USC Marshall
MASTER OF MEDICAL
MANAGEMENT PROGRAM

USC Marshall Master of Medical Management - Cohort 12, March Session
Financial Strategy Schedule

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Learning Objectives

We will review value creation concepts and frameworks. The material and discussion will focus on gaining tools and best practices for the evaluation of strategic alternatives including capital deployment, strategic investments, acquisitions and divestitures. Refining these skills will foster a continued focus on value creation in the pursuit of opportunities to invest, grow and drive innovation. In each session we will develop communication strategies for discussing the merits and possible risks of strategic investments.

Course Materials:
Corporate Finance Ross, Westerfield, Jaffe (RWJ) 9th edition. Note that electronic copies of selected chapters from the 10th edition are available electronically on Blackboard.
Harvard Business School Publishing Case Study: *Spyder Active Sports – 2004* (9-206-027)

Additional Readings and Reference Materials (electronic copies provided on Blackboard)**:**
November 5, 2012 J.P. Morgan initiation of coverage report on KYTH
November 5, 2012 Goldman Sachs initiation of coverage report on KYTH
December 31, 2013 Goldman Sachs earnings and valuation financial model on KYTH
January 7, 2013 CEO presentation at the J.P. Morgan Healthcare Conference, San Francisco

We will use Kythera Biopharma as a case study for discussion. We will discuss how the company evolved from a startup in 2005 to a publicly traded company in 2012 in a rough financial environment. We will review a Goldman Sachs valuation analysis on the company.

KYTHERA Biopharmaceuticals, Inc. a clinical-stage biopharmaceutical company focused on the discovery, development and commercialization of prescription products for the aesthetic medicine market. The company's lead product is based on this technology and now in the third phase of clinical trials. Since its founding, Kythera raised over $100 million in venture capital and corporate partnerships to support its R&D efforts. The company was able to net $70 million from its very successful IPO in October 2012. The Company's initial focus is on the facial aesthetics market. Its product candidate, ATX-101, is a injectable drug in Phase III clinical development for the reduction of submental fat, which commonly presents as an undesirable double chin. Based on clinical trials conducted, ATX-101 has exhibited results in the reduction of submental fat. ATX-101 contains a synthetic form of sodium deoxycholate. In the United States and Canada, the Company is conducting two pivotal Phase III trials of ATX-101 for the reduction of submental fat. The Company initiated this pivotal Phase III clinical program, with planned enrollment of 1,000 patients, in March 2012.

Financial Strategy I

<table>
<tr><th>Date</th><th>Learning Objectives and Session Topics</th></tr>
<tr><td>date
time
location TBD</td><td>RWJ Chapter 3 on Financial Statement Analysis, Ratios and Financial Models If you have the 10th edition of RWJ, please review Chapter 9 Stock Valuation pages 287-292 regarding comparables how discounted cash flow can be used to determine the value of an entire enterprise in addition to individual common stocks.

Performance Measurement:
Gain proficiency in financial statement analysis and evaluation of performance metrics. We will review examples considering ratios and performance metrics for various companies in the healthcare industry.
Valuation Frameworks:
Discuss Enterprise Discounted Cash Flow approach for firm valuation.
Discuss variables and assumptions used in the financial model and sensitivity analysis.
Discuss enterprise valuation methodologies including market multiples, precedent transactions and discounted cash flow analysis (DCF).
Calculate and interpret key market multiples and metrics specific to medical and healthcare industry. Consider examples of public trading comparable companies (comps).
For Discussion:
Skim both the J.P. Morgan and Goldman Sachs initiation of coverage reports on KYTH. Review the financial performance of the company and observe key trends and the drivers of profitability. Compare and contrast the differences in the valuation approaches and assumptions by the two analysts.
Review both the Goldman Sachs and JP Morgan financial models on the company (excel spreadsheet, 7th tab “DCF analysis”). Take note of the assumptions used in the DCF valuation, including the WACC (discount rate), residual (terminal) growth rate, length of forecast, and forecast drivers for sales, expenses, profitability and cash flow. We will use these examples in our discussion and will discuss the methodologies to determine these assumptions.</td></tr>
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Financial Strategy II

Date	Reading and Learning Objective
date *time* *location TBD*	*RWJ Chapter 13 Risk, Cost of Capital, and Valuation* *RWJ Chapter 15 Long-Term Financing, Chapter 20 Raising Capital* *RWJ Chapter 29 Mergers, Acquisitions and Divestitures* ***Long Term Financing:*** • Consider risk and cost of capital. We will introduce the concept of the weighted average cost of capital (WACC) and show how it can be used along with discounted cash flow to value both an entire enterprise as well as individual projects. • We will discuss how firms access capital. The financing method is generally tied to the firm's life cycle. We will consider alternative approaches to financing assets and growth through equity and debt. • What milestones impact valuation and financing (FDA approval stages, first revenue, first profit, etc.). • What are investors required rates of return (based on company and stage of development) • What attributes make a preferred more valuable than a common share (participation rights, dividends, conversion rights, etc.). ***Mergers and Acquisitions:*** • Discuss the key aspects of the M&A business process from corporate strategy, to target selection, to initial valuation, to doing the deal (including due diligence, integration planning, negotiating the agreement, announcing the deal), to closing, and integration. We cover M&A best practices. ***For Discussion:*** • We will examine a few recent acquisitions in the health care industry. Prior to our session you should research a transaction of interest to you in your industry. Form an opinion about a proposed or past deal. Be prepared to discuss whether the transaction is likely to create or destroy shareholder value for the acquiring company. A few deals for consideration might include Pfizer's acquisition of Wyeth, Roche's acquisition of Genentech and McKesson's acquisition of US Oncology.

Financial Strategy III

Date	Reading and Learning Objective
date *time* *location TBD*	***Private Company Valuation and Consideration of Strategic Alternatives*** HBS Case Study Spyder Active Sports – 2004 (9-206-027) The Spyder case allows us to consider an expansion/high-growth phase company's strategic alternatives and an owner's consideration of timing of "exit" options. We will also discuss valuation issues of a privately owned company and market timing. We will incorporate multiple topics from our financial strategy sessions in this case analysis. David Jacobs founded a high-end ski apparel company in 1978. He successfully built and grew the company, establishing a major international brand that appealed to ski racers and other active skiers. In 1995, he sought external financing to support further growth of the company and structured a financial deal with CHB Capital Partners, a private equity firm in Denver. By 2004, Jacobs was ready to consider alternative types of equity transactions that would provide a source of liquidity to him and his family, including sale of Spyder to another apparel company and sale of a large block of stock to a private equity firm. ***For Discussion:*** • Identify the different "exit" options that are feasible for Spyder in 2004, and analyze the benefits and costs of each alternative. Is this a good time to sell the business? Consider the interests and needs of the owner(s), the current state and future prospects of the company, and the current state of the financial markets. • We will perform a DCF valuation analysis of Spyder utilizing its forecast in exhibit 5. We will consider the risks to the valuation and will discuss sensitivity analysis and alternative approaches to forecasting. • Spyder is not publicly traded. We can still apply the market approach to estimate the company's implied value. Evaluate the financial data provided for Spyder and also the comparable publicly-traded company price multiples (Exhibit 11) and comparable past merger and acquisition multiples (Exhibit 9). We will use this data to determine an estimated "implied" value for the company in 2004. Note that the implied value of Spyder will be impacted by the type of buyer (strategic or financial) and type of sale (majority/controlling stake vs. minority interest/non-controlling stake). • Compare the alternative transactions described on the last page of the case. Which would you choose if you were: 1) David Jacobs; 2) CHB Capital; 3) Shimokubo? Who else is affected by this choice and how?