



CUATRECASAS

Market Trends in Spanish Private Equity Transactions

2023 EDITION

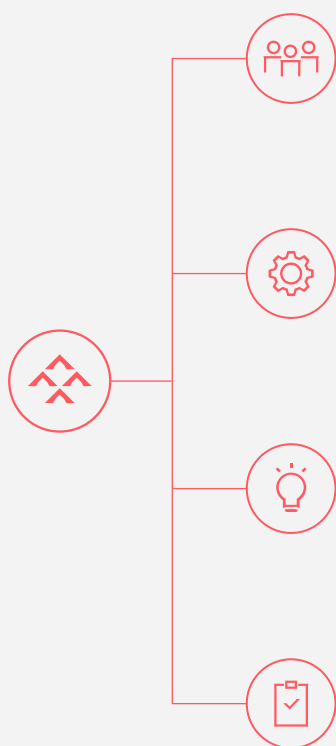
Contents

Cuatrecasas overview	3
Private Equity market outlook in Spain 2022	4
Our Private Equity practice	8
Market trends in Spain	10
Study overview	11
2022 Market trends at a glance	24

Cuatrecasas overview

THE LAWYER
European Law
Firm of the Year,
2022

Through our highly specialized legal teams with extensive knowledge and experience, we advise on all areas of business law. We help our clients with the most demanding matters wherever they are based.



TALENT

A multidisciplinary and diverse team of over **1,200 professionals across 26 nationalities**. Our people are our strength and we are committed to being inclusive and egalitarian.

EXPERIENCE

We have a **sectoral approach** and focus on all types of business. With extensive knowledge and experience, we offer our clients the **most sophisticated advice**, covering ongoing and transactional.

INNOVATION

We foment an innovation culture applied to the legal activity, which combines training, procedures and technological resources to contribute greater efficiency.

SPECIALIZATION

We offer optimal value thanks to our highly specialized teams who apply a cross-sectoral approach to our clients' business to offer efficient solutions.

Chambers
AND PARTNERS

IFLR1000

LATIN LAWYER
250

LEGAL
500

Recommended in the main
areas of law in Europe and
Latin America

THE LAWYER

Firm of the year in the
Iberian Peninsula,
2020 and 2022

LACCA
Latin American Corporate Counsel Association

Fifth most popular
international law firm in
Latin America, 2021



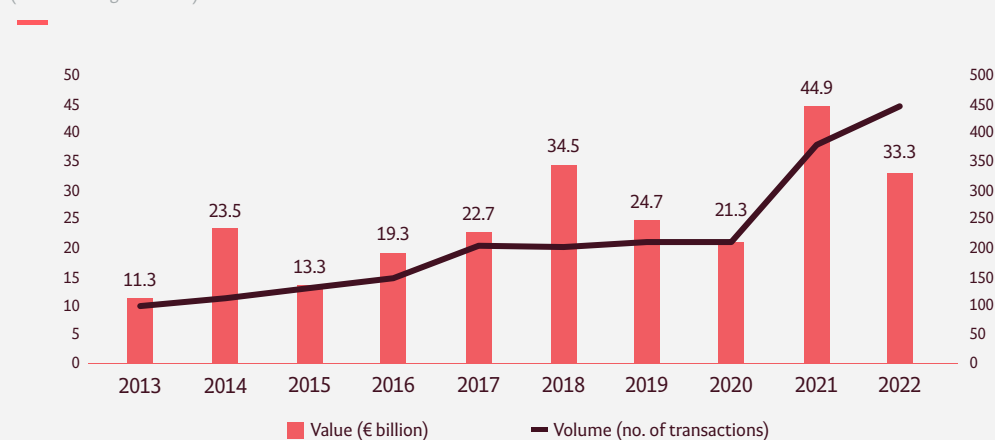
Private Equity market outlook in Spain 2022

General summary of the market

The Spanish private equity industry continues to grow, reaching another milestone, in terms of number of transactions. While the value is lower compared to 2021, when all records were broken and the transactions market reactivated after the COVID era, private equity had one of the highest transaction values, higher than almost every year in the past.

Spanish private equity transactions 2013-2022

(source: Mergermarket)



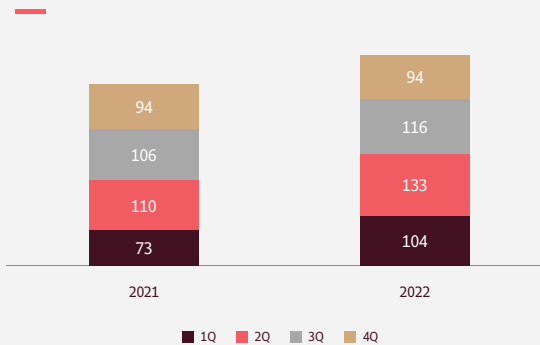
According to data produced by Mergermarket in Spain, 447 transactions were registered in 2022, totaling €33.3 billion, representing a -26% decrease in transaction value and a 17% increase in the volume of those transactions.

Other sources, such as TTR and the Spanish Venture Capital & Private Equity Association (SPAINCAP), show this same trend.

*Criteria: Private Equity transactions (Buyout, Exit, Buy and Build) announced between 01/01/2022 - 31/12/2022
Target or Bidder or Seller Dominant Geography: Spain*

Number of private equity transactions (quarterly)

(source: Mergermarket)



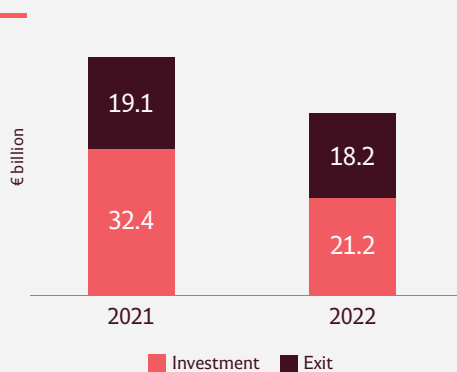
The private equity market has proved resilient, but it has also been slowing down gradually, particularly in the last quarter, strongly influenced by the global macroeconomic challenges, including the energy crisis, the Ukraine war, spiraling inflation and higher interest rates.

In 2022, the value of investments decreased compared to the previous year (-35%) and lost weight to sales, which dropped 5%.

However, in terms of transaction volume, the weight of investments increased slightly, standing at 82% of all transactions.

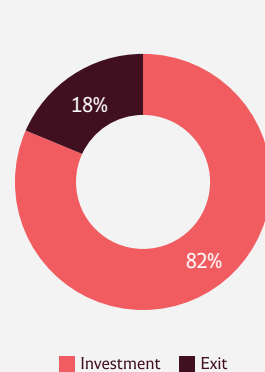
Value of private equity transactions in Spain. Investment vs exit

(source: Mergermarket)



Volume of private equity transactions in Spain in 2022. Investment vs exit

(source: Mergermarket)



Source of investment

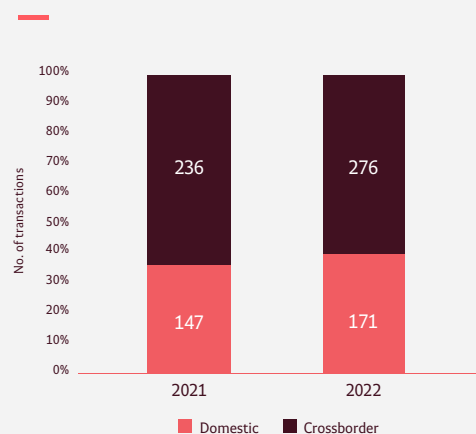
The market is still dominated by crossborder transactions: both in number (62%) and value (83%). However, the value of domestic transactions increased significantly, bucking the trend.

International investors continue to focus on high-value transactions, while national players participate in lower-value transactions.

International investors are focusing more on large deals

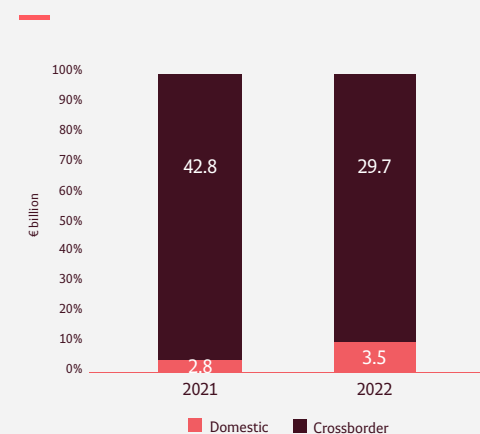
Source of private equity transactions in Spain (by volume) 2021 vs 2022

(source: Mergermarket)



Source of private equity transactions in Spain (by value) 2021 vs 2022

(source: Mergermarket)

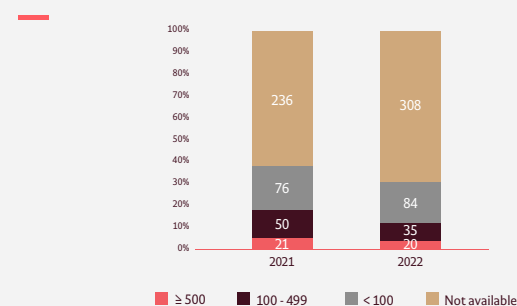


US and UK-based private equity investors led inbound transactions in Spain, both in volume and value.

Type of transactions

Size of private equity transactions in Spain 2021 vs 2022

(source: Mergermarket)



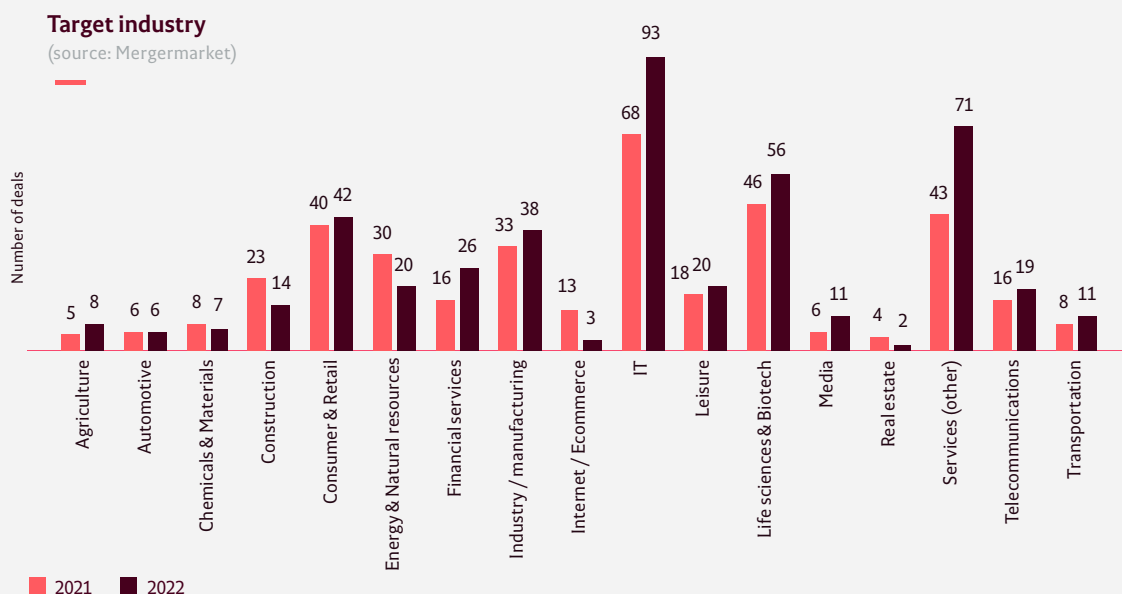
Size

The market grew in small-middle market (particularly in transactions lower than 100 million), and it contracted in high-end deals.

Industries

Transaction volume by industry continued to be similar to that of recent years, with two thirds of all activity concentrated in the technology sector (the outstanding leader with 21% of private equity transactions), services (16%), life sciences (13%), retail & consumer (9%), industry (9%) and financial services (6%).

All industries grew compared to 2021, except for internet/e-commerce, real estate, construction, energy and chemicals. This growth was particularly outstanding in some industries such as media (83%), services (65%), financial services (63%), and agriculture (60%).



Our Private Equity practice

One of the most active teams with multidisciplinary capacity and extensive experience in private equity transactions

Our large and specialized team advises clients on designing, negotiating, and implementing private equity investments and acquisitions, as well as on private equity recapitalization transactions and divestments. Our team also includes experts in setting up funds, the financing of portfolio companies and restructuring transactions. We place special emphasis on designing innovative strategies and implementing investment and divestment structures that are optimum and efficient from a tax and commercial perspective.

We regularly advise national and international private equity firms and funds, fund sponsors, management companies, investors, portfolio companies, and banks and financial institutions on all aspects and stages of a wide range of investment, financing, and acquisition transactions.

Chambers, 2021

"Has a large market share in private equity deals"

Chambers, 2022

"Strong practice group handling a broad spectrum of domestic and cross-border corporate matters for clients including private equity houses."

Large market share: In 2022, we were involved in over 70 private equity and venture capital transactions both in Spain and Portugal.

Relevant experience: We have participated in some of the largest and most complex transactions in recent years, including the largest in 2021/2022.

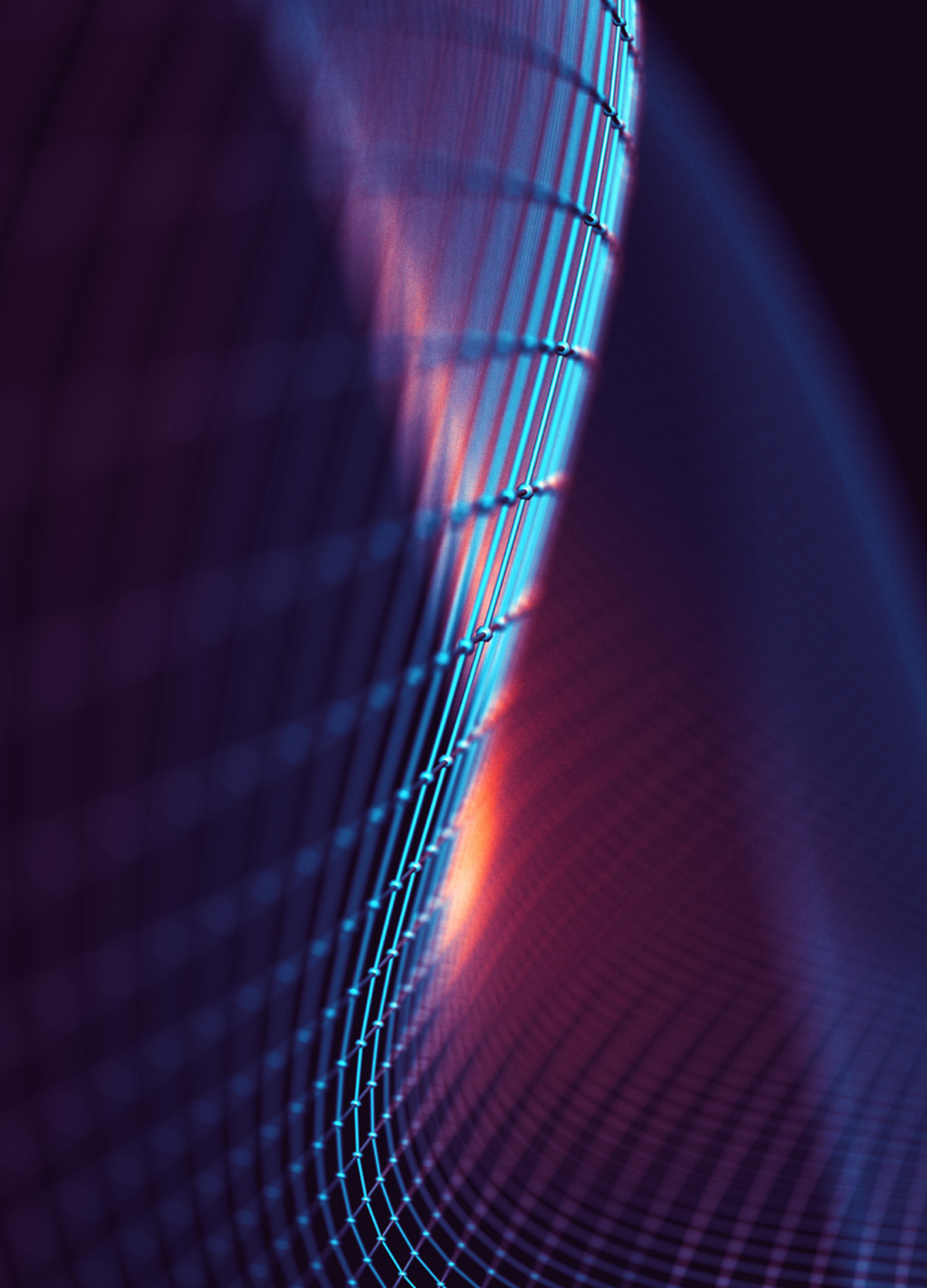
Crossborder vision: We regularly advise major international private equity firms on their investments in several jurisdictions, particularly in Spain, Portugal and Latin America.

**Highly recommended
firm in Private Equity**

Chambers
AND PARTNERS


LEADERS LEAGUE

The
**LEGAL
500**



Market trends in Spain

Significant trends in Cuatrecasas deals

This study, an overview of market trends in private equity transactions in Spain, analyzes the most significant deals on which Cuatrecasas advised.

The study analyzes 36 private equity deals signed in 2021 and 2022 in Spain with transaction values over €10 million in Spain. It does not include venture capital transactions, as they have their own features and market trends. Unless otherwise specified, all the charts include the figures for 2021 and 2022.

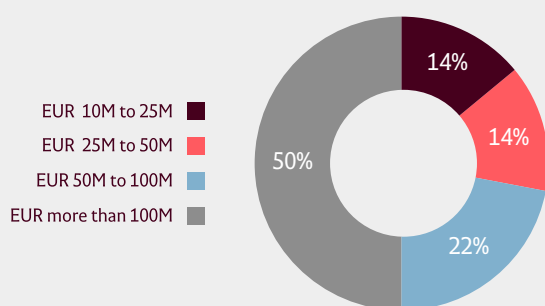


Study overview

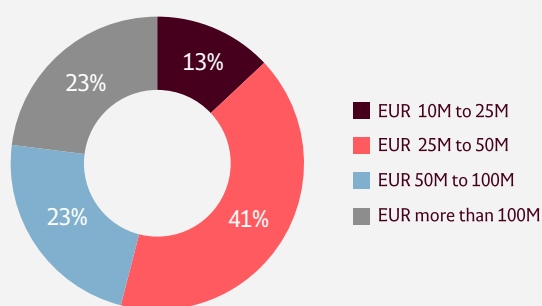
In 2021, half of the transactions that Cuatrecasas advised on were valued at over €100 million; however, in 2022, middle market transactions gained traction, with 64% of all transactions valued between €25 and €100 million.

In 2022, middle market transactions gained traction

Transaction value in 2021



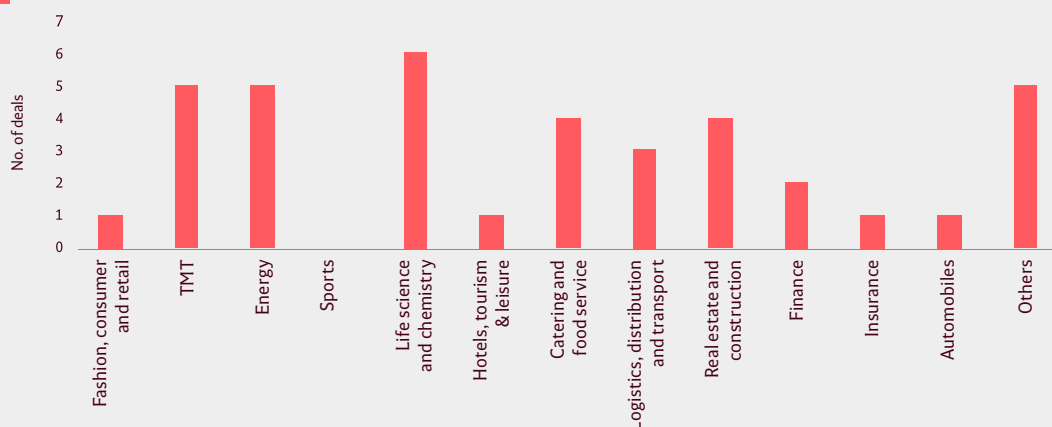
Transaction value in 2022



As always, investment was highly diversified across different sectors, with the life sciences, energy, and technology, media, and telecommunications (TMT) sectors being particularly active.

Despite the high level of investment by private equity funds in the veterinary sector in 2022, the majority of these deals were relatively small, with a value of less than €10 million, meaning they are outside the scope of this study. Furthermore, many of these transactions were structured as asset deals, not as share deals in Spain.

Target industry

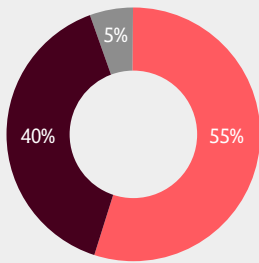


The trend continues, and investments were once again dominant with 89% of the transactions if we consider secondary buyouts (“SBOs”), where a private equity firm sells its investment to another private equity firm. There was only one pure exit transaction in 2022. However, SBOs experienced significant growth, amounting to more than 40% of the deals.

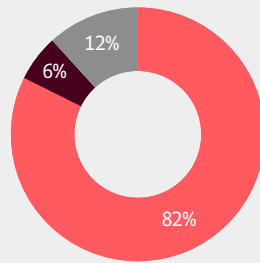
Secondary buyouts increased significantly in 2022

Although the increase in SBOs is due to several factors, it is largely caused by the high liquidity of funds due to the broad and successful capital-raising processes of recent years.

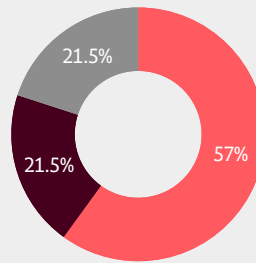
Investment vs exit 2019



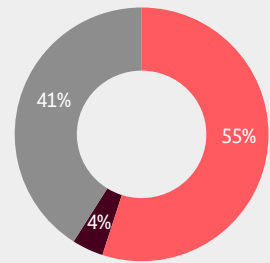
Investment vs exit 2020



Investment vs exit 2021



Investment vs exit 2022

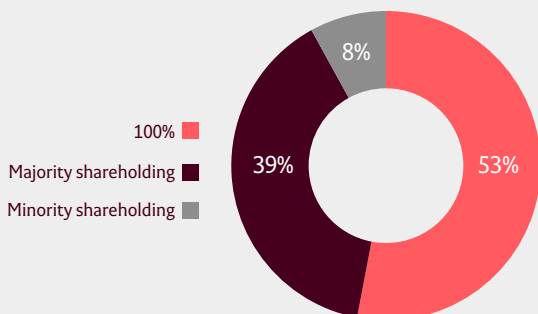


Investment Exit SBO

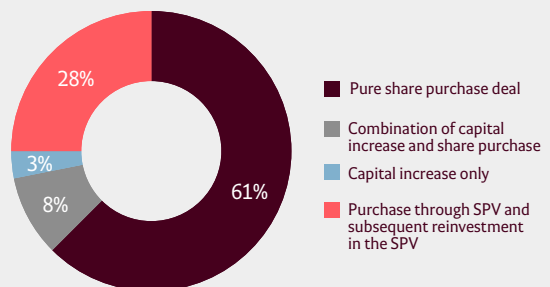
When a private equity fund invests, the most common transaction continues to be one in which it buys 100% of the target company's capital stock or takes a majority shareholding through a pure share purchase deal. This contrasts with venture capital transactions, where pure share purchase deals are rare and where the fund usually takes a minority shareholding in the company through a capital increase.

More than one-quarter of transactions continue to be ones in which the private equity fund, instead of buying a majority shareholding directly, buys the target company through a special purpose vehicle (SPV), after which the seller reinvests in the SPV, usually through a capital increase. This formula was used in the majority of deals in which the fund acquired a majority stake (85% of cases in 2022). This is due to the ease of regulating the relationships among the different shareholders in the vehicle that owns the entire capital of the target.

Majority vs minority



Investment structure

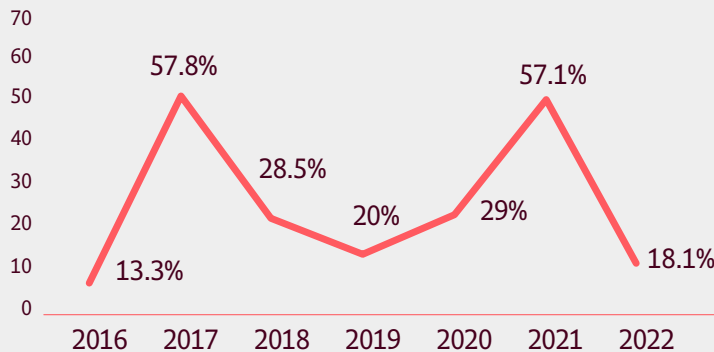


When the fund acquires a majority shareholding, the fund buys 100% of the target company through an SPV and managers or founders reinvest in the buyer's SPV

Deal process

The number of private equity transactions run as auctions increased considerably on previous years, particularly in 2021, when more than half of the transactions were auctions with expedited deadlines due to the pandemic. This trend changed dramatically in 2022, when only 18% of the deals were beauty contests with multiple prospective bidders (all within the framework of an SBO process). This is mainly attributed to the uncertainty brought about by the war in Ukraine.

Auctions process



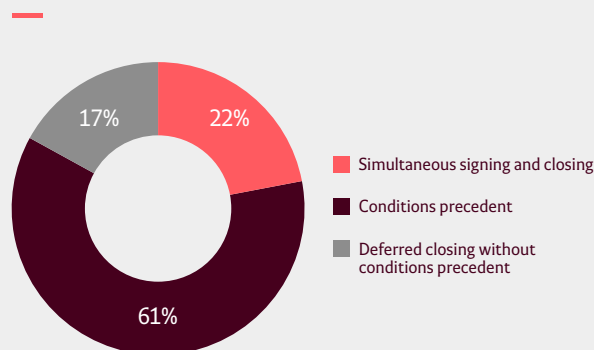
Due to the uncertainty brought about by the war in Ukraine, in 2022, there were far fewer auctions than in previous years

During the first year of the pandemic, there were fewer transactions with conditions precedent (47% in 2020). In our experience, this was probably because, unless conditions precedent were strictly necessary, the uncertain circumstances made parties prefer fast transactions with simultaneous signing and closing. In 2021, transactions returned to more usual percentages, a trend that continued into 2022, when figures remained similar to those of the previous year.

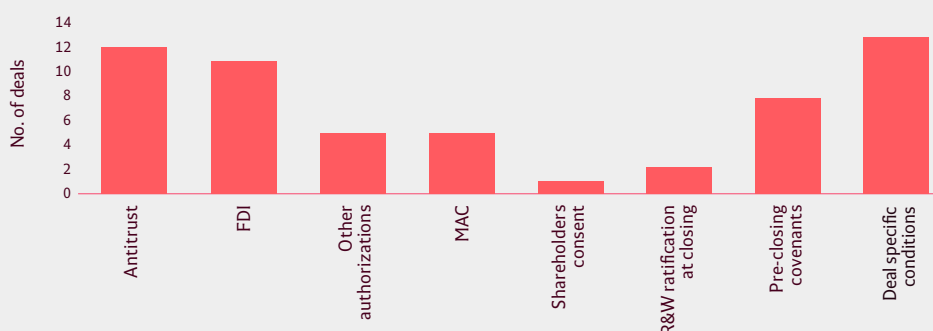


Although the transactions included a range of conditions precedent, the most common were (i) approval by the antitrust authorities; (ii) foreign direct investment (FDI) authorization; and (iii) more ad hoc conditions precedent related to the deal, mostly third-party waivers (i.e., lenders, suppliers or other parties' consent due to change of control clauses), or the execution or non-termination of certain agreements.

Simultaneous signing and closing vs deferred closing



Types of conditions precedent



Almost all the deals that included conditions precedent did so because of the need for regulatory approval—particularly antitrust clearance—and FDI screening.

The market has gradually been internalizing the implementation of a prior authorization system for FDIs. This is especially true for the private equity sector, where a preliminary analysis was needed for most deals involving international parties, given funds' interest in strategic sectors. Finally, over half of these transactions required a condition precedent due to the need for FDI regulatory approval.

More than half of the transactions required a condition precedent due to the need for regulatory approval

In our experience, the Council of Ministers in Spain takes around five months to authorize deals that require a prior FDI authorization. However, a new regulation to implement the FDI screening mechanism is expected in 2023. This had been forecasted for 2022, but it never came to fruition. As the new rules will likely reduce the number of cases where the authorization of the Council of Ministers is necessary, we predict that the period to obtain FDI clearance for M&A transactions will be shorter than it is currently.

Another important novelty for 2023 is that Regulation (EU) 2022/2560 of the European Parliament and of the Council of 14 December 2022 on foreign subsidies distorting the internal market, known as the Foreign Subsidies Regulation (FSR), which entered into force on January 12, 2023, will apply from July 12, 2023.

Generally, the FSR affects all undertakings that receive foreign subsidies. However, it will be particularly relevant to M&As, as concentrations must be notified in certain cases if foreign subsidies that distort the internal market have been granted; failure to do so will result in serious consequences. This means that, in addition to the analysis required for merger control and FDI, an analysis will have to be carried out to determine whether the transaction requires the European Commission's authorization under foreign subsidies rules, which will affect the terms and costs of the transaction. Although the FSR will apply from July 12, 2023, the prior notification requirements to obtain authorization for concentrations will not apply until October 12, 2023.

From October 12, 2023, concentrations may require a new prior authorization from the EU in certain cases if foreign subsidies that distort the internal market have been granted

Before 2020, almost half the transactions requiring regulatory approval included a hell or high water clause. This trend changed in 2020 and 2021, when only around 12.5% of the transactions included them. In 2022, this figure rose slightly to 25%. These agreements sometimes stipulated that the conditions the authorities could impose had to be accepted unless they were overly burdensome or exceeded certain limits.

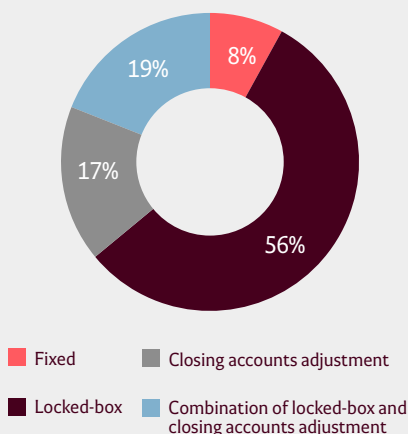
From 2019 to 2021, there was a progressive decrease in the use of break-up fees, in the event the closing did not occur or the closing obligations were breached (30%, 25% and 0%, respectively). However, in 2022, the use of break-up fees rebounded to almost 30% of the transactions with deferred closing. The percentage of the purchase price to be paid as a penalty varied, at times reaching 10% or 15%, and other times—more symbolically—being below 1%.

Conditions subsequent are not used because, once the transaction is closed and the property transferred, reverting back to the pre-purchase stage is difficult.

In 2022, 30% of transactions with deferred closing included a break-up fee

Consideration and pricing mechanisms

Pricing mechanism



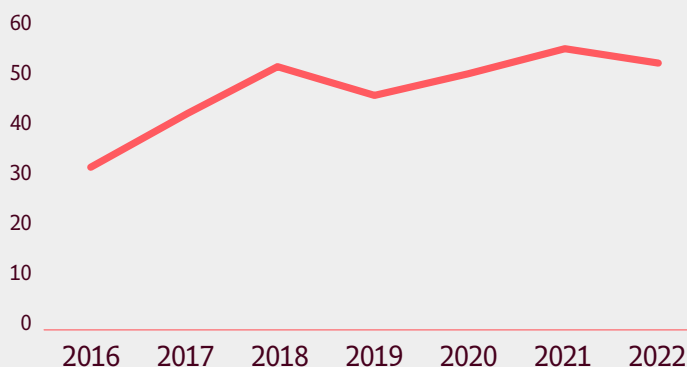
Locked-box mechanism is consolidated again in 2022 as the most used pricing mechanism

As in traditional private M&A transactions, the completion accounts or closing accounts adjustment and locked-box mechanisms are used most commonly, together with the fixed-price mechanism.

Although the completion accounts and locked-box mechanisms have their pros and cons for both parties, the completion accounts mechanism has been considered buyer friendly, while the locked-box mechanism has been considered seller friendly. However, in recent years, the use of the locked-box mechanism has significantly increased and has been consolidated as the most used pricing mechanism, regardless of whether it is a sell-side or buy-side transaction.

During 2021 and 2022, 56% of transactions used a pure locked-box mechanism, 17% the completion accounts mechanism, 8% the fixed-price mechanism, and 19% a mechanism combining the locked-box and completion accounts mechanisms.

Percentage of transactions using pure locked box



As the financial risk is transferred to the purchaser on the locked-box date within the locked-box mechanism, and because the purchaser can benefit from the profits generated from that date while the price is paid at closing, the seller will try to seek compensation, usually by using equity tickers or ticking fees. Typically, they are structured as a fixed daily amount from the locked-box date or signing date until the closing date, or, more rarely, as a fixed daily rate.

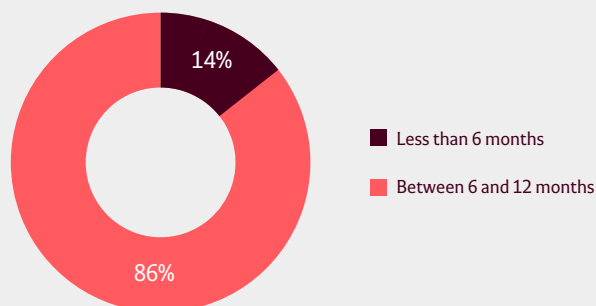
Although negotiating an equity ticker was previously uncommon in Spain, it is increasingly used. In 2021, 27% of locked-box transactions included one, and this trend has continued into 2022, with 31.25% of them doing so.

While the use of equity tickers in locked-box transactions continues to grow, adding an interest to the leakage amount is still uncommon

The seller's liability under leakage compensation is either capped at the leakage amount effectively received, or expenses and taxes are added. However, only in 14% of transactions was leakage increased by the agreed interest accrued from the leakage date.

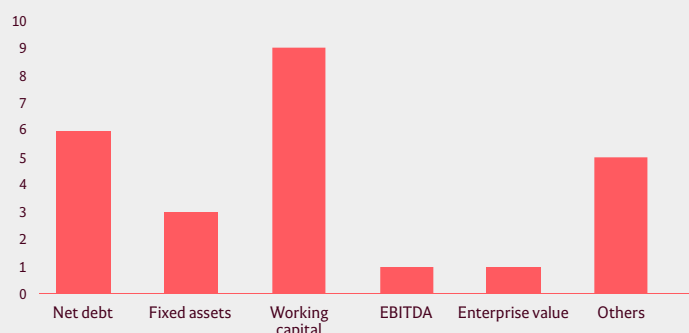
The most common limitation period is 6 to 12 months. There are no transactions with a limitation period exceeding 12 months.

Leakage limitation period



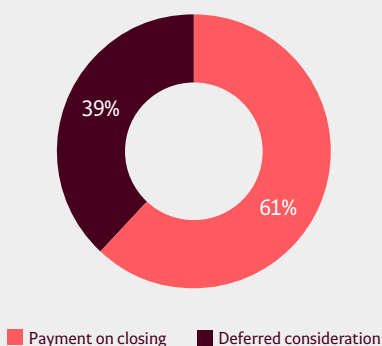
Even though the locked-box mechanism has become the most used pricing mechanism, the completion accounts mechanism was still used in 36% of the deals (if a combination of locked-box and completion accounts transactions are included), in which net debt and working capital were the most widely used financial parameters for the post-closing adjustment.

Closing accounts adjustment - Financial parameters

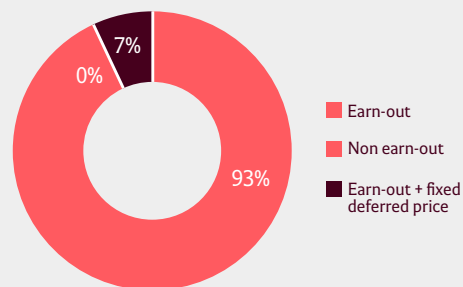


In 2022, working capital was used in 75% of the deals as the financial parameter for the post-closing adjustment

Payment on closing vs deferred consideration



Earn-out



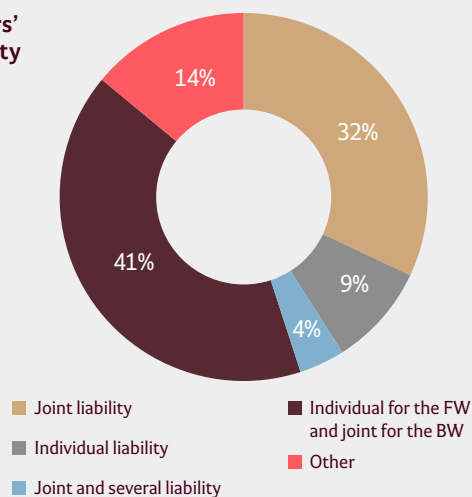
As in previous years, up to 39% of transactions included payment of deferred consideration, which were in all cases earn-outs or a combination of fixed deferred price and earn-outs. Following a trend that started in 2018, no transaction with deferred consideration had only a fixed deferred price. When an earn-out is agreed, in almost 30% of the deals, covenants to protect the seller were included. Most earn-outs are linked to EBITDA or, in general, to the company's benefits.

Warranties

Representations and warranties (R&Ws) are negotiated in share and purchase agreements (SPAs) under standard M&A practice. The agreed remedies for a breach of R&Ws are the buyer's only remedies against the seller if fundamental or business warranties are breached.

In 2021 and 2022, when there was more than one seller, their liability was usually joint or individual, or a combination of both (individual for the fundamental warranties and joint for the business warranties). Joint and several liability was hardly seen.

Sellers' liability



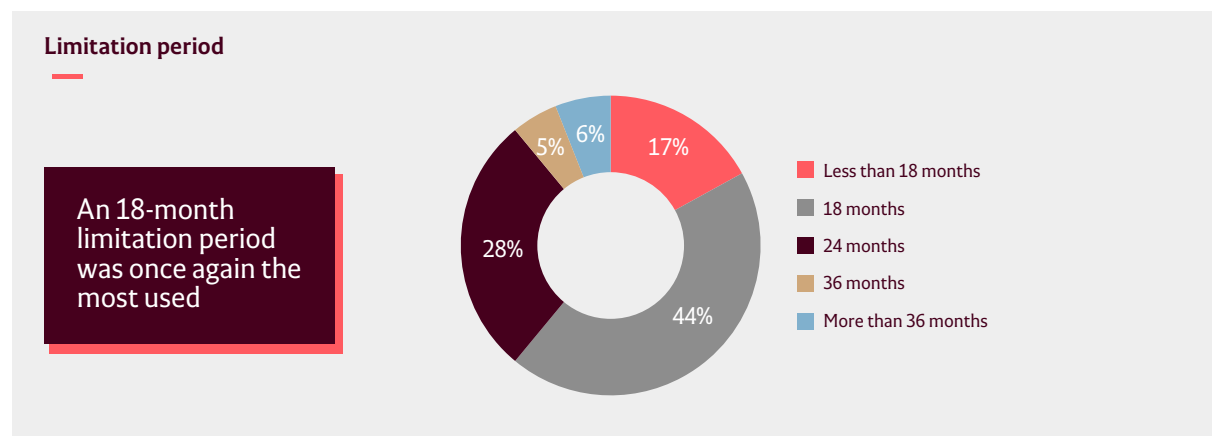
Unlike venture capital transactions, where indemnification can sometimes be in cash or, at the investors' discretion, the target company's shares, warranty payments in private equity transactions are almost always cash.

In 92% of transactions with a deferred closing, the seller was considered to repeat the R&Ws on completion.

Warranty limitations

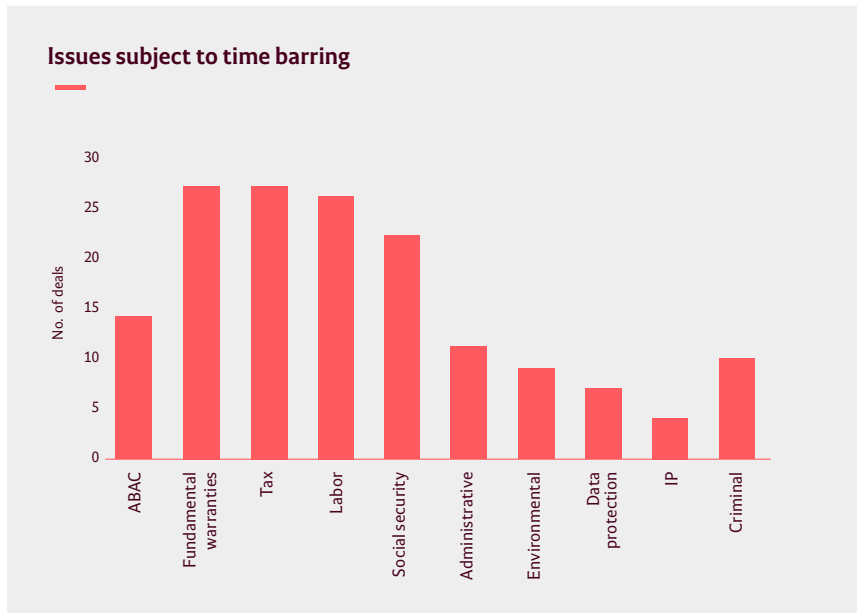
SPAs are usually limited quantitatively and temporarily. However, those limits differ depending on whether there is an investment or an exit and whether warranty and indemnity (W&I) insurance is taken out.

Although in 2018 and 2019 the seller was usually liable for a 24-month period after closing, during 2020 and 2021, an 18-month limitation period became the most used (in 46% of the transactions), a trend that continued into 2022 (in 40% of the transactions), replacing the longer periods of previous years.



Subjecting specific issues to time barring as provided by law or regulations is common practice, mainly in tax, labor and social security matters, as well as damages related to the breach of a fundamental warranty. However, it is also common in criminal, environmental, administrative, data protection, intellectual property, and anti-corruption matters.

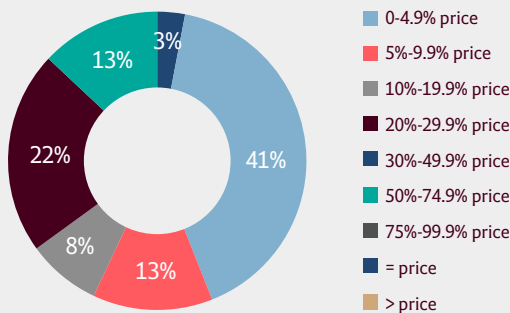
There are usually upper and lower limits on monetary limitations



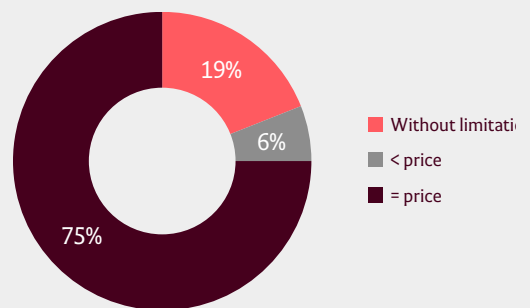
Excluding clean exits, since 2020, the most used liability cap for business and tax warranties is between 20% and 30% of the purchase price

Liability for business and tax warranties was generally capped (usually under 50% of the purchase price), in contrast to fundamental warranties, which were usually limited to the purchase price (75%) or not limited at all (19%). In 2021 and 2022, the most common liability cap for business and tax warranties was between 20% and 30% of the purchase price. This is without considering clean exits, which increased considerably over the past two years.

Liability caps-Business warranties



Liability caps-Business warranties



In 2022, the pre-2021 trend returned, where in all exit or SBO transactions, either the private equity fund (i) was not held liable for breach of business or tax warranties due to the agreement of a W&I insurance; or (ii) had a liability capped at less than 1% of the purchase price without the agreement of a W&I insurance. This had been common practice before 2021, but that year only saw it happening in 40% of the transactions.

In exits or SBO transactions, the private equity fund was not held liable for breach of business or tax warranties

Another trend that is becoming increasingly common in clean W&I insurance transactions is that in the SPA, the seller (typically a private equity fund) only grants and is only liable for fundamental warranties. Business and tax warranties are provided in a separate document known as the management warranty deed, which is executed between the target management (as warrantors) and the buyer. This is because private equity funds, as financial investors, consider that the management team is in a better position to grant business warranties that reflect how the company is run on a day-to-day basis, even if the management team's liability is often capped at a symbolic €1 in the management warranty deed.

The granting of business and tax warranties through a management warranty deed is becoming increasingly common

As usual, in all transactions in which private equity funds invested, either industrial sellers granted business and tax warranties or W&I insurance was agreed.

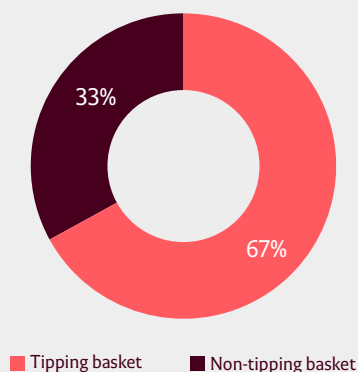
Regarding lower limits (and excluding W&I insurance transactions), (i) the seller was not usually obliged to indemnify for losses if each loss, considered individually, was less than a certain amount (*de minimis* exclusion or *de minimis* amount); and (ii) almost all deals included a basket or threshold. In these cases, the seller is not liable for damages unless the aggregate amount of the claim, together with all the claims (each over the *de minimis* amount), exceeds the basket/threshold amount.

In most transactions we saw tipping baskets, which means the seller is liable for the entire amount and not merely for the excess if the aggregate of claims exceeds the basket amount (67%

took the form of tipping baskets and 33% of non-tipping baskets).

The basket amount is still usually below 1% of the purchase price, averaging 0.69% for non-tipping baskets and 0.57% for tipping baskets. The *de minimis* amount was significantly lower in 2020 at an average of 0.02%, compared to an average of 0.118% in 2021, but it decreased again in 2022 to an average of 0.05%.

Basket

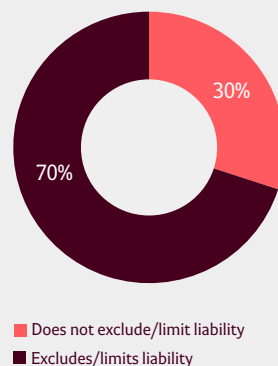


Buyer's knowledge

In Spain, the impact of a buyer's actual or deemed knowledge on claims for breach of warranties is usually negotiated under SPAs. More than 90% of the SPAs stated whether the buyer's knowledge of an inaccuracy in R&Ws limits the seller's liability for breach of warranties. Of this 91.6%, in almost 70% of transactions, the buyer's knowledge excluded or limited the seller's liability. The other 30% of transactions did not include limitations on the buyer's remedies if the buyer was previously aware of an inaccuracy or breach.

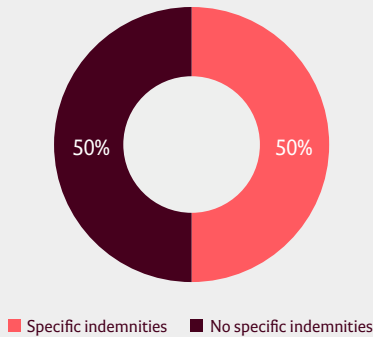
Although in previous years the percentage of the so-called pro-sandbagging clauses (not excluding liability) versus anti-sandbagging clauses (excluding liability) was more or less the same (with anti-sandbagging clauses being slightly more common), the difference has since become more pronounced in favor of anti-sandbagging clauses, particularly in 2021 and 2022.

Effect of buyer's knowledge



Since 2021, there have been more transactions with an anti-sandbagging clause than with a pro-sandbagging clause

Specific indemnities



Specific indemnities

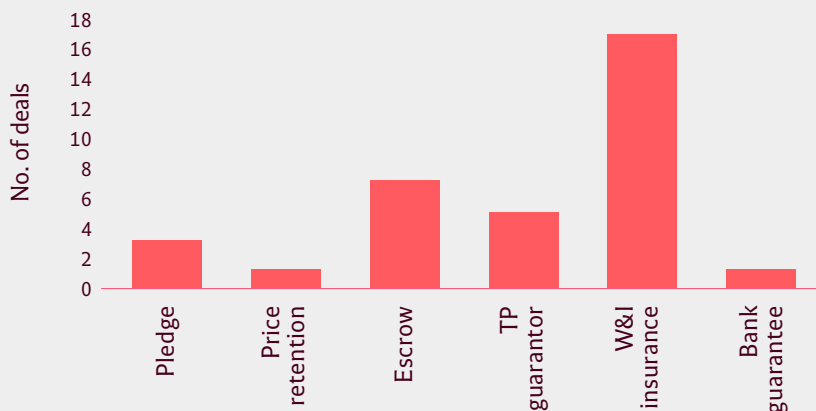
Specific indemnities are ad hoc indemnity remedies negotiated when the risk of a specific loss is high, but not 100% certain. They are not usually subject to any limitation and do not have to follow the claim procedure negotiated under the SPA. For several reasons, specific indemnities were included in 50% of transactions.

Buyer's remedies against seller's liability

To seek security against the seller's liability, including a buyer's remedy in the SPA is common. In general, during 2021, funds were less demanding in the seller's guarantees, either because they were buying highly demanded assets or because the valuation was beneficial and there was no need for further guarantees. However, in 2022, the figures returned to more usual levels, with 77% of agreements including a seller's guarantee in case of breach of its R&Ws.

Regarding classic buyer's remedies, escrows have reclaimed their position as the most used option. They had lost this position in the past two years, probably because, as money was very cheap, some escrow agreements were charging interest instead of giving it, discouraging parties. However, with interest rates on the rise, the situation has reversed. Bank guarantees, which were widely used some years ago, continue to be rarely used.

Types of sellers' guarantee

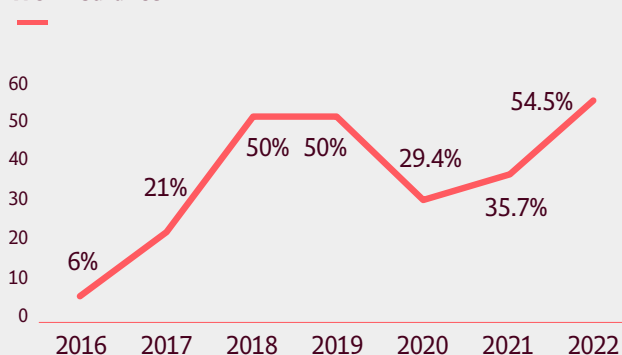


W&I insurance

W&I insurance continues to be the most used buyer's remedy in private equity and, compared to 2021, has regained ground. It is clearly consolidated as the most used buyer's remedy and not only within the framework of an exit (41% of the transactions were investments, 18% exits and 41% SBOs). Therefore, the use of W&I insurance has become widespread, both when private equity funds are investing and disinvesting, but its use has focused on clean exits (95% of W&I insurance transactions).

A clean exit is one in which the seller is not liable for the breach of any business warranty. Consequently, if there are any inaccuracies in the seller's R&Ws, the buyer's only remedy would be against the W&I insurer under the W&I insurance policy, and the buyer would not be able to take any action against the seller (or any claims against the seller would be limited to €1). However, in a clean exit, the purchaser is usually able to take action against the seller in cases of fraud, willful misconduct and breach of fundamental warranties.

W&I insurance



W&I insurance continues to be the most used buyer's remedy and is regaining ground in 2022

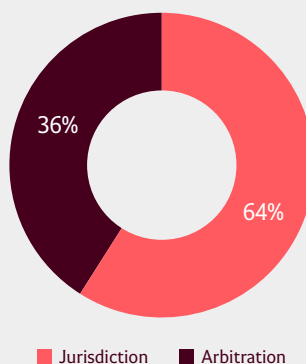
The use of arbitration is declining

Dispute resolution

The use of arbitration as a dispute resolution mechanism to resolve conflicts arising from agreements has been declining since 2018, with parties opting for this mechanism in only 36% of transactions carried out in 2021 and 2022.

The most common seat of arbitration continued to be Madrid. Arbitration proceedings were mostly managed by the International Court of Arbitration of the International Chamber of Commerce.

Dispute resolution



2022 Market trends at a glance

- | 1 Middle market transactions gained traction
- | 2 Secondary buyouts increased significantly
- | 3 When the fund acquires a majority shareholding, the fund buys 100% of the target company through an SPV and managers or founders reinvest in the buyer's SPV
- | 4 There were far fewer auctions
- | 5 Many deals required a condition precedent due to the need for regulatory approval
- | 6 2023 will be marked by the application of the new regulation on foreign subsidies that distort the internal market and the Spanish regulation implementing FDI screening
- | 7 Locked-box mechanism is consolidated again as the most used pricing mechanism
- | 8 Equity tickers continue to grow
- | 9 Working capital was the most used financial parameter for the post-closing adjustment
- | 10 An 18-month limitation period was once again the most used for business and tax warranties
- | 11 Excluding clean exits, the most used liability cap for business and tax warranties is between 20% and 30% of the purchase price
- | 12 The granting of business and tax warranties through a management warranty deed is becoming increasingly common
- | 13 There are far more anti-sandbagging clauses than pro-sandbagging clauses
- | 14 W&I insurance is the most used buyer's remedy
- | 15 The use of arbitration as a dispute resolution mechanism is declining

Spain
& Portugal

› Alicante › Barcelona › Bilbao
› Girona › Lisbon › Madrid › Málaga
› Palma de Mallorca › Porto
› San Sebastián › Seville › Valencia
› Vigo › Vitoria › Zaragoza

International

› Beijing › Bogotá › Brussels
› Casablanca* › Lima › London
› Luanda* › Maputo* › Mexico City
› New York › Santiago de Chile
› Shanghai

** in association with the respective local law firm*

www.cuatrecasas.com

