Exchange ratios

Since acquirer and target share prices can change between the announcement and closing date of a transaction, risk exists for the buyer or seller (or both). The nature of the risk at the announcement date depends on the structure of the transaction:

Fixed exchange ratio:

- Shares issued are known
- Value of transaction is unknown.

Floating exchange ratio:

- Value of transaction is known
- Shares issued are unknown.

Fixed exchange ratio example

- Target has 24 million shares outstanding with shares trading at $9; acquirer shares are trading at $18.
- On January 5, 2014 ("announcement date") acquirer agrees that upon the completion of the deal (expected to be February 5, 2014) it will exchange .6667 shares of its common stock for each shares of target's 24 million shares, totaling 16m acquirer shares.
- No matter what happens to the target and acquirer share prices between now and February 5, 2014, the ratio of shares will stay fixed.
- On announcement date, the deal is valued at 16m shares * $18 per share = $288 million. Since there are 24 million target shares, this implies a value per target share of $288 million / 24 million = $12. That's a 33% premium over the current trading price of $9.
- By February 5, 2014, target's share price jumps to $12 because target shareholders know that they will shortly receive .6667 acquirer shares (which are worth $18 * 0.6667 = $12) for each target share.

Announcement date – 1/5/14

Target share price: $9

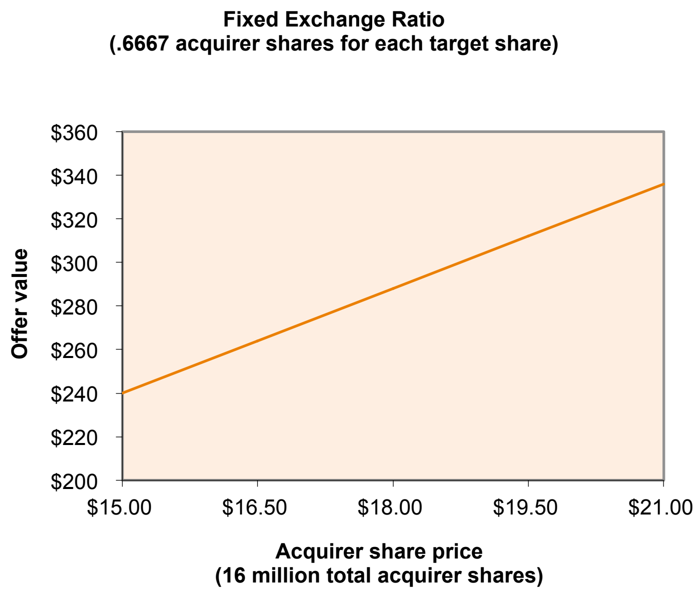
Acquirer share price: $18

Closing date – 2/5/14

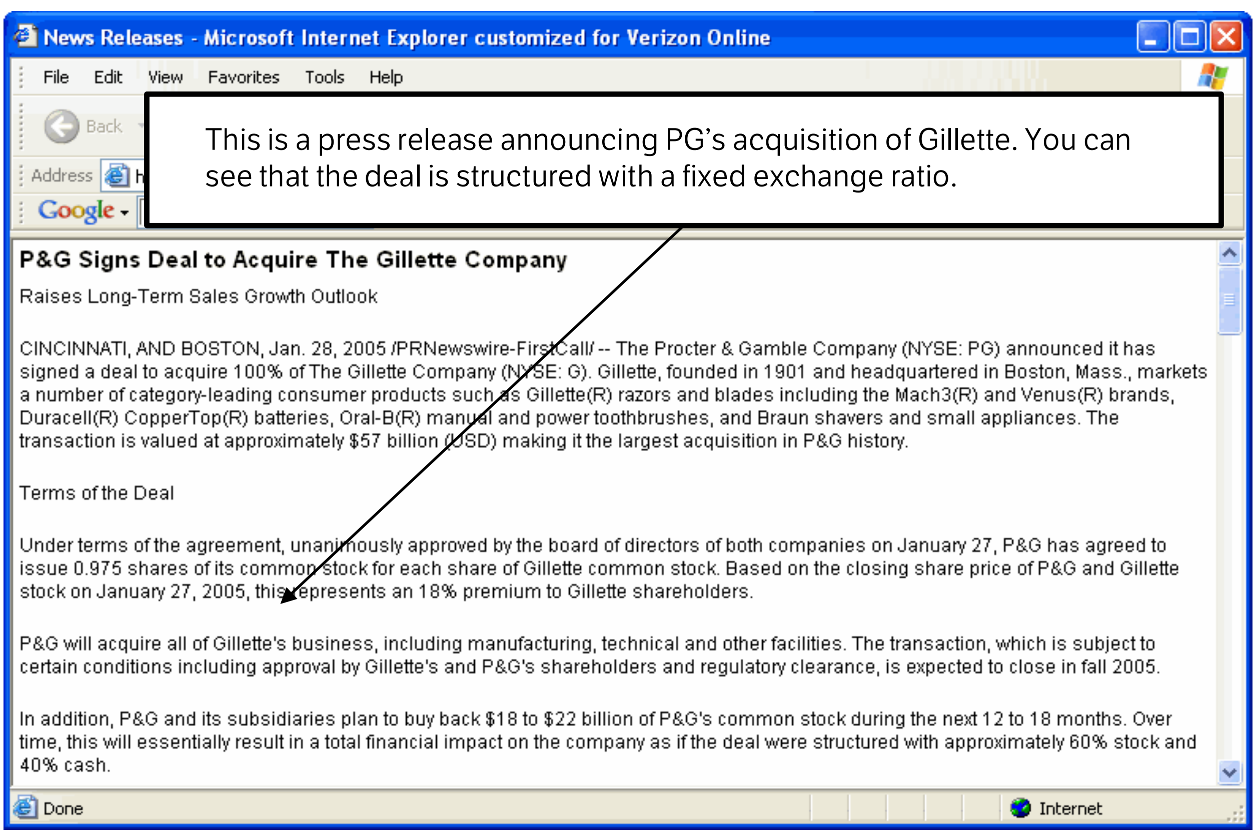
Target share price: $12

Acquirer share price: $18

- What if, however, the value of acquirer shares drop after the announcement to $15 and remain at $15 until closing date?
- Target would receive 16 million acquirer shares, and the deal value declines to 16 million * $15 = $240 million. Compare that to the original compensation the target expected of $288 million.
- It should now be clear that since the exchange ratio is fixed, the number of shares the acquirer must issue is known, but the $ value of the deal is uncertain.



- The fixed exchange ratio is generally preferred by acquirers because the issuance of a fixed number of shares results in a known amount of ownership and earnings accretion or dilution.
- Used in a majority of US transactions with deal values over $100 million.



P&G Signs Deal to Acquire The Gillette Company

Raises Long-Term Sales Growth Outlook

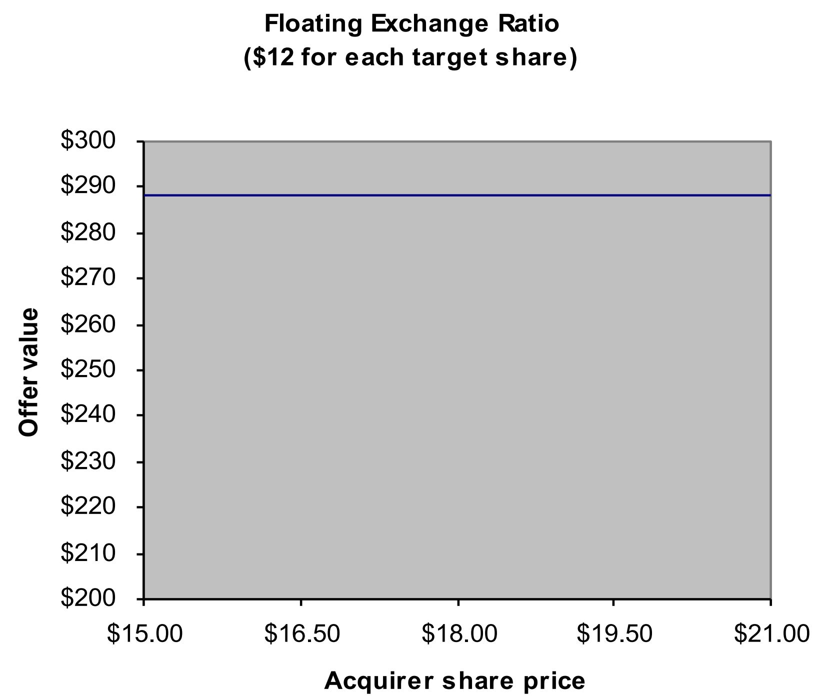
CINCINNATI, AND BOSTON, Jan. 28, 2005 /PRNewswire-FirstCall/ -- The Procter & Gamble Company (NYSE: PG) announced it has signed a deal to acquire 100% of The Gillette Company (NYSE: G). Gillette, founded in 1901 and headquartered in Boston, Mass., markets a number of category-leading consumer products such as Gillette(R) razors and blades including the Mach3(R) and Venus(R) brands, Duracell(R) CopperTop(R) batteries, Oral-B(R) manual and power toothbrushes, and Braun shavers and small appliances. The transaction is valued at approximately $57 billion (USD) making it the largest acquisition in P&G history.

Terms of the Deal

Under terms of the agreement, unanimously approved by the board of directors of both companies on January 27, P&G has agreed to issue 0.975 shares of its common stock for each share of Gillette common stock. Based on the closing share price of P&G and Gillette stock on January 27, 2005, this represents an 18% premium to Gillette shareholders.

P&G will acquire all of Gillette's business, including manufacturing, technical and other facilities. The transaction, which is subject to certain conditions including approval by Gillette's and P&G's shareholders and regulatory clearance, is expected to close in fall 2005.

In addition, P&G and its subsidiaries plan to buy back $18 to $22 billion of P&G's common stock during the next 12 to 18 months. Over time, this will essentially result in a total financial impact on the company as if the deal were structured with approximately 60% stock and 40% cash.



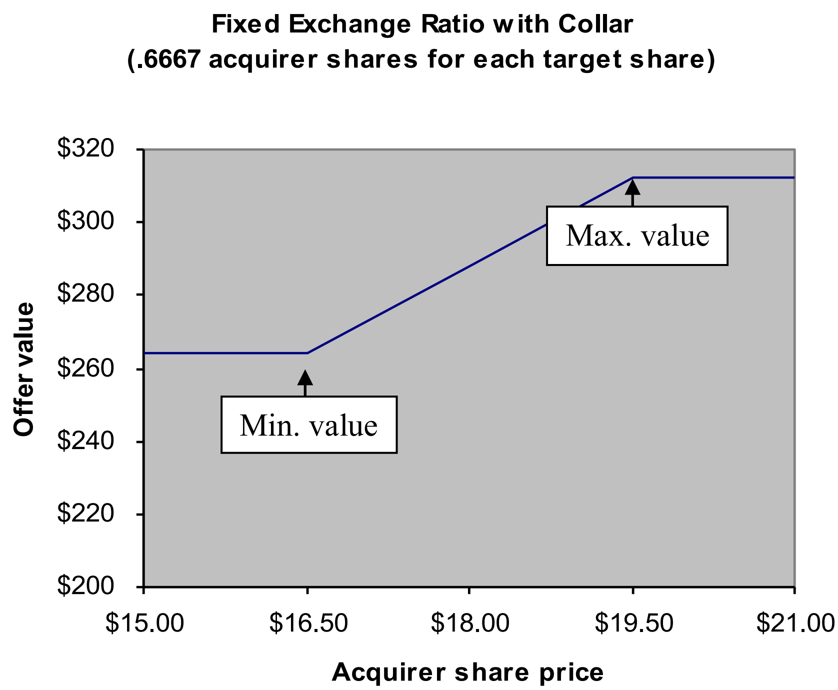
Floating exchange ratio (fixed value)

- Fixed value is based on a fixed per share transaction price, each target share is converted into the number of acquirer shares which are required to equal the pre-determined per target share price upon closing.
- Target has 24 million shares outstanding with shares trading at $12; acquirer shares are trading at $18.
- On January 5, 2014 target agrees to receive $12 from acquirer for each of target's 24 million shares (.6667 exchange ratio) upon the completion of the deal, which is expected to be on February 5, 2014.
- Just like the previous example, the deal is valued at 24m shares * $12 per share = $288 million.
- The difference is that this value will be fixed regardless of what happens to the target or acquirer's share prices. Instead, the amount of acquirer shares that will have to be issued upon closing will change with changing share prices to maintain a fixed deal value.
- While the uncertainty in fixed exchange ratio transactions is the deal value, the uncertainty in floating exchange ratio transactions is how many shares the acquirer will have to issue.
- The floating exchange ratio is generally preferred by the target because the issuance of a fixed value per share means target knows exactly how much compensation it is receiving.

- Now what happens if acquirer shares drop after the announcement to $15 and remain at $15 until closing date?
- In a floating exchange ratio transaction, it is the deal value that is fixed, while the acquirer shares are uncertain until the closing date.

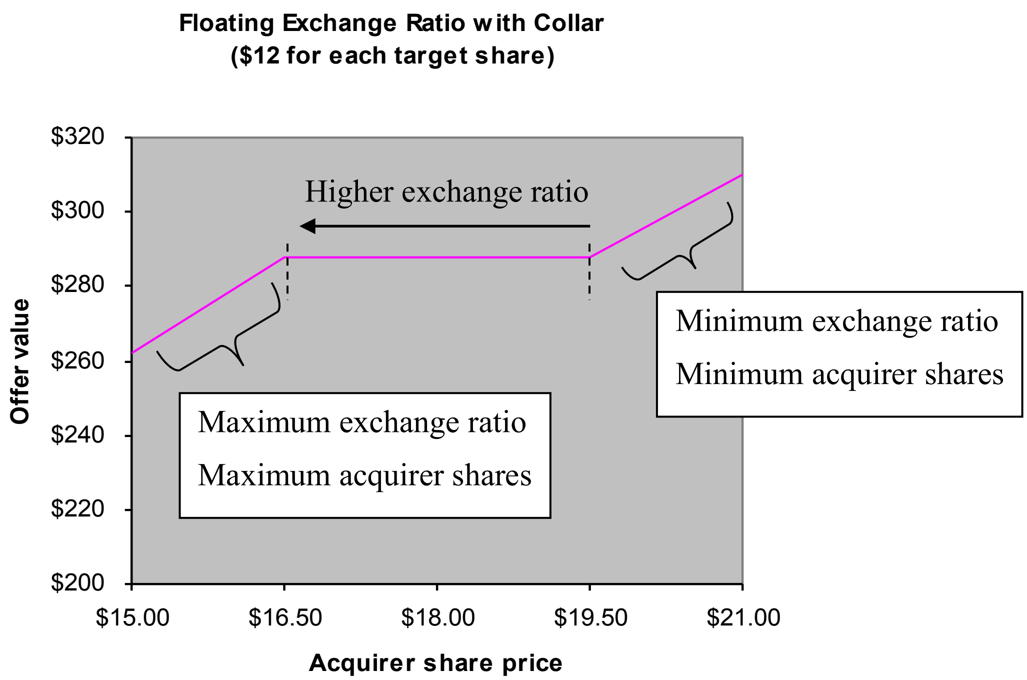
Collars and caps

Collars may be included with either fixed or floating exchange ratios in order to limit potential variability due to changes in the acquirer's share price.



Fixed exchange ratio collar

- Sets a maximum and minimum value for fixed exchange ratio transactions.
- If acquirer share price falls or rises beyond a certain point, the transaction turns into a floating exchange ratio.
- Collar establishes minimum and maximum price that will be paid per target share
- Above the maximum target price level, increases in the acquirer share price result in a decreasing exchange ratio (fewer acquirer shares issued)
- Below the minimum target price level, decreases in acquirer's share price result in an increasing exchange ratio (more acquirer shares issued)



Floating exchange ratio collar

- Maximum and minimum shares issued for floating exchange ratio transactions. If acquirer share price falls or rises beyond a certain point, the transaction turns to a fixed exchange ratio.
- Collar establishes minimum and maximum exchange ratio of shares that will be issued for a target share
- Below a certain acquirer share price, exchange ratio stops floating and becomes fixed at a maximum ratio. Now decreases in acquirer share price result in a decrease in value of each target share.
- Above a certain acquirer share price, the exchange ratio stops floating and becomes fixed at a minimum ratio. Now, increases in acquirer's share price result in an increase in the value per target share, but a fixed number of acquirer shares is issued

"Walk-away" rights

- This is another potential provision in a deal that allows parties to walk away from the transaction if acquirer's stock falls below a certain predetermined minimum trading price.