FNCE20005 CORPORATE FINANCIAL DECISION MAKING 2021

Note: A Gradescope practice submission named "Gradescope Practice Submission (Based on Tutorial 9 Questions)" is created, which allows you to be familiar with the technology employed in the final exam. Please refer to the announcement for more details. **This is NOT a substitute to weekly tutorial submission.**

TUTORIAL 9: Corporate Takeovers & Restructuring - Part 3
Answers to Section B questions to be submitted on Canvas by 10am on Monday, October 11th

SECTION A

Question 1

Yam Ltd (Y) has been evaluating the acquisition of Xavier Ltd (X). The current annual expected cash flows of Y and X are, respectively, $1.16 million per annum in perpetuity and $640 000 per annum in perpetuity. These cash flows are expected to be unaffected by the takeover. The systematic risk (beta) of Y is 0.75 and of X is 1.0. The risk-free interest rate is 10 per cent and the market risk premium is 6 per cent.

(a) Calculate the price at which X represents a zero net present value investment. Is it likely that Y's shareholders will benefit from the takeover?

(b) Assume the information in part (a), except that the post-takeover cash flow of the merged entity is expected to be $1.95 million per annum in perpetuity – with the additional cash flows attributable to realising cost efficiencies in the management of the assets previously owned by Xavier Ltd. There is no change to the systematic risk of those cash flows. What is the value of the benefit to Yam Ltd shareholders from the acquisition assuming a $500,000 control premium was paid to Xavier shareholders?

SECTION B – PRIORITY QUESTIONS

Question 2

Crocodile Ltd is considering the acquisition of Shark Finance. The values of the two companies as separate entities are $10 million and $5 million, respectively. Crocodile estimates that by combining the two companies it will reduce selling and administrative costs by $250 000 per annum in perpetuity. Crocodile can either pay $7 million cash for Shark or offer Shark a 50 per cent holding in Crocodile. If the opportunity cost of capital is 10 per cent per annum:

(a) what is the gain, in present value terms, from the merger?
(b) what is the net cost of the cash offer?
(c) what is the net cost of the share alternative?
(d) what is the *NPV* of the acquisition under:
  (i) the cash offer?
  (ii) the share offer?

Question 3

You are a senior Vice President of a consultancy firm that has been called in to advise Bidder Ltd on its proposed acquisition of ASX listed company Target Ltd. You instruct your newly recruited analyst to gather the relevant information you will need to advise the board on the viability of the deal. Your analyst provides you with the following information:

- Share price and number of shares on issue:

	Bidder Ltd	Target Ltd
Share price	$4	$2.40
Number of shares on issue	100 million	8 million

- Synergies from the deal:
    - Revenue synergies of $900,000 per annum (at year end) for the next 5 years
    - The sale of a corporate jet in 2 year's time for $2m
    - Cost savings of $300,000 per annum (at year end) for the next 5 years
- The relevant discount rate for all estimates is 12% per annum.

(a) Estimate the value of the gain from the acquisition.

(b) Given the information provided above, how many shares in Bidder Ltd would need to be offered for each share in Target Ltd for the gain from the acquisition to be shared equally such that 50% of the gain goes to Bidder Ltd shareholders and 50% to Target Ltd shareholders.