

So, how can LEAPS help me?
(the Clunker Motors Case)

- LEAPS can prove a “reasonable range” of size for your DLOM
- Characteristics of particular public companies compared to your subject provide a likely discount conclusion.
- For example, here is an actual valuation assignment....

Clunker Motors, Inc.

Valuation date: Tuesday, September 30, 2008
Interest valued: 12% of common stock
Purpose: Gift

The company:

Regional Chevrolet dealer founded in 1953
Founder is controlling shareholder
C-corp
Capitalization – all common stock
2008 sales volume (full year) = \$50 million
Profitable in each of last five years
Total assets = \$14 million
Cash = \$3.6 million
Inventory = \$7.5 million
Pays small to no dividends

A search of LEAPS in the industry shows three companies and the costs of their put options on September 30, 2008 expressed as discounts:

Discounts for Put Options Expiring on:

<u>Symbol</u>	<u>Co. Name</u>	<u>4/18/09</u> <u>(6 1/2 mos.)</u>	<u>1/16/10</u> <u>(15 1/2 mos.)</u>	<u>1/22/11</u> <u>(27 1/2 mos.)</u>
GPI	Group 1 Auto.	19.9%	27.2%	N.A.
AN	AutoNation	25.7%	36.8%	55.6%
KMX	Carmax	32.9%	44.0%	53.1%

N. A. = No option available

Both AutoNation and Carmax prove that a DLOM in the 50% to 55% range is reasonable in the industry. The cost of price protection for GPI for the 2010 LEAPS (expiring in 15 ½ months on 1/16/10) is significantly less than for the other two companies. From this, we guess that, if a 2011 LEAPS were available, it might carry a smaller cost/discount. So, we reduce the lower end of our range of reasonableness to 45%, resulting in a total range of 45% to 55%.

You can compare the companies to your subject in as great depth as you wish. For example,

	<u>GPI Group 1 Auto</u>	<u>AN AutoNation</u>	<u>KMX Carmax</u>	<u>Clunker Motors</u>
Total Sales	\$5.6 B	\$14.1 B	\$7.0 B	\$50.0 M
% Profit to Sales	Loss	Loss	0.8%	0.2%
Total Assets	\$2.3 B	\$6.0 B	\$2.4 B	\$13.9 M
% Cash to Tot. Assets	1.0%	1.8%	5.9%	25.9%
% Invty. to Tot. Assets	36.6%	31.2%	29.6%	15.0%
% Equity to Tot. Assets	26.9%	36.5%	67.0%	44.9%

To finalize a discount, we find it useful to compare the subject company to the public company LEAPS group in a “Mandelbaum factor” format as shown on the following page. The key factors in the decision for Clunker are (1) its profitability, while many in the industry are not; (2) its smaller inventory and greater cash; and (3) its much smaller size. We know from broad studies of LEAPS and discounts that company size and financial strength are major determinants of the size of discounts. Therefore, a conclusion of a 50% discount for lack of marketability is conservative and reasonable, yet well substantiated by the market.

Clunker Motors, Inc.
Mandelbaum DLOM Factors

Factor	Comparison of Subject Company To Public Company LEAPS Group	Effect On DLOM	Weight In Conclusion
<u>Financial Statement Analysis</u> debt/equity ratio; profitability; growth; stability; risk	- Much smaller in revenues and assets than LEAPS group. - Very solid financially; lots of cash - Profitable for last five years	Neutral	40%
<u>Dividend/Distribution Policy</u> size; consistency; growth	- History of small or no dividends. - Inconsistent	Increases	10%
<u>Company/Industry</u> size; position in industry; history; economic outlook	- Small, regional company - one location - Average historical growth for retailer - no acquisitions - Long history in business - Industry is depressed - no end in view	Increases	40%
<u>Company Management</u> experience; depth	- Adequate management for its size - Comparable to public companies.	None	0%
<u>Amount of Control In Transferred Shares</u>	- None. Comparable to public companies.	None	0%
<u>Anticipated Holding Period</u>	- Minimum two years, more likely five or more years. - Longer than LEAPS group	Increases	10%
<u>Restrictions on Transfer</u>	- None. Comparable to LEAPS group.	None	0%
<u>Company Redemption Policy</u> policy; financial capability; history	- None. Comparable to LEAPS group.	None	0%
<u>Likely Cost of Public Offering</u> legal ability? financial ability to afford cost?	- Public offering very unlikely; cost high	None	0%