Use excess free cash
Reduce tax on the combined company due to tax losses of the acquired company
Other

3. Valuing a business acquisition opportunity
    a. Terminology for valuation
        i. Market capitalization
        ii. Enterprise value
    b. Valuation techniques
        i. Intrinsic valuation (DCF analysis)
        ii. Relative valuation
            a) Comparable companies market multiples method
            b) Comparable transactions method

	DCF Method	Market Multiples Method
Major Steps	• Free Cash Flows in the forecast period • Terminal value (after the forecast period) • Discount FCFs in the forecast period & terminal value with WACC	• Identify the target firm's comparable companies • Convert their market values into standardized values using a common variable (e.g. earnings), which creates market multiples (e.g. P/E ratios), and take the average of comps' multiples • Multiply the average multiple by the common variable (e.g. earnings) of the target firm, resulting in the estimate for its market value (e.g. market cap)
Strengths	• Forward looking and focuses on cash flows not on profits • Allows operating strategies/synergies to be built into a model • Valuation tied to underlying fundamentals	• Very common, convenient market-based method • Provide an alternative way to perform terminal value estimation
Weaknesses	• Only as accurate as assumptions and projections used • Need to forecast managerial behavior (unless you're in control) • Need to estimate the discount rate using a theory (e.g., CAPM) that may be imprecise or tricky in some cases	• Subject to distortions due to market misevaluation and accounting policy • Not directly incorporate the operational improvements and other synergistic efficiencies that the acquirer intends to implement • Identifying closely comparable firms is challenging • Choice of dates for comparing multiples can be arbitrary

        iii. Contingent claim valuation (real option analysis)
            - troubled firm
            - natural resource company
            - start-up firms or high growth firms

Classic Questions/Calculations

1. SEOs

a. Private placement:

Issued Shares:	Pre (m)	Pre (%)	Post (m)	Post (%)
. old s'holders	10	100	10	90.9
. new s'holders	0	0	1	9.1
Total	10	100	11	100

(10/11)*100
(1/11)*100

*new share price
=10/11*$10+1/11*$9=
$9.909

Value of Equity:	Pre ($m)	Post ($m)
. old s'holders	$100	$99.09
. new s'holders	0	$9.91
Total	$100	$109

← $9.909*10m
← $9.909*1m

b. Rights issue:

- Notations:
  - Subscription price (*S*)
  - Pro-rata entitlement (*1:N*)
  - *M* is the market price of the share *cum-rights*
  - *X* is the theoretical price of the share *ex-rights*
  - *R* is the value of the right
- Trading ***cum-rights*** and ***ex-rights***

i. exercise the rights
ii. sell the rights (if renounceable)
iii. do nothing

c. DRP

2. Finance Lease Value

1) Calculate incremental cash flow: leasing – borrow to buy

Leasing (1)

1	Lease payments		-$21,300	From year 0
2	Tax-shields from lease payment	0.34 x $21,300 =	+$7,242	From year 0

If pay in advance

Borrow-to-Buy (2)

3	Cost of asset		-$78,000	In year 0
4	Tax-shields from asset depreciation	0.34 x ($78,000/4) =	+$6,630	From year 1
5	Residual asset value		+$20,600	In year 4
6	Tax on gain from sale of asset*	-($20,600 - 0) x 0.34 =	-$7,004	In year 4

**Gain on sale = Residual Value - Book Value*
Book value = Historical cost - Accumulated depreciation = $0