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As Latin America Enters Crisis Mode, Ritch Mueller Expects More Market Stratification, Refinancing Opportunities

While crises tend to create new opportunities for the legal community, the current pandemic-induced downturn is creating unique challenges – economic, professional and logistical – for companies and law firms alike. But when the dust settles, some restructurings and M&A deals are likely to come through, and law firms will need to stay alert to their clients' needs to make the most of it, says Luis Nicolau, Partner at Ritch Mueller.

Bonds & Loans: It's been an incredibly tough start to the year for most segments – corporates, banks, governments. But has the turbulence opened up certain opportunities for law firms? Are you seeing any activity in the markets that you cover?

Luis Nicolau: Yes and no. Firstly, financially law firms are typically not very well capitalized, and this lull could take a big toll on them, with personnel cuts and other cost-saving measures likely to begin soon. Secondly, in a situation like this, legal services are no longer a priority, with transactions being pushed back for various reasons. These two factors will weigh on the well-being of a lot of law firms.

At the same time, we will continue to see a weak but steady flow of transactions, in areas like restructuring or refinancing, with companies needing to reorganize investments as a means to sourcing additional capital in exchange for minority rights, for example. For those well-positioned in the financial sector that will remain the case, but for those law firms dealing in bread-and-butter type services, things will get tougher as it won't be a priority.

We have seen many crises before, from H1N1 to the 1985 earthquake and the 2008 financial crisis, but even during those periods there were geographies and economies that were far less impacted; this pandemic has engulfed much of the world. That said, the pandemic itself and its economic impact will vary from country to country, so we are likely to see some decoupling in the markets and economies. It is important to watch the direct hit on respective GDPs and the actions of respective governments in response – these two factors will dictate investor decisions and the volume of deals in those markets.

In the corporate space, those firms with stronger credit fundamentals are likely to survive; others will struggle for some time and require legal services, so in this environment it is critical for us to stay close to clients and be alert to their needs. But there is no magic formula, and things will get harder before they get better.

Bonds & Loans: As equity markets are tanking, there are a lot of discounted assets on the market. Are you expecting an increase in M&A transactions?

Luis Nicolau: At this stage we are not seeing the M&A market being very active. Well-capitalized companies can come to market and purchase assets; but their counterparties will be reluctant to sell because of the declining multiples. Eventually, as the crisis subsides, we will see activity pick up, and M&A transactions will rise, creating opportunities for us - but the market needs to bottom-out first. Over the next couple of months, we will see more distressed assets and restructurings.

Bonds & Loans: Which Latam markets will be primed for restructurings once the pandemic subsides? What are you doing to position yourselves at the forefront of this wave?

Luis Nicolau: In a sense, we don't need to position ourselves in any special way because we have a historically strong restructuring and insolvency team, which for a long time has been at the core of our business. What is likely to happen next is that there will be new market entrants trying to make inroads in this environment, so we need to stay close to our clients and offer them alternative solutions to ensure that they will turn to us in any scenario.

Bonds & Loans: Governments – both in emerging and developed markets – have been stepping up their measures to support the economy and businesses. Do you think this will lead to additional volatility in the restructuring space, as some get rescued while others are allowed to fall?

Luis Nicolau: There will definitely be a decoupling – in the likes of the US and China the government is already heavily involved, while others – such as Mexico, Spain, and Italy, have been far more passive. In some countries, the aid will lead to an immediate rebound, while others will take far longer to recover. In Latin America, I don't think any country has made any significant commitments that substantially affected market sentiment. My guess is that Southern Cone countries and Mexico will face huge competition for funding, and may not have access to those much sought-after pools of capital. Sadly, they don't have the resources of US, China, or Germany to stimulate the economy back into growth.

What would also help is a clear and consistent set of policies to fight the spread of the pandemic and soften the blow on the economy, providing the right signals to investors with regards to infrastructure and other investments. Unfortunately,

that response hasn't been uniformly resolute across the continent. In Mexico, the cancellations of construction plans in the North, for example, was not helpful. So a more proactive role in attracting new rounds of investments, namely in oil & gas, and the electricity sector, would be positive.

Bonds & Loans: You've recently participated in a USD470mn loan for Rassini. Can you share a little bit about that deal? What other transactions have you participated with recently?

Luis Nicolau: It was essentially to refinance existing debt and in that was quite successfully.

We also completed a very important USD250mn syndicated loan to MexOil, which is a Pemex supplier. And we worked on a couple of infrastructure loans too.

In the capital markets, Fibra E is looking to close a financing of toll roads projects, and the government is trying to refinance existing debt, so there is some activity, mostly in terms of refinancing.

But while it is important that these channels of financing remain open, regrettably we are seeing a liquidity crunch at the moment, and banks are basically just helping companies maintain short-term liquidity in the current volatile environment.

Bonds & Loans: More broadly, are you expecting a shift to the loan markets as EM bond yields spike? How are the corporates you work with looking to secure funding in these challenging conditions?

Luis Nicolau: It depends. Banks are relatively well capitalized, but the devaluation of MXN will have an impact on their capital positions. The capital markets are more challenging for Mexico at the moment due to the recent sovereign downgrade, which will be a drag on broad corporate credit quality in the country. The bank market will indeed be a little more active, though it is contingent on banks being able to maintain debt capital as SMEs begin defaulting, leading to an increase of NPLs and restricting the banks' capacity to lend to those companies.

In other jurisdictions, where banks are better capitalized, access to funding will be more open, but certain sectors will feel the bite of this downturn more than others regardless.

Bonds & Loans: What are the two or three areas to watch as the pandemic subsides in coming months, where do you expect to see stronger deal flows and greater opportunities?

Luis Nicolau: First of all, refinancings of all types and flavours; liability management transactions, some resulting in debt purchases; and perhaps some opportunistic M&A transactions as certain companies embark on fire sales of assets. My guess is that the government, in an effort to reactivate the economy, may provide additional support to oil & gas, infrastructure and electricity projects in Mexico.

In terms of other markets, we will see more stratification. Brazil is likely to remain attractive; so will Mexico - if the government takes the right steps; Peru and Colombia will be hit hard, and will require government interventions in the form of tax relief and subsidies. But it is hard to assess more concrete prospects at the moment - no one has a crystal ball.

LATIN AMERICA MEXICO POLICY & GOVERNMENT

Companies mentioned in this article

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