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SOUTH AMERICA

Mergers & acquisitions environment in South America

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SOUTH AMERICA IS off to its best start in a decade through the first half of this year, despite M&A transactions being off to a slow start around the globe. Leading the resurgence are Brazil, Chile, Columbia and Peru, and it is no coincidence that these participating countries have benefited from having the following fundamentals in place: (i) highly regulated and healthy banking systems; (ii) the ability to act quickly with effective stimulus packages during the financial crisis, ahead of North America and Europe; (iii) low inflation and declining unemployment rates; (iv) a decline in the public sector and rise in the managerial class of professional managers and entrepreneurs; (v) a sharp increase in the middle class and lower income consumers interested in brand oriented products, contributing to internal economic growth; (vi) investor friendly market reforms open to international trade; and (vii) lower purchase multiples for businesses compared to other regions of the world.

The primary drivers leading to Latin America's 134 percent increase and $119.4bn in deal volume in the first half of the year, as reported by Thomson Reuters, revolve around a new confidence level in South America. Renewed interest in investing in South America has been stimulated by a projected 2010 GDP growth of approximately 4 percent, increased export demand of commodities, consumer demand, and a perception of reduced investment risk. Strong trading partner relationships with the growing Asian economies, specifically China and India, have helped to fuel growth. The Economic Commission for Latin America and the Caribbean (ECLAC) predicts foreign direct investment (FDI) inflows to South America increasing more than 40 percent in 2010. With valuations at lower purchase multiples compared to those in both North America and Europe, undervalued firms in specific sectors will present attractive acquisition opportunities.

While the large cap deals in the region have focused on the telecommunication, industrial, natural resource, consumer and financial service sectors, M&A activity is taking place, under the radar screen, in the lower middle-market across a broad spectrum of industries. Multilatinas (Latin American based multinationals) are acquiring smaller family owned businesses under a buy, build and hold strategy. Multinationals with sluggish economies in many of their core markets are now seeing the emerging markets in South America as a good strategic investment, offering growth opportunities for their goods and services.

As Latin America's largest and fastest growing economy, Brazil has emerged as the biggest M&A story in South America. Brazil's Finance Minister recently announced that the economy grew 9 percent in the first quarter of 2010, the fastest rate in 15 years, and is predicting a 5.7 percent average annual growth in the 2010-2014 periods. Brazil received approximately half of all FDI into South America in 2009, and through the first half of 2010, led the region in completed deals. China has become Brazil's largest trading partner and foreign investor. The country is also becoming a major player on the global M&A front, as evidenced by the $3.8bn acquisition of Bunge Ltd.'s fertiliser nutrients assets and phosphate mines in Brazil, by the Brazilian owned Vale SA., the world's largest iron ore producer. With many of Brazil's largest strategic players strengthened by strong balance sheets and bank financing, the country is successfully leading in acquisitions outside their borders and expanding their footprint throughout South America.

Chile, Columbia, and Peru should also see strong M&A activity in 2010 and beyond. All three have solid fundamentals and will attract attention depending on the industry sector. Chile is the second largest FDI recipient in South America and has undergone important market reforms that continue to encourage additional foreign investment. Columbia, with the second largest population in South America, has undergone significant investor friendly reforms and improved its domestic security which is bringing investors back to the table. Resource rich Peru is one of the fastest growing economies in South America; private-sector investment increased by 27 percent in the first half of 2010, while the economy is expected to expand by over 6 percent this year. Its mining industry, major infrastructure projects, and its recent free trade agreements with the US and China will drive future growth.

In summary, South America has taken centre stage with its surge of M&A activity in the first half of 2010. Strong economic indicators point to a continued resurgence of investment activity. Despite the global financial crisis and sluggish economic recoveries in North America and Europe, Latin America's top 500 companies had an average increase in revenues of 22.1 percent and a 33.6 percent increase in profits in 2009, according to Latin Business Journal and Latin Trade. As the global economies continue to improve and demand for goods and services increases, South America will be a major beneficiary. Investors in the region, both foreign and domestic, can expect to be rewarded by positive growth and sustained profitability. ■

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