ACTIVISION BLIZZARD

Proposed $20.3bn take-private transaction

Investment Banking and Private Equity in Media and Entertainment – FINC GB 3145

By: Siddharth Dayama

Executive summary

PE take-private transaction of Activision Blizzard

- Activision Blizzard “ATVI” (NSDQ) is the #1 software games publisher in the US with widely popular titles such as Call of Duty™ and World of Warcraft™.
- ATVI is c.62% owned by Vivendi SA, a European media conglomerate. Following a management shuffle, Vivendi has since announced plans to realign its strategic focus by divesting non-core assets.
- In June 2012, Vivendi announced that it was exploring the sale of its stake in ATVI to strategic buyers.
- ATVI is an attractive target for a PE consortium given the company’s industry-leading position, strong title portfolio, attractive valuation, relatively stable cash flows and strong management track record. ATVI currently has no debt.
- A leveraged buy-out of ATVI yields an IRR of 22.6% and a 2.8x multiple on money, assuming a 25% purchase premium, post-transaction debt/EBITDA13E leverage of 5.1x and entry / exit multiples of 10.1x EV/EBITDA13E.
- Given its large size (projected 2018E EV of c.$23.8bn), an IPO re-listing is an ideal exit strategy for the PE consortium.

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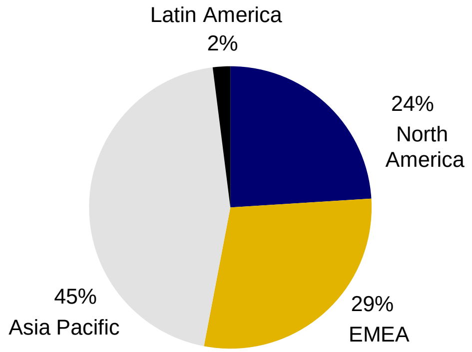
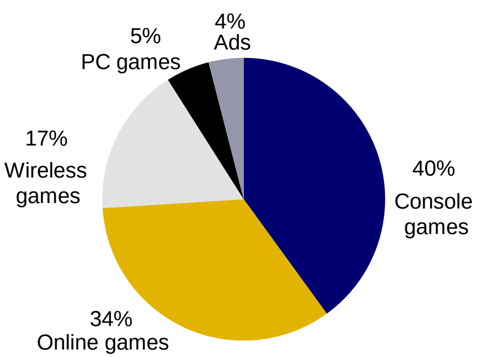
Video games industry overview

Market segmentation

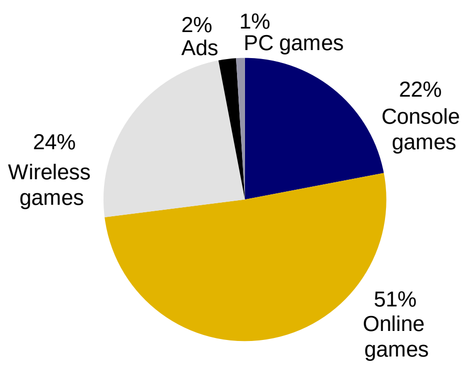
Geographic breakdown - 2013



Global market by component - 2013



Asia Pacific market by component - 2013



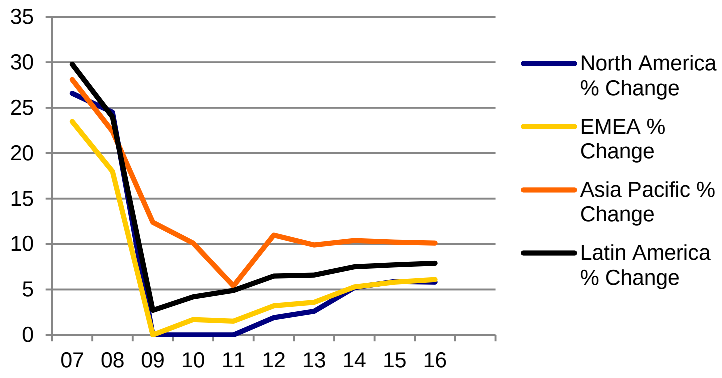
Source: IBIS World

Industry characteristics

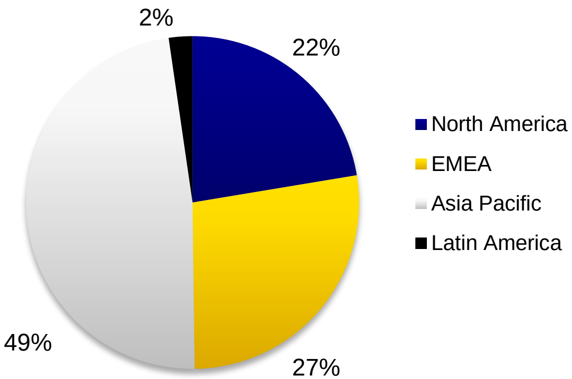
- Highly competitive
- Factors contributing to volatility in market share:
  - Timing and frequency of published releases
  - Popularity and market acceptance of released titles
- Development and sales: game consoles & peripherals
- Consolidation creates barriers to entry
- Strong content in pipeline key for sustainability

Video games industry overview (cont'd)

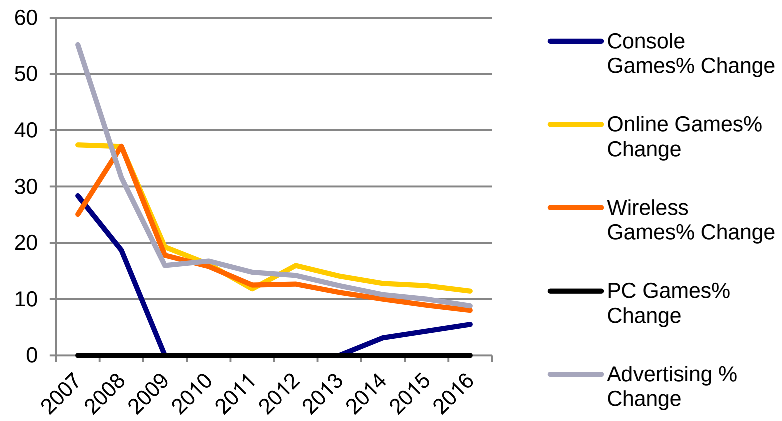
Annual % change in industry growth by region



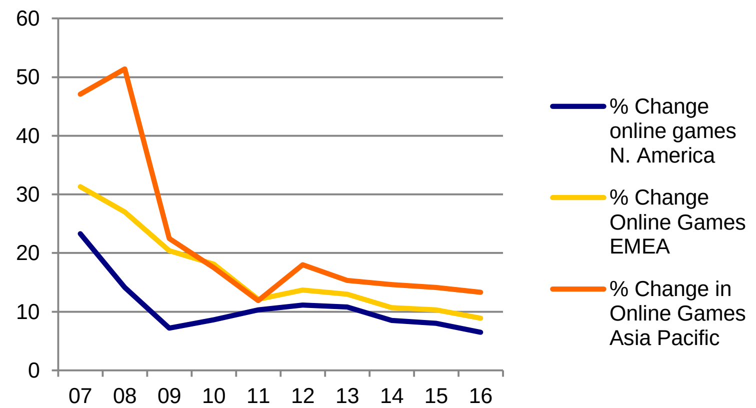
Projected 2016 market breakdown by region



Annual global % growth by industry component



Annual % change in online games growth by region



Source: IBIS World

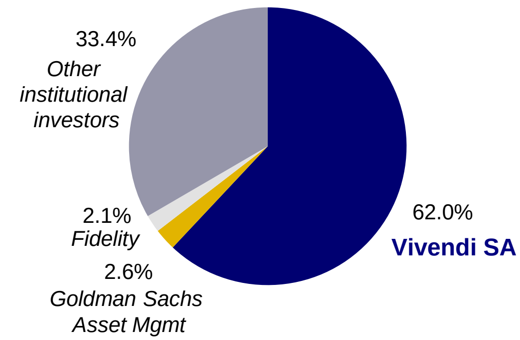
Company overview – Activision Blizzard (“ATVI”)

Company profile

- Headquartered in Santa Monica, CA
- Leading worldwide publisher of online, PC, console, tablet and handheld games by most metrics (revenue and profitability)
- Activision + Blizzard merged in 2008:
  Blizzard – online franchises, Activision – other games
- Top franchises: *Call of Duty*™, *Skylanders* ™,
  World of Warcraft ™
- Bobby Kotick – CEO since 1991 and of Activision Blizzard since 2008 merger
- The company’s games include both internally developed titles and licensed properties

Vivendi SA owns c.62% of ATVI

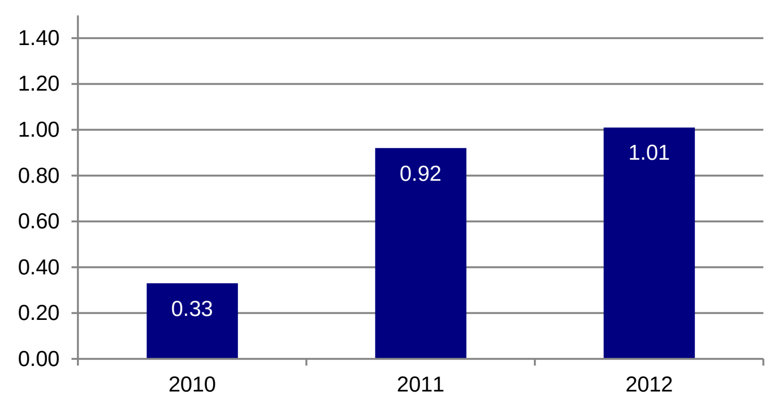
Shareholder composition



Source: ThomsonOne

ATVI experienced record EPS in 2012…

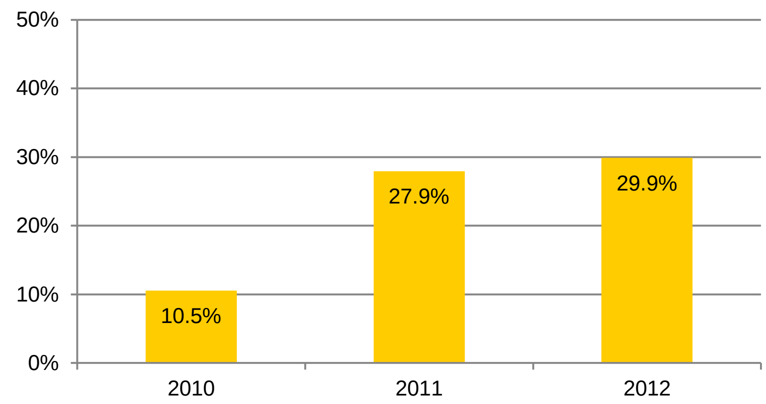
Activision Blizzard’s EPS ($)



Source: Company filings

… along with record operating margins

Activision Blizzard’s operating margins (%)

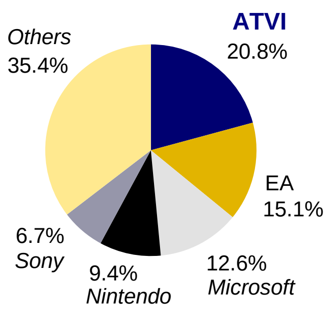


Source: Company filings

Strategic rationale – ATVI investment highlights

#1 software games publisher in the US

Market share and summary financials of industry players

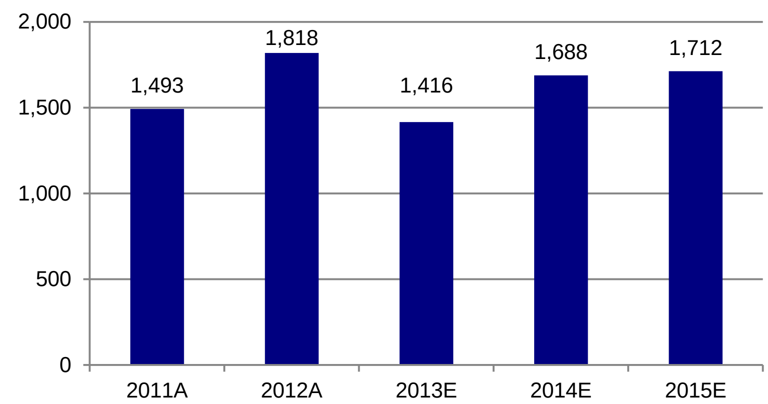


in $bn

	MC	EV
ATVI	**15.9**	**11.9**
IGT	4.3	6.0
EA	5.1	4.3
Nintendo	1.7	2.6
Zynga	2.5	1.4
Take Two Int'	1.3	1.2

Relatively stable cash flows in spite of industry

Activision Blizzard's EBITDA ($mm)



Source: IBIS World, Bank of America, Merrill Lynch, Yahoo Finance

Strong title portfolio & leading player in online/MMO

Major Activision Blizzard titles

Strong presence in online/MMO (high growth sector)

- #1 subscription-based MMO game – World of Warcraft™
- Launching Call of Duty™, as an MMO game in China

Attractive valuation levels

- ATVI is undervalued when compared to its closest comparable, EA

	EV/EBITDA	Trailing PE	Forward P/E
ATVI	**7.6x**	**14.3x**	**13.8x**
EA	11.0x	31.2x	15.9x

Strong management track record

Bobby A. Kotick, CEO

- CEO of ATVI since 2008 (CEO of Activision since 1991)
- ATVI stock rose 16x during his tenure

Eric Hirshberg, CEO Activision Publishing

- CEO of Activision Publishing since 2010
- Launched ATVI's most successful games in history – Call of Duty: Black Ops & Modern Warfare 3

Strategic rationale – incentives for Vivendi to divest its c.62% stake in ATVI

Transaction is an opportunity for Vivendi to divest a non-core asset as part of its recent restructuring efforts

Ongoing restructuring efforts as part of management's attempt to reduce leverage

ATVI represents a non-core asset for Vivendi

Attractive exit opportunity – *proposed transaction represents a 26.7% premium to Vivendi's initial investment in ATVI*

Change in management – *New CFO, Philippe Capron, has indicated desire to focus Vivendi's operations*

Vivendi's ongoing restructuring efforts

Vivendi said to plan sale of Activision Blizzard stake

- Bloomberg, June 2012

Vivendi targets Maroc Telecom stake sale by October

- Businessweek, Apr 2013

Vivendi considers sale of Brazil-based GVT subsidiary

- Reuters, Aug 2012

ATVI – a non-core asset for Vivendi

Classification of Vivendi's existing major assets

Media, core | **Telco, core** | **Non-core**

Strategic rationale – potential IPO re-listing of ATVI as PE exit strategy

Consideration of various private equity exit strategies

	IPO re-listing	Sale to a strategic player	Sale to other PE consortiums
Pros	▪ **Opportunity to gradually exit ATVI despite its large size** ▪ ATVI possesses the size and scale needed to garner investor attention	▪ Further operational synergies available to a strategic, thereby increasing the potential exit multiple ▪ Sale typically includes a control premium ▪ Opportunity for a complete exit	▪ Sale typically includes a control premium ▪ Opportunity for a complete exit ▪ Cash flows for ATVI projected to remain stable beyond 2018 ▪ Leverage projected to be low upon exit *(Net debt / 18E EBITDA of 0.4x)*
Cons	▪ Typically sold at a discount ▪ Extended exit timeframe for PE consortium *(primary offering c.20%)* ▪ Highly dependent on capital markets sentiment	▪ **Small number of potential strategic buyers due to ATVI's large size** ▪ Difficulty in preparing ATVI for sale to each potential strategic	▪ **Small number of potential interested PE consortiums due to ATVI's large size** ▪ Further operational improvements may be limited ▪ Dependent on financing availability

Financial forecasts – income statement

	$mm	FY 2011	FY 2012	FY 2013E	FY 2014F	FY 2015F	FY 2016F
1	**Revenues**						
	Product revenue	3,257	3,620	3,187	3,282	3,381	3,482
	Subscription revenue	1,498	1,236	1,062	1,094	1,127	1,161
	Total revenue	**4,755**	**4,856**	**4,249**	**4,376**	**4,508**	**4,643**
	Growth	*6.9%*	*2.1%*	*(12.5%)*	*3.0%*	*3.0%*	*3.0%*
	Cost of sales	1,772	1,662	1,352	1,393	1,434	1,477
	Gross profit	**2,983**	**3,194**	**2,897**	**2,984**	**3,073**	**3,166**
	Margin	*62.7%*	*65.8%*	*68.2%*	*68.2%*	*68.2%*	*68.2%*
2	**Operating expenses**						
	R&D expenditures	629	604	604	544	527	511
	SG&A	1,001	1,139	1,139	968	939	911
	EBIT	**1,353**	**1,451**	**1,154**	**1,472**	**1,607**	**1,743**
	Margin	*28.5%*	*29.9%*	*27.2%*	*33.6%*	*35.7%*	*37.5%*
	Non-operating expenses	25	-	-	-	-	-
	Interest income	14	6	5	-	-	-
	Investment income	3	7	5	-	-	-
	Profit before taxes	**1,345**	**1,464**	**1,164**	**1,472**	**1,607**	**1,743**
	Margin	*28.3%*	*30.1%*	*27.4%*	*33.6%*	*35.7%*	*37.5%*
	Income tax expense	246	309	291	368	402	436
	Net income	**1,099**	**1,155**	**873**	**1,104**	**1,205**	**1,307**
	Margin	*23.1%*	*23.8%*	*20.5%*	*25.2%*	*26.7%*	*28.2%*
	CAPEX	72	73	77	80	85	89
3	Depreciation & amortization	435	328	400	388	376	365
	EBITDA	**1,788**	**1,779**	**1,554**	**1,860**	**1,983**	**2,108**
	Margin	*37.6%*	*36.6%*	*36.6%*	*42.5%*	*44.0%*	*45.4%*

1

- Initial dip in 2013E revenues due to lack of major title launch
- 2014-2016F revenues projected to increase 3% YoY

2

- Initial cut in 2014F R&D due to cost-savings by reducing R&D resources on non-core franchises
- Initial cut in 2014F SG&A due to streamlining of headcount and operational efficiencies
- R&D and SG&A expenses projected to decrease 3% YoY, assuming disciplined cost management by the PE consortium

3

- Initial dip in 2013E EBITDA due to lack of major title launch
- 2014-2016F EBITDA projected to increase YoY along with margin improvements, boosting ATVI's ability to pay-down debt

Steady cash-flow business with healthy gross and EBITDA margins

Preliminary valuation – LBO analysis

Transaction considerations

- Pay down debt –
  $4.5bn of bank loan over 5 years
- 3% annual revenue growth translates into c. 50% Enterprise Value growth over 5 years
- Assumed exit multiple equal to entry multiple of 10.1x EV/EBITDA
- Potential for realizing higher exit multiple through margin growth and primary comparable Electronics Arts (“EA”) trades at 11.0x

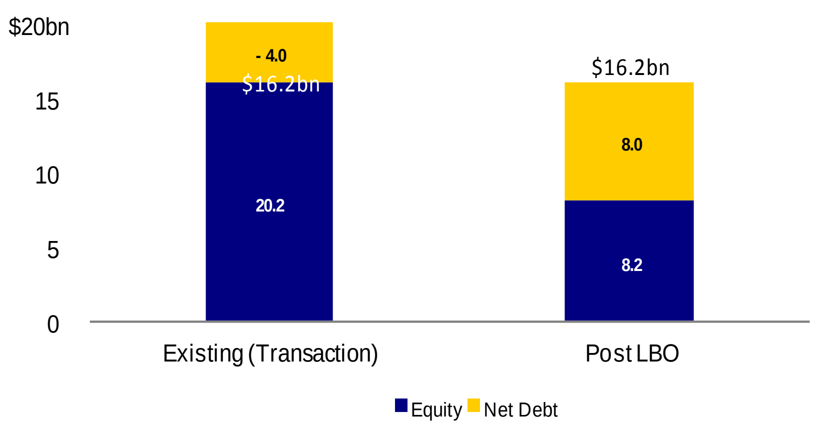
Key transaction details

- 25% premium over market price
- 10.1x EV/EBITDA multiple
- $15.6bn Enterprise value
- $4bn excess cash
- Bank Loan (LIBOR + 650bps) : 7.25%
- High Yield Loan (LIBOR + 900bps) : 9.75%

Transaction assumptions

Current share price ($)	14.40
Purchase premium	25.0%
Offer price ($)	18.00
NOSH (mm)	1,112
Equity value ($mm)	20,016
Existing debt ($mm)	-
Existing cash ($mm)	4,375
Enterprise value ($mm)	**15,641**
Entry multiple - EV/EBITDA 13E	10.1x
Debt/EBITDA 13E	0.0x
Exit multiple - EV/EBITDA 18E	**10.1x**

Capital structure comparison



Source: Yahoo finance
Note: As of April 19th, 2013

Preliminary valuation – LBO analysis

SOURCES & USES OF FUNDS

in $mm Sources:		%	Uses:		%
Excess cash	**4,000**	***19.7%***	**Equity purchase price**	**20,016**	***98.8%***
Debt			**Trans. fees & expenses**	**239**	***1.2%***
Bank loan	4,500	*22.2%*			
High yield bonds	3,500	*17.3%*			
Total Debt	**8,000**	***39.5%***			
New Equity	**8,255**	***40.8%***			
Total Sources	**$20,255**		**Total Uses**	**$20,255**	

PRO FORMA CAPITALIZATION

		Term	Pro forma	% of cap.	2013E EBITDA
Debt					
Bank loan at	7.25%	5 yrs	4,500	27.7%	2.9x
High yield bonds at	9.75%	7 yrs	3,500	21.5%	2.3x
Total debt			**8,000**	**49.2%**	**5.1x**
Equity contribution			**8,255**	**50.8%**	
			16,255		10.5x
2013 EBITDA					**1,554**

Transaction utilizes $4bn existing cash, $8.2bn new equity.
Post-transaction PF Debt/EBITDA of 5.1x

Preliminary valuation – LBO analysis

INVESTOR RETURNS

in $mm	*Close 2013*	*FY 2014F*	*FY 2015F*	*FY 2016F*	*FY 2017F*	*FY 2018F*
Entry						
EV/EBITDA 13E (x)	10.1x					
Enterprise value	15,641					
Purchase price	20,016					
Fees	239					
Equity check	(8,255)					
Investment period						
Dividends		-	-	-	-	-
Exit						
EV/EBITDA 18E (x)						10.1x
Enterprise value						23,872
Net debt						1,012
Equity proceeds						22,860
Net proceeds	**$ (8,255)**	**$ -**	**$ -**	**$ -**	**$ -**	**$ 22,860**

IRR	**22.6%**
Multiple on Money	**2.77x**

Assumes exit multiple equal to entry multiple;
PE consortium IRR of 22.6% with money multiple of 2.8x over 5 years

Preliminary valuation – LBO analysis

SENSITIVITY ANALYSIS

5-year IRR sensitivity

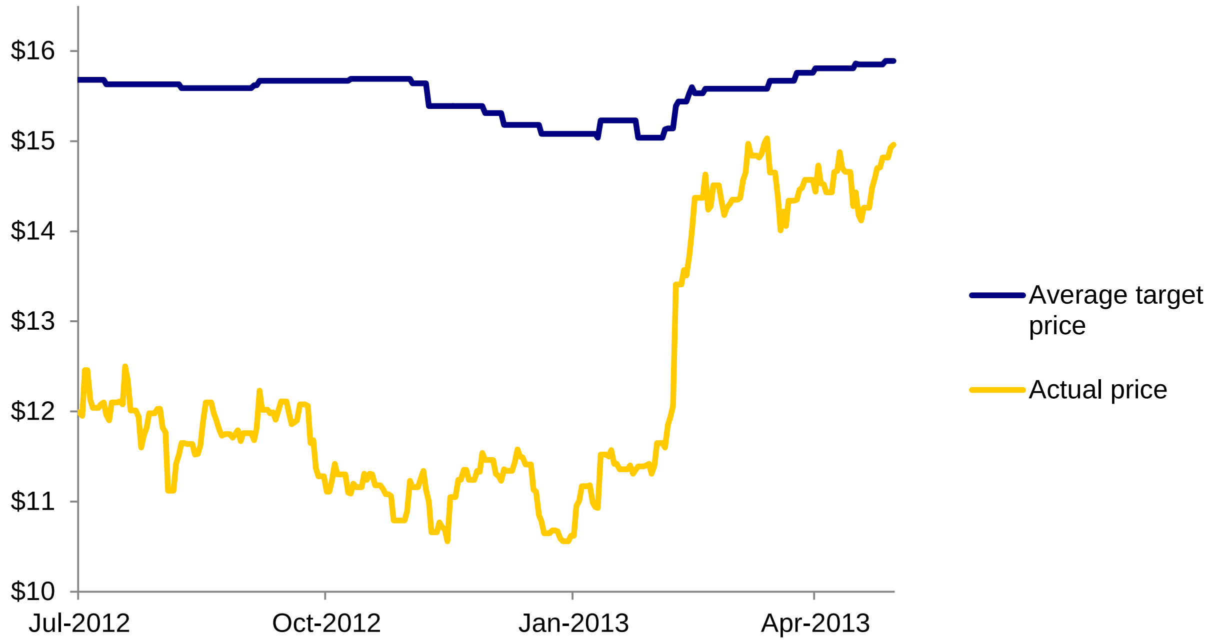
		Purchase premium				
		20.0%	22.5%	25.0%	27.5%	30.0%
Exit multiple	9.7x	24.1%	22.8%	21.6%	20.4%	19.3%
	9.9x	24.6%	23.3%	22.1%	20.9%	19.8%
	10.1x	25.1%	23.8%	22.6%	21.4%	20.3%
	10.3x	25.6%	24.3%	23.1%	21.9%	20.8%
	10.5x	26.1%	24.8%	23.6%	22.4%	21.3%

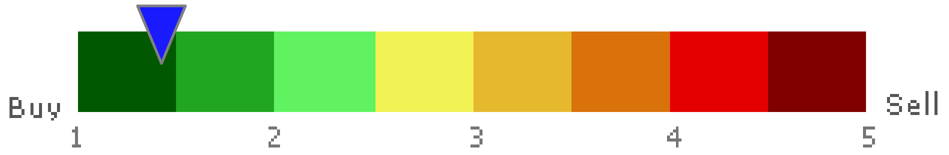
Multiple on Money sensitivity

		Purchase premium				
		20.0%	22.5%	25.0%	27.5%	30.0%
Exit multiple	9.7x	2.94x	2.79x	2.65x	2.53x	2.42x
	9.9x	3.00x	2.85x	2.71x	2.59x	2.47x
	10.1x	3.07x	2.91x	2.77x	2.64x	2.52x
	10.3x	3.13x	2.97x	2.83x	2.70x	2.58x
	10.5x	3.19x	3.03x	2.88x	2.75x	2.63x

c.20% return over 5 years even at a 30% purchase premium

Preliminary valuation – analyst targets





Source: S&P CAPITAL IQ

Strong buy recommendation with a consensus target share price of $16

Preliminary valuation – trading comparables

TRADING COMPARABLES

	Market data		Trading multiples			
Company	**Mkt Cap ($bn)**	**EV ($bn)**	**EV/EBITDA**	**Trailing PE**	**Forward PE**	**PEG Ratio (5yr)**
Electronic Arts	5.1	4.3	11.0x	31.2x	15.9x	1.3x
Take-Two Interactive	1.3	1.2	(17.2x)	nm	6.6x	9.6x
Int'l Game Technology	4.3	6.0	7.4x	17.1x	12.3x	0.9x
Zynga	2.5	1.4	24.7x	nm	319.0x	(3.0x)
Sony Corporation	16.7	16.9	4.5x	nm	87.6x	n/a
Nintendo	1.7	2.6	(20.6x)	59.7x	nm	n/a
High			**24.7x**	**31.2x**	**319.0x**	**9.6x**
Mean			**6.5x**	**24.2x**	**88.5x**	**2.2x**
Median			**9.2x**	**24.2x**	**14.1x**	**1.1x**
Low			**(17.2x)**	**17.1x**	**6.6x**	**(3.0x)**
Activision Blizzard	**15.9**	**11.9**	**7.6x**	**14.3x**	**13.8x**	**2.1x**

Source: Yahoo Finance

Note: Market data as of 19th April 2013. Median, Mean numbers are taken for the highlighted companies

Enterprise value of $14.2bn on a 9.2x median EV/EBITDA

Preliminary valuation – transaction comparables

MEDIA INDUSTRY PRECEDENT TRANSACTIONS

Ann. date	Acquiror	Target	% purchased	Price paid ($mm)	EV / implied value ($mm) [1]	EV / EBITDA (x)
Dec. 2012	News Corp.	Sports Time Ohio	100%	230	230	15.2x
Dec. 2012	Discovery	SBS Nordic Assets (from ProSieben)	100%	1,736	1,736	9.9x
Nov. 2012	News Corp.	YES Network	49%	1,470	3,000	12.3x
Aug. 2011	Scripps Networks	UKTV (from Virgin Media)	50%	555	1,110	9.0x
Feb. 2011	News Corp.	Shine	100%	670	670	13.2x
Aug. 2010 [2]	Time Warner (Warner Bros)	Shed Media	56%	160	287	6.4x
Jun. 2010 [2]	News Corp.	BSkyB	61%	11,540	18,961	11.8x
Nov. 2009	Scripps Networks	Travel Channel	65%	634	975	11.8x
Aug. 2009	Disney	Marvel Entertainment	100%	3,846	3,846	11.9x
Jul. 2007	News Corp.	Dow Jones	100%	5,766	5,766	19.8x
May. 2006	Time Warner	Court TV	50%	735	1,470	17.6x
Dec. 2005	Viacom	DreamWorks LLC	100%	1,600	1,600	16.0x
Mean						**12.9x**
Median						**12.1x**

Source: SNL, Capital IQ, FactSet, Company documents, Barclays Capital estimates
Note: Excludes deals less than $200M, and less than 50% purchased
(1) Transactions grossed up to 100%, where applicable
(2) Pending

Enterprise value of $18.8bn on a 12.1x median EV/EBITDA