SPECIAL REPORT 2014 LATIN AMERICA: GAME CHANGER

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Investment is increasing in Latin America, particularly in the energy and infrastructure sectors – but this presents new challenges for law firms, which face increased competition, decreasing fees and an escalating war for the best legal talent

The FIFA World Cup 2014 in Brazil showcased the strength of Latin American football. Germany may have won the competition but Latin American teams put in impressive performances, with seven of the 16 teams making the knockout stages coming from the region, compared to six from Europe, two from Africa and, finally, the USA.

Latin American economies, like their football teams, are starting to challenge the dominance of the old-world order. Flourishing markets, an abundance of natural resources and a burgeoning middle class are keeping both businesses and their legal advisors busy.

However, despite promising economic opportunities, law firms also have to tackle a number of problems. Latin American firms are facing increasing competition from global players looking to expand their operations in the region – this increased competition means fees are decreasing. Meanwhile, the competition for the best talent is intensifying with some lawyers now finding the prospect of working in the public sector or for a company an attractive proposition. In addition, more organisations are looking to increase the amount of legal work they do in-house in order to reduce expenditure on external advisers.

Jaime Carey, managing partner of Carey y Cía in Chile, says that Latin America is experiencing a generalised growth in investment, especially in the energy, mining and infrastructure sectors: “This opens a wide range of opportunities for law firms, which can advise companies wanting to invest in the region.”

The World Cup and Rio de Janeiro’s Olympics in 2016 are headline examples of Brazil’s infrastructure programmes but there have been other significant initiatives. These include a natural gas agreement between Rosneft and Petroleo Brasileiro, a $2 billion credit agreement between Brazil and Angola for energy and infrastructure development and possible investment in airports by Chinese companies.

Celso Costa, managing partner at Brazilian leader Machado Meyer Sendacz e Opice Advogados, says that demand from the infrastructure and energy sectors is spurring on corporate work, including M&A. “The corporate governance practice is also active, responding to the steady increase of global conglomerates – finance, infrastructure, tax and labour are also highlighted by the urgency of investments and by government stimulus.”

Alexandre Bertoldi, from Pinheiro Neto Advogados in Brazil, highlights project finance as an area of interest because, although the Brazilian economy is not growing as fast as it was in the past few years, there is a considerable amount of money to be invested in improving the country’s infrastructure, including roads, ports, airports, power generation and distribution. “The government shows signs that they will slow down direct financing via the Brazilian Development Bank (BNDES) – therefore project finance might be the only alternative for these big projects on the pipeline,” he adds.

There is similar activity across the region. Other recent matters include Latin America’s largest solar photovoltaic power plan, developed by SunEdison, constructed in Chile and inaugurated this year, a $2bn oil pact between Venezuela’s PDVSA and Rosneft, the possible sale of Total´s holding in Argentine pipeline firm Transportadora del Gas del Norte, and Ecuador securing a $2bn financing for future oil production from Chinese outfit Sinopec. In Colombia, meanwhile, Gas Natural Fenosa, Duke Energy, GFD Suez and Huadian were linked to the planned sale of a 57.6 per cent holding in state-run electricity company Isagen.

Cultural changes

The uptake of international interest underscores the socio-economic changes in Latin America. Many jurisdictions have historically been socialist countries, with state funding and monopolies the preferred model. Unprecedented growth and governmental spending priorities have meant the role of private players has increased. As a result, many jurisdictions have needed to update legislation to encourage investment.

Costa stresses that Brazil has a modern legal framework with regard to the most strategic and regulated sectors of the economy during the past decade. “We have new legislation for ports, airports, electricity, sanitation, solid waste, oil and gas, railways and telecommunication, among other sectors,” he observes. “New legal regimes have been introduced as alternative means to attract more private investment, such as public private partnerships, public consortiums and special urban projects.” Leonardo Briganti, partner at Briganti Advogados, says changes to Brazil´s tax laws have triggered a flurry of M&A deals.

Costa outlines other legislative developments like the Fiscal Responsibility Law, the new Civil Code, the Brazilian Arbitration Act, the Reorganisation and Bankruptcy Law and, more recently, the adoption of the Vienna Convention on the International Sale of Goods, and the enactment of an anticorruption law in line with the US Foreign Corrupt Practice Act and the British Bribery Act.

“Nonetheless, there is still a lot to improve,” Costa summarises. “One highlight is the proposed reform of the Brazilian Bidding Law (Law 8,666/93). The Bill of law being discussed in Congress proposes a large reform with the aim of accomplishing a more modern and efficient legal framework for bidding procedures and contracts with the government."

Other Latin America countries are taking similar steps. Mexico has ongoing reforms, including ending the monopoly of state-owned energy firms PEMEX and CFE to open up the market to foreign firms, and new governments in Venezuela, Colombia and Chile have pledged reforms to bolster international interest.

Greenberg Traurig partner Emilio Alvarez-Farré says Mexico´s energy reforms offer enticing opportunities for investors. Meanwhile, Juan Pablo Cervantes, from Galicia Abogados in Mexico, explains that the country has, in the last six months, enacted comprehensive reforms in the labour, education, energy, tax, financial, antitrust, telecommunications and commercial law areas. "Some of these reforms, which have yet to be finalised, have brought much expectation to domestic and international companies desiring to do or expand business in Mexico," he adds. "We anticipate that in the coming years this will translate into investment, projects and opportunities in areas such as energy, oil and gas, and infrastructure. Other legal amendments – in tax, financial or antitrust – will obligate companies in multiple areas to review and adjust many of their internal structures or practices – they will have to rely on their legal advisors in order to do this. Accordingly, many of these amendments will translate into important work opportunities for firms with experience in these areas."

In the case of Chile, which in March elected Michelle Bachelet as the country's new president, plans are afoot to tender long-term electricity supply contracts and improve rules governing natural resources. However, Bachelet wants to increase corporation tax from 20 per cent to 25 per cent and do away with laws that protect international investors from tax reforms.

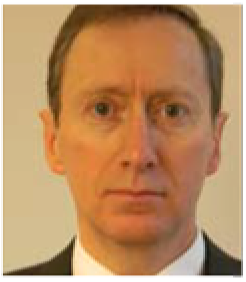
Roberto Guerrero, from Guerrero Olivos in Chile, anticipates the increasing state regulation will impact the operations of a large portion of his firm's clients. "[New regulations] made us create a practice area in administrative and public law way before our competitors, which prompted us to lead the market. Similarly, we strengthened our capabilities in antitrust regulation, tax laws and labour regulation and negotiation."

Lawyers point out that while improved regulations are welcomed, doing business in Latin American can require due diligence and planning. In Brazil, Bertoldi cites regulatory matters, such as environmental issues, red tape and the complex process for obtaining licenses and approvals, as possible bottlenecks for many projects.

Bureaucracy also remains an issue in Brazil, while Albert Castelló, who heads the Spanish and Latin American desk at Felsberg Advogados, says that Brazil has done almost nothing to give more legal certainty, not only to Brazilian companies but also to companies owned by foreign investors.

A lack of a legal framework, coupled with political risk, can dissuade investors. Argentina and Bolivia, for instance, renationalised the local energy assets of international companies, sparking anger and court action.

Guerrero says clients should take into account the possibility of increased regulation and changes to certain rules that may impact on the decision-making process. "This includes cases of nationalisation, tax reforms and other structural changes that must be followed closely."



"The ability to adapt quickly to remain competitive represents a huge challenge in this ´new´ market."
Juan Pablo Cervantes
Galicia Abogados

Regional outlook

Latin America is a disparate collection of countries and investors have to balance a country-specific strategy with the growing interconnection of a pan-regional hub. Martín Carrizosa of Prietocarrizosa in Colombia, says one of the biggest challenges that clients face is understanding the region. "Many of our clients are starting to have a regional approach to Latin America as opposed to a country-by-country perspective. They are beginning to see the region as an integrated economy. Their biggest challenges are related to defining their landing strategy. Joining our economies is more challenging now as, on the one hand, it requires regional deep knowledge and, on the other, ´on sale assets´ are now scarce."

Carrizosa highlights the surge of multilatinas, Latin American companies starting to behave as true multinationals, with appetite throughout the region and beyond. There is also the Latin American Integrated Market (MILA), an integrated stock exchange market for Chile, Colombia, Peru and Mexico. MILA was established by the Inter-American Development Bank as part of the integration efforts in the region and boasts the largest number of listings by volume in the region, with 544 companies on the exchange.

Carrizosa observes that some of the multilatinas have already accessed the international capital markets, including successful IPOs on the New York Stock Exchange, and that international dynamics, including the worldwide regionalisation trend, is impacting Latin America."By way of example, we have the Pacific Alliance – Alianza del Pacífico – which is a joint effort by Colombia, Peru, Chile and Mexico – all of them with a Pacific coast – to work together towards achieving more integration, trade and investment," he says. "By being a market of more than 215 million consumers and a combined GDP that represents 34 per cent of the total GDP of Latin America plus the Caribbean, no wonder many consider this alliance to be the most promising in Latin America. The Pacific Alliance will instantly create the eighth-largest economy in the world." Guerrero adds that law firms must pay attention to several factors that may become real opportunities, such as the sustained growth of the countries that are partners in the Pacific Alliance and the benefits of such a partnership.

It is inevitable that with new legislation, regionalisation and more complicated legal matters, law firm dynamics are changing. Bertoldi says his firm is now relying on more senior people in order to benefit from their experience in more complex deals. International firms have been ploughing into Latin America, especially Brazil, but other countries are on the radar – Hogan Lovells' launch in Mexico being the most recent example – and local practices are wary of the pressures this brings on them in terms of clients and business development. Carey claims that law firms are facing a reduction of fees demanded by the clients, and as a consequence, less loyalty from them. "Also, international firms have started to compete, setting up offices in larger countries such as Brazil, Mexico and Colombia. That's why we are seeking to create more specialised areas and provide more efficient legal work."

Carrizosa cites global law firms in the region as a challenge. "Even when the number of foreign firms that have opened offices in Bogota, Lima and Santiago is lower than the number that joined the Brazilian market some years ago, we are facing a growing trend in terms of US and English law firms that are coming to stay."

As such, his firm is committed to enhancing and promoting its alliances with top law firms in other countries in the region, as well as Spain, to indirectly increase its presence throughout Latin America. He feels that Colombian and other regional firms have a clear path to expanding their presence in the region and becoming truly cross-border players. "We see opportunities in advising our Colombian clients in their regional expansion, not only in terms of joining new markets by starting their businesses abroad but also by accessing the international and regional capital markets and financing sources," he suggests. "Moreover, we foresee new opportunities in advising non-Latin American companies and investors on their process to enter our region."

Carrizosa gives the example of Chinese and Indian companies investing in Colombia and México to produce goods and services for markets in North America as a "brilliant opportunity", particularly tapping into possible links between the Pacific Alliance and the Asian-Pacific region.

Cervantes says Mexican firms too are facing an industry changing at a very high speed, bringing new foreign participants. "While Mexican firms are still going through an institutionalisation process, they are facing new players with well-established business systems and previous relationships with international clients," he says. "The ability to adapt quickly to remain competitive represents a huge challenge in this ´new´ market."

Lawyers agree that a major element of the new market dynamics is the competition for talent. Indeed, Latin American firms are not just vying with international entrants for the best lawyers but also with the public sector and corporations. Carey says that clients are demanding more specialisation and at the same time, companies are doing more work in-house, although he adds that major and complex issues are still being outsourced.

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> Santiago Carregal
> Marval O'Farrell & Mairal

This increased internal focus means more lawyers are needed in-house. In Argentina, the government is a major hirer of lawyers (see box) while Cervantes says that the economic slowdown has seen companies reassess the roles of their advisors, including legal firms. As a result, Cervantes adds companies have strengthened their legal departments in order to depend less on their external advisers.

"They are likewise demanding more efficient, cost sensitive services, shorter response rates, and hourly fees are morphing into other billing arrangements," he continues. "Clients expect firms to do more with less. Additionally, multinational companies need their firms to accompany them to jurisdictions into which they are entering or regions or areas in which they may plan to invest. IT and infrastructure needs to be able to keep up with the demand of clients."

Bertoldi says that firms need to adapt to a more competitive environment where clients demand more for less. "We are investing heavily in training in order to improve our efficiency and remain competitive," he remarks. "Our objective is to be a reference in the market, and only by devoting a large amount of time and money in training and developing our associates can we achieve our goal and maintain ourselves as one of the leaders in the whole Latin American market."

Costa believes that with a more competitive business market, locally and internationally, clients have become much more demanding in hiring professional assistance with a view to receiving better and more cost-efficient services. The result has been a much more competitive environment for law firms which have been forced to substantially invest in a better and more efficient organisation, to train, retain and hire more talented professionals, to develop an efficient marketing and communications structure and also to enlarge the scope of the professional assistance offered by the firm given the complexities of the legal and regulatory environment through which clients navigate. "In other words, the realities concerning the clients' demands requires from us competitive costs, technical expertise, legal business vision and agility," Costa says.

Castelló is concerned about how the market could look in future. "I think the biggest challenge all law firms are experiencing is uncertainty – the economy is cyclical so we are getting prepared for a likely period of low economic growth. We are reducing our expenses, improving our legal services in order to enhance customer loyalty, and investing in our corporate image, adapting it to the new days."

As with the World Cup, the business of law is a global competition. Latin American law firms are aware that evolving to withstand the challenge of regional and international rivals is the best tactic in a tough game.

Argentina: Moving the goalposts

Despite narrowly losing to Germany in the World Cup Final, Argentina's football team remains part of the global elite. The country's political and economic performance, however, is far from top-tier.

"In Argentina, [the biggest challenge is] the State interference in private business, be it in areas of foreign exchange, international commerce, or market manipulation," says Máximo Luis Bomchil, managing partner of M&M Bomchil Abogados in Buenos Aires.

The most high-profile example of this came in 2012 when the government nationalised the holding in the local operations of Spanish oil giant Repsol, which earlier this year resulted in a $5bn settlement at arbitration. Santiago Carregal, from Marval O'Farrell & Mairal, says there are problems with political uncertainties, the rule of law and the independence of the judicial system in Argentina.

To take the example of mining, one of the historic backbones of the economy, investors have been pulling back – exploration is said to have fallen by 70 per cent between 2011 and 2013 as a result of regulations and rising inflation that have pushed up costs considerably. A better legal framework would rekindle confidence.

Even so, the country offers plenty of potential. "The biggest opportunities for law firms in Argentina are in the energy, mining and infrastructure areas," Carregal comments. "It is expected that the Argentine economy will recover in late 2014 and early 2015, and Argentina badly needs substantial investments in energy and infrastructure. Most of the investments are expected in these areas."

As an example, in July, Russia offered to bid for the contract for two new nuclear power plants while the country's shale reserves are said to be among the largest in the world. There is wider hope that next year's general election will bring in a new administration to help reduce inflation, stabilise the economy and begin new reforms to push the country forward.

Despite the wider economic concerns, Argentine law firms are facing the same issues as most counterparts across Latin America.

"The biggest challenge for the major firms in Argentina is to retain talent and manage an organic growth while maintaining an acceptable profitability in the current hostile environment for foreign investment," Carregal summarises. "The biggest competitor for talent is actually the Federal State. The government is paying good salaries and demanding much less than law firms in terms of hard work, which is unlikely to change until at least after the election in 2016."

Mexico: Client demands increase as trade bloc opens new frontiers

Clients in Mexico are demanding quicker analysis and more immediate answers to their concerns, according to Juan Francisco Torres Landa, partner at Hogan Lovells BSTL. He adds: "As a result, lawyers have a smaller amount of time to research matters – clients expect their legal team to have the knowledge required to provide answers instantaneously."

Despite the fact some reforms have been introduced to liberalise the Mexican economy, clients still face heavy regulation in some sectors. Torres Landa says: "Some activities, such as oil and gas extraction, electricity generation, and airports and water ports control, are still reserved exclusively to the state, with some of those activities allowing participation of private parties through contractual arrangements – however, other activities, such as land transportation, are reserved to domestic companies. Additionally, clients may also be limited in their participation in certain activities, such as air transportation and insurance companies, as well."

The fact that Mexico has formed a trade bloc with Chile, Colombia and Peru – called the Pacific Alliance – means that the opportunities available to investors in each country and around the region as a whole will "continue to grow exponentially", according to Jaime Trujillo, partner in Baker & Mckenzie´s Colombia office. He adds: "Considering that 35 per cent of Latin America's economic production is concentrated among the [alliance´s] member countries, with the bloc's removal of more than 90 per cent of the customs tariffs between the member countries, a long line of industries are due to be impacted with growth opportunities across borders, as well as growing competition."