

## THE \$85.4 BILLION MERGER OF AT&T AND TIME WARNER: VALUATION ANALYSIS<sup>1</sup>

*Professors Xiaokang Zhao and Frank Li wrote this case solely to provide material for class discussion. The authors do not intend to illustrate either effective or ineffective handling of a managerial situation. The authors may have disguised certain names and other identifying information to protect confidentiality.*

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On October 22, 2016, Janey Frank, a portfolio manager at Uria Investment, was shocked by an announcement made in a conference call by Jeff Bewkes, the chairperson and chief executive officer (CEO) of US television media giant Time Warner Group (Time Warner). Bewkes stated that Time Warner would soon merge with the telecommunications (telecom) operator AT&T Inc. (AT&T), formerly American Telephone and Telegraph Company. AT&T would acquire Time Warner for US\$107.50<sup>2</sup> per share, half in cash and half in stock.<sup>3</sup> In a report Time Warner filed, as required by the US Securities and Exchange Commission (SEC), Bewkes made the following statement:

This transaction is an excellent outcome for our shareholders and it's an excellent opportunity to drive long-term value into the future. We believe combining with AT&T is the natural next step in the evolution of our business and it is one that allows us to significantly accelerate our most important strategies. We believe that putting these complementary businesses together will drive innovation and accelerate the transition of the ecosystem to more and better choices for consumers.<sup>4</sup>

Time Warner also announced that the two companies had started formal negotiations as early as August 2016 and were expected to complete the deal in 2017. The merger between one of the largest distributors of content and one of the biggest producers of content, if approved in the antitrust trials that followed, would be the largest global acquisition during the year.<sup>5</sup>

AT&T agreed to buy Time Warner's total equity of 783.8 million outstanding shares for \$85.4 billion. Together with Time Warner's net debt, this would cost AT&T \$108.7 billion, the total enterprise value. Before the merger was announced, Time Warner's stock price was \$79.50 per share; the acquisition price

<sup>1</sup> This case has been written on the basis of published sources only. Consequently, the interpretation and perspectives presented in this case are not necessarily those of AT&T Inc. or Time Warner Group, or any of the employees.

<sup>2</sup> All currency amounts are in US\$ unless otherwise specified.

<sup>3</sup> "AT&T to Acquire Time Warner," news release, AT&T, October 22, 2016, accessed March 27, 2019, [http://about.att.com/story/att\\_to\\_acquire\\_time\\_warner.html](http://about.att.com/story/att_to_acquire_time_warner.html).

<sup>4</sup> Time Warner Inc., "Form 425, Pursuant to Rule 425 under the *Securities Act of 1933* and Deemed Filed Pursuant to Rule 14a-12 under the *Securities Exchange Act of 1934*," US Securities and Exchange Commission, 2016, accessed February 26, 2019, [www.sec.gov/Archives/edgar/data/1105705/000110570516000031/form425.htm](http://www.sec.gov/Archives/edgar/data/1105705/000110570516000031/form425.htm).

<sup>5</sup> Roger Yu, "AT&T Agrees to Buy Time Warner for More than \$80B," *USA Today*, October 22, 2016, accessed June 25, 2019, [www.usatoday.com/story/money/2016/10/22/reports-t-agrees-buy-time-warner-more-than-80b/92589816/](http://www.usatoday.com/story/money/2016/10/22/reports-t-agrees-buy-time-warner-more-than-80b/92589816/).

of \$107.50 implied a 35 per cent premium.<sup>6</sup> If Time Warner were to break the deal and allow other companies to become involved in the bidding, it would have to pay AT&T \$1.725 billion. On the other hand, if the antitrust agency were not to approve the deal, causing the termination of the buyout, then AT&T would have to pay Time Warner \$500 million.<sup>7</sup>

Frank was trying to anticipate the future of the merged firm, as AT&T equity represented a significant portion of her investment portfolios. She wondered if the merger would be costly or problematic for the acquirer's investors. In 2016, so far, numerous acquisitions had greatly benefited shareholders of the acquired firm at the expense of the acquirer's investors, including the \$3.8 billion acquisition of DreamWorks Animation by Comcast Corporation (Comcast) and the \$2.8 billion acquisition of Demandware Inc. by Salesforce.com Inc.<sup>8</sup> Investors had already started contacting Frank about the future of the company and the state of their investments. She needed to act fast to mitigate any potential loss of value for her investors, so she decided to make a thorough valuation analysis.

## DEAL STRUCTURE

In the merger, all of Time Warner's shareholders would receive \$107.5 per share—\$53.75 per share in cash and \$53.75 per share in AT&T stock. If AT&T's average share price was less than \$37.411 at the close of the transaction, Time Warner's shareholders would receive a fixed price of 1.437 AT&T shares per share. If AT&T's average share price was in the range of \$37.411 and \$41.349, then the exchange ratio would be an amount equal to the quotient obtained by dividing \$53.75 by the average AT&T stock price. If AT&T's share price was higher than \$41.349 per share, Time Warner's shareholders would receive AT&T shares at a fixed price of 1.300 per share.<sup>9</sup>

To raise the cash needed to fund half of the \$85.4 billion deal, AT&T planned to apply for bridge loans of \$25 billion and \$15 billion, respectively, from JPMorgan Chase & Co. and Bank of America Merrill Lynch.<sup>10</sup>

## THE ACQUIRER: AT&T

Headquartered in Dallas, Texas, AT&T had previously been known as the American Bell Telephone Company and included the Bell Telephone Company founded by telephone inventor Alexander Graham Bell in 1880. In 1984, AT&T spun off its local telephone service and kept equipment manufacturing enterprises Western Electric and Bell Laboratories, as well as the most profitable long-distance services; Southwestern Bell Communications (SBC) had its origins in this reorganization.<sup>11</sup> The United States

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<sup>6</sup> Time Warner Inc., op. cit.

<sup>7</sup> Todd Spangler, "Time Warner Would Pay AT&T \$1.73 Billion Breakup Fee if Merger Is Pulled," *Variety*, October 24, 2016, accessed March 27, 2019, <https://variety.com/2016/biz/news/time-warner-att-breakup-fee-merger-1201898492>.

<sup>8</sup> David Trainer, "AT&T Time Warner Acquisition a Rare Deal that Makes Economic Sense," *Forbes*, November, 15, 2016, accessed June 25, 2019, [www.forbes.com/sites/greatspeculations/2016/11/15/att-time-warner-acquisition-a-rare-deal-that-makes-economic-sense/#7e7270cb11fa](http://www.forbes.com/sites/greatspeculations/2016/11/15/att-time-warner-acquisition-a-rare-deal-that-makes-economic-sense/#7e7270cb11fa).

<sup>9</sup> Time Warner Inc., "Form 8-k, Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934," US Securities and Exchange Commission, October 22, 2016, accessed June 25, 2019, [www.sec.gov/Archives/edgar/data/1105705/000095015716002366/form8k.htm](http://www.sec.gov/Archives/edgar/data/1105705/000095015716002366/form8k.htm).

<sup>10</sup> Thomas Gryta, Keach Hagey, Dana Cimilluca, and Dana Mattioli, "AT&T: Reaches Deal to Buy Time Warner for More than \$80 Billion—3rd Update," *Marketscreener*, October 22, 2016, accessed June 26, 2019, [www.marketscreener.com/AT-T-INC-14324/news/AT-T-Reaches-Deal-to-Buy-Time-Warner-for-More-Than-80-Billion-3rd-Update-23257264/](http://www.marketscreener.com/AT-T-INC-14324/news/AT-T-Reaches-Deal-to-Buy-Time-Warner-for-More-Than-80-Billion-3rd-Update-23257264/).

<sup>11</sup> AT&T, "Brand-Licensing, Evolution and Domain Names," accessed June 25, 2019, <https://about.att.com/innovation/ip/brands/history>

telecommunications law of 1996 led to a major change in the competitive landscape.<sup>12</sup> SBC expanded its operations in the United States through a series of acquisitions, including the acquisition of Pacific Telesis Group in 1997 and the acquisition of Ameritech Corporation in 1999. In 2005, SBC purchased AT&T and took on its branding, with the merged entity naming itself AT&T Inc. and using its iconic logo and stock-trading symbol.<sup>13</sup>

AT&T was the largest telecom company and fixed-line telephone service provider in the United States, as well as the largest mobile phone service provider in the United States and the second-largest mobile service provider in the world. The company's businesses included wireless communications; local exchange services; remote services; data, broadband, and Internet services; video services; telecommunications equipment; network management; wholesale services; and catalogue advertising and publishing services. AT&T also provided broadband and satellite television (TV) services, and had about 135 million wireless subscribers in the United States in 2016, which made it the world's largest telecom company.<sup>14</sup>

AT&T operated in four main business sectors (see Exhibit 1). In enterprise solutions, its main businesses were wireless services, strategic services, traditional voice and data services, and wireless devices. In consumer mobile services, it provided consumer service and equipment. In entertainment and Internet services, it offered video entertainment, high-speed Internet, and traditional data services. Finally, its international business segment provided video and wireless services in Latin American countries such as Brazil and Argentina.

AT&T was committed to expanding its mobile Internet business through a series of mergers and acquisitions. It had purchased the number-three Mexican carrier Iusacell for \$2.5 billion in late 2014, and two months later, it purchased the Mexican telecom operator Nextel Mexico for \$1.88 billion.<sup>15</sup> The two acquired companies formed AT&T Mexico and helped AT&T enter the Latin American market. With the development of mobile Internet and social media, as well as changes in consumers' video-watching habits, AT&T had also started to enter the video field. In 2014, AT&T and the Chernin Group jointly purchased Fullscreen, YouTube's premier content provider.<sup>16</sup> In 2015, AT&T acquired DIRECTV, the largest US satellite TV provider, for \$48.5 billion and became the nation's largest pay-TV company, generating significant revenue growth for its entertainment business.<sup>17</sup>

## THE TARGET: TIME WARNER

Founded in 1990, Time Warner was headquartered in New York. Originally a magazine publisher, it had grown to become one of the world's top entertainment media companies after a number of mergers and acquisitions. The Warner brothers—Harry, Albert, Sam, and Jack Warner—started the first Warner Brothers Studio in 1918 on Sunset Boulevard in Hollywood. In 1923, they formally established Warner Bros.

<sup>12</sup> Staff member of National Telecommunications and Information Administration (NTIA), "The United States Telecommunications Act of 1996, Global Communications Interactive '98," accessed July 11, 2019, [www.ntia.doc.gov/legacy/opadhome/overview.htm](http://www.ntia.doc.gov/legacy/opadhome/overview.htm).

<sup>13</sup> "SBC Completes Purchase of AT&T", NBC News, accessed August 22, 2019, [www.nbcnews.com/id/10100350/ns/business-us\\_business/t/sbc-completes-purchase-att/#.XV7ulehKg0l](http://www.nbcnews.com/id/10100350/ns/business-us_business/t/sbc-completes-purchase-att/#.XV7ulehKg0l).

<sup>14</sup> AT&T Inc., *AT&T Inc. Financial Review 2016*, accessed July 11, 2019, [www.att.com/Investor/ATT\\_Annual/2016/downloads/att\\_ar2016\\_mda\\_consolidatedtables.pdf](http://www.att.com/Investor/ATT_Annual/2016/downloads/att_ar2016_mda_consolidatedtables.pdf).

<sup>15</sup> "NII Holdings agrees to sell operations in Mexico to AT&T for \$1.88 billion" *Washington Post*, accessed August 22, 2019, [www.washingtonpost.com/business/capitalbusiness/nii-holdings-agrees-to-sell-operations-in-mexico-to-atandt-for-188-b/2015/01/26/eb68ab00-a574-11e4-a7c2-03d37af98440\\_story.html?noredirect=on](http://www.washingtonpost.com/business/capitalbusiness/nii-holdings-agrees-to-sell-operations-in-mexico-to-atandt-for-188-b/2015/01/26/eb68ab00-a574-11e4-a7c2-03d37af98440_story.html?noredirect=on).

<sup>16</sup> "AT&T-Chernin J.V. Otter Media Buys Out Remaining Fullscreen, Crunchyroll Owners," *Variety*, accessed July 11, 2019, <https://variety.com/2018/digital/news/att-chermin-j-v-otter-media-buys-out-remaining-fullscreen-crunchyroll-owners-1202675621/>.

<sup>17</sup> "AT&T to Buy DirecTV for \$48.5 Billion in Move to Expand Clout," *New York Times*, accessed July 11, 2019, <https://dealbook.nytimes.com/2014/05/18/att-to-buy-directv-for-48-5-billion/>.

Entertainment Inc. (Warner Bros.) In the same year, Henry Luce and his Yale schoolmate Briton Hadden founded Time Inc. to publish the first weekly news magazine in the United States, *Time* magazine. Since the 1950s, Time Inc. had expanded into other fields, investing in the broadcast TV and cable TV networks Home Box Office (HBO) and Cinemax. In 1990, Time Inc. acquired Warner Communications Inc. for \$14 billion to eventually form Time Warner.<sup>18</sup> Time Warner had a history of expanding and adapting through mergers and acquisition. In 1996, Time Warner merged with Turner Broadcasting System Inc., the largest cable television company at that time, and become a leading player in the television distribution industry.<sup>19</sup>

At the time, Time Warner was the world's third-largest entertainment company, after The Walt Disney Company and Comcast. Time Warner operated the following companies (see Exhibit 2 for their shares): (1) HBO, an American premium cable and satellite television network with subscription services and content authorization as its main sources of revenue; (2) Turner Broadcasting System, a media network that generated revenue through subscription, advertising, and content authorization services and included brands such as CNN, HLN, TNT, TBS, Cartoon Network, Turner Classic Movies, truTV, and Turner Sports; and (3) Warner Bros., which received revenue mainly from copyrights for the production and distribution of movies, television, video games, sales of peripheral products, and home entertainment on demand.

Amid the dot-com bubble of 2000, and in search of opportunities for Internet development, Time Warner merged with AOL (formerly, America Online), the world's largest Internet service provider. However, the merger ended with a huge loss, and AOL withdrew in 2009. In 2014, Time Warner sold its Time Warner Cable segment to Comcast, then the nation's largest cable television company, for \$45 billion.<sup>20</sup> Time Warner subsequently focused on its film, television production, and cable TV channels. In July of the same year, 21st Century Fox Inc. offered \$80 billion to acquire Time Warner, but Time Warner rejected this bid.<sup>21</sup> In recent years, Time Warner's financial numbers had been relatively stable (see Exhibits 3–5).

## INDUSTRY BACKGROUND

The history of the telecommunications industry in the United States dated back to 1876, when Bell applied for the first telephone patent. After more than 120 years of development, it had become an important pillar of the American national economy. The early telecom industry had experienced periods of patent monopoly, regulatory monopoly, and free competition, one after the other. In 2016, the US telecom industry became a fully competitive market represented by telecommunications companies such as Verizon Communications Inc. (Verizon), AT&T, DIRECTV, Comcast, and Time Warner Cable.

The telecom industry was also expanding into new business lines: from the early telephone and telegraph services, it had grown to include wireless communications, satellite communication services, radio and TV transmission businesses, cellular communications, and data communication services. However, by the 21st century, the markets for cell phone service, home Internet access, and cable TV services had become increasingly saturated in the United States. More people were choosing to watch online video programs

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<sup>18</sup> Steven Mufson, "Time Buys Warner for \$14 Billion," *Washington Post*, July 25, 1989, accessed July 11, 2019, [www.washingtonpost.com/archive/politics/1989/07/25/time-buys-warner-for-14-billion/3db3e59f-4e1d-4000-aa2b-33e12d97d027/?noredirect=on](http://www.washingtonpost.com/archive/politics/1989/07/25/time-buys-warner-for-14-billion/3db3e59f-4e1d-4000-aa2b-33e12d97d027/?noredirect=on); Time Warner Inc., "Company Profile, Information, Business Description, History, Background Information on Time Warner Inc.," accessed July 11, 2019, [www.referenceforbusiness.com/history2/83/Time-Warner-Inc.html](http://www.referenceforbusiness.com/history2/83/Time-Warner-Inc.html); Warner Bros., "Company History," accessed July 11, 2019, [www.warnerbros.com/studio/about-studio/company-history](http://www.warnerbros.com/studio/about-studio/company-history).

<sup>19</sup> Thomas S. Mulligan, "Turner-Time Warner Merger Approved by Shareholder," *Los Angeles Times*, October 11, 1996, accessed July 11, 2019, [www.latimes.com/archives/la-xpm-1996-10-11-fi-52676-story.html](http://www.latimes.com/archives/la-xpm-1996-10-11-fi-52676-story.html).

<sup>20</sup> Sam Gustin, "Comcast Set to Buy Time Warner Cable for \$45 Billion," *Time*, February 12, 2014, accessed July 11, 2019, <http://business.time.com/2014/02/12/comcast-time-warner-cable/>.

<sup>21</sup> Andrew Ross Sorkin, "Time Warner Rejected \$80 Billion Offer from 21st Century Fox: Sources," *CNBC*, July 16, 2014, accessed July 11, 2019, [www.cnbc.com/2014/07/16/time-warner-rejected-80b-offer-from-21st-century-fox-sources.html](http://www.cnbc.com/2014/07/16/time-warner-rejected-80b-offer-from-21st-century-fox-sources.html).

and, consequently, subscriptions to cable TV services were decreasing. Given this scenario, traditional telecom operators were reluctant to act as conduits to allow customers to access the Internet; they hoped to gain more advertising income and subscription revenue through digital content. Therefore, mergers and acquisitions of media companies that included both content and delivery had become a new trend in the industry (see Exhibit 6).<sup>22</sup>

For example, AT&T's main competitor, Verizon, was at the time heavily engaged in the acquisition of Internet companies. In 2015, Verizon spent \$4.4 billion to acquire AOL. In February 2017, Verizon signed an agreement with Yahoo! Inc. that saw it acquire Yahoo!'s core portal and search engine businesses for \$4.8 billion. Verizon executives had made it clear that, as the telecom market became increasingly saturated and fiercely competitive, Verizon expected more revenue from Internet content and online advertising.<sup>23</sup>

Similarly, the US media industry had undergone major changes in recent years. Its focus had expanded from traditional media such as newspapers, TV and radio broadcasting, book and magazine publishing, and film to include new media such as Internet- and mobile-based social media and online video. In the context of the rapid development of the Internet, the survival of traditional media outlets was increasingly called into question, and the development of new media seemed irresistible. In terms of advertising revenue, new, online media in the US advertising market continued to gain market share in 2016, while that of traditional media such as TV and newspapers was rapidly shrinking (see Exhibit 7).<sup>24</sup>

## CONTROVERSIES ABOUT THE MERGER

As the largest mergers and acquisitions case in 2016, the AT&T–Time Warner deal attracted attention as soon as it was announced. To alleviate the concerns of the public and some investors, AT&T's CEO, Randall Stephenson, and Time Warner's Bewkes held a press conference to provide more information and further justify the decision.<sup>25</sup>

According to Bloomberg, AT&T already had a large number of home TV subscribers and many mobile and broadband subscribers through fixed telecommunications networks and DIRECTV. Through this merger with the top content provider, AT&T hoped to bring more high-quality video content to these subscribers.<sup>26</sup>

However, at an estimated price of \$85.4 billion, the deal was seen by many in the industry as too expensive and prompted comparisons with the failed transaction between Time Warner and AOL, which had been priced at up to \$160 billion. A *Fortune* magazine article mocked the deal directly: "The first rule of mergers is don't do a deal with Time Warner. The second rule, as they say, is that there is only one rule."<sup>27</sup> While Bloomberg's intelligence was more objective, its report said that the deal value was about 13 times Time

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<sup>22</sup> Jurgen Meffert and Niko Mohr, "Overwhelming OTT: Telcos' Growth Strategy in a Digital World," McKinsey & Company, January 2017, accessed November 26, 2019, [www.mckinsey.com/industries/technology-media-and-telecommunications/our-insights/overwhelming-ott-telcos-growth-strategy-in-a-digital-world](http://www.mckinsey.com/industries/technology-media-and-telecommunications/our-insights/overwhelming-ott-telcos-growth-strategy-in-a-digital-world)

<sup>23</sup> Lara O'Reilly, "Verizon Will Acquire Yahoo for \$4.8 Billion," *Business Insider*, accessed July 11, 2019, [www.businessinsider.sg/verizon-acquires-yahoo-2016-7/?r=US&IR=T](http://www.businessinsider.sg/verizon-acquires-yahoo-2016-7/?r=US&IR=T).

<sup>24</sup> "US Online and Traditional Media Advertising Outlook, 2016–2020," Marketing Charts, accessed July 11, 2019, [www.marketingcharts.com/featured-68214](http://www.marketingcharts.com/featured-68214).

<sup>25</sup> Time Warner Inc., "Pursuant to Rule 425 under the Securities Act of 1933 and Deemed Filed Pursuant to Rule 14a-12 under the Securities Exchange Act of 1934," US Securities and Exchange Commission, accessed July 11, 2019, [www.sec.gov/Archives/edgar/data/1105705/000095015716002368/form\\_425.htm](http://www.sec.gov/Archives/edgar/data/1105705/000095015716002368/form_425.htm).

<sup>26</sup> Ed Hammond, Alex Sherman, and Scott Moritz, "AT&T Discussed Idea of Takeover in Time Warner Meetings," Bloomberg, October 20, 2016, accessed April 5, 2019, [www.bloomberg.com/news/articles/2016-10-20/at-t-said-to-discuss-idea-of-takeover-in-time-warner-meetings](http://www.bloomberg.com/news/articles/2016-10-20/at-t-said-to-discuss-idea-of-takeover-in-time-warner-meetings).

<sup>27</sup> Stephen Gandel, "AT&T's Time Warner Deal Comes at a Huge Cost," *Fortune*, October 24, 2016, accessed April 6, 2019, <http://fortune.com/2016/10/24/att-time-warner-deal-share-price>.

Warner's earnings before interest, taxes, depreciation, and amortization (EBITDA), setting a new record in the media industry.<sup>28</sup>

*Forbes* magazine experts said they rarely "liked" acquisitions, in terms of the value they created for acquirers, and were often left "disappointed by how much the acquiring company overpays."<sup>29</sup> AT&T would pay \$108.7 billion to acquire \$5.1 billion of Time Warner's net operating profit after tax. According to the *Forbes* article, the return on invested capital (ROIC) would be 4.7 per cent, marginally improving AT&T's current ROIC of 4.6 per cent and equal to its weighted average cost of capital of 4.7 per cent. This deal would modestly improve AT&T's overall ROIC.<sup>30</sup>

Frank had to evaluate these differing opinions, and she needed to conduct a valuation analysis independently. She first collected data on previous comparable mergers (see Exhibit 6) and on comparable major competitors of Time Warner (see Exhibit 7). She found Time Warner's EBITDA for the trailing 12 months, which was \$8,790 million, and its earnings-per-share ratio as of September 30, 2016, which was 4.62. She also obtained all the firm fundamental information she could find about Time Warner (see Exhibit 8). Frank believed that the synergies from the merger would potentially help Time Warner maintain 8 per cent growth in free cash flow for the following five years, based on the company's historic average growth rate. However, she also thought that a more modest 7 per cent growth rate for the next five years would be more realistic. For the terminal growth rate after the fifth year, Frank decided she would follow the common practice of the majority of the financial analysts who covered the media industry and use 3 per cent.

Frank would call the AT&T and Time Warner CEOs without hesitation if she had any questions. But with all the information she had collected so far, she believed that she was ready to work on the valuation of Time Warner. Then, she would need to defend her valuation analysis in front of her investors.

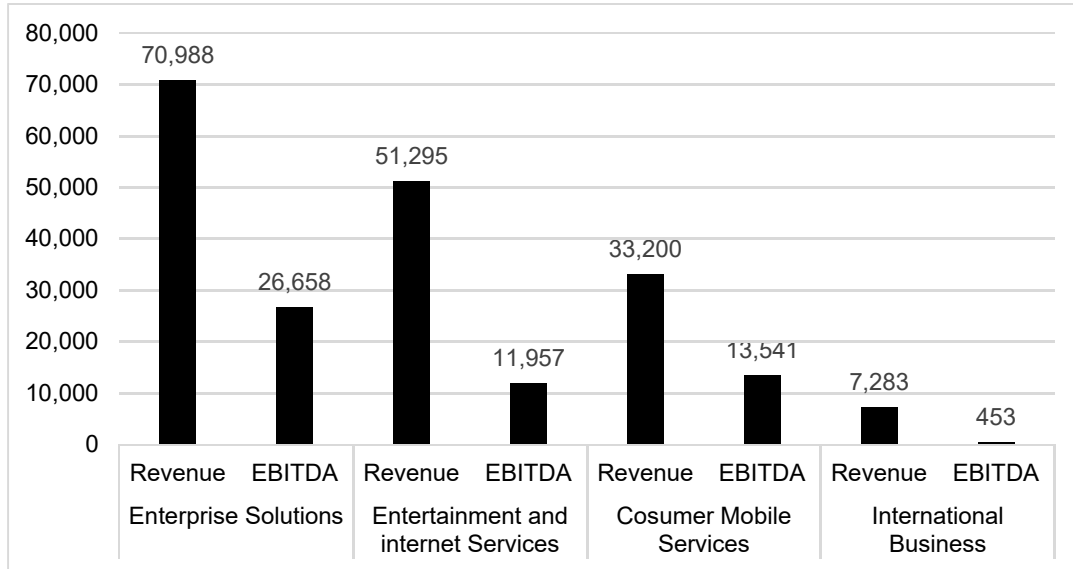
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<sup>28</sup> Tara Lachapelle, "AT&T–Time Warner: Rethink Possible. Buying Time Warner Is Risky, But It also May Be Necessary," Bloomberg, October 23, 2016, accessed April 6, 2019, [www.bloomberg.com/opinion/articles/2016-10-24/at-t-time-warner-deal-is-risky-but-may-be-necessary](http://www.bloomberg.com/opinion/articles/2016-10-24/at-t-time-warner-deal-is-risky-but-may-be-necessary).

<sup>29</sup> David Trainer, "AT&T Time Warner Acquisition a Rare Deal that Makes Economic Sense," *Forbes*, November 15, 2016, accessed April 6, 2019, [www.forbes.com/sites/greatspeculations/2016/11/15/att-time-warner-acquisition-a-rare-deal-that-makes-economic-sense/#7122464911fa](http://www.forbes.com/sites/greatspeculations/2016/11/15/att-time-warner-acquisition-a-rare-deal-that-makes-economic-sense/#7122464911fa).

<sup>30</sup> *Ibid.*

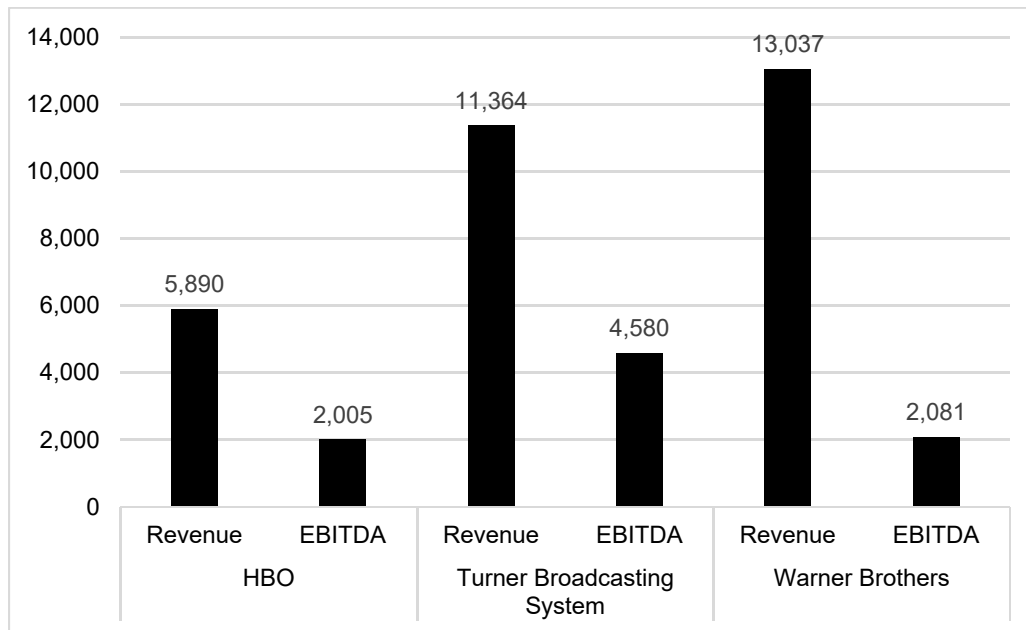
**EXHIBIT 1: DEPARTMENTAL OPERATIONS OF AT&T IN 2016 (IN US\$ MILLIONS)**



Note: EBITDA = earnings before interest, taxes, depreciation, and amortization

Source: Created by the case authors using data from AT&T Inc., "Form 10-Q, Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934," US Securities and Exchange Commission, November 3, 2016, accessed July 12, 2019, [www.sec.gov/Archives/edgar/data/732717/000073271716000233/q3\\_10q.htm](http://www.sec.gov/Archives/edgar/data/732717/000073271716000233/q3_10q.htm).

**EXHIBIT 2: DEPARTMENTAL OPERATIONS OF TIME WARNER IN 2016 (IN US\$ MILLIONS)**



Note: EBITDA = earnings before interest, taxes, depreciation, and amortization

Source: Created by the case authors using data from Time Warner Inc., "Form 10-Q, Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934," US Securities and Exchange Commission, November 2, 2016, accessed July 12, 2019, [www.sec.gov/Archives/edgar/data/1105705/000119312516756548/0001193125-16-756548-index.htm](http://www.sec.gov/Archives/edgar/data/1105705/000119312516756548/0001193125-16-756548-index.htm).

## EXHIBIT 3: TIME WARNER INC., CONSOLIDATED BALANCE SHEET

In US\$ millions, except per-share amounts	2016	2015	2014
<b>ASSETS</b>			
<b>Current Assets</b>			
Cash and Equivalents	1,539	2,155	2,618
Receivables, Less Allowances of \$981 and \$1,055	8,699	7,411	7,720
Inventories	2,062	1,753	1,700
Deferred Income Taxes	/	/	184
Prepaid Expenses and Other Current Assets	1,185	1,194	958
<b>Total Current Assets</b>	<b>13,485</b>	<b>12,513</b>	<b>13,180</b>
Non-Current Inventories and Theatrical Film and Television Production Costs	7,916	7,600	6,841
Investments, Including Available-for-Sale Securities	3,337	2,617	2,326
Property, Plant and Equipment, Net	2,510	2,596	2,655
Intangible Assets Subject to Amortization, Net	783	949	1,141
Intangible Assets Not Subject to Amortization	7,005	7,029	7,032
Goodwill	27,752	27,689	27,565
Other Assets	3,178	2,855	2,406
<b>Total Assets</b>	<b>\$65,966</b>	<b>\$63,848</b>	<b>\$63,146</b>
<b>LIABILITIES AND EQUITY</b>			
<b>Current Liabilities</b>			
Accounts Payable and Accrued Liabilities	\$7,192	\$7,188	\$7,507
Deferred Revenue	564	616	579
Debt Due Within One Year	1,947	198	1,118
<b>Total Current Liabilities</b>	<b>9,703</b>	<b>8,002</b>	<b>9,204</b>
Long-Term Debt	22,392	23,594	21,263
Deferred Income Taxes	2,678	2,454	2,204
Deferred Revenue	486	352	315
Other Non-Current Liabilities	6,341	5,798	5,684
Redeemable Non-Controlling Interest	29	29	/
<b>Equity</b>			
Additional Paid-In Capital	146,780	148,041	149,282
Treasury Stock, at Cost (880 Million and 857 Million Shares)	(47,497)	(45,612)	(42,445)
Accumulated Other Comprehensive Loss, Net	(1,510)	(1,446)	(1,164)
Accumulated Deficit	(73,455)	(77,381)	(81,214)
Total Time Warner Inc. Shareholders' Equity	24,335	23,619	/
Non-Controlling Interests	2	/	/
<b>Total Equity</b>	<b>24,337</b>	<b>23,619</b>	<b>24,476</b>
<b>Total Liabilities and Equity</b>	<b>\$65,966</b>	<b>\$63,848</b>	<b>\$63,146</b>

Source: Excerpted from Time Warner Inc., *2016 Annual Report*, 60, *2017 and 2015 Annual Report*, 71, US Securities and Exchange Commission, 2016, accessed February 8, 2019, [http://annualreports.com/HostedData/AnnualReportArchive/t/NYS E\\_TWX\\_2016.pdf](http://annualreports.com/HostedData/AnnualReportArchive/t/NYS E_TWX_2016.pdf). and [www.sec.gov/Archives/edgar/data/1105705/000119312516477965/d280491d10k.htm#tx280491\\_3](http://www.sec.gov/Archives/edgar/data/1105705/000119312516477965/d280491d10k.htm#tx280491_3).



**EXHIBIT 4: TIME WARNER INC., CONSOLIDATED STATEMENT OF OPERATIONS**

In US\$ millions, except per-share amounts	2016	2015	2014
Revenues	29,318	28,118	27,359
Costs of Revenues	(16,376)	(16,154)	(15,875)
Selling, General, and Administrative	(5,123)	(4,824)	(5,190)
Amortization of Intangible Assets	(190)	(189)	(202)
Restructuring and Severance Costs	(117)	(60)	(512)
Asset Impairments	(43)	(25)	(69)
Gain (Loss) on Operating Assets, Net	78	(1)	464
Operating Income	7,547	6,865	5,975
Interest Expense, Net	(1,161)	(1,163)	(1,169)
Other Loss, Net	(1,191)	(256)	(127)
Income from Continuing Operations before Income Taxes	5,195	5,446	4,679
Income Tax Provision	(1,281)	(1,651)	(785)
Income from Continuing Operations	3,914	3,795	3,894
Discontinued Operations, Net of Tax	11	37	(67)
Net Income	3,925	3,832	3,827
Less Net Loss Attributable to Non-Controlling Interests	1	1	—
Net Income Attributable to Time Warner Inc. Shareholders	\$3,926	\$3,833	\$3,827
Average Basic Common Shares Outstanding	780.8	814.9	863.3
Average Diluted Common Shares Outstanding	792.3	829.5	882.6
Cash Dividends Declared per Share of Common Stock	\$1.61	\$1.40	\$1.27

Source: Excerpted from Time Warner Inc., *2016 Annual Report*, 61–62, 2017, accessed February 8, 2019, [http://annualreports.com/HostedData/AnnualReportArchive/t/NYSE\\_TW\\_X\\_2016.pdf](http://annualreports.com/HostedData/AnnualReportArchive/t/NYSE_TW_X_2016.pdf).

**EXHIBIT 5: TIME WARNER INC., CONSOLIDATED STATEMENT OF CASH FLOWS**

(In US\$ millions)	2016	2015	2014
<b>OPERATIONS</b>			
Net Income	\$3,92	\$3,83	\$3,82
Less Discontinued Operations, Net of Tax	(11)	(37)	67
Net Income from Continuing Operations	3,914	3,795	3,894
Adjustments for Non-Cash and Non-Operating Items:			
Depreciation and Amortization	669	681	733
Amortization of Film and Television Costs	8,324	8,030	8,040
Asset Impairments	43	25	69
Venezuelan Foreign Currency Loss	—	—	173
(Gain) Loss on Investments and Other Assets, Net	(131)	31	(493)
Equity in Losses of Investee Companies, Net of Cash Distributions	324	161	232
Equity-Based Compensation	277	182	219
Deferred Income Taxes	236	328	166
Premiums Paid and Costs Incurred on Debt Redemption	1,008	72	—
Changes in Operating Assets and Liabilities, Net of Acquisitions:			
Receivables	(1,20)	(112)	(403)
Inventories and Film Costs	(8,77)	(8,52)	(7,78)
Accounts Payable and Other Liabilities	631	(200)	592
Other Changes	(637)	(616)	(1,75)
Cash Provided by Operations from Continuing Operations	4,683	3,851	3,681
<b>INVESTING ACTIVITIES</b>			
Investments in Available-for-Sale Securities	(9)	(41)	(30)
Investments and Acquisitions, Net of Cash Acquired	(1,22)	(672)	(950)
Capital Expenditures	(432)	(423)	(474)
Proceeds from Time Inc. in the Time Separation	—	—	1,400
Proceeds from the Sale of Time Warner Center	—	—	1,264
Other Investment Proceeds	309	143	173
Cash Provided (Used) by Investing from Continuing Operations	(1,36)	(993)	1,383
<b>FINANCING ACTIVITIES</b>			
Borrowings	3,830	3,768	2,409
Debt Repayments	(3,30)	(2,34)	(72)
Proceeds from Exercise of Stock Options	172	165	338
Excess Tax Benefit from Equity Instruments	88	151	179
Principal Payments on Capital Leases	(14)	(11)	(11)
Repurchases of Common Stock	(2,32)	(3,63)	(5,50)
Dividends Paid	(1,26)	(1,15)	(1,10)
Other Financing Activities	(1,10)	(260)	(173)
Cash Used by Financing Activities from Continuing Operations	(3,92)	(3,31)	(3,94)
Cash Provided (Used) by Continuing Operations	(599)	(455)	1,121
Cash Used by Discontinued Operations	(17)	(8)	(190)
Effect of Venezuelan Exchange Rate Changes on Cash	—	—	(129)
<b>INCREASE (DECREASE) IN CASH AND EQUIVALENTS</b>	<b>(616)</b>	<b>(463)</b>	<b>802</b>
<b>CASH AND EQUIVALENTS AT BEGINNING OF PERIOD</b>	<b>2,155</b>	<b>2,618</b>	<b>1,816</b>
<b>CASH AND EQUIVALENTS AT END OF PERIOD</b>	<b>\$1,53</b>	<b>\$2,15</b>	<b>\$2,61</b>

Source: Excerpted from Time Warner Inc., *2016 Annual Report*, 63, 2017, accessed February 8, 2019, [http://annualreports.com/HostedData/AnnualReportArchive/t/NYSE\\_TW\\_X\\_2016.pdf](http://annualreports.com/HostedData/AnnualReportArchive/t/NYSE_TW_X_2016.pdf).

**EXHIBIT 6: COMPARABLE MERGERS AND ACQUISITIONS TRANSACTIONS (IN US\$)**

Date	Acquirer Company	Target Company	Deal Value	EBITDA Multiple
June 2016	Lions Gate Entertainment Corp.	Starz Inc.	\$4.40 billion	10.9×
April 2016	Comcast Corporation	DreamWorks Animation SKG Inc.	\$3.80 billion	32.3×
November 2012	News Corporation	Yankee Entertainment and Sports Network	\$3.90 billion	12.2×
August 2009	The Walt Disney Company	Marvel Entertainment Group Inc.	\$4.24 billion	12.7×

Note: Note: EBITDA = earnings before interest, taxes, depreciation, and amortization  
Source: Created by the case authors using data from Bloomberg.

**EXHIBIT 7: MULTIPLES OF MAJOR COMPETITORS IN THE MEDIA INDUSTRY**

	P/E Ratio	EV/EBITDA
<b>Entertainment Division (Warner Brothers)</b>		
The Walt Disney Company	16.23	9.51
21st Century Fox Inc.	15.93	9.01
CBS Corporation	15.29	10.97
<b>Channels and Network division (Turner and HBO)</b>		
AMC Networks Inc.	12.54	5.93
Discovery Communications Inc.	13.64	8.75
Scripps Networks Interactive Inc.	10.57	4.74

Note: P/E = price-to-earnings; EV/EBITDA = enterprise value-to-earnings before interest, taxes, depreciation, and amortization  
Source: Created by the case authors using data from D&B Hoovers database.

**EXHIBIT 8: DISCOUNTED CASH FLOW MODEL INPUTS FOR TIME WARNER**

<b>WACC Inputs</b>		<b>Description</b>
Weight of Debt	21.00%	= 23.3 ÷ (23.3 + 85.4)
Weight of Equity	79.00%	= 100% – Weight of Debt
Cost of Debt	3.50%	Most Recent Bank Loan Interest Rate
Risk-Free Rate	2.31%	Long-Term Governance Bond Yield
Beta	1.9	From Bloomberg
Market Risk Premium	5.00%	Common Practice for North America
Tax Rate	35.00%	Marginal Tax Rate
<b>Free Cash Flow (2016) Inputs (in US\$ millions)</b>		
EBIT		6,583
Depreciation and Amortization		669
Capital Expenditure		432
Working Capital 2016		3,782
Working Capital 2015		4,511

Notes: WACC = weighted average cost of capital; EBIT = earnings before interest and taxes.  
Source: Created by the case authors.