3 Winners and Losers From Latest M&A Deal

Description

Fool contributor David Jagielski couldn't have compared two more newsworthy stocks if he tried.

In a head to head between **Metro, Inc.** (TSX:MRU) and **Jean Coutu Group PJC Inc.** (TSX:PJC.A), Jagielski opted for the drugstore chain with its higher dividend, simpler operation, and less exposure to a rising minimum wage.

Well, as it turns out, owning either stock would have made you money September 27 on the news that Metro was in talks to buy Jean Coutu for $4.5 billion, or $24.50 per share; Metro and Jean Coutu were up almost 10% and 6%, respectively, with an hour to go in the day's trading.

According to the information available, Metro is using cash for 75% of the purchase price and issuing stock for the remainder. Offering a 6% premium to its September 26th closing price, Metro is paying about 14 times EBITDA to acquire the Montreal-based drugstore operator.

Like all deals, there are winners and losers. Here are three I feel win or lose in a completed transaction.

Winner: Jean Coutu, the founder

As of June 3, 2017, Jean Coutu owned 107.5 million of the company's 184 million shares outstanding — a 58% economic interest in the drugstore chain he founded back in 1969. In addition, the founder holds 93% of the voting shares, so no deal gets done without his blessing, which he's reportedly given.

If the terms of the deal remain the same, Coutu will get almost $2 billion in cash and $650 million in Metro shares, which works out to 15 million based on Metro's September 27 share price.

That will pay for a lot of prescription drugs for the octogenarian and his family.

For Metro shareholders, it means a lot more debt because it has very little cash. Metro has $1.4 billion in debt at the moment; it will add $3.4 billion in the deal, bringing the total to $4.8 billion if and when it's completed. On top of that, it will have to issue approximately 25 million shares to make up the $1.1 billion remaining.

Jean Coutu's shares will give him 5.9% of the approximately 252 million shares outstanding after Metro issues new shares as part of the purchase price. Coutu would likely be the company's largest individual shareholder.

I'd say that's a win.

Winner: Alimentation Couche Tard

As many **Alimentation Couche Tard Inc.** (TSX:ATD.B) shareholders are aware, Metro owns 32 million shares of the convenience store operator, which represents 22% of the votes. That's down from its previous ownership levels but remains significant.

Metro needs cash if it wants to reduce the amount of debt it must borrow to pay for Jean Coutu. Couche Tard executive chairman and co-founder Alain Bouchard needs to buy a substantial amount of shares in order for him and the other co-founders to retain control of the business.

In a previous article about Couche Tard, I suggested that the founders had a 23% economic interest in the company, but they controlled the voting shares through a dual-class share structure that's set to expire in 2021.

Based on 568 million shares outstanding, the economic interest is actually 20%. If the founders were able to come up with the $2 billion to buy Metro's shares, its economic interest rises to 25% — more than double Fidelity's ownership position.

As I stated previously, Couche Tard shareholders ought to think hard about the impending deadline. Metro helped it get off the ground a long time ago; it's time for Couche Tard to return the favour.

Loser: Empire Company

With a successful merger, Canada will have two large grocery/pharmacy businesses — the other being **Loblaw Companies Ltd.** — leaving **Empire Company Limited** (TSX:EMP.A) on the outside looking in.

Unfortunately, because it paid almost $1.5 billion too much for Safeway back in 2013, it couldn't enter the bidding even if it wanted to. Sure, Empire has Lawton Drug Stores on the East Coast, but it's hardly the same thing.

While the turnaround at Sobeys might be underway, a Metro/Jean Coutu tie-up leaves Empire's biggest investment stuck in third place — likely, permanently.

Where I sit, Empire Company is the biggest loser of all.

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Date
2025/08/26
Date Created
2017/10/02
Author
washworth