

Corporate Finance 15.402
Assignment 3: Debt Policy at UST Inc.

Prepare a memo addressing the following questions:

1. Suppose that you are considering purchasing UST's bonds. Briefly describe the attributes and business risks associated with UST that you would find of interest.
2. UST Inc. has a long history of conservative debt policy. Briefly describe why they are considering a recapitalization that involves issuing debt and repurchasing equity?
3. Should UST Inc. undertake the \$1 Billion recapitalization? Calculate the effect on stock price assuming that the entire recapitalization is done immediately (January 1, 1999).
 - a. In this calculation, assume the following:
 - i. Corporate tax rate is 38%
 - ii. All equity is bought back at a price that reflects the added value of the tax shield.
 - b. Prepare a Pro Forma Statement to analyze whether UST will be able to make the interest payments.
 - i. Use Exhibit 8 to determine UST's credit rating and interest rate.
 - ii. State your assumptions clearly.