LATIN AMERICA ADVISOR

A DAILY PUBLICATION OF THE DIALOGUE

www.thedialogue.org

Friday, January 12, 2018

FEATURED Q&A

Why Are Companies Making Fewer Deals in Mexico?

Mergers and acquisitions and other deals have slowed in Mexico for a second straight year. // File Photo: Pexels.

Q Dealmaking by Mexican companies declined in 2017 for the second consecutive year, according to data compiled by Dealogic. Mergers and acquisitions involving Mexico-based companies amounted to $23.7 billion last year, a 5 percent decrease from 2016. What are the main reasons behind the decline? Will M&A continue declining this year in Mexico? Which sectors are the most affected by the trend?

A Amy Glover, CEO for Mexico at Speyside Corporate Relations: "It is natural that with uncertainties like the NAFTA renegotiation and the presidential election hanging over the Mexican economy this year, investors may be hedging their bets in the short run, particularly in sectors like the automotive industry. A 5 percent decrease is hardly a damning trend, however, and with the depreciation of the peso this year, there may well be interesting deals to be made in acquiring companies with promising medium- to long-term prospects. Mexico remains an attractive country for investment, with 120 million people, most of whom are in their late 20s. It is no secret that many companies based in Mexico praise the productivity and commitment of the country's workforce, particularly in engineering. The country has a privileged geography that ties it to North America, Latin America and countries across the Pacific, and with 12 free-trade agreements covering 46 countries, Mexico is one of the most open economies in the world. Mexico's energy market remains too interesting to ignore, both in terms of oil and gas and renewables, despite uncertainty over public

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TODAY'S NEWS

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Four Confirmed Dead in Sinking of Boat Carrying Venezuelans

In addition to the confirmed deaths, 28 people are missing after a boat carrying Venezuelans heading to Curaçao sank in the Caribbean.

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Fiat Chrysler to Move Heavy Duty Truck Production From Mexico

The automaker said it will invest $1 billion in its Warren truck assembly plant in Michigan and move production of its Ram Heavy Duty truck there from Mexico.

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Standard & Poor's Lowers Brazil's Credit Rating

The ratings agency lowered its credit rating for Brazil further into junk territory, a defeat for Finance Minister Henrique Meirelles who had sought to avert a downgrade.

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Meirelles // File Photo: Brazilian Government.

ECONOMIC NEWS

S&P Cuts Brazil's Credit Rating Further Into Junk Territory

Ratings agency Standard & Poor's on Thursday lowered its credit rating for Brazil deeper into junk territory, citing the country's failure to approve President Michel Temer's pension overhaul, Bloomberg News reported. S&P lowered its long-term rating for Brazil's sovereign debt to BB- from BB with a stable outlook. The new rating is three notches below investment grade and is the same as S&P's ratings for the Dominican Republic, Bangladesh and Macedonia. "Passage of legislation to structurally reduce the fiscal deficit remains elusive, creating difficult conditions for the next administration, given Brazil's high and rising government debt," S&P sovereign analysts Lisa Schineller and Joydeep Mukherji wrote in a note, the Financial Times reported. In response to the downgrade, Brazil's Finance Ministry said it is still determined to win the approval of pension and other reforms and also to strengthen the country's budget by postponing salary increases for public workers. "The federal government maintains its commitment to fiscal consolidation," the ministry said. "We always count on the approval of the measures necessary for the country through the congress, and we are certain the same will continue to work in favor of the reforms." Finance Minister Henrique Meirelles has pushed for fiscal reforms, but lawmakers have been reluctant to support changes to the pension system in an election year. S&P's decision marks a defeat for Meirelles who met late last year with officials from the three major ratings agencies in an effort to avert a downgrade, Bloomberg News reported.

SUBSCRIBER NOTICE

The Latin America Advisor will not be published on Monday, Jan. 15 in observance of the Birthday of Martin Luther King, Jr. holiday in the United States. We will resume publishing on Tuesday, Jan. 16.

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policies in the sector after the presidential election. There are also important potential acquisition plays in the tech space that may make sense, given that e-commerce is growing, but still has significant upside. Despite the U.S. tax reform, business groups in Mexico estimate that the effective corporate tax rate differential between the United States and Mexico comes to around 7.5 percent—not minor—but not a factor that will radically alter investment and merger and acquisition decisions in the long run."

A **Amanda Mattingly, senior director at The Arkin Group in New York:** "Uncertainty about the future of the North American Free Trade Agreement (NAFTA) is the number-one factor contributing to the decline in M&A activity involving Mexico-based companies in 2017. Concerns about the security situation in Mexico have plagued the country and negatively affected the business environment for some time, and misgivings about the upcoming presidential election in July and the prospect that Mexicans could elect left-leaning nationalist Andrés Manuel López Obrador are factors as well. But the overriding issue pertains to NAFTA, the stalled negotiations among the parties, and to what the dissolution of the agreement would do to the Mexican economy. In recent years, the Mexican economy has expanded slowly at an average rate of barely 2 percent, with 80 percent of Mexican exports going to the United States. If the United States were to withdraw from NAFTA, Mexico could expect GDP growth to decline, the peso to suffer, foreign investment to decline, capital flight likely to occur, and exports to plummet amid Mexico's ongoing search for new trading partners and trade agreements with countries in South America, Europe and China. The dislocation to the Mexican

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NEWS BRIEFS

Trump Denies Vulgarly Disparaging Countries at Immigration Meeting

U.S. President Donald Trump this morning denied vulgarly disparaging some countries during a meeting Thursday with lawmakers in the Oval Office. Trump reportedly became frustrated during the discussion on protecting immigrants from Haiti, El Salvador and Africa, saying, "Why are we having all these people from shithole countries come here?" according to several people briefed on the meeting, The Washington Post reported. However, Trump tweeted this morning, "The language used by me at the DACA meeting was tough, but this was not the language used." He added, "Never said anything derogatory about Haitians other than Haiti is, obviously, a very poor and troubled country. Never said 'take them out.' Made up by Dems. I have a wonderful relationship with Haitians."

Four Confirmed Dead as Boat Carrying Venezuelans Sinks in Caribbean

Four people have been confirmed dead and 28 more missing after a boat filled with people leaving Venezuela sank in the Caribbean waters, Venezuelan authorities said Thursday, the Associated Press reported. The boat carrying 34 people left for Curaçao on Tuesday, Venezuela's Regional Civil Protection director said. He said two people safely swam to Curaçao.

Thousands Protest Pardon of Peru's Fujimori

Thousands of Peruvians took to the streets in protest of President Pedro Pablo Kuczynski's pardon of former President Alberto Fujimori from his 25-year prison sentence, the Associated Press reported. Thursday night's protests in Lima marked the second time Peruvians have joined in mass demonstrations against Kuczynski's decision to pardon Fujimori.

POLITICAL NEWS

Ecuador Grants Citizenship to Wikileaks' Assange

Ecuador on Thursday announced it had granted Wikileaks founder Julian Assange citizenship, The New York Times reported. The announcement escalated a standoff with Britain hours after the country rejected Ecuador's request to grant Assange diplomatic immunity so that he could leave the Ecuadorean Embassy in London, where he has been living since seeking political asylum 2012. "Ecuador knows that the way to resolve this issue is for Julian Assange to leave the embassy to face justice," Britain's Foreign Office said in a statement. The office added that it was not in talks with Ecuador's government on the matter. On Tuesday, Ecuador said it was seeking an arrangement to allow Assange to leave the embassy, saying it would be "unsustainable" for him to live in the embassy indefinitely. He first sought asylum after Sweden sought his arrest in connection with allegations of rape and assault. Sweden is no longer seeking his extradition, but Assange has refused to leave Ecuador's London embassy out of concern that the United States would seek his extradition for leaking classified government documents in 2010.

BUSINESS NEWS

Fiat Chrysler to Move Truck Production to U.S. From Mexico

Fiat Chrysler on Thursday said it will invest $1 billion in its Warren Truck Assembly plant in Michigan in order to move production of the Ram Heavy Duty truck to the United States from Mexico, The Detroit News reported. The move will bring 2,500 new jobs to the Detroit area by 2020, when the upgrades to the plant are completed, the company said. The decision may also lower risks for the company ahead of any potential changes to the North American Free Trade Agreement, Dow Jones reported. Fiat Chrysler also said it plans to give its 60,000 hourly and salaried U.S. employees $2,000 bonuses. "These announcements reflect our ongoing commitment to our U.S. manufacturing footprint and the dedicated employees who have contributed to [Fiat Chrysler's] success," CEO Sergio Marchionne said in a statement, The Detroit News reported. He added, "It is only proper that our employees share in the savings generated by tax reform and that we openly acknowledge the resulting improvement in the U.S. business environment by investing in our industrial footprint accordingly." U.S. President Donald Trump praised the move on Twitter Thursday, saying it was "more great news as a result of historical Tax Cuts and Reform."

THE DIALOGUE CONTINUES

Why Is Maduro Freeing Opponents?

Q Venezuelan President Nicolás Maduro on Christmas Eve freed dozens of government opponents who had been imprisoned on charges ranging from inciting violence to subversion, and instead gave them lighter sentences, such as community service. The country's best-known political prisoner, Leopoldo López, remains under house arrest, however. The prisoners were freed just days after Maduro and the country's pro-government Constituent Assembly moved to bar opposition parties from participating in this year's presidential election, saying they had lost legitimacy by not participating in the December local elections. What is behind the government's decision to free the prisoners? Does the opposition have any chance or will to compete in elections later this year? Under increasingly desperate economic circumstances, what are the chances that Maduro will be forced from power?

A Jason Marczak, director of the Atlantic Council's Adrienne Arsht Latin America Center: "The December release of 80 government opponents—although hundreds remain imprisoned— could be perceived as a gesture of goodwill from the Venezuelan government following the opening of negotiations with the opposition coalition, Democratic Unity Roundtable (MUD). But this government has no goodwill. Instead, it was more likely an attempt to distract from the latest wave of anti-democratic decisions coming out of the illegal Constituent Assembly, including barring parties from competing in this year's elections. What is certain is that U.S. sanctions are having a profound effect on the government. One of the chief reasons that Maduro's government is interested in pursuing dialogue with the opposition is that it hopes to find compromises that will result in the United States forgoing additional sanctions or relaxing existing ones. That will not happen without basic guarantees of democratic freedom in Venezuela, among other conditions. At the same time, as we look to this year's presidential contest, the opposition is focused on using the dialogue to press for the reforms and guarantees that could result in freer and fairer elections. Still, with the current electoral conditions, and the systematic tactics used by the government to manipulate, confuse and intimidate voters, the opposition has very slim chances of winning any elections. The deck is stacked against it. That is why electoral conditions must be changed and international observation must be guaranteed if the MUD is to have a shot at winning the vote. But this government is anything but democratic. It will bring out all tools in its arsenal to ensure that dissent is squashed and its cronies remain in power."

EDITOR'S NOTE: The comment above is a continuation of the Q&A published in Wednesday's issue of the Advisor.

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economy and to Mexico-based companies would be significant, making the possibility of increased M&A activity in Mexico unlikely in 2018. Even the threat of a U.S. withdrawal from NAFTA has been enough to cast a pall over the Mexican economy and business environment and to increase political pressures, particularly in an election year."

A **Tapen Sinha, professor of risk management at the Instituto Tecnológico Autónomo de México and professor at the University of Nottingham Business School:** "In Mexico, all mergers and acquisitions are subject to Article 28 of the Mexican Constitution, which prohibits any monopoly, unless the industry is run by the government. Thus, post, telegraph, oil and their derivatives are traditionally not considered monopolies. However, from 2015, oil and its derivatives are no longer government monopolies—at least in theory. Many experts expected a stronger wave of mergers in the energy sector that would take advantage of deregulation taking place by reducing the monopoly power of state oil company Pemex. It did happen in 2016. However, the reality turned out to be much more complicated. As a result, many potential buyers in the sector were strongly discouraged. In manufacturing, 2016 saw the election of Donald Trump as the president in the United States. He ran on the platform of the promise of killing NAFTA. South of the border, presidential frontrunner Andrés Manuel López Obrador is also promising to abandon NAFTA if he wins this year's election. Thus, cross-border mergers took a huge hit during 2017. It is also clear that until the uncertainty about the July election in Mexico is settled, and until the decisions about NAFTA are clear, cross-border mergers will be strongly discouraged in the near future. Similarly, uncertainty about the future of the Mexican economy also puts a damper on mergers between Mexican firms."

A **Richard Sinkin, founder and partner of InterAmerican Group in San Diego:** "M&A activity in Mexico has declined in the past year. There are three principal reasons. The first is great uncertainty about the future of NAFTA. The Trump administration has proposed new terms in the protracted negotiations that are clearly unacceptable to both Mexico and Canada, not the least of which is a 'sunset' provision that would destroy the certainty of any agreement. Since many M&A projects involve manufacturing companies that will be involved in cross-border trade, the uncertainty has put these deals on hold. A second factor is the rising possibility that the populist candidate, Andrés Manuel López Obrador, will be the winning candidate in July's presidential election. Although trying to reposition himself as a moderate, there is deep concern about his negative impact on Mexico's relatively well-run financial markets. And, finally, many are deeply concerned about the huge amount of seemingly intractable corruption throughout the political and judicial systems. Investors want trade certainty, political stability and rule of law. At the moment, Mexico does not present an attractive picture."

> **"Investors want trade certainty, political stability and rule of law."**
> **— Richard Sinkin**

The Advisor welcomes comments on its Q&A section. Readers can write editor Gene Kuleta at **gkuleta@thedialogue.org**.

LATIN AMERICA ADVISOR
is published every business day by the Inter-American Dialogue, Copyright © 2018

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Latin America Advisor is published every business day, except for major U.S. holidays, by the Inter-American Dialogue at
1155 15th Street NW, Suite 800
Washington, DC 20005

www.thedialogue.org

ISSN 2163-7962

Subscription inquiries are welcomed at
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