

UNIVERSITY OF ROCHESTER

William E. Simon Graduate School of Business Administration

Finance 423
Corporate Financial Policy & Control

Professor G. William Schwert
Winter 2008

Case 2: Microsoft and Yahoo Takeover

Study the recently announced takeover offer by Microsoft for the acquisition of Yahoo. One article from the *Wall Street Journal* is attached. Also, data for the closing stock prices of these companies, along with the S&P 500 index, are available in a spreadsheet on the case web page. You may use any information that is available as of February 15, 2008, but you may not let events that occur after February 15 influence your analysis.

Your assignment is to analyze this takeover battle from the perspective of each of these firms, and to make recommendations for each of these firms about how to proceed in the future with respect to this takeover. Among the set of questions you should address include (but are not limited to):

- (1) Do you think that Microsoft will eventually acquire Yahoo on the current terms? If not, why not?
- (2) Do you think that one of Yahoo's competitors will try to block this merger through litigation and/or regulatory battles? If so, which strategy should they pursue, and is this a $NPV > 0$ project for them?
- (3) Is it likely that the relevant regulatory authorities will allow this merger to occur? Why?
- (4) Is it likely that Yahoo shareholders will seek to obtain a higher price from Microsoft? Will they sue Yahoo management?

You must prepare a report summarizing your analysis (due March 11) and be prepared to defend your position in class.

February 1, 2008 9:58 a.m. EST

Microsoft Unveils \$44.6 Billion Bid For Web Ad, Search Rival Yahoo


By **KEVIN J. DELANEY** and **ANDREW EDWARDS**
February 1, 2008 9:58 a.m.

Microsoft Corp. offered \$44.6 billion to buy **Yahoo** Inc., in a bold attempt to dramatically expand its online business and compete more effectively with **Google** Inc. in services ranging from email to Internet advertising sales.

The offer was made in a letter sent Thursday by Microsoft Chief Executive Steve Ballmer to Yahoo's board of directors. One person familiar with the matter said that Microsoft decided to "go hostile" with its bid within the last few weeks after Yahoo ignored its latest overtures.

The offer, \$31 a share in cash and stock, is a 62% premium to Thursday's closing price. Microsoft said Yahoo holders would be able to trade their shares for cash or 0.9509 Microsoft shares a piece, with no more than half of the overall purchase price paid in cash.

DOW JONES REPRINTS

 This copy is for your personal, non-commercial use only. To order presentation-ready copies for distribution to your colleagues, clients or customers, use the Order Reprints tool at the bottom of any article or visit: www.djreprints.com.

- [See a sample reprint in PDF format.](#)
- [Order a reprint of this article now.](#)

MORE

- [Vote: What do you think of Microsoft's offer?](#)¹
- [Text of Microsoft statement, letter; Yahoo response](#)²
- [Deal Journal: Live blogging the Microsoft conference call](#)³



Ballmer

RECENT HEADLINES

- [Yahoo's Bostock Succeeds Semel as Chairman](#)⁴
02/01/08
- [Google's Quarterly Growth Disappoints](#)⁵
02/01/08
- [Yahoo Says It Faces 'Headwinds'](#)⁶
01/30/08

FROM THE ARCHIVES

- [Microsoft Ad Chief Quiets Rumors of Yahoo Deal](#)⁷
05/23/07
- [With Big Buy, Microsoft Joins Online-Ad Flurry](#)⁸
05/19/07
- [Microsoft's Deal Dance With Yahoo](#)⁹
05/05/07
- [Yahoo Executive Calls for Overhaul](#)¹⁰
11/18/06
- [Microsoft Learns to Love Online Advertising](#)¹¹
11/16/06

"We're very, very confident that it's the right path for Microsoft and for Yahoo," Mr. Ballmer said in a conference call Friday. The bid is "the next major milestone in Microsoft's companywide transformation to embrace online services overall and to invest very successfully" in online search advertising.

Mr. Ballmer said he discussed the offer late Thursday with Yahoo Chief Executive Jerry Yang. He also signaled the announcement of Microsoft's deal was aimed particularly at Yahoo's employees. Morale has been an issue at Yahoo as the company has struggled and prepares for a round of layoffs.

In a statement, Yahoo acknowledged that it received the proposal from Microsoft and said that its board of directors "will evaluate this proposal carefully and promptly in the context of Yahoo's strategic plans and pursue the best course of action to maximize long-term value for shareholders."

The offer may be an attempt to get Yahoo back to the table after the companies held collaboration discussions in late 2006 and early 2007. Those talks included the potential of a merger proposal, but Yahoo told Microsoft in February it wasn't interest in buyout talk.

Any combination would likely attract the attention of antitrust regulators in the U.S. and Europe.

An acquisition of Yahoo would give Microsoft massive firepower in its long-running effort to boost its online offerings. The two companies are second and third in the hot area of Web search behind Google and among the top sellers of advertising online. In his letter to Yahoo, Mr. Ballmer said the online advertising market is "increasingly

dominated by one player," a reference to Google. "Together, Microsoft and Yahoo can offer competitive choice while better fulfilling the needs of customers and partners," he added.

Yahoo shares soared on the news, jumping 49%, or \$9.44, to \$28.60 in morning trading on the Nasdaq Stock Market. Microsoft fell \$1.26 to \$31.34, also on Nasdaq.

Microsoft noted the market for online advertising is "increasingly dominated by one player. Together, Microsoft and Yahoo can offer competitive choice while better fulfilling the needs of customers and partners."

The company added the deal would also result in "combined engineering talent to accelerate innovation," a hint that Microsoft can't alone take on Google with its current staff. Microsoft executive Kevin Johnson said a merger would result in "R&D critical mass to deliver innovation breakthroughs. The industry will be well served by having more than one strong player."

Renewed takeover speculation fired up after Yahoo late Tuesday posted a drop in fourth-quarter net income and issued a 2008 outlook that fell short of analysts' expectations.

Speculation about a Yahoo buyout has swirled since last year, when Microsoft's interest in such a deal was reported. Buying Yahoo would theoretically place Microsoft as significant competitor in the Internet search market, where it has so far lagged behind both Yahoo and Google. Microsoft, which has thriving software businesses that could fund a much deeper foray into Internet markets, hadn't actively dispelled rumors it was considering an acquisition of Yahoo.

The proposal is subject to the negotiation of a definitive agreement between the two companies. Microsoft is saying a deal could close in the second half of the year.

--Matthew Karnitschnig contributed to this article.

Write to Kevin J. Delaney at kevin.delaney@wsj.com¹² and Andrew Edwards at andrew.edwards@dowjones.com¹³