

## Country Report - Spain

### M&A update

Autumn 2013



# Spain reaches an inflexion point

**Improving economic indicators including GDP, export figures, labour costs and unemployment rates suggest that Spain is exiting a period of deep recession and building a foundation to leverage growth. Low company valuations, technological expertise, a skilled workforce and an increasingly competitive business environment will trigger a rise in M&A volumes.**

### The key observations from our research:

■ **Large Spanish companies are increasingly targeting overseas businesses**

The focus is shifting from deleveraging to growth via international expansion. The main rationale behind these acquisitions is entering new markets and geographies rather than accessing product portfolios and technological expertise.

■ **Spain is a buyers' market**

The impact of the financial crisis has created opportunities for local and foreign investors to acquire attractively-priced mid-sized companies and distressed assets across a range of sectors. Spanish companies in financial distress which need to rebuild their balance sheets have lowered price expectations.

■ **Private equity (PE) is active in the market**

PE is targeting the steeply-discounted property portfolios of Spanish banks, as well as divesting pre-crisis acquisitions to trade buyers and other PE funds. Tourism and hospitality is a particularly attractive sector, and small and medium-sized enterprises (SMEs) geared towards exports will be targeted as export volumes grow.

■ **Investors are entering the market through acquisitions and joint ventures**

In order to complete deals, buyers need to fund them through higher levels of equity than debt, or negotiate vendor financing. Alternative sources of capital are slowly becoming available which will drive M&A activity.



**“With deleveraging processes almost complete, Spanish companies are looking to increase their size and global presence through international acquisitions. Foreign investors are taking advantage of low valuations to acquire in Spain.”**

Igor Gorostiaga, Partner, NORGESTION

The debt deleveraging process is nearing completion

## Economic recovery supports new investment

**Increased exports, enhanced competitiveness, growing consumer confidence and the opening of credit lines are greatly helping Spain's economic recovery. GDP fell by just 0.1% in the second quarter of 2013, compared to 0.5% in the same period last year, and growth is expected by the end of 2013. With company valuations still low, now is a good time to invest in well-managed and good-quality manufacturing and service companies.**

### Access to capital is improving

There are signs that the debt deleveraging process is nearing completion, with a significant proportion of Spanish companies reaching debt levels of 2-3x EBITDA, see Figure 2. Banks have increased their capital base through the sale of non-strategic industrial assets and real estate portfolios. Large private sector corporates have also been selling assets to strengthen their balance sheets. Repsol sold off €5 billion of

assets in the past year, most recently its liquefied natural gas business to Shell, in order to upgrade its credit rating. Companies are therefore now better placed for new investment.

The financial system restructuring process continues to be a key focus in Spain, with commercial and savings banks consolidating in order to meet strict capital requirements and avoid financial distress in an increasingly competitive market. The number of banks decreased from 50 in 2009 to 12 in 2012. With Nationalised banks NCG Banco and Catalunya Banc still up for sale and a potential merger between Unicaja, Banco Mare Nostrum and Ibercaja-Liderbank, this figure is likely to fall to nine.

Banks are currently reluctant to lend over 3x EBITDA, but are showing interest in financing solid investment projects, which will help reactivate the M&A market.

Figure 1: Selected sectors being targeted by foreign investors



Source: Mergers Alliance

- In March 2013, the Spanish government launched FOND-ICO Global, a public venture capital fund with initial capital of €1.2 billion. The fund will provide financing to innovative SMEs that have struggled to secure bank loans in order to promote competitiveness and international growth by matching investments from the private sector.

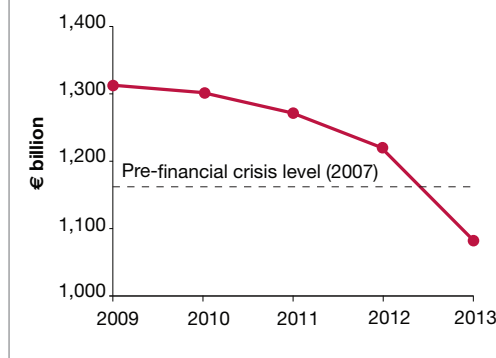
### Investor confidence is growing

- With the number of new foreign direct investment (FDI) projects rising to 274 in 2012, Spain is ranked fourth in Europe in terms of attractiveness to foreign investors, behind the UK, Germany and France. Structural reforms, lower wages and higher productivity has increased competitiveness and strengthened investor confidence in the Spanish market. The majority of investment came from the USA, Germany and the UK; business services and software received the most funding, although FDI inflow also increased in the chemicals, automotive and financial services sectors.
- Due to the downturn in the internal market, Spanish companies have been forced to focus on international trade. In 2012, for the first time since it joined the EU, Spain reported a current

account balance surplus (€7.7 billion in 2012), with exports rising 3.8% to reach a historical high of over €222 billion. Continuing geographic diversification has led to a significant increase in exports to Africa, Latin America, North America and Asia, with major sectors in terms of total exports including equipment, food, chemicals, automobiles and semi-manufactured goods. Success over the last 15 years in the development of technology in engineering and construction has led to growth in exports of infrastructure related to the power and electricity, water management systems and rail sectors.

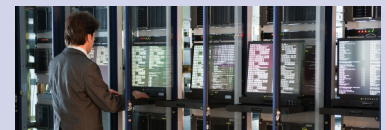
Spain continues to attract significant levels of FDI

Figure 2: Non-financial company debt has fallen 18% since 2009



Source: Banco de España (figures from July)

## Market Entry Case Study: Host Europe Group UK-based internet & web hosting services provider



Host Europe has established leading market positions in domain registration and application, cloud and managed hosting for SMEs, and has recently been acquired by private equity firm Cinven for €509 million.

### The strategic importance of Spain

Host Europe identified Spain as a key market for growth. In 2010, the company launched its Spanish operations under the Webfusion brand, with the aim of becoming a leading market player by offering an extensive product portfolio including its virtual private servers and e-marketing tools. Competitors include Dada Group and Arsys Group, recently acquired by German group United Internet for €140 million.

### Acquisition used to consolidate position in Spanish market

In January 2012 Host Europe acquired Spanish shared hosting and domain registry services company RedCoruna, attracted by its strong track record in web hosting, with 100,000 domain names under management, and 40% growth rate over three years. The transaction was in line with Host Europe's strategy to increase its international presence, and could also be used as a platform to cross over into Portugal.

Companies are achieving growth by making overseas acquisitions

## M&A volumes set to recover

**We are seeing increased signs of confidence returning to the market and expect to see M&A activity start to recover from its post-financial crisis lows, with the number of domestic and inbound deals set to increase in the second half of the year.**

Alternative financing options (such as FOND-ICO Global) are becoming available, valuation gaps are narrowing (in some cases because companies are in financial distress) and cross-border deals are increasing, with acquirers from Asia and Latin America helping to boost volumes. For example, Mexican bus transportation Grupo ADO recently acquired passenger road transport company Grupo Avanza for €800 million.

### Spanish companies are focusing on overseas growth and rebuilding balance sheets

Larger Spanish companies are targeting growth by making overseas acquisitions. Accessing new markets, rather than expanding technical capabilities or product portfolios, is their primary focus.

- In April 2013, Spanish elevator manufacturer Orona acquired Brazil-based AMG Elevadores, with the intention of increasing revenues in the Brazilian market to €100 million by 2018.

- In February 2013, Carlyle-backed Applus Servicios Tecnológicos, a testing, inspection and certification firm, announced the acquisition of Chinese engineering and automotive design company EDI. The transaction will enable Applus to consolidate its position in China and help its objective to provide global coverage to international clients.

Spanish firms which need to rebuild balance sheets and strengthen margins have been divesting non-essential assets and focusing on core businesses. Overseas buyers are stepping in to acquire distressed assets at low prices.

- In line with its 2012-14 business plan to generate €300 million in capital gains after failing a stress test, in January 2013 Banco Popular Español completed the €135 million divestment of its debt collection business to KG EOS Holding, a German provider of information, arrears and receivables management services.
- Fomento de Construcciones y Contratas (FCC) continued with its divestment plan and realised capital gains of €81 million through the sale of the remaining 50% stake in Proactiva Medio Ambiente, the Spanish provider of water and waste management in Latin America, to Veolia Environnement for €268 million in June 2013.

## Trade perspective: SAICA

“At SAICA we are looking to generate growth through overseas acquisitions. We have developed excellent technology and human capital, so our predominant focus is increasing market share. We’ve done this successfully in the UK since 2006 by gaining a significant market share in the packaging industry, investing in a state-of-the-art £290 million recycled paper mill and guaranteeing raw material supply by acquiring Futur Recycling, Houghton’s Waste Paper, Stirling Fibre and Cutts Recycling & Waste Management in 2011/2012.”



**Pedro Gascón**  
Managing Director, SAICA

*SAICA is an integrated consumer packaging group that was advised by UK partner Catalyst Corporate Finance on its four UK acquisitions.*

“70% of Spanish companies are SMEs and it’s difficult for them to jump directly into foreign markets. They will either be taken over by larger players or must merge with other domestic firms to reach the necessary scale to compete internationally.”



## Foreign investors are targeting new technologies and access to different geographies

Overseas firms are using an investment in Spain as a platform to access the European and Latin American markets.

- US biopharmaceutical firm OPKO Health will establish a presence in Europe with the recently-announced €14 million acquisition of pharmaceutical, nutraceutical and veterinary product manufacturer Farmadiet.
- Westcon Group, a US distributor of communications, network infrastructure, data centre and security solutions, has acquired Madrid-based IT solutions and services group Afina for €51 million in order to access the €235 billion IT market in Latin America, as well as consolidate its position in Iberia and North Africa.

Many Spanish companies have developed technological expertise which make them attractive acquisition targets.

- In 2012, Belgian IT and telecommunications infrastructure management services provider Econocom Group acquired Ermestel in order to access its expertise in the virtualisation and cloud computing services market.
- Natural language and intelligent conversation startup company INDISYS was acquired by US multinational Intel in September 2013 for around €20 million. The transaction will enable Intel to benefit from INDISYS' voice recognition technology and expertise in artificial intelligence.



Access to Europe and Latin America enhance Spain's attractiveness to foreign companies

## Case Study: CareFusion's acquisition of SENDAL

**NORGESTION is advising CareFusion, the US medical technology multinational, on the acquisition of SENDAL, a Spanish manufacturer of disposable speciality medical products that primarily serves the Western European market.**

### M&A strategy

This transaction is in line with CareFusion's strategy of global expansion in the Infection Prevention business line.

Despite the relatively small size of the target, the acquisition will support CareFusion's growth plans by introducing its products into SENDAL's existing commercial network and enhancing its presence and expertise in the non-dedicated infusion market.

The deal also complements CareFusion's traditional strength in its core business and grants access to leading market share in certain products and geographies.

### Acquisition challenges

The main challenge is to overcome the cultural differences between a listed US multinational and a Spanish family-owned business.

For example, an acquirer of this scale would typically be expecting the seller to have a detailed understanding of historical and future performance and present key customer relationships and opportunities.

Trust is a key issue in the Spanish business market so it is greatly beneficial to work with a local advisor, and with family-owned businesses, both the acquirer and the seller must consider the potential future involvement of major stakeholders, such as family members and employees.

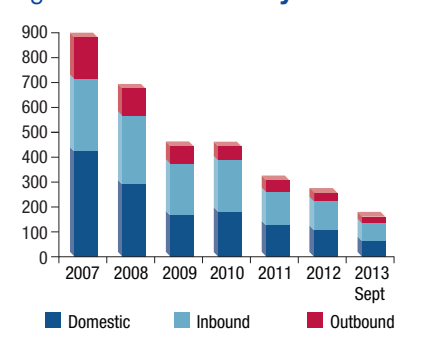
## Our perspective on M&A trends in Spain

**NORGESTION is Mergers Alliance's Spanish partner. Igor Gorostiaga, NORGESTION's Corporate Finance Division Managing Partner, discusses M&A trends and investment opportunities in Spain.**

### Q. How would you describe the M&A market in Spain?

It is a buyer-controlled market where the investors have negotiating strength following the reduction in price expectations by sellers. Deal volumes have clearly decreased since the beginning of the financial crisis (from 881 in 2007 to 256 in 2012, see Figure 3) and market activity is currently low.

Figure 3: M&A activity



Source: Corpfm (2007 - Sep 2013)

However, there are positive signs that M&A activity will increase following a number of outbound deals among mid-sized industrials. For example, Orona Group has recently acquired Brazil's AMG Elevadores, and Ormazabal, which supplies integral solutions to medium voltage distribution systems, has bought US broadband communications services provider CURRENT Group.

### Q. How has the deleveraging process affected M&A activity?

There is no major difference in forms of financing. However, the market is at a stage where, in order to complete a

deal successfully, buyers need access to a larger base of equity rather than debt, or negotiate structures that involve greater financing by the seller (such as vendor financing or earn outs). Magnum Capital Industrial Partners completed its recent €80 million secondary buy-out (SBO) of flavours and fragrances firm Iberchem without any debt financing.

### Q. Is Spain an attractive destination for investors?

Yes. The general perception is that domestic consumption levels have bottomed out, and so medium-term prospects are positive. Due to the domestic market downturn, company valuations have decreased.

Furthermore, many Spanish companies have been able to compete in the international market, even with internal credit constraints, by undergoing organisational restructuring and making manufacturing processes more efficient. They are therefore now more competitive and, with recent labour market reform, will become more so, bringing interesting opportunities for foreign investors.

Spain is also a means of accessing the European market. The most active foreign investors in Spain in the last five years have come from the USA, see Figure 4. Acquirers can also access the Latin American economies and benefit from good local knowledge, an established contact network and the highest number of double taxation and investment protection agreements in the region.

### Q. What are Spanish companies looking for in their overseas investments?

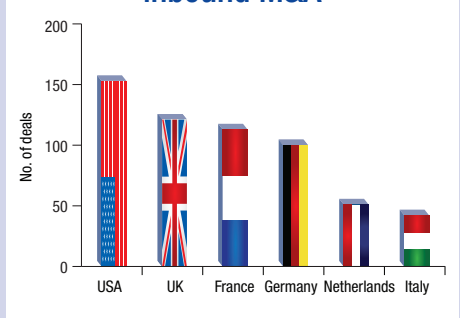
Most of the Spanish companies investing abroad have already developed very good product ranges and are therefore focusing on

accessing new markets. For some sectors, such as renewable energy, power transportation and distribution, and construction engineering, the growth of the domestic market between 1997 and 2007 led to the development of excellent technology and technical expertise. These companies are now investing worldwide, or even making domestic acquisitions of smaller but technologically-focused companies.

### Q. How is private equity approaching Spain?

Private equity activity has dropped continuously since 2010 in terms of transaction value, but we have seen a renewed interest in inbound investment from foreign investors such as HIG, Blackstone, KKR and Cinven. During the last 12 months, the market has been involved in some interesting transactions, such as the acquisition of Softonic by Partners Group (growth transaction in the internet sector) and the purchase of a 39% stake in Bridgepoint-backed Dorna Sports by the Canada Pension Plan Investment Board for €390 million. One of the main reasons for the decrease in domestic PE activity has been finance limitations. International investors that do not have to rely on financing in Spain can take advantage of this situation.

Figure 4: USA is leading inbound M&A



Source: Corpfm (2007 - Sep 2013)

# PE prepares to invest €12.7 billion in Spain

**Challenging economic conditions and financing limitations resulted in a decrease in the value and volume of deals in 2012, but private equity has continued to invest in Spain, with 24 buy-outs completed at a combined value of €3 billion.**

- Foreign private equity firms have begun targeting the steeply-discounted distressed property assets of Spanish banks and cash-strapped government organisations.

HIG Capital beat rival bids from Lone Star Funds, Apollo Global Management and Colony Capital to acquire a 51% stake in 'bad bank' Sareb's €100 million "Bull Portfolio", part of a €90 billion collection of repossessed real estate.

Madrid's regional government and city council sold portfolios of 3,000 residential flats and 1,860 rent controlled properties to Goldman Sachs and Azora (for €201 million) and Blackstone (for €126 million) respectively.

- M&A volumes have remained steady in 2013. 16 PE-backed buy-outs at a total value of €1.8 billion have been

completed so far this year and large international PE houses have set aside €12.7 billion to invest in Spain. Specific sectors of interest include tourism & hospitality, with hotel properties representing high performing assets at low valuations, and healthcare, in light of the reorganisation of publicly-funded services. SMEs, particularly distributors geared to exports, are also attractive targets as export volumes continue to grow.

- Private equity funds are looking to divest highly leveraged acquisitions completed prior to the financial crisis.

Spanish firm MCH Private Equity sold its 80% stake in air gun ammunition manufacturer Gamo Outdoor, bought in 2007 for €70 million, to PE house Bruckmann Rosser Sherrill & Co for €80 million.

As well as secondary buy-outs, exit activity includes trade sales. Germany-based United Internet recently announced the €140 million acquisition of web hosting and domain registration services firm Arsys Internet from The Carlyle Group and Mercapital.

PE is competing for distressed property assets

Figure 5: Selected recent M&A transactions

Date	Target company	Target Country	Target activities	Acquirer	Acquirer Country	Deal Value (€m)	Deal type
Sep-13	INDISYS	Spain	Artificial intelligence development	Intel	USA	20	Inbound
Aug-13	Gamo Outdoor	Spain	Air gun ammunition manufacturing	Bruckmann Rosser Sherrill & Co	USA	80	Inbound (PE)
Aug-13	Arsys Internet	Spain	Web hosting and domain registration	United Internet	Germany	140	Inbound
Aug-13	Grupo Avanza	Spain	Bus transportation and station operation	Grupo ADO	Mexico	800	Inbound
Aug-13	SENDAL	Spain	Disposable medical products manufacturing	CareFusion	USA	nd	Inbound
Jun-13	Proactiva Medio Ambiente	Spain	Environmental management (50%)	Veolia Environnement	France	268	Inbound
May-13	Iberchem	Spain	Flavours and fragrances manufacturing	Magnum Capital Industrial Partners	Spain	80	Domestic (PE)
Apr-13	AMG Elevadores	Brazil	Elevator and escalator manufacturing	Orona	Spain	nd	Outbound
Apr-13	Avalon Biometrics	Spain	ICT software development	Gemalto	Netherlands	nd	Inbound
Mar-13	CURRENT Group	USA	Broadband communications provision	Ormazabal	Spain	nd	Outbound
Mar-13	APIA XXI	Spain	Engineering and architecture	Berger Group	USA	nd	Inbound
Feb-13	Softonic	Spain	Software download portal operation	Partners Group	Switz.	83	Inbound (PE)
Feb-13	EDI	China	Automotive design and engineering	Applus Servicios Tecnologicos	Spain	nd	Outbound
Feb-13	NH Hoteles	Spain	Hotel operation (20%)	HNA Group	China	234	Inbound
Jan-13	Banco Popular Español	Spain	Debt collection business	KG EOS Holding	Germany	135	Inbound

Source: Corpfm

## Find out more

### Specialist advice on call...

For information on sector trends and M&A in Spain, please contact



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- Acquisition search assignments in Spain
- Advice on structuring and completing deals in Spain, with guidance through complex transaction issues in order to identify and avoid potential risks
- Information on sector trends and valuations in the Spanish market
- Access to corporate and governmental decision-makers at all levels

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