



Anand Wadadekar

Leveraged Buyout (LBO)

“
The purpose of leveraged buyouts is to allow companies to make large acquisitions without having to commit a lot of capital. In an LBO, there is usually a ratio of 70% debt to 30% equity. LBOs today focus more on growth and complicated financial engineering to achieve their returns.”

This Article has been published in 'Sanhita' A Corporate Legal Magazine by the Pune chapter of The Institute of Company Secretaries of India (ICSI) in May 2007

ABOUT AUTHORS

Anand Wadadekar is MA (Economics), MBA (Finance), AMFI

The views are personal

Leveraged Buyout (LBO) has been in the news recently which said that, Corus an Anglo-Dutch company would be taken over by TATA an Indian company.

Being a relatively new business concept for us, this Article aims to highlight what 'LBO' is all about, its advantages and disadvantages. It cannot be ruled out that, India Inc. may have to see take-overs in the form of LBOs, amidst Globalisation.

What does LBO actually mean technically?

Simply put-it is the purchase of a company by using a small investment and a large loan. The new owner would gain control with a small amount of invested capital because he or she is able to secure a large loan for the balance of the amount needed. A leveraged balance sheet has a small portion of equity capital and therefore a large portion of loan capital.

Leveraged Buyout also called as 'Highly-Leveraged Transaction (HLT)'-occurs when a financial sponsor gains control of a majority of a target company's equity through the use of borrowed money or debt.

Typically, the loan capital is borrowed through a combination of prepayable bank facilities and/or public or privately placed bonds, which may be classified as high-yield debt, also called junk bonds. Often, the debt will appear on the acquired company's balance sheet and the acquired company's free cash flow will be used to repay the debt.

A leveraged buyout is essentially a strategy involving the acquisition of another company using a significant amount of borrowed money (bonds or loans) to meet the cost of acquisition. Often, the assets of the company being acquired are used as collateral for the loans in addition to the

