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Private Equity Challenge

Investment Committee Paper on Intercos

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Abstract

This paper presents an investment proposition developed strictly for academic purposes, studying the acquisition of Intercos through a leveraged buyout. Intercos is a leading provider of beauty outsourcing services. The group consistently invests in R&D, treating it as the primary driver of growth. Transitioning to a full-outsourcing business model, implementing operational improvements, and pursuing a market-consolidation strategy in South Korea can yield an IRR of 26% and a MoM of 3.2x. The group section of this report summarizes the Investment Committee Paper, while the individual sections thoroughly analyse value creation, valuation, capital structure, LBO, exit, and due diligence.

Key Words: Private Equity, Beauty Industry, LBO, Market Consolidation, Western Market Leader, Global, Outsourcing, Financial Analysis

Group Part

1. Company Overview

a. Company Profile

Intercos S.p.A. (ICOS:MI) is the global leader in outsourced make-up and the Western leader in outsourced beauty services. It is headquartered in Italy and was founded in 1972. Intercos has three business units: Make-up, Skincare and Hair & Body. Intercos is the innovation and manufacturing engine behind many global beauty brands.

Intercos differentiates itself from competitors through innovation in formulations and quality products. The Research and Development (R&D) department has been the driver of the group's development in production, formulations, and revenue growth. R&D remains a significant expense as a percentage of revenues, reflecting the positive growth in revenues.

The group is a global leader that emphasizes local trends. The company operates in America, Europe and Asia, through a network of 12 research centres, 16 production facilities and 16 commercial offices. It still holds most production facilities and sales in Europe, but it is expected to keep expanding in Asia and America.

b. Business Model

Intercos acts as a full-service partner that manages the entire process from R&D to formulation, production, packaging and delivery. This integrated model covers the entire value chain for beauty brands, positioning them as an Original Design Manufacturer (ODM). The products are then sold to multinationals, emerging brands or retailers with private labels. Intercos' clients ultimately sell their products to the final consumer.

The full outsourcing business model accounts for 75%-80% of revenues. It is the standard in all Make-up and most Skincare business units, with a limited growth in the Hair & Body business unit. The production process consists of six steps: Trend Scouting, Explanatory & Applied Research, Formulation & Design, Packaging Engineering, Manufacturing and Quality Control & Logistics.

The contract manufacturing business model accounts for the remaining 20%-25% of revenues. This model involves production based on customer formulas. The group receives the customer's technology and transfers it to its own facilities to manage the entire supply chain and production processes. Profitability is lower compared to the full outsourcing model, as Intercos does not own the Intellectual Property (IP) of the formula and has less pricing power. The production process consists of three steps: Packaging Engineering, Manufacturing and Quality Control & Logistics.

c. Diversification in Business Units

Make-up is the main business unit, accounting for nearly 60% of Intercos' revenues. As make-up is fully integrated into the full outsourcing business model, it achieves a significant EBITDA margin (13.4%). Make-up drives the group's revenue growth. Most raw materials and R&D expenses are allocated to this business unit, as this segment is most strongly driven by innovation. The rise in raw materials costs in the past two years impacted the EBITDA margin negatively. As the costs in raw materials are expected to stabilize, the Make-up EBITDA margin can raise.

Skincare is the business unit with the most stable revenues, as its revenue growth is consistent with Intercos' overall revenue growth. This business unit holds the highest EBITDA margin of the group (15.2%). Skincare developed with Korean R&D is the fastest-growing pillar with substantial innovation depth.

The acquisition of Cosmint in 2017 enabled Intercos to expand its business into the Hair & body segment. Hair & Body is the fastest-growing business unit for Intercos. Because most of this business unit is produced through contract manufacturing, it has the lowest EBITDA margin (12.6%).

d. Diversification in Geographies

Most of Intercos' revenues come from EMEA (Europe, Middle East and Africa), with a focus on Europe. EMEA is the core region, with strong relationships with multinationals. In 2024, EMEA accounted for 53% of revenues. The US leads revenues from the Americas, with a growing presence in Brazil. In 2024, this region accounted for 28% of revenues. Asia has had the highest revenue growth. Emerging Asian markets follow K-beauty trends, strengthening Intercos' presence in South Korea increases.

e. Diversification in Clients

Emerging Brands and Multinationals have generated the most revenue over the past 5 years for Intercos. Retailers account for a small percentage of revenues.

Emerging Brands have become increasingly crucial to Intercos over the years. In 2024, revenues from Emerging Brands accounted for the largest share of total revenue, outweighing Multinationals for the first time. They account for a fast-growing client base, including influencer and celebrity-led brands relying on full outsourcing for innovation, speed to market and expansion into Skincare and Hair & Body.

L'Oreal, Estée Lauder, Coty and Shiseido are the main Multinational clients. Multinational Brands have accounted for a significant share of revenue over the past 5 years. Global beauty groups leverage Intercos for high-complexity, regulatory-compliant and globally consistent products across prestige and mass channels.

Retailers are private-label and full-service partners with demand driven by short innovation cycles and rapid product turnover. In 2024, it represented only 7% of Intercos' revenues.

2. Market Overview

a. Beauty Market

The beauty industry started strong in Ancient Egypt and Ancient Greece, as people used natural minerals, plants and oils to enhance appearance and care for their bodies. It then evolved into a global, scalable market during the late 19th-century industrial revolution. The Industrial Revolution enabled large-scale cosmetic production and the rise of major brands such as L'Oréal. In the modern Era, this market has been characterized as a global growing market influenced by K-trends and social media. The 20th century brought innovation, mass advertising and scientific progress, transforming cosmetics into a global, technological-driven industry.

Skincare is the largest segment of the USD 405b beauty industry, accounting for 40% of the industry. Hair & Body consists of Fragrances and Hair Care. Fragrances is the fastest-growing segment, while Hair Care is a globally scalable, premium-positioned segment. Make-up is the fastest-growing segment in EMEA, supported by its high innovation potential.

There are four main industry drivers: emerging geographical markets; holistic approach to beauty; innovation and technology; and an active M&A landscape. Firstly, in countries such as India, it is expected to have a significant expansion in this industry, driven by strong economic outlooks, rising disposable income and younger, digital-savvy, value-driven consumers. Consumers are redefining beauty through wellness and self-care, embracing "skinification" through the use of multifunctional products that combine aesthetic and therapeutic needs. Companies have been investing heavily in R&D to develop biotechnological, natural and personalized formulations, leveraging nanotechnology and natural ingredients. There has been

a high level of activity in acquiring innovative brands to modernize portfolios and expand globally. These drivers enabled the market to grow at a 5.3% CAGR (compound annual growth rate) over the past 5 years. The beauty market is expected to grow at a 6.3% CAGR over the next 5 years.

b. Outsourcing Market

The outsourcing market is expected to outperform the beauty market by 1% to 1.6%, depending on the segment. Key players have been opting to move toward outsourcing for several reasons. Beauty companies have been refocusing on brand management and product marketing, leading to an increase in the outsourcing of upstream activities. Outsourcing manufacturers tend to anticipate trends more effectively and use innovative ingredients to meet rapidly changing consumer needs. Players struggle with pricing due to the increase in the number and variety of technologies used in production and the growing demand for product customization. New brands lack extensive know-how and production capacity to produce in-house and rely heavily on outsourcing.

The leading outsourcing key players are Koreans. The top 3 outsourcing key players consist of: Cosmax (South Korean), Intercos (Italian) and Kolmar Korea (South Korean). Each of the top 3 key players has revenues exceeding EUR 1b, whereas the remaining key players have revenues below EUR 400m in their cosmetics outsourcing business units. Most key players have their revenues locally focused, whereas Intercos has globalized revenues. Due to Intercos' diversification, it is the leading B2B beauty manufacturer worldwide, offering a comprehensive product portfolio.

3. Historic Financials

Intercos' revenues have grown constantly since 2021. It reached its peak growth in 2022 and 2023. Adjusted EBITDA kept growing constantly over the analysed period. EBIT Margin and Net Profit both peaked in 2023. The decrease in EBIT and Net Profit in 2024 is mainly due to ongoing inflation in raw material acquisition costs and ongoing IT operational expenses following a cyberattack. The inflation in raw materials is expected to stabilize, positively impacting next year's returns.

Assets have been growing steadily alongside revenue growth. Property, Plant and Equipment (PP&E) expanded over the last 5 years due to the expansion of production facilities in India and South Korea. Total assets and total equity continued to rise, driven by growth in their main accounts. Retained earnings are the Equity's main account. Due to the company's ability to retain inventory, net working capital has been rising over the years.

The majority of the production facilities are located in Europe. To enable the expansion to the Americas, it expanded its production and R&D facilities to the USA and Brazil. As emerging Asian markets follow K-beauty trends, it is strategic to acquire production facilities in East Asia. The latest expansion in production facilities has been in Asia to get closer to K-beauty trends.

4. Investment Thesis

Considering the Market Overview and Company Overview analysis. There were five main highlights that justify the viability of this investment.

Firstly, the main market highlight is that Intercos is inserted in a resilient, healthy market. It is a fast-paced, dynamic market characterized by resilient growth and robust projected growth. It is a highly fragmented market undergoing rapid geographic expansion. Additionally, there has been a shift toward outsourcing.

The remaining four highlights are regarding the company overview. It is a market leader in the make-up outsourcing market and the leading Western player in skincare outsourcing. Additionally, it is the most significant player, with a comprehensive business unit offering and long-standing client relationships. It has a strong M&A track record. In 2017, they acquired Cosmint, entering the Hair & Body business unit. Furthermore, Intercos is an innovation-driven firm used for new formulations. Over the last five years, raw materials costs in R&D accounted, on average, for 9% of R&D expenses. Intercos produces, on average, 1 500 new formulas per year, driven by a significant R&D budget. The final highlight is its diversification by geography, type of client and business unit, making it the most diversified global player in outsourcing beauty market. These highlights make Intercos a hidden gem in the beauty market.

There are three main value creation strategies that could improve revenue growth and EBITDA margin over the next three years.

The first two strategies concern the market and company overviews. EBITDA margin is expected to grow as bottom-line performance improves. By focusing on digitalization, automation and renegotiation of contracts between suppliers and customers, COGS and Operating Expenses will reduce as a % revenues, meaning that EBITDA margin would grow over the years. Revenues are expected to grow organically. Market revenues are expected to expand in MEA, Asia and America, while having a significant forecasted growth for the next five years. Besides that, Emerging Brands are growing in both MEA and Asia. Moreover, Indie American brands are looking to outsource to K-beauty products and other beauty products. As Emerging Brands became the most critical client segment, their growth is an excellent opportunity for Intercos' revenue growth.

Given that, Emerging Brands were the primary client segment in 2024, and their importance for Intercos has grown significantly since 2020 and with the Asian market expected to skyrocket,

Intercos is faced with a golden opportunity. C&C International is a company headquartered in South Korea. The South Korean market is innovation-driven and a global trend-setter. C&C International operates mainly in South Korea, but its largest export market is the USA, which is expected to have the highest CAGR in Indie Brands. Indie Brands and Asian Emerging Brands seek K-beauty outsourcing, enabling potential exponential growth for South Korean outsourcing players. Intercos has one production facility in China and another in South Korea, just like C&C International, allowing cost synergies in raw materials, personnel expenses and SG&A (selling, general and administrative), allowing for EBITDA margin improvements. As a result, Intercos should pursue market consolidation in South Korea, targeting C&C International.

5. Business Plan & Forecasts

The value creation plan is expected to generate a cumulative EBITDA margin increase of 4% over the business plan period. Gross profit margin expansion is primarily driven by stronger outsourcing revenues and accelerated growth in Emerging Brands. During the transition toward a full outsourcing business model, particularly within the Hair & Body segment, gross profit margin is projected to increase by 3% in 2025. In addition, the acquisition of C&C International and the associated operational and commercial synergies, aligned with this business model transition, are expected to contribute a further 2% increase in gross profit margin between 2026 and 2029.

The R&D function plays a central role in this strategy, as product and formulation innovation is a key enabler of the full outsourcing model and a critical driver of revenue growth and margin expansion. As a result, operating expense synergies arising from the acquisition are expected to impact only SG&A, while R&D expenditure is maintained to support innovation-led growth. Overall, these initiatives lead to an expected EBITDA CAGR of 17.8% between 2024 and 2029.

Organic growth is projected to account for 31% of EBITDA growth, M&A activity for 32% and margin expansion linked to the transition toward full outsourcing for the remaining 37%.

The acceleration in unlevered free cash flow further reinforces the growth strategy and supports the long-term value creation required to sustain the acquisition of C&C International. Intercos' corporate tax rate is assumed to remain constant at the Italian statutory rate, as any changes would depend on future legislative developments. As EBIT increases over the forecast period, cash taxes are expected to rise accordingly. Net working capital is projected to increase through 2029, reflecting higher activity levels, improved maintenance capacity and the strengthening of relationships with suppliers and customers.

Capital expenditures are expected to grow as a result of continued investment in automation, which is projected to drive productivity improvements. The acquisition of C&C International will also lead to a temporary increase in capex, with capex as a percentage of revenues peaking in the year of acquisition. Maintenance capex is expected to continue rising through 2029, while expansion capex is projected to decline after 2026, as C&C International represents the only planned acquisition. Unlevered free cash flow is therefore expected to decline only in the acquisition year, before resuming steady growth thereafter. As unlevered free cash flow grows at a faster pace than EBIT, the free cash flow conversion rate is expected to improve throughout the period, except for 2026. Overall, unlevered free cash flow is expected to grow at a CAGR of 39% between 2024 and 2029.

6. Capital Structure & Leveraged Buyout

To determine the appropriate capital structure, an entry valuation for Intercos was first established. The valuation was performed as of 31 December 2024 and relied on four complementary methodologies: Discounted Cash Flow (DCF), Exit Multiple, Trading Multiples and Transaction Multiples. These approaches were selected to combine intrinsic

valuation techniques with market-based benchmarks, ensuring a balanced assessment of Intercos' value.

With respect to intrinsic valuation, both the DCF and the Exit Multiple methods were applied. In both cases, free cash flows were forecast over the explicit business plan period and discounted using a weighted average cost of capital of 6.2%. Under the DCF approach, cash flows beyond the explicit forecast period were extrapolated using a terminal growth rate of 2%, consistent with long-term inflation expectations. This resulted in an implied EV/EBITDA multiple of 9.7x and an implied EV/Sales multiple of 1.0x. Under the Exit Multiple approach, the terminal value was instead estimated by assuming a sale of the company at the end of the explicit forecast period using an EV/EBITDA trading multiple of 10.8x. Discounting the resulting cash flows at the same WACC led to implied valuation multiples of 13.6x EV/EBITDA and 1.3x EV/Sales.

Relative valuation was assessed through both transaction and trading multiples. For transaction multiples, eight precedent M&A transactions involving targets with characteristics comparable to Intercos were analysed. The observed EV/EBITDA multiples ranged between 6.3x and 13.4x, while EV/Sales multiples ranged between 0.8x and 2.3x, reflecting differences in deal size, strategic rationale and business model.

Trading multiples were derived from a peer group composed of both ODM players and global B2C beauty companies, selected to reflect similarities in product scope and geographic exposure. Greater weight was assigned to ODM peers to better capture Intercos' outsourcing-focused business model. Based on this weighted peer set, EV EBITDA multiples ranged between 10.1x and 13.9x, with five-year average EV EBITDA multiples ranging between 10.5x and 13.3x. EV Sales multiples ranged between 1.3x and 2.3x. The five-year average EV

EBITDA multiple was also considered to smooth short-term market volatility and cyclical distortions.

For the final valuation, each method was assigned a different weight to reflect its reliability and relevance, with the DCF getting the highest emphasis. As a result, the computed EV/EBITDA is 10.9x and EV/Sales is 1.1x. Leading to an Enterprise Value of EUR 1 576.8m.

For the LBO, total proposed debt should be 5.75x EBITDA to keep a B2 rating profile. It will be divided in senior debt and junior debt. In senior debt, terms A, B and C will be used, as well as the CAPEX facility, providing extra liquidity to fund the C&C acquisition. Given the currently competitive credit market and B2 rating profile, these will be issued at par and have an interest rate of EURIBOR + 350 bps. The CAPEX facility has a committee fee of 30% of the margin and a drawdown period of 2 years. EUR 20 will be drawn down in 2025 and EUR 269m in 2026. For junior debt, a PIYC (Pay If You Can) second-lien loan will be used at 98.5% of par. When the company decides to pay in cash, an interest rate of EURIBOR + 550 bps will be applied. If the company chooses to PIK (Pay In Kind), the interest rate becomes EURIBOR + 625 bps. Regarding equity analysis, it will be segmented into Sweet Equity and Fixed Return Instrument (FRI). Regarding sweet equity, the management team and key executives will invest EUR11m, which corresponds to 2 years' salary, to get 10% of the ordinary shares. This ensures that they have a "skin in the game", motivating them to drive operational improvements and hit performance goals. FRI has a PIK element of 10%, to provide investors with a contractual fixed return, independently of the company's performance.

7. Returns

The investment's expected returns are assessed using Internal Rate of Return (IRR) and Money-on-Money Multiple (MoM), which together provide a balanced view of performance, as it captures both the speed and magnitude of value creation. Based on projections for a 2029

exit, institutional investors are expected to grow their EUR 817m investment to EUR 2,586m, delivering a 26% IRR and a 3.2x MoM over five years.

At exit, projected EBITDA of EUR 238m and a constant exit multiple imply an enterprise value of EUR 3,582m and total equity of EUR 2,745m. The Sweet Equity structure effectively aligns management and investor interests: management acquires 10% of ordinary equity for EUR 11m, which could be worth EUR 159m at exit, with more modest but still meaningful outcomes under downside scenarios. Value creation is driven primarily by revenue growth (55.3%) and EBITDA margin improvement (45%), supported by outsourcing trends, inorganic growth, and operational efficiencies. Strategic initiatives—particularly market consolidation and operational improvements—account for the majority of incremental value creation, underscoring that returns are driven by sustainable strategic execution rather than financial engineering.

8. Exit and Due Diligence

For Intercos, there are three likely exit strategies: IPO (Initial Public Offering), Strategic Sale and Secondary Buyout.

An IPO is when a private company becomes a public company by offering a portion of its ownership to investors through newly issued shares. As it is a European group, its IPO should be on Euronext.

Strategic sale is when a private company sells directly to a competitor or client, aiming to vertically integrate, unlocking operational synergies and enabling an expanded product mix.

Secondary buyout is when the company is sold to another private equity fund, as the market is expected to remain attractive and with potential to implement alternative value-added strategies.

As a result, the best exit strategy for Intercos is IPO, given its likelihood and high valuation.

When it comes to due diligence, we highlight five key areas for further analysis: commercial, operational, financial, legal and IT. Regarding commercial due diligence, there are three main focuses: market analysis, competitors and customers. Regarding operational due diligence, there are three analyzed focuses: supply chain, production capacity and innovation capability. Financial due diligence has its main focus on financial statements. Legal due diligence focuses on tax and local regulations. Lastly, IT due diligence focuses on admin systems and cybersecurity.

Individual Assignment Rodrigo Coelho: Exit and Due Diligence

1. Preamble

The individual report is centered on a portion of my total contribution to the Intercos Investment Committee Paper. The topics analyzed in this individual assignment will be the exit strategy options and their process, and due diligence. For the due diligence, the key areas will be analyzed in depth, whereas the exit strategies will be explored from the perspective of what should be the best strategy for Intercos.

2. Private Equity Exit Process

Identifying potential buyers with appropriate size industry expertise and established market presence becomes the main strategic priority, as private equity funds prepare to divest their stakes in portfolio companies, in this case, Intercos. An exit strategy is a defined plan for divesting or relinquishing a strategic position at a specified time to maximize return. It is a strong pillar of successful investments, making it an important section to go over while analysing the acquisition of a target by a private equity firm. Consequently, it is essential to include the main potential exits that can be associated with Intercos as part of the analysis of this Investment Committee Paper. If a private equity fund holds its position for too long, it risks losing investment returns, which increases the impact this step has on the Investments Committee Paper. The fund needs to consider the strategic approaches they could opt for and why they should divest in the company they acquired by the exit year (2029).

In order to approach an optimal exit, there are several topics to consider. Firstly, the financial motives leading to the exit strategy should be analyzed deeply. The main question associated with this topic is: At what valuation of this portfolio company should the fund be willing to sell, while meeting its own expectations regarding the target return and securing additional capital

for further investments in other targets? Secondly, the market conditions need to be thoroughly analyzed. Specifically, macro conditions such as inflation result in the rise of interest rates. This implies a slow and deal-making process of the sale of the portfolio company, which may lead to a sale at a discount. To analyze the market conditions thoroughly, both macroeconomics and market conditions need to be studied. Besides that, the negotiations and deal structuring should be planned to result in an effective exit strategy. PE firms should use their own industry insights and refer to industry analysts and networking relations, resources and capabilities, to conduct a careful due diligence and evaluation of potential target buyers. The three analyzed exit strategies will be IPO, strategic sale and secondary buyout. Each strategy will have different potential target buyers and associated advantages and disadvantages.

a. IPO

An IPO occurs when a privately held company lists its shares on a public stock exchange. It is possible to list only a portion of shares or the entire equity stake, as the exit can be gradual if desired. The shares should be issued in the regional stock market. For example, a corporation in South Korea would issue its shares on KOSDAQ. If an Italian corporation goes public, its shares would be issued on Euronext Milan. This transaction is heavily dependent on prevailing market conditions. In bull markets, characterized by strong investor confidence and robust demand, companies tend to reach higher valuations and increased activity. On the other hand, in bear markets, high uncertainty tends to drive conservative pricing.

There are two main associated advantages. Firstly, it has higher market liquidity and opportunities for a broad range of investors. There is a broad range of potential buyers as the shares would be available to the public, leading to a higher price flexibility. This characteristic allows higher market liquidity, as it is forecasted that Intercos will keep growing with healthy financial statements. The other main advantage would be that the capital raised through the IPO

may be used to repay debt, as well as finance company activities such as R&D and CAPEX. As R&D is an important driver of growth in the industry, Intercos has established a financing mechanism to enable reinvestment in that department. Besides that, repaying debt allows the company to achieve healthy financial statements, supported by the company's growth.

On the other hand, the associated disadvantage is that it brings substantial extra costs, from underwriting to expanded reported obligations, with the reporting burden becoming a permanent recurring expense. The costs are associated with the regular quarterly report submission. It will have associated costs in gathering accurate information regarding the company's ongoing operations for each quarter. These reports allow investors to have a better understanding of its profitability growth and revenue growth. It also accounts for a potential seasonality analysis.

b. Strategic Sale

Strategic sale occurs when a privately held company is sold directly to a competitor or to a client seeking vertical integration. It aims to unlock operational synergies and broaden its product mix, enhancing overall efficiency. By selling it to a competitor, it must sell to a bigger player, empowering that outsourcing player's market position, in this case. If the sale is to a client, it needs to be a transaction that will result in the client's profitability growth and long-term strategic goals. This exit strategy is usually used by relatively small players in growing markets.

There are two main advantages associated with this exit strategy. Firstly, there is a potential for a higher exit valuation given the premium paid by the acquirer for the possible synergies and strategic fit. Regarding the synergies' evaluation, there is a possibility of overvaluing the target, which could bring some upside to the seller. Industries that are reliant on the R&D department may have revenue synergies over the years if R&D and formulas are shared. Secondly, given

the low concentration of the beauty market, there is much room for consolidation. This allows smooth negotiation among the involved parties. Outsourcing has a successful M&A track record, meaning that this exit strategy would be plausible.

On the other hand, its main disadvantage is that when trying to negotiate terms and deal structuring, it can lead to several rounds of renegotiation. Competitors usually have harder negotiating terms as they don't have the same ability to scale their revenues as clients. The transaction will only go through if the competitor/client has enough financial leverage to acquire its target. If the negotiating terms are not optimal for both parties, the deal should not proceed.

c. Secondary Buyout

Secondary buyouts account for 48% of private equity exits. A secondary buyout occurs when a portfolio company is sold to another private equity fund or institutional investors. This means that the portfolio company would be transferred to a private equity fund with deeper expertise in the market into which the portfolio company is inserted. This strategy is used when there is an opportunity for substantial continuous exponential long-term growth, as the buyer would stimulate EBITDA growth, driven by its value creation strategies.

There are two main advantages associated with this strategy. Firstly, it offers faster execution, quicker liquidity and lower transaction complexity, with PE buyers generally more flexible on deal structure. As the client would also be a private equity fund or investment identity, the deal structuring and valuation would be linear and easily determined by reaching a similar fair value for the transaction. The fast-negotiating process allows quick liquidity. Secondly, it is often supported by the management team due to financial incentives, as it would be a fast process, due to the common understanding of the portfolio company's returns.

On the other hand, its key disadvantage is that it typically delivers a lower valuation, as financial sponsors need room for their own returns. This is driven by the core assumption that private equity funds are driven by exponential returns. If they acquire a target at a discount, their returns will probably be higher. This leads to a less aggressive value creation strategy from the buyer.

d. Best exit scenario for Intercos

IPO is the most reasonable exit strategy as it's the most organic strategy. Besides that, it is the most plausible exit strategy, as Korean players or players with significant activity in South Korea tend to go public while continuing to grow healthily. As Intercos production operations are expected to keep growing in South Korea, it may be an accurate exit strategy in the exit year. Strategic sale does not look as likely as IPO, as Intercos is already a Top 3 outsourcer in the beauty market. There is only one player with higher outsourcing revenues than Intercos. That player still does not have enough financial leverage to acquire a group of the size of the portfolio company. B2C players need outsourcing suppliers in order to achieve economies of scale. This means that, by acquiring an outsourcer, the B2C players would drop their profitability and their profit margins. As for the secondary buyout strategy, as it is not a common strategy in the beauty outsourcing market, it is difficult to account for success cases. This means that there would be a considerable valuation, but the lack of occurrence makes it harder to evaluate it as an exit strategy.

3. Due Diligence

Due diligence is the process through which private equity firms assess whether the deals are worth pursuing. It assesses the portfolio company's financial, legal, operational, management incidents and industry dynamics, to assess risks and to identify value-creation opportunities. This analysis is presented before a private equity firm commits to an investment or acquisition of a target company. If it is efficiently done, it would minimize the risks and maximize the value

for the private equity firm. The key steps for a thorough due diligence include industry research, detailed financial analysis and operational review (including cost structure), legal and regulatory assessments and returns expectations. It involves a thorough evaluation of the target company, ensuring that there are no hidden liabilities and that the company is positioned for sustainable future growth.

Due diligence should be focused on several different areas. Commercial due diligence focuses on market conditions. Operational due diligence focuses on operating expenses and COGS. Financial due diligence explores potential risks regarding financial statements. Legal due diligence focuses on local regulations and taxes. IT due diligence considers administrative services and cybersecurity. Most private equity firms use a combination of internal resources with external consultant advisors to efficiently conduct due diligence.

a. Commercial Due Diligence

Regarding commercial due diligence, the fund should ask consultants to provide analyst reports, corroborating forecasted market growth. These analyst reports would also enable a deep analysis of potential risks and opportunities.

Commercial due diligence gathers risks regarding three main areas: market analysis, competitors and customers. The market analysis area covers essentially growth drivers and trends. Beauty trends and outsourcing trends are aligned with Intercos' growth drivers. As K-beauty trends grow globally, their associated risks should be thoroughly studied. Western Indie Beauty Brands are reaching out to Korean beauty outsources to get access to quality products and be on par with K-beauty trends. This could mean that the growth of outsourcing players with facilities in South Korea would benefit from this phenomenon. Besides that, emerging Asian markets are also following K-beauty trends. McKinsey & Company should be chosen to act as an advisor to help answer the following questions regarding forecasted market growth

from South Korean products: How much more should the K-beauty market grow than its domestic market is expected to? As K-beauty is heavily associated with Skincare and Make-up, should only these two segments account for an exponential potential growth? Another concern regarding market analysis would be understanding how long outsourcing is expected to outperform the beauty market. In the past few years, it has outperformed the beauty market by over 1p.p. to 1.6p.p. and is expected to keep outperforming. Regarding this topic, Brain & Company should be chosen to act as an advisor to help answer the following main questions: Is the outperformance growing? Will the outperformance slow down, and potentially how? When it comes to competitors, an analysis of key market characteristics should be conducted. It is known that the two main competitor dominate the Asian market and are keeping an eye on the American market, as they have expanded their geographical revenues to America. For that reason, it's necessary to assess its competitors' growth-associated threats. Regarding customers, to keep stable sources of revenue, the client base should be even more diversified, as it may be a red flag to have 50% of the revenues coming from the top 10 clients. As the huge weight on the Top 10 clients can not be diversified instantly, the contracts should be reviewed to ensure that those Top 10 clients keep buying products from Intercos on a large scale. BCG should be chosen to act as an advisor to mitigate potential risks.

b. Operational Due Diligence

Regarding operational due diligence, there will be a higher focus on supply chain, production capacity and innovation capabilities. The goal is to assess the efficiency of Intercos in these three areas. There should be an in-depth assessment of functional expertise, organizational structure and supply chain relationships. For this key area, confirmatory due diligence should be used to obtain a more realistic result.

Regarding the supply chain, contracts with suppliers should be reviewed to secure suppliers' relationships. Besides that, there should be a diversification of suppliers, allowing Intercos to have a higher bargaining power, while not being dependent on a few suppliers. This way, it should be easier to mitigate price fluctuations. Yet if there is a global inflationary crisis, most of the raw materials are expected to increase in cost. These risks should be monitored with the help of PwC as an advisor. When it comes to production capacity, the key facilities should be thoroughly inspected to validate potential synergies and operational improvements. Productivity KPIs should be analyzed with PwC's help. If the KPIs are accurate, the synergies may be higher than expected, whereas if the production facilities need to be renovated, production synergies will not be as effective. As the R&D department is a key driver of outsourcing players' growth, innovation capabilities should not be overlooked. The patent portfolio should be analyzed and expanded for key products. In addition, there should be an analysis of its key personnel. To conduct an efficient analysis, Intercos should choose Kearney as an advisor. As a result, employee complaints and key patents near expiration dates should be managed through an ongoing process.

c. Financial Due Diligence

Financial due diligence approaches the financial statements. It has to do with cost evolution and operational margins to determine a comprehensive valuation on financial health and potential risks. It also includes examining the balance sheet, income statement and cash flow statements for the past 5 years, with emphasis on net debt, operational margin and profit margin. To conduct a better analysis, Deloitte should be chosen as an advisor.

There should be a careful analysis regarding NWC and CAPEX to understand capitalized accounts. With the help of a consultant advisor, the monitoring of Intercos over the analyzed period may cut down discrepancies between its real growth and the group's expectations. This

could impact the portfolio company's growth expectations severely. The growth may be higher than the conservative expectations of growth at the same rate as the market, as long as there is a consistent investment in R&D. Otherwise, if there is a sudden shift in global trends impacting a change in raw materials, the growth will eventually slow down.

d. Legal Due Diligence

The main goal of legal due diligence is to uncover any legal issues or other potential risks associated with the acquisition of the target. For that, it is needed to analyze EU legislation, USA and Brazilian legislation, and eastern Asian legislation (India, China, South Korea and Japan). As it is aimed to increase operations and expand sales in Asia, focusing on South Korea, there should be a thorough analysis of Asian local regulations in China and South Korea. Besides that, this key area should also focus on contracts with its suppliers and customers. Legal due diligence should be conducted by Deloitte.

The two main areas analyzed would be tax and local regulation. Regarding taxes, the core tax rate should be the Italian corporate tax rate, as Intercos is headquartered in Italy. Tax changes in overseas companies also influence the tax rate paid by Intercos. Corporate tax rates in South Korea are dependent on the size of the company, but outsourcers tend to have financial benefits in some regions in China and in South Korea. The other countries in which Intercos has operations are expected to remain constant over the years. South Korean labor regulation may help Intercos achieve optimal synergies when acquiring C&C International. This may have a heavy impact on ongoing litigations. Regulations regarding sustainability may increase costs in raw materials, for example, Intercos uses Malaysian palm oil as its sustainable, because it is a member of RSPO. Another raw material that implicates sustainable regulation is Indian mica. If there are other used materials included in new sustainability standards, Intercos will probably use them through a sustainable supply.

e. IT Due Diligence

IT is a crucial department for corporations in the XXI century. Intercos suffered from a cyber-attack in 2024, which negatively affected operating expenses. As a result, there should be a continuous investment in IT. Besides that, an efficient IT investment allows automation. Automation is usually associated with productivity. This means that by increasing the automation, the productivity may be increased, as through that process, personnel expenses will be reduced.

The two main focuses in this key area are cybersecurity and administrative systems. The technology literacy of the group needs to be studied. Leading to the following questions: Does Intercos have low technological literacy? Can the group and their target adapt efficiently to a single complete IT system? These questions will allow us to better evaluate the IT impact in this industry. If its quality is aligned with R&D performance, it is expected to be an efficient method, improving operational efficiency, especially in production and administrative processes. A better IT system is expected to allow faster general and administrative tasks, leading to a more efficient SG&A performance. As a result, it is well applied, which will impact the operating result positively. The only associated risk is to assess how to estimate realistic cost efficiency. The cyber-attack slowed Intercos' operations; by reinforcing the cybersecurity systems, its main goal is to prevent future cyber-attacks. It will be a preventive investment as its main goal is not to raise value. The main goal of this investment is to try to mitigate potential operations slowing down, meaning that operations may remain efficient for a few years, leading to constant growth.

4. Conclusion

All in all, due diligence analysis is crucial to deciding whether a private equity fund should go through the acquisition of a certain target company or not. In this case, the targeted company is

Intercos. The analysis is based on risk assessment and information that can be attained with consultant advisors. On the other hand, the exit strategy is also a crucial step in the Investment Committee Paper, as this strategy could still increase returns. All exit strategies should be analyzed from the perspective of their likelihood given the industry the portfolio company is inserted in and its intrinsic valuation to the private equity fund.

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Glossary

AI	Artificial Intelligence
BCG	Boston Consulting Group
CAGR	Compound Annual Growth Rate
CAPEX	Capital Expenditures
COGS	Cost of Goods Sold
DCF	Discounted Cash Flow
EBIT	Earnings Before Interest and Taxes
EBITDA	Earnings Before Interest, Taxes, Depreciation and Amortization
EM	Entry Multiple
EMEA	Europe, Middle East and Africa
EU	European Union
EUR	Euro
EURIBOR	Euro Interbank Offered Rate
EV	Enterprise Value
FCF	Free Cash Flow
FRI	Fixed Return Instrument
ICOS	Intercos ticker
IP	Intellectual Property
IPO	Initial Public Offering
IRR	Internal Rate of Return
IT	Information Technology

KPI	Key Performance Indicator
LBO	Leveraged Buyout
LLC	Limited Liability Company
MEA	Middle East and Africa
MI	Euronext Milan exchange code
NPV	Net Present Value
NWC	Net Working Capital
ODM	Original Design Manufacturer
OPEX	Operating Expenses
PE	Private Equity
PIK	Pay In Kind
PIYC	Pay If You Can
PP&E	Property, Plant and Equipment
R&D	Research and Development
ROIC	Return on Invested Capital
RSPO	Roundtable on Sustainable Palm Oil
SG&A	Selling, General and Administrative
TV	Transaction Value
UFCF	Unlevered Free Cash Flow
USA	United States of America
USD	United States Dollar
WACC	Weighted Average Cost of Capital