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Sense & Nonsense

Our view on deal rumors

- Speculation on deals has resulted in sustained moves in the stocks of some companies, in contrast to daily and often unsubstantiated rumors.
- The Dow Jones Investment Banker column-writing team has taken a close look at some of these, taking into account the economic and strategic rationale – sometimes not the same thing – to come up with some hard-hitting conclusions.
- Some of our views are fleshed out in longer articles available only to subscribers of Dow Jones Investment Banker. These opinions often contain downloadable spreadsheets, PDFs, videos, exclusive graphics and links to primary sources.

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PE Interest In RadioShack Overplayed

Our View

RadioShack isn't cheap on a relative basis, and there is little for a private buyer to do to extract money. This deal shouldn't happen, and probably won't.

Key Stats

- **Sales:** \$4.3B
- **EV:** \$2.75B
- **EV/Ebitda:** 5.9x
- **Net Debt/Ebitda:** (0.5x)

Breakdown

- **The Run Up:** Stock up 12% on rumor of a private equity takeout by Apollo. Other potential PE buyers include firms such as Apax, KKR and Madison Dearborn.
- **Quick Take:** There are few levers that any private equity buyer can pull, i.e. real estate or non-core assets, to extract value out of Radioshack. While stock may be cheap at 5.9 times EV/Ebitda, it is not out of line with larger, more diversified peers such as Best Buy, which trades at a similar multiple.

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Danone Should Look Beyond Dean

Our View

Weak growth, low margins, and a rich valuation ought to make Danone look elsewhere —perhaps toward a baby formula deal.

Key Stats

- **Sales:** \$7.2B
- **EV:** \$7.2B
- **EV/Ebitda:** 7.7x
- **Net Debt/Ebitda:** 1.2x

Breakdown

- **The Run Up:** Shares up 5% on rumor of a takeover by Danone, the French dairy giant
- **Quick Take:** Takeover of low growth, low margin Dean is unlikely by Danone, which has spent the last few years diversifying away into baby food and medical nutrition, businesses that boast a better growth profile. Valuation of 7.7 times is not very attractive either for a largely private label food company. Danone would be better served by acquiring either Mead Johnson or Wyeth Nutrition, both of which will serve to enhance its market share in the fast growing and profitable baby foods category.

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Whirlpool In A Spin Over Private Equity

Our View

Whirlpool could carry LBO-leverage, but with the crisis fresh in mind, banks may not be ready to fund a \$10 billion deal. This one's on hold.

Key Stats

- **Sales:** \$17.1B
- **EV:** \$8.8B
- **EV/Ebitda:** 7.2X
- **Net Debt/Ebitda:** 1.1x

Breakdown

- **The Run Up:** Market whisper that private equity buyers may target Whirlpool
- **Quick Take:** Whirlpool's net debt/Ebitda of 1.1x suggests private equity could further lever up the company. Though sales fell 9.7% in 2009 from 2008 demand should pick up this year as the economy stabilizes. The company has enough cash flow to manage more debt but lenders have not been amenable to super-size buyouts – and a \$10 billion deal would probably be too much.

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AB InBev Shouldn't Quench Modelo Thirst Yet

Our View

In the long run, Modelo belongs with AB InBev, but management should be patient and avoid paying too much. Time is on their side.

Key Stats

- **EV:MXN233B/**
\$19B
- **EV/Ebitda:** 9.2x

Breakdown

- **The Run Up:** Heineken's acquisition of Femsa Cerveza earlier this year and sell-side analysts chatter put AB InBev's M&A strategy under the spotlight now that a significant portion of the company's debt has been rolled over to 2013 and 2015.
- **Quick Take:** Buying full control of Grupo Modelo likely tops AB InBev agenda, but the company's management would do well to be patient and play it cool. The price for the half of Modelo they don't own could be unreasonably high relative to the growth potential in the business. In addition, Modelo's strong current financial and strategic positioning may make it difficult for ABI to extract meaningful synergies.

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PE Could Stomach A Rich Nutreco

Our View

With little debt and a low enterprise value, Nutreco makes sense for a buyer who can stomach a rich valuation.

Key Stats

- **Market cap:**
EUR1.59B
- **EV:** EUR1.84B
- **EV/Ebitda:** 8.3x

Breakdown

- **The Run Up:** The market whisper is Nutreco could soon be on the block. Nutreco has been on the radar for quite some time; its stock price has rallied 66% since March 2009 and has outperformed the market by about 20 points (an absolute 20%) year on year.
- **Quick Take:** Nutreco's EUR1.84 billion enterprise value makes it an easy target for trade buyers, despite its valuation having shot up since March 2009. It offers low single-digit operating margins, but low gearing and significant cash flow generation could entice private equity firms.

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Pfizer Should Say Nada To Stada

Our View

Pfizer should pass on Stada—it can't reap significant costs savings and the business prospects aren't great.

Key Stats

- **Sales:** EUR1.5B
- **EV:** EUR2.6B
- **EV/Ebitda:** 9.5x
- **Net debt/Ebitda:** 3.1x

Breakdown

- **The run-up:** The share price of Stada, Germany's third-place generic drugs player, rose recently on rumors of a takeover by Pfizer, which had failed to win the auction for the country's number two company, Ratiopharm.
- **Quick take:** Any takeover in this space has to be driven by cost savings, which Pfizer won't be able to make, owing to few overlaps. If Pfizer couldn't match Teva's winning bid for Ratiopharm, there's no reason why it would pay a similar or higher multiple for Stada. Stada faces problems of its own, has been on the rumor mill for years (to no avail), and its business will be squeezed further by Teva's presence as Germany's number two.

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Leap Into The Arms Of MetroPCS

Our View

Leap Wireless should jump into the arms of MetroPCS. They need each other badly given the amount of consolidation going on.

Key Stats

- **Sales:** \$2.4B
- **EV:** \$3.5B
- **EV/Ebitda:** 9.6x
- **Net Debt/Ebitda:** 5.9x

Breakdown

- **The Run Up:** Leap Wireless' stock is up 30% since the start of the year on rumors of a merger with either MetroPCS or Deutsche Telekom's T-Mobile. The price suggests that a takeover premium is already factored in.
- **Quick Take:** Like MetroPCS, the company is a small player in the US market which should consolidate around the big four players. If MetroPCS bought Leap, the new company would be a better target in the long-term.

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Telefonica Will, In Time, Buy TI

Our View

Telefonica will clear up the complicated Telecom Italia holding structure by buying the whole of the company in time.

Key Stats

- **Sales:** EUR29B
- **EV:** EUR57B
- **EV/Ebitda:** 5.0x
- **Net Debt/Ebitda:** 3.0x

Breakdown

- **The Run Up:** Telecom Italia's stock spiked at the start of the year on a flurry of rumors that Spain's Telefonica will buy the company.
- **Quick Take:** Telefonica has a 43% stake in holding company Telco, which has a 22% stake in TI. It bought it at a much higher level, and while the value was written down to EUR2.2 a share, the price languishes nearer EUR1 a share today. While Telefonica does not want to be bounced into a deal, a full takeover is the sensible conclusion to this structure.

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Buyers For Palm Should Wait A Little Longer

Our View

The Palm operating system is number five in the market. While it has some value, it would be better to wait until the company is really in trouble before making an attempt to buy it.

Key Stats

- **Sales:** \$1.07B (e)
- **EV:** \$911B
- **EV/Ebitda:** -
- **Net Debt/Ebitda:** -

Breakdown

- **The Run Up:** Stock has been volatile as expectations were built up for the Palm webOS system, with the price going from \$2 to around \$17. However, sales have been weak and the stock fell sharply, only to bounce from \$4 to as high as \$8 on takeover rumors. Potential buyers mentioned include Lenovo and HTC.
- **Quick Take:** The Palm operating system is a distant number five in the market, after Apple, RIM, Symbian and Android. With around 1% of the market, it would need a company with strong marketing and deep pockets to make an impact on the other players. Palm is widely expected to run out of cash next year and therefore it would make sense for any prospective buyer to wait to buy the company. Given that Palm's annual R&D is around \$200M, an all-in price of around \$400M might make sense, given the situation. That said, it is unlikely that any buyer could turn webOS into a successful product given the competition.

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A Chinese Purchase Of Whitehaven

Our View

The trend of Chinese investment in Australian coal points toward a Whitehaven buyout

Key Stats

- **Sales:**
A\$412.2M
- **EV:**
AUD\$2.6B
- **EV/Ebitda:** 13.3x

Breakdown

- **The Run Up:** The Australian miner sits on 2.8M tons of saleable coal in New South Wales and port access at Port Waratah plus an 11% stake in a contractor developing a new coal terminal at Port of Newcastle.
- **Quick Take:** An acquisition or stake by a Chinese power company, steel maker or coal/energy company would fit in with the Chinese track record of investing in Australian coal assets.

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PE Has More Sense Than To Buy Harley

Our View

A big valuation, heavy debt, a troubled financing subsidiary, impending need for capital...smart buyers will stay away

Key Stats

- **Sales:** \$4.8B
- **EV:** \$12.7B
- **EV/Ebitda:** 18.3x
- **Net Debt/Ebitda:** 6.4x

Breakdown

- **The Run Up:** Harley stock is up 21% over the last three weeks on a rumor of a buyout by private equity giant KKR.
- **Quick Take:** A valuation of 18 times EV/trailing Ebitda and a burgeoning debt load of 6.4 times net debt/Ebitda makes any takeover unpalatable for a rational financial buyer. Further, rising retail delinquencies at HDFS, Harley's funding subsidiary, increases the risk profile of the company at a time when sales are expected to stay weak in light of high unemployment. The brand needs capital infusion to prop up product extensions. Maybe a rich banker or sheikh with passion for motorbikes could jump-start the brand repositioning.

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- Our exclusive insight is totally independent and adheres to Dow Jones' standards of editorial ethics
- Our focus is exclusively on the interests of investment bankers

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