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## The Aftermath

### Microsoft-Yahoo!: Ten Takeaways

[Wendy Tanaka](#), 05.05.08, 6:00 AM ET

BURLINGAME, CALIF. - **Microsoft's** three-month quest for **Yahoo!** came to a close Saturday as the software giant withdrew its multibillion-dollar bid for the Internet portal, confounding industry observers. They had placed bets on two other scenarios: a friendly merger between the tech titans at a higher price than the \$31 per share Microsoft had originally offered, or a hostile takeover from Microsoft. Here's what happened--and what's next.

### Why did the deal fall apart?

**Microsoft** (nasdaq: [MSFT](#) - [news](#) - [people](#)) and **Yahoo!** (nasdaq: [YHOO](#) - [news](#) - [people](#)) could not agree on an acquisition price. Microsoft Chief Executive Steve Ballmer and Senior Vice President Kevin Johnson met Yahoo! co-founders Jerry Yang and David Filo in Seattle on Saturday to negotiate. Ballmer raised Microsoft's offer to \$33 a share but Yang, Yahoo!'s chief executive, wanted \$37. After the meeting, Ballmer sent a letter to Yang stating Microsoft's withdrawal and adding that "a deal is not to be."

### Did Microsoft do the right thing by walking away?

Probably. Microsoft offered a hefty premium to Yahoo!'s price. The software titan's original \$31 a share offer on Jan. 31 was a 62% premium to the Internet portal's stock price on that date. Microsoft said its last offer of \$33 would have added another \$5 billion in value to the deal. The deal was originally valued at \$45 billion, but in the ensuing months, it fell to \$42 billion as Microsoft's stock price dipped.

### Did Yahoo! do the right thing by not accepting Microsoft's higher offer?

Probably not. Yahoo! doesn't have an alternative deal that would return as much to shareholders.

### How will Wall Street and shareholders react?

Yahoo!'s shares likely will take a beating. Analysts expect the stock to fall back to \$19, the price it was trading at when Microsoft launched its bid. By contrast, Microsoft's shares likely will rebound above \$30.

Yahoo! has already been hit with shareholder lawsuits and should expect more. Microsoft's shareholders aren't expected to sue, but they're anxious to know how the company plans to boost its stock.

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## **What's Microsoft's next step?**

It will pursue other acquisitions. In a meeting with employees last Friday, Ballmer indicated that he'll turn his attention to other companies. "If the Yahoo! deal doesn't happen, we know that there's a different set of things that we'll wind up investing in," he said. "Yahoo! is not a strategy; it's part of a strategy." And Microsoft is no stranger to acquisitions: it has bought hundreds of companies in its 33 years.

## **What other companies is Microsoft interested in acquiring?**

Speculation is swirling about Microsoft might be interested in acquiring AOL from **Time Warner** (nyse: [TWX](#) - [news](#) - [people](#)) or MySpace from **News Corp.** (nyse: [NWS](#) - [news](#) - [people](#)). Trip Chowdry, managing director at Global Equities Research, wouldn't name names, but says Microsoft will seek out up-and-coming companies that have innovative technologies and also generate revenues from either licenses, transactions, subscriptions or advertising. "Microsoft will acquire a portfolio of companies beyond Web 2.0 plays," Chowdry says. "Microsoft doesn't want to fight yesterday's story; it wants to capture the future."

## **What's Yahoo!'s next step?**

The company is now under enormous pressure to find an alternative deal, or deals, that can rev up its stock. It's considering a search-advertising outsourcing partnership with **Google** (nasdaq: [GOOG](#) - [news](#) - [people](#)) to generate more revenue. The two companies launched a trial partnership a few weeks ago that is said to be going well. Look for an announcement on this pact.

Yahoo! also might still be considering a merger with AOL. Yahoo! also had discussions with News Corp. to acquire its social networking behemoth MySpace. But later, News Corp. switched sides and considered joining Microsoft's bid for Yahoo!, so a deal with News Corp. seems unlikely now.

## **Will Microsoft come back at Yahoo! later?**

If Yahoo!'s stock tumbles, industry observers say the acquisition door could open again, perhaps later this year. Microsoft will "watch what happens to Yahoo! and wait for Yahoo! to falter," says Edward Deibert, a director at law firm Howard Rice Nemerovski Canady Falk & Rabkin. "If Yahoo! is unable to deliver, Microsoft could take another stab at a [lower] price."

## **What will happen to Ballmer and Yang?**

It's unclear whether Ballmer will be seen as a strategic genius or the guy who couldn't get the deal done. Chowdry says Ballmer only went after Yahoo! and put a sky-high price on the company to make sure no other company acquired it. And while Ballmer has done lots of deals, he's never done a deal as big as Yahoo! It would have been at least seven times larger than Microsoft's biggest deal to date--the \$6 billion buyout of digital marketing firm aQuantive last year.

Yang could be ousted if he doesn't find a way to bump up Yahoo!'s stock in a hurry. Industry watchers are scratching their heads about why he wanted so much more than what Microsoft offered.

## **What is Silicon Valley's reaction to the news?**

I think people are pretty shocked and surprised" that a deal didn't happen, says Keith Rabois, vice president of strategy and business development at Slide, a Web application developer. "The Internet trendsetters all think of Yahoo! as past its prime" and expected it to accept a good offer.

Jay Bhatti, co-founder of search engine Spock.com, says start-ups in the Valley are generally relieved that the deal didn't happen because two major acquirers are still intact. The deal would have consumed both Microsoft and Yahoo! for a year while they integrated their operations and would have left the Valley with just one major acquirer where once there were two. Now, "Ballmer and Microsoft will want to do more small acquisitions," Bhatti says. "They might spend \$10 billion buying 20 small start-ups. I think the Valley's pretty happy about that."

Rabois notes that Microsoft's image in the Valley has improved as well. "Microsoft had a bad reputation among Internet elitists mostly because of the browser wars" in 2000 when Microsoft put Netscape out of business, he says. Now, Microsoft is considered a good business partner. Slide, for instance, has an advertising partnership with Microsoft. The software titan's most high-profile partnership is with Facebook, in which it owns a small equity stake.

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