Wall Street warm to cold feet at MGIC

Shares rise 17% as company rethinks deal with Radian

By Paul Gores of the Journal Sentinel

Posted: Aug. 9, 2007

MGIC Investment Corp.'s decision to reconsider its planned acquisition of Radian Group Inc. received some encouragement from investors Wednesday, as shares of MGIC rose more than 17%.

Milwaukee-based MGIC issued a statement Tuesday afternoon saying it wasn't obligated to complete its merger with Radian. Like MGIC, Radian, of Philadelphia, insures lenders against losses if homebuyers don't pay their mortgages. The industry has been battered by the crisis in the subprime mortgage market.

Shares of MGIC rose $6.06 to close at $40.90 on Wednesday. Radian shares closed up 38 cents, or almost 2%, at $21.

"The market is pretty much saying, 'We don't think it's a good deal anymore, and if in fact you step away from it, your stock's worth more than if you go through with it,' " said Dan Olszewski, a business school professor at the University of Wisconsin-Madison.

It's possible the deal still will go through, but at renegotiated terms, according to Steve Stelmach, a stock analyst with Friedman, Billings, Ramsey & Co. In a research report, Stelmach said he thinks that's probably what will happen.

He said Radian, because of a weaker credit rating position, needs the deal to be completed much more than MGIC does.

When the stock-for-stock deal was announced in February, it was worth about $4.9 billion. At Wednesday's closing prices, the transaction would be worth $3.2 billion.

In announcing Tuesday that it was "not obligated" to complete the Radian acquisition, MGIC cited last week's announcements that the two companies could lose their entire $1 billion joint investment in a subprime mortgage company called Credit-Based Asset Servicing and Securitization LLC, or C-BASS.

MGIC said Wednesday it would have no further comment. The company said it would finish its analysis of the situation by Monday.

A Radian spokeswoman said the company had no comment beyond its press release issued Tuesday night, in which it said, "We do not believe the impairments related to C-BASS LLC affect MGIC's obligation to go forward with the merger agreement."

Radian's statement said it has fully complied with all of its obligations under the merger agreement and that it was looking forward to completing the deal "as promptly as possible."

Laxson Boyd, a principal at Wadsworth Whitestar Group consultants in Milwaukee, said this may simply be a case in which the company being acquired looks less and less attractive to the acquirer given what's happened to the mortgage industry.

"You could be seeing a situation where MGIC has gone a little further into this thing, got its due diligence ramped up and began to see some hair on the deal as it relates to the subprime market from Radian," Boyd said.

The merger agreement includes a $185 million termination fee, but whether that is an issue in negotiations wasn't known. A breakup fee typically is the penalty a company pays to get out of a deal if another suitor comes along and offers a higher price.

"If shareholders see the deal as having been bad, they are going to get points for walking away from it even if it costs them a lot of money to do so," said Boyd.

Jon C. Bruss, chief executive of Fortress Partners Capital Management Ltd. in Hartland, said both companies have "taken it on the chin" as the subprime mortgage market has tanked.

"The question is whether the merger agreement will view this as a material adverse change and allow MGIC to escape," he said.

Stelmach said the merger "is not without its merits" for MGIC, "namely the added breadth of product offerings at (Radian) and the cost savings available if the deal is completed."

When the merger was announced last winter, the companies predicted a pretax savings of $128 million and a quicker entrance into markets abroad.

Bloomberg News contributed to this report.