

EFB343 Corporate Finance - Group Assignment

Coverage: Topics 2-5

Length: Approximately 2,000 words (Guide: 1,500 words for Part A; 500 words for Part B; excluding calculations, tables and appendices)

Due date: Sunday, 13th October 2019 (Week 11) at 11:59pm

Weighting: 40%

Assignment objectives:

1. To gain an understanding of the investment decision-making process in relation to assessing mergers and acquisitions (M&A hereafter) opportunities.
2. To explore the dynamics of corporate valuation used in M&As and understand the process of information retrieval, limitations of valuation methods and the impact of uncertainty on the valuation process.
3. To develop valuable teamwork skills that will be sought-after and highly valued once you have left university.

Group formation and assignment submission:

Students are to complete this assignment in groups of 2-5 members. All group members must sign on the same group number on Blackboard. Submission of the assignment must be through Blackboard, NOT via email (further instruction will be provided). Students are required to complete and submit all calculations in an Excel file. The report must be submitted in a PDF file.

The assignment consists of: (1) a group component (Part A), which is to be completed by the group; the grade awarded for Part A will be the same for each group member; and (2) an individual component (Part B), which is done separately by each group member; the grade awarded for Part B will vary depending on the quality of individual reports.

Reports for Parts A and B should be combined and submitted in a single PDF document, with reports for Part B having a clear indication of the individual writer's name and student ID for marking purposes.

*****All assignments will be cross-checked for plagiarism! Please do your work within your group only!*****

Assignment information:

This assessment task is worth 40% of your overall grade for the unit, with marks allocated in accordance with the assignment task outlined below:

- Part A – Target selection and firm valuation (30%)
- Part B – Individual self-reflection (5%)

Please see each part for detailed instructions. You will be required to present your findings/answers in a formal report. An additional 5% is allocated to your writing skills. Please see the criteria sheet for a more detailed explanation of our expectations.

Assignment Task

You work for a prestigious investment bank, Credit Suisse (CS), which has been recently commissioned by Intel Corporation (Intel hereafter) to investigate potential M&A opportunities. The lead partner has asked you to prepare a report with a detailed summary of your assessment and evaluation of potential takeover targets.

PART A – TARGET SELECTION AND FIRM VALUATION (30%)

Intel is seeking to grow through M&As. Your major task is to locate one target firm that would interest Intel and make a deal. Towards this end, you and your team are required to investigate all *listed firms* around the world and identify three target candidates. *At least one of the target candidates must be a listed firm in the U.S.* There is no limitation on the industry in which the potential target candidate operates, so long as decent synergies can be created through this M&A and it fits the current and future strategic goal(s) of Intel. It's a challenging task. You and your team should do it following the step-by-step guide below.

Step 1. Conduct a full SWOT analysis (Strengths, Weaknesses, Opportunities and Threats) of Intel.

Hint: Analyze Intel's strategy, market position and industry overlook. Useful information can be obtained from Intel's most recent 10K Annual Report (provided) and other sources such as business press and news articles.

(4 marks)

Step 2. Based on your SWOT analysis, decide whether Intel should make a diversifying, vertical or horizontal M&A. Justify your choice.

(3 marks)

Step 3. Use the questions below as potential selection criteria to identify three listed target firms that can potentially interest Intel. *At least one of the target candidates must be a listed firm in the U.S., and it must have at least five years of accounting information necessary to conduct evaluation in Step 4.* To check the availability of accounting information, search for the firm's annual reports on Form 10-K using the "Company Search" for the U.S. SEC's [EDGAR database](#).

Carefully address the following questions about the proposed target candidates. In your answer, you should be specific and back up your arguments by linking them to the *actual* characteristics of the merging firms, i.e., Intel and the proposed target firm.

- a.** Identify at least two channels through which synergistic gain can be created through the acquisition of each of the proposed target candidates.

Hint: For example, synergy gain can arise when a target firm has: (i) a pipe line of innovative projects that can potentially lead to promising products in the future; (ii) strong expertise that allow Intel to expand its existing expertise; or (iii) a presence in a fast-growing market in which Intel wants to enter in. Here, do some brainstorming! To be specific, you should clearly specify, for instance, the type of potential products in Example (i).

(6 marks)

- b.** Discuss how likely Intel can successfully integrate each of the target candidates' business, technology, human capital and other resources to materialize potential efficiencies and synergies that motivate the deal.

(3 marks)

- c. Identify at least three external/internal factors that can potentially lead to a failed takeover attempt (i.e., the deal goes bust). Discuss the relevance of these factors and whether they present threats to the success of any of your proposed deals, i.e., the probability of Intel successfully acquiring the proposed target firm.

(6 marks)

Step 4. Use the Free Cash Flow Methodology to estimate the value of the target candidate (as identified in Step 3) that is a listed firm in the U.S. and has at least five years of accounting information necessary for evaluation. Narrow it down to one particular target if you have more than one target firm that meets the above criteria. The purpose of this valuation is to establish a minimum offer price for the target firm.

Here you need to use the target firm's past five years financial data to forecast the firm's future sales, variable cost, fixed cost, depreciation, working capital and capital expenditure. You then need to work out the WACC (Weighted Average Cost of Capital) which will be used as the discount rate in your free cash flow analysis. Below is a step-by-step guide:

Construct future cash flows to firm:

- Use the average sales growth rate over the last five years to forecast sales in the next 4 years.
- Variable cost is assumed to grow at the same rate as sales.
- Use the average depreciation over the last five years as the depreciation for the future.
- Use the average fixed cost over the last five years as the fixed cost for the future.
- Use the average sales to working capital ratio over the last five years to work out the future levels of working capital.
- Use the average capital expenditure over the last five years as the future capital expenditure.
- Make assumptions about the growth rate of future net cash flow after year 4. Justify your assumption.

Calculate the discount rate (WACC):

- Get the equity beta of the firm from [Yahoo Finance](#); Risk free rate is assumed to be 2% and market risk premium is assumed to be 5%.
- Work out the cost of debt of the firm by searching for information about the effective interest rate in the firm's latest 10K annual report. If such information is unavailable, use the interest payment and its long-term debt to work out the cost of debt.
- Use the book value of long-term debt (or total liability) and market value of equity to work out the proportion of debt and equity in your WACC formula.

Calculate the value of the target firm:

- Find the present value of the cash flows for year 1-4 as well as the terminal value to get the value of the firm.

(8 marks)

**** Keep your calculations and formulas as simple as possible - don't make them overly complicated. It can make your assignment difficult to understand which can lead to us not allocating full marks for your effort, particularly when your answer is incorrect! ****

PART B – INDIVIDUAL SELF-REFLECTION (5%)

Your lead partner commends you on your group effort in preparing the preliminary report for his perusal. As a final task, he has asked each of your group members to reflect on their personal experience of working in a group in such a fast-paced and competitive working environment. Specifically, he has asked each of you to address the following two issues (make sure you address both):

1. Reflect on your role and contributions to the group.

Hint: You can discuss your contribution to various group processes such as formation of the group, organization of group meetings, establishment and enforcement of group policies designed to deal with team problems (e.g., free-riding), and provision of feedback to other group members.

(2 marks)

2. What are the two main lessons you have learned that can help improve your teamwork next time?

(3 marks)

As you prepare your reflection on the above two tasks, make sure to draw on specific examples to back up your points.

===== End of Assignment =====

For your reference only

This group assignment provides you with the opportunity to develop and practice a host of teamwork skills that are increasingly important in today's professional world — it is a highly desirable graduate attribute that can set you apart from other graduates. Here are some techniques that may help you to build a well-functioning team.

At the Beginning:*Let's sit down and talk*

- Have a thorough discussion with your potential teammates to find out whether you all share the same goal, e.g., achieving 7/6/5, and are motivated and committed to work together towards achieving this goal.

Set clear individual responsibility and accountability

- Write down and agree on what needs to be done and by whom; Use individual strengths to allocate tasks.
- Write down and agree on the deadline for individual tasks.
- Ensure all members have a role to play in working toward the team goal.
- It is recommended that you select a team leader/coordinator who can be in charge of overseeing the process, e.g., make sure individual team members complete their task(s) timely; process stays on schedule; output meets the quality standards as planned.

Determine the consequences for non-adherence to rules

- Working in teams can be both rewarding and challenging. To ensure effective teamwork, it is important for group members to write down and agree on possible consequences for non-adherence to rules. In this case, a “group contract” can be potentially helpful.
- Here is a [Sample Group Contract](#) from the Teaching, Learning, and Technology Centre, UC Irvine. Feel free to make changes to create your own contract that reflects your group's expectation, policies, etc. Once a contract is created, it's recommended that each group member sign to indicate their agreement to the contract and to ensure the validity of the contract.

During the Process:*Keep good records*

- Summarise discussions within meetings and share minutes with team
- Ensure all team members agree to decisions as recorded

Stick to the plan and monitor progress

- Follow through on plan
- Discuss progress or other issues regularly