

Latin America Comes of Age

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David Snow, Privcap: We are joined today by Ralph Keitel from the International Finance Corporation. Ralph, welcome to Privcap Today.

You have played a number of roles at the IFC, but right now you're in charge of investments in Latin America. So I'm very interested to hear your analysis of what's going on in those markets. Why don't we start with the fact that you have many meetings with GPs who are hoping to form a capital partnership with the IFC from Latin America. What is the flow of opportunities like from your perspective, and what does it say about the developments in the Latin American private equity market today?

Ralph Keitel, IFC: Well, I think, David, there are two things in particular that stand out in private equity in Latin America these days. One, is that the region as a whole is doing exceptionally well. Funds in Latin America raised over \$10 billion in 2011, which is a significant 25% uptick over the 2010 numbers, which in itself was 50% higher than 2009. So the region is enjoying very strong support from international investors.

And the second thing, I think, that stands out is obviously Brazil. Brazil is the second largest destination for private equity with \$8 billion dollars raised, which is second only to China. So Brazil is quite hot among investors these days.

Snow: I'd like to get to Brazil in a second because obviously that's the most developed, and in many ways, the most popular market. But are you seeing any recurring themes among the funds that come to you? For example, is there an uptick in certain region or is there a certain strategy that is trying to get off the ground?

Keitel: I would say besides Brazil, which is the 800 pound gorilla in the room, a lot of investors are our touring and Andean region right now. Colombia in particular, is quite fashionable these days. Peru. And Mexico is showing some strong fundraising this year.

Snow: And the interest from the international investors in some of these regions, Peru, Columbia, is that basically encouraging the formation of GP groups? They're coming forward and attempting to meet the demand from investors?

Keitel: Yes, it does very much. If you look at Colombia, in particular, take that country. Colombian funds raised \$100 million last year. Fundraising is always cyclic, but if you add up the five, eight, maybe 10, funds that are currently in the market actively raising funds for Colombia, you easily get to a billion dollars now. Not all of that will be successful, but the fact that money is available--

And one thing we should remember is that in Latin America in particular it's not just international institutional money that's available. But there's a lot of domestic capital available. Markets like Brazil, Mexico, Colombia Peru as well, have a lot of local money, domestic pension fund money, that is available. So that is actively encouraging the creation of new GPs, yes.

Snow: What should a GP, let's take Colombia for example, what should a GP from that region, who possibly has not previously raised capital from your organization, or institutional capital, what should that GP know about your process, and what you're looking for in a GP?

Ketiel: Well, IFC as a developmental financial institutions, we have a dual mandate in certain areas. So on one side, we are eager to generate returns on the funds that we support. But on the other side, it's also about the development impacts.

That is jobs being created. Governance is very important for us. That is female employment. We have a particular focus on climate change funds these days. So it's about avoiding greenhouse gases. So we look at both of these sides.

Beyond that, we have a mandate to support early managers, first time fund managers. Here we don't necessarily need to see an institutional joint track record, but we need to have individuals, that normally work together as a team, that bring individual track records then that complement each other well. So in a certain way, we are no other than the average limited partner. We look for teams that we believe in. And where the government is in place, where we feel we have the right terms, and that have a business model that really captures the opportunity in that given market.

Snow: You mentioned the 800 pound gorilla in the market, in the Latin American market, and that's Brazil. With the IFC's mandate to essentially help develop the ecosystem of these regions, has Brazil turned a corner? Is it almost at a point where the IFC's role is no longer as important?

Ketiel: I think you raise a very valid question. The question what is the role of an institution like IFC in a very rapidly developing market like Brazil. Again, I mentioned it earlier, eight of the \$10 billion for private equity that was raised in 2011, in Latin America, was for Brazilian funds.

But then if you dig a little bit deeper, actually, the picture starts to change a little bit. And the first thing you realize is that out of those \$8 billion raised, seven was in fact raised by just four GPs. So those are very large groups that are raising a billion and a half or more each. Now, if you take that away, you are left with \$1 billion for a market of almost 200 million people, which is with rapid growth.

The second thing is that those groups that I just mentioned, together with international investors, such as the Carlyle's, the Blackstone, the TBG's of the world, that are competing in the upper end of the market, but there are many markets, segments, as well as regions, that are not getting any private equity capital at all. So there is still opportunity in the mid-market, or in the lower mid-market.

And the third thing I'd point out to, in particular, is that Brazil, while it is what we at the World Bank term a middle income country, has more poor people than most of the remaining

Latin American countries together. So there is huge opportunity to target that segment of the market. It's called the bottom of the pyramid, or I've seen we call it the inclusive business models.

Snow: Well, your history, around the world, but also in Latin America, gives you an interesting ability to look at the average track record, or the average performance of that region, do you have enough data to date from the Latin America fund investments that you've made to get a sense of how performance has been in general?

Keitel: I think one very interesting thing is what we're seeing right now is a maturing of the Latin American private equity market. I'd call it a coming of age if you wish. Yes, \$10 billion was raised, but on the other side it's interesting to see that \$10 billion were achieved in exits and returned to investors. So--

Snow: Last year?

Keitel: In Latin America, in 2011, so that's a very positive development. And returns in Latin America are strong. If you look at the three, the five, or the 10 year benchmark returns they're in line with emerging market, in general, which are very good, which are very comparable to developed world. IFC's portfolio too, in Latin America, very strong. IFC's funds portfolio has returned over 20% over the last 10 years. And Latin America is very much aligned with that.

So it's a very broad opportunity, really a coming of age of the market, and again, it's not just Brazil. Yes, Brazil has raised 80% of the capital, but in terms of investment is only 66%, it's 2/3 of the money. And in terms of exits, it's half. So what we're seeing is that the opportunity is broad. It's not just Brazil.

I mean, our portfolio, for example, one of our funds had a very successful exit. There's a company called Arcos Dorados, which is a local McDonald's franchise, which went public, and NASDAQ, in fact, and it generated a 10x, return for our fund. So it's a very broad opportunity. And really money not just going in, but money being realized, which is, of course, what investors want.

Snow: Now Ralph, with the IFC you have been in other parts of the world. You were, for a while, in charge of Eastern Europe, Russia, then you spent some time in Johannesburg overseeing the African program. What did you learn in those two locations, by way of lessons or insights, that you've been able to bring to the Latin American geography?

Keitel: Well, Eastern Europe, and Russia in particular, is a fascinating private equity market as you know. And I almost tend to think that Russian private equity is rather unique and doesn't compare to anything, but one thing that has taught me, or taught us in the IFC, is the importance of governance. Investing in emerging market, investing in private equity, is all about implementing good governance at the manager level.

Africa was certainly very interesting in that we are active in a lot of frontier markets. Under my watch we've created funds in the DRC, and Sierra Leone, and Liberia, all of which is very unique. And all of which are lessons that you can apply very well if you go into markets like Central America. Or just this past month we were busy creating a fund, first institutional private equity fund, for Haiti. So lessons that you learned in markets like Sierra Leone, and Liberia, and DRC, where I've travelled to, are very much applicable to places like Haiti.

Other than that, let me just make one more point, and that is that one universal lesson that you draw when you're active in emerging market private equity is that it's all about growth essentially. Private equity in emerging market is growth capital. It is investing in companies that are rapidly growing. It's the rising the business class with disposable incomes, spending money, which drives not just GDP growth, but it also drives returns for private equity. And that's a common theme across the emerging market.

Snow: Ralph, you mentioned Haiti, it's probably safe to say that it's among the poorest regions in the world, but certainly in Latin America, or rather in the southern hemisphere, is the IFC active there? And can you talk about what you have done there, and what your objectives are?

Keitel: I think it's safe to say that Haiti is not only one of the poorest countries in the world, but is also significantly impacted by the earthquake that happened two years, of course. And even two years on you will see that there's still tremendous need for pretty much any good, any service, housing--

So this is some of the interesting part of the things that we do in IFC. And this is where you really see IFC in action, where we bring out the best in the organization. We were given the mandate to try and put together a private equity fund that invests in Haiti. We've provided an anchor commitment to that fund. We did a search for fund managers that bring experience. Unfortunately we didn't find one in Haiti, so we had to take one from another place and transplanted them. Make sure that they have local staff and local knowledge.

But yes, there's a lot of donor money available for Haiti as you know. The institutions, the international donor community, has provided a lot of money. But very little of it makes its way into the country, and very little is yet effectively being deployed because many of the infrastructure bottlenecks aren't yet addressed. There's a lack of housing. There's a lack of even hotel spaces for the international donors to stay in. So we're hoping that by creating an SME fund in Haiti we can address some of those bottlenecks.

Snow: So that's interesting, so as opposed to a fully formed GP group coming to you and saying, we will be investing in Haiti, you went out and proactively, essentially, created one. How often does the IFC do that?

Keitel: We do that once in awhile. I mean, obviously we wouldn't have a 20% return if that's the only thing we did. But we've come up with a program that address particular post conflict countries. This is where we put together about a half a dozen funds in places such as the DRC, or Sierra Leone, Liberia, in Yemen, and so this gave us the experience to essentially put together a GP on our own, putting out an anchor commitment, and working with a GP. We're providing them with technical assistance and training.

But the truth is that in a place like Haiti, you wouldn't have a commercial GP that comes to you and says, here's my fully cooked concept. Please invest, and I'll go find the rest of the investors. In places like Haiti we need to be proactive. We need to actively go out and actively start creating those managers on our own.

Snow: Are there any other countries in either Latin America, or in the world, where you are actively seeking a GP group to address a need?

Keitel: We do that in a lot of places. We do that in small countries where there's essentially a complete lack of private equity. In Asia, we do it in places like Bhutan and Nepal. Countries in Africa I mentioned.

And we're, given the events of the North African spring, we're putting together fund managers in North Africa. And the fund in Haiti. We're also very active in Central America right now. In fact, half of the funds that we're supporting this year in Latin America are in Central America, where we're creating one SME fund, and one renewable energy.

Snow: Well, Ralph Keitel, thank you so much for joining Privcap today.

Keitel: Thank you. It's been a pleasure being here. Thanks, David.