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# MEXICO BUCKS SLOW M&A AND IPO GROWTH PREDICTIONS FOR LATAM

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Mexico will drive growth in Latin America over the next five years with the fourth-highest predicted increase worldwide in the number and value of mergers and acquisitions, according to a global M&A and IPO forecast conducted by economic analysts Oxford Economics – while Argentina, Brazil, Chile, Colombia and Peru are predicted to see slower rates of growth in both areas.

Commissioned by US firm Baker & McKenzie LLP, the survey based its predictions on completed domestic and cross-border transactions, and included deals of any value that were reported by Reutersin 2014. The predictions account for cyclical and structural variables between countries, such as freedom of trade, stock market capitalisation and legal and property rights in each jurisdiction.

Based on the data, Oxford Economics predicts Mexico will have the fourth-highest growth in mergers and acquisitions globally by 2020. From 150 transactions worth US$11.7 billion in 2014, deals will increase in both number and value to reach 246 worth US$26.2 billion in 2017. The data also suggests that the value of IPOs by Mexican companies will remain at a fairly steady value of between US$1-2 billion over the five-year period.

Many credit the predicted M&A growth in Mexico to the recent opening of the country's energy sector to private companies, which saw the Mexican government dismantle Pemex's 75-year monopoly through legislative reform passed last year. Partner Jorge Ruiz at Baker & McKenzie (Mexico) argues that the economy has yet to fully react to these reforms, and that from 2016 onwards they will drive further growth. "It is just a matter of time," he says. "The next five years seem to be very favourable for Mexico."

Others argue the reforms have already begun to have a positive effect on the economy. Pointing to the higher number and value of transactions in 2015 compared to the previous year, Creel,

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García-Cuéllar, Aiza y Enriquez SC partner Jean Michel Enriquez says this trend has been helped by the weak peso against the dollar, which has made local companies attractive acquisition targets for foreign buyers – particularly in the manufacturing sector. Mexico's manufacturing sector has seen double-digit growth for several years, he explains, because growth in the US market has a knock-on effect on Mexico. For example, earlier this month Renault-Nissan entered a 50/50 joint venture with Daimler to build and run a US$1.3 billion car plant in Mexico, to take advantage of Mexican skilled labour and low costs to sell cars in the US market. "The value of the peso will make this continue," says Enriquez.

By contrast, Argentina is not predicted to enjoy the same level of growth in mergers and acquisitions and IPOs. The survey estimates that the value of M&As will plummet from nearly US$8 billion in 2014 to half a billion this year, before increasing to US$2.5 billion in 2020. IPO growth is far healthier, rising from US$15 million in 2014 to a predicted US$162.4 million within five years.

Although the figures are positive in the medium term, the upcoming presidential election is making investors more cautious this year as they wait for a more business-friendly administration. Partner Jorge Luis Pérez Alati at Pérez Alati, Grondona, Benites, Arntsen & Martínez de Hoz (h) agrees that the number of IPOs and mergers and acquisitions in Argentina will pick up by 2016, and argues that whoever wins the election will promote an environment more conducive to business development than the current administration. "A good skipper will be able to generate that business environment needed to attract investments and open up capital markets," he says.

However, Pablo Viñals Blake, partner at Marval, O'Farrell & Mairal, warns that whoever wins the presidential elections must make dealing with the country's holdout creditors a priority. Argentina owes its holdout creditors US$7.1 billion, after a recent ruling by US judge Thomas Griesa gave equal rights to other bondholders as he gave to US hedge fund NML Capital, meaning Argentina must pay both before it can resume interest payments. "If the next government does not begin some kind of negotiations, Argentina will find it difficult to have access to international financing markets. YPF is one of the few local companies with access to the international markets, but [single] offerings of US$1 billion or US$2 billion are not relevant in the long term," he says, adding the country will need many more large placements if it wants to see higher economic growth. The state-run

oil company issued US$1.5 billion worth of bonds in April.

In Brazil, the survey suggests that the number and value of M&As will drop substantially this year, before rising again in 2016. The rumbling Petrobras scandal and accusations of financial impropriety by the Rousseff administration has led to a plummeting in value of the real in the past year and has led to investor pessimism, discouraging them from acquiring companies or launching IPOs. Alberto Mori, partner at Trench, Rossi e Watanabe Advogados (in cooperation with Baker & McKenzie), says domestic buyers are wary of taking out expensive, high-interest bank loans to fund expansion projects, contributing to the fall in mergers and acquisitions and IPOs, but that foreign nationals eager to take advantage of Brazil's weakened economy are snapping up distressed assets, meaning M&A activity remains buoyant.

Driven by a decelerating economy, the ongoing corruption scandal and restricted access to credit lines, several Brazilian companies are selling off assets to pay debts or simplify their portfolios. Lawyers believe the statistics underestimate the number and value of M&As because of such divestments. For example, Petrobras's recently announced sale of 20 per cent of its subsidiary BR Distribuidora over the next three years could raise US$58 billion. "That operation alone is able to break any [M&A] predictions made for the period," notes partner Carlos Fernando Siqueira Castro at Siqueira Castro Advogados.

IPOs in Brazil are expected to increase in value this year and next, from US$172 million in 2014 to US$1.03 billion in 2016. Partner Pedro Whitaker de Souza at Mattos Filho, Veiga Filho, Marrey Jr e Quiroga Advogados says this is due to a number of IPOs from state-owned or mixed-capital companies launching by the end of the year, as the government attempts to plug this year's fiscal

deficit.

Despite political tensions and Brazil's hefty fiscal deficit, lawyers are confident that there are still reasons for investors to come to Brazil. "A country as big as Brazil decelerates like a large ship, and [the same is true] while accelerating," says Whitaker de Souza. "Brazil will always have 200 million potential consumers and a big GDP. That alone will keep the country as an interesting place for investments."

Meanwhile in Chile, the figures predict the number of mergers and

acquisitions to increase steadily until 2020, although their combined value is predicted to fall from US$13.5 billion in 2014 to US$4.2 billion in 2015. The country is not predicted to see an end to its year-long IPO drought in 2015.

Carey partner Francisco Ugarte says the high value of M&A transactions in 2014 was anomalous, fuelled by large acquisitions such as CorpBanca's merger with Itaú Unibanco for US$2.2 billion. Ugarte does not believe the country will see values as high as last year in 2015 and is pessimistic about the entire region. "Analysts project a 36 per cent decrease in the total M&A deals in [Latin America] compared to the first quarter of 2014. Chile is no exception."

Macarena Letelier, a senior associate at Morales & Besa, cites two key elements that could impact growth in Chile over the next three years. Firstly, the devaluation of the Chilean peso, from 480 pesos to the dollar in 2013 to 652 to the dollar this month, which could fuel a higher number of acquisitions by foreign companies but at a lower value. Secondly, Letelier argues government reforms in the tax and labour sectors have created a climate of uncertainty in Chile. "Local investors are paralysed until they have clarified the new regulations," she insists.

In Colombia, the study anticipates the number and value of mergers and acquisitions will remain fairly steady throughout 2016. The data shows that like Chile, there were no IPOs in 2014, and that there will be no IPOs this year.

Baker & McKenzie (Colombia) partner Jaime Trujillo says an economic slowdown in Colombia, combined with falling global oil prices and competition from more attractive developed markets in the US and Europe recovering from the financial crisis of 2008, is limiting the numbers of mergers, acquisitions and IPOs. However, Trujillo says there are elements of the Colombian economy to be optimistic about over the next five years and points to the devaluation of the peso, which is making Colombia more attractive to foreign investors; the launch of the government's fourth-generation infrastructure programme, which is expected to boost economic growth; and progress in peace talks with FARC, which has increased investor confidence and security.

Neighbouring Peru is not predicted to see an IPO for the next five years. M&A volume is expected to rise every year from 2014 to 2020,

although the value will drop sharply from US$17.3 billion in 2014 to US$1.9 billion this year due to the distorting effect of the record-breaking purchase of the Las Bambas copper mine by a Chinese consortium in April last year.

Partner Jorge Ossio at Estudio Echecopar member firm of Baker & McKenzie International, admits that the Peruvian fishing industry has suffered recently, but he says that health care, retail, education and agriculture remain attractive for investors. An investor switch away from emerging markets to more stable and developed US and European economies has negatively affected the Peruvian economy.

Partner Jean Paul Chabaneix at Rodrigo, Elías & Medrano Abogados agrees with Ossio, highlighting the Chinese economic slowdown and – crucially for a mining country – the drop in the price of metals as leading a decrease in mergers and acquisitions. Of the large mining protests against the Tia Maria copper project, which has dented investor confidence in Peru's mining industry, Chabaneix notes that the government has so far "not been successful in solving the political and social issues [surrounding] the natural resources industry" and says it will have to resolve these issues if it wants to boost investment in the sector.

Both Ossio and Chabaneix agree that, for now, Peru remains some way behind some of its neighbours in terms of IPOs, because Peruvian companies generally are not large enough to launch international offerings worth hundreds of millions of dollars. But both lawyers are positive about Peru's economic outlook in the next five years. Chabaneix says health, education and the service sector will drive growth, although says the country will not see the higher GDP rate it enjoyed prior to 2014. Ossio points to six key factors, which he believes will drive growth: all presidential candidates for next year's general election have adopted a positive approach to the economy; Peru's GDP growth continues to be one of the highest in the region; Peru's economy is open and its legal structure business-friendly; only about 5 per cent of all mining areas in the country are under development so far, creating investment opportunities in the country; the Pacific Alliance initiative signed with Mexico, Chile and Colombia should bring in new investments in Peru; and finally, the country's involvement in numerous trade agreements with the US, EU, China, and soon in the Transpacific Partnership Agreement, should bring in investment and lead to further growth.

Despite impressive figures in Mexico and glimmers of hope throughout the region – such as steady growth in IPOs in Argentina and M&As in Chile – the predictions suggest Latin America should prepare for lower numbers and the value of these transactions compared to the boom years. Francisco Ugarte puts the situation bluntly. “M&A transactions have increased in a worldwide basis, but not in the case of Latin America. Analysts project a 36 per cent decrease in the total M&A deals in the region compared to the first semester of 2014.” Only Mexico escapes the general trend of reduced IPO values and sluggish M&A growth.