**Assignment: Exit Strategy**

1. The venture investors and founders of the ACE Products venture, a closely held corporation, are contemplating merging the successful venture into a much larger diversified firm that operates in the same industry. ACE estimates its free cash flows that will be available to the enterprise next year at $5,560,000. Since the venture is now in its maturity stage, ACE’s free cash flows are expected to continue to grow at a 6 percent annual compound growth rate in the future. A weighted average cost of capital (WACC) for the venture is estimated at 15 percent. Interest-bearing debt owed by ACE is $17.5 million. ACE currently has 5 million shares outstanding with 3 million held by venture investors and 2 million held by founders. The venture investors have an average investment of $2.50 per share while the founders’ average investment is $.50 per share.
   1. Based on the above information, estimate the enterprise value of ACE Products. What would be the value of the venture’s equity?
   2. How much of the value of ACE would belong to the venture investors versus the founders. How much would the venture be worth on a per share basis?
   3. What would be the percentage appreciation on the stock bought by the venture investors versus the investment appreciation for the founders?
2. The BETA firm is proposing to acquire the ACE Products venture described in Problem 1. BETA estimates that ACE’s free cash flow for next year could be improved to $5,860,000 because of synergistic benefits in the form of operating or distribution economies. The potential acquirer also believes that ACE’s perpetuity growth rate could be increased to 7 percent annually. However, the riskiness of the cash flows would be increased causing the appropriate WACC to increase to 16 percent. Interest-bearing debt owed by ACE is $17.5 million. ACE Products has five million shares of common stock outstanding.

A. Determine ACE’s enterprise value from the perspective of BETA. What is ACE’s equity worth to BETA in dollar amount and on a per share basis?

B. Use the per share value of ACE from Problem 1 and the per share value from this problem and establish a range of values (i.e., without and with expected synergistic benefits). If one-half of the synergy derived benefits were allocated to ACE’s venture investors and founders, what price per share would the merger take place?

C. BETA has thirty million shares of stock outstanding with a market capitalization value of $600 million. What is BETA’s stock price? Determine the exchange ratio between ACE’s stock value and BETA’s stock price at each of ACE’s values established in Part B. That is, what would ACE’s venture investors and founders receive in BETA’s shares for each share of common stock they currently hold in ACE Products?