Versus

2009/2010

"Proper Valuation is critical to the success of any M&A deal. Without it a company might pay too much or the target might accept a price that is too low." – Scott Moeller & Chris Brady (2007)

Did Kraft pay too much or did Cadbury accept too low a price?

Initially hostile bid	Cross border – UK vs. US	Strategic
Unsolicited bid	Nostalgic UK brand	Conglomerate

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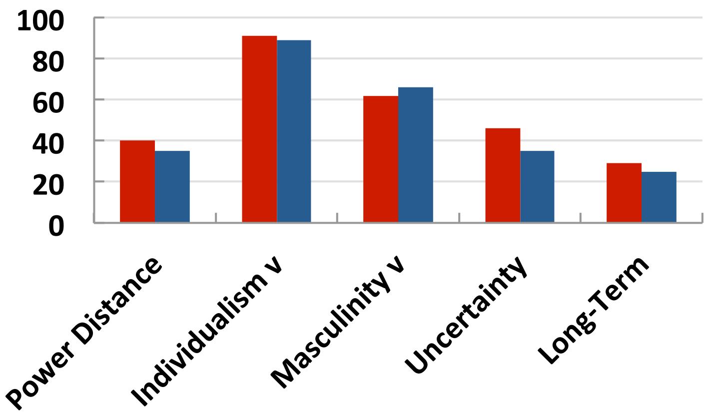
13th December 2011

Where was the value from Kraft's perspective?

Kraft's Strategy

- Kraft was heavily dependent on North American market (Oreo, Kraft Cheese)
- Had a strategy to:
  - Change the categories they operated in
  - Change their geographic footprint
- Kraft operates a brand based business
  - This takes time to establish
  - Is geographically independent



National Culture Fit (US/UK)
(Hofstede Cultural Dimensions)

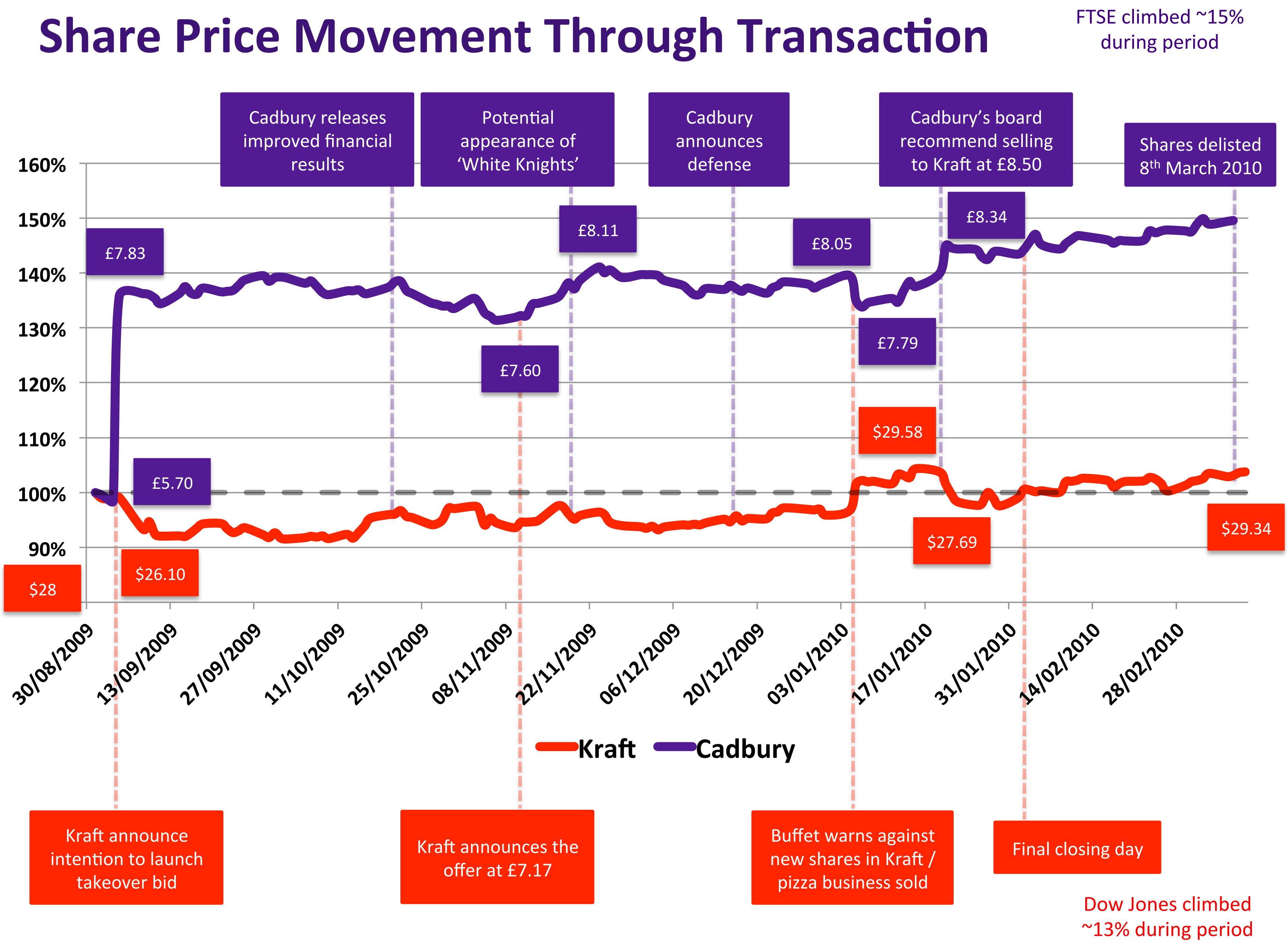
The Cadbury Opportunity

- Access to higher growth markets (snacks/confectionary)
- Cadbury had strong growth in emerging markets (Latin America and India) which represented 40% of revenues
- Very different footprints, opportunities to:
  - Distribute Kraft products through Cadbury distribution channels (Africa/India)
  - Distribute Cadbury products through Kraft distribution channels (Russia/China)
- Acquisition of Cadbury would take Kraft to global **number 1** in chocolate and confectionary
- Up to **$2bn** additional revenue through Synergies
- Expected combined **$675m** in annual cost savings
- Kraft expected ROI of 'mid teens' on the cost of capital
- Theoretical cultural fit

Analysis

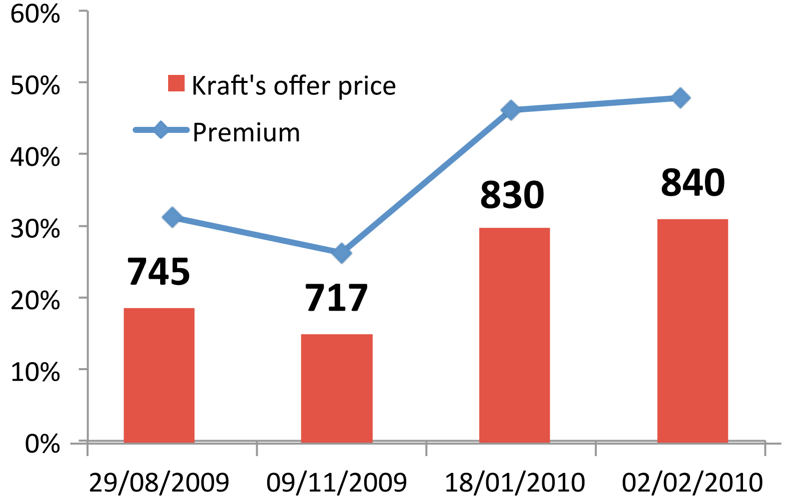
- Cadbury acquisition allowed a shortcut in achieving strategic aims
- Acquisition facilitated the split in Kraft (Announced August 2011)
  - Snacks (chocolate, candy and gum), circa 45% of the company
  - North American Grocery Business, circa 55% of the company

Share Price Movement Through Transaction



Surely Kraft's offer undervalued Cadbury?

The Offer



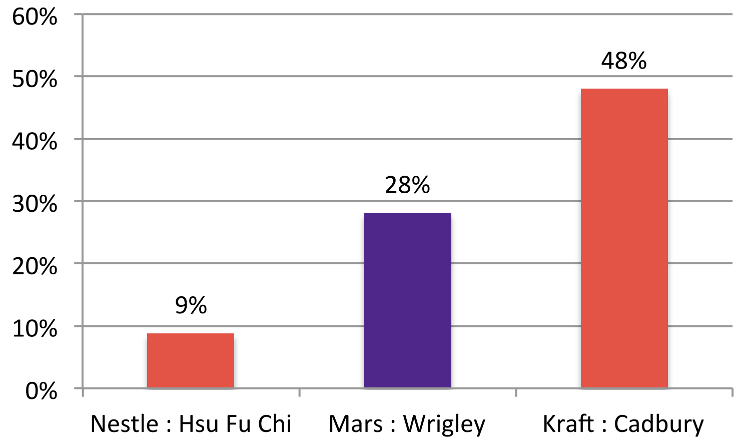
Challenges faced by Cadbury:

- Low share price
- History of failing to meet ambitious profit targets
- Salmonella contamination in 2006
- Schweppes split took longer than anticipated
- Investor concerns over business strategy
- Rescinded on discussions to return money to shareholders in 2008
- Predicting falling profit margins in H2 2009 due to product launches

Compared to other deals the final offer looks low:

Buyer/Unit	Announcement	EV/EBITDA (LTM)
Mars/Wrigley	2008	18.5x
Pefetti/Van Melle	2001	17.0x
Wrigley/Kraft Candy	2004	15.0x
Cadbury/Addams	2002	14.3x
Kraft/Cadbury	2010	13.0x

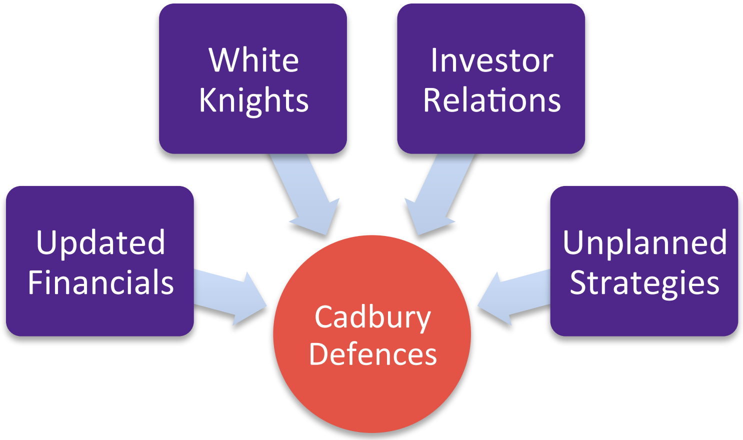
Share price premium is above the sector average



Analysis

Cadbury did not have the track record to be able to justify a higher share price which recognized inherent issues in the business.

Defence to prevent takeover or get a better price?



Unplanned events can aid defence:

- UK public outcry/ demonstrations
- Public attack by Lord Mandelson
- Was Warren Buffet's shareholder revolt a ploy?
  - It came the same day as Kraft's sold their pizza business and caused Kraft's share price to rise above 100%.
  - It also meant Nestle dropped out of the bidding.

Defence Outcomes

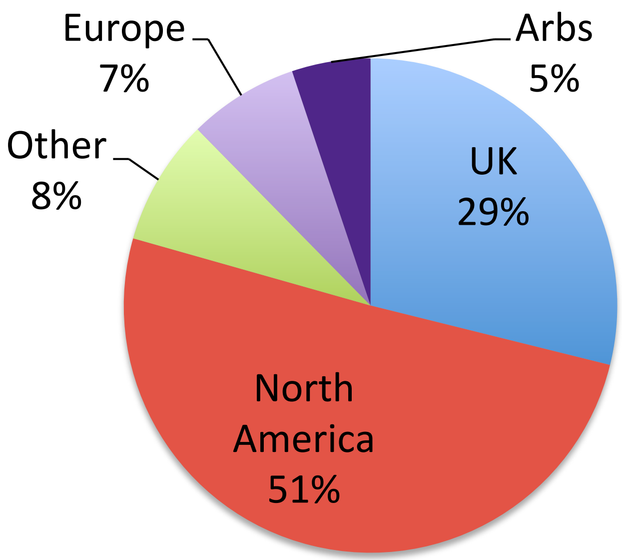
- White knights competition pressured Kraft to increase their offer even with no competing bids.
- Updated financials showed Kraft's offer under valued the company (according to Cadbury).
- Cadbury defences didn't impact share price.

Cadbury Did Not Want To Prevent Takeover

Defence strategies fall into two types; prevent takeover and maximise takeover premium.

- No takeover prevention defences used e.g. returning cash, selling assets. Cadbury did not try to block the takeover their defence focused on getting a better price for shareholders.
- No preventative defence which made them a target – complementary markets, attractive brands and low share price. An IPA report shows Cadbury's intangible assets alone were worth £12bn.
- Schweppes demerger made them more attractive.

US Long Funds Sell and the Arbs Take Control



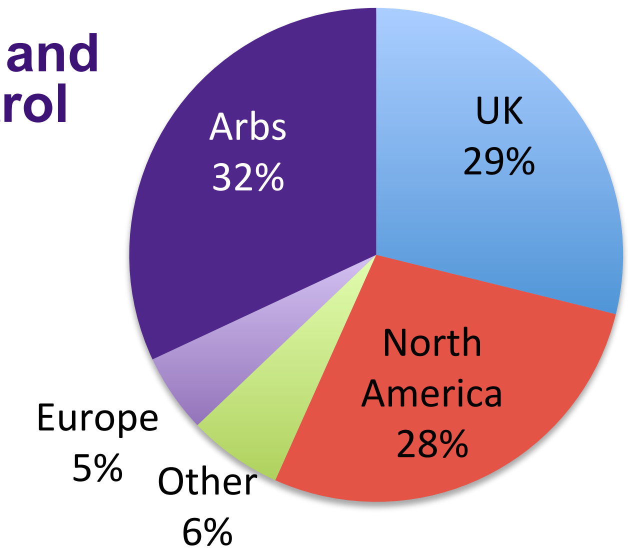
4th September 2009

North American Funds Sell To Hedge Funds to lock in profit

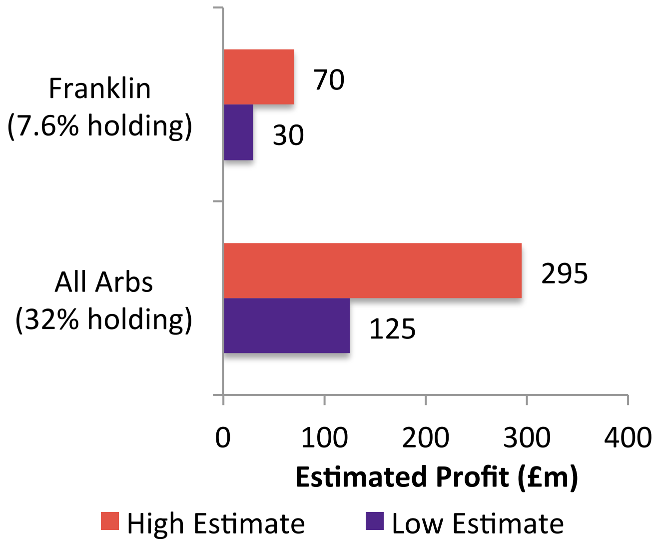
BUT

UK Funds do not

Just 136 days later



18th January 2010



Franklin Resources Cadbury's largest shareholder estimated profit was between £30m to £70m.

Result of Arbs Control

Kraft knew that 32% of shareholders would sell even for a small profit. Therefore they only needed to convince another 18% to sell to reach 50%. We conclude that Kraft would have focused on convincing the North American fund managers.

Paul Myners, the ex-Marks & Spencer chairman suggested a minimum period before you are entitled to vote on shares.

Why did UK funds not sell?

- As a UK company they understood Cadbury's true value.
- IR would have been focused on UK funds due to proximity

Recommendation

If Cadbury wanted to remain independent they should have preventatively focused on trying to get more UK fund investment.

Valuation is an art not a science; variables can be manipulated depending on who is doing the valuation…

Method	Basis of Assumption	Value (in GBP Mio.)	Weighting	Adjusted Value
DCF	£10.47 target price (independent DCF)	£14,239	50%	£7,120
Book Value	Net Assets as of 31/12/2008 (Company Accounts)	£3,534	10%	£353
EV/EBITDA	Based on multiple estimate of 9.8 in 2009 (Case Study)	£9,976	20%	£1,995
P/E	CBRY estimated EPS for 2009 and Forward looking P/E (2010)	£9,052	20%	£1,810

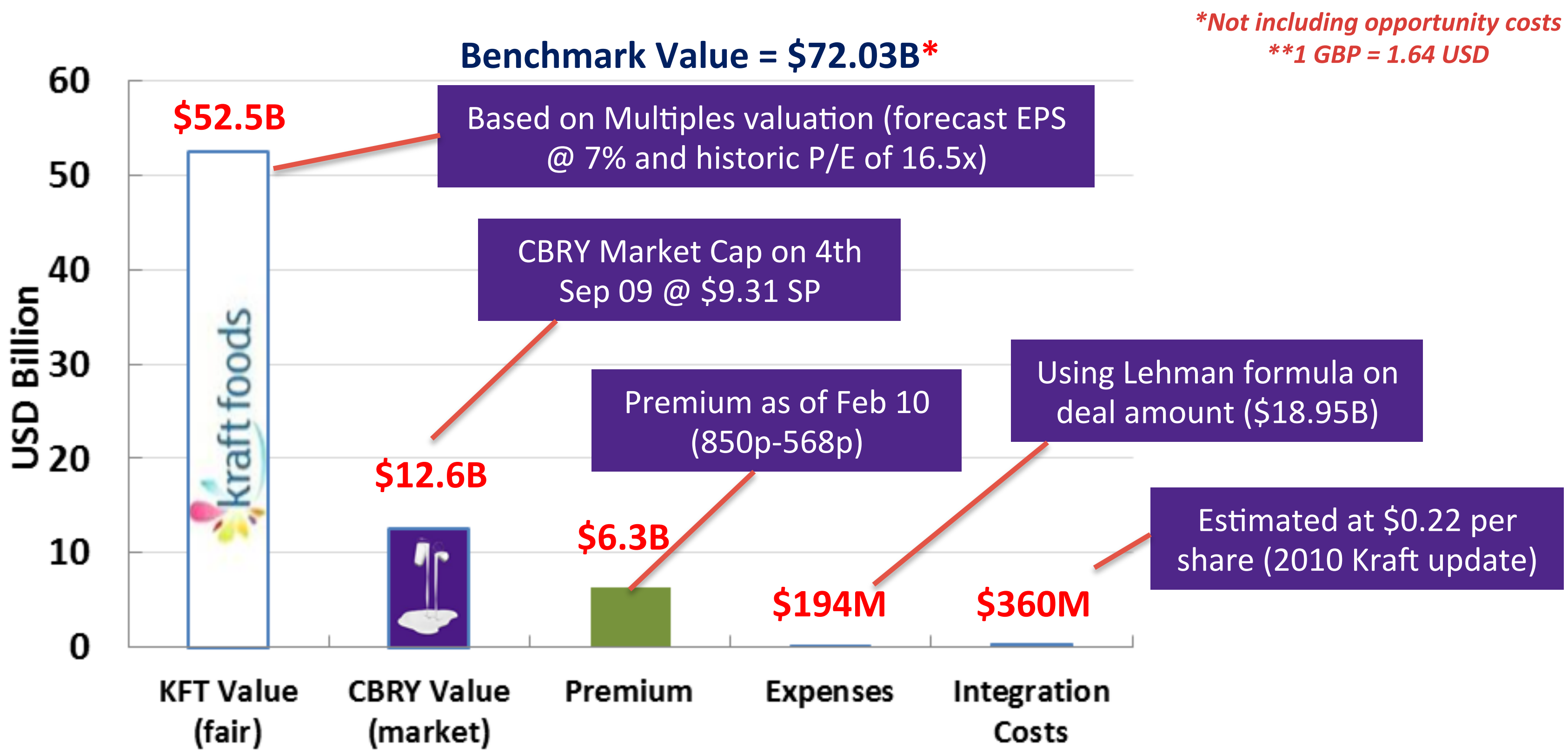
CBRY Fair Value = £11,279M
=> Fair Value / Shares Outstanding = 829p

- Cadbury fair value calculated using four different methods with importance weightings for each one
- From this we valued the company at **829p**, which is a **46% upside** to the CBRY share price of 568p on 4/9/09, but 2.5% less than the final offer of Kraft for the company
- Therefore **Kraft overpaid for the company by 21p**, which equates to £286M *(based on 1,360M shares outstanding and 1.64USD/GBP)*

M&A valuation is very subjective!

Any changes to the terminal growth rate (in DCF), choice of multiples (in EV/EBITDA and P/E), or relative weighting makes a big difference to the valuation.

Value creation from M&A depends on the combined entity's added value and the time it takes for this value to be delivered…



V (KFT+CBRY) > V(KFT) + V(CBRY) + P + E + IC + OC (?)

- Our calculations show the combined entity's value should exceed $72.03B for the deal to be value creating
- Kraft has not set specific timeframes over which value added should be assessed
- With the company's proposed split of the US Grocery and International Snack businesses set to happen in 2012, overall value creation will be harder to assess (*to the company's benefit?*)

Excluding opportunity costs we can conclude that the right price for Cadbury (from Kraft's perspective) would have been below 830p…

In USD Million	Estimate		Scenario 1 @830p	Scenario 2 @745p
KFT Value (fair)	$52,528		$52,528	$52,528
CBRY Value (market)	$12,661		$12,661	$12,661
Premium	$6,286		$5,825	$3,945
Expenses	$194		$190	$171
Integration Costs	$360		$360	$360
Opportunity Cost	???		???	???
VALUE	$72,029		$71,564	$69,665
Value KFT/CBRY	$67,300	$71,907	$71,907	$71,907
Difference	**-$4,729**	**-$122**	**$343**	**$2,242**

Based on current KFT Market Cap (SP $36.75) and 850p offer for CBRY

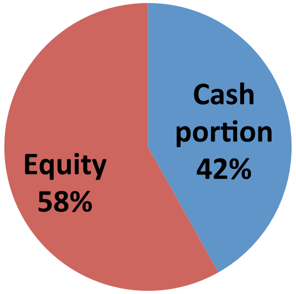
KFT Market Cap based on 12 Mo. Consensus Analyst Target Price (SP $40) and 850p offer for CBRY

Forward looking KFT Market Cap if CBRY offer was 830p (Fair value of CBRY)

Forward looking KFT Market Cap if CBRY offer was 745p (1st offer)

- *Based on market cap of KFT 22 months on (9/12/11), __the deal is value destroying__*
- *Based on forward looking (12mo.) consensus estimates of analysts (9/12/11), the deal is also __marginally unsuccessful__*

Previous Offer



On 5 January 2010, 11 days prior to Kraft's final bid to Cadbury, **Warren Buffet voted "no"** on Kraft's proposal to authorise the issuance of up 370m shares to facilitate the acquisition of Cadbury

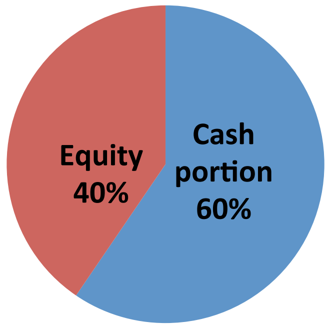
Rosenfeld used the proceeds from the sale of the pizza business to Nestle to increase the cash portion of their offer.

Rosenfeld removed the need for shareholder approval.

By selling its pizza business to Nestle, Kraft essentially took out one of Cadbury's suitors.

By increasing its cash proportion Rosenfeld signals to shareholders that Kraft wanted to capture the value Cadbury for itself and did not want to share in the upside with Cadbury shareholders.

New Offer



The financing mix can be as important as the amount offered, for both parties.

Critique of the Cadbury Defence

"Cadbury put up a staunch defence and achieved acceptable shareholder value. However a takeover was always inevitable."

"Value was achieved through becoming an acquisition target rather than through operational growth."

For	Against
In January 2010, a deal of 840p plus 10p dividend per share was a circa 50% premium on the undisturbed price	In August 2009, the undisturbed share price of 568 pence was evidently undervalued. Arguably, they would not have become an acquisition target unless they were undervalued.
At £11.7billion the final offer was almost a £1billion more than original offer.	The final offer valued Cadbury at 13 times 2009 core EBITDA against comparable transactions at 14.3 to 18.5 times EBITDA.
Cadbury put up a staunch defence and achieved acceptable shareholder value.	At such a large share premium, some shareholders will have been forced to accept for fear of share price collapse.
If the executive's role was to secure shareholder value, this was achieved.	This was achieved through becoming an acquisition target rather than through operational growth.

Key Takeaways	Further Discussion
Valuation is key for the success of a deal	Should merger assurances that are made and then go on to be broken incur fines? E.g. not closing factories
Lots of ways to value a company and none are "right"	Should key/ iconic/ important national brands be afforded more protection from overseas bidders?
How to structure the financing plays a big part in how both sets of shareholders view the deal	Will we ever know if the deal was a success now that Kraft is splitting in two? Should the shareholders care?
Arbs involvement have a huge impact on the outcome of M&A deals	Takeover panel repeatedly asked Kraft's CEO, Irene Rosenfeld to appear before them to explain the U-turn on the factory closing and she declined. Should the takeover panel have more power?
UK takeover rules state that any information released by the bidder or target can be trusted by investors or heavy penalties imposed	Are M&A deals merely a wrestling match for claiming value? Does any value for Kraft simply come out of the pockets of Cadbury? Can you have a deal that creates value for both sides. That is why when we are asked to cite the winner, it could be argued either way, ie. win-win.
Liaising with shareholders to canvass their views is key	As this was such a strategic deal for Kraft would they have done the deal at any cost?
Investor relations are key to M&A success both for the bidder i.e. Warren Buffet intervention	How do you factor in the stockmarket movement throughout the deal on the share premium? The 50% share premium was gained against the back drop of a 15% rise in the FTSE.
Defences can be used to defend the takeover or increase the price premium	Should the takeover rules be changed to stop the corporate raiding by hedge funds?
The threat of hostile takeovers might lead managers to abandon a long-term view in favour of short-term profits. This on its own would not be good for industry. However, the threat also adds to the wealth of those holding shares in the takeover target	