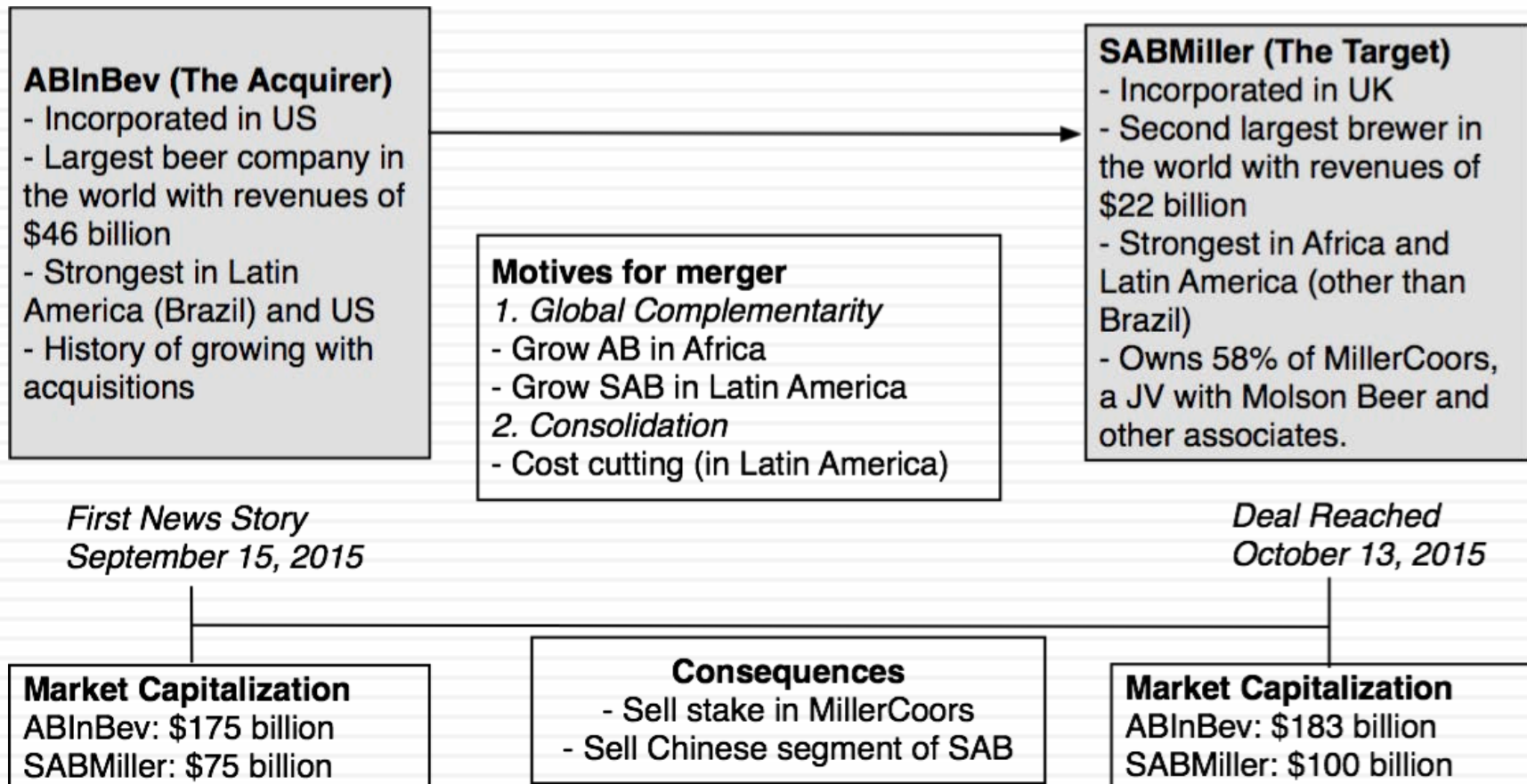




GOOD DEAL OR BAD ONE? AB INBEV ACQUIRES SABMILLER

The Fog of the “Big” Deal

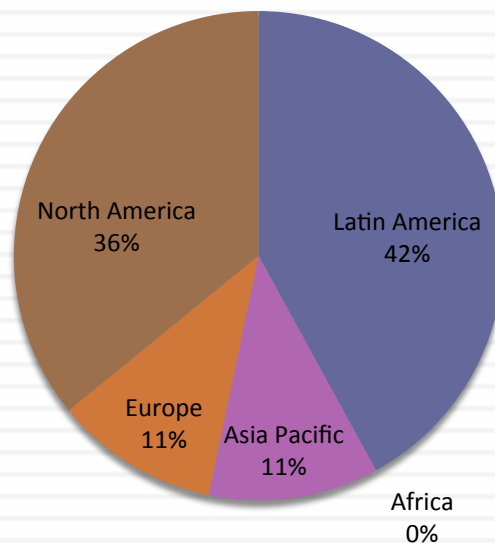
A Really Big Deal!



The Acquirer (ABInBev)

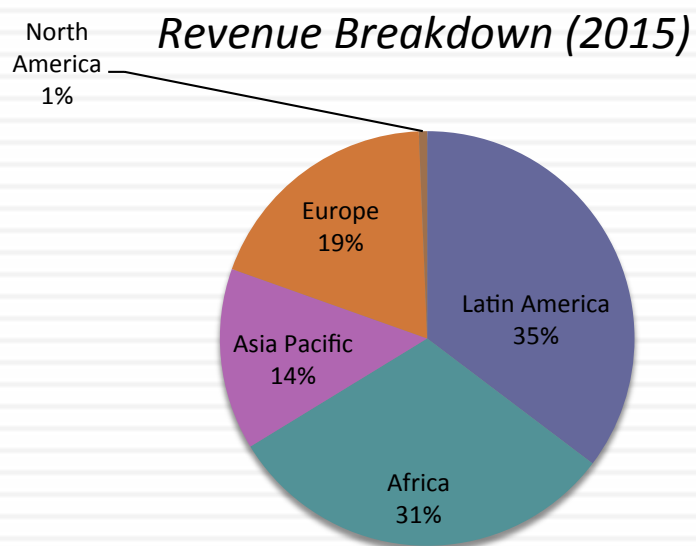
<i>Capital Mix</i>		<i>Operating Metrics</i>	
Interest-bearing Debt	\$51,504	Revenues	\$45,762.00
Lease Debt	\$1,511	Operating Income (EBIT)	\$14,772.00
Market Capitalization	\$173,760	Operating Margin	32.28%
Debt to Equity ratio	30.51%	Effective tax rate	18.00%
Debt to Capital ratio	23.38%	After-tax return on capital	12.10%
Bond Rating	A2	Reinvestment Rate =	50.99%

Revenue Breakdown (2014)



The Target (SABMiller)

<i>Capital Mix</i>		<i>Operating Metrics</i>	
Interest-bearing Debt	\$12,550	Revenues	\$22,130.00
Lease Debt	\$368	Operating Income (EBIT)	\$4,420.00
Market Capitalization	\$75,116	Operating Margin	19.97%
Debt to Equity ratio	17.20%	Effective tax rate	26.40%
Debt to Capital ratio	14.67%	After-tax return on capital	10.32%
Bond Rating	A3	Reinvestment Rate =	16.02%



Setting up the challenge

- SAB Miller's market capitalization was \$75 billion on September 15, 2015, the day ABInBev announced its intent to acquire SABMiller.
- The deal was completed (pending regulatory approval) a month later, with ABInBev agreeing to pay \$104 billion for SABMiller.
- Can ABInBev create \$29 billion in additional value from this acquisition and if so where will it find the value?
 - The market seems to think so, adding \$33 billion in market value to the combined company.

The Three (Value) Reasons for Acquisitions

- Undervaluation: You buy a target company because you believe that the market is mispricing the company and that you can buy it for less than its "fair" value.
- Control: You buy a company that you believe is badly managed, with the intent of changing the way it is run. If you are right on the first count and can make the necessary changes, the value of the firm should increase under your management
- Synergy: You buy a company that you believe, when combined with a business (or resource) that you already own, will be able to do things that you could not have done as separate entities. This synergy can be
 - Offensive synergy: Higher growth and increased pricing power
 - Defensive synergy: Cost cutting, consolidation & preempting competitors.
 - Tax synergy: Directly from tax clauses or indirectly through debt

Four numbers to watch

1. Acquisition Price: This is the price at which you can acquire the target company. If it is a private business, it will be negotiated and probably based on what others are paying for similar businesses. If it is a public company, it will be at a premium over the market price.
 2. Status Quo Value: Value of the target company, run by existing management.
 3. Restructured Value: Value of the target company, with changes to investing, financing and dividend policies.
 4. Synergy value: Value of the combined company (with the synergy benefits built in) – (Value of the acquiring company, as a stand alone entity, and the restructured value of the target company)
- The Acid Test
- Undervaluation: Price for target company < Status Quo Value
 - Control: Price for target company < Restructured Value
 - Synergy: Price for target company < Restructured Value + Value of Synergy

SAB Miller Status Quo Value

	<i>SAB Miller</i>	<i>+ Coors JV</i>	<i>+ Share of Associates</i>	<i>SAB Miller Consolidated</i>
Revenues	\$22,130.00	\$5,201.00	\$6,099.00	
Operating Margin	19.97%	15.38%	10.72%	
Operating Income (EBIT)	\$4,420.00	\$800.00	\$654.00	
Invested Capital	\$31,526.00	\$5,428.00	\$4,459.00	
Beta	0.7977	0.6872	0.6872	
ERP	8.90%	6.00%	7.90%	
Cost of Equity =	9.10%	6.12%	7.43%	
After-tax cost of debt =	2.24%	2.08%	2.24%	
Debt to Capital Ratio	14.67%	0.00%	0.00%	
Cost of capital =	8.09%	6.12%	7.43%	
After-tax return on capital =	10.33%	11.05%	11.00%	
Reinvestment Rate =	16.02%	40.00%	40.00%	
Expected growth rate=	1.65%	4.42%	4.40%	
Number of years of growth	5	5	5	
<i>Value of firm</i>				
PV of FCFF in high growth =	\$11,411.72	\$1,715.25	\$1,351.68	
Terminal value =	\$47,711.04	\$15,094.36	\$9,354.28	
Value of operating assets today =	\$43,747.24	\$12,929.46	\$7,889.56	\$64,566.26
+ Cash				\$1,027.00
- Debt				\$12,918.00
- Minority Interests				\$1,183.00
Value of equity				\$51,492.26

Price on September 15, 2015: \$75 billion > \$51.5 billion

SABMiller: Potential for Control

	<i>SABMiller</i>	<i>ABInBev</i>	<i>Global Alcoholic Beverage Sector</i>
Pre-tax Operating Margin	19.97%	32.28%	19.23%
Effective Tax Rate	26.36%	18.00%	22.00%
Pre-tax ROIC	14.02%	14.76%	17.16%
ROIC	10.33%	12.10%	13.38%
Reinvestment Rate	16.02%	50.99%	33.29%
Debt to Capital	14.67%	23.38%	18.82%

SABMiller: Value of Control

	Status Quo Value	Optimal value	
Cost of Equity =	9.10%	9.37%	
After-tax cost of debt =	2.24%	2.24%	
Cost of capital =	8.09%	8.03%	
After-tax return on capital =	10.33%	12.64%	
Reinvestment Rate =	16.02%	33.29%	
Expected growth rate=	1.65%	4.21%	
<i>Value of firm</i>			
PV of FCFF in high growth =	\$11,411.72	\$9,757.08	
Terminal value =	\$47,711.04	\$56,935.06	
Value of operating assets today =	\$43,747.24	\$48,449.42	
+ Cash	\$1,027.00	\$1,027.00	
+ Minority Holdings	\$20,819.02	\$20,819.02	
- Debt	\$12,918.00	\$12,918.00	
- Minority Interests	\$1,183.00	\$1,183.00	
Value of equity	\$51,492.26	\$56,194.44	<i>Value of Control</i>
			\$4,702.17

Price on September 15, 2015: \$75 billion > \$51.5 + \$4.7 billion

The Synergies?

	<i>Inbev</i>	<i>SABMiller</i>	<i>Combined firm (status quo)</i>	<i>Combined firm (synergy)</i>
Levered Beta	0.85	0.8289	0.84641	0.84641
Pre-tax cost of debt	3.0000%	3.2000%	3.00%	3.00%
Effective tax rate	18.00%	26.36%	19.92%	19.92%
Debt to Equity Ratio	30.51%	23.18%	29.71%	29.71%
Revenues	\$45,762.00	\$22,130.00	\$67,892.00	\$67,892.00
Operating Margin	32.28%	19.97%	28.27%	30.00%
Operating Income (EBIT)	\$14,771.97	\$4,419.36	\$19,191.33	\$20.368
After-tax return on capital	12.10%	12.64%	11.68%	12.00%
Reinvestment Rate =	50.99%	33.29%	43.58%	50.00%
Expected Growth Rate	6.17%	4.21%	5.09%	6.00%

The value of synergy

	<i>Inbev</i>	<i>SABMiller</i>	<i>Combined firm (status quo)</i>	<i>Combined firm (synergy)</i>
Cost of Equity =	8.93%	9.37%	9.12%	9.12%
After-tax cost of debt =	2.10%	2.24%	2.10%	2.10%
Cost of capital =	7.33%	8.03%	7.51%	7.51%
After-tax return on capital =	12.10%	12.64%	11.68%	12.00%
Reinvestment Rate =	50.99%	33.29%	43.58%	50.00%
Expected growth rate=	6.17%	4.21%	5.09%	6.00%
<i>Value of firm</i>				
PV of FCFF in high growth =	\$28,733	\$9,806	\$38,539	\$39,151
Terminal value =	\$260,982	\$58,736	\$319,717	\$340,175
Value of operating assets =	\$211,953	\$50,065	\$262,018	\$276,610

Value of synergy = 276,610 – 262,018 = 14,592 million ₁₂

Passing Judgment

- If you add up the restructured firm value of \$56.2 billion to the synergy value of \$14.6 billion, you get a value of about \$70.8 billion.
- That is well below the \$104 billion that ABInBev is planning to pay for SABMiller.
- One of the following has to be true:
 - I have massively under estimated the potential for synergy in this merger (either in terms of higher margins or higher growth).
 - ABInBev has over paid significantly on this deal. That would go against their history as a good acquirer and against the history of 3G Capital as a good steward of capital.