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M&A: Environment of uncertainty reduces activity

By Samantha Pearson in São Paulo

Sitting in the top-floor office of Estáter, a Brazilian consultancy firm, in São Paulo's financial district, you would not know Europe and the US were deep in crisis.

"We're just seeing a process of adjustment here ... It shouldn't last long," says Pércio de Souza, the group's founder.

Estáter, which has gained a reputation for engineering some of the country's most ambitious deals, is itself a reflection of Brazil's rapidly changing environment for mergers and acquisitions.

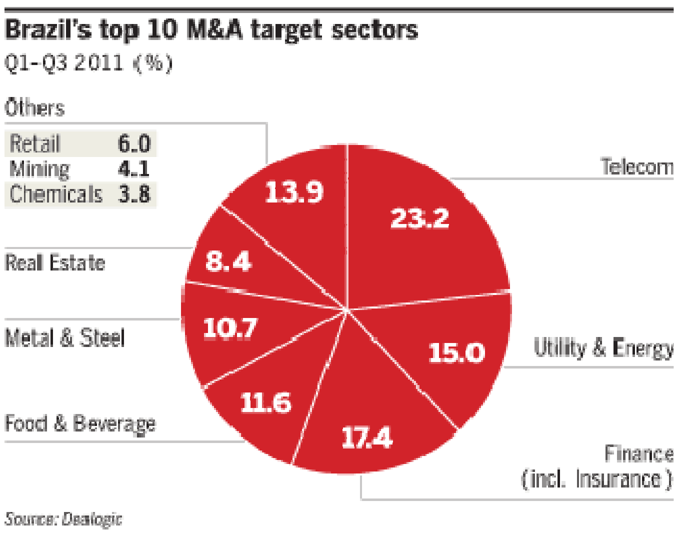
Founded in 2003, it began by advising on domestic deals in the petrochemical sector but has broadened its focus to international deals.

Most recently it helped Pão de Açúcar, a retailer, put together a bid for the local assets of Carrefour, the French group.

After opening an office in London this month, Mr de Souza plans to expand to New York next year to meet the growing demand for cross-border deals.

For most of Brazil's M&A bankers, the turning point came in 2006 when Vale, the mining company, acquired Inco, a Canadian nickel miner, for about $18bn.

"You had previously just seen companies trying to buy companies in Brazil but the Vale deal showed the country was not only a target but could also be an acquirer," says Marco Gonçalves, head of M&A at BTG Pactual, Brazil's largest independent investment bank.



"The market really has grown enormously," he says, adding that the size of the deals has also increased sharply over the past 10 years.

"At the end of the 1990s into the early 2000s, if you got a deal of $300m or $400m there would be a huge celebration. Now the deal size has grown to billions."

In fact, Brazil-targeted M&A volumes have grown more than 13-fold to $153.5bn in 2010 from $11.4bn in 2005, according to Dealogic, a data provider.

Brazil has also looked for opportunities in the rest of Latin America. Last year, there were 88 cross-border M&A deals in the region worth $15.7bn – more than 13 times as much as in 2000, when only 37 deals were done totalling $1.2bn.

"Things really started to pick up in 2004, 2006 was even better and 2007 was the peak for IPOs and equities, but M&A activity has maintained more momentum," says Renato Ejnisman, director of Bradesco's investment banking arm, Bradesco BBI.

"Now we're seeing locals buying locals, foreign companies buying Brazilians, Brazilians buying foreigners – everything," he says.

This growth can be partly explained by the natural development of Brazilian companies during a period of relative stability, as well as a gradual appreciation of the local currency that increased buying power abroad.

The development of the country's capital markets themselves was also fundamental in this process.

"The rise of M&A activity in Brazil has gone hand in hand with the development of capital markets," says Jaime Singer, head of investment banking at Deutsche Bank in Brazil.

"You now see deals that are much more complex in the way they are financed. They are structured in a way that just wouldn't have been possible 10 years ago," he says.

As a result, the crisis in global markets, which has dragged the stock index down about 15 per cent this year, has also taken its toll on M&A – it has left companies with fewer options to raise capital and created an environment of uncertainty.

"We have several situations where there is clearly a deadlock between buyers and sellers, where they can't find common ground in valuation," says Marcelo Naigeborin, head of investment banking at Morgan Stanley in Brazil.

However, bankers largely see the current difficulties as a blip in an otherwise positive trend.

In fact, even though Brazil-targeted M&A volume this year has halved from the same period in 2010, at $63.4bn it is still already higher than 2009's full year total of $59.4bn.

Ambitious deep-sea oil projects, pressing infrastructure needs as the country prepares to host the World Cup and the Olympics, and a hot consumer market should all help support both stocks and M&A activity.

"The fundamentals are still very strong," says Christian Egan, head of equities at Itaú BBA, an investment bank.

"The three main pillars are commodities, infrastructure needs and also the Brazilian consumer story."