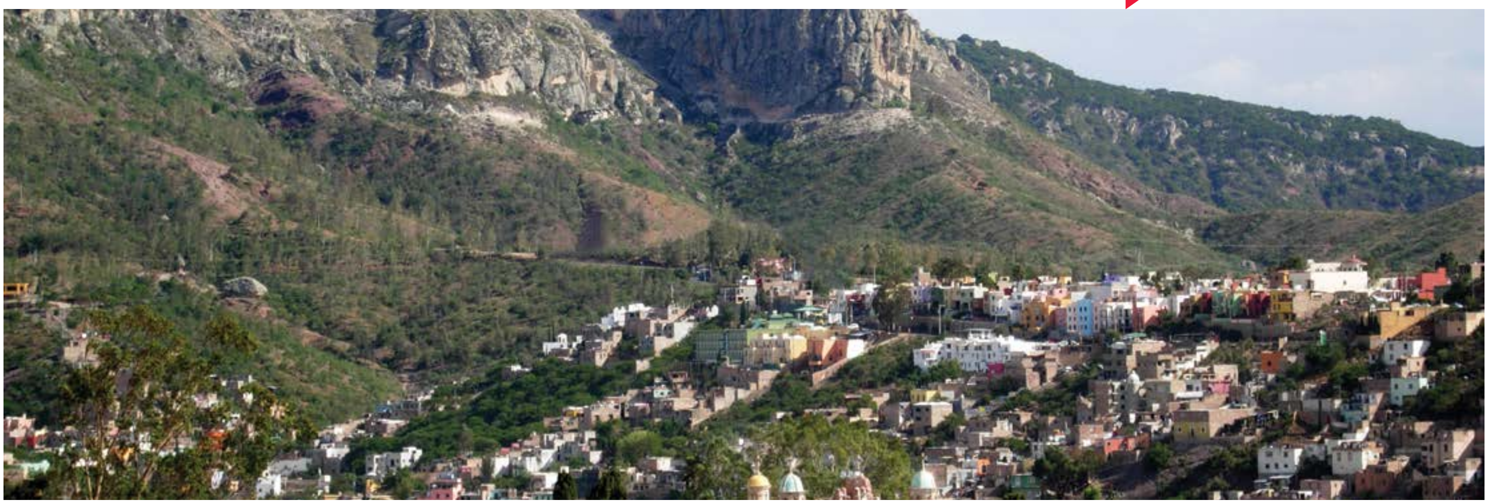
BDO KNOWS INTERNATIONAL PRIVATE EQUITY: SPOTLIGHT ON MEXICO



Fred Campos, Director of Transaction Advisory Services at BDO USA, sat down with **Bernardo Soto**, partner at BDO Mexico, to discuss the latest PE trends in the region. Here are some insights from their conversation.

Fred Campos

Bernardo Soto

According to BDO's sixth annual PErspective Private Equity Study, more than one in four private equity fund managers expect to pursue cross-border transactions during the next 12 months. When evaluating these international opportunities, Latin America was ranked the second most attractive target for new investment opportunities.

What investment trends are you seeing right now in Mexico, Bernardo?

Mexico has flown under the investment community's radar over the past few years, falling in the shadow of more popular targets like Brazil. However, we're slowly seeing that sentiment change. In a study conducted by LAVCA and Collar Capital last year, "Latin America Private Equity Study," respondents named Mexico as one of the most attractive markets in the region. The survey also indicated that investors are seeing a worsening risk/return ratio in Brazil.

We're seeing numerous Mexican legislative changes that are contributing to an environment friendlier to foreign direct investment, such as loosened monopolies in the telecom and energy industries. There is also greater collaboration to encourage regional economic and stock integration within Latin America; in 2013, Mexico became a part of the Pacific trade block, along with Chile, Colombia and Peru.

Which industries do you think will be most attractive to investors looking into Mexico?

The energy market in Mexico will be an extremely attractive market for investors looking for business opportunities in 2015 and beyond. Last year, the government ended a 70-year state monopoly on oil production, opening the industry to private investment, both local and foreign. With investment in the energy sector estimated to reach as much as $13 billion in 2015, the privatization of the oil industry is poised to grow Mexico's economy. In fact, a recent Bloomberg article, "KKR Looking at Mexico Opportunities, David Petraeus Says," noted that economists predict the Mexican economy will grow 3.5 percent in 2015 – a 1.2 percent increase from 2014. This

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expected growth can likely be attributed to the anticipated investment in energy.

To encourage investment in the energy industry, former Mexican President Vicente Fox (now a board member for Mexican private equity firm EIM) toured Texas this past October to encourage investors to look to Mexico—though many investors need no encouragement. Many firms, like KKR, have already begun capitalizing on opportunities.

Further, investors should keep their eyes on the telecom industry, with the government also acting to open the market. As competitive conditions continue to improve in 2015, we'll likely see an increase in foreign investment and acquisitions.

What type of capital flow are you seeing coming into Mexico right now?

We're seeing capital flowing in from different parts of the world with a great deal coming from North America. Mexican family-owned companies are seeking local investment and that is driving many larger U.S. private equity firms to carve out sub-segments of existing funds to dedicate solely to Mexico.

Many international companies are targeting small to mid-size Mexican companies, with revenues ranging from $25 to $50 million.

What is the untapped market in Mexico or the next hot opportunity for PE investment locally?

We're seeing a resurgence in manufacturing, specifically in the auto industry. This was a hot sector prior to the economic downturn in 2008, and it is slowly coming back. For many companies in this space, the end goal is to turn a profit by exporting goods to the United States.

The textile and mining industries may also be the next big opportunity for investment, especially small companies ripe to be acquired. However, these are heavily unionized industries, and investors must remain cognizant of labor laws and unions.

Anything else to note?

Taxes are always a challenge, especially among foreign investors unfamiliar with local laws. For the last six years, corporations have been subject to thorough reviews requiring stringent compliance, especially in regard to VAT and federal income tax.

Potential tax implications related to asset versus stock acquisitions should also be considered by investors. Unlike in other countries, such as Brazil, asset acquisitions can be particularly attractive in Mexico but tax diligence is crucial to determining whether the transaction will qualify as an asset acquisition and protect the buyer from successor liability.

For more information about private equity in Latin America please see the latest issue of our BDO PEerspective newsletter here: http://www.bdo.com/download/3464

CONTACT:

FRED CAMPOS
Miami
305-420-8044
fcampos@bdo.com

BERNARDO SOTO
México
+52 (55) 8503 4200
Bernardo.Soto@bdomexico.com

LEE DURAN
San Diego
858-431-3410
lduran@bdo.com