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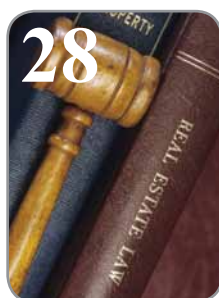
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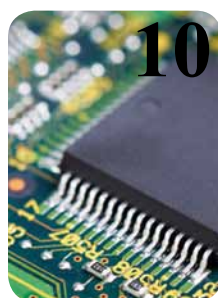
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A low-angle photograph of a man in a dark suit and tie, looking upwards with a slight smile. He is positioned in the lower right foreground. Behind him are several tall, modern glass skyscrapers that reach towards a bright blue sky with wispy white clouds. The perspective makes the buildings appear to converge towards the top of the frame.

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Letter from the Editor

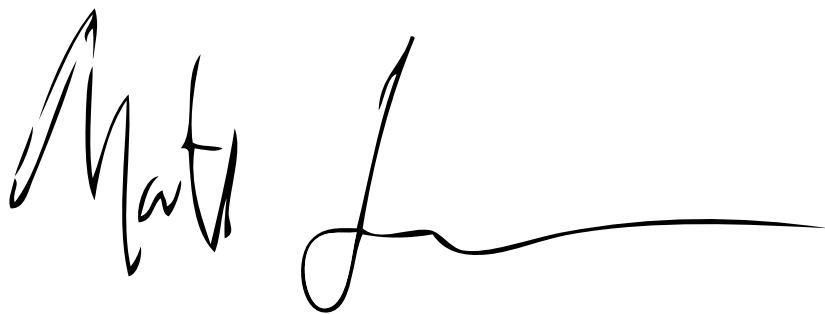
Dear Readers,

Open this Mexico-focused issue of *Alternative Latin Investor* with a simple question: When did Noah build the ark? The answer is before the flood. For those of us who have been on the ground in LatAm, who saw the past, current and future potential of this region, we well know it's raining heavily and the flood is imminent. 2011 saw Brazil overtake the United Kingdom as the world's 6th largest economy; last year's Apex acquisition of Tivet was for US\$1 billion; Barclay's and Blackrock are competing for US\$9.3 billion worth of Mexican pension funds; the city of Buenos Aires is issuing bonds; and the list goes on.

Despite this visible growth of interest in LatAm, the same principals still apply: we cannot forsake the lessons of the past, basking in FDI without closely monitoring the international players and, just as important, local governments' attitudes towards them. Compared with emerging markets of the past, LatAm countries have generally not thrown open their arms in a welcoming embrace, but rather embraced their own people in policies of protectionism and regulation. It is this type of legislation and monitoring which will make future growth and prosperity possible, relegating the possibility of an economic bubble.

The question from the investors point of view is: From what vantage point can you see this wave of investment coming, from what perch can you analyze the opportunities and pitfalls of this goldmine of a region? It is my most sincere hope that, sticking with this metaphor, where ever it is, you've managed to stay dry, and that *Alternative Latin Investor*, if only in a small part, has helped to elevate your point of view, understanding and knowledge of the LatAm investment environment.

Nate Suppaiah



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What Hedge Fund Association (HFA) Members Have to Say About LatAm

Daniel J. McClory



Daniel J. McClory is a seasoned international merchant banker whose transactions have spanned the U.S., Europe, Asia and Africa. He serves as Managing Director of the Hunter Wise Financial Group, LLC, in Southern California. Mr. McClory has completed public offerings, financings and M&A deals for clients listed on the London Stock Exchange, NASDAQ, NYSE Amex, the Toronto Stock Exchange, and the Over-the-Counter Markets.

Are you looking to increase your LatAm exposure in 2012?

Yes. We anticipate funding several transactions for Brazil in 2012 including mining, alternative energy and retail.

What was it in 2011?

Zero. We initiated several potential transactions and began monitoring companies and conducting preliminary due diligence.

Why the change?

We have added Marc Fogassa as Managing Director for Hunter Wise. He is from Sao Paulo and operates a Bovespa-listed fund called Hedgefort from Beverly Hills.

What sectors and regions interest you in LatAm?

Diamonds, iron ore, apparel, oil and gas. Brazil and Peru.

Jeffrey D. Jones



*Jeffrey Dow Jones is a managing director at Jones & Company (www.Jones-Funds.com). He serves as the firm's macroeconomic strategist and jointly manages a portfolio of hedge funds. He holds a degree in Business Economics with a specialization in Computer Programming from UCLA. He is the publisher of the popular investment newsletter *The Draconian* and author of the book *The Trade of the Decade*.*

Are you looking to increase your LatAm exposure in 2012?

We're not looking to increase exposure to the area at this point. Our current strategic outlook suggests caution is warranted at the global level, with global GDP likely to be weak. Latin America tends to exhibit more volatility than developed economies and we want to be careful about how and where we expose ourselves to volatility. In a world where correlation between risk asset movement is at or near all-time highs, investors need to rethink what it means to have a truly diversified portfolio.

What was it in 2011?

We didn't have much exposure to the area last year, though we do have some. Most of it is in the form of private equity, and for sophisticated investors who know how to navigate the landscape, a private equity approach probably offers the most attractive risk/reward characteristics. Alternatives like that are also the way that investors can get true diversification and lack of correlation.

Why invest in LatAm?

Having a little exposure to Latin America can be an important component of a geographically diverse portfolio. Our area of expertise is in alternative investments and we're comfortable with what we have in that space – it's one piece of a broad portfolio. Generally speaking, investors that are risk averse probably already have minimal exposure to Latin America. Investors with a higher level of risk tolerance may already be looking at Latin America, but these folks may want to think about increasing exposure in advance of the next cyclical economic expansion.

What sectors and regions interest you in LatAm?

As investors, we tend to be rather conservative. So when we look at the Latin American space, we prefer economies that share two qualities: 1) a relatively stable currency regime, and 2) minimal geopolitical risk. The Mexican peso fell apart last year but found strong technical support. It's also one of the most fundamentally undervalued currencies in the world on a purchasing power parity basis. Mexico also has some advantageous demographic tailwinds and a relatively young population. I think that, coupled with a base of desirable exports, makes it an economy to keep one's eye on over the next decade or two.

Michael P. Hennessy

Michael Hennessy is Co-founder and Managing Director at Morgan Creek Capital Management, with US\$9 billion AUM. Previously Mike was with UNCMC (UNC-Chapel Hill), DUMAC (Duke University) and Smith Breeden Associates. He received an M.B.A. from Fuqua (Duke), and a B.S. from William & Mary. Mr. Hennessy is a Trustee of the College of William & Mary Foundation Board, and Chair of its Investment Committee.

Are you looking to increase your LatAm exposure in 2012?

We currently have an overweight to LatAm and have had an overweight for a while now. We will continue to maintain that overweight in 2012. However, the nature and character of that exposure will likely change. We are looking to diversify our exposures further by incorporating more asset classes, sub-asset classes, countries and strategies as opposed to general equity exposure. Even within equities, we are looking for certain more focused, specialist exposure. We are always looking for world-class skill, no matter what or where the strategy.



What was it in 2011?

Without getting into the specifics of gross exposures vs. net exposures and beta-adjusted exposures, our exposure to LatAm was approximately one-third of our Emerging Markets exposure, which itself had an overweight at about 15 percent of our overall portfolios. We have maintained a considerable overweight to Emerging Markets for a very long time, really since the 1994 Mexican tequila crisis. Our exposures to LatAm have increased as time went on. Again, the exact nature of those exposures has changed over time to reflect the differences in opportunities and risks between countries, sectors, asset classes, strategies, and, importantly, skill sets of fund managers. There clearly was also a dependency on the development, structure and integrity of bourses, markets, and fund structures.

Why the change?

As long-term investors, it seems clear that investing in emerging markets makes great sense. For many of the same reasons, it makes sense to invest in LatAm. There continues to be a secular transfer of wealth from the developed economies to the developing. This has always been the history of mankind, since the very beginning. That transfer is happening faster than ever in history due to the effects of globalization and technology. It doesn't mean one needs to abandon developed markets. To the contrary, we have increasingly integrated economies and markets. Some of the world's best global companies are in developed markets. Some of the world's best global companies are also in Emerging Markets, including LatAm. Further, the dynamics of demographics is very powerful, and the various regions of the world differ significantly

on this factor. Lastly, there is the crucial issue of valuation levels. Valuation, prudent portfolio rebalancing, and shifting exposures within LatAm, have in aggregate resulted in a net similar overall weighting this year.

What sectors and regions?

We continue to expand outside Brazil and into more regions and countries. We are also, as mentioned, broadening exposures beyond just equities. We continue to seek and incorporate other strategies such as select global macro, fixed income, currency, commodity, real estate and infrastructure strategies. All these strategies must compete with traditional securities as well as private equity, in which we also are active.



The Hedge Fund Association, HFA, is an international not-for-profit industry trade and nonpartisan lobbying organization devoted to advancing transparency, development and trust in alternative investments.

Membership in HFA includes hedge fund firms, global financial institutions with hedge fund offerings including private banks, asset management firms and broker dealers, investors including funds of hedge funds, family offices, public and private pension funds, endowments and foundations, high net worth individuals, allocators, and service providers including prime brokers, administrators, custodians, auditors, lawyers, risk managers, technologists and third party marketers.

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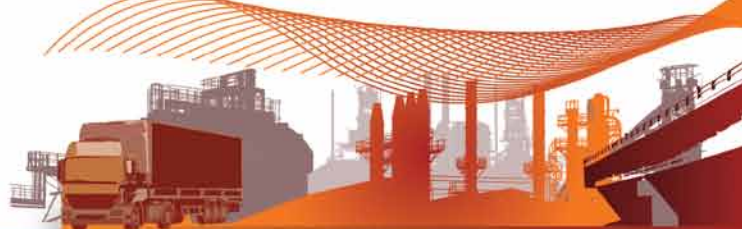
Major projects are soon to be tendered by many of the governments in Central America, the Caribbean and the Andean region.

In Colombia alone, an estimated US\$20bn in infrastructure projects is needed through 2014 and governments in the region are looking for new investors.

This is why, Bogota is the ideal place to discuss and seek out opportunities in the region's new energy, transport, social and water infrastructure projects.

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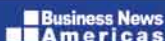
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The Importance of Investing in Technology-Based Small Enterprises in Peru

Peru is a country rich in ecological diversity and natural resources, but remains behind other LatAm countries due to a lack of foreign investment in innovative technology. In recent years, Peru has been rated as one of the strongest economies on the continent, stemming mainly from an increase in the production of exportable products – 88.6% of exports are commodities that come from natural resources, 8.5% are products with a low technological focus and 0.6% with a high technological focus.

However, Peru invests only 0.15% of its GDP in research, development and innovation, unlike neighboring countries who invest significantly more – Argentina (0.40%), Chile (0.60%) and Brazil (0.95%). Government subsidies are not substantive or long term, nor are they able to support the most rural populations; and academic interest is limited due to the geographical distance from most innovators. Individuals and organizations that produce innovative technology are not yet well supported, thus there exists a real opportunity for impact investment in Peru.

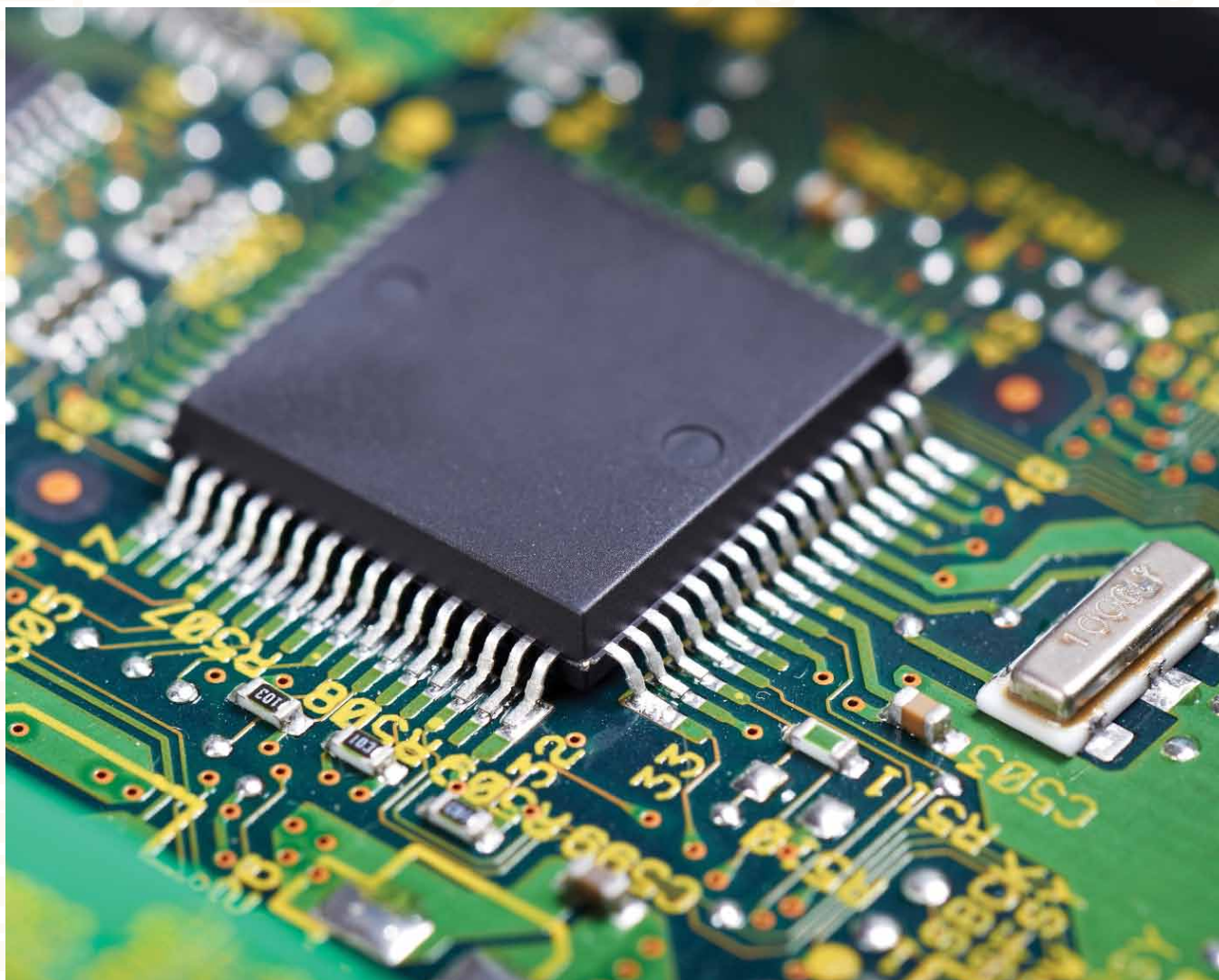
Technology-based small businesses have a significant positive social impact in various regions of the country. Innovators produce affordable technology – primarily based in agriculture and livestock – that directly impacts the social needs of the populations,

and are thus prime for expansion. Examples include machinery to modernize agriculture and enable farmers to increase their income, water purification tools for productive use and consumption, medical devices for use in small, rural hospitals, and fuel-efficient cook stoves to reduce costs. The varied examples confirm that small technology-based businesses can generate a high social impact.

For this reason NESsT – an international social enterprise catalyst based in Santiago, Chile – launched the RAMP Peru program supported by The Lemelson Foundation, which seeks to provide direct support to these businesses so they can launch, consolidate and become sustainable. Through RAMP, inventors who have a technological vision as well as a social mission and basic business knowledge are selected and supported in their efforts to develop a sustainable business plan. NESsT provides ongoing capacity building in the planning, incubation and scaling stages of enterprise development, including timely financial support in the form of grants, loans and equity.

RAMP has been a positive influence on regional and national governments in promoting small technology-based businesses that promote employment and income for local inventors and contribute to national development. To date, the RAMP program has launched 17 technology companies in three regions of Peru – Cusco, Puno and Cajamarca – and has supported competitions and events that have reached more than 100 local stakeholders in developing innovative proprietary technology, useful for society.

Through these types of technologically innovative development efforts, local entrepreneurs begin to strengthen their capacity and further their reach, preparing themselves for investment from the extended impact investing market. Already, the majority of these enterprises have taken loans and have a high repayment rate. Peru needs investors that are willing to move into this riskier space of technological innovation in order to yield real social impact while generating financial returns.



About NESsT

NESsT is a catalyst for social enterprises in emerging markets and worldwide. We achieve our mission by providing financial capital, training and mentoring, and access to markets for a high-impact portfolio of social enterprises. We combine the tools and strategies of entrepreneurship and investment with the mission and values of the social sector to enable our portfolio companies to better plan, improve management capacity, grow, and increase their social impact.



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Senior Investment
Officer, Energy Division,
*Inter-American
Development Bank*

Rogério Ramos
Head of Clean Energy
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**Gonzalo Ruiz de
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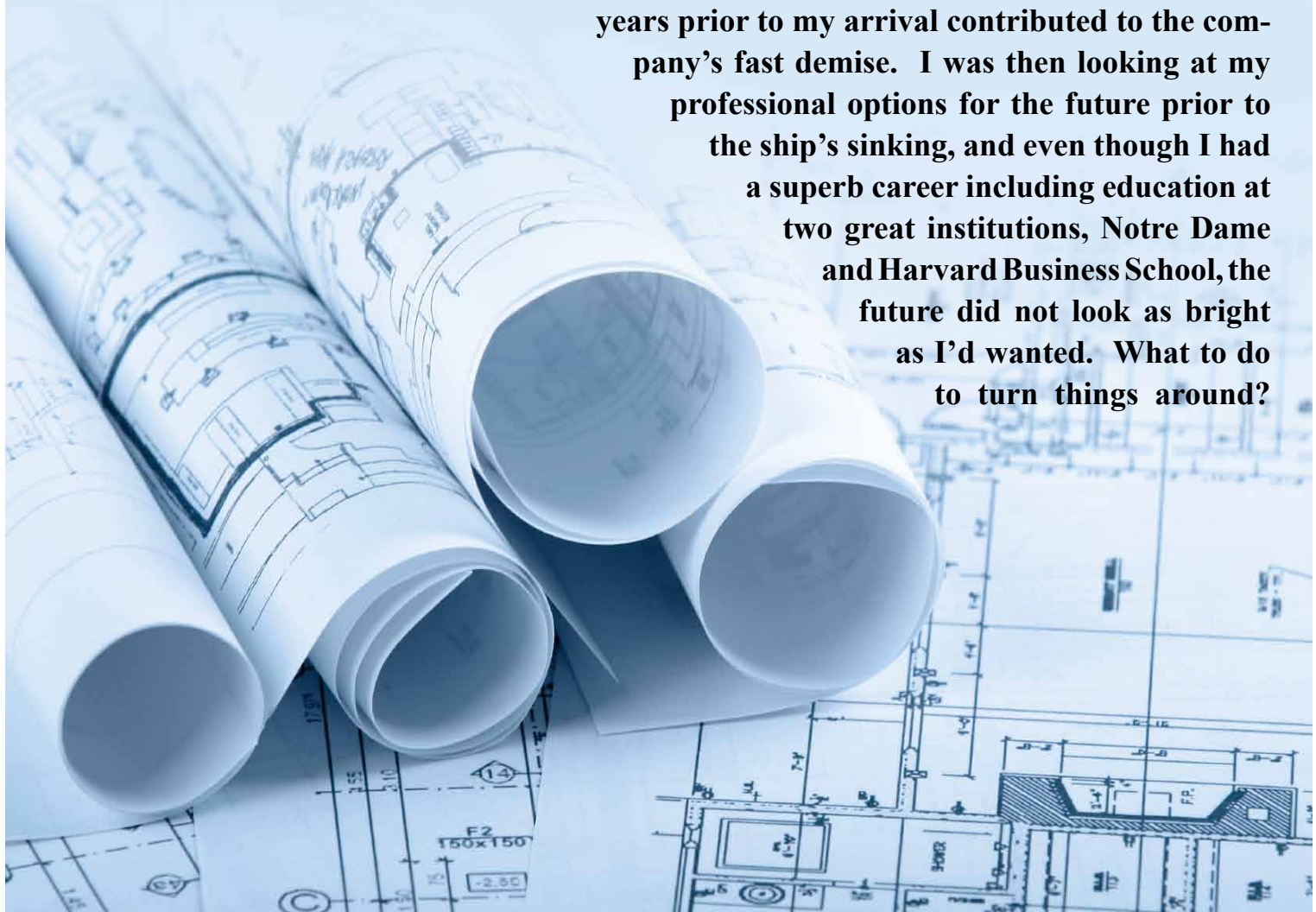
FORTY YEARS

of Residential and Commercial Development

IN COLOMBIA

■ Felix Villalba, with
contributions by Rafael
Fierro

Several years back, the private equity (PE) firm I worked for was imploding as an indirect result of the macroeconomic slowdown in the U.S. That slowdown combined with the investments that were made by the firm many years prior to my arrival contributed to the company's fast demise. I was then looking at my professional options for the future prior to the ship's sinking, and even though I had a superb career including education at two great institutions, Notre Dame and Harvard Business School, the future did not look as bright as I'd wanted. What to do to turn things around?



Schumpeter talked about creative destruction. Here I was...now forced to get out of my cozy six-figure job and go apply all that I had learned. The answer, therefore, lay in a question: What have I been deeply involved in that has been successful for many years?

1. Real estate developments in Colombia.
2. PE and venture capital investment vehicles in the U.S.

In my search for my next steps, I concluded that combining the two was the winning formula. The result was a solid, growing firm, Grand-Accordo Group of Funds.

I had the good fortune of observing my very successful father in action at building his company, Grand Construcciones e Inversiones, in a difficult environment (Colombia in the 1970's and 80's). Not only had he started from nothing, but he did it successfully for more than forty years with double-digit returns. Had I not seen it myself, I would not have believed the returns he had back in the 80's. Our family business had internal rates of return (IRR) higher than 50% annualized per project. I remember an investments professor telling me how risky our business must be simply because we had high returns and it was located in Colombia.

That came from an academician who did not realize the fallacy of his statement and who ignored how good management and good business fundamentals can yield high

returns with very low risk. For example, in the 1990's we shielded the company from the ups and downs of high-end residential construction business cycles. In fact, we profitably shut down operations in the 1990's prior to the Colombian real estate market bubble and subsequent downturn. We identified at the time that the market fundamentals were not in line with the extensive supply. Things turned around years later and we reopened our operations.

I have also had the good fortune of learning how to manage a PE fund in the U.S., and I observed first-hand the high risk taken by investors in the U.S. for a mere 10% return versus the high returns/low risk of our real estate developments in Colombia. Our investments in Colombia have always had relatively low risk primarily because the principal has had a high degree of protection (low site cost in higher-end locations and building with customers' cash) and also because many cities in Colombia have not and have never been as risky as their bad reputations suggest.

I remember an investments professor telling me how risky our business must be simply because we had high returns and it was located in Colombia.

Another important fact for investors is that, in the words of Colombian attorney at law and Professor at a local university, Mr. Rafael Fierro, "foreign investments are now protected under a new 2005 law [Ley 963 de 2005]. This law provides for a guarantee that investors' rights will not be changed if during the life of a contract any law mentioned in the contract is changed by the state. If that change in law is important to

Here are some facts about Colombia:

- It has always been a capitalistic society with great respect for property rights.
- For decades it has had an independent central bank.
- The Colombian peso has always been a stable currency, with no shocks à la Mexico or Argentina.
- There has never been hyperinflation à la Brazil.
- It is one of the strongest democracies in the Americas, dating back to 1810.

the investment, then the investors will have the right to continue applying the previous law for the duration of the contract."

In knowing these facts, it was clear that there must be an opportunity to invite smart U.S. investors who use facts to make their decisions rather than the media's hype. These are investors that can see through the fog and see reality: in the U.S. they are not going to find the same low-risk investment yielding our type of returns. Hence, I decided to set up my fund management firm, Accordo LLC, and later successfully raised capital for Accordo Fund 1 LP to be invested in Colombia's real estate market using my family's business formula based on 40 years of success. In other words, we share the riches with U.S. investors, allowing us to grow.

So what is in store today for Colombia and our Grand-Accordo Group of funds? Simply look at the recent fundamentals:

- A continuous decrease in unemployment since 2002.
- A more secure environment for private property than Peru, Brazil, Mexico, and Argentina (Source: 2009 IMD World Competitiveness Yearbook).
- Improved security (per the U.S. State Department: "Security in Colombia has improved significantly in recent years").

Here are some of the tenets that drive our business today:

- Protect your principal.
- Sell first, build later or build with customers' cash.
- Build high quality because customers do catch on.
- Be keenly aware of the time-value of money.
- Do the opposite of the market; be a niche player.

- Safer big cities than many in the U.S.
- Colombia is the U.S.'s only real ally in South America.
- 45 million people (and 50 million by 2020), the 29th largest population in the world, with a growing middle class and an upward-trending consumer confidence.
- The signing of the Colombia-USA Free Trade Agreement in 2011.
- 2011 also saw the Colombian government's debt upgraded to investment grade by Moody's, S&P, and Fitch.

As I sit here today, we have started returning capital to our Accordo Fund 1 investors and are now looking at a promising future with Accordo Fund 2 and many more to come.

Felix Villalba, Managing Director Grand-Accordo Funds

Felix Villalba has over 15 years of experience on both the operating and investment side of business transactions. After his MBA, Felix worked for captive financial services companies at Dell and Whirlpool, and later spent over five years as CFO with two venture-backed technology companies. Dell's successful effort to start Dell Financial Services marked Felix's official involvement in the venture industry in 1997. It was after that when he joined an Austin ventures-backed company that later led to his joining Pacesetter Capital Group. At Pacesetter, a PE firm, he was Vice President and served as Portfolio Manager for several inherited deals, some of which required intervention strategies. In 2009, Felix formed his own PE management firm, Accordo LLC, and raised Accordo Fund 1 and 2, placing investments in residential and hospitality developments in Colombia.

Felix is a graduate of the University of Notre Dame with three degrees, a Masters in Business Administration, a B.S. in Civil Engineering, and a B.A. in Economics. He successfully completed the Harvard Business School's Executive Management Development Program. felix@accordollc.com



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2012

LatAm's Year of Wind Energy

The Latin American Wind Energy Association, LAWEA, was born in 2007 with the intention of promoting the development of this energy source in the region. "Since then, we have been working on strengthening the industry through the dissemination of the achievements and relevant accomplishments towards its development, and this has consolidated LAWEA as the most important network in the region," explains Fernando Tejada, LAWEA's co-founder and president. Since its beginnings, the institution has been betting on this clean and sustainable source of energy, trying to support the formation of strong local supply chains to conquer a common auspicious future for the people in this region.

LAWEA detected the necessity of supporting the development of this type of energy in order to take full advantage of the wind resources in the region. "We respond to the need to form a strong block to remark the benefits and potential from the implementation of this source of energy," says Mr. Tejada, "as well as other complementary sources that allow our countries to go towards more diverse and efficient energy matrices with fewer and fewer harmful atmospheric emissions. Latin America is an emergent region rich in natural resources with powerful winds and a growing demand for electricity; it

is mandatory to take this opportunity and ensure sustainable development from now on."

The current panorama of LatAm indicates that "there are countries in the region that are generating more than eighty percent from renewable energy," Mr. Tejada adds, "in contrast with other countries in which that same percentage is provided by fossil fuels, mostly imported. Renewable energy sources are called upon to give a comprehensive response to this imbalance in the energy matrix of the region." It is in this sense that the wind industry appears as an interesting option, in light of the growth that has been evident in recent times. In 2008 wind capacity grew by twenty percent, with the installation of just over 500 MW; in 2009 it passed the barrier of 1,000 MW installed, an increase of one hundred percent; and in 2010 it added 703 MW of wind power to the grid in LatAm, with Brazil being the industry leader. In 2011 we have seen similar increases, so we think that the LatAm wind market is beginning to show sustained growth.

Experience, coupled with the determination of various governments and the complementarities that exists with proven hydropower, is giving these energy sources recognition as clean, cost-effective options. In the next two decades, there is the po-

tential for wind power in LatAm to create hundreds of thousands of new skilled jobs. It could definitely be a trigger for the economic and social development of communities with better wind resources and also contribution to environmental care and the reduction of the so-called carbon footprint. Realizing this outcome is our greatest desire, and we are doing everything possible to transform it into an immediate reality. For now, the local supply has increased with the opening of manufacturing plants, and some of them with their own technology. Gradually, we will depend less on the import of equipment, thereby reducing installation costs and adding to the economic and social development throughout the area.

While considerable efforts have been made regarding regulatory frameworks, among which include certain countries that have set growth targets for clean energy sources, wind-energy-specific auctions and other incentives, LAWEA proposes adding strong support in each nation to deepen these trends. Undoubtedly, the region has the required potential and enthusiasm enough to make the winds blow ever harder with every gust and finalize the "Latin American Dream," building a common future with the same impulse: THE WIND.

For more information visit: www.lawea.org or contact Fernando Tejada - ftejeda@lawea.org or at 001.281.710.7456

What We Talk About When We Talk About Infrastructure

Manuel Rodriguez of GBM on a New Generation of Investment Opportunities

Recent years have seen intensified interest in Mexican infrastructure. There is a consensus that massive investment is needed in the sector to relieve the bottlenecks resulting from a growing population, an increasingly demanding middle class, and the agriculture, mining, manufacturing and tourism at the heart of Mexico's economy. That economy, the 13th largest in the world in terms of nominal GDP, ranked only 79th in the World Economic Forum's Global Competitiveness Rankings infrastructure index. The current president, Felipe Calderón, has been generally praised for meeting the challenge, with his administration's National Infrastructure Plan investing US\$233 billion in the sector through 2012.

Yet according to Manuel Rodriguez Arregui, the Director General of GBM Infrastructure, one of the country's most important private-sector investors in infrastructure, the best opportunities for investors in the coming years are not necessarily in public works but in what he calls the business of managing infrastructure.

"Usually when people talk about infrastructure," he says, "the emphasis is on public works. But you have to differentiate the public works arena, which is mostly about construction, from the arena of managing

infrastructure as a business. We tend to put them together, but I think they're completely different businesses."

Mr. Rodriguez has unique expertise in infrastructure in the region, having worked at high levels in both the public and private sectors. A graduate of MIT and Harvard, he worked in the Calderon administration as the undersecretary of transportation. Now, at GBM, Mexico's largest investment bank, he is managing a US\$500 million fund that will invest in infrastructure, raised primarily from institutional investors in Mexico, as well as some from abroad.

The business of managing infrastructure, he says, is primarily about understanding and serving the customers who will be using that infrastructure. He gives airports as an example of a subsector where this has been done successfully in Mexico. "We have three airport groups quoted on the stock market that are doing well, and there has been a transformation in the last ten years toward managing those airports as businesses and understanding the different lines of business within that business, both the regulated and nonregulated revenues." Indeed, a recent report on Mexico City's airport by Latin Business Chronicle confirms that business travelers give it high grades.



If you compare the success of airports with other subsectors, however, there are marked drop-offs, he says. As an example, he gives an important stretch of the Chamapa Highway near Mexico City. “In 36km you have, on one side, no gas station and no convenient store, and on the other side, one gas station. That’s the equivalent of operating an airport without shops. The reason is that you traditionally have operators of toll roads who merely think of the toll road without understand-

where there are huge opportunities, as well as in water and energy.”

Mr. Rodriguez notes that the business of managing infrastructure is still nascent the world over, with infrastructure-focused funds being raised only in the last five or ten years in most countries. “It’s still the early stages. We still identify many opportunities, and those in reality come from the fact that new business models are coming into play. We’re going to see more privatiza-

has a deficit and excess debt, a PPP is not a solution – it’s just more debt. What you’re going to see instead is governments leveraging assets, making them liquid, and using those funds to reduce debt while at the same time letting the private sector do things that are more in need in terms of the customer.” He also believes that, in cases of infrastructure projects that meet important social needs, subordinated capital from the Mexican Infrastructure Fund (a sovereign fund) should be used to allow investors to have preferred equity,

“The reality is that the opportunities in Mexico in the next ten years we believe are going to be very good, especially with the way we have structured private equity in Mexico through the stock market. That seems to be a contradiction, but what you have is the economics of private equity with the transparency of the stock market, and that is starting to attract foreign investors.”

ing the customer. But in the business of infrastructure, as in any other business, you have to start by understanding the customer. And with toll roads, the customer not only wants to save time; they want security and a reasonable place for a driver to take a rest. There are many other needs associated with transportation that are part of the business, the same way that in airports you have to take into consideration the catering of foods and the cleanliness of bathrooms.”

Mr. Rodriguez says that revenue models also need to be improved with toll roads. “There’s no reason not to do market studies to understand preferences and the elasticity of demand. If you look at the way we pay for tolls, it’s highly unsophisticated.”

The opportunities are not limited to toll roads, but stretch across subsectors. “In the last 20 years,” he adds, “the population of Mexico has increased roughly 20%, but the movement of goods has increased 600%. We tend to think of infrastructure in terms of people, but you also have to think of it in terms of the transport of goods. That is

tions, financial restructurings, spinoffs, consolidations, and new financial structures.”

The investors investing in his fund, he says, are attracted by Mexico’s new, highly regulated structured vehicles, which are designed allow Mexican pension funds specifically to invest in infrastructure and private equity. “The reality is that the opportunities in Mexico in the next ten years we believe are going to be very good, especially with the way we have structured private equity in Mexico through the stock market. That seems to be a contradiction, but what you have is the economics of private equity with the transparency of the stock market, and that is starting to attract foreign investors.” (See the article in this issue on CKDs.)

Public-private partnerships (PPPs), he says, will be important, as they have been increasingly across the region, but again he stresses an important distinction. “There are two types of PPPs. There are PPPs that are no longer off-balance-sheet, and I don’t think that we are going to see as many of them as people think, because it’s equivalent to debt. If you have a local government that

thereby reducing enterprise risk and making those projects more attractive.

Ultimately, he says, while investors interested in capitalizing on the wave of construction can merely buy stocks of construction companies on the Mexican exchange, investors interested in the more long-term business of managing infrastructure must pay keen attention to these questions of revenue, financing and the like. “Someone investing in infrastructure in order to see the returns we’ve seen with airports,” he says, “is going to have to pay a lot of attention to synergies with other projects, understand how to grow the business, optimize the tariffs, use sophisticated revenue management, find operating efficiencies, improve the financial structure of the project and create a platforms to access financial markets.”

Mr. Rodriguez Arregui was very encouraged by the recent passage, on January 15, of a new Public Private Partnerships Act, which he says “prioritizes private over public investment,” greatly facilitating the former and enabling more infrastructure development in Mexico.

Finding the Value in Mexican Real Estate

Bruce Greenberg on Real Estate Appraisal in Mexico

The distressed properties, stalled development projects, and steep price fluctuations in real estate these days testify to the importance of real estate appraisal. Bruce Greenberg is an expert in the art. He began in the U.S. 38 years ago, establishing his company Bruce Greenburg, Inc., before bringing his practice to Mexico in 1995 with Evaluaciones Montaña Verde S.A. de C.V. Montaña Verde has since completed 1,200 assignments comprising 3,500 properties in Mexico. It has recently established alliances with Deloitte Mexico, helping them develop a real estate services division, and with the time-share company RCI, helping them prepare market and feasibility studies for hospitality and luxury housing.

Mr. Greenberg says his methods bring a sophistication to Mexican real estate appraisal that is necessary as Mexico becomes more present in the global markets. The difference between his company's appraisal and analysis methods and the methods that have prevailed historically in Mexico and LatAm as a whole, he says, is that "LatAm appraisers have been architects and engineers who look at the bricks and mortar, at what an asset cost, while my discipline is of one supply and demand, of the economics, taking more of a market-based approach, and taking future value into consideration."

"Now that Mexico is understanding the need to be in the global financial marketplace," he adds, "the Mexican banking community and equity funds don't want these brick-and-mortar appraisals anymore, but reports following international standards." He says that information and analysis such as what his company provides is precisely

what many players were lacking during the recent housing and real estate crises in the U.S. and Mexico.

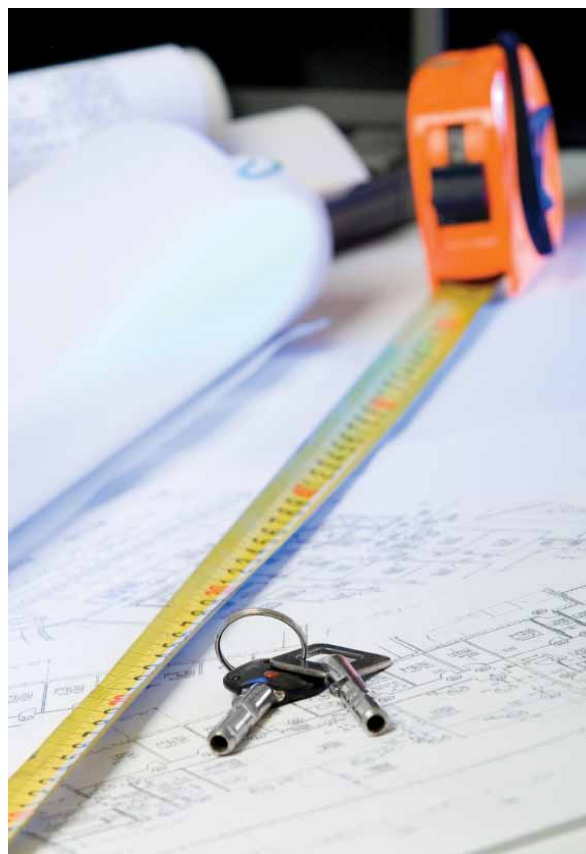
"If you look at what happened in Mexico, as well as in the U.S., in the last five years, it was really a breakdown of communication. The bankers were not talking to the bankers, the developers weren't talking to the developers, the municipalities and governments weren't talking to anybody. The quick change we saw in real estate really came down to that: if we really understood supply and demand and absorption, we wouldn't have had this crisis."

As a result of the crisis, he says, we are in the midst of a "vast correction period" in the luxury second-home subsector as well as in luxury hospitality; those are the areas where one finds distressed properties. Yet he points out that, while the typical second-home in the U.S. lost about 40% of its value in the last 24 to 36 months, the same kind of home in Mexico has typically lost about 20%. And as those homes are typically paid for in cash, there have been very few foreclosures.

"There is distressed real estate, mostly because of an oversupply in tourism corridors: too many condos, too many hospitality projects built. But everyone is working through those generally."

He points to an interesting niche where development and profits have picked up. "People saw that there were not a lot of business hotels in the country, so some of the big resort developers are stopping to catch their breath and build business hotels, and they are being very successful."

"If I were looking to invest today," he says, "I would look into these business hotels, as well low-end housing." Outside of real estate, he also mentions retail and the aircraft and automotive industries as being particularly attractive.



Investing in Argentina

A legal perspective

An Interview with
Javier Canosa from
Canosa Abogados,
Buenos Aires, Argentina

Do you think that government protectionist policies will ease in 2012 during Cristina Fernández Kirchner's second term?

No, I certainly do not think so. Although a “moderate” has been appointed as Ministry of Economy, the real power lies in the hardcore interventionist Secretary of Domestic Commerce, Guillermo Moreno.

How have these policies impacted foreign investment?

Although it is difficult to say whether such protectionist policies have impacted FDI or not, it is true that some foreign companies have reaped great benefits from Argentine protectionism. However, in general, investment decisions are very carefully analyzed and appraised and even in cases where the decision to invest has been made, the amount of the investment is reduced to the minimum amount necessary to close a certain deal. There is almost no long term perspective.

Who have they helped?

These measures have helped certain specific sectors working with the domestic market with long terms ties in Argentina, those who produce in Argentina, those who benefit from less competition from overseas.

Please give us a brief summary of forex and land ownership legislation? How has this changed recently?

New regulations have been put into place in connection with those two issues. In connection with forex, as of November 2011 the

government requires that prior to any purchase of foreign currency by resident individuals or local companies, an authorization from the Argentine Tax Authorities must be obtained, authorization that will relate to the specific purchase in terms of amount and the determined tax payer. In practice, it has been quite cumbersome to purchase foreign currency. Now the system is running more smoothly.

In connection with land ownership: In December 2011 a new law restricting foreign ownership of rural land was passed in Argentina. This new law limits the percentage of rural land that can be owned in Argentina. The limit has been set at 20% of the arable rural lands in Argentina. Currently, foreign individuals or companies own 7% of Argentina's arable rural land according to official information. The definition of “foreigner” is broad and it encompasses foreign companies, foreign individuals and local companies controlled –directly or indirectly – by foreign companies or individuals. Another noteworthy restriction set by this law is that foreigners (as defined above) cannot own more than 1,000 hectares of rural land in Argentina.

Finally, it is also noteworthy that in December 2011 the criminal code was amended incorporating private banking (i.e., without the Central Bank's authorization) as a crime (one to four years of imprisonment).

What is the easiest way (sector), from a legal perspective, to do business or invest in Argentina?

Certain services supplying the local market, such as consultancy and accountancy firms, have little restrictions to operate in Argentina. Any export-related business will also have things easier as

compared to others. In general, any import-related business and business that require certain specific approvals (insurance companies, banks, etc.) will have more rigmarole and complications than others.

Are there any regulations, or legislation, that are enticing to foreign business/investment?

In general, there is little or no incentive for “foreign” business or investment as such. There are some incentive for companies from Mercosur countries (Argentina, Brasil, Paraguay, and Uruguay) and Mercosur-associated countries (Bolivia, Chile, Colombia, Perú, Venezuela and Ecuador) to do business in Argentina. These types of incentives are provided locally in the relevant provinces, such as Córdoba, the City of Buenos Aires or Salta. Regulations do not provide for what should be construed as a company from Mercosur. We have seen cases with a parent company from Europe or the U.S. with a subsidiary in one Mercosur country, having the subsidiary in the Mercosur country holding more than 50% of the stake in the local Argentina company, and this scenario was admitted by the local authorities.

With Argentina having a reputation as not the easiest place to do business, does this create an opportunity that could be attractive to the brave investor?

There are so many opportunities in Argentina with the economy growing at Chinese rates for the past years. The price for nearly everything in Argentina has increased dramatically in the past 5/6 years and will likely continue doing so. In real estate, commodities, services, etc., there are many opportunities waiting to be seized.

Other sectors have been underdeveloped, like the mining sector (with Argentina having one of the largest lithium reserves in the world), or the oil industry (with the recent discovery of massive shale oil reserves). In any event, like they say, “no pain no gain,” and one has to learn to deal with a government like this and be ready to push the deal to the end in order to make it happen.

What is the government stance on large foreign investors/acquisitions, e.g., from China?

The Government has tried to attract that kind of investment from China, but it has been difficult to develop something very organically.

What is the rationale, and potential outcome of the import/export policy, e.g., BMW exporting rice, Barbie dolls, etc.?

In that case it is a problem of the balance of payments. The government is trying to limit the amount of dollars leaving the country and therefore asks companies that import products to maintain their balance of payments balanced.

The government is trying to limit the amount of dollars leaving the country and therefore asks companies that import products to maintain their balance of payments balanced.

What is your outlook for Argentina in 2012? What do you see as being the biggest opportunities and dangers?

2012 will be more difficult than 2011. Salaries discussions will take place in April, the effect of the withdrawal of the subsidies to users of public utilities remain to be assessed, and a falling price for Argentine commodities could create some complications in 2012.

However, I still believe there will be many sectors that can reap great opportunities. For example, the meat sector has to be liberated soon and be able to export again and current meat prices are very low, with the tenderloin at AR\$60 per kilo, almost the same as a pizza; those prices for the meat should be accommodated. Other sectors, not so much dependent on the local market, such as mining, some services (call centers) and export-related sectors could see great benefit with a potential appreciation of the dollar vis-à-vis the Argentine peso.



Mexico's Outlook for 2012 and Beyond

ALI Asks the Experts



The uncertainty among investors regarding Mexico's future revolves around several main issues. One is the horrific, drug-related violence that has wracked certain areas of the country, and which has been covered sometimes sensationalistically by international media. Another is the country's close relationship with the U.S., whose recession Mexico could not evade, and from whose sluggish recovery it has had to extricate itself. Then there is the question of the upcoming presidential and congressional elections, as well as the widespread frustration with the current government's inability to usher through the reforms that many think are necessary for more robust investment in Mexico. ALI asked several experts for these opinions on these issues. Below are some of their responses.

■ Kevin Fisher, President, Dartmouth Research & Investing

On Violence: The rise in crime is affecting things at a number of different levels. There is a persistent fear, and I think a rightfully earned fear, on the part of investors coming in. But it's very geographically specific. Northern towns and cities are more affected than Mexico City is; I think Mexico City is so chaotic that no drug lord can control it, and that's the virtue of it. Personally, I've never seen serious crime in Mexico City, but of course it's there. As with any big city, you do have your crime threats. For an investor I would really think of it from the perspective of: pick your geography. There's still a lot of protection for projects being built and for tourism.

On De-Coupling with U.S.: For the first time Mexico is trending in a different direction than the U.S., and I think that's a good thing. It's still in pretty close lockstep with the U.S. economy, but its unemployment issues are not as severe as in the U.S.; their deficit is not as bad. This is primarily because they have a growing middle class and it's been consistently growing over the last ten or fifteen years, which has created sustained, internally generated demand.

On Outlook: There are a lot of other foreign investors who are looking at Mexico as a market that's not as radical as a China or an India might be; Mexico's business environment is similar to the typical Western economies, so there's that level of familiarity. Though there are still issues of Mexican law that make it somewhat challenging for investors to come into the market.

■ Jaime Salinas, Managing Director, Darby Overseas Investments

On Violence: Well, I think it obviously doesn't help [investment]. It is a problem particularly in the Northern part of the country, but it's business as usual in other parts. My sense is that the impact on investment is limited. The reason international investors have been looking elsewhere in the last two or three years doesn't have much to do with violence and security, but with other reasons.

On Outlook: Mexico's outlook is good.

The last estimate is that GDP is going to grow 3.7% this year. We have elections next year, and this is important. Everybody is expecting a change in the government, the party in control, and as we get closer to the elections, investment is going to be slower because, with changes in the administration, no one is going to want exposure to long term investment until the picture is clearer. Obviously this country needs to have more reforms; we don't know who the new government will be, but these reforms are critical. We especially need to have a government that allows private investors to invest in energy in critical sectors. But the prospects are good.

On Brazil: Most of the international investors have been more attracted to Brazil, where there's the possibility of investing in sectors where they can't invest or are not allowed to invest in Mexico, such as power, energy, and oil and gas. Brazil has been a story of growth in the recent years, but Mexico has had only a moderate increase in GDP, so it has not been a story of growth. But that's changing now, because I think international investors feel Brazil is becoming more expensive – valuations are much higher than in Mexico: with a ticket of US\$15 or 30 million you can buy control of a good company in Mexico, but not in Brazil. So I think they're looking back to Mexico and hopefully we'll see more international investors in the coming years.

■ Arturo Saval, Senior Managing Director, Nexxus Capital

On Violence: Yes, change has been perceived. It has been a negative issue in parts of Mexico, in some cities. And this is because, of course, we are neighbors to the largest drug market in the world. What we have been lousy at is marketing: it still shocks me when people say Colombia is a nicer place to do business than Mexico, when the last time I checked, they were one of the largest cocaine producers in the world and had lost a large portion of the country to guerillas. We are by no means in that position!

On Outlook: Reserves are at an all time high; the trade deficit is not there; the currency has been very stable. So the macro view is quite healthy. We have presidential elections next year and the outcome is going to be limited by the actual legal frame, which we think forces everyone to be not leftist or rightist, but centrist. And that is

essential, because, yes, there are some reforms, such as in energy, that won't pass under this administration and in this congress, but at the same time the good that we have, the independent central bank and certain regulations, will hold firm. So fiscally speaking, there will be no dramatic change.

On Brazil: Brazil for the last few years has received tons of money for PE, while Mexico was kept on the side. But in the last year and a half, there has been a change of attitude. The numbers show that the region as a whole has been more stable than the norm during and after the crisis, and in Mexico, even though we are closer to the U.S. and that slowed us down, our macro prospects are stronger than ever, even stronger than Brazil's proportionally speaking, in particular regarding inflation, as well as the leverage of the general consumer in aggregate: Mexico is still very underleveraged in terms of individuals and households.

■ Michel Montant, Director of Development, Grupo Posadas

On Crime: Tourism to Mexico has been affected. We don't know how much is due to economy and how much due to the bad publicity of security in Mexico, but it's definitely been affected: demand is down 3% to 8% from last year, which was already not very good in general terms. But how much of that is due to people in the U.S. not being keen for security or for economic reasons, it's hard to say.

■ Manuel Rodriguez Arregui, Director General, GBM Infrastructure

On Outlook: The jury is still out with what's going to happen with Greece and the E.U. and the banks' lending to Greece and so forth, and that's why you're seeing fluctuations in stock markets. But when you are talking about infrastructure, the issue is not the coming year, it's the coming twenty. You have to look at the medium and long term, and in Mexico those prospects are looking very good at this point.

The world's first economic bubble involved the collapse in the 1630's of the greatly inflated tulip market in the Netherlands. Since this period in the Dutch Golden age, referred to as "tulip mania," the flower industry has consisted mainly of regional players. In the 1960's flower exports from South America began challenging California growers, when the industry was concentrated near primary

employ 100,000 workers. According to a U.S. International Trade Commission report, "Fresh cut flowers were produced on 5,630 hectares in Colombia, on more than 500 farms. Most of Colombia's fresh cut flower production is located around Bogota, with small production areas in the Rio Negro and Antioquia regions around Medellin and Cali. Roses, standard and miniature carnations, and chrysanthemums account for al-

1983. According to Audubon Magazine, "Every year Americans buy about 1.5 billion roses, almost all of them from Latin America. Flowers have become the third pillar of Ecuador's economy, behind only oil and bananas. More than 90 percent of Ecuador's blooms are exported, primarily to the United States, and mostly for two holidays—Valentine's Day and Mother's Day." Ecuador has the advantage of 12 hours of

RED ROSES, BLUE SKIES

A Glimpse at the LatAm Flower Industry

■ Stephen Kaczor

markets in the E.U. and U.S. Also during that time, big changes over the previous decade saw growing operations increasingly located in regions with favorable climates and economic advantages due to the cost of land, labor, water, fertilizer and other resources.

Three major players in the current flower export market are Colombia, Mexico and Ecuador. Colombia is the world's second-largest flower exporter, and the Colombian Free Trade Agreement (passed last year) eliminated tariffs on cut flowers. A subsidiary of Dole is one of the largest growers in Colombia, where flower plantations em-

ploy 80 percent of Colombian production and exports. Colombia has ideal growing conditions for cut flowers, abundant labor and land, and high light levels, giving it a production cost advantage." Augusto Solano, president of the Colombian Association of Flower Exporters (Asocolflores) is considering the Mexican market as "an attractive option for Colombia cut flower exporters." Solano also sees possibilities in Japan, Poland and Russia.

Ecuador is known as the best rose grower in the hemisphere, a reputation quickly gained when the first roses were planted there in

sunlight year round and a favorable cost structure. They experience a slight disadvantage relative to Colombia in terms of freight rates, but benefit from lower labor costs. Fresh cut flowers are produced on 2,700 hectares on 264 farms with 50,000 people involved in direct production operations. Traditionally over 90 percent of the country's total cut flower production has been exported, mostly to the U.S. but also to the Netherlands and Russia.

Mexico is perfectly situated for flower exportation, but restrictions on U.S. imports of Mexican soil restrict potted plant



sales, while cut flower imports have been growing since Nafta passed in 1994. Mexico's flower export industry is in its infancy, with exports from 150 growers amounting to about \$100 million in sales during 2011. Last year, flower growers in the Mexican state of Baja California exported \$8 million worth of flowers to the U.S., making Baja California the only state to export almost all its floriculture.

Furthermore, lower costs in Mexico are one-fourth the prices realized by nurseries across the northern border, easily accessed by refrigerated trucks.

The global recession hit the floral industry hard in recent years, leading Dole, for example, to close operations at several of its many farms. Furthermore, the sector can be complicated due to issues related to

pesticides, packaging and shipment. With the economy showing signs of improving, however, the outlook is positive for flower exporters.

For more on the business of flowers, there are two excellent books, *Flower Confidential: The Good, the Bad and the Beautiful in the Business of Flowers* and *Guiding the Lily*, both by Amy Stewart.

Author Biography

Stephen Kaczor is Chairman of the Big River Foundation, a non-profit focused on river and watershed ecology conservation initiatives throughout the Americas. He is an organic farmer, eco-entrepreneur, consultant, and a writer with a documentary film in production in Central America. As a Panama-based consultant, Stephen's focus is sustainable organizational development, research & management. In addition to consulting and writing, he is passionate about sustainable agriculture, Latin American culture, travel, and the ecology. www.BigRiverFoundation.org – Healthy Rivers, Healthy Communities.

Unconstitutional regulation in Brazil

Foreign Land Ownership

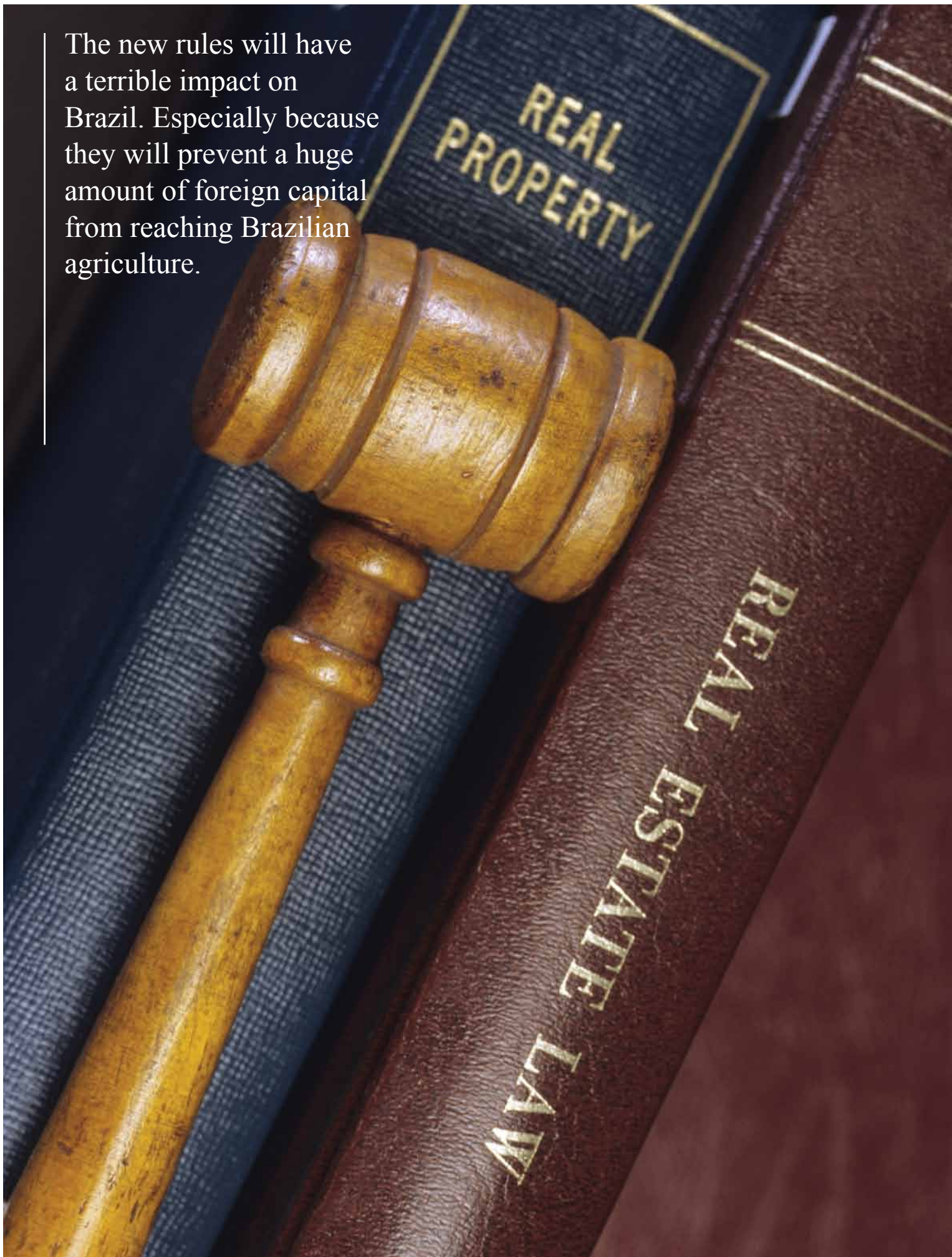
■ Adler Martins

The end of 2011 was not a good time for foreign investment regulation in LatAm. As predicted many times during 2010 and 2011, Brazil finally issued rules that severely restrict the purchase of rural land by foreigners, foreign companies and Brazilian companies with a majority of shares or quotas under the control of non-residents. (Instrução Normativa Incra n. 70)

First, a noteworthy assessment. The taxation over rural land in Brazil is negligible: it barely shows up in government statistics. The agriculture lobby, on the other hand, is one of the most powerful. And it has gained more and more influence as Brazilian industries are bending under Chinese competition. Now the agriculture lobby and some misguided rural producers' associations have managed to lead Brazil on a big lap backwards.

The new rules will have a terrible impact on Brazil. Especially because they will prevent a huge amount of foreign capital from reaching Brazilian agriculture. Other adverse impacts include the limitation of competition in the agriculture space and the concentration of production and land ownership at the hands of some already very big players in the Brazilian market.

The new rules will have a terrible impact on Brazil. Especially because they will prevent a huge amount of foreign capital from reaching Brazilian agriculture.



From a legal perspective, the new rules restricting purchase of rural land by foreign-controlled Brazilian companies are blatantly unconstitutional. The main reason is that the Brazilian constitution does not differentiate between Brazilian companies regarding the place of residence of its owners. They are all considered to be Brazilian companies, and that is it. The new rules are unconstitutional because they create a distinction between Brazilian companies and Brazilian companies with a majority of foreign capital, and to differentiate companies without a constitutional basis constitutes a clear violation of rights and a government-sponsored discrimination.

What the new regulation says

The new “Incra” regulations repeat and tighten the restrictions first established by Law 5.709 from 1971, which forbade foreign companies from purchasing rural land larger than 50 rural modules (a rural module varies from 2.5 to 247 acres, depending on the state) and only allowed foreign companies to purchase land if it was to be used for an agriculture project or other projects related to land use.

The total land owned by foreign companies was not allowed to surpass 25% of a municipality area. Also, companies of individuals of the same nationality could not own more than 10% of the same municipality area. There were also restrictions regarding national protection and security areas.

The same law provided that non-resident individuals could purchase land up to 3 rural modules (on aggregate) without restriction. The new rules are extremely restrictive. The new demands a foreign company must meet in order to purchase land are as follows:

- Approval of the project to be developed by the Ministry of Agriculture, after approval of a series of government bodies, including Incra and, where applicable, the Ministry of Industry and Foreign Commerce, Ministry of Tourism, the Brazilian Institute for the Environment (IBAMA) and the Brazilian Forest Institute, among others.
- For areas larger than 100 modules, authorization is needed from the National Congress.
- After both conditions are fulfilled, which may take one or two years, with luck, the foreign company must present a petition to Incra asking permission to purchase the land.
- Incra will scrutinize the company and the project and may approve the purchase, if all conditions are fulfilled.

How to avoid the restrictions

However, the rules have a weak spot: they do not prevent shareholder’s agreements. That is, a Brazilian company with 51% of capital in the hands of Brazilians, but in which the control power is in the hands of foreigners, is allowed to purchase as much land as it can. Thus, on top of being un-

constitutional, the new Incra rules are also flawed in that they still allow foreign companies to own land in Brazil, through the following procedure:

1. A foreign group or individual sets up a Brazilian company in which a Brazilian resident owns the majority of shares/quotas.
2. They enter into a shareholder’s agreement with the Brazilian party, establishing that the company control will remain with the minority shareholder (the foreigner), and also providing for a disproportionate distribution of profits.
3. This Brazilian company, which is controlled by the foreigner, will then proceed to purchase the land, without limitation.

This is, of course, only one possibility. It bears risk, namely future discussions between the foreign partner and the Brazilian partner. But it is a clear example of the new regulation’s flaws.

Finally, the new regulations are expected to be contested in court. At least one lawsuit has already been filed against them. Yet another bill is being discussed now, aiming at restricting the purchase of land even more, especially if the purchasing entity is a non-governmental organization

Adler Martins

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Argentina's Rural Land Law: Is This Just Nativism?

■ Wiener Soto Caparrós Law Firm – Buenos Aires, Argentina

Last week, in an extraordinary session before summer recess, the Argentine Congress enacted a controversial law to restrict foreign ownership of rural lands. Law 26,737, introduced by the Executive Branch, passed with almost no floor debate. According to statements made by public officials, the law protects national sovereignty over natural resources by, among other things, limiting foreign ownership of rural lands to 1,000 hectares (approximately 2,500 acres) for each foreign person. Supporters of the law point to the massive holdings of Benetton and Ted Turner (Patagonia) and Douglas Tompkins (northern Argentina wetlands) as examples of foreign wealth locking up sovereign resources. Read on for more about these restrictions and the disquieting uncertainties prompted by the law.

■ Summary of the Rural Land Law

The Rural Land Law restricts ownership and possession of rural land by natural and legal foreign persons. “Rural land” is broadly defined as “all land outside the urban area,” regardless of its location or use. While the Rural Land Law does not affect already acquired property and rights, it would affect future investments such as the acquisition of companies with rural land holdings.

■ Restrictions

The law imposes three restrictions on foreign ownership:

- Foreign persons may not own more than 15% of all rural land in Argentina.
- Of that 15%, no more than 30% may be owned by foreign persons of the same nationality.
- Any one foreign person may not own more than 1,000 hectares (roughly 2,500 acres) in any “cluster” (zona núcleo) (a term that is not defined by the law).

The Rural Land Law bans outright all foreign persons from owning coastal lands or other land adjacent to significant bodies of water. The law further prohibits foreign ownership of land within “border security zones,” absent consent from the Ministry of Internal Affairs, consistent with the exceptions and procedures established by law.

To implement its restrictions, the Rural Land Law calls for the creation of a “National Rural Land Registry,” a subdivision of the Ministry of Justice, and an Inter-Governmental Council of Rural Lands. The National Registry will be charged with creating a database of rural lands owned by foreign persons. Current rural land owners subject to the “foreign person” definition are required to notify the National Registry within 180 days of the release of implementing regulations by the Executive Branch (which has not occurred yet). Any change in the ownership of a legal entity holding rural land must also be notified to the National Registry within 30 days of its occurrence.

■ Defining Foreign Persons

Foreign natural persons are not defined by the law but presumably the term excludes both natural-born and naturalized Argentine citizens. The law exempts three categories of foreign natural persons from its restrictions:

- Those with 10 years or more of permanent and continuous residence in Argentina;
- Those having Argentine children and at least five years of permanent and continuous residence in Argentina; and
- Those married to an Argentine citizen for at least five years before acquiring the rural land (or interest in a legal person holding the land) and five years or more of permanent and continuous residence in Argentina.

As to legal persons domiciled in Argentina, the law defines them as “foreign” when:

- Foreign natural or legal persons own more than 51% of its capital;
- They are effectively controlled by any

foreign legal person (which is presumed when foreign ownership exceeds 25%);

- They have issued negotiable obligations or debentures, which allow a foreign holder to convert the instrument into equity representing more than 25% of the company's capital stock; or
- In the case of a trust holding rural land, when foreign beneficiaries have an interest in excess of 25%.

The law further declares rural land as a "non-renewable natural resource," the acquisition of which will not be considered a protected investment under any Bilateral Investment Treaty to which Argentina is a party.

Commentary: Whose Interest is Being Protected?

The Rural Land Law is fraught with uncertainty, making it hard to assess its application. The law is patently contradictory in

defining foreign legal persons (e.g., does a 51% or a 25% ownership threshold apply?). The law prompts obvious questions (e.g., would a foreign secured creditor be barred from foreclosing on a rural land mortgage? What is the consequence of exceeding a nationality threshold? If a quota system, does a perspective buyer await an opening? How are natural persons with dual nationality to be considered?). Some or even all of these questions may be answered by the Executive Branch when it releases regulations. Nonetheless, it is unclear when this will be done.

The absence of meaningful debate only adds to the confusion prompted by the Rural Land Law. While a government may rightly assure that a country's natural resources be available to its citizens, it would appear that the legislators have confused sovereignty with nationality. The owner's nationality does not affect the State's power to tax, to regulate, to condemn or even to expropriate in the pub-

lic interest. It is hard to understand the Rural Land Law as upholding any national interest, unless one accepts that the law will rightfully keep Argentine rural lands from being a world market commodity, thereby protecting the ability of Argentine citizens to acquire large landholdings without competing with foreign wealth. If so, it is hard to imagine the Argentine landed gentry as a class requiring the State's protection.

For more information on the Rural Land Law or on investment in Argentina in general, please contact Laurence P. Wiener (lwiener@wscllegal.com) or Mariela del Carmen Caparrós (mcaparrós@wscllegal.com).



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CKDs: The Marriage of Wealth and Growth

Mexican pension funds, or *afores*, have over US\$130 billion under management, about 11% of the country's GDP. Yet until recently, they were legally prohibited from investing in private equity. The restriction restrained the growth of Mexico's PE market: according to LAVCA, private equity flows were only 0.05% of GDP in Mexico in 2006, compared to 0.08% in the rest of LatAm and 3.96% in the U.S. Mexico was missing out on the trend among LatAm's fastest-growing markets, including Brazil, Chile and Colombia, where pension funds were beginning to invest in PE, much to those economies' benefit. According to Roberto Terrazas, a managing director at Nexxus Capital, Mexico's oldest PE fund, "Around the whole world, pension funds are one of the major investors in PE, accounting for about 30% of PE resources. But in Mexico, that possibility simply didn't exist."

The situation changed dramatically in 2009 with the advent of *certificados de capital de desarrollo*, or CKDs, a structured vehicle listed on the Mexican stock market that effectively allows pension funds to invest in private equity as though it were public equity.

As James Anderson of Tierra Capital Partners, a real estate private equity advisor focused on LatAm, explains, "The genesis of this product, which at the end of the day is equity, was a workaround to give pension funds the ability to invest in assets that otherwise would be prohibited from their investing plans. It is a customized product, so that pensions can simply buy CKDs instead of going the legislated congressional route."

In the words Manuel Rodriguez Arregui, the Director General of GBM Infrastructure, CKDs essentially give pension funds exposure to "the economics of private equity with the transparency of the stock market."

The Road to Reform

The reforms began back in 1996, when the Mexican government privatized the country's pension system, creating *afores*. Over the next twelve years, the restrictions on the *afores'* investment capabilities were progressively liberalized, as they diversified their portfolios from government bonds into public securities. In 2008-2009, the government finally decided to structure a vehicle that would allow *afores* to invest in private equity, particularly in the infrastructure and real estate sectors – just as pension funds in many countries are allowed to do, typically with about 15% of their portfolios. As Mr. Terrazas explains, the motives behind this move were to give the *afores* exposure to higher returns and to help channel the their massive amounts of capital into the development of the Mexican economy.

Mexican regulators established the rules governing CKDs on July 22, 2009. The certificates are issued by a given company via a trust, which receives its resources by means of its places on the Mexican stock exchange, Bolsa Mexicana de Valores (BMV). Regulations regarding issuance and corporate governance are based closely on the Mexican Securities Law. Disclosure requirements are strict but vary according to the stake a given CKD fund has in the company. A controversial aspect of the original framework was that capitals calls were not allowed. Instead, investors had to provide their capital to the fund up front. As Mr. Rodriguez Arregui explains: "For many institutional investors, this was not a good thing, because you had a negative carry early on. Now, however, after what Mr. Rodriguez Arregui calls a "positive change in the regulation," capital calls are allowed and CKDs do not have to be pre-funded."

CKDs are issued for four different areas of investment: infrastructure, real estate, pure pri-

vate equity, and distressed debt. As Mr. Terrazas explains, many of Mexico's 13 *afores* are now diversifying their exposure across those areas. CONSAR, Mexico's pension fund regulation agency, has established 8% of the *afores'* portfolio as the maximum that can be invested in CKDs. As of the end of Q2 last year, they had invested a total of US\$3.5 billion in CKDs, well below that maximum.

New Era

The first issuance of CKD came in October 2009 with, from a well established toll road company called Red de Carreteras de Occidente. In all, 16 CKD funds have been raised, by foreign and domestic managers alike, including Prudential, Macquarie, ProLogis, Vertex Capital, Wamex, I2, Conduit, and Nexxus.

Nexxus, Mr. Terrazas's firm, has raised five PE funds since 1997, their investments targeting mid-size Mexican companies with great growth potential. Their CKD fund, launched in 2010, was their fourth fund. Eighty-five percent of its investors are Mexican pension funds, while the rest are foreign institutional investors. (Though tailor made for Mexican pension funds, CKDs are available to all investors.) The fund was raised parallel to a traditional limited partnership fund (the firm's fifth fund); the two essentially constitute a single fund and will be invested in tandem pro rata.

Mr. Terrazas concedes that there are complicated aspects to the CKD: "You have to go through the stock market, comply with some regulations regarding the issuance of public securities, have a brokerage firm to help you with the issuance, prepare a public offering memorandum instead of private, and report to the public markets, sending some general information about your fund. Reporting and the complexity of the issuance are the two biggest drawbacks."

But he insists that, in spite of the restrictions and regulatory red tape, the benefits of CKDs outweigh any perceived drawbacks by far: “The negatives are small compared to the positives. It’s an extremely positive development.” The pension funds, he says, now have access to the higher returns typical of well-executed PE investments; the economy grows as a result; and more private equity transactions are taking place in Mexico. “That whole time [before CKDs], when we were raising new funds, international investors would ask how much was going to be invested from Mexican investors, and the reality was that there was just one domestic institutional investor, the Mexican Fund of Funds [a vehicle created by various Mexican development banks]; that that was the only institutional LP that invested in PE. But now that we are able to raise a fund with significant money from Mexican investors, it is great for the industry.”

Mr. Rodriguez Arregui, whose firm is currently raising a CKD fund that will invest in infrastructure, agrees, adding that the transparency and regulation of CKDs will help attract foreign investors who want exposure to Mexico’s growth but aren’t familiar with its market.

“Many institutional investors around the world have wanted to invest in Mexico, but they didn’t know the system, who was going to manage the money, with what transparency, etc. What CKDs will allow is for other institutional investors, such as insurance companies and sovereign funds, who we are looking for the economics of PE but want the transparency and governance of something that is regulated the way other public instruments are, to come in,” helping managers raise larger funds.

Emerging Skepticism

In spite of the nearly unanimous optimism for CKDs, there are some contrarian opinions, including that of Mr. Anderson of Tierra. He worries, first, about the quality and viability of some of the companies issuing CKDs. By his reckoning, not all CKDs are created equal, and he thinks pension funds should draw a distinct line between issuers who are already operating companies, with assets and positive cash flow, and those that are essentially startups looking for capital to get them off the ground.

“The problem with the latter is that, since these are basically PE structures that are listed on the Mexican bolsa, you are out of the gate cash flow negative because of fees, and when you combine that with the risk of a startup, my view is that we’re going to see a broad range of performance going forward, and it’s going to be hard for a chunk of these issuers of CKDs to actually make money for the investors.”

Mr. Anderson also worries that the strict terms and timetables according to which capital raised by CKDs must be invested and monetized will not work well in volatile markets such as real estate. “What happens if interest rates go up in three years and the deal you invested in all of a sudden needs another year or two to season? You’re going to be forced to take a loss or the terms are going to have to change. In a pure PE play, that is an agreement you can reach with your investors very easily; they’ll be amenable or not, but it’s a discussion between the manager and the LP. But in this situation, the way they went about struc-

turing these certificates, they’re not going to be able to renegotiate because there are going to be other interested parties, regulators, congress. It’s going to be very hard to change the terms, so I think in the case of some of these CKDs you’re going to see severe underperformance.”

“Our view,” he says in summary, “is that over time, on a risk adjusted basis, we believe the product will underperform, and in select cases we believe certain CKDs will severely underperform.” He and his firm are currently at work on a proprietary index to track CKD performance.

Mr. Anderson admits that his skepticism is “totally contrary to the industry” consensus, but says that it is based on conversations with various parties who have grown concerned with the problems he mentions. Nevertheless, he believes the CKD market is “going to grow exponentially in size. In the next five years it could easily go from US\$1.7 billion in issuance to over US\$10 billion.”



Private Equity in Mexico

Capitalizing on the Growing Middle Class

One of the most important stories in LatAm in recent years for private equity (PE) investors has been the growth of the region's middle class in terms of population and purchasing power. Exposure to consumer goods manufacturing and retail has been one of the best ways to gain exposure to the region's hottest economies, beyond the commodities exposure one tends to find on international exchanges. The same is true in the case of Mexico, and perhaps even more so, as middle-class consumer demand-related sectors are those least at the mercy of troubles in the U.S. and Europe, relying instead on the country's propitious demographics.

"When we started investing in 1998, the per capita income was US\$3,000," says Arturo Saval, the Senior Managing Director and a Co-Chairman of Nexxus Capital, the oldest and largest PE firm in Mexico. "Now it's close to US\$11,000 dollars. So the numbers are there."

Nexxus has raised five funds focusing on sectors with exposure to this middle class, including clothing retail, medicine, fast food, and health and fitness. They are also interested, Mr. Saval says, in insur-

ance brokerage, anticipating a demand that should increase as the middle class matures. Though Nexxus is sector-agnostic in principle, Mr. Saval explains, they have so far avoided infrastructure and real estate, as there is already significant amounts of money flooding those markets. They also focus on mid-market deals, in the US\$30 to 50 million range, avoiding the competition over pricier tickets. "These midsize companies have a harder time getting financing from banks," he says, "and we can be pretty selective."

Nexxus has raised five funds so far, making 16 investments, exiting out of 9 of them, with IRRs in the range of 22% to 28% in U.S. dollar terms. "We were able to obtain those IRR because we have been able to take three of our companies public, two of them being widely known." Those two companies are Homex, a housing company that listed in 2004, and Genomma Lab, a pharmaceutical company that listed in 2008. The third is a family health and fitness company called Sports World, which listed in 2010.

Nexxus raised its first three funds mainly from foreign offices and multi-laterals. Its

fourth fund targeted Mexican afores, or pension funds, taking advantage of a newly coined structured vehicle called CKDs. (See the article in this issue on CKDs.) The fifth fund was raised parallel to the fourth and the two will be invested together.

Mr. Saval explains the strategy behind some of Nexxus's most successful investments: "In most cases we have decided to invest in a given platform, investing in an initial company and then bringing together similar plays to consolidate within a region, expanding the platform in industries where there aren't any dominant players. For instance, we just invested in a fast food platform called Taco Holding, beginning with a master franchise of Crispy Cream and now comprising a local taco chain, a local burger chains, an ice cream chain; we are also acquiring the master franchise for Sbarro pizza. So we have two franchises, four domestic brands – six concepts and about 300 points of sale.

"Those are the kind of plays we're doing. We're doing something similar in apparel. When you add it up and put everything in same holding company, you have enormous leverage in terms of leasing spaces and pur-

“I would say the regulation that protects minority rights in Mexico is stronger than in Brazil, and for stability of agreements it’s easier to enforce and execute in Mexico. So there are very good conditions for PE funds to make money here. And obviously we have track records, so we can show the stories of investing, creating value, exiting, and generating very interesting returns. I think the opportunity is very good here in Mexico.”

chasing power. We love that kind of play. And in addition, there aren’t similar players on the Mexican exchange, so the road is nicely paved for an IPO.”

Darby Overseas Investments is another firm targeting the Mexican middle class. According to Jaime Salinas, the firm’s Managing Director, Darby has made ten investments in ten different companies in Mexico, completing the cycle in seven of those, and originating an overall IRR of 26%. It is currently in the process of launching a new fund with Mexican institutional investors.

“We focus on the US\$15 to 25 million range in terms of our investments,” Mr. Salinas explains, “across several industries, including consumer goods, pharma, housing, financial services. We focus on the mid market, where we can have control and influence the companies.”

“The penetration of PE in Mexico is still very low,” he adds, “about 0.4%, compared to 2% in Brazil. There are many opportunities out there. There are more than 30,000 companies in the mid market that could be candidates for receiving the support of a PE fund.”

There are other factors, too, which make Mexico more attractive than Brazil to foreign PE investors, he says. “I would say the regulation that protects minority rights in Mexico is stronger than in Brazil, and for stability of agreements it’s easier to enforce and execute in Mexico. So there are very good conditions for PE funds to make money here. And obviously we have track records, so we can show the stories of investing, creating value, exiting, and generating very interesting re-

turns. I think the opportunity is very good here in Mexico.”

Mr. Saval of Nexxus agrees that mid market opportunities abound, and emphasizes that the growth of Mexico’s middle class is still in its early stages. “This is a very young country: 20% of the country is younger than 15 years old. There is a demographic bonus that we have been tapping in for the last ten years, but there is still quite a lot of growth to come, and the middle class will keep growing and keep demanding world class goods and services. That’s what we want to do in essence: create world class, sustainable companies. And world class means keeping up with the standards of this growing middle class.”



Improving Mexico's Housing Finance Infrastructure

Kevin Fisher of Dartmouth Consulting & Research on the Necessary Reforms

The huge demand for housing in Mexico, especially in low- and middle income segments, requires that the country's financial infrastructure be reformed and improved, according to Kevin Fisher, the senior manager and principal strategist at DRC Mexico S.A. de C.V., the Mexican subsidiary of Dartmouth Consulting and Research.

"The Mexican market has huge demand right now," he says. "It is well capitalized through the activities of Infonavit. But the Mexican market itself is facing challenges in implementing the right infrastructure that really supports investors."

Infonavit is the private, state-supported fund that issues mortgages to employees in the formal private sector. According to Global Property Report, in 2011 it issued 66% of Mexican mortgages as of Q2. FOVISSSTE, a similar fund for public sector employees, issued 11%. The remainder were issued by private banks (20%) and SOFOLE's (special purpose non-bank financial institutions), mostly targeting the middle and upper markets.

Mr. Fisher and his firm have worked with a number of different regulators and agencies who issue mortgages to Mexican workers and debt to the capital markets to support those mortgages. Infonavit is one their clients, and he points to that fund as a successful case over the last few years. "Infonavit still the largest lender in terms of individual units of housing, which is the largest addressable need today. It was the only active issuer in the Western hemisphere in 2009, and that was because they had a base of in-

vestors. I'd like to think we had something to do with their success, since we worked on the initial design of the vehicles, how they were going to address the market, and how they could cultivate their investors and maintain full flow of information to them."

Mr. Fisher is familiar with the lower, middle and upper markets, having worked with institutions across the spectrum to develop their strategies and vehicles. "It doesn't matter if it's low or upper income. A loan is a loan. It's a matter of how you structure that loan and how you use it to support the lifecycle of the asset class you're financing."

"If you want to get into why the U.S. market has gone so wrong for so long," he adds, "there's just a complete mismatch between the type of instruments used and the type of assets used to fund the loans."

According to Mr. Fisher, a more supportive financial infrastructure would include an improved secondary market. "The secondary market for mortgage bonds, for example, is not truly supported from an infrastructure perspective; it still lacks real time pricing of the bonds, which limits the activity of investors in the secondary market. Those things need to be addressed systematically, by regulators. The regulatory framework in Mexico is lagging and keeping the market from following international trading standards."

A major symptom of the systemic problems, he says, can be seen in how the private sector is not going out to where the real market need is, in the low- and middle income seg-

ments, but staying up market where there is asset-based lending.

"Infonavit has been the only real strong player. SOFOLEs have been for the most part a failure. When they began they were given access to funds, but it was a free for all, and everyone went after the needs of the upper end of the market, which became saturated quickly. These people were allowed access to money for virtually no risk to build some US\$300,000 and US\$400,000 condos in Mexico City, when what you really need are many US\$40,000 homes."

He says that the root of the problem is the lack of a cohesive national housing and housing finance policy that "would take the edge away from prospective investors coming in." As an outsider looking in, he says, it seems that "the institutions that are set up to facilitate housing and housing regulation are in constant conflict with one another. This sends a conflicting message to prospective investors."

It is up to the government, he says, to give direction to policy, and it is essential that they look at the entire life-cycle of investments, instead of merely facilitating "one-off" transactions. "You're financing homes that will last 20 years, and the product needs to reflect that. There needs to be a commitment to changing the infrastructure related to how securities are issued to the market and how they're maintained over the long-term secondary market. Money will come if they take the barriers way."

Mexico City: Car Addiction

An Interview with Salvador Herrera Executive Director,
Center for Sustainable Transport - Mexico

Interview Provided by BNamericas

“The most important topic for 2012 will be the creation of an integrated public policy that benefits both mobility and urban development”



Urban mobility is high on the infrastructure agenda in Mexico. While highways continue to be a priority, the capital and other large cities across the country are looking to implement mass transport systems such as bus rapid transit (BRT) lines.

At the heart of Mexico City's transport policy is a contradiction that is typical of the country as a whole. The government is spending big on line 12 of the metro system and has introduced the first Metrobús BRT line in the country, but continues to concession the construction and operation of large toll roads, including the controversial Supervía Sur-Poniente highway.

In the following interview, Salvador Herrera, executive director of the center for sustainable transport (CTS), a non-profit organization supporting sustainable transport, speaks about the elements of a sustainable transport system, the structural limitations affecting policy implementation and Mexico City's addiction to the car.

What's the answer to mobility problems in Mexico's big cities: more highways or improved public transport?

The center's focus is on an integrated transport system. For the last few decades the country has focused on infrastructure dedicated to the car. We want to challenge this paradigm so that infrastructure is directed at different forms of mobility. This includes prioritizing modes of transport that contaminate less, and move more people in a safe and efficient manner.

Going by these criteria, the car loses its place atop the hierarchy – but that doesn't mean that the car should be completely discounted. We do, however, need to have a rethink to ensure equality for other forms of mobility that do meet these criteria.

Do you think Mexico City's mayor, Marcelo Ebrard, has focused too much on the car through large-scale construction of highways, or does the capital's public transport policy balance this out?

Mexico City needs a mobility agreement that includes the government and civil society, as it's difficult for a government to

manage mobility issues on its own. And it's especially difficult when there is resistance from civil society to do without cars.

A lack of quality public transport infrastructure keeps people in their cars, but that leads to more highway infrastructure, which in turn leads to more congestion. It's difficult to see a way out of this cycle.

Both the government and civil society have to make a sacrifice, as happened in Barcelona some years ago. The convenience of driving has to be balanced against the costs to society, such as contamination, congestion and noise.

The government must also invest in and prioritize infrastructure that gives wider benefits to society, even if these projects take more time and are more complicated to carry out. It is very easy to build a flyover because it is uncomplicated in terms of logistics and finances, but it is a very short-term solution.

A long-term solution such as the Metrobús bus rapid transit (BRT) system requires co-operation from far more stakeholders, so the government is discouraged from carrying it out.

Can the capital's Metrobús system be replicated across Mexico?

There are currently four Metrobús systems in Mexico. The model is replicable but the physical solution varies. The model gives priority to public transport, accessibility and reliability. The physical solution can vary a lot depending on the context of each individual city.

Tampico's plans to build a Metrobús system have met with opposition from transport concession holders. Is this a common problem, and if so how can it be overcome?

Yes, it's a common theme in practically all of LatAm. There is a certain resistance from concession holders in terms of new transport projects. Generally this is due to a lack of information.

The vast majority of cities don't have accurate information about mobility, so it is

difficult to conduct direct, open and frank dialogue with the concession holders. Many authorities decide to conduct studies in private before launching a project, and this causes a lot of tension because the concession holders and public wonder why they haven't been told. This information gathering should be part of the project and done more openly.

Do you think Mexico City residents can wean themselves off their dependency on cars?

I think it will be very difficult. Mexico City's dependency on cars cannot be viewed in an isolated context. Petrol is very cheap in Mexico, car tax is being revoked nationwide and the government has pushed for the commercialization of cars and the availability of individual financing.

On the other hand, there's the question of urban expansion. The most important topic for 2012 will be the creation of an integrated public policy that benefits both mobility and urban development. This has been done in Brazil and Spain, where people have realized that mobility and urban development are not completely disassociated components.

You mention Brazil – how do Mexico's mobility policies compare?

Brazil is structurally hierarchical. The federal government has clear responsibilities, its policies and institutions are well defined and, above all, the financing system is clear in terms of urban development and transport.

In Brazil, the national government retains oversight over the states and municipalities. In Mexico, it's the opposite. The municipal governments are free to choose their own routes and there is no consistency between them. There is also no institution that groups the municipalities together to create a uniform policy in terms of land use or integrated transport systems. As a result, the municipalities do the best they can with a certain amount of influence from the state and national governments.

In Brazil, if a mayor doesn't have an up-to-date urban development plan, he receives no funding from the national government.

If a mayor omits part of the development plan or changes it in order to grant favors, he would be immediately sanctioned. There are no such mechanisms in Mexico. Mayors receive investment with or without a plan and there is no institution that supervises the manner in which work is carried out.

Would a national public-private partnership law attract more investment and improve public transport services?

I think so, yes. There's plenty of space for the government to professionalize transport provision through private companies and through mixed public-private participation.

The most important aspect is the development of clear and transparent financial models under which the public sector does not take on an unbearable amount of risk. It is important that the public sector doesn't go off on any adventures, because the country's mobility is at risk.

What are the elements of a successful and sustainable transport system?

A good institution that is responsible for mobility, planning, construction, operation and maintenance is necessary. A battery of financial instruments in order to raise funds is also important.

In addition, there needs to be infrastructure that is accessible and convenient, that provides a large coverage and equal access across the city. In Mexico, we start with building the infrastructure and then we face the institutional challenge: how do we operate and finance the project? We don't look at access and equality until the end.

We need to change our short-term focus to something more long term that includes a more far-reaching agreement between government and society.

About the Author

Salvador Herrera is a town planning expert with 10 years' urban planning experience in Mexico, the U.S. and Spain. A former director of Chihuahua's municipal planning institute, Herrera studied town planning at the Autonomous University of Aguascalientes, urban development at the École Nationale d'Administration in France and has an MA in urban and landscape design at the Iberoamericana University in León. Herrera is a confirmed speaker at the BNamericas Mexico Infrastructure Summit - to be held in Mexico City from February 15-16.

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Investment Opportunities in Business Hotels and Affordable Tourism

Tourism has long been a staple of Mexico's economy. The country was the tenth most popular destination for international tourists in 2010, with 21.3 arrivals, contributing US\$11.8 billion to the economy that year. The majority of these tourists hailed from North America and Europe, with many destined for popular resorts such as the Riviera Maya and Cancún. Yet as investors look to capitalize on tourism and related industries in Mexico, the best opportunities are those that cater not to money-flush foreigners seeking their Caribbean tans, but the increasing amounts of Mexican and LatAm tourists from the region's swelling middle class, as well as business travelers navigating the lesser-known hubs of the region's growing economies.

Grupo Posadas is one company that has capitalized on the growth in precisely these areas. Based out of Mexico, where it owns and operates 200 hotels, it is the largest hotel company in the LatAm region, with operations in Argentina, Chile, and Brazil and plans to open hotels in Panama and Colombia soon. It currently has five-, four- and three-star brands, comprising 8,000 rooms, 10,000 rooms and 2,000 rooms, respectively.

Michel Montant, Grupo Posadas's director in charge of development of new hotels, explained that the company has thrived on the mid market. "We were one of the first companies to launch a four-star brand here, about fifteen years ago, and we've been very successful with that. We are the number one 4-star brand in Mexico, and we perceive that as our opportunity to be present in all of the region. Our growth is mostly going to be in three- and four-star brand, because of the growing middle class in the region and the lack of adequate, modern chain hotels serving those segments, especially in the middle-sized cities."

Grupo Posadas, Mr. Montant says, is capturing the growth of intra-regional travel: "There is tremendous growth there," he says. "A lot more Brazilians, Argentines and Colombians are coming to Mexico, and vice versa." But he stresses that where the real demand lies is in business hotels.

"The lack of lack of hotel infrastructure in the region is in business hotels. If you go to Brazil or the other LatAm countries, in a midsize city of 200,000 people you won't find any decent modern hotel property that meets the needs of the travelers. But there is an increasing amount of travel between these cities, more and more as the economies are growing; the economies are sort of dispersing in all of these midsize cities. Many of these cities in Brazil, for example, with more than a million people don't have decent hotel accommodation."

This perceived demand has shaped Grupo Posadas's strategy. "We are looking for important industrial cities that have demand for hotels by business travelers," says Mr.

Montant. “We look at a city of a certain size with industry and we look at the supply. If we see that the supply is old and not adequate to international standards, we are interested.”

He says that competition is starting to mount as international companies up their presences in the region, but that domestic companies such as Grupo Posadas have a distinct advantage.

“International companies are definitely looking at the region; they want to come in more

strongly. Most are already present but with five-star brand in major metropolitan regions. Now they are trying to enter the markets more strongly, but they aren’t willing to invest in development of hotels, which makes it difficult for them. Our advantage is that, since we’re a LatAm company, we have a deeper knowledge of the market and the investment community in the region, which helps us find partners to develop hotels. The region is growing and has good prospects, but it’s not easy: the land is not readily available and you need to have these relationships with partners and investors.”

After a solid 2011 during which occupancy was up again, revenue rose 10%, and his company was able to open about one new hotel per month, Mr. Montant says that Grupo Posadas’s goals in 2012 are to open 17 new hotels and increase revenue per hotel by 5% to 8%.

“We look at a city of a certain size with industry and we look at the supply. If we see that the supply is old and not adequate to international standards, we are interested.”



How Will European Banks' Problems Affect LatAm?

■ Bernard Lapointe

European banks provide 45% of all the external credit lines to LatAm. Could a pullback from their international lending activities affect the operations of LatAm companies?

According to the Bank of International Settlements (BIS), European banks provide US\$206 billion in credit lines to LatAm, making them the biggest providers of external funding for the region. Continued pressure from the financial crisis in Europe raises questions about the extent to which these banks will need to restrain or even reduce their global lending activities. One can assume that it will take time before European banks regain their ability and willingness to extend international credit at the pace they have during the last decade. Most of the international claims reported by the BIS are trade-finance-related and inherently short term.

For the region as a whole, the impact of such a potential deleveraging does not appear to be significant. However, some countries would be more vulnerable, namely Chile and Uruguay, where European banks provide 63% and 57% of total funding, respectively (Table 1).

Country	Total claims by European banks (USD bn)	% of total International claims
Argentina	9.9	46
Brazil	78.6	38
Chile	30.8	63
Colombia	7.6	45
Mexico	57.2	50
Peru	12.2	38
Uruguay	4.2	57
Venezuela	5.0	42
TOTAL	205.5	45

Source: BIS, HSBC

Table 1. International claims of European banks in LatAm

We look at a few factors that can be used to measure the impact of a shift in European bank lending on LatAm.

■ How fast can the current credit lines disappear?

Looking at the maturity of these loans can give us an idea of how quickly European banks could restrain credit. Data show that a significant amount of credit lines to LatAm corporates need to be renewed in the next 12 months, and apparently a majority are not being renewed. Short term maturities of less than one year account for 40% of international bank claims in Brazil and Mexico (Table 2). In the case of smaller economies like Uruguay and Colombia, that number is over 50%.

	% of total claims
Argentina	60
Brazil	40
Chile	49
Colombia	61
Mexico	41
Peru	57
Uruguay	58
Venezuela	33

Source: BIS, HSBC

Table 2. International claims by European banks, less than one-year maturity

What is the reliance of the region's economies on credit lines?

We use the ratio of European banks' claims on foreign exchange reserves (Chart 1). Here the data show that Mexico, Chile and Uruguay are quite dependent on European banks' funding, while Brazil, due to its high level of foreign reserves, is in a comfortable position. For Argentina and Peru, exposure to European banks funding is fairly low. In their case, this is the result of the limited access these two countries have had to international financing over the past few years.

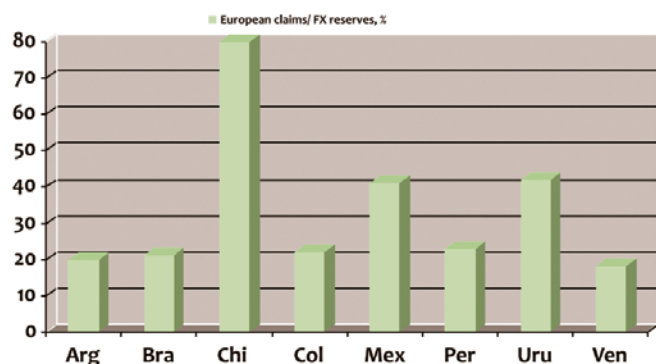


Chart 1. European banks claims as a % of international reserves, June 2011

Are there alternative sources of financing to fill the gap left by European banks?

The sheer size of the involvement of European banks in LatAm suggests that funding may turn scarce for a while and result in higher borrowing costs for exporters. There are already signs of retrenchment by some European banks in Brazil. Banco Santander, Spain's largest bank by market capitalization, which underwrote 11% of Brazilian debt sale in 2011, is currently not working on any large-sized underwriting deal.

Inevitably Asian banks will eventually step in but probably only gradually. Asian banks for the most part are very well capitalized-- in fact exceeding Basel III requirements-- quite experienced in trade finance and looking to expand globally. The three Japanese megabanks-- MUFG, SMFG and Mizuho-- in particular and a handful of Chinese banks could well become the next major funding partners for LatAm exporters. In the case of Mexico, the close association with its northern neighbor could possibly bring American banks to play a larger role in that country.

Regional development banks such as the Inter-American Development Bank (IADB) and Corporación Andina de Fomento (CAF) could also provide USD credit lines. BNDES in Brazil, a large development bank, will most likely be able to maintain access to capital markets even during a period of stress and supply exporters with reasonably priced credit lines. Other possible sources of USD liquidity are the central banks. In Chile, in 2008, the central bank provided liquidity through a program of swaps and repos to the country's financial system. Given the size of its foreign exchange reserves—US\$350 billion – the Central Bank of Brazil could auction a small amount of its international reserves to its domestic exporters.

What is the ability of LatAm exporters to absorb potential higher costs associated with a reduction of European banks' lending activities?

Industrial exporters are likely to be more affected than commodity-related exporters due to the real appreciation of some currencies in the region during the past decade. The Brazilian real has nearly doubled in value, in inflation-adjusted terms, since 2000. During the same

period the Chilean peso, the Colombian peso and the new sol in Peru have all appreciated between 18% and 26% in real terms. Commodity-related exporters have a better protection against higher funding costs because terms of trade in the region in general remain historically high (Chart 2). That is, export prices have risen faster than import prices, so higher funding costs are unlikely to erode export competitiveness and profitability.

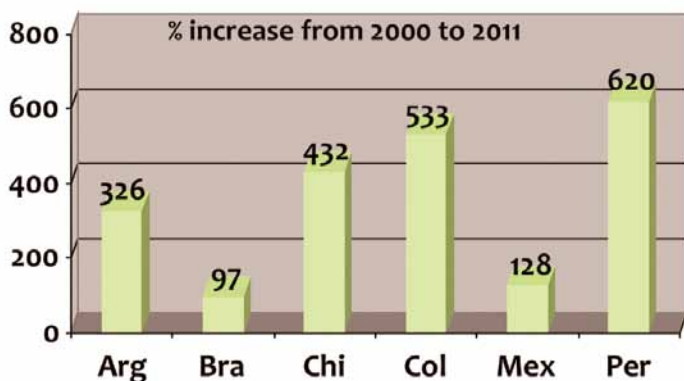


Chart 2. Terms of trade by country

Source: Bloomberg

Can the size of local subsidiaries of European banks become destabilizing?

Local subsidiaries of European banks in the region act like local banks due to their size. Their deposit base is domestic and in local currencies. Three of the five largest banks in Mexico and Argentina are subsidiaries of European banks as well as two out of the five largest in Brazil. In Chile, Banco Santander of Spain is the largest bank by far. However, local subsidiaries are generally independent of their headquarters when it comes to making decisions on funding activities. There is obviously a risk that local subsidiaries receive ‘orders’ from Europe to become more conservative in their lending decisions. That seems far-fetched, as the opposite is most likely: grow more aggressively overseas to compensate for a slowdown at home. Since LatAm as a whole is expected to experience GDP growth of around 3.5% in 2012, local subsidiaries of European banks are unlikely to suddenly stop credit expansion. Moreover, it is worth remembering that many of these local subsidiaries are listed on domestic stock markets, hence owing part of their capital base to local investors.

Conclusion

The risks to LatAm exporters arising from a reduction of European banks’ funding appear manageable. USD-denominated funding costs will likely increase during the first half of 2012. Industrial goods exporters, having suffered from a decade of appreciating currencies, are more vulnerable than commodity-related exporters. The latter will fare better because raw material prices remain high by historical standards, making the sector very competitive.

Chile and Uruguay appear most vulnerable due to their substantial reliance on funding from European banks. At the other end of the spectrum are Argentina and Venezuela, which have very little dependency on foreign funding. Brazil, Mexico and Colombia are in the middle.

Author Biography

Bernard Lapointe is a Portfolio Manager in the Overlay Strategies division at Caisse de dépôt et placement du Québec, a Canadian-based global fund manager. Mr. Lapointe has been a portfolio manager and trader of equities, currencies and commodities since 1994. He holds a Masters degree in Economics and speaks French and Mandarin.

The Mexican Investment Environment

Interview with Maximiliano Del Vento Assistant Vice President, Investment Solutions at the Partners Group

How is the Mexican investment environment taking into consideration the strong coupling with the United States?

Mexico's economy has always been strongly linked to that of the US; and more so since signing the NAFTA trade agreement in 1994.

The US is Mexico's largest trading partner, accounting for close to half of all of its exports and more than half of its imports. At the same time, for the US, Mexico is the third largest trading partner after Canada and China.

As an export-oriented economy, more than 90% of Mexican trade is under free trade agreements with more than 40 countries including the EU, Canada, and Israel, and much of Central and South America. However, the economy has not been able to break its strong ties with the US and Canada.

How has cartel violence affected investor confidence?

The drug war has definitely had an impact on investor confidence and the country's



economic perspectives, but it has not really represented a specific damage that can be quantified, taking into account that FDI is above 2005 and beyond levels. For 2011, preliminary figures are around USD 18bn (which is similar to the levels shown in Brazil). However, this view is not shared by all; although a clear majority agrees that there has not been a significant decrease in FDI, certain economic analysts have stated that violence in Mexico has taken away one hundred bps of GDP growth per year.

The Secretary of Economy states that FDI has not been affected, but rather re-configured. Certain states (in the Northern border) have seen closing of industries and shifting of investments to other areas of the country. Within these states the government has tried to generate more employment and more competitive processes for local players to grow and boost the regional economy.

Both foreign and national investors see Mexico as a long-term strategy; they believe the drug war will cease at some point. On a macro level, the country has proven itself stable with moderate growth, controlled inflation and a less volatile currency. With the creation of structures as SAPI's, minority shareholder rights have been strengthened; tax and structural reforms are being discussed; and there are friendly policies for investors.

Mexico has positioned itself as a competitive player in the global market. Rather than the drug war, the main concern in Mexico which still hinders investor confidence is trust in institutions and rule of law within them.

How is Mexico capitalizing on the growth of South America?

Mexico has been an associate member of the Mercosur since 2002, however relations between Mexico and the South American countries are limited. In the past, South American countries have linked Mexico to the US (especially from those countries with a more radical left leadership), considering it an outsider in the region. The strongest relationships Mexico has with Latin America are with Central America and with Colombia; the two closest regions.

Has Mexico seen a growth or change in investors from a geographic perspective? That is to say, interest from new regions, Middle East, China, India?

Not dramatically; the US is still by far Mexico's largest investor, however, according to official data from the Ministry of Finance, FDI flows from Switzerland and The Netherlands have increased substantially.

In Brazil, particularly, there has been a huge migration of citizens returning to their home country to work as opposed to NYC, London, and Miami. Has Mexico seen a repatriation of talent?

As opposed to Brazil in which there is a net inflow of talent into the country based on the growth prospects and economic potential; Mexico is still seeing an outflow of highly educated professionals seeking better opportunities.

Most would agree that a high percentage of Mexicans with a PhD degree immigrate to the US primarily due to better economic and security prospects. According to official data, there will be a 33% increase in educated talent leaving the country in 2011 (which represents approximately 20,000 people with higher education) vs. levels of 15,000 in 2005.

Fundraising & Alternatives questions:

What is the client demographic of Partners Group?

Partners Group's clients are primarily institutional investors based in Europe, North America, Latin America, the Middle East and the Asia-Pacific region. Over 85% of the firm's total assets under management is

managed on behalf of institutional clients. These include public and corporate pension funds, insurance companies, sovereign wealth funds, endowments, family offices, and banks.

Our client base is comprised of more than 450 clients across the globe, the largest of which makes less than 5% of the firm's total assets under management. This further illustrates Partners Group's independence and its diversified client base across types of institutions and geographies.

What is the global market's opinion of LatAm alternative assets? Too small, too risky, too illiquid?

Latin America has proven (in the majority of its economies) to have strong fundamentals, well capitalized banking systems, stable political environment, less volatile FX, steady growth rates, and controlled inflation. Certain microeconomic reforms and corruption-related issues still need to be addressed, but investor confidence in the region remains high.

We have been an active investor in Latin America since 2001. In January 2011, we opened a new office in São Paulo which serves as a base for Partners Group's investment activities and as an ideal hub to support further investments and the growing number of client relationships in Latin America. We have invested more than USD 1bn in Latin America in private equity, private real estate, private debt and private infrastructure.

With 580 million people and a GDP of approximately USD 6.2tn, Latin America has evolved to become an attractive destination for private markets investments in recent years. The ever-increasing interest

“Most would agree that a high percentage of Mexicans with a PhD degree immigrate to the US primarily due to better economic and security prospects.”

in the region is based on privatization and de-regulation rounds in certain parts of the economy, trade liberalization, stronger governance, a healthy banking system, prudent fiscal and monetary policies and a commitment to control inflation, a sharp decrease in real unemployment rates and a strong network of commercial and free trade agreements.

Even more important is the secular trend of growing consumer wealth and favorable demographics. Contrary to general perceptions, domestic consumption is the largest driver of Latin American GDP and accounts for 63% of regional GDP. Indeed, domestic demand grew by 8.5% across the region in 2010, with many LatAm economies posting double-digit gains, including Brazil, Peru and Chile. Also, a more equal distribution of wealth will result in a burgeoning middle class. All these have made the region very attractive for FDI into industry, capital markets and alternative investments.

Private equity fundraising has boomed: in 2010 fundraising by Latin-American focused private equity funds reached a new record high at USD 8.1bn, more than double the amount raised in 2009, according to the Latin American Venture Capital Association (LAVCA). Supporting this trend, the results of the 1H 2011 Mid-Year LAVCA report show that global investor appetite for exposure to Latin America remains high, with fundraising and capital inflows still growing at unprecedented levels, primarily driven by Brazil, but also with yearly improvements in Peru and Colombia. 55% of LPs stated that they expect to increase their commitments into the region in the next 12 months, on par with 2010. But a further 13% of respondents, or 68% of the total, said they plan to increase their commitment to the region over the next 36 months, up from 50% in 2010.

Access to leverage is still available at moderate levels (between 2.0 – 3.0x) and historically exits have materialized through equity markets (primarily in Brazil); but the joint venture of the Chile/Peru/Colombia stock exchanges provides an indication of the increased sophistication across these markets.

Statistics show that Latin America is quickly turning into the new private equity playground as limited partners and general partners alike are recognizing the region's untapped potential. Partners Group has long identified the potential in South America and has been investing in the region for over a decade. With the recently opened São Paulo office Partners Group intends to not only be closer to its investments but also to further foster sourcing capabilities.

How does this compare to alternative assets in other regions?

The majority of growth in new capital continues to be driven by a handful of markets, with funds dedicated to investment in China, India and Brazil collectively drawing 70% of capital raised between January and June, versus 50% in all of 2010.

*Partners Group
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In particular, China-dedicated funds raised USD 10.3bn in 1H 2011, putting China on pace to eclipse the USD 14.5bn raised in 2008. China's share of the fundraising total has risen to 45% of all capital raised through mid-year, its highest share to date. The increased pace of fundraising through mid-year was driven in part by greater participation from local investors. In China, Yuan-denominated funds drawing on local investors, including government agencies, accounted for 56% of the funds by number and 40% of the total capital raised. Unlike China and Brazil where the trend is towards localization of capital sources, commercialization is the theme for African funds,

which are increasingly drawing on a more international and institutional investor base, i.e., pension funds and asset managers, and relying less on financing from development finance institutions. Sub-Saharan African funds raised USD 1.1bn through June 2011. As with fundraising, a handful of markets accounted for the majority of deal activity. Again, China and India together captured 68% of the total invested, with USD 5.8bn going into China and USD 3.8bn into India, and 54% of transactions completed through June 2011, with 136 in China and 142 in India.

China's share of total investment volume (USD) has been steadily increasing, rising from 19% in 2008 to 41% in the first six months of 2011.

Although activity is concentrated in some of the larger and more mature private equity markets, investments took place across 54 countries in the first six months of 2011, including more nascent markets such as Honduras, Laos, Madagascar, Mongolia and Uruguay.

Have you seen a growth in exposure to emerging markets?

We expect LPs to accelerate their new commitments to EM PE to ensure exposure to high-growth markets. Growing skills and experience in the GP community and an improved risk-return profile are further factors positively influencing investment decisions.

Partners Group has been an active investor in emerging Asia since 1999 and in Latin America since 2001. We have one of the largest emerging markets teams with over 70 investment professionals who are culturally integrated, speak the local languages and have established an extensive local network.

Looking to the future, emerging markets have a huge untapped potential and many of them are making credible efforts to undertake domestic reforms to support sustainable economic growth. For those countries that maintain political stability and succeed with their structural reforms, the future is promising.

What is the general investment position of LatAm clients/HNWI? Are they increasing exposure to alternatives?

We are seeing a high level of interest from HNWIs and family offices, and expect allocations to alternatives to increase due to HNWIs need for capital preservation, inflation protection, diversification and enhanced risk adjusted returns.

Our experience is backed by findings of the 2011 World Wealth Report, by Capgemini and Merrill Lynch, in which, the allocation rate of HNWIs to alternatives is expected to increase to 8% by 2012.

To achieve the above, private markets asset managers together with wealth managers and financial advisors will have to familiarize HNWIs with the benefits of this asset class.

What fund raising methods seem to be most effective?

Our approach is to offer better client servicing. Our specialized and highly educated team of more than 60 investment solutions specialists ensures proximity to clients and focuses on their overall needs and long term plans. Each client has two dedicated investment solutions managers. They act as a central point of contact for client questions as well as information requests, ensuring timely and efficient responses. In addition to scheduled portfolio reporting, they visit clients regularly to foster knowledge sharing, strengthen long-term relationships, provide information on investments, discuss the market in general and give updates regarding comparable matters. Clients can also benefit from Partners Group's periodic conferences, education seminars, and comprehensive understanding of local regulations.

What are the top things investors are looking for in new products?

As interest in alternative investments grows, institutional investors in the region are demanding greater transparency, more robust administrative support and a seamless combination of services and sustainable performance. LPs are really 6

focusing on what GPs have done to deliver returns across market cycles. They are looking in detail at portfolio companies and what the value creation strategy has been for them. They are also putting emphasis on the stability, global footprint and deal sourcing capabilities of investment teams.

We offer our clients full exposure to private markets in private equity, private real estate, private infrastructure and private debt by combining direct investments, purchase of portfolio companies on the secondary market and primaries. Investing in this manner allows us to take maximum advantage of market opportunities at a specific stage of the economic cycle.

We consider this integrated, relative value approach to be the foundation for superior long-term investment performance for our clients.

Do you believe Brazil is over valued? What other LatAm regions look promising?

Overall, there is a strong interest in Latin America; probably decreasing in Brazil due to overheated valuations, although still strong, but increasing in Colombia, Peru, and Chile.

Apart from Brazil, Partners Group views Chile and Colombia as the most attractive private equity destinations within Latin America. Both countries have demonstrated great resilience throughout the recent economic downturn and offer promising economic outlooks. Chile is the wealthiest Latin American economy in terms of per capita GDP, which amounted to USD 11,828 in 2010 compared to Brazil's USD 10,816 according to the IMF. However, Chile has a much smaller population of 17.2 million, compared to 193.3 million in Brazil, 108.6 million in Mexico, 45.5 million in Colombia and 29.6 million in Peru.

According to LAVCA, Chile was the third largest Latin American private equity market in terms of 2010 investment activity, after Brazil and Colombia. Overall, 22 private equity transactions were closed in 2010 amounting to a total volume of USD 346 million. However, average deal sizes are relatively small and there are fewer exit

opportunities in Chile as was seen in 2010 with only one private equity exit. Moreover, despite increased interest, commitments by Chilean pension funds to local private equity funds are still relatively low, limiting the upside for secondary buyouts.

In Colombia, the case for private equity investing is supported by strong deal flow (19 deals amounting to a combined USD 475 million in 2010) and attractive protection of minority shareholder rights. In 2010, investment activity was focused around the energy sector which accounted for almost 70% of the total invested. Colombia has made impressive progress in terms of business environment as reflected by the significant increase in the country's ranking in the World Bank's "Doing Business Index" where Colombia gained 40 rankings between 2007 and 2011 when it came in in 39th place. In particular, Colombia ranks 6th highest in terms of investor protection, surpassing the USA and the UK. Also, there have been considerable improvements in corruption and the rule of law. These improvements led Standard & Poor to raise Colombia's sovereign debt rating to investment grade status in March 2011.

Finally, Peru reported an impressive 2010 GDP growth rate of close to 9% and is expected to post another strong year with projected growth of 7.5% in 2011. The country is a small economy with a 2010 GDP of USD 152.8 billion. In recent years, Peru has seen strong improvements in the "ease of doing business" ranking; business formation has been simplified and labor regulations are more flexible. Nonetheless, further progress is required in the area of property and minority shareholder rights protection as well as tax laws. From an investment perspective, we have become more cautious and are taking a wait-and-see approach with regards to sourcing further opportunities in the country.

How do you believe the European debt crisis is affecting LatAm ?

Whereas in the last two to three decades, many sovereign crises or defaults originated in Latin America, the table has now turned. Latin American countries are in a much bet-

ter position to withstand an external shock than at any other time in the past.

The European debt crisis could impact Latin America via lower exports and capital flows, however international trade between Latin America and Europe is relatively limited: Latin American economies export on average approximately 12% of their total exports to Europe. Thus, while a slowdown would certainly be felt, we do not believe it would considerably dampen growth as domestic demand remains robust.

The above is supported by the fact that central banks have turned more neutral or even more expansionary in their monetary policy stance. In the case of Brazil, for example, the central bank has already reduced its target rate. Regarding capital flows, while risk aversion has resulted in capital outflows, these are likely to be temporary as the strong fundamentals in Latin American have created an attractive environment.

In fact, Partners Group believes that the unfolding of the European debt crisis may turn into an opportunity from a Latin American perspective: on the back of the European debt crisis and the US's high indebtedness levels, Latin American investments look relatively less risky, and thus, more attractive. Higher real yields and the superior

growth outlook should attract foreign investments in the years to come. With world economic growth increasingly depending on emerging markets, Latin American – as well as emerging Asian – economies are well positioned to increase their importance and reach on a global scale

Maximiliano Del Vento, Assistant Vice President, Investment Solutions
Maximiliano Del Vento is a member of the investment solutions team in the New York office. His responsibilities include investment origination and client relations in Latin America. Prior to joining Partners Group, he worked at Merrill Lynch, Pierce, Fenner & Smith in New York, covering private clients and middle market institutions in Latin America. His responsibilities included asset allocation, manager due diligence and client relations. Previously, he was an associate at Bank of America Merrill Lynch global investment bank in New York, covering Financial Sponsors in North America. He holds a Master's degree in Corporate Finance from the University of Barcelona, Spain, an LL.M. in Law and Economics from the University of Torcuato Di Tella, Argentina, a Law degree (J.D. equivalent, with honors) from the University of Belgrano, Argentina and earned a Financial Risk Management Certificate from New York University.

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Cultural Patrimony: Valuations and Regulations

“When buying a work of LatAm art outside of its country of origin, it is critical to note if the work is listed as cultural patrimony and whether there are associated import or export regulations.”

■ ArtVest Partners LLC

As interest in LatAm increases and its art becomes a more meaningful component of global collections, there are important considerations buyers and sellers need to take into account. These issues are particularly critical for collectors who want to trade in LatAm art internationally.

Artwork classified as cultural patrimony – meaning it has ongoing historical, traditional or cultural importance – is often prohibited from being permanently exported from its country of origin. These works can be offered for sale by international auction houses but can only be sold to buyers who agree to keep them in their respective countries. In the May 2011 Latin American Art evening sale at Sotheby’s New York, a painting by Diego Rivera entitled *Peregrina Tlaxcalteca* was offered with this type of purchase stipulation. As part of the National Heritage of Mexico, the work could be sold in the New York sale but could not be permanently exported from the country. Similarly, *La Nube (The Rain)* by Dr. Atl (Gerardo Murillo), offered at Sotheby’s in the same sale, could only be released to a purchaser in Mexico.

When buying a work of LatAm art outside of its country of origin, it is critical to note if the work is listed as cultural patrimony and whether there are associated import or export regulations. When selling LatAm art internationally, promotion through a global auction house can increase awareness, but it is necessary to be conscious that cultural patrimony cannot leave its country, which may limit prospective buyers.

Mexico and Peru have very strong patrimony laws, and collectors should be knowledgeable about whether or not their collection can be exported and if special permits are required. In addition to country-specific export laws, U.S. law also expressly restricts the import of any pre-Colombian monumental sculpture and murals from Central and South America, certain archaeological objects from Guatemala, El Salvador and Peru and Colonial period objects, such as paintings and ritual objects, from several LatAm countries. Even if these items are exported, importation into the U.S. is permitted only when accompanied by an official export permit. Objects currently in the U.S. that fall into these categories were either im-

ported prior to restrictions taking effect or were brought into the country illegally, so be wary if there are no official papers accompanying a work you are considering buying.

These laws and regulations derive primarily from the provisions set forth by UNESCO, The United Nations Educational, Scientific and Cultural Organization, which, in 1970, hosted a convention dedicated to prohibiting the illegal import, export and transfer of cultural property. Summaries of these laws for Mexico, Peru and Venezuela are accessible on the website for IFAR, the International Foundation for Art Research (www.ifar.org).

Regulations also exist barring the trade of certain materials and endangered species. According to United Nations law, licenses are required to import tortoise shell, bird feathers, mother of pearl, certain woods including Brazilian rosewood, red coral and most ivories. Many LatAm Colonial items, such as furniture, decorative boxes and traveling chests include some of these materials and therefore cannot be sold on the international market. Mexican col-

lages in the plumaria tradition are made of bird feathers and are thus subject to restrictions, as well. Generally objects containing any parts of an endangered species cannot be imported or exported, and permits from Fish & Wildlife Services are obligatory for many types of flora and fauna. Bans on the international trade of endangered species has significant implications for LatAm art, which often includes these restricted materials.

Valuations are another critical consideration for those buying and selling LatAm art outside the region. The concept of fair market value – meaning the price at which a willing buyer and willing seller will make a deal – is an American concept. In LatAm, appraisals are generally completed on the basis of replacement value, which can be considerably higher. When bringing works onto the international market, sellers should be aware that valuations can vary widely based upon location. A replacement value in a regional market may not correlate to a set of auction house estimates in the U.S. Having your artwork appraised by a professional who considers the value on the international marketplace will give you a more realistic idea of the price your works can fetch outside of LatAm.

Cultural patrimony, import and export regulations and valuations are just three of the essential factors with which international buyers and sellers of LatAm art should be familiar. Regulations, laws and professional practices differ in each country, and serious collectors should always consult seasoned professionals for guidance.

About ArtVest Partners LLC

Artvest is an independent advisory firm that provides investment advice for the art market. With three decades of experience in art and finance, Artvest offers impartial guidance and custom strategies for acquiring and selling art, protecting art wealth and passing it on to future generations. Artvest fills a need in the market by introducing a disciplined financial focus for collectors at all stages.



Lot 43
Dr. Atl (Gerardo Murillo)
La Nube (The Rain)
signed lower right
oil and Atl Colors on masonite
31 1/4 x 38 3/8 in. (79.4 x 97.5cm)
Est. \$250/300,000
Sold for \$326,500



Lot 48
Diego Rivera
Peregrina Tlaxcalteca
signed and dated 1946 upper left
oil on canvas
26 1/4 x 18 1/2 in., 66.5 x 47 cm.
Est. \$250/300,000
Sold for \$278,500

Understanding the Mexican Mortgage:

Interview with José Jesús Gómez
Dorante, CFO of Infonavit



Tell us about Infonavit.

Infonavit is the Largest mortgage lender in Mexico. Every year we issue almost half a million mortgages, and we have a portfolio of almost five million mortgages total. Our balance sheet, depending on exchange rate – which is very volatile – is about US\$60 billion. Infonavit's mandate is to lend to formal private sector workers in Mexico. The Mexican constitution mandates that employers supply housing to employees, and our institution was created to enforce that mandate. It was created in 1972, funded through contributions of employers on behalf of every worker: 5% of every salary. That is the source of the fund capital of the housing fund we manage; every two months we collect 5% of private sector payroll in Mexico and invest that in mortgages. Total cash flow for any given year is about US\$10 billion.

How has your need for capital changed in recent years, with the Mexican middle class growing so rapidly? Is the market now undercapitalized, over? Where are you meeting the demand for housing?

We are mostly funded through these payroll contributions. Obviously, over five million mortgages on our balance sheet creates a huge cash flow, so funding is not really a relevant issue for us. We only use capital market funding through issuers of mortgage backed securities, but those represent only about 10% of our total funding at the most, and these securities don't affect our balance sheet. On our balance sheet we have zero pesos of debt.

“Our official projections for now are assuming very moderate growth, positive but moderate, and the reason is that we haven't seen a sustained high growth rate of formal jobs in Mexico.”

How has the demand for mortgages changed in recent years?

Early last decade, there was a huge backlog of demand that had accumulated for a number of years. In the 1980s and 90s, there was a lot of market volatility in Mexico and there was not an active mortgage market, so we had a significant growth rate just to meet that backlog. In 2000 we originated about 200,000 loans, and we went from there to almost half a million in 2006. Afterwards we saw the stabilization of our lending program; there was a decline in 2009 because of the global crisis, but we've returned and will probably set a new record this year. But the growth rates we saw between 2001 and 2005, double-digit growth rates, are now behind us and we're seeing more stable growth.

How is the demand met on the other side, in terms of construction? Is there enough being built to meet the demand of workers who need housing?

I think so, yes. We have to make a significant distinction between those segments of the Mexican population that are currently being served by Infonavit and Fovissste, a similar fund that has a mandate to serve government employees, and those segments of the population that are working in the informal economy or are not formally affiliated with our fund. The latter represents the largest chunk of the population, and they are probably not being served adequately, as they probably don't have access to formal housing finance. If you ask me if there is an adequate supply of houses to meet the demand – yes, there is for the segments of the population being served by Infonavit. For the other segments of the population, I wouldn't be able to say the same

Does Infonavit handle low-income housing, too?

Yes. Most of the lending we do goes to low-income individuals. But they are low-income formal workers – someone working as a Walmart cashier or in power plant, for example. We're not lending to someone selling food in the street, for instance, because they are most likely informal workers.

What are your projections for the coming years? Will there be an increase of demand as the Mexican workforce and middle class grow?

It's very difficult to predict. Our official projections for now are assuming very moderate growth, positive but moderate, and the reason is that we haven't seen a sustained high growth rate of formal jobs in Mexico; for us to be able to assume higher rates, we would have to expect labor law reforms

“If you ask me if there is an adequate supply of houses to meet the demand – yes, there is for the segments of the population being served by Infonavit.”

in Mexico, or something that transforms the employment dynamics in the country, which obviously we cannot forecast. They can take place, but it's not our role to forecast about that. But let me emphasize this: There is huge demand for housing in Mexico. The problem is that most of the demand comes from segments of the population that are not being currently served by formal housing finance.

What are your lending criteria as an institution?

We are able to collect the mortgage from a direct payroll deduction that we do from every single worker, so as long as the worker remains formally employed, we have zero credit risk. That basically determines our underwriting criteria. We have a scoring

ample, being a fiscal authority: the collection of the contributions for the mortgages is a fiscal obligation for employers. But we are not a government institution. I am not a government employee, we don't get funding from the federal budget, from taxes. So it is a unique situation. We consider ourselves a private sector institution.

Where does the ownership of the company lie?

That's a very good question. Our total equity base right now is about 80 billion pesos, but the reality is that we don't know who the owner of that 80 billion pesos is. Every single worker in Mexico that has an active account with us is somehow our shareholder, but that is around 40 million individuals. The reality is that we don't spend

philosophy has always been to have a strong institution that is isolated from political circumstances.

What are Infonavit's goals in 2012?

As I said, this is going to be a record year for us, in terms of our lending program. The most mortgages we originated in a given year was 494,000, in 2008; we think for the first time this year we are going to break the half-a-million mortgages mark. But we have been working over the last few years on making a stronger emphasis on quality of life for the people we lend to, rather than just issuing a loan. Although we are not responsible for housing policy in Mexico, since we're the largest player in housing finance in the country we do play a role in the way cities are developing, so we are fo-

"The most mortgages we originated in a given year was 494,000, in 2008; we think for the first time this year we are going to break the half-a-million mortgages mark."

model that tries to distinguish those workers that have a higher likelihood of staying part of the formal private sector from those who are more likely to switch to the informal economy, and since we are able to collect that information and are part of the formal social security of Mexico, we have all the labor and salary employment information from every single worker in Mexico. So we're pretty much like "big brother": we know where you've worked how much you have made in the past. So based on that information, which is all in our databases, we are able to develop a scoring model to determine who is more likely and less likely to stay.

Is Infonavit a government institution or does it operate privately?

We were created by a presidential decree and we have some powers that were granted to us by the Mexican government – for ex-

a lot of time wondering who owns us. We have a management philosophy that we try to put in place and follow. The lawmakers that created Infonavit 40 years ago didn't really determine the question of ownership, but at some point in time someone is going to have to do it.

What are your thoughts on next year's elections? What changes will that bring for your business?

It's difficult to say. We do believe the housing policy in Mexico has to be a state policy rather than a political party's policy; in the end, the need for housing comes from demographics, not politics. And obviously the Mexican population requires housing finance institutions. We have a very strong corporate government, and I think we'll be vigilant in maintaining sound management practices here at Infonavit. We can't forecast what will happen next year. Our

cused on creating more synergies with other institutions, both public and private, to have a better urban development policy in Mexico to create better quality of life. In Mexico we have been so successful increasing our lending program that many municipalities have not been able to keep up the pace, and that has had consequences in terms of the provision of public infrastructure in some cities, the development of roads, water, etc. Infrastructure is not going at the same pace and that creates bottlenecks. We're making sure that we align more of those policies so we can ensure that the quality of life of whoever purchases a house with a loan from Infonavit is better. We have made major efforts there, and I think we have a very well defined strategy and we should continue to see improvements in that area.

Trading LatAm Currencies in 2012:

“Steady
As
She
Goes”



■ Tom Cleveland

Emerging market economies have been the “darlings” of the investment world over the past decade, and LatAm has not been an exception. Stocks have soared in price, appreciating by sizeable multiples over the period. But 2011 was a year of correction marked by uncertainty, as the long-anticipated global economic recovery stalled and Europe wobbled on the brink of collapse. LatAm economies, highly dependent on the commodity export trade, also stalled, but weakening currencies were welcomed as 2011 concluded.

Currency Trends in 2011

Currency markets were in flux this past year. Uncertainty was the hallmark, driving volatility to levels not seen since the early days of the recession and forcing many investors to the sidelines in search of “safe havens.” To review the impact on LatAm currencies, the best source available is the JP Morgan Latin America Currency Index maintained by Bloomberg.

The index comprises weighted values for six currencies versus the U.S. dollar. The six countries, constituting 85% of the GDP in LatAm, are Argentina, Brazil, Chile, Colombia, Mexico, and Peru. Success has drawn investment capital over the years, accounting for a portion of the general appreciation in currency exchange rates. The average for the index for the past five years has been 112, just above current valuations.

If prices had been plotted for ETFs related to LatAm stocks or general building commodities, the same pattern would have emerged. Quantitative easing in the U.S. weakened the dollar for the first half of the year, but the uncertainty in Europe raised doubts as to whether a global economic recovery would take shape and return demand for commodities and other exports. As a result, the year ended with LatAm currencies bound in a “ranging” corridor, waiting for signs of improvement.

What are the prospects for currency valuations in 2012?

Near the end of 2011, favorable economic data began to surface in the U.S. economy, signaling a modest recovery that hopefully can withstand the lack of activity across the Atlantic in Europe in 2012. Experts expect the dollar to continue to appreciate and for growth to begin ascending once again in Asian markets. LatAm exports also fuel the industrial engines in Asia where officials have modified growth estimates to reflect lesser demand in the West.

Japan will recover from its natural disasters as the “USD JPY” currency pair moderates, but the world’s Forex market will continue to be racked by volatility. Uncertainty in Europe will disrupt capital flows across the globe, but a strengthening dollar does not necessarily mean that LatAm currencies will weaken. Foreign investment will return, as well as demand for commodities, as the global recovery gathers steam.



Government officials may wish to weaken currency valuations in order to encourage export trade, but these actions may trigger higher inflation. Currency controls may cause unwanted repercussions. It is better to raise interest rates, as investors would prefer, thereby ensuring a return of much needed foreign capital.

Concluding Remarks

Timing will be everything in 2012. Economies the world over will be walking a tightrope of sorts as Europe continues to muddle along. LatAm, on the other hand, is primed for positive growth, as long as the global economic recovery puts pressure on commodities. Currencies in the region may fluctuate within manageable levels, but the catchphrase will be "steady as she goes" for the year.

Author Biography

Tom Cleveland of Forex Traders has had an extensive career in the international payments industry with over 30 years of experience in executive management, corporate governance and business development. Tom served as CFO for various Visa International entities from 1980 until 1999, retiring with the title of Group EVP and Treasurer. While at Visa, Mr. Cleveland was instrumental in expanding the global reach of the Visa system, building the necessary financial and settlement infrastructure to support that growth, designing and deploying global risk management processes, and securing necessary regulatory approvals for existing operating standards. The Visa forex system cleared and settled over \$5 billion a day in 22 currencies at that time. He has also built and operated a private payments network connecting twenty countries, specializing in B2B, C2B and C2C cross-border payments. Mr. Cleveland earned an engineering degree from Georgia Institute of Technology and did graduate work in Finance at Georgia State University. Currently, Tom writes for ForexTraders.com and offers a lot of insight by expressing his ever-growing investment knowledge.

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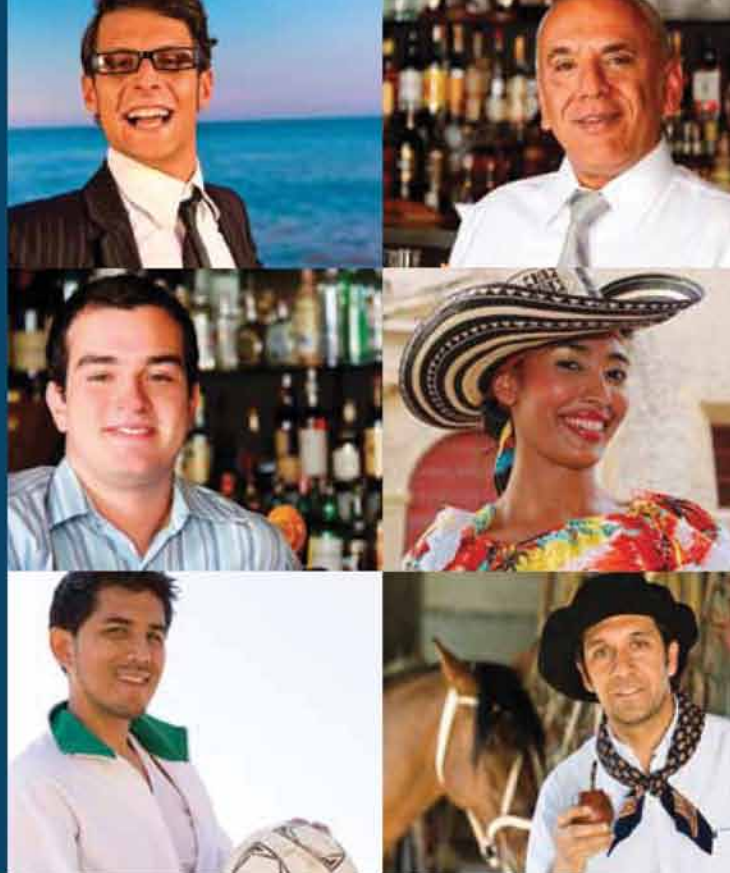
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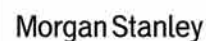
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