FLUIDRA S. A.

Corporate Finance

Final Project

During this Project we put together all the different chapters made through the subject.

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1. Introduction.

FLUIDRA SA is a company formed thanks to the fusion of several big corporations, like AstralPool España, Cepex Comercial, Master Riego and Certikin, all of them being leaders in their respective markets, being these markets all related to water treatment.

At the moment, Fluidra has become the leader in the global pool sector, with more than 5.500 employees, developing its activities in more than 45 countries and with the recent fusion with Zodiac that will allow the company to secure a stable growth in innovation and results.

At last we want to highlight this fusion with the American company Zodiac as it will affect in a huge measure the results and balances of the Catalan group.

2. Analysis of the firm's governance structure.

The company's structure of its board of directors goes like this:

2.1. Board of Directors.[1]

President: Sr. Eloi Planes Corts

CEO: Sr. Bruce Brooks

Vocal: Sr. Óscar Serra Duffo.

Honorific President: Sr. Joan Planes Vila.

Vocal: Sr. Gabriel López Escobar.

Vocal: Sr. Bernat Garrigós Castro.

Vocal: Sr. José Manuel Vargas Gómez.

[1] https://www.fluidra.com/uploads/media/default/0001/02/a001f4c25880fab8a29820a330d65461d66cfbfa.pdf All the information about the organization chart was taken from here.

Vocal: Sr. Richard J. Cathcart.

Vocal: Sr. Juan Ignacio Acha-Orbea Echeverría.

Vocal: Steven M. Langman.

Vocal: Sebastiá Mazella di Bosco.

Vocal: Jorge Valentín Constans.

Vocal: Bernardo Corbera Serra.

Secretary: Albert Collado Armengol.

Vicesecretary: Maximino Montero Lastres.

2.2. Management Advisory Committee.

President: Sr. Eloi Planes Corts.

CEO: Sr. Bruce Brooks.

CFO: Sr. Xavier Tintoré

General Director of North-America: Sr. Tory Franzen.

General Director of South-Europe and Asia: Sr. Carlos Franquesa.

General Operation Director: Sr. Joseph E. Linguadoca.

General Director of I+D: Sr. Keith McQueen.

Director of Production: Sr. Jaume Carol.

Global Director of Human Resources: Sr. Juanjo Masoliver.

2.3. Auditor Committee.

Presidente: Sr. Juan Ignacio Acha-Orbea Echeverría.

Vocal: Sr. Jorge Constans Fernandez.

Vocal: José Manuel Vargas Gómez.

Conclusions.

The first thing we wanted to highlight was the absence of women in these committees. We know it should make no difference in financial terms, but it is just surprising how difficult it is to find a woman in these levels of hierarchy.

Secondly, we believe that the members that form the board of directors are quite large in number. We believe that, as professor Damodaran said, the perfect number should be 10 members. In this case the company has 15 members, which could be excessive (even if 2 of them are only secretaries with no power of decision).

At last, the board of directors have some conflict of interest between the CEO and President, and the main function of this board, which is to control the operation of the company. While the CEO and its Managing committee decide what to do each day, it makes no sense to have both heads in both committees. On top of that, the previous president was Sr. Joan Planes Vila, which has family relations with the president of the board as well as the Managing Committee, Sr. Eloi Planes Corts.

However, the company claims there is no conflict of interest between the different members and the managing committee. We think this is a false claim as we can clearly see conflict of interest between them. We know this because we have compared the board of directors and managing team from **2007**[2] to **2018** (the latest available), and we can see how the members do not change or if they do, they "promote" people from the previous managing team to the board of directors. This is the example of the president, Sr. Eloi Planes Corts, which probably put together a board of directors of its past managing team when he was CEO and Sr. Joan Planes Vila, the actual honorific president, was president. We got to remark that the honorific president is now one of the main stockholders which gives him and his family most of the power in the firm, doing almost whatever he wants to it, this is why they are able to establish the members they wanted in the board of directors.

2 https://www.fluidra.com/uploads/media/default/0001/01/49813837fa292a31d2339dff114764cb19d26cd2.pdf Information of 2007 organization chart.

In order to solve this, we recommend that the investors stablish a obligatory rotation of the different board members or a maximum of years the members can be part of the board. This could prevent the group from creating an imperial CEO situation close to what it has now.

3. Calculation of the Cash-flow for the period 2015 to 2019.[3]

	2015	2016	2017	2018	2019
Free Cash Flow	36,95	46,90	36,15	26,6	133,44

The Free Cash Flow of Fluidra are rather stable during the first years of the company. During this time the company has a stable growth.

However, in 2017 things change as the growth stops. Clearly, we can see that this situation is ought to the increase in tax paid, increase in capital expenditure and decrease in change in Payables.

This could be translated as an effort from the company to secure a higher growth for the following years. As the Capital Expenditure increases it means that more projects are being made or the size of those are bigger. Also, we can see this effect in the future, with an increase in the Sales and other charts.

However, this increase is not materialized in the 2018 year as the fusion with the company Zodiac occurs. During this year, a lot of changes in the different accounting books of the company occur, affecting the Free Cash Flow as well. But what really affects the situation of the Free Cash Flow in this penultimate year is the Capital Expenditure once again. We can see how there is an increase in this, matter that could derive in an increase in the income for the following years. At last, we want to remark

[3] More information about the calculations are provided in the Excel

the change in payables, as we can see how the company increases the lends on payables in respect to the other years, meaning clients should pay them in the future.

This last claim is clearly seen in the year 2019 as the sales of the company, as well as the end Free Cash Flow increase much more than the previous years. Same happens with the payables, which have an incredible increase with respect to the previous years. Finally, we expect a return in a stabilize increase as we can see how the capital expenditure does not increase and there is not any special operation in the future.

4. Estimation of the Firm's cost of capital at the beginning of 2020.[4]

The Cost of Capital of the firm is of 6,6%. That means that the overall financing of the firm will cost the company a 6,6% in return.
The Weight representation is 59% for Equity and 41% for Debt. That means that the company finances more through Equity than Debt. However, we can see that this is one of the smallest differences between the weights during the overall period studied. We can see that the change in this tendency is made around 2017, where there is an increase investment for future activities as well as the end talks for the fusion with Zodiac.
On top of this, we can see how the Cost of Equity is higher than the Cost of Debt. This is obvious as the investors are left with the leftovers of the Net Income, while the creditors must be paid before reaching this chart.
In conclusion, the company will have to obtain a return of investment higher than 6,6% if it wants to be capable of paying back the cost of its financing.

5. Assessment of the firm's capital structure.

Break-Even EBIT.

ROA = 0,278%

Assets = 2.997,1

Break-Even EBIT = 8,3€

EBIT end 2019= 80,7€

[4] More information about the calculations are provided in the Excel

Evolution of the Capital Structure.[5]

	2015	2016	2017	2018	2019
Weight of Equity	59,48%	60,65%	75,87%	68,39%	62,38%
Weight of Debt	40,52%	39,35%	24,13%	31,61%	37,62%

Explanation.

Firstly, it is remarkable how Capital Structure changes so much during the years. We can see how there was a tendency towards the reliance on Equity rather than debt until the late stages of 2017 and the beginnings of 2018. During this period that goes from 2015 to mid-2018, we can see how the company increases the amount of debt progressively. However, the amount of Equity generated thanks to the Net Income results compensates for these increases and leaves the company with a higher reliance on Equity.

This situation radically changes in 2018, when the fusion with Zodiac occurs and the company gets an operating income of 7,4, contrasting massively from the previous year's operating income of 63. The need for finance made the company massively increase their amount of debt, something we can see on the Debt Issued in 2017 to finance the activities of 2018 in the Cash Flows. In contrast, this situation did not affect the Market Capitalization of the company. When all this happened, the company still increased its value reaching 2.735,1€ of overall value. This happens thanks to the positive perspectives of that the investors had about the company after the fusion with the company Zodiac[6].

[5] More information about the calculations are provided in the Excel
[6] https://www.elconfidencial.com/mercados/2017-11-06/fluidra-fusion-zodiac-gigante-mundial-piscinas-cotizacion-bolsa_1473015/ News on the increase on the price of the share when the fusion was announced

This shows the importance of **Positive Financial Leverage**. As we have calculated, the Break-Even EBIT was 8,3€, while the actual EBIT has been 80,7€. This situation leaves the company with the necessity to increase finance through debt in order to increase the value of the share, which in the end is increasing the wealth of the shareholders. This increase in Debt will be rentable until the Cost of Debt, which will keep increasing with the overall risk, is not bigger than the rentability that the company obtains from its activity.

<u>Situation per share</u>

	2015	2016	2017	2018	2019
EPS	0,1	0,2	0,3	-0,18	0,04
Price of the Share	3,4	3,88	7,11	10,24	8,68

We calculated the Earnings Per Share in order to see what we explained earlier is reaffirmed. Unfortunately, we can see how there is a decrease in the price of the share in 2019. This is because the data we got was from mid-2020. The reason for this decrease is because the company's value decreased. This was ought to bad results during 2019 and not giving any kind of dividend as a way of protection from this crisis.

However, on book value terms the Equity had almost no effect on its value, which confirms that the reason for the decrease in price and value of the company was founded on the expected results of the company, not the actual value of it.

Then, we can conclude that now the amount of Debt that the company is generating is helping the company to increase the value of the company. Then we can state that the cost of debt is assumable for the company as well as the financial risk it generates. On the other side, it is the business risk and the activity of the company which is worrying the stockholders, with a decrease in the expectation for future growth well founded as the results of 2019 were not as expected, the value of the firm is getting affected.

6. Assessment of the dividend policy of the firm.[7]

	2015	2016	2017	2018	2019
DPS	0,09	0,13	NA	NA	NA
Pay-out	51'6%	41,5%	48,3%	NA	NA
Dividend Yield	2,65%	3,35%	NA	NA	NA

It is striking that only the first two years pay dividends. This is due to several reasons. As can be seen in the table, the Dividend Per Share that is distributed has a constant growth trend. This aspect has the advantage that, in principle, if it is maintained, it will not go down and will always go up. The problem arises when, as is the case, the company cannot sustain that level of growth it and therefore stops paying for it. This can be seen in the following years, when the policy changes as there is a special operation in the way, the fusion with the American company Zodiac. On the following years the company decides on not to pay dividend, taking advantage on the current situation, when even with the change in policy the value of the company rises for the mere **information** content of a fusion with another leader of the industry.

On the other hand, with the information provided we could see the change in policy through the payout. This data gave us more evidence about the type of DPS the company was following. As can be seen in the table, the payout starts at 51. 6%, the highest during the period studied. However, as the years go by we can see that the payout drops and still the DPS increases, this means that the net income has grown. The problem arises when we approach the third and fourth year, which is when our company suffers a big structural change explained several times. Even though the payout has been reduced, there is no net income from where to pay dividends. We think this is ought to the increase in the need for investment during that year, something which we have demonstrated during the third point. At last, as the payout

[7] All the information is taken from the Excel

being the best indicator for the dividend policy, we can derive there was a desire to reduce it through a stable growth of the company, maintaining a growth in the cash used for shares. However, recent events prevented from giving more dividends.

Finally, the last index we have analyzed and had to calculate since it did not appear in the information provided by Fluidra is the dividend yield. This indicator gives us information about the relationship between the price and the dividend given by the company. It is the return that the share offers us considering what we pay for it. The fact is that in our company as it is obvious our profitability increases in the years in which we have information available. As no Dividend Per Share is paid in the following years no calculation can be made.

We recommend that the company returns on the payment of dividends so it can have some kind of protection for the upcoming crisis. Thanks to the dividends provided the dividend yield will maintain or increase, preventing the share from dropping too much.

7. <u>Conclusions.</u>

It is an interesting period we have studied. We have seen the changes of a huge corporation in terms of the financial books. What surprise us the most was the way how the policies change before the fusion with Zodiac. During this study we were able to appreciate how a company with no special actions behave and what are the results after this special behavior has happen.

At last, we have tried to make our recommendations in the different point so we could improve the situation of the company in order to reach the final objective of increasing the end value or, what is the same, the wealth of its stockholders.