Growing Mergers and Acquisitions Trends in the Community Association Management Industry

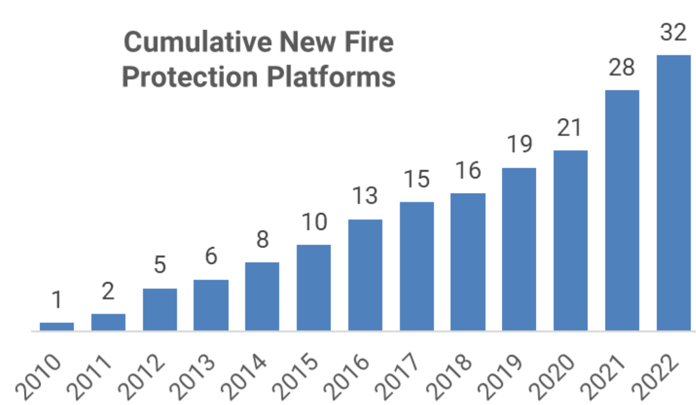
Well-funded consolidators are driving a dramatic rise in Mergers and Acquisition (or "M&A") activity within the Community Association Management Industry. An increasing number of these consolidators are being backed by Private Equity (or "PE") sponsors, who will partner with a well-positioned operating company and seek to drive growth through acquisitions and other channels. Several adjacent property services-related industries have previously been targeted for consolidation in recent years to the benefit of many business owners in those spaces, including landscaping, HVAC, janitorial services, security and disaster recovery, among others.

Why is this happening? Common characteristics that make these industries attractive targets for consolidation and PE firms include:

1. They are large markets comprised of many small companies;
2. Revenue tends to be highly recurring, which is great for predictability of cash flow; and
3. Services provided are generally critical to their customers.

Is consolidation beneficial to the industry? Industry consolidations have historically brought business owners in targeted industries the opportunity for life-changing financial outcomes because of industry-wide growth in valuation multiples driven by increased demand for acquisitions. Many of these business owners have further amplified their success by partnering with the acquirers and retaining a portion of their equity post-transaction for a "second bite of the apple" when the consolidators ultimately exit their investment.

Let's look at an example — the Fire Protection industry. Through 2022, there are at least 30 active PE backed consolidators (known as a "platform") in this industry alone relying heavily on acquisitions to drive growth. Annual M&A activity has increased dramatically, with the average number of deals over the past three years more than quadrupling versus the same measure from 10 years prior. As much as approximately 20% of the U.S. market has been acquired by consolidators through 2022. The proliferation of consolidators has increased competition for acquisition targets, which has in turn driven EBITDA-based valuation multiples higher across the board, even for relatively small companies. Five years ago, a quality, regional company in this space which would have reasonably expected an EBITDA valuation multiple of 8x-10x can now potentially sell for as high as 13x-16x, with some examples reaching the high-teens and even exceeding 20x.



Selected PE Platform Companies – Fire Protection

Source: Pitchbook. Only includes transactions registered in Pitchbook's database.

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Private equity firms seek to rapidly grow their platforms over a several year period with the goal of eventually liquidating the investment by either (i) selling to a strategic buyer or a larger consolidator/PE sponsor or (ii), with enough scale, taking the combined companies public via an IPO. Along the way, many firms take cash out through distributions to the ownership group. One such example of this in fire protection includes a familiar name to most in the Community Association Management industry – private equity firm Wafra Partners exited their investment in Century Fire Protection through a sale to FirstService.

Is the Community Association Management industry different? The investment characteristics of a Community Association Management company are attractive, possibly even more so than those adjacent industries mentioned previously due to the following favorable characteristics, among others:

1. Highly recurring core revenue base through monthly management fees;
2. Excellent customer retention rates;
3. Numerous opportunities to develop and grow ancillary revenue streams;
4. Extremely fragmented with 8,000-9,000 U.S.-based management companies; and
5. A relatively small sliver of market share being controlled by the top players.

In addition, PE firms are sitting on all-time high levels of "dry powder" approaching $2 trillion at the end of 2022 according to S&P, up 21% compared to the prior year. Industry roll-ups continue to be one of the most effective ways for these funds to invest. The Community Association Management industry is a near-perfect destination for a portion of that cash waiting to be deployed.

What is the current state of consolidation in the Community Association industry?

Historically, PE activity has been deterred due to difficulty finding Community Association Management companies with enough size or "scale" to warrant an initial acquisition to launch a platform. This is changing quickly. In 2022 alone, we have seen the acquisition of Texas-based RealManage by American Securities, an investment in Continuum Companies out of Philadelphia by CIVC Partners, as well as the launch of the CAM Collective out of Chicago backed by Taubman Capital. In CIVC's case, the firm had identified Community Association Management as a sector of interest several years ago and began a search for an appropriate initial platform acquisition. They abandoned their active search due to difficulty identifying a large enough number of potential targets until being introduced to Continuum in 2022. American Securities also went several years with interest in the space before eventually partnering with RealManage. In addition to these three notable new platforms, Fidelio Capital, owner of Sweden-based property manager Odevo, entered the U.S. market in late 2022 with the acquisitions of KW Property Management and Spectrum Association Management in the Florida and Texas markets. Several other private equity investors and family offices have also been actively searching for platforms in the space, and new private equity investors have taken notice of recent transactions and attractive industry dynamics. The number of funds actively targeting this space has grown rapidly, which will undoubtedly result in the formation of more platforms.

The buzz heading into 2023 is that Community Association Management is in the earlier phases of industry consolidation. Using the paths followed by other consolidating industries as a guide, business owners should reasonably expect a few things if this continues to play out:

1. Increasing volume of M&A activity;
2. An expansion of the active buyer pool;
3. Growth in valuation multiples as PE firms compete for new platforms and existing platforms compete for add-on acquisitions, and;
4. Shakeup of competitive landscape within the industry.

How can a business owner take advantage of consolidation?

Broadly speaking, consolidation will create opportunities that simply have not existed previously, which is positive for all business owners in the industry.

Business owners in the Community Association Management industry have two general paths they can follow to best take advantage of a consolidation wave.

1. Position yourself as a platform opportunity
2. Prepare for an eventual sale to a consolidator

The optimal path will vary for different business owners, and several factors need to be taken into account, including:

1. Owners' stage in life;
2. Appetite for risk and additional effort;
3. Size/maturity of the business;
4. Owners' long-term goals;
5. Specifics of the business (e.g., geography, customer mix, etc.); and
6. Financial resources/capacity.

These paths are not mutually exclusive. A business owner may choose to remain independent for a period while implementing strategies to maximize the value of the enterprise in the future. This could include becoming an acquirer themselves and pursuing acquisitions to build scale before pursuing their own transaction.

Alternatively, a business owner could partner with a PE firm or existing platform, taking some chips off the table near-term and retaining a minority ownership position and remaining a part of the day-to-day operations (possibly in an adjusted role). The goal in this case is an eventual full exit in the future when the company is larger and more valuable. All else equal, larger, more sophisticated companies will command higher valuations, which is a central pillar to what drives industry consolidations across sectors.

How can I best position myself as a platform?

A platform is the primary company in a particular industry into which a private equity firm makes an investment. The platform then serves as the vehicle to acquire and tuck in additional, often smaller companies, generating growth. It is usually of a large enough scale at the time of the initial investment to support a professional management team capable of serving as the nerve center of a much larger business in the future. The platform also needs to be large and profitable enough to command a valuation that will get a private equity investor's attention. A business does not need to deliver everything on a private equity firm's wish list, but one that does will usually be rewarded with the highest valuation. A few key attributes PE firms interested in this industry will look for are:

1. Adjusted EBIDTA of at least $3+ mil depending on other factors;
2. Solid management team who will remain with the business;
3. Quality reporting of financial and other key business metrics, and;
4. Consistent financial performance.

Business owners interested in pursuing this strategy can consult with an M&A advisor who has experience working with community association managers to evaluate their company, discuss what can be done to help build an attractive platform, and help to identify the PE partner who fits best with the business.

What steps can I take if I'm preparing to sell to a consolidator?

For business owners more interested in becoming acquired, preparation combined with a strategic market approach can have a meaningful impact on the outcome of what is often a once-in-a-lifetime transaction. A seller should define in advance what would be considered a successful outcome before approaching the market so that the marketing process can be designed to optimize for the sellers' goals and priorities. Examples include:

1. Any special timing considerations;
2. Desire to maximize cash versus retain equity;
3. Special considerations for employees/management;
4. Goal of retirement versus continuing to work; and
5. Articulating the importance of cultural fit with a potential partner.

A business preparing for a transaction should have processes in place to capture, analyze and logically present financial information and other Key Performance Indicators that help to facilitate evaluation by potential buyers. The due diligence process for a transaction will also require a long list of other critical details and documentation, including customer/vendor contracts, organizational documents, human resources information, tax, insurance and other categories which can be prepared for in advance. Inability to provide the information needed to evaluate an acquisition in a timely manner and in a comprehensive, reliable form can result in delays, lost value and failed transactions. This information should also be packaged in a way that presents the company in the best possible light.

Business owners can begin working with an experienced M&A advisor in the early stages to navigate this preparation phase, identify and engage with potential acquirers and form a story to be presented to the market. Once preparation is completed, the advisor will execute a process to approach buyers, solicit offers and negotiate proposals. The marketing process is intended to efficiently generate multiple options for business owners and create competitive tension among interested buyers ensuring that value is not being left on the table. A professional M&A advisor will have experience presenting similar companies in the way that is most attractive to buyers and will have market knowledge about the desires and characteristics of different industry buyers to ensure the right fit.

Accessing a broader network of potential buyers/investors and lessening the burden of a transaction process on owners and the management team is another benefit of discussing plans with an advisor early. A business owner should also consult in advance of a transaction with their accountants and personal financial advisors to assess estate and tax planning options. The sooner this step is taken, the more flexibility advisors will have to make any desired changes that may be beneficial.

Consolidation has already begun to accelerate in the Community Association Management industry and will create exciting new opportunities for many business owners over the next several years. Owners who recognize this trend and act early will stand to benefit the most. Preparation and a strong team of advisors are critical to ensuring that stakeholder value is maximized in any transaction, and business owners should be encouraged to begin these discussions even if a transaction is still several years away.

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About the Author

Thomas Hill is a Managing Director at Griffin Financial Group with over a decade of experience in sell-side M&A and capital raise advisory services across a broad range of industries. Most recently, Thomas advised community manager Continuum Companies in its transaction with CIVC Partners and has developed a strong understanding of the industry as well as an extensive network of potential strategic and Private Equity investors who have expressed interest in Community Association Management companies.

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Case Study – Continuum Companies

Company Overview

Continuum Companies ("Continuum" or "the Company"), based in Conshohocken, PA, is an integrated platform company providing property management and associated residential services to HOA communities. Beginning in 2014, the Company's founder and CEO, Marcus Mayo, acquired several property management businesses operating in the Philadelphia area. In 2019, Continuum was formed as a centralized platform to further consolidate the Company's end markets by effectively leveraging economies of scale and technology. Since then, Continuum has experienced rapid growth and has become one of the largest property management and residential service companies in the Mid-Atlantic, serving nearly 700 communities and more than 100,000 doors across its 12 brands.

Continuum Co.

has received investment from

CIVC PARTNERS

September 2022

Situation

After successfully scaling the business and building a market leading platform, the Company sought a private equity partner to help accelerate Continuum's ambitious acquisitive and organic growth strategies. With an extensive pipeline of acquisition targets and a goal of becoming the acquirer of choice in the HOA management and services space, access to additional capital and expertise was crucial for the execution of Continuum's goals. The Company sought a partner with a strong reputation that would help bolster growth, allow a significant amount of equity to be rolled to participate in the "second bite of the apple," and provide a liquidity event for some shareholders.

Solution

Continuum Companies selected and engaged Griffin as its exclusive investment banker to solicit interest from potential partners. Griffin worked with Continuum to identify and approach a highly targeted group of private equity investors and manage an expedited competitive process generating multiple proposals in a short period of time. The Company ultimately chose to partner with CIVC Partners, a private equity firm based in Chicago, IL. CIVC has extensive experience in the facilities services industry and has had tremendous success in accelerating growth for founder-owned companies. Marcus Mayo and other top management from Continuum will retain a significant equity stake in the business alongside CIVC.

For more information on this transaction, contact Thomas A. Hill, Managing Director, at 610.478.2034, R. Patrick Wood, Senior Vice President, at 717.255.7383, or Jeff R. Tallman, Associate, at 610.205.6013.