Crowe Horwath

The Global Corporate Advisor

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The Corporate Finance newsletter of Crowe Horwath International

Welcome to the December issue of The Global Corporate Advisor. This newsletter has a special focus on the merger and acquisition activity in Latin America this year. We find that government policies impact business more than in many other parts of the world. Many countries are in a state of flux and are considering reform. Tools to help navigate the domestic and international geo-political and regulatory environment are more important than ever.

As a collective area, Latin America continues to show signs of weakness due to global factors out of the region's controls such as the direction of oil prices, the effectiveness of Japan's economic policies, and moderation of growth in China, as well as the region's largest M&A contributor, Brazil, witnessing a stagnating economy as weakening demand and investment have been caused by a decline in the commodity prices for key exports. On the positive side, the second largest M&A country in Latin America, Mexico, should benefit from the economic growth of its closest neighbor, the United States, with US companies looking for investment opportunities south of the border.

PVarley

Peter Varley
Chairman of GCA
+44(0) 207 842 7353
peter.varley@crowecw.co.uk

Inside This Issue:

Contact Us

The GCA team is here to respond to your needs relating to M&A transaction support, valuations and advisory services. If there is a topic you would like us to cover in future issues of the GCA newsletter, don't hesitate to contact Peter Varley, Chairman of GCA, at peter.varley@crowecw.co.uk. Alternatively, please contact your local GCA team member to discuss your ideas.

M&A Latin America

Argentina

by Norberto Rosemberg, Buenos Aires

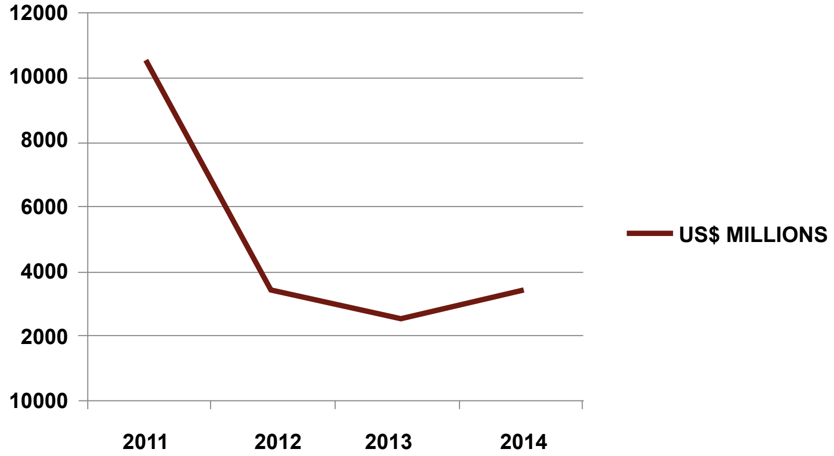
In 2012, we used to say that M&A activity is slowing down in Argentina. This was when Argentina dropped from the second to the fifth position in Latin America (LA), overtaken by Mexico, Brazil, Chile and Colombia. Today, that negative view deepens.

At a time when M&A activity in Latin America is reflecting the good conditions most of the region is experiencing, Argentina is competing with Venezuela in economic irrationality and adopting measures which result in scaring away investors.

Currently, Argentina has dropped to the sixth position, overtaken also by Peru, not only in the amount of transactions but also in connection with the investment volume, which is worse, with only 3% of the amount transacted.

As shown in Figure 1, the sharp decline in the amount transacted is evident. This is a result of limits on foreign exchange and commercial restrictions in force in the country, which discourage investments.

Figure 1: M&A TRANSACTIONS IN ARGENTINA



Argentina barely exceeded the much smaller Uruguay in the amount of transactions in 2013, with US$2.5 billion against a little bit more than $2 bn of Uruguay. In number of inhabitants, territory and the global economy size, Uruguay is almost 10 times smaller than Argentina.

The main transactions involve YPF (the oil company recently renationalized), both as buyer of other oil companies in Argentina, and as seller of a part of its shares, for example, to George Soros. Except for the abovementioned situation, it is hard to find single transactions over $100 million.

For more information

Norberto Rosemberg is the Corporate Finance Manager at Crowe Horwath, Argentina.
He can be reached at +54 11 4394 8091 or norberto.rosemberg@crowehorwath.com.ar

M&A Latin America

Brazil

by Francisco D'Orto Neto, São Paulo

According to the São Paulo Industries Federation (FIESP), Brazilian investment rate for 2014 will be lower than 18% of the GDP, which in turn is lower than 2013 figures. The investment rate decline may be explained by the poor performance of the Brazilian economy during 2014, which is continuously impacting investors' confidence in the country's development outlook.

Despite the decrease in the investment rate, the volume of mergers and acquisitions (M&A) in 2014 has increased. There may be good reason to believe that the M&A market will continue to be active in 2015, but a significant change in the direction of the Brazilian economy and the legal framework will determine whether one should expect less or more interest in Brazil in the coming years.

The volume of M&A transactions until the third quarter of 2014 has increased at an approximate rate of 10% compared to the average of the last years. Market sources expect that this growth will be sustained or even exceed this percentage by year end.

The sectors that lead the ranking in volume of transactions include IT, services and retail, but any analysis of the Brazilian M&A environment needs to take into account agribusiness and infrastructure sectors due to their role in the economy and increasing demand. The majority of the deals in these sectors had the participation of strategic investors but, as in recent years, private equity and other financial investors became relevant players and important sources of funding.

The IT sector led the way and was responsible for about 17% of the total number of transactions reported until the third quarter of 2014. Heightened activity in the IT sector may be explained by the need for consolidation felt in this market – a trend which will most likely continue in 2015.

On the other hand, services and retail sectors, which also saw a sizeable number of transactions, are maintaining or even reducing their share in the total volume of 2014 as compared to 2013. One may expect a further decrease in volume of transactions for the next years in view of the challenges these sectors are already facing and due to the slow pace of growth of the economy and consumption in 2014.

The agribusiness sector is the big star of the Brazilian economy in 2014. Despite the rest of the economy going down (GDP growth is expected to be at a rate of around 0.2% to 0.3% in 2014), the Brazilian agribusiness sector is expected to grow 4% from 2013. This sector will continue to be relevant in the coming years in terms of M&A activity, despite some adjustments that may be imposed on the ethanol industry, which will certainly go through more consolidation and financial restructuring during 2015.

Investment in infrastructure will be key to obtaining sustainable economic growth in the country. Infrastructure related to industries and sectors such as oil and gas, energy, telecommunications, mining, hydro ways, ports, airports, railroads and roads is highly dependent on a fairly stable policy. However, the legal framework for many of these sectors has been quite unstable in the last few years.

Despite the lack of interest in long-term investments in many of these sectors, existing assets continue to be attractive to investors, especially assets that will benefit from continuous growth of the agribusiness sector and increasing demands by the population in relation to urban mobility. M&A may be a tool for consolidation of some of these industries and an aid for many of them facing financial challenges in projects already contracted but not necessarily, or properly, funded.

In terms of players involved in M&A deals, the economic slowdown tends to affect short-term investors more compared to strategic players taking a long-term view. However, short- or medium-term players such as private equity and other financial investors may actually look into Brazil as an opportunity, given the devaluation of the Brazilian currency and the reduction of price expectation by Brazilian sellers.

Many of these M&A growth drivers (consolidation in certain sectors, importance of agribusiness, additional infrastructure requirements and financial restructuring) will continue to result in a significant volume of transactions but this volume will not be sustainable if the Brazilian macro-economic environment is not adjusted and the country does not offer stability to investors in its legal framework.

For more information

Francisco D'Orto Neto is the GCA head at Crowe Horwath Brazil.
He can be reached at +55 11 3372 3756 or francisco.dorto@crowehorwath.com.br

M&A Latin America

Chile and Peru

by Sergio Bascuñán, Santiago

Chile

When analyzing the Chilean economy, it is impossible to leave out the mining sector, particularly its copper industry. Copper provides 20% of GDP and 60% of all Chile's exports, so it can be said that this metal is the nation's most valuable resource.

But looking back at 2014, two other sectors, pharmaceutical and salmon farming have been marked by purchases of multinational companies, changing both industries' scenario. While Chile has experienced a difficult year in terms of economical expectations and growth, our neighbor Peru seems to be the blooming economy of South America.

The mining sector

The sector is seeing a mild appetite return to acquisitions (such as Glencore's approach to Rio Tinto), divestments (any major diversified mining), mergers (the abortive attempt between Barrick Gold and Newmont) and even a split (BHP Billiton).

The recent acquisition by Lundin of some Freeport copper assets is notable and there is speculation that Anglo American may consider some copper assets in Chile in the future. In Chile, investors are focusing on underperforming companies to institute cost-cutting measures enabling better returns to shareholders. Casablanca Capital is using this approach in Cliffs Natural Resources, where it holds a little over 5%.

Private equity and specialized funds with a medium- to long-term outlook are being active. Magris Resources (together with CEF Holdings and Temasek) reached an agreement in early October to acquire the IAMGOLD Niobec mine.

The major diversified miners have been following the strategy of selling non-core assets. BHP Billiton announced the cleavage of a number of assets, and the new management team can choose to reshape the portfolio.

The sector will be affected in 2015 by an increase in operational costs, regulatory changes, lagging productivity and lower international prices for copper and other precious metals, such as gold, mainly because of the increase in production costs and a stronger dollar that has moved investors back to other markets such as the United States and Europe. All this will limit the sector's growth and mining expansion plans.

The pharmaceutical sector

The global pharmaceutical sector has seen several multi-billion dollar deals in 2014, which has been the busiest year for healthcare acquisitions.

In Chile, the wave hit in December 2013 when Grünenthal Group, an international research-based pharmaceutical company headquartered in Aachen, Germany, completed the acquisition of Andrómaco Laboratories. Grünenthal launched a public tender offer for acquisition of all issued and outstanding shares of Andrómaco. After the acquisition, Grünenthal has become one of the top four players in the Chilean market, doubling its revenues up to $450 million in Latin America, according to company officials quoted in the media.

We also saw the acquisition of two major retail pharmacy networks in Latin America. In May 2014 Alliance Boots, a multinational pharmacy-led health and beauty group, signed an agreement to acquire Farmacias Ahumada. The acquisition comprises two main businesses, which together operate over 1,400 stores, with combined revenues of around $1.4 billion. Farmacias Benavides is the third largest retail pharmacy chain in Mexico with around 1,000 stores, and Farmacias Ahumada is one of the three largest retail pharmacy chains in Chile with around 400 stores.

Most recently, CFR Pharmaceuticals has been acquired by Abbott Laboratories, uniting the largest maker of heart stents and adult nutritional beverages with Chile's biggest drugmaker in a $2.9 billion deal.

Chile will continue to attract multinational investments in 2015, since it has a stable political system, efficient legal framework and business-friendly environment.

Salmon deals

This year has seen the attention of Norwegian majors. Feed producer EWOS and the world's largest fish farmer, Marine Harvest, bought bankrupt mid-sized Chilean salmon companies Nova Austral and Acuinova.

Several Norwegian firms have been active in the selling and buying of firms and licences in the sector.

Peru

Peru has seen market mergers and acquisitions which exceed $13 billion in 2014, up from $12.254 billion recorded in the 2013, according to industry statistics.

The advance is said to have been driven by the acquisition of the Las Bamba copper mining project by China Minmetals Corporation, which paid $5.85 billion to Glencore Xstrata. The purchase of Master Peru for 1.404 million soles ($103.7 million) from Sodimac by the conglomerate Falabella Peru added to the total.

The accession of Epensa Trade Group to the El Comerico Group through a partnership agreement for $17.2 million was another highlight.

For more information

Sergio Bascuñán is the Audit and International Liaison Partner at Crowe Horwath in Chile.
He can be reached at +56 2 2328 30 00 or sergio.bascunan@crowehorwath.cl

M&A Latin America

Mexico

by Miguel Moreno Tripp and Alejandra Muñoz, Monterrey

In Mexico, there were 186 M&A registered transactions from January to October 2014, according to the monthly report of Transactional Track Record. This represents an increase over the total number of transactions made last year, which were 175.

By sector, the highlights have been the technology sector, with eight transactions, followed by finance and insurance with with 24 and 18 M&As respectively.

As for cross-country operations, the foreign companies that have made purchases in Mexico include those from Colombia, Norway and Spain. On the other hand, Mexican companies' M&A operations were set in France, Spain and the United States.

Among the most significant transactions this year are, quoting the headlines published:

- AT&T Inc., the second-largest U.S. mobile-phone carrier, agreed to buy Grupo Iusacell SA from billionaire Ricardo Salinas for $2.5 billion to expand further into Latin America.
- America Movil SAB contacted potential suitors including AT&T Inc. and SoftBank Corp. as it prepares to sell assets along the east coast of Mexico that could fetch as much as $17.5 billion.
- U.S. chemicals maker PPG Industries Inc. said it had formally finalized its acquisition of Mexican paints maker Consorcio Comex for $2.3 billion.
- Southern Cross Group, a Latin-American private equity firm, and media company Time Inc. announced that Southern Cross was acquired by Grupo Expansión, a Time Inc. subsidiary for an undisclosed amount.

Nine Mexican listed companies have expressed their intention to make a purchase. They have about US$5.1 billion in available cash as of the third quarter, which will enable them to carry out their plans. These companies are: Femsa, Cemex, Lala, Bimbo, Genoma Lab, Herdez, Soriana, Mexichem and Chedraui. Bimbo just recently agreed to acquire Canadian-based Saputo Bakery.

It is expected that the during the last quarter of the year, the number of transactions will increase, knowing that there are some that will close before the end of 2014, as in the case of Empaque, a Mexican packaging company being acquired by Crown Holding at $1.225 billion. In the retail sector, Soriana is rumored to buy Comercial Mexicana, the third largest retail company in Mexico, a transaction that may take place soon and Femsa has confirmed the acquisition of FarmaCon, an east coast Mexican pharmaceutical retailer.

There has been considerable reporting on events in the southern part of Mexico. So much so, that it prompted some legal and internal security reforms that will be implemented during the next months. Despite considerable news coverage, we do not think this will slow the economic activity for Mexico in 2015.

However, the reduction in the world oil prices will have a double negative effect on the Mexican economy for future years. On the one hand, close to 30% of the government's income comes from Pemex, the state-owned oil company and on the other, the much needed and finally launched, oil industry reforms may not take off due to the predicted economic boom.

For more information
Miguel Moreno Tripp is Director GCA at the Crowe Horwath Gossler Monterrey office in Mexico.
He can be reached at +52 1 (81) 8020 2344 or miguel.moreno@crowehorwath.com.mx

Alejandra Muñoz Soto is the Manager GCA at the Crowe Horwath Gossler Monterrey office.
She can be reached at +52 1 (81) 8120 3002 or alejandra.munoz@crowehorwath.com.mx

M&A Latin America

Venezuela

by Rafael Stroobants, Caracas

When Standard & Poor's, Moody's, and Fitch downgraded Venezuela´s ratings in 2014 to respectively CCC+, Caa1, and B (all meaning speculative investment grades with high risks), the socialist Bolivarian government downplayed the actions as typical imperialist aggression. But when China´s main rating agency, Dagong Global Credit Rating, followed course and degraded the country to BB-, it was remarkably quiet on the otherwise very noisy revolutionary front. After all, China has been propping up the country´s finances since 2008, with loans totaling more than US$50 billion (next in line comes Russia, which has lent more than $10 billion).

Dagong predicts that the country will end 2014 with a deficit over 14% of GDP (primarily due to falling oil prices), debt levels at 52% of GDP (huge for developing countries and emerging markets), a contraction of the economy (at -2 to 3% of GDP), and a reduction of international reserves (up to 20%).

While the above is quite a performance for a country which, over the last decade, received a trillion dollars in revenues, the story doesn´t end there. We must add to the picture strict and unreliable exchange controls (the reason why foreign airlines no longer fly to the country or only accept hard currency) and regulations on prices and profits (such as the recently enacted Law of Just Costs and Prices). Venezuela also has a legal framework which is not investor-friendly, rated worst in Latin America and 182nd out of 189 countries worldwide, according to the World Bank report, Doing Business 2015. There are also factors such as the country´s exit from the International Centre for Settlement of Investment Disputes (ICSID), its bureaucracy and red tape, not to mention crime and corruption.

All this explains why, in spite of having the world´s largest recoverable oil reserves, investors have had no appetite for Venezuela in 2014. M&A activity has been very low to almost non-existent. On the contrary, the event that made the headlines was the disinvestment of Clorox Co., which after 20 years in Venezuela, announced its exit. The company was immediately taken over by the government and joined a long list of companies that have been nationalized over the past 10 years (AES Corporation, CMS Energy, PSEG, Lafarge, Cemex, Techint, Verizon, Conoco Philips, Gold Reserve, Owens-Illinois, Cargill, and Santander, among others). Many of them have yet to receive full payment of the settlement they agreed on with the government (Swiss cement maker, HOLCIM, for instance, announced in 2014 that it's still owed $97 million from the 2008 seizure of its assets). A total of 26 companies are awaiting the results of their legal arbitration processes (another 2014 headline: Exxon Mobil is awarded $1.6 billion compensation by ICSID for the 2007 nationalization of its investments).

The best illustration of the situation regarding the country and its M&A activity, is probably JP Morgan's EMBI+ index for Venezuela´s sovereign risk, which reached an all-time peak of 1986 points in 2014 and is currently the highest investment risk in the world.

In conclusion: no good M&A news came from Venezuela in 2014. Even the government's nationalization program of privately held companies has stalled – we jokingly speculate that this is due to lack of money and perhaps because there are no companies left to be expropriated.

The only exceptions to the lackluster environment have been the state-owned oil companies from China (CNCPC, Sinopec) and Russia (Rosneft, Gazprom) that have partnered with the country's national oil company PDVSA in joint-ventures, with a little bit of equity investment (always as minority shareholders, according to Venezuelan oil laws) and a huge amount of debt financing (the loans sponsored by their respective governments). On the other hand, companies such as Russia's private companies Lukoil and Surgutneftegas and Malaysia's Petronas have sold their share in these joint-ventures and overall foreign investment in the oil sector is down.

Finally, we would like to mention two cases where Crowe Horwath was directly involved through valuation and due diligence services: the acquisition of Norpro, a proppant (fracking material) manufacturer and a subsidiary of French company Saint Gobain by national oil company PDVSA, and the government's acquisition of Monaca, a food conglomerate owned by Mexico's Gruma group.

Last but not least are some facts and figures from the Economic Commission for Latin America and the Caribbean (ECLAC) for 2013, the most recent available.

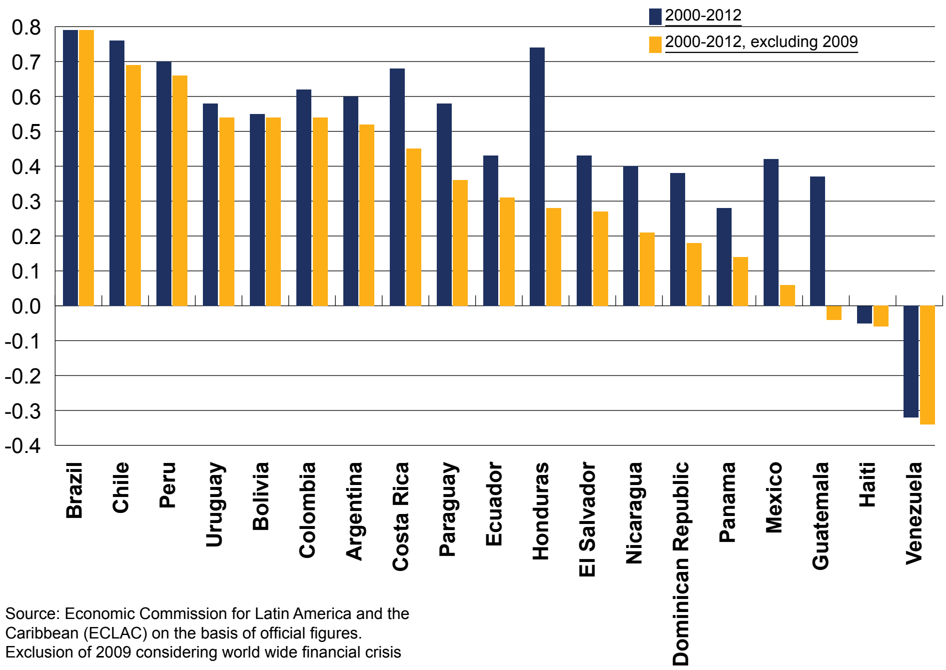
Figure 2: Latin America: foreign direct investment inflows by receiving country or territory, 2004-2013 (Millions of dollars and variation in percentages)

Country	2004-2007 [a]	2008	2009	2010	2011	2012	2013	"Absolute variation 2012-2013 (amount)"	Relative variation 2012-2013 (percentages)
South America	**49,546**	**94,237**	**56,870**	**95,866**	**130,978**	**142,171**	**129,890**	**-11,929**	**-8**
Argentina	5,350	9,726	4,017	11,333	10,720	12,116	9,082	-3,033	-25
Bolivia	618	1,302	687	936	1,033	1,505	2,030	525	35
Brazil	21,655	45,058	25,949	48,506	66,660	65,272	64,046	-1,226	-2
Chile	8,584	15,518	12,887	15,373	23,444	28,542	20,258	-8,284	-29
Colombia	7,243	10,596	7,137	6,746	13,405	15,529	16,772	1,243	8
Ecuador	449	1,058	308	163	644	585	703	118	20
Paraguay	95	209	95	216	557	480	382	-97	-20
Peru	3,284	6,924	6,431	8,455	8,233	12,240	10,172	-2,067	-17
Uruguay	1,001	2,106	1,529	2,289	2,504	2,687	2,796	109	4
Venezuela	1,267	1,741	-2,169	1,849	3,778	3,216	7,040	3,824	118
Mexico	**25,647**	**28,337**	**17,055**	**23,027**	**23,009**	**17,628**	**38,286**	**20,658**	**117**
Central America	**5,042**	**7,651**	**4,533**	**5,881**	**8,535**	**8,809**	**10,691**	**1,881**	**21**
Costa Rica	1,255	2,078	1,347	1,466	2,176	2,332	2,682	350	15
El Salvador	697	785	385	-230	218	482	140	-342	-71
Guatemala	535	754	600	806	1,026	1,245	1,309	64	5
Honduras	686	1,006	509	969	1,014	1,059	1,060	1	0
Nicaragua	290	626	434	508	968	805	849	44	5
Panama	1,578	2,402	1,259	2,363	3,132	2,887	4,651	1,764	61

Source: Economic Commission for Latin America and the Caribbean (ECLAC) on the basis of official figures and estimates as of May 2014.
[a] Simple averages.

Figure 2 illustrates direct foreign investment in Venezuela. While representing on average only 2% of total foreign investment in South America, the numbers seems to indicate a record amount in 2013. Unfortunately, quite the opposite is true and almost two thirds of the investments flowing into the country were reinvested earnings. This is because the government does not allow repatriation of dividends, so they're diverted into other assets, especially real estate. The other third were loans from parent companies. This is because the government does not release foreign currency to import products, spare parts, or machinery, so the parent companies buy them on behalf of the Venezuelan plants. In reality, capital investments were virtually non-existent in 2013, according to ECLAC, which expects even worse results for 2014 (ECLAC, Economic Survey of Latin America and the Caribbean, 2014: Venezuela).

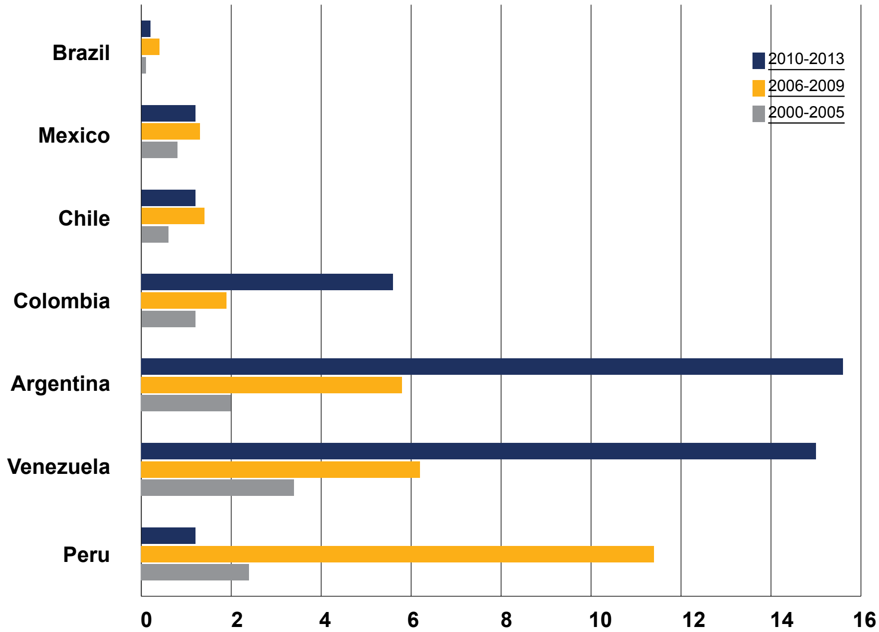
Figure 3: Latin America and the Caribbean (selected economies): correlation between changes in foreign direct investment and in gross fixed capital formation, by country, 2000-2012 (Coefficients)



Source: Economic Commission for Latin America and the Caribbean (ECLAC) on the basis of official figures.
Exclusion of 2009 considering world wide financial crisis

In fact, as shown in Figure 3, Venezuela has experienced divestment rather than investment over the previous years, with negative capital formation through huge capital outflows. These outflows were not channelized into formal mergers and acquisitions by Venezuelan investors abroad. As Figure 4 indicates, outbound foreign investment from the country is minimal, with investments only by PDVSA. Even in this regard, there will be probably more divestment that investment, since PDVSA is planning to sell, totally or partially, its stake in Citgo (USA), Hovensa (Virgin Islands) and Chalmette (Louisiana refinery).

Figure 4: Latin America: foreign direct investment by main source countries, annual averages, 2000-2013 (Billions of dollars)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official information.

For more information
Rafael Stroobants is a Partner of Advisory Services at Crowe Horwath in Venezuela.
He can be reached at +58 0212 43 06 or rafael.stroobants@crowehorwath.com.ve.

Regional GCA Leadership

China
Antony Lam
antony.lam@horwathcapital.com.cn

Indian Subcontinent / Middle East
Vijay Thacker
vijay.thacker@crowehorwath.in

Southeast Asia
Alfred Cheong
alfred.cheong@crowehorwath.com.sg

East Asia
Mok Yuen Lok
yuenlok.mok@crowehorwath.net

Latin America
Francisco D'Orto Neto
francisco.dorto@crowehorwath.com.br

USA / Canada
Marc Shaffer
marc.shaffer@crowehorwath.com

Central and Eastern Europe
Igor Mesenský
igor.mesensky@tpa-horwath.cz

Oceania
Andrew Fressl
andrew.fressl@crowehorwath.com.au

Western Europe
Peter Varley
peter.varley@crowecw.co.uk