A proxypower report

Report on the Proxy Statement (Sch. 14A) of

Dell Inc.

(NASDAQ: DELL)

Proxy Statement dated:	May 31, 2013
For a special shareholders meeting on:	July 18, 2013
For holders as of:	June 3, 2013

Report Overview

It's not the principle. It's the money.

Reports in the financial press have criticized Michael Dell's procedures in making his February 5 offer of $13.65 a share, along with Silver Lake Partners, for the 84% of Dell shares he doesn't own.[1] That offer was presented to shareholders on May 31 for a vote at a special shareholders' meeting on July 18.[2]

Our objection is not to the principle or the process. Our objection is to the amount of the offer. The $13.65 per share offer is below both the average 38% market premium as measured from the day before the offer and the average 46% premium as measured from 41 days before the offer.

Therefore, we recommend a No vote on the proposal to adopt the Plan of Merger with the entities that were formed by Mr. Dell and Silver Lake to take Dell private. We also recommend a No vote on the two other proposals in the Proxy Statement (Schedule 14A), both of which are incidental to and supportive of the going-private transaction.[3]

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[1] See, e.g., Gretchen Morgenson, "Dell's Intentions Get a Hard Look," The New York Times, Feb. 24, 2013, p. BU1, and Andrew Bary, "Michael Dell's Folly," Barron's, April 1, 2013, p. 18.

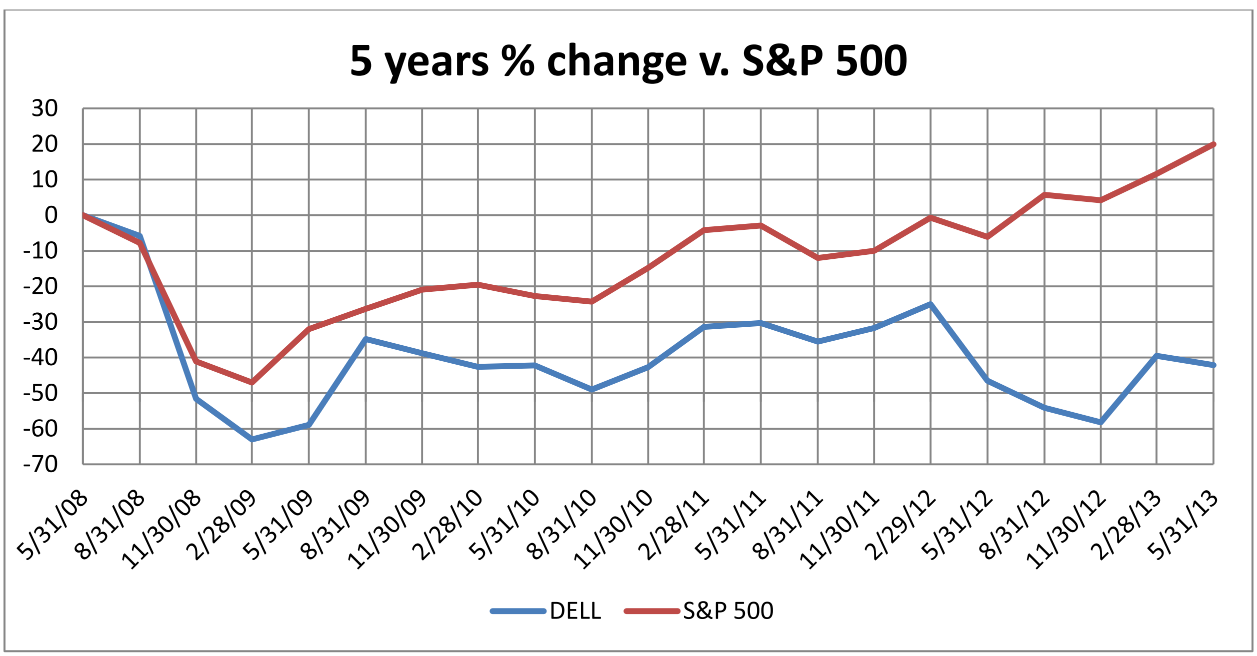
[2] The definitive proxy materials are available on the SEC's website at http://www.sec.gov/Archives/edgar/data/826083/000119312513242115/d505470ddefm14a.htm. Although dated May 30, they are effective as of May 31.

[3] See p. 10 of this report for the proposals.

Company Overview[4]

Sector:	Technology	Diluted EPS:	$1.35
SIC:	3571 (Electronic computers)	Cash flow from operations/share:	$2.13
CEO:	Michael S. Dell	P/E:	12.62
Since:	2007 (and 1984-2004)	Dividend:	$0.08, quarterly
Chairman?	Yes	Yield:	2.4 %
Succeeded:	Kevin B. Rollins	2013 return on equity:	26.6 %
Market cap:[5]	$ 23.34 billion	Three year avg. return on equity:	39.4 %
Net income:	$ 2.4 billion	2013 return on assets:	5.3 %
Share Price:	$ 13.35	Three year avg. return on assets:	7.4 %
		Liabilities/equity:	3.44

Share price performance



[4] Information is from or derived from 2013 10-K (FYE 2/1/2013) unless otherwise specified.
[5] Market cap, share price, P/E and yield are from Yahoo! Finance as of May 31.

Discussion

Michael Dell and Dell, Inc. have received a lot of criticism for the process by which he and Dell's board of directors made and reacted to his offer.

One noted criticism of the proposed deal came from the New York Times, whose Gretchen Morgenson has said that "an independent, peer-reviewed analysis of Dell's enterprise value should be done on behalf of its outside shareholders." According to Ms. Morgenson, "such an assessment would assure investors that they are being bought out at a fair value."[6]

There are two problems with this criticism.

First, the only fair value in capitalism is the price the market will bear. So far, none of the proponents of a higher intrinsic value for Dell have offered to pay all Dell shareholders what they claim those shares are worth. According to Ms. Morgenson's article, "Southeastern Asset Management, one of Dell's largest outside shareholders, estimates that the company is worth $23.72 a share, almost 75 percent more than the buyers are offering." But that's what Southeastern wants *Michael Dell* to pay *them*. It's not what *they* are willing to pay for Dell's shares.

Same with Carl Icahn. In a March 5 letter to the Dell board, he proposed that Dell pay a one-time $9/share dividend, financed in part by money he or his

[6] Gretchen Morgenson, "Dell's Intentions Get a Hard Look," The New York Times, Feb. 24, 2013, p. BU1.

company would lend Dell.[7] But that debt would have constituted a legal obligation on Dell's part to repay Mr. Icahn and/or his company. It would not have been as risky to Mr. Icahn as Mr. Dell's offer is to Mr. Dell, even at the price Mr. Dell is offering. And Mr. Icahn has not offered to pay the $22.81 per share he says Dell is worth.[8]

Mr. Icahn's second offer was to pay $15 per share up to a maximum of $15.6 billion, which would have gotten him about 60% of the company.[9] His third (and as of now, latest) offer risks even less of his own money. He teamed up with Southeastern to propose that Dell shareholders get a choice between a $12 cash dividend and more stock.[10] The source of the financing for this deal was not disclosed, but one guesses that Mr. Icahn himself would be a source, meaning he could become both Dell's second largest shareholder (behind Southeastern) and largest creditor. Mr. Dell is the only billionaire right now with an offer to buy Dell.

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[7] A copy of Mr. Icahn's letter was attached to Dell's March 7 Schedule 14A filing. Mr. Icahn has since changed his offer twice.

[8] See Dell's March 7 Schedule 14A for Mr. Icahn's figure.

[9] See Dell's March 29 Schedule 14A (Preliminary Proxy Statement), p. 45, for Mr. Icahn's offer, which was made March 22. $15.6 billion / $15/share = 1,040,000,000 shares. According to Dell's most recent 10-K, there were 1,747,220,324 shares outstanding. 1,040,000,000/ 1,747,220,324 = .595. As of May 31, there are 1,781,176,938 shares outstanding, meaning Mr. Icahn's offer would have amounted to 58 %. 1,040,000,000/1,781,176,938 = .584.

[10] See the joint Icahn/Southeastern Schedule 14A dated May 10, 2013.

Second, Dell has done a decent job of answering its critics on the process issue. It managed to get Mr. Dell and Silver Lake to raise their original offer of $11.22-$12.16 per share[11] to $13.65. On March 7, Dell said that "Evercore Partners, an independent financial advisor to the Special Committee [of Dell's board], is actively soliciting third parties to determine their potential interest and is incentivized to find a superior proposal if one exists."[12] Also according to Dell:

> During the go-shop period, Evercore contacted a total of 67 parties, including 19 strategic parties, 18 financial sponsors and 30 other parties, including sovereign wealth funds, to solicit interest in pursuing a possible transaction. Evercore also received unsolicited inquiries regarding a possible transaction from four additional parties, including two strategic parties and two financial sponsors. Of the 71 total parties with which Evercore communicated, … 11 parties … expressed interest in evaluating a possible transaction.[13]

The upshot of all this was that both Blackstone Group, through Evercore, and Carl Icahn, communicating directly with Dell's board, made offers to buy a substantial chunk of Dell at a share price higher than Michael Dell and Silver Lake are offering,[14] although both have since withdrawn their offers. And buying a substantial chunk is not the same as buying 100%.

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[11] Dell's March 29 Preliminary Proxy Statement, p. 26.

[12] See Dell's March 7 Schedule 14A. Is "incentivize" a word?

[13] Dell's March 29 Preliminary Proxy Statement, p. 42.

[14] Blackstone's offer was "in excess of" $14.25 per share, subject to an unspecified cap. Mr. Icahn's offer was $15 per share, up to $15.6 billion. Dell's March 29 Preliminary Proxy Statement, p. 42. Blackstone withdrew its offer on April 18; see Dell's April 19 Schedule 14 filing.

While the terms of Dell's agreement with Evercore haven't been disclosed, presumably Evercore gets a fee if they find a buyer above $13.65 per share, although the likelihood of that happening seems low. If there were other potential buyers out there, they would have come forward by now. Regardless, one hopes that Evercore gets paid something if an offer is made for the whole company, not only if the offer is consummated – they would have added value for Dell's shareholders even if the offeror is outbid by Mr. Dell (or someone else).

Another criticism of Mr. Dell's offer came from Leon Cooperman, an investment manager quoted in Barron's, who said that Mr. Dell is "not doing this because he thinks his company is overvalued. He wants to make money."[15] Isn't that why people are in business? Isn't Mr. Cooperman in business to make money?

The only thing wrong with Mr. Dell's process is the amount of the offer that resulted from it. Dell tries to sell the offer by pointing out that it "provides value certainty at a 37% premium above the average price for the 90 days before rumors regarding the transaction surfaced."[16] That sounds good, but the fact remains that

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[15] As quoted in Andrew Bary, "Michael Dell's Folly," Barron's, April 1, 2013, p. 20.

[16] See Dell's March 6 Schedule 14A. The same argument is made in the May 31 materials (see pp. 5, 87). DELL closed at 10.88 on Friday, January 11, having closed no higher than 11.00 since August 2012. Over the next two trading days, it climbed 21% to close at 13.17 on January 15. This is strong circumstantial evidence that the deal was leaked over the January 12-13 weekend. Historical stock price data from Yahoo! Finance.

the average premium for consummated takeovers where the target was listed on the NYSE or Nasdaq from 1990-2008 was 38.38%, as measured from the closing price the day before the announcement[17]; and the average final offer premium for public U.S. targets from 1973-2002 was 46.1% as measured from 41 days before the first bid.[18] Mr. Dell's $13.65 per share offer is below both averages.

Dell closed at $13.35 on May 31, up from $13.27 the day before, less than a 1% change. That means the market is predicting the deal will be approved by shareholders at $13.65, and that the Southeastern/Icahn proposal will not: assuming an investor can borrow at some amount less than 6 %, she could borrow $13.35 now, buy Dell shares now and repay $13.65 on October 31 when the merger closes and she gets cash for her shares.[19] If the market thought either that the Southeastern/Icahn proposal will gain shareholder approval,[20] or that Mr.

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[17] J. Kesten, "Managerial Entrenchment and Shareholder Wealth Revisited: Theory and Evidence from a Recessionary Financial Market," 2010 BYU L. Rev. 1609 (2010), App. E. Dell's close on February 4 was 13.27, meaning the offer was a 2.9% premium.

[18] B. Eckbo, "Bidding Strategies and Takeover Premiums: A Review," Journal of Corporate Finance, vol. 15, pp. 149-178 (2009), Table 3. Dell's close on December 27, 2012 was 10.19, meaning the offer constituted a 34% premium.

[19] May 31 close = 13.35. 13.35 x .06 = 0.801. 0.801 x 5/12 = 0.33 (assumes deal closes October 31, five months after May 31). 13.35 + 0.33 = 13.68. Dell expects the deal to close on during its third accounting quarter, which ends November 1. May 31 Schedule 14A, p. 4.

[20] Southeastern, apparently with Mr. Icahn's approval and participation, filed its own Schedule 14A with the SEC on May 31, urging Dell shareholders "to refrain from signing or returning any proxy card voting for the Management Buyout Proposal (or, for that matter, any proxy card sent to you by Dell)." The Southeastern filing did not explicitly urge shareholders to vote "No" on the Dell/Silver Lake offer.

Dell's offer would not be approved (or both), the price would be something other than roughly equivalent to Mr. Dell's offer. Whether higher or lower depends on what you think of the Icahn/Southeastern proposal and Dell's business prospects.

This tells me that the market thinks the merger proposal is ok. But the fact remains that the premium is below average. And with the market at or near record highs, the premium should be higher.

If you need the money now, sell. If you don't need the money now, vote "No."

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Appendix

Voting Items (Board recommendation)	**proxypower** recommendation
1. Proposal 1 – Proposal to adopt the Agreement and Plan of Merger, dated as of February 5, 2013, by and among Denali Holding Inc., Denali Intermediate Inc., Denali Acquiror Inc. and Dell Inc., as it may be amended from time to time. (For)	Against
2. Proposal 2 – Proposal to approve, on an advisory (non-binding) basis, the compensation that may become payable to the named executive officers of Dell Inc. in connection with the merger, as disclosed in the table under "*Special Factors — Interests of the Company's Directors and Executive Officers in the Merger — Quantification of Payments and Benefits — Potential Change of Control Payments to Named Executive Officers Table*," including the associated footnotes and narrative discussion. (For)	Against
3. Proposal 3 – Proposal to approve the adjournment of the special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the special meeting to approve the proposal to adopt the merger agreement. (For)	Against