



Thinking Your Way Through A Corporate Takeover

Description

There are few better feelings than waking up to the news that a company you own shares in has received a takeover offer at a significant premium to the prior day's close. An immediate sense of bravado takes over and for the first time in months, you are very likely to log in to your quote provider of choice at 9:30am, as the market opens, to bask in the glory of your new found wealth.

But wait. What if that price you see as the market opens isn't the takeover price you read about. It's higher! What's going on? How high could this thing go? Both very fair and very human questions. However, when it comes to investing, thinking like a human doesn't tend to work. To best handle this kind of scenario, we don't want you to think like a human. We want you to think like a Fool!

We Got a Live One

This very scenario is currently playing out in the Canadian market as **First Quantum** ([TSX:FM](#)) has made a third offer for fellow copper producer **Inmet** (TSX:IMN). After being rebuffed by Inmet's board at \$62.50 and \$70, First Quantum is taking its new offer of \$72 per share to Inmet's owners, the public shareholders, to seek their approval. Inmet shares however currently trade above this \$72 level, an indication that the market expects First Quantum, or somebody else, to pay even more.

This kind of scenario can leave Inmet shareholders, or any shareholder of a company facing a similar situation, scratching their head as to what to do next. What's the right move? The way we see it, there are three options, two primary and one hybrid.

Option #1

The first option is to take the market price that is higher than the bid, and liquidate your entire position. Essentially, take the money and run, thus removing all risk that the deal goes through at the offered price (lower), or worse, doesn't go through at all. While selling out will allow you to immediately line your pockets, it doesn't necessarily allow you to participate if subsequent bids are made. This could mean you're leaving thousands of dollars on the table. Not ideal from a financial standpoint, but potentially much worse when it comes to your investment psyche as your regret from selling could be significant.

Option #2

Do nothing. This implies that you are whole heartedly convinced that another bid is coming. By doing nothing, you are trading the risk that the deal falls through for the upside potential that another bid would bring.

Option #3

The hybrid solution involves selling a portion of your holdings, but holding onto the rest in case another bid does arrive. From an emotional standpoint, the hybrid is in most cases the easiest to digest. By selling some of your position, you are at least able to crystallize a portion of the gain you have made. In addition, you are reducing the risk that something goes awry with the deal. Even if it falls through, chances are that you're still going to feel good about yourself for having taken some money off the table.

On the other side, you leave the door ajar to participate should a higher bid appear. In this case, you won't feel the regret that you would have had you completely sold out (option #1), although you'll be less well off financially than you would have been had you just gone with option #2.

Learning From Each Other

For investors, this whole process boils down to "regret minimization," a term that I first heard from Motley Fool co-founder David Gardner, who in turn had it described to him by Amazon.com founder Jeff Bezos. These corporate transactions have a lot of variables at play. You want to make the decision that will minimize your regret, regardless of how it all plays out.

Even though we're dealing with a financial transaction here, we suggest that whatever action Fools take should maximize that initial sense of awesome that you felt when you first learned of the takeover. This doesn't always mean maximizing your profit. Understand your financial upside, and downside, before making a decision but under most of these takeover situations, your brain will thank you for taking the hybrid route.

Neither Iain Butler nor The Motley Fool owns any of the stocks mentioned in this article.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:FM (First Quantum Minerals Ltd.)

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Date

2025/09/28

Date Created

2013/01/09

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