Quebec's Favourite Convenience Store Operator Just Got a Floor Price

Description

It's probably the worst-kept secret so far in 2017.

Metro, Inc. (TSX:MRU) announced October 12 that it was selling 85% of its 32 million shares in **Alimentation Couche Tard Inc.** (TSX:ATD.B) to fund its $4.5 billion acquisition of **Jean Coutu Group PJC Inc.** (TSX:PJC.A).

When Metro announced the deal to buy the Quebec drug store October 2, I immediately speculated that the four founding shareholders, including executive chairman Alain Bouchard, would buy the Metro stake to further their hold on the world's second-largest convenience store operator.

My rationale was that Metro helped Couche Tard in the early stages of its growth; it was now time for the company to return the favour. It did, but not exactly as I thought it would.

Couche Tard gets a new crew of shareholders

Metro needed cash for its acquisition, so it was clear from the outset that it would look for a buyer; it found three.

In the first transaction, Metro sold 11.37 million Class B shares (one vote per share) to a couple of investment dealers in a bought deal arrangement for $57.17 per share. That brought in $650 million. The second deal saw it sell 11.37 million Class A shares (10 votes per share) to Caisse de dépôt et placement du Québec, the Quebec pension fund, also for $57.17 per share and proceeds of $650 million. Finally, the third deal saw Couche Tard (not Bouchard or the three other founders) repurchase 4.37 million Class B shares for cancellation, also at $57.17 per share.

So, Couche Tard trades Metro for the Caisse and whomever the investment dealers can get to buy the shares above $57.17 a share.

Several things to note about these transactions

First, and most importantly, is the fact these transactions establish an artificial floor price of $57.17, which should give Couche Tard shareholders a warm fuzzy feeling. That's because the Caisse is all about delivering returns for Quebec shareholders. It's not about to buy any Couche Tard shares for $57.17 if it doesn't feel they're worth more than that.

As I write this, Couche Tard shares have closed October 12 trading at $61.24 — 7.1% higher than what all three buyers paid for their shares, which brings me brings me to my next point about the transactions.

Although Bouchard and the rest of the founders didn't buy any of the shares Metro put up for sale, the company repurchased 4.7 million shares, which lowers the total number outstanding, increasing the founder's grip on the company if ever so slightly.

Normally, I'm not a big fan of share repurchases, because they're often done at inflated prices, but given its history with Metro, it really had no choice but to take some of the action. The buyback is a case of win/win.

Metro makes tactical error

Lastly, and this is directed to Metro shareholders, your company just paid a significant price to get a deal done, because when it announced the acquisition, the shares were worth $1.84 billion; it sold them for $1.55 billion — $290 million less for a 16% haircut. It could have borrowed the $1.55 billion for much less while holding on to a valuable asset.

Metro sold part of its stake in Couche Tard back in January 2013 to three banks for $47.90 per share ($15.97 per share adjusting for three-for-one stock split). In hindsight, it shouldn't have done that. Given the terms of the latest deal, I don't think it should have sold at this point, either.

Metro had 15 million Class A shares in July 2012 and 5.7 million Class B shares. Today, if it kept all of them, it would have 45 million Class A shares and 17.1 million Class B shares worth $3.8 billion.

So, not only did it get $290 million less than the going rate for selling the 27.1 million shares, it also lost $1.8 billion by selling in 2013.

This is a big win for Couche Tard.

For Metro, it'd better hope the integration of Jean Coutu goes well, or this could turn out to be one of the worst M&A deals in Canadian history.

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