

Apple gets into debt

The big story of the day is Apple's entering the debt market, with a planned debt issue of about \$17 billion. At first sight, it may seem odd that a company with Apple's huge cash reserves would need to borrow money, but as the old adage goes, those who need the money least are more likely to borrow it. Since it brings together all of the issues that we have talking about in class on capital structure and dividend policy, I thought I would line them all up.

1. The trade off: On the qualitative trade off, do you think Apple will benefit from debt? If yes, why? If not, why not?
2. Optimal capital structure: Using the optimal capital structure spreadsheet, I have computed the optimal debt ratio for Apple to be about 60% (that is \$240 billion in debt capacity). As with any technology firm, red flags will go off. So, go into the optimal capital structure spreadsheet and see how much buffer Apple has to borrow. (Drop the operating income by 20%, 30% or even 50% and see what happens to debt capacity).
3. Debt Design: In the news story, there is a broad description of the debt design that Apple is using: *The Apple offering comprises six chunks of debt, according to a regulatory filing from the company. Four chunks of fixed-rate debt are being offered maturing in three, five, 10 and 30 years. Apple is also selling two tranches of floating-rate debt, maturing in three and five years.* Based on our discussion in class about the "right debt" for a company, do you think that this is the right type of debt for Apple. (Put differently, do the maturities make sense? How about the currency choice? And the floating rate debt?
4. Cash return: Apple is proposing returning about \$100 billion in cash over the next two years to its stockholders. Based on our discussion of dividend policy so far, do you think that makes sense?
5. Dividends versus Buybacks: The cash will be returned primarily in the form of stock buybacks with only a small dividend increase. Do you agree with that mix? If yes, why? If not, why not?