

Hot Brazil

As the South American giant races ahead, its improved fundamentals have attracted big global private equity funds

BY VYVYAN TENORIO

THE LAST TIME private equity designated Brazil as “hot,” the country was felled by double-digit inflation and an Internet-fueled bubble. This time Brazil has all the hallmarks of a buyout mecca: a thriving economy, political stability, sound fiscal policies, vast natural resources and vibrant consumer sectors. Brazil was among the last to enter into recession in the region and the earliest to rebound.

The markets point to a sounder investing environment. A survey by Washington’s Emerging Markets Private Equity Association and London’s Collier Capital Ltd. shows Brazil surging ahead of China and India for the first time as the most attractive emerging market for dealmaking in the next 12 months. Limited partners give it top marks on political risk, and better grades for entry valuations.

For now, it seems, everyone’s humming samba tunes. “The macro environment in Brazil is very different now,” says Alex Pellegrini, a partner at Apax Partners LLP, which last year bought a majority of Brazil’s largest IT and business process outsourcing company, Tivit Terceirização de Tecnologia e Serviços SA. It was Brazil’s first take-private, valuing the São Paulo company’s stock at around 1.7 billion reais (\$1 billion).

Historically, Brazil has had an active PE industry. While most were midsized funds, that’s changing. Regional funds have grown larger, and there are more of them. About 30 Brazil-focused funds have raised about \$9.5 billion in the last three years, according to Preqin Ltd. A further 20 funds are targeting \$10 billion currently.

Advent International Corp., one of the more active firms, closed a \$1.65 billion, fourth Latin American fund last April. While a record at the time, it was beaten by Buenos Aires-based Southern Cross Group, whose fourth fund drew \$1.68 billion in September, attributed to demand from new LPs globally. With offices in the region’s major capitals, Southern Cross is among the largest operations in Brazil, alongside alternative asset managers Gávea Investimentos, Pátria Investimentos and GP Investments Ltd., now also raising a big new pool.

Focusing on Brazil, Mexico and Argentina, Advent has had a presence in São Paulo since 1997 when it made its first investment in credit card processor CSU CardSystem SA. Its team, led by managing partner Patrice Etlin, has since expanded to 17 investment professionals, the largest PE unit domiciled in Brazil.

What’s noteworthy, says Marcello Hallake, a Thompson & Knight LLP partner in New York who frequently advises on regional deals, is that global PE firms are muscling in. Blackstone Group LP paid \$200 million for a 40% stake in Pátria to secure a foothold. Carlyle Group, 3i Group plc and Warburg Pincus have set up shop. Carlyle came in 2008 and cut three deals last year. It paid \$1 billion for a controlling stake in medical insurer Grupo Qualicorp, followed by \$126 million for a 51% stake in women’s underwear maker Scalina SA. Earlier it bet \$250 million on Brazilian tour operator CVC Brasil Operadora e Agência de Viagens SA. Carlyle is raising its first dedicated

regional fund, targeting \$500 million.

Consumer-oriented businesses are a big draw. Apax scouted targets for years before nailing Tivit. The company, which has a big credit card transaction business, “is a way to play the macro consumer growth trend” as Brazil catches up with developed markets in outsourcing noncore services, says Pellegrini.

Even with some 70 investment firms active in Brazil, Etlin says, it’s still underpenetrated compared with China and India. Competition differs by sector, he says, and his firm hasn’t yet gone head-to-head with others on 90% of its deals.

While available from commercial sources, leverage is expensive. Still, Carlyle and Advent both tapped some debt on certain deals. Etlin says Advent uses a “prudent” amount—averaging below 1-1/2 times Ebitda across its Brazilian portfolio.

Which means PE firms create value the old-fashioned way. This year Advent acquired 50% of Terminal de Contêineres de Paranaguá SA, Brazil’s third-largest container port terminal, plowing \$500 million into an all-equity transaction. Etlin says the stake came at a fair valuation, given that infrastructure has huge capacity bottlenecks. Other sectors such as healthcare or pharmaceuticals carry higher premiums. “Multiples are higher than they were four or five years ago, but their growth prospects are also better,” he says.

China, India and Brazil all offer “interesting growth-adjusted valuations,” says Pellegrini. For those who have been around for years, it feels like things are more expensive, but, he says, “We think multiples are stable and reasonable.” ■

