# CAPSTONE PROJECT

Executive Summary

Project B1- Financial Analysis of publicly real estate companies in CEE



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## Purpose of this project

The purpose of this project was to come up with a research in two publicly listed real estate companies and to perform the company and the market analysis. The outcome would be to present the opportunity to investors by putting together a slide deck.

There were some certain triggers that I paid attention to in deciding the companies which would better serve the model for acquiring publicly listed real estate companies, SPAC. They should be traded at discount to their book value as that would attract investors, but the discount in their fair value should not indeed reflect a decline in their value, rather than a depression in the price due to the recent pandemic situation . A good debt ratio would be around 40-50%, making it less of a burden for investors to constrain their dividends and not satisfy their needs. Moreover, the market cap should not exceed 1 billion, the cash flow structure should be steady and the firm should embody potential to grow, improve and outperform in the market. A particular interest should be paid also to the shareholders structure and recent movements in shares withheld by shareholders should be captured in order to derive any further interest from them to sell the remaining shares.

## Introduction to SPAC

SPAC are formed by investors or investment banks to pursue deals in business sector through an initial public offering which would raise money to buy another company. The funds raised are needed to complete the acquisition or otherwise to return it to investors if SPAC is liquidated. SPAC companies, often times called blank check companies have no operations but their intention to go public is for the intention to acquire a company or merge with one. Once public offering has been declared prompt, SPAC will trade as units or common shares on the stock exchange.

Finding good and broken companies in the sense that help in better management of its business would guarantee growth, would make this special purpose acquisition vehicle highly attractive. For this purpose, this research was of a great interest and beneficiary to the client I worked with.

## Market Concentration of real estate companies

I started the research of companies by firstly choosing the market which is seen as very favorable by major of investors nowadays. Poland market seems very promising as there is happening a progressive urbanization, it has a strategic position between Eastern and Western Europe and the current low interest rates maintained by National Bank of Poland and low inflation are boosting the overall economy. Moreover, the construction cost savings are higher in Poland than in Germany, indicating a higher IRR for investors in real estate market. Poland had had one of biggest housing booms in Europe since 2008, because of its rapidly growing economy in the last years.

Number of residential dwellings completed for rent or sale are steadily increasing and so are the flats sold. Despite higher prices driven by high demand, sale of apartments is still high. Particular interest is also paid from institutional investors who prefer to rent out the apartments.

Commercial Real estate in Poland is promising as well due to high number of international brands which have entered the market and office market metrics show increase in rental year to year. There is still high vacancy rate for commercial real estate development in cities such as Wroclaw, Lodz and Cracow. The office market remains as the greatest investment market in 2019. The value of the transactions was more than 52% of the total investments in real estate market in Poland.

Moreover, Poland is one of the newest European country to introduce a REIT regime and become an EPRA member whose mission is to develop and promote European public real estate companies. The FTSE EPRA Nareit Global Real Estate Index constitutes around 500 companies and it provides big exposure to the real estate companies.

Due to its size, scale and high capitalization rates investors are attracted more on Polish real estate compared to countries in Western Europe.

## Reasons behind selection of the companies

First of all, I concentrated in the fundamentals of each company like profitability by looking at the revenue growth, gross margins, ROE, and net margins; debt ratio by looking at current ratio, debt to capital ratio and interest coverage ratio; earnings quality by looking at operating cash yield, accruals, days sales in inventory and days sales in receivables; trailing P/E, P/E relative to 5 years average and relative to WIG index.

The fundamentals in each of the companies should represent high chances of grow and strong foundations within the company.

Moreover, I paid special attention to what is in their balance sheet, what are the sources of their income and what is their free cash flow. A consolidated and clear breakdown of their portfolio was done and each of their main activities such as residential and commercial sector was looked upon. Detailed financials were looked for each of the main activities of the company in order to evaluate what is their most profitable business and where might be need for better improvement and perfection. Location and occupancy of their premises was also considered to make sound implications regarding the position of the company in the market. Statistics such as number of apartments sold, number of apartments on offer, delivered or signed acts upon were compared with previous years to indicate progress and legacy on the market.

Future triggers that influenced the decision to select those particular companies were dividends due to higher funds from operations and if in the future the real estate company has a solid bank land which will secure almost sure pre-sales and boosting the gross margins through construction. Moreover, if their balance sheet was strong meaning that disposal of their commercial objects in future would cover the current debts and if current commercial objects possessed high probability of revaluation gains, would influence the decision to choose them. Another trigger would be in cases when the company itself has published news that it is actively looking for strategic investors or industry partners that would allow the group to fully use its potential and increase the scale of its operations.

## What to improve in these companies?

As these companies are not perfect, it is advised to also highlight areas where further improvements is needed.

Examples for improvement in the companies are :

- A better business model for its main commercial objects.  Lower occupancy rate in one of their commercial building drives the need for revising the business model and recreating something else, being it turning the retail spaces into office spaces which have higher yields in Polish market.

- Change of the board of directors in cases when they are not considered to be very much experienced such as their average tenure is lower than 2 years.

- Revising the dividends payout ratio, in cases when operating cash flows are negative. This yet is a hot topic as lowering dividends might signal something wrong in the market and erode their fund-raising ability.

- The current pandemic has made companies revisit their targets for 2020/2021 and their number of units sold or introduced to the market will depend on the market situation.

## Key Learnings Outcomes

A thorough and detailed analysis should be conducted in choosing a company to invest on. It is of a great interest to look at all the sides of the history and getting to know also the areas where the company is not functioning very properly.

Yet finding good companies with a legacy in the market and well known, but with need to have improvements is particularly important in order to serve the long term benefit of Hussar & Co to create SPAC, the blank check company and after to make the names of the companies selected known to the public.