

EVALUATING THE CONDITIONS AND TERMS OF THE AT&T AND DIRECTV MERGER

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ABSTRACT

On May 18, 2014, AT&T Inc., the second-biggest U.S. mobile-phone carrier, agreed to acquire DirecTV, a satellite-television company, for \$49 billion. At the time of announcement, DirecTV had a market value of \$45 billion after its shares rose 43 percent in the past year. Speculation about an AT&T-DirecTV combination was not new. Back in 2010, AT&T had already considered such deal to be “industrial logic”, but it worried that regulators might not allow the transaction. The talks with DirecTV emerged quickly after AT&T was restricted from buying Vodafone Group Plc, Europe’s largest mobile carrier, due to U.K. takeover regulations. In the meantime, Comcast Corp.’s failed intent to acquire Time Warner Cable Inc. to create an even bigger provider of both TV and Internet in the U.S. had accelerated the drive for consolidation in the rest of the industry. As AT&T currently faced increased uncertainty in both the wireline and wireless business, the acquisition of DirecTV could not come at a better time, which would provide AT&T with earnings growth and additional spending flexibility.

However, the terms and conditions of the AT&T and DirecTV merger are complicated. First, each DirecTV share will be converted into a number of AT&T shares, equal to a pre-determined exchange ratio plus \$28.50 in cash at the close of the deal. The exchange ratio varies between 1.724 shares to 1.905 shares of AT&T. Second, the exchange ratio is contingent on the average AT&T stock price, which is determined by the average of the volume weighted averages of the trading AT&T share prices on each of the thirty consecutive trading days ending on (and including) the trading day that is three trading days prior to the date of the effective time of the merger.

The purpose of this paper is twofold. First, we intend to evaluate the operational, strategic, and financial impacts of the AT&T-DirecTV merger on AT&T, the surviving company. Second, we will use a simple contingent claims pricing approach to model DirecTV’s stock price, to determine whether it was fairly priced prior to the approval of the Federal Communications Commission. The results of this paper will be presented at the conference.