



Deal Logic

Time Warner Inc. / AT&T Inc.

WHU Finance Society

Contact: info@whufinancesociety.org
Website: www.whufinancesociety.org

Date: 02.11.2018

Authors: Julius Fuhrmann, Benjamin Kryut, Jacqueline Zeiss, Mengyao Zhang

To continue receiving subsequent publications, subscribe by [clicking here](#).

Abstract

In the transformation driven by technology and stream-video challenges, media giants have taken acquisition strategies to uphold their current status and seek for vertical business expansion via entering content creation area. AT&T, the telecom and media giant, initiated an acquisition of Time Warner in October 2016 at a bid of USD 85bn, which was considered as the biggest M&A deal that year worldwide. But the process was blocked mainly by the US Department of Justice (DOJ) and stagnant for nearly 2 years. In June 2018, the vertical merger was approved by the U.S. District Judge and completed on 14.06.2018. Concerns about legitimate regulation should be largely taken into account of the evaluation of success of acquisitions.

I. Market Overview

The telecommunication services market had a value of around USD 1.4tn in 2017, and is forecasted to grow to almost USD 1.46tn in size by 2020. The biggest markets for telecom services are the Asia/Pacific region, Europe, and North America. On the basis of usage, entertainment, point-to-point communication, infotainment, news, internet-enabled services, and critical communication are the major categories.

Global entertainment and media revenues are set to rise at a CAGR of 4.2% to USD 2.2tn in 2021 according to PwC. A challenge for media companies is twofold: maintaining or even increasing content quality, while also finding ways to extract maximum value from that content. Advances in mobile, video, and wireless technologies have ignited an explosion in the growth of streaming services. Content discovery is another market opportunity for media and entertainment companies.

II. AT&T and Time Warner

For AT&T buying Time Warner is a way to set itself apart from its key rival, Verizon, which has done its own content deals by acquiring both AOL and Yahoo. Concerns about such a vertical integration are outweighed by the new wave of already vertically integrated, consumer-based digital giants like Netflix, Amazon, Apple or YouTube. To go on the offensive, AT&T will have to show that it can actually create more value from its ownership of Time Warner's assets than either company could capture before. It will be in a better position to collect information on users' watching habits and schedule or cross-promote shows, also with full ownership of the material it produces – an advantage when it comes to digital content.

III. Challenges During the Acquisition Process

Ever since the deal was announced in October 2016, it has received much public attention due to its high value and the potential of major anti-trust issue. The deal was also a highlight in the MEGA policies put forward by Trump's candidacy, claiming power would be centralized in the hands of too few companies.

In 2017, though the European Commission approved AT&T's acquisition of Time Warner, claiming that the acquisition would not raise competition concerns, the DOJ's anti-trust department filed a lawsuit to block the acquisition, saying the deal would impede innovation and threaten competitors. Soon, AT&T's CEO announced that the company will put up some resistance and emphasised that no vertical merger had been challenged in forty years and showed positive attitude for the suit.

After nearly one year of review, U.S. District Judge Richard J. Leon rejected all of the government's claims in June 2018 and the transaction was closed 2 days after.

IV. Impact on Industry & Takeaway

The vertical merger has the potential to transform the whole US media industry and reflects the few monopolies' fear and reaction strategies when being faced with the challenges powerful young tech and stream-video companies, especially FANG

Disney announced to buy 21st FOX in 2017 with Comcast, cutting in with a bid of USD 65bn. Shortly after AT&T continued its expansion in the content creation field by acquiring full ownership of Otter Media in August 2018.

All values in USDm, except Price, Initial (USD) & Price, Paid (USD)

Summary

Target	Time Warner Inc.
Acquirer	AT&T Inc.
Date, Announ.	22.10.2016
Date, Effective	14.06.2018
Deal Attitude	Friendly
Consideration	55% Cash / 45% Stock
%Held/%Acq.	0% / 100%
Deal Value	79,406.5
Price, Initial	100.1
Price, Paid	100.1
Total Fees	210
Premium*, 1d	20.6
Premium*, 1w	25.8
Premium*, 4w	30.4

* Pre-bid (%)

Sources: Thomson Reuters (Eikon, SDC Platinum)

Synopsis

- AT&T Inc acquired the entire share capital of Time Warner Inc for USD 79,406.5m
- AT&T offered USD 53.75 in cash and 1.437 common shares per Time Warner share
- Based on AT&T's closing stock price of USD 32.22 on 13 June 2018, the last full trading day prior to the announcement of the exact exchange ratio, each Time Warner share was valued at USD 100.1 per share
- The deal was subject to a collar agreement, which was dependent on AT&T's average stock price around the closing, resulting in the exchange ratio of 1.437
- Transaction is tax-exempt under IRC s386

LTM Transaction Multiples

	Target	Acquirer	Industry†
EV/Sales	3.10x	2.68x	3.5x
EV/EBITDA	5.80x	8.74x	15.5x
EV/EBIT	14.55x	9.64x	23.9x
EV/FCFF	17.90x	11.14x	42.0x
P/E	14.31x	8.85x	25.4x

† Of Target, Entertainment Production (own calculations), SIC: 78

Rationale

- Take advantage of innovation in media and communications sector through consolidation to offer new products and services in television, mobile, and broadband
- Accelerate delivery of content to customers
- Combined subscriptions and operations help pay for the cost of content creation
- Expected pre-tax synergies of USD 2.5bn:
 - USD 1.5bn in annualized cost synergies by end of year 3 following close
 - USD 1bn of annualized revenue synergies by end of year 3

Financial Advisors

Target	Fees	Acquirer	Fees
Allen & Company	50.0	Perella Weinberg Partners	n/a
Citigroup	50.0	JPMorgan Chase	n/a
Morgan Stanley	40.0	BAML	n/a

All values in USDbn, except EPS

Recent News*

- **2016/08:** The entertainment conglomerate said Wednesday that it has paid USD 583mn for a 10% stake in Hulu, joining an existing ownership group that includes Walt Disney, 21st Century Fox, and Comcast—each of whom now own a 30% stake.
- **2016/01:** Activist shareholders are circling the New York media giant with a view to pushing either a sale of the entire company or a spinoff of its valuable HBO business.
- **2014/08:** 21st Century Fox abruptly abandoned its takeover pursuit of Time Warner Inc., citing both Time Warner's unwillingness to "engage with us" and a sharp drop in Fox's stock price which made a deal "unattractive to Fox shareholders."

* Prior To Deal
Sources: Thomson Reuters Eikon, Capital IQ, Fortune, NY Post, WSJ

Company Description

- **Time Warner, Inc.** (now Warner Media, LLC), founded in 1985, is an American multinational mass media and entertainment conglomerate headquartered in New York City. The company operates in three segments:
- **Turner:** branded news, entertainment, sports, and kids multi-platform content
- **Home Box Office:** premium pay and basic tier television, and video content services comprising of HBO and Cinemax; HBO NOW
- **Warner Bros.:** television programming and feature films; digital and physical home entertainment products; and produces and distributes games, licenses consumer products and brands

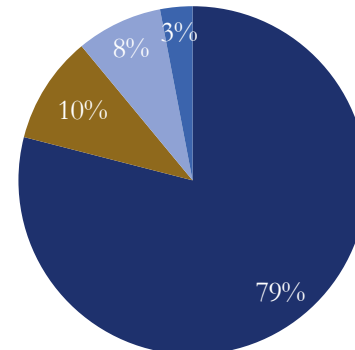
Key Management & Ownership Structure



John T. Stankey
CEO
Since 2018



Pascal Desroches
CFO
Since 2018



■ Norges bank Inv. Mgmt.
■ AP Fonden 7
■ Numen Capital LLP
■ Degroof Petercam Asset Mgmt.

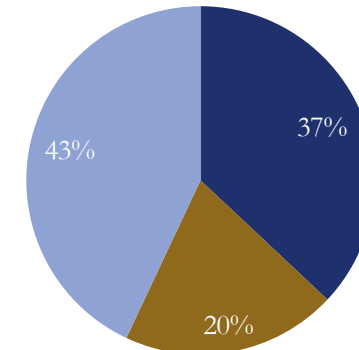
Key Financials

	2016A	2017A	2018E	2019F	2020F
Sales	29.3	31.3	32.7	34.6	
% growth	4.3	6.7	4.5	4.8	
EBITDA	8.6	9.1	9.3	9.6	
% margin	29.2	29.0	28.5	28.0	n/a*
Net Inc.	7.9	8.4	8.6	9.2	
% margin	27.0	26.8	26.2	26.8	
EPS	4.94	6.64	7.78	8.26	

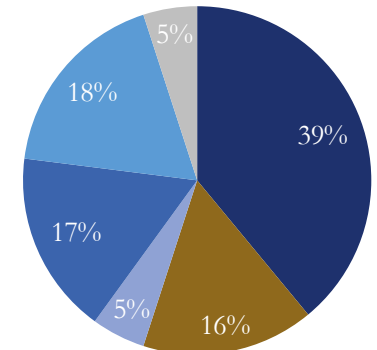
*Not available as Time Warner Inc. has been delisted from the stock market

Sales Split

Segments: FY2017 | Product: FY2018



■ Turner
■ Home Box Office
■ Warner Bros.



■ Subscription
■ Advertising
■ Content and other
■ Television Product
■ Games and other

All values in USDbn, except EPS

Recent News*

- **2016/10:** AT&T plans to issue about USD 40bn in new debt to finance the cash portion of its USD 85.4bn takeover of Time Warner; the balance sheet of the merged company would have so much debt on it — about USD 175bn — that it would exacerbate its position as the largest nonbank corporate issuer
- **2016/06:** Warren Buffett divided AT&T from Berkshire Hathaway's portfolio of high-yield dividend stocks during the first quarter of 2016. Warren Buffett acquired his stake in AT&T during the third quarter of 2015 as a result of AT&T's acquisition of DirecTV.
- **2015/07:** AT&T closed its USD 49bn acquisition of satellite television provider DirecTV on Friday, after the Federal Communications Commission ratified the deal. The deal will make AT&T the country's largest pay TV provider, with more than 26 million total subscribers

* Prior To Deal
Sources: Thomson Reuters Eikon, AT&T Inc Investor Relations and Company Filings

Company Description

AT&T Inc., founded in 1983 and based in Dallas, Texas, is the world's largest telecommunications company, the second largest provider of mobile telephone services, and the largest provider of fixed telephone services in the United States.

- **Business Solutions:** offers wireless services, strategic services, wireless equipment, and other services.
- **Entertainment Group:** provides video entertainment and audio programming channels, broadband and Internet services.
- **Consumer Mobility:** offers postpaid and prepaid wireless voice and data communications services, wireless wholesale and resale subscribers.
- **International:** offers digital television services, including DIRECTV and SKY brands throughout Latin America.

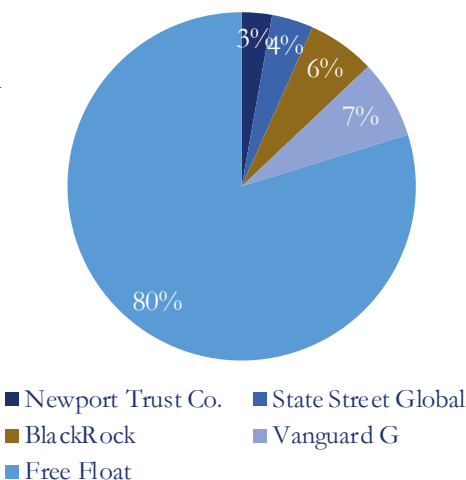
Key Management & Ownership Structure



Randall Stephenson
CEO
Since 2007



John Stephens
CFO
Since 2011

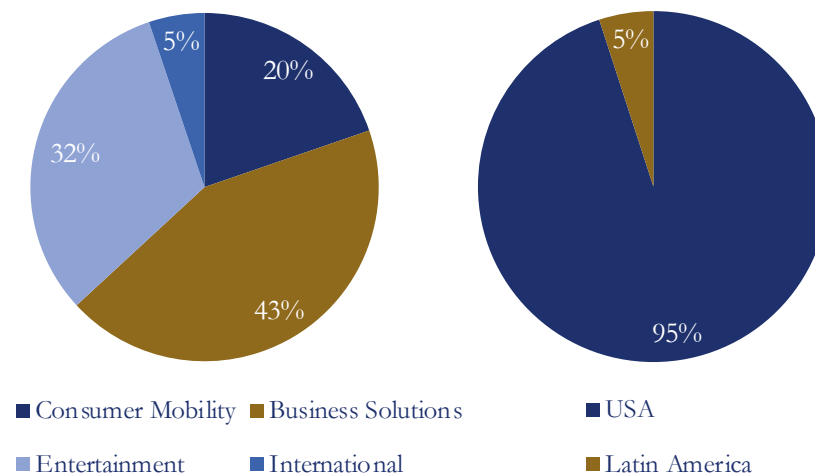


Key Financials

	2016A	2017A	2018E	2019F	2020F
Sales	163.8	160.8	171.2	185.2	185.7
% growth	11.6	(1.8)	6.4	8.2	0.2
EBITDA	52.5	51.5	56.2	60.8	60.7
% margin	32.1	32.0	32.9	32.8	32.7
Net Inc.	17.5	18.8	23.1	25.7	26.2
% margin	10.7	11.7	13.5	13.9	14.1
EPS	2.8	3.1	3.5	3.6	3.6

Sales Split

FY2017



Disclaimer

PRIVATE AND CONFIDENTIAL

This document is being sent to you for your information only by the WHU Finance Society e.V. (“WHU FS”) and should not be forwarded to any third party. This document should not be used as a basis for trading in the securities or loans of the companies named herein or for any other investment decision. This document does not constitute an offer to sell the securities or loans of the companies named herein or a solicitation of praxis or votes and should not be contrived as commenting of investment or tax advice. Past performance is not indicative of future results.

The views and opinions expressed may differ from the views and opinions expressed by WHU FS or other departments or divisions of WHU FS and its affiliates. Investors are urged to consult with their financial advisors before buying or selling any securities. WHU FS has no obligation to provide any updates or changes.

Any reference to a specific company or security listed herein does not constitute a recommendation to buy, sell or hold securities of such company nor does it constitute a recommendation to invest directly in any such company. This information should not be construed as research or investment advice regarding a particular security and should not be relied upon in whole or in part in making an investment decision.

Although certain information has been obtained from sources believed to be reliable, we do not guarantee its accuracy, completeness or fairness. We have relied upon and assumed without independent verification, the accuracy and completeness of all information available from public and non-public sources.

Views and opinions expressed are for informational purposes only and do not constitute a recommendation by WHU FS to buy, sell, or hold any security. Views and opinions are current as of the date of this document and may be subject to change, they should not be construed as investment advice.

Certain information set forth in this document contains “forward-looking information”, including “future oriented financial information” and “financial outlook”, under applicable securities laws (collectively referred to herein as forward-looking statements). Except for statements of historical fact, information contained herein constitutes forward-looking statements and includes, but is not limited to, the (i) projected financial performance of WHU FS; (ii) completion of, and the use of proceeds from, the sale of the shares being offered hereunder; (iii) the expected development of WHU FS’s business, projects and joint ventures; (iv) execution of WHU FS’s vision and growth strategy, including with respect to future M&A activity and global growth; (v) sources and availability of third-party financing for WHU FS’s projects; (vi) completion of WHU FS’s projects that are currently underway, in development or otherwise under consideration; (vi) renewal of WHU FS’s current customer, supplier and other material agreements; and (vii) future liquidity, working capital, and capital requirements. Forward-looking statements are provided to allow potential investors the opportunity to understand management’s beliefs and opinions in respect of the future so that they may use such beliefs and opinions as one factor in evaluating an investment.

These statements are not guarantees of future performance and undue reliance should not be placed on them. Such forward-looking statements necessarily involve known and unknown risks and uncertainties, which may cause actual performance and financial results in future periods to differ materially from any projections of future performance or result expressed or implied by such forward-looking statements.

Although forward-looking statements contained in this document are based upon what management of WHU FS believes are reasonable assumptions, there can be no assurance that forward-looking statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. WHU FS undertakes no obligation to update forward-looking statements if circumstances or management’s estimates or opinions should change except as required by applicable securities laws. The reader is cautioned not to place undue reliance on forward-looking statements.

©WHU Finance Society e.V. All rights reserved.
