

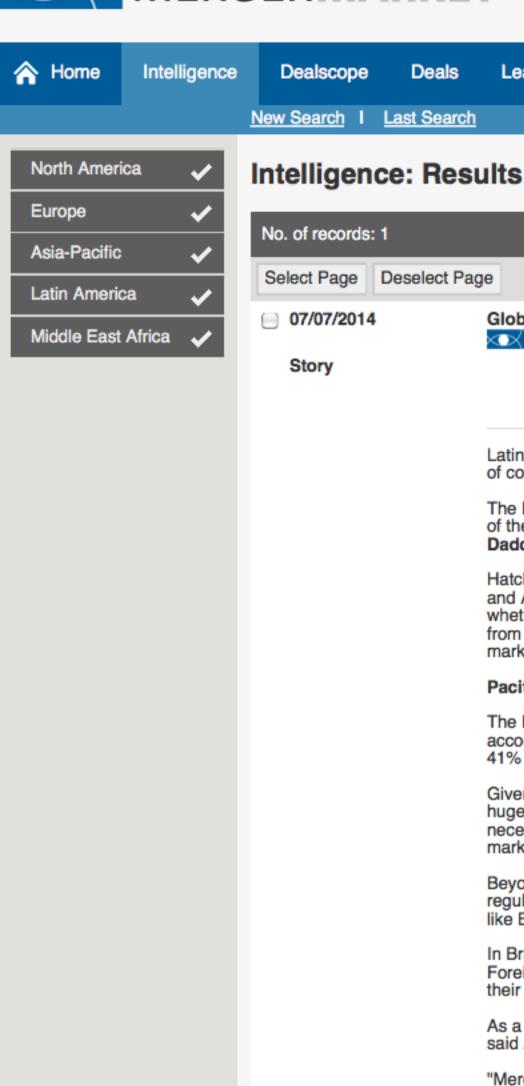
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High cost, complexity favor referral networks as alternative to acquisitions

Medium-size firms most likely buyout targets

Latin America is considered a key growth market by global law firms competing to offer services to a growing cadre of companies outgrowing their domestic markets, several attorneys at international firms told Mergermarket.

The Pacific Alliance between Mexico, Colombia, Peru and Chile, a trading bloc formed in 2011, increases the allure of the region for international legal networks, noted Michael Hatchwell, a consulting attorney at UK-based Gordon Dadds and former president of the Globalaw affiliate network.

Hatchwell said firms like Gordan Dadds had a keen interest in advising clients on emerging markets in Latin America and Asia-Pacific, particularly, but noted the costs associated with establishing a presence in such far-flung regions, whether a new practice or an acquisition, made global law firms think long and hard about setting up a base so far from home. It rarely makes sense, he said, except when a firm wants to attend to existing clients directly in a new market where those clients have a growing presence.

Pacific Alliance

The Pacific Alliance represents the eighth largest economy and seventh largest exporting bloc globally. The alliance accounts for 36% of the GDP of Latin America and the Caribbean, concentrates 50% of the total trade and attracts 41% of the direct foreign investment that flows to the region, according to the group's web site.

Given these statistics, there is tremendous interest from international law firms in Latin America, but there is also huge complexity, Hatchwell noted. Many international law firms enter Latin America, because they feel it is a necessity to be there to serve existing clients entering the region and new clients growing beyond their home markets, rather than because they want to, Hatchwell said.

Beyond the high costs associated with setting up a new practice in a foreign territory, international law firms face regulatory obstacles preventing them from practicing directly in some of the most attractive markets in the region, like Brazil.

In Brazil, foreign law firms can only have representational offices to work under the laws of their home jurisdictions. Foreign firms are not permitted to practice under Brazilian law and cannot offer the range of services they can in their home market or in more liberal international territories.

As a result, instead of M&A, alliances or associations between international and domestic peers are established, said Andre de Almeida, founding partner of Sao Paulo-based Almeida Advogados.

"Merging with an international firm can be a very successful story, but it can also be a nightmare. Costs can go up and your client base can leave you. Becoming part of a larger animal isn't necessarily good, he said. "Sometimes these international firms market that they can operate everywhere. That doesn't mean that they're good everywhere," he added, asking rhetorically, "How can you assure your clients that your UK attorneys can control and dominate the very strange tax system in Brazil?"

In the years ahead, commoditized legal work surrounding ethics, trademarks and copyrights, will be done by international firms that have offices everywhere, de Almeida predicted. Global firms can replicate that in all their offices around the world, he said. More sophisticated work, however, like M&A, project finance and strategic litigation, requires the best local knowledge, de Almeida said. Local firms will maintain an edge in performing this kind of work in partnership with international firms advising on cross-border transactions.

Almeida Advogados has been growing aggressively, organically and by acquisition, within Brazil, and the firm will continue to be on the lookout for buys to expand beyond its current footprint in Sao Paulo, Rio de Janeiro, Brasilia and Belo Horizonte, de Almeida said. Natural resources, agriculture and financial services are sectors where the firm is keen to grow its practice by absorbing other firms and attorneys. He noted he could look to acquire firms based in Mato Grosso, Mato Grosso do Sul and Rio de Janeiro. He said he'd never considered expanding beyond Brazil and even if the regulatory obstacles to cross-border M&A between international and Brazilian firms were eliminated, he'd not likely be compelled to engage in a sale or merger.

Jordi Dominguez, a partner at Latham & Watkins, noted that the top Latin American firms had little incentive to sell to international firms. They already have prestige in their local markets, and for any large M&A transaction they will be the go-to legal advisors to handle the work that falls under local jurisdiction. Many international firms, meanwhile, find they can handle the project finance and capital markets work with a strong Latin American practice in New York.

Tradition

Another deterrent to M&A between international firms and their local peers in more liberal markets of Latin America is tradition. Bufete Aguirre, a small firm with seven attorneys founded in 1940 by partner Fernando Aguirre's father in La Paz, Bolivia is one example.

Bufete Aguirre has been approached by international firms exploring the market, Aguirre said, whether for takeover or some other form of partnership. He emphasized, though, that a sale is "unlikely to happen given the characteristics of our firm." He said it was unusual to see local firms merge given their penchant for upholding their traditional, tight-knit family structure and independence.

A Globalaw affiliate, the firm relies on its long-standing reputation and deep-rooted contacts in the country to capture some of the most important clients from the local market and abroad. Aguirre said he sees no value to selling equity to an international firm and noted he prefers to work as a member of an affiliate network. The partner said his small firm had no aspirations to set up shop in other jurisdictions across the region and noted the Globalaw network obviated the need to have a proprietary presence internationally.

Hatchwell acknowledged it was tough to compel traditional family firms in attractive, stable and growing markets of Latin America. like Peru and Chile, to hand over the reigns and allow themselves to be beholden to masters in London or New York firms. There have been some serious buyout attempts in Chile among family-owned practices that were thwarted by this aversion to foreign oversight, he said, noting the same applied to Peru.

"I'm sure there are some firms looking at [acquisitions in] larger jurisdictions like Mexico and Brazil, but it's quite a high risk strategy," said Hatchwell. "Most of the large firms that have transactions in these countries will use a good local law firm," he said. "The large global firms tend to be American and English. The way they like to run their firms doesn't necessarily appeal to the local management style," Hatchwell said.

Sweet Spot

Mid-tier firms are more likely to sell or merge their practices with new entrants from the US and the EU, according to Latham & Watkins partner Jordi Dominguez. Firms across Latin America that might not have the same name recognition as the leading firms, but still have an attractive client roster, might be more compelled to sell to an international firm for the prestige and access to international clients, Dominguez noted.

Ferran Escayola, managing partner of Garrigues' New York office, said the Spanish firm has been aggressive in entering Latin America. Garrigues has its own offices in Bogota, Lima, Mexico City, Santiago, Chile and Buenos Aires. It has opted to grow mostly by attracting talent to its own offices rather than by acquiring local firms. It did acquire a small tax firm in Colombia, but for the most part it has taken advantage of Garrigues alums and the experience it had with local firms to retain talent.

The firm has followed Spanish multinational clients in their growth throughout the region and has channeled Asian investment into Latin America through Spain. Escayola said he expected to see more rivals from the US and EU entering Latin America, by acquiring local firms or attracting talent to their own offices.

In the end it boils down to clients, Hatchwell said. Major clients want to have one accountant, one auditor. The same applies from a legal perspective. This will be one driver for M&A among firms, he said. Another advantage to acquisitions in the field is the ability to gain an instant practice and enter a market with an existing local client base, he said.

Europe recovers

Meanwhile, with a recovery in the EU economy, there has been a shift in focus back to the old world, said Hatchwell. During the latest recession many firms sent lawyers to other markets where there was more work, said Hatchwell. "That has been one of the ways the very large firms have been able to survive the last recession – by growing into places like Singapore and China," Hatchwell noted.

With growth in the EU, however, many European countries have the economic growth potential of emerging markets, but with a more stable regulatory framework and less political risk, he said. Gordan Dadds acquired UK-based peer Davenport Lyons this year in an opportunistic deal that illustrates the opportunities many EU firms see in their own back yard, Hatchwell noted.

With more mature markets recovering from recession and the logistic and bureaucratic hurdles to expanding through M&A, global law firms may find alternative ways to grow their presence in the region. Many firms may find it easier to work in remote regions via a referral or affiliate networks.

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