A Buy-and-Build Strategy in the Services Industry

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Abstract

Amidst an unprecedented scenario of widespread pandemic situation and major economic downturn, this dissertation tries to discover the viability of an investment in a leading, yet recent, player in what was an initially unknown market - the Spanish residential property management market.

The dimension of the market, the competitive landscape as well as what drives customers to choose a company over another were all questions that this dissertations answers. The residential property management sector proved to be extremely resilient due to customer inertia and highly fragmented, opening an opportunity for the target company to put a buy-and-build strategy into place.

Moreover, the analysis on the company also confirmed its past success on its acquisition strategy, its tech-driven approach to customers as a differentiation factor among its peers and a outstanding rate of clients' retention.

To enable the scrutiny of the viability of a possible investment, a financial model was performed by projecting several input variables in a time-horizon until 2030. Finally, this dissertation designs a mezzanine investment structure that mitigates the risk of losing capital and provides equity-like returns (20,8% Internal Rate of Return and 2,5x Money Multiple in the central scenario).

Resumo

Num cenário ímpar de situação pandémica globalizada e de grande recessão económica, esta dissertação tenta descobrir a viabilidade de um investimento num player líder, mas recente, naquilo que era um mercado inicialmente desconhecido - o mercado espanhol de administração de condomínios.

A dimensão do mercado, a paisagem competitiva, bem como o que leva os clientes a escolher uma empresa em detrimento de outra, são questões a que esta dissertação responde. O sector de administraçao de condomínios revelou-se extremamente resiliente devido à inércia dos clientes e altamente fragmentado, abrindo uma oportunidade para a empresa-alvo de colocar em prática uma estratégia de crescimento por aquisição.

Além disso, a análise da empresa também confirmou o seu sucesso passado nas aquisições já efetuadas, a sua abordagem tecnológica ao mercado como factor de diferenciação entre os seus concorrents e uma taxa notável de retenção de clientes.

Para permitir a validação da viabilidade de um possível investimento, foi realizado um modelo financeiro através da projecção de vários indicadores num horizonte temporal até 2030. Por fim, esta dissertação desenha uma estrutura de investimento mezzanine que atenua o risco de perda de capital e proporciona retornos semelhantes aos de acções (20,8% de Taxa Interna de Retorno e 2,5x Múltiplo de capital no cenário central).

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To the two Guilhermes, for mastering the art of coexisting with one another and always knowing when to intervene, making me a better professional and happier friend at the same time.

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To my friends with whom I have been lucky enough to meet along the way. For accepting me, supporting me and improving me. For being there in my ups and downs. Without them none of my achievements would make any sense.

To my parents. For their lifelong example. For excelling in doing what they love and setting the bar so high. I was never meant to follow your footsteps, but I always meant to make you proud.

To the ones out there also chasing their dreams.

"You can't make a race horse out of a pig."
"No", said Samuel, "but you can make a very fast pig"

John Steinbeck, East of Eden

Contents

Acronyms and Symbols

CAGR	Compound Annual Growth Rate
CapEx	Capital Expenditures
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CG	Capital Gain
CHRO	Chief of Human Resources Officer
COGS	Cost of Goods Sold
CXO	Chief of Expansion Officer
EBITDA	Earnings before interest, tax, depreciation and amortization
EV	Enterprise Value
HNWI	High Net Worth Individuals
HOA	Homeowners Association
IRR	Internal Rate of Return
LTM	Last Twelve Months
MM	Money Multiple
OPEX	Operating Expenses
SG&A	Selling, General and Administrative Expense

List of Figures

Chapter 1

Introduction

Early in the history of mankind, our ancestors soon realized that, in order to thrive individually and collectively, they had to organize themselves to live in society by following and complying with certain rules, procedures or guidelines, thus creating common ground for sustainable governance. This kind of primitive rationale may have evolved throughout the years but it is still nowadays what is behind the way cities or even corporate organizations for instance, are structured.

With the rural exodus of past centuries and consequent densification of urban areas - a trend that still prevails, despite environmental concerns or Covid-19 may have an impact in the opposite direction regarding this matter in the future -, people started living in increasingly larger condominiums and cohabiting with more and more families. This led to the aforementioned increasing need to establish rules for governance in the places we live - taking that into account, homeowners associations (HOAs) were created.

For this type of association - widespread and, in many countries, even obliged by law to be established in buildings with more than a certain number of homes -, homeowners pay a fixed fee per month based on their properties' relative size among the total size of the building. This calculation is usually measured on a permillage basis and means, for example, that homeowners with bigger properties will contribute more to the HOAs total budget. In exchange for the payment of the fee, homeowners expect the HOA administration to use its budget to pay the bills, hire external staff to take care of standard maintenance or solve any issue that may arise inside the condominium's premises. However, if in the past some homeowners enjoyed the responsibility and used to volunteer for being in charge of the administration, nowadays, with the increasing size of condominiums and subsequent increasing complexity to manage them, this is a job that not many people are fond of.

As a consequence, a shortfall of homeowners willing to assume the responsibilities of managing the HOA on a daily-basis began to exist, thus triggering an increase in demand for HOA professional management companies.

Regarding this type of companies, it is of elementary relevance that one understands their business model: HOA management companies usually charge a fixed amount - regardless of the

property area - for each home that a condominium may have. This happens mainly because it is expected that the HOA administrator that is overseeing the condominium takes care of the common areas such as hallways, garages or gardens. The size of the property has little impact on the HOA administrator's functions since problems inside each property concerns its owner only (certainly acknowledging that, if the situation affects contiguous homes, the HOA administrator will have to help and mediate a potential conflict that could arise from there).

This business model gives companies the opportunity to achieve synergies in some of their operations by expanding their client base: new HOAs will almost surely mean hiring new HOA administrators, but accounting, for instance, can easily be centralized in the back-office with a small team. Also, by taking advantage of economies of scale, HOA management companies can find providers at the best prices in the market, favouring their clients to such a degree that the discount in providers' prices immediately justifies the standard management fee they charge.

In a sector with such a big client base and many companies in the area with low degree of professionalisation, someone saw the opportunity for a market consolidation strategy. To support this business idea, Oxy Capital - the company where this dissertation was held - was contacted to analyse a possible investment opportunity.

1.1 About HoldES

In 2017, the Promoter of the company under analysis [1], c. 30 years old at the time, industrial engineer with a strong financial background - having previously worked in a renowned worldwide strategic consultancy firm and afterwards in a Spanish Private Equity company - raised €4,5 million from 11 High Net Worth Individuals to create a residential property management company from scratch.

In Figure 1.1, it is possible to see the organization of the company and its subsidiaries:

- **HoldES:** is the holding company from where all subsidiaries come from. This type of companies are usually designed because it is easier to legally align shareholders' interests in one company only than having multiple shareholders' agreements with the same purpose. Oxy Capital, if the deal proceeds, will invest in this company despite the fact the target of the investment will be the operational companies of the group.

- **CondES:** is the most important company inside HoldES' perimeter, and the root of the business idea. CondES is a HOA management company and was created with the goal to become the Spanish market leader through a market consolidation strategy. With the capital of its shareholders, CondES soon had enough financial resources to start buying other HOA management companies or their portfolios with the expectation of high returns not only in standard administration fees but also in cross-selling opportunities and agreements with their providers (the latter two only achievable with the scaling up of the business).

[1] For confidentiality reasons, the real name of the company and its subsidiaries will not be disclosed. Operational and financial figures were also changed

- **ObrES:** created 2 years after CondES' inception, once a considerable number of HOAs under its administration was attained. ObrES is a construction & repairs company and was designed to address maintenance works - the largest expenditure in the HOA budget - inside CondES' portfolio.
- **ImovES:** company with residual activity yet due to its short existence (founded in early 2020). ImovES is a Real Estate Brokerage company that wants to be the link between potential homebuyers and properties for sale in HOAs run by CondES. On top of its brief history, ImovES was severely impacted by Covid-19 (down to 0 in revenues during quarantine period) and, for these two reasons, will not be subject of further analysis.

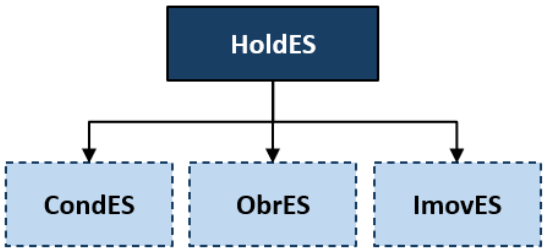

Figure 1.1: Company's Organizational Chart

Any other following businesses that may arise from cross-selling opportunities in the future will all be held by HoldES and consequently inside the perimeter of a possible transaction performed between HoldES and Oxy Capital.

1.2 About Oxy Capital

Oxy Capital is a Portuguese private equity firm founded in 2011. Having initiated its activity immediately after the financial crisis of 2008, Oxy Capital's first funds (still active) were created for restructuring purposes - i.e., investments in debt of viable, but over-leveraged, companies with the purpose of maximizing the returns by converting the debt into equity and applying operational improvement measures. Under these funds, companies like Cabelte, Prio or Grupo Amorim' assets in the tourism industry (e.g. Vilalara or Lake Resort) have integrated Oxy's portfolio.

As time passed by and the economy started to rebound back, the financial health of the Portuguese companies significantly improved in the subsequent years. It wasn't a time for restructuring funds anymore, so new funds were designed for growth investments - i.e., acquiring (either majority or minority positions) or financing companies with stable financial situation and high growth potential. Following the establishment of these funds, Lingote (exited in 2019), Fitness Hut (exited in 2018) and more recently Saphety or Cloudware were invested by Oxy Capital.

Traditionally, the targets of these funds have been Portuguese companies only and the group of investors includes Portuguese Banks, European Investment Banks, Portuguese family offices as well as Oxy itself.

Considering all the companies currently under Oxy Capital management, the portfolio is valued at over €1,1 Billion.

1.3 Aims of the Dissertation

The ultimate ambition of this dissertation is to help Oxy Capital accurately evaluate an investment opportunity and, upon a favourable assessment, successfully close the transaction in the best conditions possible to the company.

To this matter, this thesis aims at obtaining maximum knowledge of this highly unknown market that is the residential property management. Namely, it intends to discover how its economics work - possible revenue streams or typical margins in the sector -, what drives customers when choosing a professional HOA management company or what are the main players and their current positioning among the market.

On the financial side, the goal is to develop a financial model that projects HoldES' subsidiaries future performance in a time horizon until 2028. On top of that, it is also important to understand which type of deal structure suits best both CondES' CEO needs and Oxy Capital's expected investment returns.

1.4 Methodology

The analysis of this investment opportunity went through a series of steps as follows:

- Amidst March 2020, the opportunity arrives at Oxy Capital through its network. By the end of the month, early talks with the CEO were held for a brief introduction of the company and to understand his motive for seeking financing;
- Signing of a NDA (Non-Disclosure Agreement) between both parties followed by an information request, Q&A session and several video conference calls (due to Covid-19 not a single face-to-face meeting was held) organized by Oxy Capital for better understanding of the company and its business model;
- Financial modelling based on the financial information, previous years' financial statements and management Business Plan meanwhile provided. This step precedes a detailed market and financial analysis to avoid focusing efforts on analyzing a company whose economical returns do not meet Oxy's expectations;
- Approval by Oxy's Investment Committee to sign a NBO (Non-Biding Offer) and carry all the Due Diligences needed;

- Validation of market and company assumptions regarding commercial, financial, tax and legal matters;
- Exposure of all findings coming from the Due Diligences in the Investment Committee. In that Committee meeting, a final decision was taken regarding moving forward or dropping the deal.

1.5 Dissertation Structure

Not withstanding the methodology described before, this dissertation is structured as follows:

- **Chapter 2** overviews the state-of-the-art in this type of investment analysis;
- **Chapter 3** introduces CondES and ObrES in more detail, namely their business model and Management Business Plan until 2023;
- **Chapter 4** discloses all the key findings of CondES and the HOA management market arising from the commercial due diligence carried to the company;
- **Chapter 5** explains which assumptions were considered when designing the financial model and reveals the expected returns of the investment, if successfully closed;
- **Chapter 6** brings together all the outcomes from all the analysis that were carried and concludes, based on them, whether Oxy Capital should, or not, invest on CondES.

Chapter 2

Literature Review

This dissertation entails several distinct fields among the financial and corporate world, namely in the Private Equity industry. In this chapter, the aim is to introduce the main concepts with particular relevance to this work, namely how organizations and analysts evaluate companies, how buy-and-build strategies work and what is a mezzanine financing instrument.

Private Equity (PE) firms have gained a reputation over the years due to their investments in non-publicly traded companies and achieved returns. Literature background on this topic provides evidence that Private Equity firms consistently outperformed the global market. Higson and Stucke (2012) shows that U.S. buyout funds created from 1980 to 2008 had returns 5pp per annum above the S&P500 as of June 2010. Harris et al. (2014) also found similar results by comparing how much a PE investor would earn in an equivalent investment in the public market, showing that PE returns outperformed S&P 20% to 27% over the life of the funds. However, Figure 2.1, shows that, in recent years, only top-notch PE institutions clearly surpassed the global market.

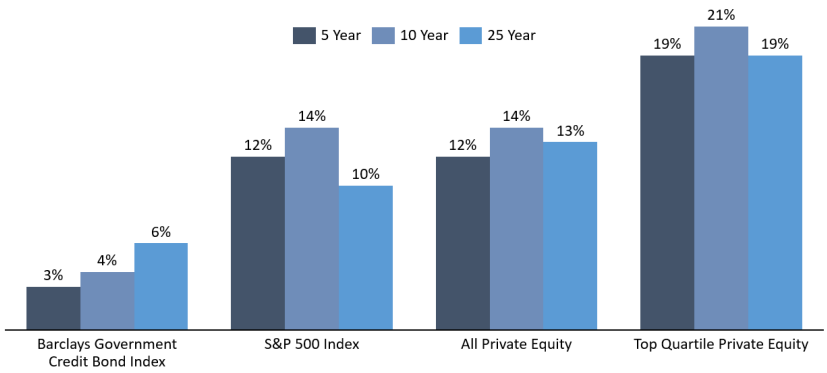

Figure 2.1: *Source: Apollo Global Management, Investors Presentation August 2020*

This evidence is in line with Brown and Kaplan (2019) that claim that, despite still remaining true that U.S. buyouts outperform the global market, this has been an increasingly difficult task as purchase valuations are at its historical high aligned with the fact that capital raised by PEs is also at record levels - thus pressuring more PE firms to close deals.

In order to invest and develop their business model, PE firms have to raise capital from investors. As described by Kaplan and Strömberg (2009):

"A private equity firm raises equity capital through a private equity fund. Most private equity funds are "closed-end" vehicles in which investors commit to provide a certain amount of money to pay for investments in companies as well as management fees to the private equity firm. Legally, private equity funds are organized as limited partnerships in which the general partners manage the fund and the limited partners provide most of the capital. The limited partners typically include institutional investors, such as corporate and public pension funds, endowments, and insurance companies, as well as wealthy individuals. The private equity firm serves as the fund's general partner. It is customary for the general partner to provide at least 1 percent of the total capital."

By closed-end, Kaplan and Stromberg meant Funds whose investors cannot withdraw their capital until the end of the Fund's life. In opposition, mutual funds and hedge funds are open-ended, which decreases the management conditions to invest the money (Stein, 1992).

Regarding how well succeeded PE companies are in convincing institutional investors or High Net Worth Indivuals to commit their money to PE Funds, Cumming et al. (2005) provide evidence that fundraising achieves higher values among funds with higher performance fees and lower fixed management fees for the PE firm. Loos and Schwetzler (2017) complemented this analysis and found a positive effect of a shorter-holding period of previous Funds in the likelihood of raising capital to the same investor by Private Equity firms, meaning their investors are not prone to having their money tied up for long periods of time.

Once the Fund is constituted, the firm may start investing money to meet its investors' expectations. In Figure 2.2, it is possible to see a J Curve that reflects the balance between influxes and outflows of money during a Fund's Life Cycle. During the first years, the Fund will make its best efforts to invest all the capital while it may be already making some early distributions to its investors - typically portfolio firms' dividends.

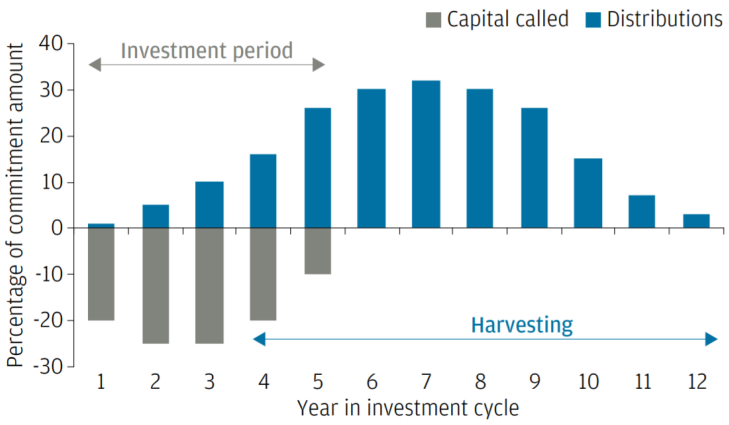

Figure 2.2: "J-Curve Effect".
Source: J.P. Morgan Asset Management, Private Equity Group

2.1 Enterprise Valuation

In order to invest their investors' money, PE firms daily-life is to analyse target companies. To do so, there are countless measures to evaluate them. Figure 2.3 shows the most common valuation methods used among by Morgan Stanley analysts.

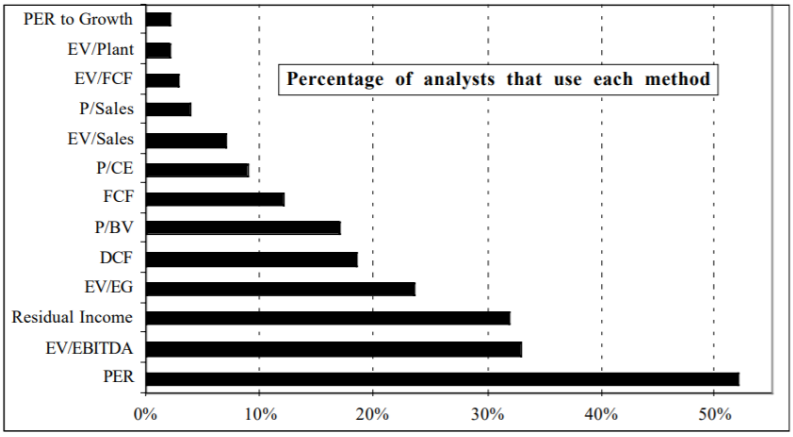

Figure 2.3: Most Used Valuation Methods.
Source: Morgan Stanley Dean Witter Research

Park and Lee (2003) claim that these type of metrics should be seen as relative valuation metrics and not absolute methods. For the purpose of this dissertation two of them will be addressed and compared.

Price to Earnings Ratio - PER or P/E Ratio

This is the most commonly used valuation method, specially in publicly traded companies. Equation 2.1 shows the formula behind its calculation.

$$P/ERatio = \frac{MarketCapitalization}{NetIncome} = \frac{StockPrice}{EarningsPerShare} \tag{2.1}$$

P/E Ratio can be calculated in a simple and fast way and shows how the company's stock is being valued by the market. To do so, investors only need the market capitalization and net income of the company, which are both elements that are public and can be instantly accessed online.

However, according to Damodaran (2002), P/E Ratio is also the most misused valuation metric. Two reasons are behind this rationale: (i) there is more than way to calculate the metric - a investor may use last twelve months (LTM) earnings whereas other investor may use the expected earnings for next year - which may cause to discrepancies in the company's valuation and (ii) net income represents the earnings after all expenditure, which gives us little information regarding the company's structure and respective breakdown between operational and financial costs.

Enterprise Value/EBITDA - EV/EBITDA

Despite not being the most used overall, EV/EBITDA is the main valuation method among the Private Equity industry. The main advantages of its use are three, according to Damodaran. Namely: (i) there are less firms with negative EBITDA than negative Earnings (if one of the latter is negative, the metrics lose their meaning); (ii) there are several accounting methods around the world that may impact the way depreciations and amortizations are incorporated into companies' financial reports - this will affect Net Income, but not EBITDA; and (iii) EV/EBITDA allows the comparison of companies with different financial leverages - interests also impact net income but not EBITDA.

Enterprise Value translates how much the business is worth, regardless the capital structure, i.e., breakdown between equity and debt. Investors analyse this indicator as, in case of a buyout, they have to assume the company's liabilities. Equity value, on the other hand, is the value of the shares of the company and translates the value that PE firms have to pay to the shareholders to take over the company (disregarding Net Debt that is calculated by Total Debt minus Cash or Cash Equivalents. Equation 2.2 shows the bridge from one metric to another.

$$EnterpriseValue = EquityValue + NetDebt \tag{2.2}$$

Dividing the equation for EBITDA in order to calculate EV/EBITDA, we have:

$$EV/EBITDA = \frac{EquityValue + NetDebt}{EBITDA} \tag{2.3}$$

In private transactions, the value of the equity is not given, but rather an output. Bearing that in mind and rearranging 2.3, Equation 2.4 demonstrates the most common equation of a Private Equity analyst.

$$EquityValue = \frac{EV}{EBITDA} \times EBITDA - NetDebt \tag{2.4}$$

NYU Stern Business School provides data of average multiples by sector in the United States as of January 2020. In this particular case, the average multiple in the "Real Estate (Operations & Services)" sector is estimated to be 12,6x EV/EBITDA.

2.2 Buy-and-Build Strategies

There are two main ways for businesses to thrive: organic and inorganic growth. The first implies a growth based on in-house development of the current business whereas the latter implies growth through integration of external entities.

The main business strategy behind this dissertation is the concept of buy-and-build. This strategy entails a focus on growing by acquiring competitors - specifically one with relatively big dimension - and following market consolidation - with several subsequent add-ons to the main platform initially bought. According to Bain & Company (2019):

"When we talk about buy-and-build, we don't mean portfolio companies that pick up one or two acquisitions over the course of a holding period. We also aren't referring to onetime mergers meant to build scale or scope in a single stroke. We define buy-and-build as an explicit strategy for building value by using a well-positioned platform company to make at least four sequential add-on acquisitions of smaller companies."

The reason why buy-and-build deals are so attractive for PE firms, Boston Consultancy Group (2016) claims, is that they generate an average Internal Rate of Return (IRR) of 31,6%, outperforming standalone deals, whose average IRR is 23,1%. Also according to BCG, the creation of value in this type of deals usually comes from synergy levers such as scale effects in procurement and SG&A expenses, enhanced sales force performance and better pricing.

Hammer et al. (2017) finds evidence that the likelihood of add-on acquisition is positively related to moderate degree of fragmentation of the sector and previous Mergers and Acquisitions (M&A) experience of the target firm.

Valkama et al. (2013) corroborates that add-on acquisitions have a positive impact on both equity value and enterprise value of the companies. This evidence is in line with Acharya et al. (2012) that finds that deals with add-on outperform the ones without, regarding operational margin and multiple arbitrage.

Despite such an interesting outlook on buy-and-build strategy, Hammer et al. (2017) analyzed 9548 transactions performed by 1798 PE firms from 1997 to 2012 in 86 countries and discovered that 80% of all add-on acquisitions was performed by solely 16% of the PE firms, suggesting that only top-notch companies achieve this kind of strategy. The authors found positive correlation of add-on acquisitions with acquisition experience and reputation of the PE firm.

Interestingly, Hammer et al. (2017) also finds evidence that many deals with add-on acquisitions may not fully consolidate the market due to its time-restrictions, creating an opportunity for a possible future exit by selling to other PE firms that may want to continue the buy-and-build previously put in place.

2.3 Mezzanine Financing Instruments

Another concept that ought to be contextualized for better comprehension of this dissertation is how Small and Medium Enterprises (SMEs) finance their treasury to fulfill their needs and how Private Equity firms can invest in a company without effectively buying a stake in it.

Companies usually follow the pecking order theory to finance their activity, i.e., at first companies use internal financing, then external financing (as banks for instance) and ultimately give up some of its equity when the first two are not available (MYERS, 1984). The latter option happens because access to financing is usually an important growth constraint for this type of companies (Beck and Demirguc-Kunt, 2006).

In light of the above, a different type of hybrid financing appeared - Mezzanine Financing. In the words of Hoffmann (2008):

"Mezzanine (so-called 'subordinated debt' or 'junior debt'), which is usually unsecured, is categorised between senior debt and equity.[...] Terms and conditions concerning maturity (between 5 to 15 years), interest payment (fixed or variable) and amortisation (e.g., monthly vs. pay-in-kind amortisation, for example, through the divestment of non-core assets at maturity) are structured dependent on future cash flows and the specific financing requirements of the buyout. Compared to senior debt, mezzanine is junior in right of payment. In the case of bankruptcy, mezzanine lenders receive their funds only after the fulfilment of claims of senior debt lenders. Hence, mezzanine is riskier than senior debt. Therefore, the cost of funding is higher than those of senior debt. [...] Further, mezzanine can be structured as junior mezzanine when mezzanine lenders are also granted equity options (a so-called 'equity kicker')."

This type of financing with downside protection of a loan (despite being junior to senior debt from banks) combined with upside potential of equity ends up being a great fit with regard to risk/return trade-off for Private Equity firms pretensions. According to the European Comission (2013), the target market for mezzanine financing are top-notch SMEs due to strict criteria that has to be fulfilled to be granted with mezzanine: solid track record, stable cash-flows and experienced management team. Due to its nature of being used as an alternative to senior debt, Amon and Dorfleitner (2013) claim that mezzanine financing increases during times of financial crisis, which makes it specially important in a year that is marked by an economic and pandemic crisis.

Svedik and Tetrevova (2014) identify 6 types of mezzanine debt divided among Loans and Bonds. On one hand, a loan is an operation between two parties, ruled by a contract where the company will borrow the money and pay for interest. In opposition, bonds are a debt instrument that is issued by the company to fund itself and sold publicly in the financial markets (BBVA, 2018).

- **Loans**
  - **Subordinated Loans** that have the exact same conditions as a regular loan with the exception they are junior to senior debt in case the company enters in a default situation (Yoo et al., 2018);

  - **Participating Loans** that are subordinated to the claims of all senior creditors in case of bankruptcy but have the upside incentive of having the remuneration of the loan indexed to the profit of the borrower (van Gelder)

- **Bonds**

  - **Subordinated Bonds** that are the analogous to subordinated loans. John et al. (2005) confirms that subordinated bonds have higher yields when compared to senior ones within companies with the same leverage rating.
  - **Participating Bonds**, as claimed by Johnson (2004), bonds with a additional variable interest according certain levels of the company's performance;
  - **Convertible Bonds** that, besides the characteristics of a regular bond, have a conversion option to transform bonds into shares at a already stipulated value. Investors will thus convert the bonds if the stock price is higher than the call option (Stein, 1992);
  - **Bonds with Warrants** also entail the possibility for the investor to convert shares at a pre-agreed price (strike price). However, the main difference to convertible bonds, is that this instrument separates the bond with the option to convert shares (warrants), meaning that, upon a conversion event, the company still has to remunerate the debt to the investor (Rahim et al., 2014).

The authors also identify other types of mezzanine financing mechanisms that, due to their nature, should be considered more as a mezzanine equity instrument:

- **Silent Partnerships**, where investors hold shares of the company but are not liable towards the company's creditors (Comission, 2013). The designation "silent" comes from the fact that investors are not evolved in the daily management.

- **Preferred Shares** seem a debt-like instrument in the sense that it also provide pre-agreed fixed returns. However, this investor's returns come in as dividends, therefore not being tax-deductible by companies. On the other hand, as they are a type of financing that is seen as equity, companies have incentives to issue this type of shares to escape regulatory constraints (Ravid et al., 2007). For investors it is also an attractive mechanism and their dividend is senior to common shares' dividends (Paddock et al., 1980).

For this type of financing instruments, PE firms expect returns between 15% and 25% Internal Rate of Return compared to the 25% to 50% interval of pure equity investments (Silbernagel, 1999).

Chapter 3

The Investment Opportunity

This chapter, presents the current situation of the target company as well of its future prospects according to the management business plan.

By analysing this information, the goal is to understand its activity and business model. Also, it is important to focus on operational and financial highlights such as leveraging ratios or operational efficiency.

This analysis is carried every time an investment opportunity arrives at Oxy Capital and the majority of the companies do not even pass through this stage.

CondES is a Spanish residential property management company located in Madrid. Having initiated its activity in 2017, CondES has been following an inorganic growth strategy since day one - bought a large, recognised player in Madrid with 60 years of experience to start the business - and has been buying several companies or portfolios as add-ons to its operation.

By March 2020, CondES was already a top 3 player in Madrid in a highly fragmentated market - a market share below 2% of the city's buildings -, having a portfolio of 1.957 HOAs distributed between 15 offices with 104 workers.

In order to keep up with the acquisitions' strategy and to expand, for the first time, outside Madrid, CondES identified a recognized player in the Mediterraneo area that would be an excellent fit for CondES' pretensions, since it could work as a platform for further development in the region (same *modus operandi* as the one used in Madrid). To accomplish this buyout of c. €1,8 million, CondES started talks with several banks to guarantee financing at the beginning of the year. However, with Covid-19 pandemic situation spreading all over the world and reaching Spain by the end of January, banks soon focused their efforts on Covid-19 credit lines, which resulted in the impossibility of financing CondES.

Amidst this situation, CondES' CEO, whose desire was to continue buying competitors despite Covid-19, started working on alternative strategies to achieve his goals. With this being said, Oxy Capital was contacted in the middle of March - the beginning of quarantine in Portugal - by CondES, which was seeking a €5 million financing amount through a mezzanine debt instrument.

3.1 CondES' Business Model

Once both companies initiated talks to search understanding for an agreement that (i) could help CondES with its acquisitions and (ii) would provide Oxy Capital the possibility to achieve its targeted returns with the investment, the management team presented CondES' business model.

Regarding revenues, the operation includes three revenue streams:

HOA recurring fees

This fee is for providing HOAs a standard service of administration - this should include services like managing bank accounts, accounting, yearly budget drafting or collecting homeowners' debts. For this, CondES charges each condominium an average monthly amount of c. 5€/unit, being the term "unit" the equivalent to a home or to 5 stores or garages, as the latter are estimated to represent solely 20% of the workload when compared with homes. This line of income is highly stable and 100% recurring as revenues from a certain month will be equal to the previous and upcoming ones if we disregard organic growth, churn (the latter two to be demonstrated in Chapter 4) and occasional pricing updates to follow inflation and Consumer Price Index. Taking organic growth and churn figures into account, the scenario looks encouraging as well, as historical churn figures (measured by lost revenues, in Euros) of the company are c. 3,5% and outperformed by the organic growth (c. 7,3% organic growth March 2020 LTM). Moreover, non-paying Homeowners are not an issue as well: CondES' management fee represents, on average, only c. 5% of the total HOA budget and they are always the first provider being paid in the first days of the month, as they are the ones who manage the HOA's bank account. This means that it is highly unlikely that HOAs enter in a default situation where CondES wouldn't get paid.

Provider agreements

As CondES started to build a bigger client base, their portfolio gained increasing importance to many suppliers in areas such as energy, communications or construction and repairs. To many of them, CondES' portfolio even became their biggest client, allowing CondES to gain a favourable negotiation position with many suppliers and take advantages of economies of scale. In addition, CondES' accounts managers are the ones who suggest new service providers to their HOAs (c. 60% out of HOAs OPEX is addressable by CondES) meaning that providers are willing to lower their margins to pay a marketplace fee and partner up with CondES in order to get direct access to its clients. Bearing that in mind, CondES increased its bargaining power among providers and started charging a 5% commission based on their revenues.

Other Operating Income

This line of income has little weight in total sales when compared with the previous two. It includes all the services that are not contractually included in the standard administration service hired by the HOAs, being examples of that every extraordinary HOA meetings, managing the payroll of HOA employees or tax fillings for some HOAs that are obliged by law to present them.

Regarding costs, CondES' structure doesn't comprise any Cost of Goods Sold (COGS) as there is not any product being traded, but a service being provided. Thus, the majority of costs are

Personnel Costs, namely:

Network Personnel

Includes all the account managers that are the ultimate responsible for each HOA - they end up being the core of the business as HOA management is a lot about personal engagement and clients are heavily relying on them. Each account manager is in charge for, in average, c. 90 HOAs corresponding to 3.000 units (c. €180k in sales). To help them in their job, CondES also hires assistants that work closely with the account managers and accountants - the latter don't work directly with clients as CondES already centralized accounting to achieve cost synergies.

Corporate Personnel

This line contains the costs with the top management team excluding the CEO (COO, CHRO, CXO and CFO) as well as the people who report directly to them before network personnel.

The remaining operational costs are SG&A expense, in particular Office Network Expense - mostly rental and some office supplies - and Corporate Expense - software subscriptions or commercial expenses.

In Figure 3.1 it is possible to observe what is the weight of each item of the income statement to the final calculation of both adjusted and reported EBITDA.

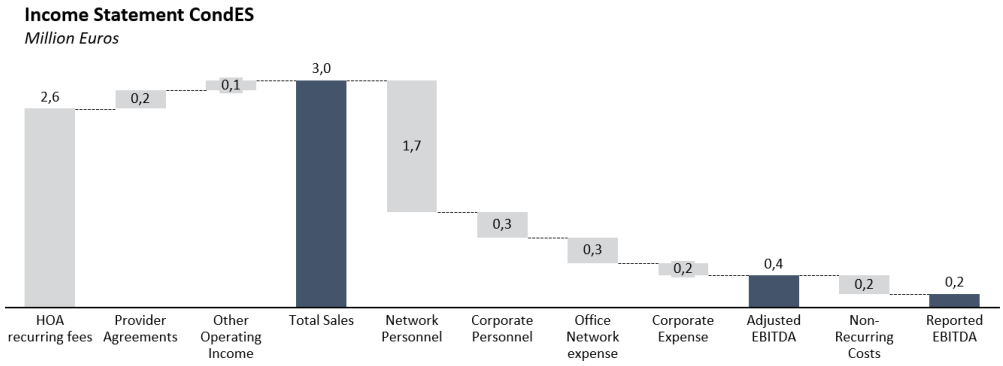

Figure 3.1: CondES Income Statement 2019

3.2 EBITDA Assessment

As seen in the literature review, the correct assessment of a business EBITDA is of elementary importance to the valuation of the company. Thus, EBITDA, which is supposed to be the best proxy for a company's operation, needs to be adjusted in order to purge all the non-recurring costs.

With this being said, CondES incurs in 3 other line of costs that are considered in the reported financials CondES presents every year, but shouldn't be taken into account in our valuation:

- **Management fee:** used to pay the CEO's honorariums but should be disregarded as his services will be no longer needed - in his own words - in a scenario where CondES stops growing because the rest of the management team could handle the business as a going concern.

- **Growth-linked incentives:** yearly bonuses given to every worker to compensate them for the extra workload that acquisitions require, instead of hiring temporary employees. Once again, in a zero growth scenario these will stop existing.

- **Other non-recurring growth costs:** comprised of transaction costs as intermediation fees that will also disappear once acquisitions stop.

Besides the aforementioned adjustments, our valuation of the company should also be based on run-rate figures, i.e, taking last month financial figures numbers and annualize them by multiplying them by twelve months. This is our best proxy because (i) this is a highly recurring business and (ii) CondES is following an aggressive inorganic growth strategy. For instance, if CondES buys a competitor in December 2020 with the same EBITDA as CondES itself, the 2020 reported EBITDA wouldn't capture that growth, as the increase in EBITDA would only be noticeable in a single month - December 2020 -, thus having small impact in yearly figures. On the other hand, using run-rate figures the EBITDA would, in fact, double.

3.3 Cross selling opportunities: ObrES' rationale

By managing directly many HOAs and having to identify providers to serve their needs, CondES soon realized that many repairs and constructions that HOAs hired from providers could be done partially internally. Hence, in 2019 HoldES founded ObrES to address those opportunities thus enabling cross-selling and providing its clients a broader range of services.

In terms of business model, due to the cyclical nature of construction, maintenance and repairs - usually follows economical situation, in opposition with HOA management - ObrES outsources around 33% of its work, as a de-risking strategy. Consequently, there are two revenue streams, namely, (i) sales from ObrES internally provided works and (ii) sales from works that were outsourced.

Regarding costs, the COGS item includes materials and construction employees salaries in the works fully managed by ObrES, whereas in outsourced works it's only the cost of the third party. This leads to an implied gross margin of 31% and 25%, respectively. Other costs comprise corporate personnel - mainly architects and administrative personnel - and SG&A - vehicle renting for instance. Finally, CondES charges ObrES a 5% marketplace commission as any other provider that has an agreement with them.

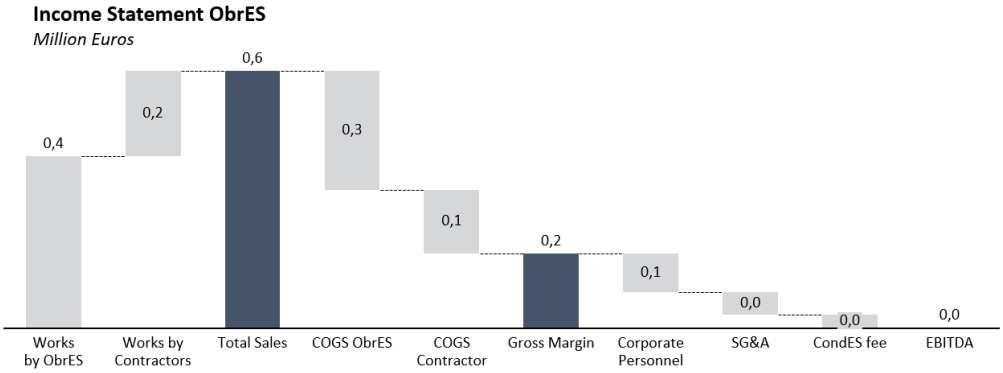

Figure 3.2: ObrES Income Statement 2019

3.4 Financial Situation

Another indicator that, while PE firm, we also account for is the financial leverage of the target company. To calculate it, the most common metric is Net Debt in function of EBITDA. Considering EBITDA the best proxy for the generation of cash by the company's operation, this indicator estimates how many years will the company be paying its outstanding debt.

As seen in the literature review, Net Debt is calculated by the total debt minus cash or cash equivalents. Bearing that in mind, it is necessary to check the company's balance sheet (Figure A.1) and see what items have to necessarily be included. Figure 3.3 demonstrates the calculations of the company's net debt of 2019.

Net Debt Calculation	
Short-Term Financing	400.000
Long-Term Financing	985.500
Total Debt	**1.385.500**
Cash	524.244
Financial Investments	200.000
Client Advances	(432.299)
Cash or Cash Equivalents	**291.945**
Net Debt	**1.093.555**
(÷) EBITDA	701.383
Net Debt/EBITDA	**1,6x**

Figure 3.3: Financial Leverage

The company totals c. €1,4 million in bank financing. On the other hand, it has c. €0,5 million in cash, which would end up in a net debt value of €0,9 million. However, further adjustments have to be made. The company made a financial investment of €0,2 million and financial investments are considered to be almost liquid assets, thus being considered a cash equivalent.

Moreover, due to its rental management activity, the company holds c. €0,4 million of its clients money.

With this being said and taking the company's EBITDA into account, calculations point to a 1,6x Net Debt/EBITDA multiple, which is not considered to be an over-leveraging situation.

Nevertheless, just by borrowing an additional €1 million for its expansion strategy, CondES would reach 3,0x Net Debt/EBITDA, which is usually considered the threshold for over-leveraging. Considering the financing amount of €5 million, the company reaches 8,7x Net Debt/EBITDA.

This level of indebtedness increases the risk of financing the operation thus requiring better potential returns for its investor.

3.5 Management Business Plan

CondES' CEO is seeking this financing amount in order to keep up the pace in the current acquisition strategy.

With this, CondES pretends to more than triple the number of HOAs under management in the next 3 years, thus increasing HOA management fees and fostering cross-selling opportunities (either for provider agreements in CondES, for ObrES construction works or even for new upcoming Business Units), achieving a run-rate turnover of €23,3 million in 2023, as seen in figure 3.4.

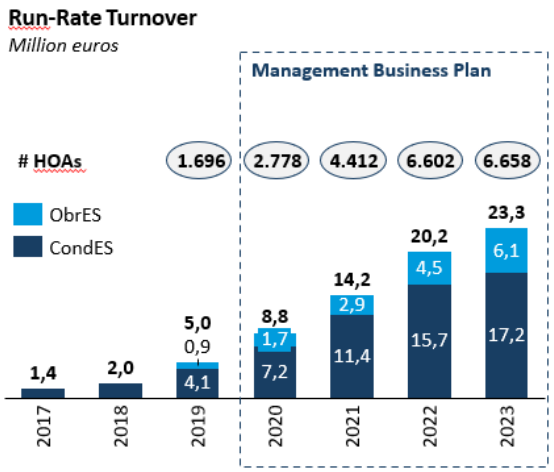

Figure 3.4: HoldES Run-Rate Turnover 2017-2023

As expansion continues, CondES' focus will not be only to grow, but also to achieve cost synergies, thus confirming the advantages of a buy-and-build strategy in the residential property management sector. In the short-term, CondES will achieve better margins by centralizing back-office services or digitalizing many administrative procedures. In the long run, CondES will be able to redesign its office network to minimize, for instance, transportation costs.

With all aforementioned synergies, HoldES' plan is to achieve a 25% EBITDA margin by 2023, as shown in Figure 3.5.

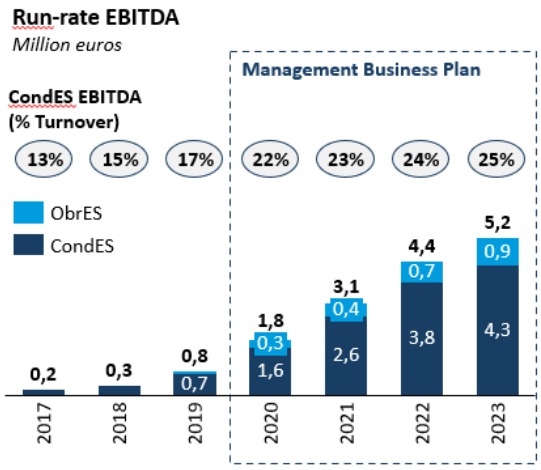

Figure 3.5: HoldES Run-Rate EBITDA 2017-2023

To reach the financial figures mentioned above, the company intends to spend €14,2 million until 2023 in portfolios' acquisitions. Since its foundation, CondES spent €4,6 million in the last 3 years. Other CapEx comprises mainly maintenance expenditures (software and hardware, for instance) and expansion expenditures (extra costs in acquisitions, such as branding and image expenditures).

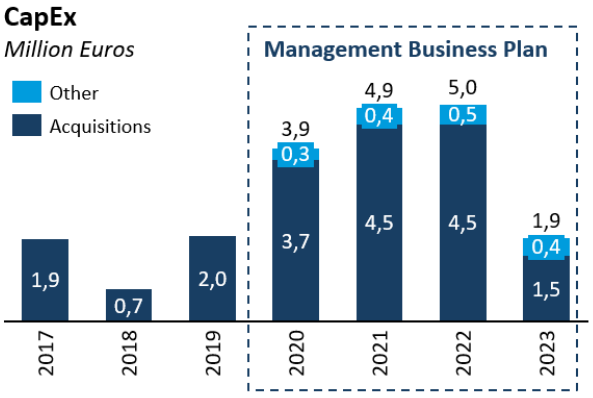

Figure 3.6: CapEx 2017-2023

Chapter 4

Market & Company Due Diligence

Every time Oxy Capital comes across with a promising investment opportunity - and, specially in this business case, the company is interested in entering in a completely unknown market - it is necessary to make all proper due diligences to guarantee that the most informed judgement is being made when the time to move forward or drop the deal comes.

The rationale behind this chapter is to expose all the key findings made in the commercial due diligence that was carried through a deep dive in the residential property management market. With this, is was possible to gain awareness regarding the competitive landscape, customers trends, as well as analyse key points of the company's historical performance. By gathering and analysing as much information as possible, it is expected that one may corroborate - or not - the viability of the management business plan and understand what are its main advantages and risks.

Parallel to the commercial due diligence, Oxy Capital also carried financial, tax and legal due diligences, having hired a renowned consultancy firm and a major worldwide law firm in order to identify which major fiscal and legal contingencies could arise in the future if the deal proceeds. All the findings coming from those reports will not be subject of analysis in this thesis.

4.1 Market Sizing

To further understand the market and the company's growth potential, a very common analysis that it's usually done is to estimate the size of the market in question and what is the company's current positioning. In this particular transaction however, this analysis becomes uncommonly important as the viability of the business plan requires the existence of enough space in the market for CondES to expand.

By analyzing the latest Spanish *Censos* study, it is possible to gain awareness regarding the Spanish Housing Stock, namely the number of existing HOAs in the country, i.e., CondES' potential client base. In figure 4.1 it is possible to see those numbers divided by region, thus allowing us to better comprehend the potential future expansion of CondES either in Madrid as well as in other regions of Spain.

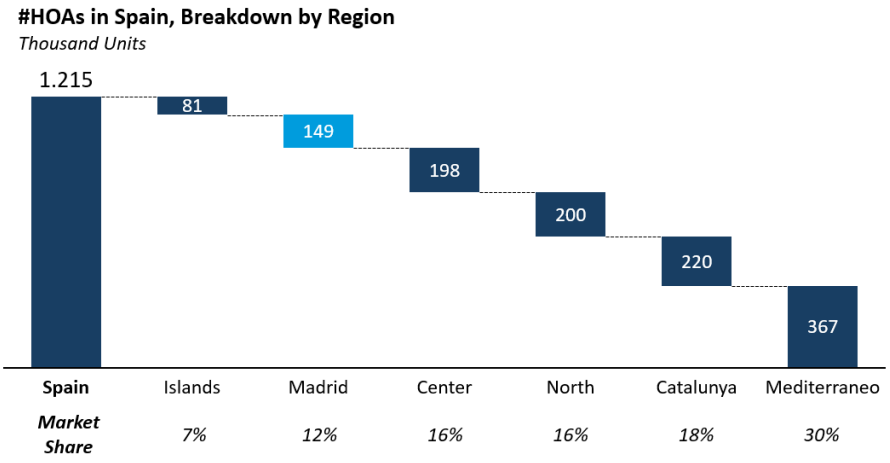

Figure 4.1: Number of HOAs by Region

Taking again into account that CondES had, by March 2020, 1.957 HOAs in Madrid, making it a top player in the region, and Madrid has c. 149.000 HOAs, the conclusion that arises is that there is still plenty of room to grow in the capital city. On top of that, even in a scenario where Madrid would be entering in a situation of market saturation, and despite being the biggest city in Spain, Madrid only comprises 12% of the total HOAs in Spain, giving support to the management business plan that assumes that there is enough space in the Spanish market to continue increasing CondES' market share by acquiring portfolios of HOAs.

Interviews with the top management team brought another encouraging fact about CondES: they have been striving in Madrid, which happens to be the Spanish city where the residential property management market is most fierce and competitive. This is partially explained by the fact that Madrid inhabitants are typically more demanding as a result of being a city where a high percentage of the housing stock is intended for first habitation, thus being owner-occupied. As a consequence of that, homeowners like to be in full control of what happens in their HOAs, demanding high quality service and transparency in the HOA's operations. Other fact that supports the allegation of high competition in the city is that Madrid has c. 3,5k HOA administrators out of c. 15k in Spain, a 23% market share, despite only having 12% of the HOAs, turning the city into a place where supply clearly surpasses demand (when compared with the rest of Spain), thus transferring bargaining power to consumers that may request more from their providers.

In contrast, Mediterraneo region, where CondES will be partially using the financing amount to buy a platform to foster future expansion, is the biggest Spanish region with regard to number of HOAs. In addition, the typical HOA in the region is usually a resort with plenty of vacation houses, meaning its owners won't spend the same time there as in a first habitation (many of them are not even Spanish) and some just own these houses as a financial investment, therefore not being so demanding with daily HOA's needs and services provided. This opens an opportunity for CondES to more easily propose ObrES or partner providers to tackle these HOAs necessities.

4.2 Competitive Landscape

After analyzing the big picture in the residential property market, it is time to take a closer look at the best Spanish competitors to evaluate what is CondES' current position among its peers.

Firstly, it is important to check on the financial status of CondES' main competitors and understand their profitability and financial leverage.

By analyzing Figure 4.2, which combines the latest available financial data Oxy Capital had access, i.e., CondES financial data from 2019 and competitors financials from 2018 (gathered from Orbis, an European financial database), some facts are noteworthy:

- CondES is a player with relevant profitability, only surpassed by Competitor C, whose EBITDA margin is remarkable and even above CondES' prospects for 2023, giving support to the management business plan that such high EBITDA margins are not impossible to reach in this sector.

- Competitor A, which is considered by CondES' CEO the best peer, has a turnover more than 50% higher than CondES, being the top player in Spain, but mainly in the Mediterraneo area. Nevertheless the company hasn't been growing much in recent years - Compounded Annual Growth Rate (CAGR) of 2%.

- Competitor C is the company with worst margins mainly due to high labour costs per worker. This happens because Competitor C is a corporative company, meaning it is an association of employees that control the company, thus incurring in higher personnel costs - they pay themselves better than they would be paid elsewhere.

- Competitor D is the boldest competitor of CondES as they had been following an aggressive growth strategy by acquisition as well, even to the point of outbidding many offers made by CondES in the past and cutting many jobs from the target companies once the deal is completed in order to create cost synergies. Luckily for CondES, this strategy does not please people who are selling their lifelong businesses, so CondES usually can win a bid despite presenting a lower offer than Competitor D. Competitor D's EBITDA shows up with negative value but this is probably just a consequence of their buy and build strategy combined with the fact we don't have adjusted financial figures for their company.

- Most important and remarkable of all, residential property management market generates a lot of cash as we can infer from the Net Debt in function of EBITDA column. Almost every competitor presents Net Cash (negative value of Net Debt). CondES and Competitor D (net debt of €308k) are the only ones that present some level of indebtedness as a consequence of their acquisition strategy combined with its short existence, not having yet given enough time for considerable cash generation that would outperform their investment needs.

Comparable Spanish HOA Management Firms, 2018-2019
Thousand euros

Company	Sales	CAGR last 2 years	EBITDA	EBITDA Margin	Net Debt x EBITDA	# Workers	Sales / Worker	Labour c. / Worker	Region
A	6.552	2%	978	15%	-0,4x	151	43	30	Madrid, Levante y Costa del Sol
B	4.864	(5%)	183	4%	-20,0x	49	99	87	Madrid
CondES	4.083	74%	701	17%	1,2x	93	44	29	Madrid
C	3.956	16%	1.045	26%	-2,8x	n.a.	n.a	n.a.	Madrid
D	3.081	72%	(77)	(3%)	n.a	68	45	26	Madrid, Málaga, Murcia, Alicante
E	2.258	6%	300	13%	-8,2x	33	68	34	Barcelona

Figure 4.2: Financials of Main Competitors

Regarding customer trends - and recalling the fact that this is a market where people are demanding and want fast resolution of its HOA's needs - Figure 4.3 confirms that CondES is well positioned among its peers, offering a full set of services in the Real Estate market (insurance brokerage is a segment that CondES plans to be in the upcoming years, increasing its cross-selling opportunities). However, CondES' most distinguishable advantage over its competitors is its very strong customer service and customer interface, being the only company alongside Mediterraneo that provides a smartphone App where customers can talk with their HOA administrator or even see the HOA bank account and movements history, thus increasing the transparency in the HOA management, another appreciated feature in the business.

Comparable Spanish HOA Management Firms
Services offered

Company	HOA Mgmt.	Rental Mgmt.	Real Estate Brokerage	Insurance Brokerage	APP	Customer Serv. 24/7	Client Area in Website
A	✓	✓	✓	✗	✓	✓	✓
B	✓	✓	✓	✓	✗	✗	✓
CondES	✓	✓	✓	✗	✓	✓	✓
C	✓	✓	✓	✗	✗	✗	✓
D	✓	✓	✓	✓	✗	✓	✓
E	✓	✓	✓	✓	✗	✓	✓

Figure 4.3: Services offered by Main Competitors

Regarding prices, in such a competitive environment, all major players here presented - as well as other Spanish players with relevant dimension that were studied mainly through website visits - have prices in line with one another (around 5€/unit/month for the standard administration service, disregarding any other extra works that may be provided under a cross-selling rationale).

To sum up, CondES is making a statement in the Spanish residential property management market by following an aggressive strategy of buying several portfolios, having reached the top 6 in just 3 years of existence. At the same time, the company managed to develop a differentiated service to interact with its clients, creating competitive advantage over its peers without charging more for that.

4.3 CondES' Historical Acquisitions

One of the assumptions that was presented to Oxy Capital was the possibility of buying competitors at a 6x EV/EBITDA valuation. With that in mind, an analysis to CondES' former acquisitions was carried out. This is not an usual step in a regular Due Diligence for two reasons: (i) not always a target company that Oxy Capital may be analyzing took over any other company in the sector in the past and (ii) even if that happened, the ultimate goal of that buyout was probably not multiple arbitrage but rather the integration of both companies for operational or commercial purposes. With this being said, this analysis gains increasingly importance when it's a buy-and-build strategy that it's under evaluation.

In Figure 4.4, it is possible to observe the invested capital in the 23 historical acquisitions made by the company - which include the initial platform plus 22 further add-ons to the operation in Madrid - reaching a total amount of €5,4 million.

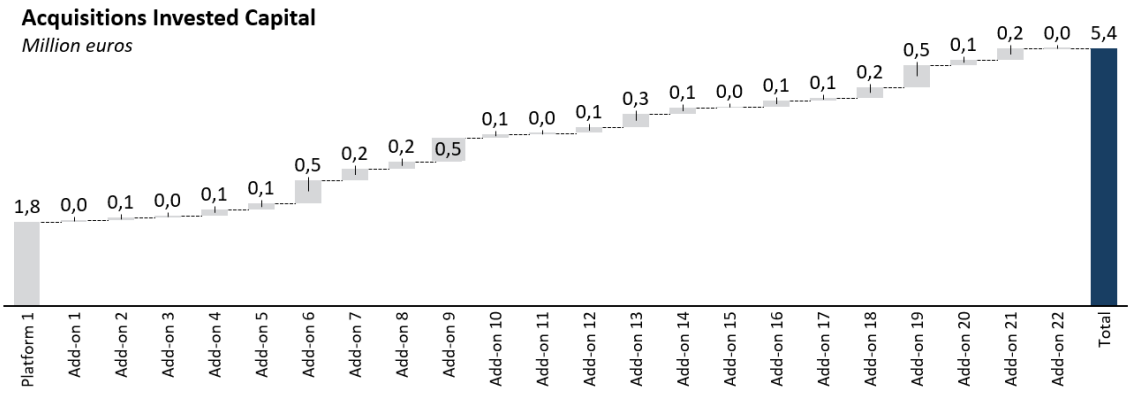

Figure 4.4: Historical Invested Capital in Madrid

In Figure 4.5, it is shown the EBITDA bridge with several adjustments to determine what was the acquired EBITDA in the past by the company. By April 2020, CondES had an EBITDA run-rate of €734k, which dividing to the aforementioned invested capital leads to an implied valuation of 7,4x EV/EBITDA, slightly above what was expected.

However, further scrutiny brought promising insights: Platform 1, whose acquisition price reached to €1,8 million, had an EBITDA of c. €180k meaning it was carried at an implied valuation of 9,7x EBITDA - a premium valuation as a consequence of buying a top player in Madrid. Excluding Platform 1, invested capital is down to €3,7 million for an EBITDA of c. €554k (adjustment #1), leading to a valuation of 6,6x EBITDA.

On top of that, the EBITDA CondES presents today has to be adjusted to be comparable with the one bought in acquisitions. On one hand, as one can see in adjustment #2, CondES has structure costs, namely corporate personnel expenses of €430k, that don't come with portfolios. This means that acquired EBITDA would reach €983k. On the other hand, we also have to take into consideration that, at the time CondES made the acquisitions, the portfolios didn't include any provider agreements (with the exception of Platform 1 that already had this type of revenue stream). Therefore, knowing CondES had by April 2020 €332k in Provider Agreements from which only €140k came from Platform 1, there are €192k that should be disregarded in the calculus of the acquired EBITDA - adjustment #3

Bearing that in mind, the EBITDA that came from the buy and build strategy is €792k and was acquired by investing €3,7 million, entailing an implied valuation of 4,6x EV/EBITDA - even below the target valuation that was firstly presented -, thus confirming the management information regarding average market valuations.

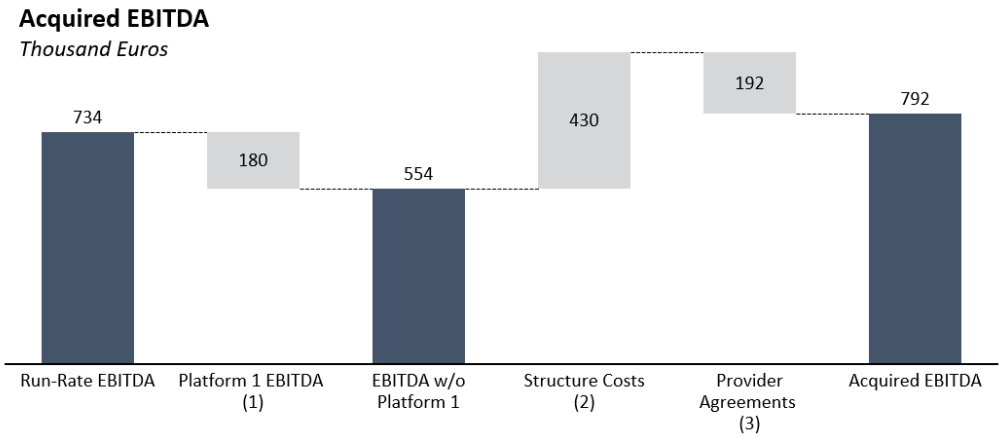

Figure 4.5: Bridge From Run-Rate EBITDA to Acquired EBITDA

It's noteworthy to refer that, while guaranteeing its financing amount, CondES still continued in talks with possible future competitors to acquire. According to the management team, all these negotiations were being held inside the range of valuations presented to us.

4.4 Project Mediterraneo/Platform 2

To fully analyze all acquisitions performed by CondES, it's relevant to verify not only historical buyouts, but also Platform 2, where Oxy's hypothetical financing will be put into use. After 3 years of consolidation in Madrid, Platform 2 - a big, renowned player in the region - represents the opportunity for CondES to expand to the Mediterraneo area.

In Figure 4.6 it is possible to take a look on Platform 2' adjusted Income Statement - i.e, already including corporate costs for a Regional Director. The company has €1,3 million in sales combined with an EBITDA margin of 34,4% - substantially higher than the operational efficiency CondES currently has. Considering CondES' April run-rate financials, the acquisition of Platform 2 will represent an increase of 28% in topline (€4,4 million to €5,7 million) and a 59% growth in EBITDA (€0,7 million to €1,2 million).

Regarding the value of the transaction , the deal is agreed to close upon a price of €1,8 million, meaning it will be carried at a valuation of 4,2x EV/EBITDA, lowering CondES' average multiple previously calculated from 4,6x to 4,5x EV/EBITDA.

With this being said, the structure of the deal looks promising: big portfolio with interesting profitability combined with a valuation that is being done at a considerably low multiple, specially taking into account that CondES would be willing to pay more for a company that will work as a gateway to the region and that Competitor D has made an offer of 5,1x EV/EBITDA months earlier.

Income Statement

Thousand euros

Recurring Fees	1.059
Provider Agreements	114
Other Revenues	80
Total Sales	**1.254**
Personnel	(676)
SG&A	(146)
EBITDA	**431**
EBITDA Margin	*34,4%*

Figure 4.6: Platform 2' Financials

However, regarding Platform 2' portfolio, the scenario is not as encouraging as the financial analysis was. Unlike the majority of the acquisitions CondES has made in the past, Platform 2 has a highly concentrated portfolio, managing 3 large resorts in the region that represent c. 80% of revenues according to management information, which increases the risk of the investment as the assumption of business revenues' recurrence may be questioned.

To address this threat, CondES negotiated some extra protections in the structure of the deal, namely the existence of an earnout, meaning the cost of the transaction will not be fully paid upfront, but rather only part of it, with the remaining value being deferred and indexed to the future performance of the company. This agreement, aligned with a shareholder transition period of 2 years and the fact that one of the selling partners will join CondES as Regional Director, gives high incentives to the counterpart to maintain, and even grow, the portfolio during this period and brings CondES downside protection, as the price will decrease in a scenario where EBITDA decreases as well. Another mitigant is that, in opposition to regular HOA contracts, Platform 2 has negotiated contracts with the resorts, whose average durations are from 4 to 5 years, giving CondES some confidence in the short-term, at least until new acquisitions in the region are made in order to reduce exposure to client concentration.

4.5 Public and Private Comparables

Another assumption that lacked confirmation was the possibility of developing an operation that would be potentially valued above 10x EV/EBITDA, key condition to guarantee a multiple arbitrage, i.e., the creation of value even in a scenario where no operational improvements or growth occur, just by increasing the multiple at which the company is sold compared with the one at it was bought.

To verify this premise, a search through the international residential property management market was carried, despite the fact there are not many players with a similar business model and strategy as the one CondES has.

Firstly, amongst the publicly traded companies, there is one large HOA management company from Canada that has operations in the United States and Canada itself - First Service Corporation (listed as FSV in the NASDAQ Stock Market and in the Toronto Stock Exchange). FSV is market leader in the US market with 6% of market share (calculated in number of residential units) with c. 350.000 HOAs under its management and 24.000 employees as of July 2020. As HoldES, FSV has 2 operational branches, one - First Service Residential - whose core business is HOA management and the other - First Service Brands - that provides ancillary services as construction & repairs (such as ObrES). In 2019, the company presented a total turnover of $2,4 billion - from which 59% came from the HOA management branch and 41% from cross selling - and an EBITDA of $235 million (c. 9,8% EBITDA margin) - 52% and 48% respectively -, giving evidence to the potential of the ancillary services market in the residential property management business.

Regarding the valuation of the company, in Figure 4.7, an analysis to the 1st semester of 2020 evolution was carried. By December 31st 2019, FSV's stock closed at $93,29, which multiplied by the number of outstanding shares at the end of 2019 - 38.662.000 - entails a market capitalization of $3.597 million. To calculate the Enterprise Value, it's necessary to sum to Net Debt of 2019. Finally, by dividing the Enterprise Value for the adjusted EBITDA of 2019 it is possible to discover the implied valuation at which FSV' stock was being traded - 19,2x EV/EBITDA.

NASDAQ: FSV	*31/12/2019*	*31/03/2020*	*31/06/2020*
Stock Price ($)	93,04	73,36	100,75
(x) Outstanding Shares	41.495.957	41.615.957	43.439.466
Market cap ($M)	3.861	3.053	4.377
(+) Net Debt ($M)	646	330	400
Enterprise Value ($M)	4.506	3.383	4.776
(÷) EBITDA ($M)	235	250	256
EV/EBITDA	**19,2x**	**13,5x**	**18,7x**

Figure 4.7: FSV Stock Valuation

Notwithstanding a considerably high, thus encouraging, valuation at the beginning of 2020, it was important to study the evolution throughout the first semester, especially in such an atypical year as 2020. Preliminary talks with CondES started in early March and, by the end of the month, in the midst of quarantine all over the world, valuation of FSV stock was down to 13,5x EV/EBITDA, which is a considerably lower, but still high, valuation and an unequivocal proof of an impressive confidence by investors. To reach this number, it was necessary the use of the financial figures at end of March 2020 (presented by the company in the 1Q2020 report): Net Debt and EBITDA March LTM 2020, which was calculated as the sum of 1Q2020 EBITDA and EBITDA 2019, minus 1Q2019 EBITDA.

At the end of the second quarter of 2020, in a period where the sanitary crisis had already gone through its worst, FSV stock was already gaining 8% in the year-to-date period, resuming the growth trend that was occurring before Covid-19. In the mean time, EBITDA also grew 2% in such a tough quarter, which shows the high resilience and recurrence of the business in a period of crisis. With this being said, FSV closed the first semester of 2020 at a valuation of 18,7x EV/EBITDA.

Taking these valuations into account, the thesis of multiple arbitrage in a buy-and-build strategy in the HOA management market seems more reliable. However, valuations in the public market are usually higher than those seen in private companies as investors pay a premium for (i) the liquidity of the stock market - they can sell their stocks instantaneously at market prices while private equity deals take several months to be concluded - and (ii) the fact that buying stocks it's a risk-free operation regarding legal and fiscal contingencies that could arise on the target company, whereas in private deals the investor could have a joint responsibility on those issues.

In consideration of the foregoing and in order to obtain a more consistent demonstration of market multiples, the private international market was also studied.

Among the European market, there is also one major residential property management French player - Foncia Group. Foncia was created in France in 1972 to develop a growth by acquisition strategy in the property management market and started since then to expand to other related business - same trend observed in HoldES or First Service. By 2020, Foncia is market leader in France, Germany and Belgium, and player #2 in Switzerland, having presented a turnover of c. €900 million with an EBITDA of c. €200 million in 2019, and offering innovative ancillary

services - Foncia has its own energy brokerage company, buying energy and energy futures to sell it afterwards to their HOAs homeowners.

Regarding the valuation of the company, the most interesting fact is that Foncia has a track-record of being owned by Private Equity companies and there is available data about the transactions. By 2011, Eurazeo - an asset management company -, alongside with Bridgestone - a private equity firm -, bought an 81% stake in Foncia's capital. Records at the time mentioned that the deal was closed upon an Enterprise Value of c. €1.000 million, which divided by Foncia's 2010 EBITDA of c. €90 million (the transaction was done by May 2011 so this EBITDA should be only considered as a proxy as there's no publicly available EBITDA at the time), results in a approximated valuation of 11x EV/EBITDA.

In the meantime, both companies acquired the remaining shares of Foncia (18%) in November 2014 by €185 million, which entails a total equity value of €1.028 million. In this case, to calculate the Enterprise Value and EV/EBITDA of the transaction, financial figures of 2014 were used (considered to be the best proxy as there's only one month between the two events). Bearing that in mind, the deal was closed upon an Enterprise Value of €1.448 million (2014 Net Debt of €420 million) and an implied valuation of 11,6x EV/EBITDA (considering a 2014 EBITDA of €125 million).

Finally, by mid 2016 and after 5 years running the company, Eurazeo and Bridgestone exited Foncia by selling it to another private equity firm - Partners Group. At the time, a press release was issued where Eurazeo disclosed that the deal was done at an Enterprise Value of €1.833 million, which divided by 2015 EBITDA - 132 million - leads to a valuation of 13,9x EV/EBITDA. Moreover, Eurazeo also presented the return of the investment in Foncia which arose to 2,4 money multiple - meaning that for every €1 both companies invested, they received €2,4.

All in all, after studying the international market of CondES' comparables and its past transactions, there is evidence to believe that, if Oxy Capital decides to move forward with this deal, it will be possible to exit the company at a valuation over 10x EV/EBITDA.

4.6 CondES' Performance

After successfully verifying some of the market assumptions in the investment thesis, it was necessary to go at a more micro level and analyse deeply the company, namely whether CondES was a company that fulfilled, or not, its customers requirements as well as if it was capable of attracting new ones.

Service level and client satisfaction are usually measured and studied by companies through customer surveys but, in this case, CondES had only implemented this kind of client approach recently, thus not having a solid track-record of past client satisfaction, making it impossible to study the evolution of the company through that data,

Bearing that in mind, a more detailed approach was followed: Oxy Capital asked for, and was provided with, the data of all HOAs that were ever part of CondES' portfolio and the prices they

were charged per month during that time - this analysis also comprised Platform 1 analogous data in order to extend the time horizon of the analysis as CondES only started in 2017.

The rationale behind this information request was to be able to successfully estimate, on one hand, organic growth - rate of new customers under CondES' management - and, on the other, churn - rate of customers that cease their contract -, on a yearly basis and its evolution. The two aforementioned indicators are specially analysed in service providers that work based on a subscription model, which is the case of HOA management companies, and its analysis is what can support the premise of high recurrence of the business, hence its importance for our analysis. To produce it, two methods can be followed: (i) rates can be calculated in terms of won or lost HOAs or (ii) organic growth and churn are measured in terms of won or lost revenues with those same HOAs. Despite measuring the same concept, both end up being slightly different as HOAs are different in terms of number of homes or services contracted, therefore paying different administration fees to CondES.

In this buy-and-build strategy in the HOA management market, although both indicators are relevant, churn ends up being of ultimate importance for the company's vision.

The market is characterized by customer inertia, making it extremely difficult to considerable enhance its client base organically. On top of that, it is also not possible to increase organic growth by an increment in prices to customers - despite being a top-notch, client-oriented player in the market, HOA standard administration is not a differentiated service in such a way that the company can charge above the market prices. This was one of the premises behind the beginning of this buy-and build approach to the market - by managing to buyout competitors that bring clients attached with them, CondES overcomes the organic growth barrier by expanding inorganically.

Taking that into account, CondES' most important role is to maintain clients satisfied with the company's service level to avoid churn and subsequent lost of revenues to maintain the viability and expected financial returns of the acquisitions. Moreover, in this specific market, a condominium that ceases its contract with CondES today may be one less potential customer in the future, as a bad service experience could make homeowners not even consider CondES in the future to run their HOA.

In Figure 4.8, it is possible to observe the historical churn rates of both companies since 2010. To calculate them, revenues referring to each HOA at December of each year were considered and annualized - as seen before, this is the most accurate method to estimate revenues of the following twelve months for a HOA management company. Having done that, it was then time to see which HOAs left in each year (for instance, if a HOA had a certain amount of revenue in December 2011 and showed a null value by December 2012, that meant it left Platform 1 somewhere that year). Knowing that information on a yearly basis, it was only necessary to see which was the revenue associated to the leaving HOAs in the prior year and divide by the revenues of December of the prior year as well (thus being calculated at constant prices, disregarding any influence that inflation could have). By analysing the presented values, there's not a fully defined pattern - churn is relatively higher in the post crisis period, but there's no evidence that the two events are related -, just a slight improvement in the average churn rate once CondES took over the business.

Even disregarding the aforementioned improvement, churn figures were always below 5%, which shows a consistent service level from Platform 1 and CondES - it is also noteworthy to refer that the presented churn figures are in line with the ones presented by First Service and, therefore, considered to be the standard for a successful company in the sector (it is hard to imagine a company with 0% churn in a sector that correlates so much with people's lives, thus being so demanding).

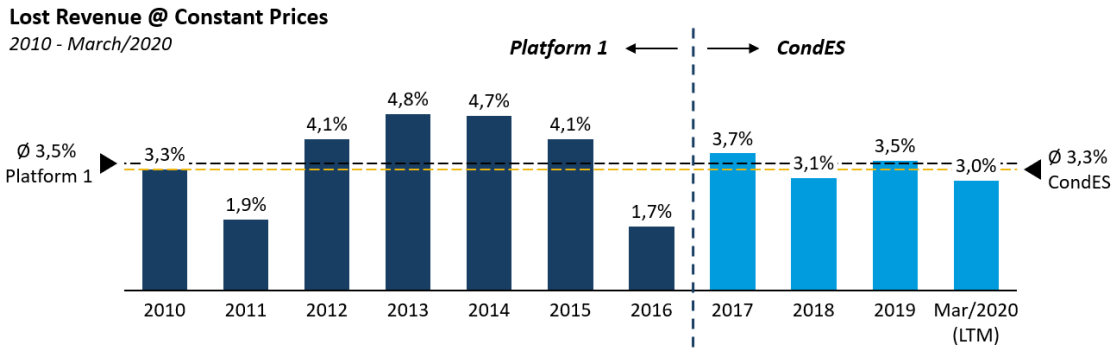

Figure 4.8: Churn Rate Historical Figures

Regarding that matter, when questioned about the main causes for CondES' churn, the CEO estimated the breakdown of 2019 churn - 3,5% - in four main categories, namely:

- **Acquisitions:** When buying portfolios from other companies, there's always a small part of the recently integrated HOAs that end up churning for not wanting to be managed under the administration of a company they never heard of - even though CondES typically integrates the HOA administrators that work with each portfolio, in order to smooth the transition by reducing as far as possible the differences for the mentioned HOAs. This type of churn was responsible for 1pp.
- **Political:** Spanish HOAs - unlike Portuguese ones that delegate the full responsibility of running the HOA to an external company - have a representative homeowner, denominated as the HOA's President, that is the official administrator of the HOA, being CondES just an advisor to its work. This may seem just a technicality, but the truth is that this gives an extra influence in HOA' meetings to the person who holds this title. Therefore, changes in the HOA's presidency may lead to churn as the newly appointed President may want to change the management company, biasing other homeowners to support that decision in assembly. This type of churn was responsible for another 1pp and it's considered to be inevitable.
- **Service:** as mentioned before, in such a demanding sector, any error comes attached with a high price and, many times, the ultimate price to pay is the consequent churn of the unsatisfied HOA. 1pp of the revenues were lost in 2019 due to service flaws.

- **Price:** is the factor with lower preponderance (0,5pp). For customers, way more important than paying a lower price, is not having to bother with their HOAs problems. This hypothesis was very difficult to believe at first, but later confirmed in meetings with Portuguese top players in the HOA management market - Portuguese market leader even referred its average price was 15% above market standards.

Taking a closer look again on CondES' churn figures and bearing in mind the aforementioned breakdown, is possible to infer that it's more difficult to provide and maintain a high quality service at the same time it is being implemented a growth by acquisition strategy, which further enhances the presented values by the company.

On top of that, our analysis had to also account for the HOAs that CondES gained organically, meaning that they did not come from acquired portfolios.

In Figure 4.9, it is possible to observe the evolution of organic growth in the same time frame as the previous churn analysis. By comparing Platform 1 growth behaviour with its churn profile, it is possible to conclude that the company was losing more clients that the ones they were gaining - 2,8% organic growth against 3,5% churn (yearly average figures).

However, when looking at CondES' numbers, the scenario looks a lot more promising. If in the first two years of CondES' administration, organic growth figures were in line with Platform 1, by 2019 organic growth skyrocketed reaching 8,5% - and 7,3% by March 2020 LTM. What seemed an outlier in our analysis has, in fact, an explanation behind it: by 2019 CondES hired a new Chief Commercial Officer and started investing on digital marketing.

Future growth prospects point to continue investing in this kind of business promotion so that this phenomenon does not end up being a one-off event, but rather causing a structural positive effect in the company's growth outlook.

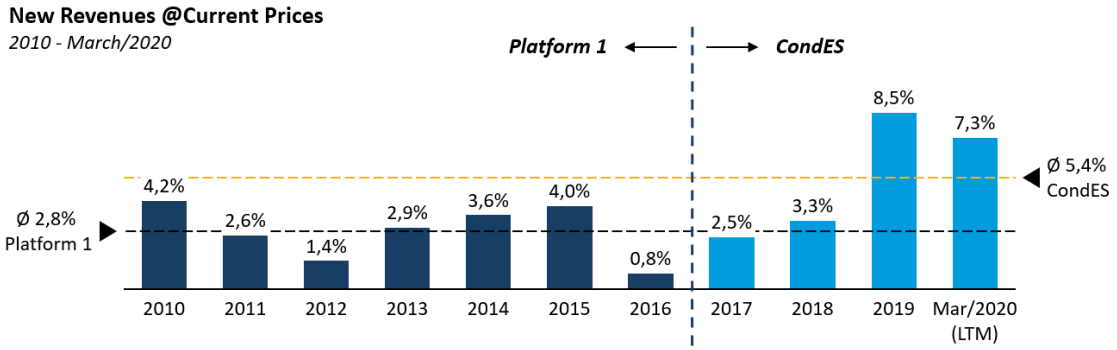

Figure 4.9: Organic Growth Historical Figures

4.7 Covid-19 Impact

Amidst an unprecedented scenario of global pandemic crisis, taking investment decisions is far more risky than the usual. The premise of business recurrence even in crisis situations was presented to us but still lacked confirmation.

Bearing in mind that early talks with the company started in March and the final offer was presented in mid-June, the financial behaviour of both subsidiaries during that period ought to be analysed.

In Figure 4.10, it is possible to confirm the absence of downside impact in CondES' financials during confinement period. Sales grew 0,2% month by month from February to May and EBITDA showed a 1,6% analogous increase.

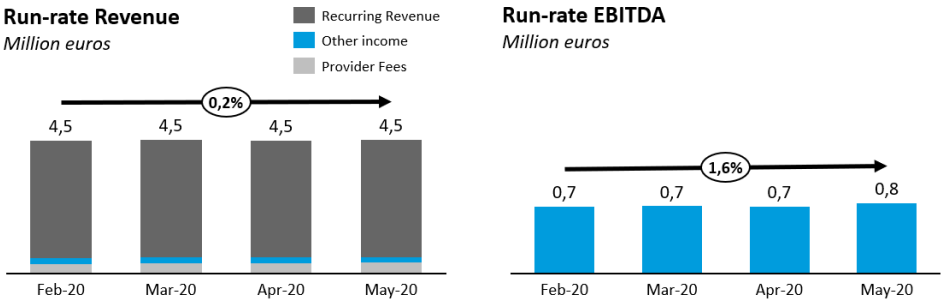

Figure 4.10: CondES Turnover and EBITDA Feb-May 2020

As for ObrES, Covid-19 highly impacted the operations of the company from March to April, where ObrES presented marginally negative EBITDA.

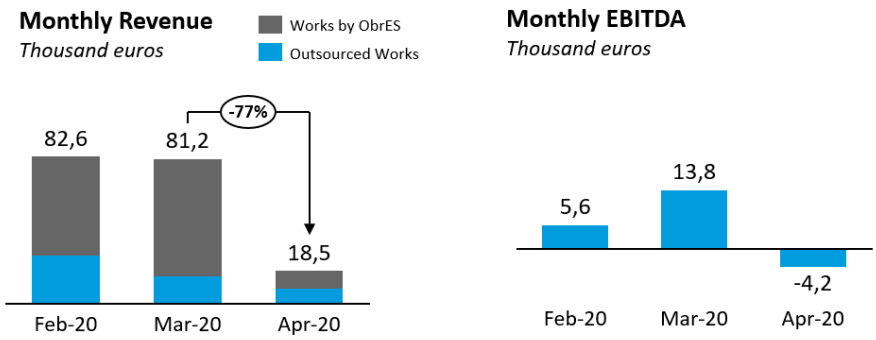

Figure 4.11: ObrES Turnover and EBITDA Feb-Apr 2020

Despite a worst performance of ObrES, CondES' outlook was encouraging and Oxy Capital decided to still continue the transaction.

Chapter 5

Financial Modeling

In this last chapter of analysis, the goal is to present the operational and financial projections - and grounds behind them - for the next 10 years of the company. This period is linked with the Fund's expected lifetime, i.e., as seen in the literature review, PE firms have stipulated periods to (i) invest the Fund's money and (ii) execute their exit plan.

This is the first step at analysing a target company and usually done with a simple, standard investment structure at first, in order to debate among the team as soon as possible - in the PE industry, fastness is of upmost importance. Moreover, PE firms' core business is to meet investors' expectations with regard to targeted returns and the financial model is the tool that enables the analysis of the viability of each investment.

The investment structure presented at the end of this dissertation was the final one, after several interactions and negotiations with the counterpart.

A financial model is a mathematical model that forecasts the company's 3 financial statements - income statement, balance sheet and cash-flow statement - based on a multiplicity of input variables. By generating different outputs according to particular inputs for each variable, PE firms can estimate their potential returns, hence the importance of financial modelling as a decision-making tool (notwithstanding proper due diligences to the company and the market to qualitatively verify the investment case).

5.1 Operational and Financial Highlights

In order to create a financial model that reflects the reality of the business, it is important to promptly identify the main drivers of the company's business model. In this particular case, two companies ought to be considered.

5.1.1 CondES

Regarding CondES and its buy-and-build strategy, the investment case study confirmed the relevance of (i) buying a lot of portfolios and (ii) at the cheapest valuations possible to enhance multiple arbitrage upon an exit event. Figure 5.1 and 5.2 reflect our projections bearing that.

As seen in Chapter 3, Oxy had already been provided with the Management CapEx Plan until 2023. Hence, until that point, Oxy Base Case accompanies that trend with the exception of 2020, where we only considered acquisitions already executed, the buyout of Platform 2 and already shown pipeline. Beyond 2023, the reasoning behind the Management BP was to invest, each year, c. 66% of EBITDA $_{t-1}$, where t is the year in question. Oxy Base Case estimates half of that investment as a conservative projection. It's noteworthy to refer that both scenarios entail a reduction of investment in acquisitions by 2023 that is linked with the investment structure to be covered further on. In a crisis scenario, the estimate for 2020 is to accomplish solely €2,0 million in portfolio acquisitions and CapEx is projected to slightly decrease until 0 by 2023. From that point on, no further acquisitions will be performed in this scenario.

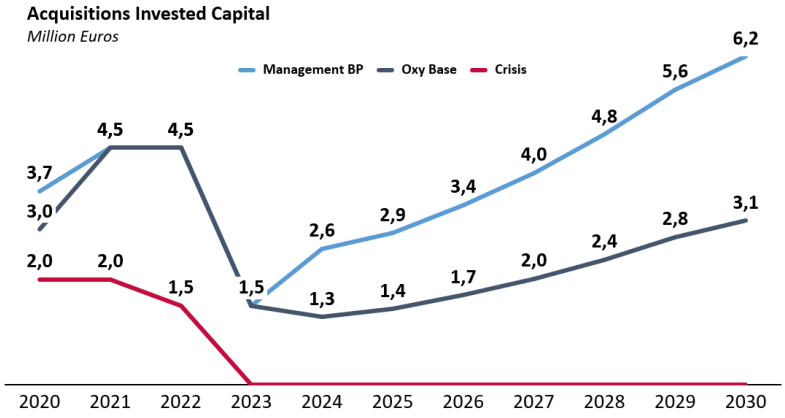

Figure 5.1: Acquisitions CapEx Forecast

As for acquisitions valuations, the management team initially presented us the possibility to buy competitors at 5-6x EV/EBITDA, premise that was carefully analysed and confirmed. Despite that, we have to account for two different kinds of acquisitions: if in the case of Platform 2 and past acquisitions that originated new offices CondES was buying the operation, in a buy-and-build rationale, it is more important to buy portfolios of clients and integrate them in our already established operation. In the first case, it is vital to evaluate at what EV/EBITDA we are buying. In the latter, it is more important to look at another type of valuation - EV/Sales multiple - and the underlying EV/EBITDA multiple is dictated by our EBITDA margin in the period of reference.

Bearing that in mind, Management scenario projected a 1,25x EV/Sales future portfolios' valuation - in line with the 1,0x to 1,5x interval that we also confirmed in our due diligence (in parallel to the EV/EBITDA valuations). In our Base Case, we estimated an increase in portfolio

pricing from 1,25x in 2021 to 1,50x by 2026, as a consequence of 2 factors: (i) CondES is currently targeting the better deals in the market so, as expansion continues, it is expected that the best investment opportunities will be already taken, and (ii) the presence of a big player in the market, with a reputation of buying several portfolios, will probably increase the average valuations in the sector. In the crisis scenario, valuations also arose to 1,50x - this assumption is questionable and ends up being more of a worst case scenario analysis, as one can argue that, in a economic downturn situation, people would be willing to sell their companies at a discount price to satisfy their short-term liquidity needs.

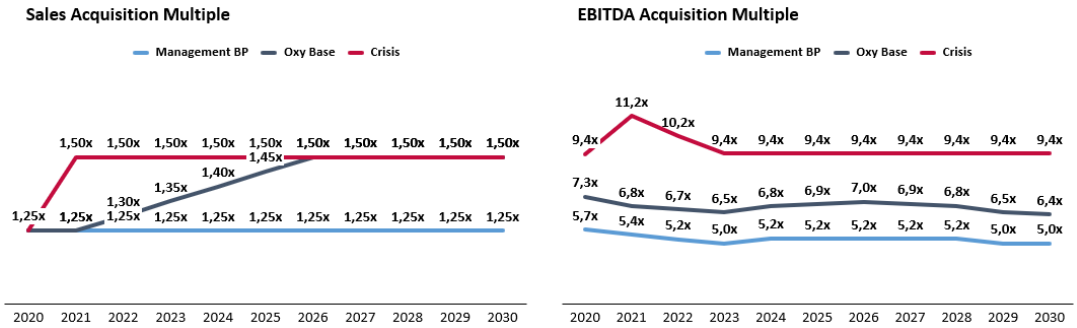

Figure 5.2: Acquisitions Valuation Forecast

However, for each of the described scenarios, it is noticeable that the EV/EBITDA projection doesn't behave like that of EV/Sales. This happens due to the estimated operational efficiencies obtained with the buy-and-build strategy - Figure 5.3. The reasoning behind these margins - and remembering CondES had by 2019 a 17,2% EBITDA margin - are to accomplish all of the presented synergies by the CEO in the management BP, half of them in our Base Case and loss of margins in the next 2 years due to higher labour costs associated with potential layoffs during an economic downturn and slight recovery after that.

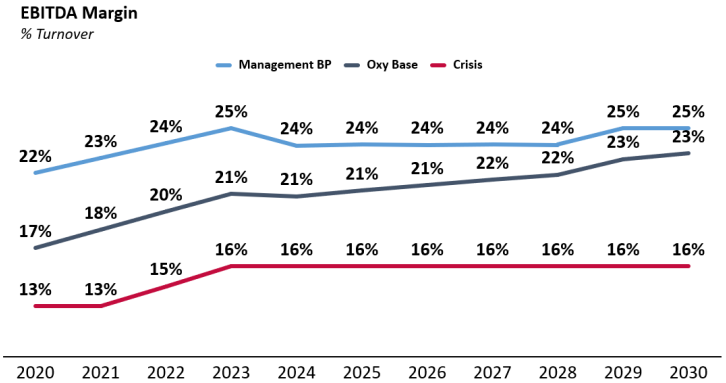

Figure 5.3: CondES EBITDA Margin Forecast

In this investment thesis, we have also analysed the importance of maintaining the clients that come in the portfolios CondES is buying as well as the ability of gaining new customers organically and not by acquisition. With this being said, projections for churn and organic growth were also done - Figure 5.4.

In the Management scenario, projections point to organic growth of 4,5% in the short-term and 8,5% in the long-run. Our projections anticipate no growth at all this year as a conservative projection of Covid-19 impact and 5,5% in the long-run. A crisis scenario was projected to foreseen a zero growth in the next two years and 4,5% in the long-run once the economy rebounds.

As for churn, both management BP and our base case entail a continuation of the churn figures observed in the past. In a stress situation of crisis, we projected an evolution from 7,0% churn in 2020 to 2,5% figures by 2024 - in the crisis scenario, by that year, CondES won't be already performing any acquisitions, hence churn figures can be reduced by 1pp according to the churn breakdown previously presented.

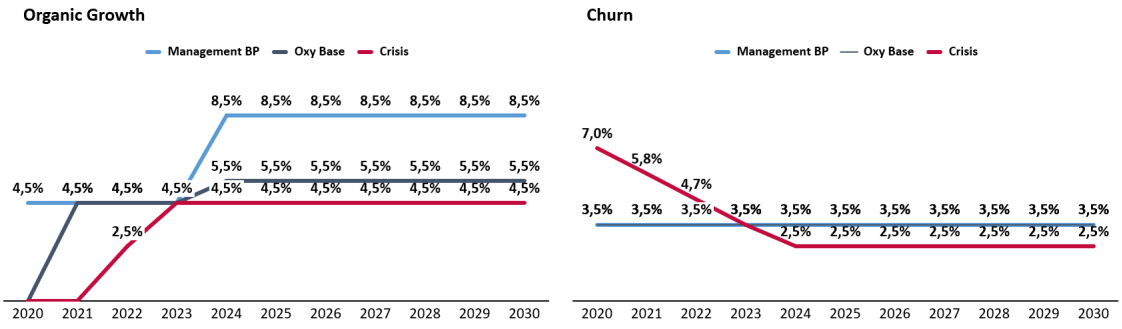

Figure 5.4: CondES Performance Forecast

5.1.2 ObrES

Analysing ObrES, and having its business model in consideration, the two main drivers for its financial performance are (i) the share of the HOA total budget that condominiums allocate for repairs and constructions and (ii) the percentage of those works among CondES' buildings assigned to ObrES. In Figure 5.5, those indicators were projected.

Regarding HOA budget allocation to maintenance works, CondES estimated that its portfolio condominiums spent 3x more in maintenance comparing to the money spent in administration fees. This is an empirical evidence from administrators that deal daily with the portfolio and all the three scenarios estimate that figure in the long-run. However, in Oxy Base we estimated a lower expenditure (2x administration fees) in maintenance due to Covid-19 but increasing linearly to the 3x reference by 2022. In the crisis scenario, we estimated an even more pessimistic 2020 (1,5x administration fees) but with signs of linear recovery (+0,5x per annum) until 2023.

As for ObrES penetration among CondES' portfolio maintenance works, in 2019 - year of ObrES' foundation - this figure arose to 30% of the total number of works. However, the management team considered it to be completely exceptional as a result of a strong marketing campaign with pricing below market standards, in order to gain market share. For the future, management BP assumes a long-run penetration of 15% whereas Oxy Base estimates 13,5% in a more moderate approach. The crisis scenario projects figures above our base case. This may seem a paradox, but the reasoning behind those projections was that, in a scenario without acquisitions, the company's efforts in cross-selling opportunities would have to increase.

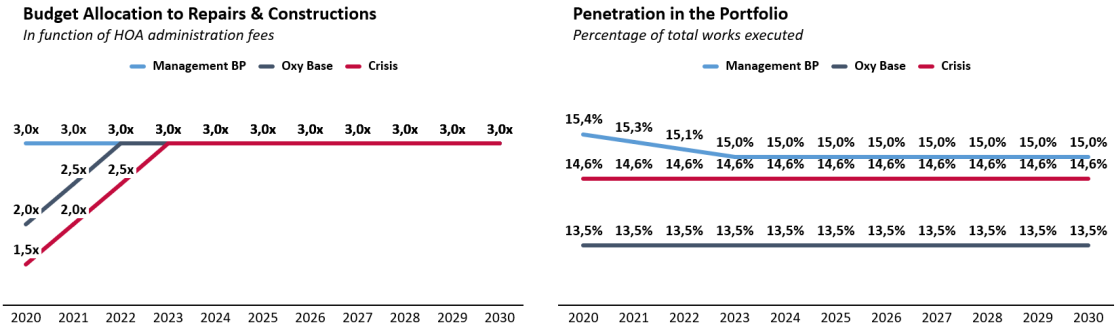

Figure 5.5: ObrES Performance Forecast

5.2 Investment Structure

"There are different mechanisms that Portuguese SMEs can explore: mezzanine debt that is more expensive but sustained"

Carlos Moreira da Silva

After several iterations with the counterpart, Oxy Capital proposed a mezzanine solution that could potentially fit the interests of both parties. This mechanism entailed (i) a loan and (ii) a warrants' structure.

As for the loan, Oxy Capital offered HoldES the possibility to get the €5 million financing amount with a 8% PIK (Paid-in-Kind) annual interest loan with maturity by 2024. PIK interest means that, instead of HoldES paying every year the respective interest amount, the interest will add to the amount in debt and thus capitalized. Formula 5.1 shows the calculus of the returned capital to Oxy Capital upon maturity.

$$ReturnedCapital = FinancingAmount \times (1 + PIKinterest)^{t} \tag{5.1}$$

where t is the number of years that the loan is outstanding.

Introducing the values of the proposal in the formula, returned capital in 2024 arises to c. €6,8 million, implying a capital gain for Oxy Capital of €1,8 million with a 8% IRR (Internal Rate of Return). However, as seen in the literature review, PE firms target above 8% IRR investments and mezzanine instruments have the possibility to account for a potential upside for the investors, what leads us to the equity-kicker - the warrants.

Remembering mezzanine structures with warrants from the literature review, the best part to the investor is that this kind of mechanisms completely separate the loan from the option to acquire equity. This means that Oxy will get the total reimbursement of the loan and still maintain its option to acquire shares.

The main part here is to define the value of the option, i.e., over which percentage of the capital of the company will Oxy Capital have the option to buy. The calculations were structured as follows: both parties agreed a pre-financing equity value for HoldES of c. €15,2 million. Taking the amount of €5 million into account, and assuming it would enter the company in a warrant exercise situation - the company releases new shares and sells them in exchange for a cash infusion, diluting the original investors' positions -, that would mean an increase in equity value up to c. €20,2 millions, where Oxy would hold a €5 million stake, corresponding to 24,7% of the company.

This means that Oxy Capital will lend money to HoldES until 2024 and, parallel to that, will have the option to buy a 24,7% share in the company for €5 million. This is interesting because, if the company, maintains its growth trend, Oxy will have equity-like returns upon a possible future sale, by exercising the warrants at the same time a hypothetical buyer presents its offer. In a no-sale scenario, and due to the Fund's time restrictions, the proposal entailed the obligation for HoldES to buyback our Warrants between 2026 and 2028 upon an already established valuation of 10x EV/EBITDA of CondES and 5x EV/EBITDA of ObrES. ImovES and future subsidiaries will require future negotiations.

As for the transaction structure, we also account for different situations in our scenarios. In the Management BP and Oxy Base everything happens according to the stipulated deadlines - warrants buyback in the first year of the given time-frame (2026-2028) as in a growth scenario the company has strong incentives to buy the warrants back as soon as possible. Parallel to that, in the crisis scenario, even despite being obliged to that, we projected a default situation where the company would only pay us by 2030, 2 years after the deadline.

By analysing Figure 5.6, it is possible to graphically observe our projections for the warrants value in the Oxy Base scenario. The future Enterprise Value is given by the sum of the products between each subsidiary run-rate EBITDA and its respective exit multiple - EV of €48,8 million by 2026. Afterwards we have to account for both subsidiaries' debt, totaling an equity value of €38 million. Regarding this, another extra protection that Oxy negotiated was a floor to the future equity value, meaning the company will always have to buy us the warrants back at a minimum equity value of €22 million - in this case, that restriction doesn't apply. Then the €5 million will be infused, increasing the equity value to €43 million. Over that value, Oxy will own a 24,7% share, corresponding to €10,6 million, that will sell to the company. Taking in consideration we

invested €5 million, the warrants mechanism will represent a capital gain for Oxy will arise to €5,6 million.

	Oxy base	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
1	**EBITDA CondES - run-rate**	**1.112**	**1.952**	**2.875**	**3.354**	**3.584**	**3.959**	**4.377**	**4.859**	**5.420**	**5.837**	**6.050**
2	Exit Multiple CondES	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x
3	**EBITDA ObrES - run-rate**	**147**	**294**	**576**	**794**	**869**	**943**	**1.022**	**1.112**	**1.216**	**1.336**	**1.363**
4	Exit Multiple ObrES	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x
	EV (1*2+3*4)	**11.855**	**20.991**	**31.629**	**37.512**	**40.184**	**44.300**	**48.881**	**54.145**	**60.278**	**65.048**	**67.316**
	(-) Net Debt CondES	3.771	8.147	12.024	12.416	12.619	12.372	12.222	12.184	11.651	11.646	11.850
	(-) Net Debt ObrES	112	3	61	9	(308)	(790)	(1.320)	(1.893)	(2.426)	(3.215)	(4.039)
	Equity Value	**7.972**	**12.840**	**19.544**	**25.087**	**27.872**	**32.717**	**37.979**	**43.854**	**51.053**	**56.617**	**59.505**
	Minimum Equity Value	22.000	22.000	22.000	22.000	22.000	22.000	22.000	22.000	22.000	22.000	22.000
	Equity Value (floored)	**22.000**	**22.000**	**22.000**	**25.087**	**27.872**	**32.717**	**37.979**	**43.854**	**51.053**	**56.617**	**59.505**
	(+) Cash Infusion	-	-	-	-	-	-	5.000	-	-	-	-
	Equity Value (post-infusion)	**22.000**	**22.000**	**22.000**	**25.087**	**27.872**	**32.717**	**42.979**	**43.854**	**51.053**	**56.617**	**59.505**
	% Oxy II (warrants)	-	-	-	-	-	-	24,7%	-	-	-	-
	Warrants Value	**-**	**-**	**-**	**-**	**-**	**-**	**10.629**	**-**	**-**	**-**	**-**
	(-) Investment	-	-	-	-	-	-	(5.000)	-	-	-	-
	Capital Gain Oxy	**-**	**-**	**-**	**-**	**-**	**-**	**5.629**	**-**	**-**	**-**	**-**

Figure 5.6: Warrants Value Calculations

The same exercise was performed to the management Business Plan - Figure 5.7. In this scenario the warrants are worth more than the double by 2026 - €11,9 million.

	BP management	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
1	**EBITDA CondES - run-rate**	**1.580**	**2.624**	**3.761**	**4.302**	**4.806**	**5.688**	**6.710**	**7.918**	**9.342**	**10.395**	**10.915**
2	Exit Multiple CondES	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x
3	**EBITDA ObrES - run-rate**	**250**	**430**	**677**	**922**	**1.012**	**1.202**	**1.418**	**1.674**	**1.975**	**2.330**	**2.446**
4	Exit Multiple ObrES	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x
	EV (1*2+3*4)	**17.057**	**28.384**	**40.993**	**47.631**	**53.126**	**62.893**	**74.195**	**87.545**	**103.296**	**115.602**	**121.382**
	(-) Net Debt CondES	4.328	8.248	11.539	11.233	11.998	12.189	12.514	12.952	12.659	12.859	13.428
	(-) Net Debt ObrES	112	114	93	(41)	(415)	(927)	(1.474)	(2.127)	(2.638)	(3.904)	(5.271)
	Equity Value	**12.617**	**20.021**	**29.360**	**36.439**	**41.543**	**51.630**	**63.156**	**76.720**	**93.274**	**106.647**	**113.225**
	Minimum Equity Value	22.000	22.000	22.000	22.000	22.000	22.000	22.000	22.000	22.000	22.000	22.000
	Equity Value (floored)	**22.000**	**22.000**	**29.360**	**36.439**	**41.543**	**51.630**	**63.156**	**76.720**	**93.274**	**106.647**	**113.225**
	(+) Cash Infusion	-	-	-	-	-	-	5.000	-	-	-	-
	Equity Value (post-infusion)	**22.000**	**22.000**	**29.360**	**36.439**	**41.543**	**51.630**	**68.156**	**76.720**	**93.274**	**106.647**	**113.225**
	% Oxy II (warrants)	-	-	-	-	-	-	24,7%	-	-	-	-
	Warrants Value	**-**	**-**	**-**	**-**	**-**	**-**	**16.855**	**-**	**-**	**-**	**-**
	(-) Investment	-	-	-	-	-	-	(5.000)	-	-	-	-
	Capital Gain Oxy	**-**	**-**	**-**	**-**	**-**	**-**	**11.855**	**-**	**-**	**-**	**-**

Figure 5.7: Warrants - Management BP

In the crisis scenario, the floored equity value is active due to low performance of the company - even though the company more than doubles its EBITDA and triplicates its equity value. In this case, Oxy Capital would still be entitled to receive €1,7 million for its warrants - Figure 5.8.

	Crise	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
1	**EBITDA CondES - run-rate**	**665**	**818**	**1.093**	**1.381**	**1.408**	**1.436**	**1.465**	**1.494**	**1.524**	**1.555**	**1.586**
2	Exit Multiple CondES	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x	10,0x
3	**EBITDA ObrES - run-rate**	**63**	**105**	**161**	**236**	**273**	**279**	**284**	**290**	**296**	**302**	**308**
4	Exit Multiple ObrES	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x	5,0x
	EV (1*2+3*4)	**6.965**	**8.704**	**11.738**	**14.984**	**15.449**	**15.758**	**16.073**	**16.394**	**16.722**	**17.057**	**17.398**
	(-) Net Debt CondES	2.344	4.616	6.787	8.310	8.322	7.941	7.538	7.113	6.451	5.971	5.495
	(-) Net Debt ObrES	112	(2)	68	148	166	68	(85)	(244)	(393)	(570)	(749)
	Equity Value	**4.509**	**4.090**	**4.883**	**6.526**	**6.960**	**7.748**	**8.619**	**9.525**	**10.664**	**11.656**	**12.652**
	Minimum Equity Value	22.000	22.000	22.000	22.000	22.000	22.000	22.000	22.000	22.000	22.000	22.000
	Equity Value (floored)	**22.000**	**22.000**	**22.000**	**22.000**	**22.000**	**22.000**	**22.000**	**22.000**	**22.000**	**22.000**	**22.000**
	(+) Cash Infusion	-	-	-	-	-	-	-	-	-	-	5.000
	Equity Value (post-infusion)	**22.000**	**22.000**	**22.000**	**22.000**	**22.000**	**22.000**	**22.000**	**22.000**	**22.000**	**22.000**	**27.000**
	% Oxy II (warrants)	-	-	-	-	-	-	-	-	-	-	24,7%
	Warrants Value	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**6.677**
	(-) Investment	-	-	-	-	-	-	-	-	-	-	(5.000)
	Capital Gain Oxy	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**1.677**

Figure 5.8: Warrants - Crisis

Having projected the expected returns with the loan - the same for all three scenarios - and the warrants, it is possible to plot the expected cashflows with the investment throughout the next 10 years - Figure 5.9.

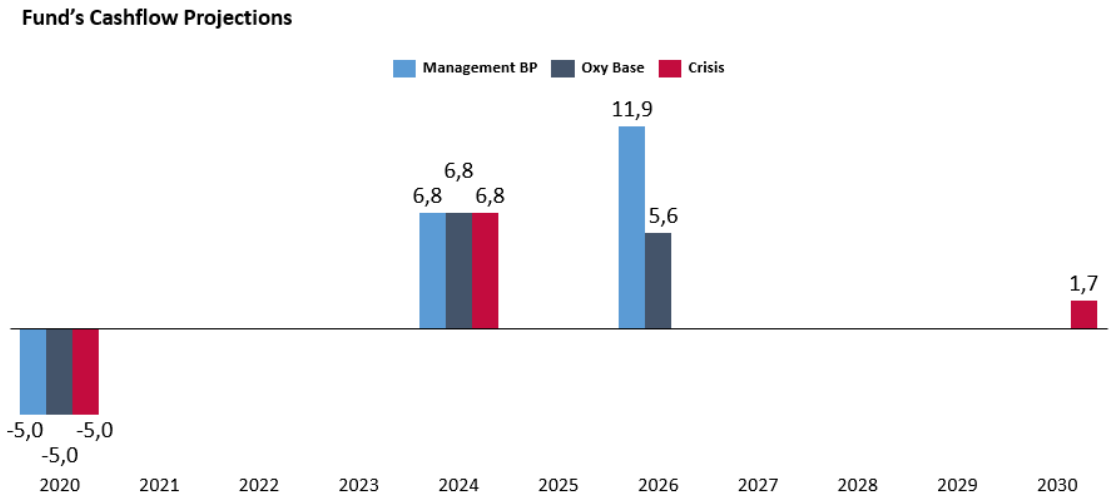

Figure 5.9: Cashflows Projections

Finally, in Figure 5.10 it is possible to calculate the final returns for Oxy Capital for each of the three scenarios.

By analysing the outcomes it is clear than in the management scenario, the outlook would be extremely favourable to Oxy Capital as the mezzanine instrument would capture part of the company's outstanding growth reaching a 3,7x Money Multiple.

In the central scenario - Oxy Base - we can also confirm the attractiveness of the investment. Despite lower potential returns when compared to the Management Business Plan, it is necessary

to refer that this is the scenario we actually believe the most. With that being said, achieving a 2,5x Money Multiple in a debt-risk instrument is remarkable.

In the crisis scenario, mezzanine instruments also prove to be extremely efficient in improving the risk/return profile of an investment. Even a scenario where no acquisitions are performed after 2023, operational margins decreases, churn increases to historical levels, the warrants still bring some upside return for the mezzanine investor.

	IRR	MM	CG
Management BP	29,1%	3,7x	13.657
Oxy Base	20,8%	2,5x	7.431
Crisis	11,3%	1,7x	3.480

Figure 5.10: Returns for Oxy Capital

Chapter 6

Conclusion

Having performed an end-to-end analysis on this investment opportunity, it is necessary to highlight the major conclusions that arose from this dissertation.

What was a completely unknown market at the beginning of this analysis has proven to be a recurring, highly fragmented market which opened an opportunity for a buy-and-build strategy.

The way the deal is structured the transaction entails an attractive risk/reward profile:

- Stable, highly recurring business with 3-4% churn figures due to customer inertia in exchanging the HOA administration company;
- Interesting operational margin (from 15% to 25%) which is considered to be relatively high when compared with other sectors in the overall corporate landscape;
- Low Covid-19 impact, which projects an encouraging outlook on the business future performance during any hypothetical economical downturn that may happen;
- Structure provides equity-like returns (20,8% IRR and 2,5 Money Multiple in our base case) with a debt instrument.

Also, bearing in mind the literature review on buy-and-build strategies, CondES configures a well positioned platform to take advantage of inorganic growth and multiple arbitrage:

- Highly fragmented market where CondES, despite being #2 in Madrid, only represents c. 2% of the total buildings in the city;
- Growing trend of younger customers preferring more interactive customer interfaces, mirroring changes in the demographics of home ownership, where CondES already has a head start;
- Future expansion to the Mediterraneo area which is the biggest regional market and where prices are actually bigger compared to the ones practiced in Madrid;
- Acquisitions of competitors at c. 5x EV/EBITDA (implied 1-1,5x EV/Sales) when overall international business is valued in the 10-20x EV/EBITDA range.

As any other PE investment, this opportunity also entails some risks namely:

- Sub-execution of the investment plan which is the main growth lever but that is mitigated with the equity-floor on the warrants buyback exercise;
- Client concentration in Platform 2, that is also mitigated by longer-term contract with clients and the integration of the former owners of Platform 2 inside CondES' operations.

Taking everything into account this dissertation confirms the possibility of developing a mezzanine financing structure that fits both (investor and borrower) pretensions in a growing recent business in a new market for Oxy Capital, having equity-like returns with a debt risk profile.

Moreover, Dikova et al. (2010), Hayward (2002) and Very and Schweiger (2001) claim that investments in cross-border acquisitions may suffer from information asymmetries and coordination costs that can be reduced through learning gains, making this transaction an opportunity for Oxy Capital to develop and expand geographically its network so that more international investment opportunities arrive at the company in the future.

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Anexo A

Appendix

Balance Sheet	
	Dec/19
Goodwill	4.641.651
Intangible assets	7.334
Tangible assets	209.782
Financial investments	200.000
Other fixed assets	160.755
Fixed assets	**5.219.522**
Accounts receivable	100.381
Cash	524.244
Other current assets	5.774
Current assets	**630.398**
TOTAL ASSETS	**5.849.921**
l/t bank financing	985.500
Fixed liabilities	**985.500**
Client advances	432.299
s/t bank financing	400.000
Accounts payable	12.345
Taxes and employees	282.599
Other current liabilities	13.962
Current liabilities	**1.141.206**
TOTAL LIABILITIES	**2.126.706**
Capital	4.430.000
Hybrid instruments	0
Reserves	4.381
Previous years net income	(277.001)
Current year net income	(434.166)
TOTAL EQUITY	**3.723.215**

Figure A.1: CondES Balance Sheet