Private equity roundup – Latin America

Private Equity in Latin America is published quarterly by Ernst & Young to provide insight and analysis on capital markets trends as they apply to this important emerging market.

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Value of PE deals jumps to US$552m, reaching the second-highest quarterly investment total in the last 18 months

Latin America has continued to see significant PE activity over the last several months, as local and global firms are drawn to the region's compelling domestic growth story. This is despite the deceleration of the global macroeconomic environment that has challenged growth over the near-term and led to significant policy interventions designed as countermeasures against economic headwinds and consumer credit saturation.

In the second quarter, the value of PE deals announced in Latin America jumped significantly, to US$552m, up from US$206m in the first quarter of the year, making it the second-highest quarterly investment total in the last 18 months. Q2 deals were spread across the region, substantiating the continued maturation and diversification of the industry. Companies headquartered in Brazil represented less than half of new investees, while countries including Chile, Colombia, and Peru all saw new investment over the last three months.

The second quarter also saw a number of PE exits, including the reopening of the IPO market in Brazil after nine months without a new offering. In April, PE-backed Companhia de Locacao das Americas (Locamerica) went public on the Bovespa exchange, raising US$146m in its market debut. It was quickly followed by Banco BTG Pactual, the largest IPO in Brazil since 2007. BTG raised more than US$1.7b in its IPO and achieved a market capitalization of more than US$14.7b. In 2010, a group of investors including J.C. Flowers and several soverign wealth funds invested US$1.8b in exchange for an 18% stake in the bank.

Fundraising continues to remain robust, with funds focused on Latin America continuing to draw investor interest. According to Preqin, PE firms focused on Latin America have raised nearly US$3.5b year-to-date. Perhaps more importantly, there are a number of new vehicles on the road at various stages of the fundraising process – currently more than 60 funds focused on Latin America are vying for investors attentions. In the aggregate, they are seeking more than US$ 19.7b in new commitments, signaling a continued ready pool of capital for new acquisitions.

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Economic overview

Global macroeconomic headwinds fed by continuing uncertainty across the Eurozone combined with fears of a temporary saturation of the increased level of credit for local consumer spending and led to a slowdown across many Latin American economies in the first half of the year. Brazil is currently expected to show a growth rate of 1.9% for the full year 2012, down from 2.7% in 2011, and 7.5% in 2010. Policymakers have responded aggressively to economic challenges through additional monetary and fiscal stimulus. The country's Benchmark SELIC rate currently sits at an all-time low of 8% with additional cuts possible, and government intervention in the form of tariffs and tax breaks aim to protect domestic industries and accelerate domestic spending.

While near-term challenges remain — notably, continued weakness in the Eurozone and now China, powerful secular trends and demographic shifts suggest that the region's long-term outlook should remain strong. Already, many economists see signs of improvement. In Brazil, retail sales grew by 1.5% in June over May, and job creation increased in July over the prior month, from 120,000 jobs to 142,000 new jobs.

Regulatory update

Brazil antitrust changes take effect

In June, the National Anti-Trust Council (CADE) began exercising new powers under legislation signed last December, which seeks to streamline the M&A approval process. Previously, merger approvals were obtained after the close of a transaction and could stretch on for years for complex deals. Under the new rules, approvals must be obtained before the deal closes. For its part, CADE will review cases within 240 days.

The new regulations also focus the agency's resources on Brazil's largest deals — those where the acquiring company's revenue exceeds R750m and the target's revenue exceeds R75m. This represents an increase from an earlier proposal, under which reviews would be applicable for any deal with acquirer revenues above R400m and target revenues above R30m. What remains to be determined is whether the regulations will be interpreted to include a PE firm's entire portfolio when considering target revenues. If so, larger PE firms could be required to seek approval for a significant number of their deals. Regardless, the revised R75m target revenue limits will provide some measure of relief by exempting a significant percentage of middle-market PE deals, and the quicker approval process should be a positive change for all PE firms.

Transactions

Deal values rebound off Q1 lows

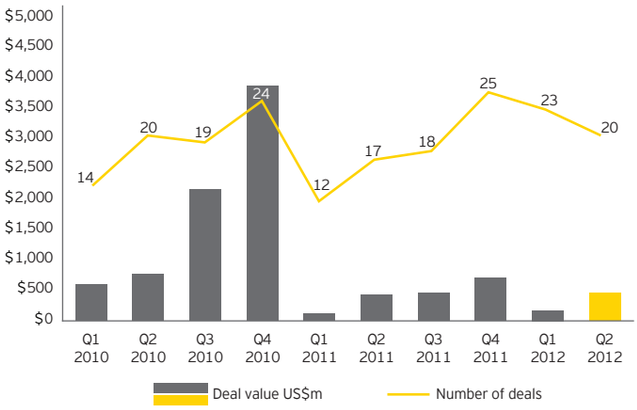
The value of PE deals announced in Latin America jumped substantially in the second quarter to US$552m – up from US$206m in the first quarter of the year. This is the second-highest quarterly investment total in the last 18 months. The volume of deals dipped moderately, from 23 transactions in Q1 to 20 announced transactions in the second quarter.

The increase in deal value was driven to a large extent by BTG's US$335.4m investment in Leader Participacoes SA. The acquisition underscores the continuing interest in companies poised to benefit from Latin America's rising middle classes and the associated spending power. Leader Participacoes, a Rio de Janeiro-based retailer, has 62 stores across eight Brazilian states, with plans to open another 19 stores within the next year. The deal follows another BTG investment in the consumer sector – in April, the firm was part of a consortium that acquired a controlling stake in Colombia-based BodyTech, Latin America's largest fitness chain.

Retail and consumer goods companies have accounted for over 37% of PE acquisitions in the last 18 months. These deals are likely to continue into the foreseeable future, as PE firms work to consolidate and expand promising businesses in these high-growth sectors.

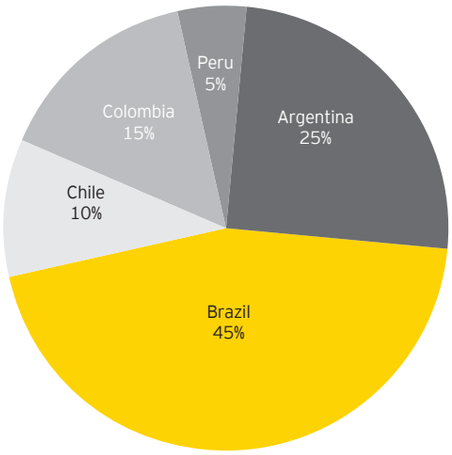
Q2 deals illustrate the continuing diversification and maturation of the Latin America PE industry across the region. In the second quarter, less than half of PE transactions were for companies headquartered in Brazil. Argentina accounted for 25% of the quarter's transactions, followed by Colombia, Chile and Peru. Moreover, the region continues to see investment from a diverse range of global and local PE players. In Q2, 10 deals were executed by PE firms headquartered in the US, and 2 in the UK and Canada. On a value basis, firms in Brazil accounted for over 60% of the region's total investment.

Figure 1. Latin America deals, Q1 2010–Q2 2012



Source: Thomson One

Figure 2. Latin America deals by investee nationality, Q2 2012



Source: Thomson One

Figure 3. Selected deals, Q1 2012

Company	Country	Deal value (US$m)	Investor(s)
Leader Participacoes SA	Brazil	$335.4	Banco BTG Pactual SA
Despegar.com, Inc.	Argentina	$92.5	Tiger Global Management LLC
BSM Engenharia SA	Brazil	$53.5	ACON Investments
Empaques Flexa SAS	Colombia	$33.7	Nexus Group
Estrella International Energy Services, Ltd.	Argentina	$24.4	Southern Cross Group

Source: Thomson One

Fund-raising

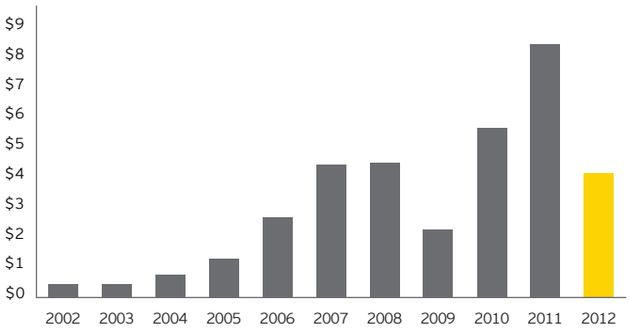
Q2 sees US$441m in new commitments; more than 60 funds are currently fund-raising for Latin America

According to Preqin, PE firms focused on Latin America raised just over US$440m in the second quarter of 2012, adding to the US$3.1b of funds closed in the first quarter of the year. 2012 has seen a number of significant closings by local funds and global investors alike, the largest of which was the US$850m in commitments achieved by Victoria Capital Partners' second fund.

Another significant close was the May closing of Capital International's sixth PE fund. While not targeted exclusively on the Latam region, the firm has been an active player in the market for years. Last year, the firm took two portfolio companies public — Arcos Dorados on the NYSE in April 2011, raising US$1.4b, and Magazine Luiza in Brazil, raising US$566m. According to Capital International, the firm enjoyed a 90% re-up rate among existing investors with an active allocation to private equity. Other closes during the quarter included GTIS Brazil Real Estate Fund, with US$850m in assets, and Rio Bravo Energia (renewable-energy sector), which closed with US$235m in commitments.

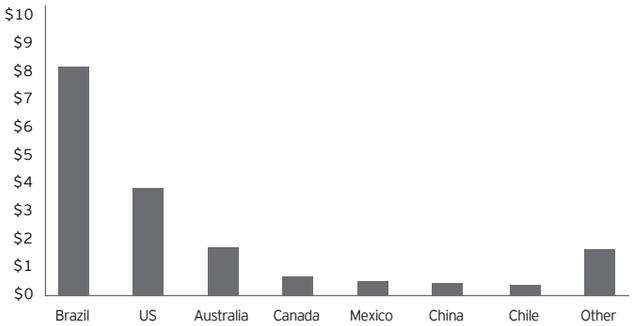
As 2012 progresses, fund-raising looks poised to continue at historically high levels as LPs allocate funds to the region. Over 60 PE funds are currently raising funds, seeking a total of more than US$19.7b in investor commitments. Brazil-based funds represent about 50% of that amount, and US-based funds are 22%. The balance, however, demonstrates the region's broad appeal to investors across the globe — Canada, Australia, China and Europe are all home to managers with LatAm-focused funds.

Figure 4. LatAm-focused fund-raising, 2002–Q2 2012 (annualized, in US$ billion)



Source: Preqin, includes funds with an exclusive or predominant focus on Latin America

Figure 5. Firms currently on the road — total target commitments by manager nationality (in US$ billion)



Source: Preqin

Figure 6. Closed funds 2012 YTD

Fund name	Type	Commitments (US$m)	Closed
Victoria South American Partners II	Buyout	$850	30-Mar-12
GTIS Brazil Real Estate Fund II	Real Estate	$810	1-Mar-12
Arias Resource Capital Fund II	Growth	$504	15-Feb-12
Brasil Petroleo I	Infrastructure	$339	1-Feb-12
FIP Sondas	Infrastructure	$312	13-Feb-12
Rio Bravo Energia I	Infrastructure	$235	4-May-12
Multinational Industrial Fund II	Expansion/Late Stage	$160	30-Mar-12
Redpoint e.ventures	Early Stage	$130	23-Jul-12

Source: Preqin

Number of Latin American funds in the PEI 300 doubles over last year

PE firms across the emerging markets have been increasingly positioned among the industry's largest firms. In the recently released Private Equity International rankings of the world's 300 largest PE funds, which ranks firms based on their five-year fund-raising totals, eight firms were based in Latin America, up from four in 2011. Gavea Investimentos entered the top 100, climbing from 136 to 84, based on the firm's successful final close on Fund IV, which added US$1.8b to the firm's assets under management.

Figure 7. Latin America in the PEI 300

Firm	2011 PEI Rank	2012 PEI Rank
Gavea Investimentos	136	84
GP Investments	110	138
Southern Cross Group	141	152
Patria Investimentos	252	187
BTG Pactual	N/A	203
Vinci Partners	N/A	228
Modal Administradora de Recursos	N/A	271
BRZ Investimentos	N/A	291

Source: Private Equity International

Several Latin America-based funds are new to the rankings. BTG Pactual debuted at 203, with US$1.6b raised over the last five years; Vinci Partners ranked 228, with US$1.4b raised; Modal Administradora de Recursos ranked 271; and BRZ Investimentos, which was spun off from GP Investments in 2006, ranked 291 with US$1.0b raised over the last five years.

Exits

Brazil sees first IPO in nine months, lists two PE-backed deals

Brazil saw its first IPO in nine months in April, when PE-backed Companhia de Locacao das Americas (Locamerica) went public on the Bovespa exchange. The car rental company is backed by BV Empreendimentos e Participacoes SA and raised US$146m in its market debut.

Locamerica was quickly followed by Banco BTG Pactual, the largest IPO in Brazil since Banco Santander in 2007. BTG raised more than US$1.7b and achieved a market capitalization of more than US$14.7b. In 2010, a group of investors including J.C. Flowers and several sovereign wealth funds invested US$1.8b in exchange for an 18% stake in the bank.

There were also a handful of M&A exits in the second quarter. The largest was GP Investimentos' sale of restaurant chain Fogo de Chao Churrascarias for US$400m to US-based Thomas H. Lee Partners. GP first invested in the company in 2006 and helped the company aggressively expand, ultimately leading to seven retaurants in Brazil and 18 across the US. The sale was one of two that GP Investimentos announced during the quarter. In April, the firm sold its stake in Sascar Tecnologia e Seguranca Automotiva to Empreendedor Brasil and JCR for an undisclosed amount.

Outlook

Despite global macroeconomic deterioration, strong regional fundamentals remain supportive of investment

In the short term, macroeconomic volatility will continue to strain many of Latin America's export-led economies because of flagging demand for key commodities in Asia, the US and particularly the Eurozone. However, strong domestic fundamentals driven by prudent fiscal and monetary policies in many key countries, coupled with Latin America's ongoing shift toward an economy more heavily influenced by domestic consumers, should act as a strong counter to external pressures. These factors will provide an environment conducive for continued opportunistic investment in high-potential companies across both the region and a range of industries.

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