**CASE STUDY: ALEXANDRIA HOTEL**

**PRIVATE COMPANY LBO**

**TRANSACTION:**

KW Ltd, a Private Equity firm, is interested in buying Alexandria Hotel, a 300-room hotel in South Beach, Miami, Florida. The asking price is $120 million. After few due diligence visits, KW Ltd will need $15 million of renovation to bring the hotel up to today’s modern standards. The purchase of the hotel, the renovation and transaction fees (calculated as 3.0% of total debt raised) will be financed by combination of traditional bank loan, private mezzanine note, and equity provide by KW Ltd.’s Fund II. The Company reported $40 million of Revenues and $20 million of EBITDA (Year 0).

**CAPITAL RAISING:**

**BANK LOAN**

|  |  |
| --- | --- |
| **Amount:** | Based on 3.0x Year 0’s EBITDA |
| **Interest** | SOFR + 4.0% (Assume SOFR is 1.0% increasing 0.5% year 2, 0.5% year 3 and 1.0% year 4) |
| **Term** | 7 years |
| **Scheduled Principal Payments** | Yr 1: $3mm, Yr 2: $4mm, Yr3: $5mm, Yr4: $5mm. Yr5: $6mm, Yr 6: $7mm. Yr 7: The balance (balloon payment) |

**MEZZANINE NOTE**

|  |  |
| --- | --- |
| **Amount:** |  Based on Total Debt/Yr 0’s EBITDA of 5.0x (Including Bank Loan) |
| **Interest** | FIXED 8.0% |
| **Term** | 10 years |
| **Scheduled Principal Payments** | Yr 1- Yr 9= $0, Yr 10: the balance (100% redemption) |

**EQUITY FINANCING**

Equity will be investing the balance of the financing. The minimum expected return is based on CAPM (use Risk Free rate of 1.0%, Hotel Industry Beta of 1.727x and Market premium return of 11.0%. Ideally KW Ltd needs 25% per year Return.

**OPERATING ASSUMPTIONS (Yr 1-10)**

|  |  |
| --- | --- |
| Revenue | 5% growth |
| Cost of Revenue | 35% of Revenues |
| Operating Expenses | 15% of Revenue |
| Depreciation | 3.0% of Revenues |
| Amort of Fees | Use 7 years |
| Tax Rate | 22.0% |
| Working Capital Exp | 1.0% of Revenues |
| Capex | 3.0% of Revenue |

**ASSIGNMENT**

1. Prepare the Transaction Sources & Uses and calculate the WACC
2. Construct the Debt Schedules
3. Build a DCF
4. Calculate the Equity Return Analysis (Terminal Values based on EBITDA multiples and Perpetuity method)