GETTING THE DEAL THROUGH

market intelligence

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Private Equity

Post-Brexit investor confidence returning

Simpson Thacher & Bartlett lead the global interview panel

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Welcome to GTDT: *Market Intelligence*.

This is the fourth annual issue focusing on global private equity markets.

Getting the Deal Through invites leading practitioners to reflect on evolving legal and regulatory landscapes. Through engaging and analytical interviews, featuring a uniform set of questions to aid in jurisdictional comparison, *Market Intelligence* offers readers a highly accessible take on the crucial issues of the day and an opportunity to discover more about the people behind the most interesting cases and deals.

Market Intelligence is available in print and online at www.gettingthedealthrough.com/intelligence.

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In this issue

PRIVATE EQUITY IN MEXICO

Luis Burgueño is a partner at Von Wobeser y Sierra SC with more than 18 years of experience advising global leading corporations that are part of the Dow Jones, S&P, DAX, Nikkei, Bolsa Mexicana de Valores, the Fortune 500 and Forbes 100. His practice covers banking and finance; corporate, structured and project finance; energy and natural resources; foreign investment; M&A; joint ventures; and securities and capital markets. Luis has been involved in a number of matters related to transnational companies in Mexico, Latin America and the Caribbean.

Andrés Nieto is a partner at Von Wobeser y Sierra SC with more than 16 years' professional experience in Mexico, New York and Latin America. His clients appear in the Fortune 50 and Fortune 500, as well as the Dow Jones, S&P 500, DAX and the Nikkei. Andrés has a multidisciplinary practice, with an emphasis on cross-border transactions, which includes experience in several of the principal transactions that have taken place in Mexico and the United States in the legal areas of banking and finance, securities, corporate and M&A, as well as in venture capital transactions, private equity, structured financing, project finance, mediation and arbitration.

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GTDT: What trends are you seeing in overall activity levels for private equity buyouts and investments in your jurisdiction during the past year or so?

Luis Burgueño & Andrés Nieto: Generally, the trends of last year have continued. Energy is still one of the most important sectors and renewable energies in particular have continued to grow at a strong and steady pace. The telecoms sector is also doing well, with both sectors benefiting from the regulatory changes that were the result of extensive legal reforms in the past few years.

These reforms opened the market to private investment, making it attractive for private equity. New investment vehicles are continuously being introduced, designed and perfected in the country, and professionals are getting to know them, which means the market is constantly improving. If you combine this with a long tradition in Mexico of doing business abroad (Mexico has the most bilateral treaties in the world), the result is a high level of activity.

Mexico is still working on new legal reforms in order to maintain this trend of growth. One of the most appealing sectors worldwide is fintech, and we are expecting a new law that will be applicable to this sector very soon, which will give clarity and provide certain benefits to investors, such as fairness and competition under one set of rules. Despite the absence of applicable regulation, we have witnessed a strong appetite in the past year for crowdfunding alternatives (peer-to-peer lending), payment systems and, of course, the cryptocurrency market.

GTDT: Looking at types of investments and transactions, are private equity firms continuing to pursue straight buyouts or are other opportunities, such as minority-stake investments, partnerships or add-on acquisitions, also being considered?

LB & AN: We are now seeing almost every type of investment. The appetite is so great that all alternatives are being considered and pursued. We have seen leveraged buyouts, mezzanine loans, typical equity transactions and a variety of arrangements with start-ups (most of them focused on fintech).

This is, of course, combined with the 'traditional' big operations in the energy and telecoms sectors.

GTDT: What were the recent keynote deals? And what made them stand out?

LB & AN: According to the Latin American Private Equity & Venture Capital Association (LAVCA), Credit Suisse intends to raise up to 6.2 billion pesos via real estate fiduciary certificates incorporating the characteristics of capital development certificates. The real estate credit market is still at an early stage of development in Mexico (there are no mortgage-backed bonds), and financial institutions and other key players intend to innovate and offer opportunities in this market.


Luis Burgueño

In a study conducted by LAVCA, Glisco Partners, a spin-off of the investment bank Evercore, is seeking to raise US$300–US$400 million for its first independent private equity fund, which will invest in Mexican mid-market companies. Glisco aims to close the first fundraising round by the end of 2017. The company focuses on minority investments in medium-sized high-growth Mexican companies, which is promising for the future.

GTDT: Does private equity M&A tend to be cross-border? What are some of the typical challenges legal advisers in your jurisdiction face in a multi-jurisdictional deal? Are those challenges evolving?

LB & AN: Cross-border transactions have been, and still are, common in Mexico, as a large proportion of private equity comes from foreign investors. In addition, the legislature continues to encourage this trend. Private equity M&A has continued to grow, despite the political uncertainty in Mexico in the past year, and we expect this growth to continue.

Regarding the typical challenges, one of the most difficult is explaining the Mexican business culture. The investment business has become increasingly global and Mexican professionals are used to the typical vehicles involved, so this is not an issue. The problem comes with the personal side of doing business – there is still a large number of family businesses in Mexico that tend to be run using old-fashioned methods. However, this situation is changing.

GTDT: What are some of the current themes and practices in financing for transactions? Have there been any notable developments in the availability of debt financing or the terms of financing for buyers over the past year or so?


Andrés Nieto

LB & AN: As a result of financial reforms, private equity has increased significantly. Those reforms together with government programmes have had an impact on the market by promoting investments in different sectors, including those that have been exclusively for the state. Private investments have multiplied in the past few years, placing Mexico as one of the leading markets in Latin America for general partner investments. Although Mexico has improved significantly in this area, progress is still not meeting expectations, but we foresee this changing in the coming years as capital funds continue to grow in the country.

GTDT: How has the legal, regulatory and policy landscape changed during the past few years in your jurisdiction?

LB & AN: The reforms that we have mentioned (related to telecoms and energy, for example) have made Mexico more attractive for private equity transactions. The opening of the oil and gas sector to private investment exemplifies this, and we are expecting new developments, such as the planned fintech law.

This is complemented with a set of new anti-money laundering and anti-corruption laws, in response to foreign investor and international demands. Mexico is gradually becoming a more transparent market, which will provide more legal certainty for investors.

GTDT: What are the current attitudes towards private equity among policymakers and the public? Has there been any noteworthy resistance to private equity buyouts by target boards or shareholders? Does shareholder activism play a significant role in your jurisdiction, and if so, how has it impacted private equity M&A?

LB & AN: A notable impediment to private equity in Mexico has been the absence of the rule of law. According to a Commission on Environmental, Economic and Social Policy study, the lack of legal certainty and a fiscal policy that facilitates activity in the private sector has decelerated private equity growth. Even though Mexican authorities have implemented positive and ambitious structural reforms, private equity accounts for 18 per cent of Mexico's gross national product, which does not indicate substantial growth. One of the main challenges when it comes to private equity is the reluctance of entrepreneurs and families heading many of the companies in Mexico to surrender control of their companies and to accept investment by capital funds as partners or shareholders. Still, private equity has been growing in the past few years, and the government's support has given Mexico an advantageous position in comparison to other emerging markets.

GTDT: What levels of exit activity have you been seeing? Which exit route is the most common? Which exits have caught your eye recently, and why?

LB & AN: The most common exit route is the transfer of the investor's investment to another company, generally a related company such as a competitor, supplier or client that finds strategic value in it. Nonetheless, we have also seen direct transfers to another capital fund and public stock offers on the securities market are increasing.

GTDT: Looking at funds and fundraising, does the market currently favour investors or sponsors? What are fundraising levels like now relative to the past few years?

LB & AN: Currently, the idea of seeking pure capital investments has shifted towards sponsors with hands-on expertise and management skills that may add value.

Since 2009, fundraising activities have been increasing as the government allowed retirement fund administrators to invest in private equity.

Well-publicised successes, financial growth and the latest amendments to the applicable law have extended the base for private equity and investment.

GTDT: Talk us through a typical fundraising. What are the timelines, structures and the key contractual points? What are the most significant legal issues specific to your jurisdiction?

LB & AN: Companies looking to obtain funding to develop their business can do so primarily through contributions of capital from their partners or shareholders, financing by the government, private equity, project finance, financing by banking institutions and financing through the securities market. Each transaction is unique and requires the

THE INSIDE TRACK

What factors make private equity practice in your jurisdiction unique?

The fact that publicly traded companies are typically controlled outside the stock market (ie, by a family or other closely held group) substantially limits public-to-private equity deals. Mexican firms are very reluctant to give away control or even provide transparency as a condition to accept private equity. Many Mexican firms (ie, their owners and managers) lack experience in M&A transactions, and do not perceive them to be an integral part of a firm's growth strategy. As a result, deals in Mexico can move very slowly, which is frustrating for private equity firms. Understanding and getting used to the Mexican business culture and traditions can be very complicated.

What should a client consider when choosing counsel for a complex private equity transaction in your jurisdiction?

Counsel should not only have experience in the technical part of private equity deals, but also in the industry (or a similar industry) where the target operates.

On the other hand, experience in only one sector might not be enough. As these deals usually involve the participation of experts in several legal areas particular to Mexican law (labour, tax, environmental, etc), and with time being of the essence, a firm should be able to provide a comprehensive legal assessment and should have enough resources readily available to give a timely and high-quality response to private equity clients. For complex deals we highly recommend a full-service law firm.

What interesting or unusual issues have you come across in matters that you have recently worked on?

Currently, we are working on a global deal involving around 30 countries in which Mexico plays a key role, as it is the biggest single producer of the group. In addition to the complexity of this deal, the Mexican entities, as well as other companies of the corporate group in several other jurisdictions, are also facing a class action lawsuit. As if that were not enough, production involving thousands of workers cannot be stopped at any point, as products need to be timely delivered to customers in order to comply with their schedules. In other words, we are facing a unique and extremely complicated deal. We expect it will be one of the biggest deals of 2018 globally.

Luis Burgueño and Andrés Nieto
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preparation and negotiation of different specific legal instruments. The timeline of each transaction will depend on its complexity.

GTDT: How closely are private equity sponsors supervised in your jurisdiction? Does this supervision impact the day-to-day business?

LB & AN: No specific treatment is granted to private equity sponsors. Yet, there are specific legal provisions that must be complied with, and tax issues must be addressed carefully depending on the nature of these operations. Usually, when the planning and composition in the early stages of the project have been done carefully, the authorities do not intervene in the day-to-day business.

GTDT: What effect has the AIFMD had on fundraising in your jurisdiction?

LB & AN: The AIFMD has had hardly any impact on normal operations in Mexico. The operations that have been affected by the Directive are those of European fund managers managing alternative investment funds and alternative investment funds established in Europe.

GTDT: What are the major tax issues that private equity faces in your jurisdiction? How is carried interest taxed? Do you see the current treatment potentially changing in the near future?

LB & AN: With a view to boosting investment, Mexico grants benefits to trusts operating investment capital. Challenges arise in receiving these benefits, as all legal requirements must be met, such as strict compliance with tax requirements. These benefits, such as not taxing trust operation investment activities until the revenues are allotted to private hands, have helped to consolidate these practices in Mexico.

As proof of the government's willingness to open the market to new alternative schemes, the tax treatment of investment schemes has been frozen until November 2018 in order to encourage confidence in alternative investment structures and to foster the development of solid funding.

GTDT: Looking ahead, what can we expect? What might be the main themes in the next 12 months for both private equity M&A and fundraising?

LB & AN: Through the course of the past year, sectors such as fintech and telecoms have become more attractive for investments, and planned regulatory policies are expected to greatly improve the current scenario.

In addition, since the 2014 energy reform in Mexico, the energy sector continues to be a positive prospect for investment.

Finally, the anti-corruption constitutional reform of 2015 helped Mexico to become a more significant player in terms of investment and private equity, which is expected to increase over the next few years.

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