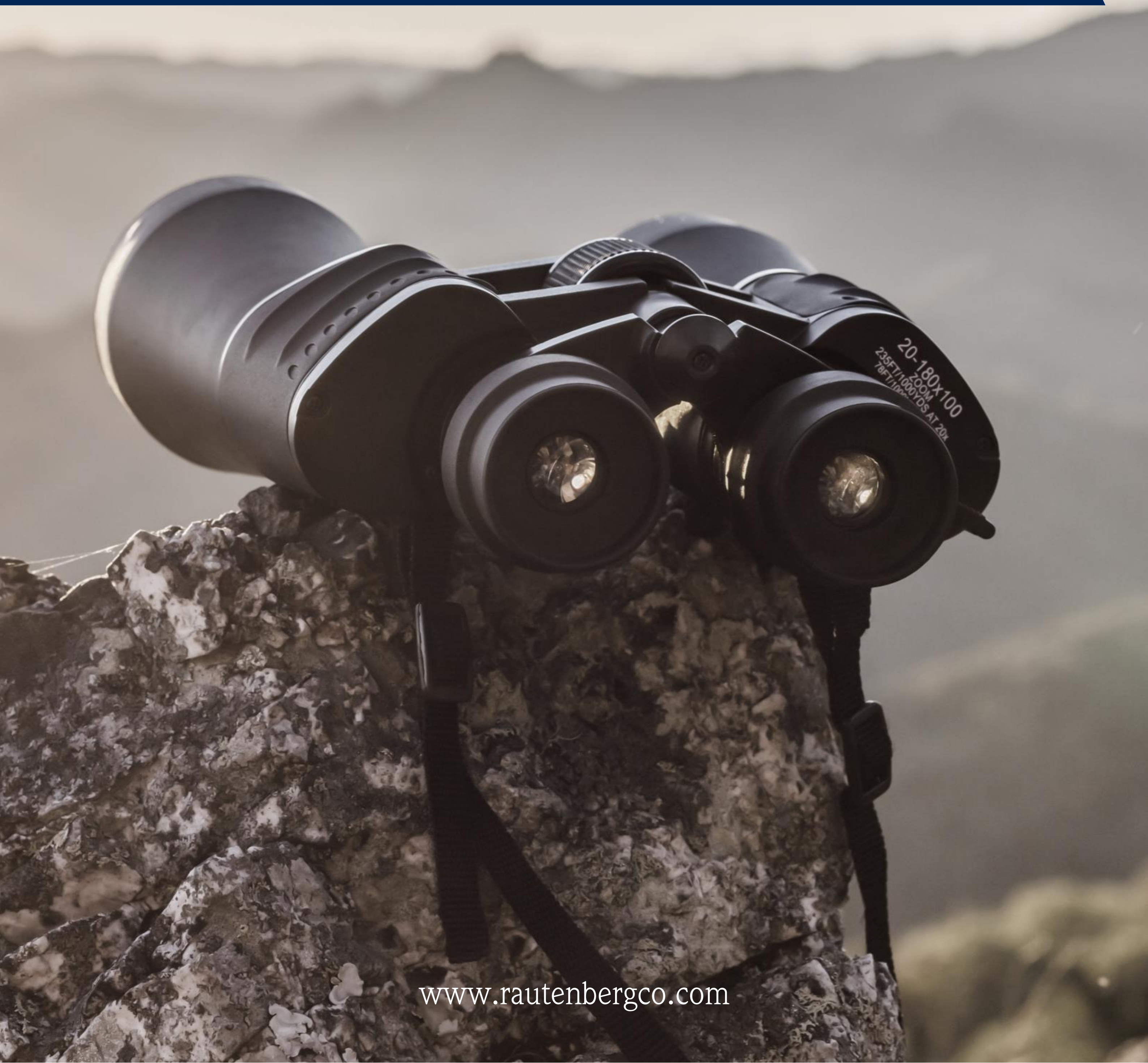
RAUTENBERG
& COMPANY

Commercial Due Diligences

DECISION SUPPORT RATHER THAN TRAVELOGUE!



www.rautenbergco.com

Commercial Due Diligences ("CDDs") are offered by numerous advisory firms in various formats and at differing price points.

According to Arndt Rautenberg and Boris Herzog of Rautenberg & Company, just because it says "Commercial Due Diligence" on the cover, it does not mean that this is what you are actually getting.

Rather than an overload of descriptive graphs and commentary, they firmly believe a CDD should deliver a concise discussion and an accurate assessment of the target, based on sharp analysis and with a clear set of recommendations.

"In God we trust, all others bring data!

We all have encountered such reports before – the business model is "depicted" on the first ten pages, often barely distinguishable from the description on the website or company brochure. Colourful charts with historic revenue and profit lines follow, and with a little good fortune, even a brief description of notable deviations. Next, the report is filled with graphs of the target's budget figures and five pages with roughly sorted quotes from all kinds of industry experts.

This type of document is obviously not very helpful, especially when the CDD report was not only commissioned as a "tick the box" exercise but was genuinely meant to serve as a crucial support for making a complex investment decision. The remarkable circulation of such reports is even more disappointing as there is by no means a lack of good CDD examples.

Based on our experience of dozens of CDD engagements every year, we have formulated five key requirements that at least our Commercial DD reports simply must contain in order to be effective.

OUR 5 KEY REQUIREMENTS

1

ANALYSIS BEATS ILLUSTRATION.

A CDD requires comprehensive and accurate financial and operational data as a basis to derive relevant and reliable conclusions. Internal as well as external data should not just be plotted across a time axis but first and foremost checked for plausibility, analysed, and presented effectively. More often than not, this can be done in two dimensions to focus the reader on key implications of the data set. All data presented should certainly be relevant in terms of value and/or risk, and should be interpreted accordingly.

If the question: “So what does this tell us?” does not have a good answer, the analysis was probably not very relevant.

2

FOCUS IS MORE IMPORTANT THAN COMPLETENESS.

At the beginning of the analysis phase, the DD team needs to develop a clear understanding of the relative importance of all P&L, balance sheet and cash flow levers. “Bridges” and sensitivity analyses are useful tools to achieve this. A comprehensive picture of the target and especially its financial status must be developed during the initial phase – the team however must not “retire” once this has been accomplished but needs to proceed with thorough consideration of the major value drivers and risks associated with a particular target.

We have seen great reports that dedicate two thirds of the content to those 20% of the business plan that truly make a difference. Poor reports simply lack such emphasis and focus.

3

WINDSCREEN VS REAR-VIEW MIRROR.

Just like in a car race, what counts is the next lap ahead. In almost every transaction, the business plan should be the focus of the analysis. While historic data and explanations are important for an assessment, they generally should be no more than an entry point into the evaluation of the target's future potential. The focus on analysing its value creation opportunities and risks is of central importance – what levers actually drive performance, and thus value? What are the real risks limiting the attainment of these objectives?

Per se, it is less crucial how exactly the various plan parameters might develop, but rather understanding **why** they are likely to develop in a particular way. The team needs to understand and question the reasons that drive this development, by assessing the measures and goals defined by management.

SAY IT HOW IT IS.

4

If the CDD report is really meant to serve as a decision support tool, it must provide an honest assessment of the crucial aspects of the target: How realistic is the implementation of a particular measure? How certain is the operational effect it creates? Can this effect really drive the KPI in question and ultimately the financial numbers to the budgeted level? Are the measures sufficient to secure the predicted effect on the business plan?

Past data provides a reference point for these and many other questions but should never be construed as proof. Prerequisites, risk factors and risk mitigation strategies must be evaluated based on their probability and effectiveness. This is where less useful CDD reports frequently use conjunctives on what might happen, serving more to exonerate the authors rather than to advise the recipients. Generally, this is not helpful, in particular when the Info Memo already contains a hotchpotch of company-specific and macroeconomic risks.

IMPLICATIONS FOR VALUE CREATION.

The crucial questions ultimately arise shortly before the team finishes the report – which unfortunately collides with the phase during which reports are typically "quality assured", an activity that mainly involves the responsible partner reworking the action titles. Much more important than this exercise should be interpreting the results of the analyses, and assessing their implications for the value creation during the holding phase of an asset: What do these results mean for the overall assessment of the target, its business plan and the implicit value creation potential? What measures must be taken to ensure that the target actually achieves the plan and the risks remain under control? What does the full value creation plan post closing look like? Is the target's management and the organisation adequately sized and skilled to achieve it? What investment will it require?

And, ultimately: What does all this mean for the ultimate investment decision? A good CDD report needs to give conclusive answers to these questions. In doing so, it will not only facilitate immediate action after closing but ultimately the long-term success of the transaction. A good report should inform and determine the final decision on the delivery of a bid, its aggressiveness and critical conditions attached to it.

5

ONE MORE THING.

It is our conviction that a great CDD mandate actually needs to deliver **two products**:

1. A (bankable) CDD report of course, AND
2. a set of qualitative statements, ideally even recommendations, on a set of topics that are highly relevant to the deal team but not per se a scope item for the CDD report.

Here are some of the questions that we are frequently asked:

1. **How good is management, really, and will they deliver the plan?**
2. **Are there any competency gaps that need to be filled?**
3. **Who must we not lose, and what does this mean for a retention scheme?**
4. **Would we invest our own money into this business …?**
5. **… at the valuation and in the structure on the table?**

The answers to these questions are what really matters, much more than any single analysis.

In summary, a Commercial DD is not rocket science, but considerably more than a travelogue written by a student group about their recent company visit.

LET US SHOW YOU WHAT WE MEAN.

In the complex world of investments, comprehending the essence of Commercial Due Diligences (CDDs) is akin to solving a convoluted puzzle.

A high-quality CDD report is more than just data; it represents a roadmap that guides investment decisions and offers invaluable support to both new investors and management teams.

Join Arndt and Boris as we dive into the depths of a CDD – a tool that transforms raw information into actionable insights, providing the clarity needed to come to a balanced and thus reliable investment decision.

Arndt Rautenberg
Managing Partner

Arndt is the founder and Managing Partner of Rautenberg & Company and heads up our Düsseldorf office. He has vast experience in advising financial investors and their portfolio companies as well as corporations. His special expertise is in strategy development and value creation as well as in corporate finance and M&A.

He started his professional career in 1994 at Boston Consulting Group, after completing his studies of business administration at WHU – Otto Beisheim School of Management and at Georgetown University. In 2000, he and two partners founded a technology investment and advisory firm which they later successfully sold to Sapient, a NASDAQ-listed technology corporation based in Cambridge, USA. After several years as an executive board member of Sapient, Arndt was appointed Chief Strategy Officer of Deutsche Telekom, where he was responsible for both the group's strategy development as well as the portfolio management. Since leaving in 2008, Arndt has focused on advising financial sponsors and strategic investors in all phases of a transaction.

Boris Herzog
Partner

Boris is a Partner at Rautenberg & Company. He is an experienced advisor, focusing on due diligences, strategy development / execution and the development or evaluation of business cases and value creation plans in a variety of industries, particularly digital infrastructure, IT, tech & media as well as services.

After his studies of computer science and operations management at ESB Reutlingen and ESC Lille, Boris started his professional career in 2007 with Arthur D. Little. Over the course of his six years tenure, he led numerous national and international strategy development and performance improvement assignments in diverse industries and conducted various transactions related projects (commercial due diligence, value creation, post merger integration, carve out).

Prior to moving to Rautenberg & Company in May 2014, Boris completed his MBA at IE Business School (Madrid, Spain), where he graduated on the Dean's List honours in 2013.

About Rautenberg & Company

Rautenberg & Company accompanies financial investors and their portfolio companies as well as corporates and medium-sized companies in all phases of a transaction: from initiation and implementation to value creation, as well as the preparation and support of successful sales. The market-leading offer consists of two central components – Strategy and Value Creation Consulting and M&A Advisory – led by an exceptionally experienced and highly competent team.

Contact us:

+49 211 900 999-0

mail@rautenbergco.com

www.rautenbergco.com

RAUTENBERG
& COMPANY

Our Rhine Office
Königsallee 61
40215 Düsseldorf

Our Main Office
Neue Mainzer Str. 52-58
60311 Frankfurt

Our Thames Office
23 Berkeley Square
London W1J 6HE