"A solution to the Palm—3Com spin-off puzzles"

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ABSTRACT

This paper revisits the relative pricing of Palm and 3Com at the peak of Internet pricing. We offer a simple rational explanation of the pricing during the Palm—3Com spin-off episode (when it was suggested that the market valued the common stock portion of Palm owned by 3Com at more than the whole of 3Com) based on the observation that Palm shares issued in the IPO had higher valuation than shares still held by 3Com due to the lending fees that Palm shares could have earned.

In valuing 3Com we use Palm's post-spin-off forward prices, which can be calculated from the market prices of calls and puts. Considering forward pricing resolves various pricing puzzles. We also re-interpret empirical evidence about the relative pricing movements between Palm and 3Com in light of the resolution of uncertainty about the spin-off.