

**BRAZIL**

# mineral

MINING - METALLURGY - OIL

Special Issue - 2012 - ISSN 0102-4728

**MINING IN BRAZIL**

**BREAKING  
RECORDS**



# The Bovespa road to growth: recent developments

Eduardo Vale \*

The purpose of this article is to provide readers of Brasil Mineral's special issue with selected remarks and insights about the evolving progress of Bovespa and its potential role as an important source of risk venture capital for the Brazilian mining industry. It should be borne in mind that the target sector for accessing this funding includes foreign exploration and mining companies operating in Brazil or elsewhere in Latin America, since they have the option to be listed on Bovespa in the future.

At the beginning of December 2010, when I was finishing my contribution to the 2011 special issue of Brasil Mineral, there was a noticeable trend among many companies to seek listings on more than one exchange. Although dual or triple listing strategies have been adopted by several companies, the relative preference for regional stock exchanges in emerging countries was new and remarkable. It certainly makes sense, since the root of global economic growth is moving to the South. Depending on the location of its core assets, the affluence of some regional risk venture capital hubs seems to be increasingly perceived as strategic by several companies. In addition to facilitating access to regionally generated

risk venture capital, this move reinforces the political side of the equation. As always, this dimension is a real concern, especially nowadays, in the case of a number of mining jurisdictions.

The arrival of the emerging economies as global players reinforces the importance of regional stock exchanges. They act as poles of attraction for risk capital to be invested in the region or to be generated in the form of savings from regional growth. These hubs are located on the frontier of expansion of the global economy. In their areas of influence there is an ever-increasing stock of risk capital. Part of this capital is locked and blocked within national boundaries under different constraints: regulatory, the availability of technology, transaction costs, and others.

Among these regional centers, the steady and relatively rapid rise of the Hong Kong Stock Exchange (HKEx) as a new global hub for accessing mining funding seems inexorable. The magnitude of the stock of economic wealth concentrated in Asia – natural resources, capital, human resources, technology, biodiversity and intangible resources – in addition to its higher rates of economic growth (the flow dimension), combine to cause a dramatic increase in the regional availability of risk venture capital. There is, in fact, a huge market there, in the form of very high growth rates and numerous outstanding global economic opportunities. From the perspective of Chinese investors, the HKEx seems to offer a unique platform to access international companies operating under codes, rules and practices similar to those adopted in the main financial centers. In this context, the HKEx is attracting not only Asian companies but also some global players such as Vale, Glencore, Resourcehouse and Kazakhmys.

Latin America is another region where a process of integration and consolidation is under way, triggering the rise of regional hubs. The most important event in 2011 was the creation of the Latin American Integrated Market (MILA).



# Investment

The basis of MILA is the integration of operations of three stock exchanges, those of Chile (BCS), Colombia (BVC) and Peru (BVL). It is expected to rank second in regional market capitalization. According to BVL, the first trade carried out under the newly-introduced MILA was an order from Colombia for the purchase of shares in a Peruvian zinc producer. Importantly, the Mexico City Stock Exchange (BMV) has expressed an interest in joining MILA. This would immediately put MILA in second place with a market capitalization of close to 70% percent of Bovespa's. This subject will probably be discussed during the second presidential meeting of the Pacific Alliance (Alianza del Pacifico) scheduled for the beginning of December. Finally, in a parallel and independent move from MILA, BVL and BVC announced their intention to merge. This transaction will reinforce synergies and leverage MILA as the fourth largest stock exchange in the region.

As far as the mining industry is concerned, BVL has the leadership in attracting foreign (mostly Canadian) mining companies looking for a second or third listing. Taking into consideration the recent additions of Luna Gold and Sulliden Gold, there is now a group of at least 17 foreign mining companies listed on the Lima exchange. In Colombia, the advancement of political stabilization has enhanced the huge potential of the Colombian mining industry. Clear signs of this trend are the success achieved in recent subscription calls by both Ecopetrol, the government-owned oil corporation, and Empresa de Energía de Bogotá (EEB), as well as EBX's announcement of its plan to list its coal and gold mining subsidiaries on both Bovespa and BVC.

According to the World Federation of Exchanges (WFE), at the end of 2010 Bovespa ranked tenth in worldwide market capitalization with around US\$ 1.5 billion. In comparison, HKEx had a figure of US\$ 2.7 billion. In terms of investment flows (capital raised by shares), Bovespa ranked third with US\$ 100.5 billion, behind HKEx with US\$ 109.5 billion. However, 2010 was an anomaly. The Bovespa figure reflects the massive impact of the mega capitalization of the national oil corporation, Petrobras. In 2009, for example, Bovespa ranked only seventh with an investment flow of around US\$ 41.7 billion. In Latin American terms, Bovespa's share of the regional market amounts to over 60 percent. Adding together Bovespa, Mexico's BMV, and the three exchanges that are members of MILA, their aggregate market capitalization at year-end 2011 amounted to 93 percent of the HKEx figure.

South American integration is on course. Apart from the massive investments that are being made at the national level, there are a number of multina-

tional projects on the geopolitical agenda. Regional integration will be leveraged by the inescapable implementation of a multi-billion dormant portfolio of the most important regional infrastructure projects. On the other hand, over the years Latin America has been the most popular exploration destination. Since 1994, it has received around a quarter of the aggregate global exploration investments. The combination of these two kinds of investment — exploration and infrastructure — will bring enormous mineral wealth. These aspects illustrate some of the principal components of the economic reasoning behind the integration of Latin American capital market hubs. Viewed from a medium- to long-term perspective, the present size of the market and its anticipated rates of economic growth suggest that an ever-increasing volume of risk venture capital will be forthcoming from regional investors. Certainly, part of this growing flow of risk venture capital will show an appetite for financing mineral exploration. In fact, this is already happening though only on a small scale so far. Finally, it should be borne in mind that these considerations are abstracting the migration of risk capital, including that associated with the decision of global players and financiers to set up shop in the region.

## Brazilian Bank Depositary Receipts - BDRs

The first time the Comissão de Valores Mobiliários (CVM), Brazil's securities commission, addressed the BDR question was in October 1996, under Instruction 255, which regulated the issuance and trading of Brazilian Bank Depositary Receipts (BDRs). At that time, following the first two years of stabilization under the Real Plan currency reform, BDRs seemed to have good growth potential. This mechanism enabled investors in Brazil to purchase — at their local market costs — shares in foreign companies listed abroad. At the same time, from the foreign investor's strategic viewpoint, BDRs offered a mechanism for funding their Brazilian and/or Latin American operations, for example, designing structured issues on Bovespa. The official debut of BDRs was analyzed in Brasil Mineral's special issue on Investing in the Americas 1997 (1). Then in December 1999, the CVM issued its Instruction No. 321, making several changes to the earlier one. In April 2000, Instruction No. 322 cancelled both the previous ones, replacing them with a new legal framework. Finally, in March 2011, Instruction No. 493 enacted the latest set of changes to the law.

Up until the third quarter of 2010, BDRs remained fairly dormant without any significant outstanding event. However, the pattern of BDR issues in the last twelve months suggests that, at



long last, BDRs are now being perceived as an interesting channel for accessing new funding. The level of activity displayed by several players — foreign companies, institutional and qualified investors and investment funds, for example — supports this assertion. At the beginning of December 2011, BM&F/Bovespa had 60 BDR programs (Level I without sponsor). Dozens of major foreign companies are already listed in these BDR programs, including Apple Inc., Arcelor Mittal, Avon Products, Bank of America, Exxon Mobil, Goldman Sachs, Google Inc., McDonald's, Pfizer Inc., WalMart Inc., Cisco, Alcoa, Citigroup, Wells Fargo, Freeport-McMoran Copper & Gold, Intel, Microsoft, Merck, and Procter & Gamble. The current portfolio is fundamentally North American oriented. BM&F/Bovespa is looking for a higher participation of European and Asian companies. At the end of November the BDR program with the highest liquidity was that of Freeport-McMoran Copper & Gold Inc.

At the moment, only the so-called super-qualified investors (a minimum investment of R\$ 1 million) are entitled to purchase BDRs. The CVM is considering lowering this minimum requirement to R\$ 300,000, opening the market to so-called qualified investors and making it possible to place BDRs through investment funds. This change is expected to leverage the attractiveness of BDRs.

BDRs can add strategic value as an economic and financial tool. A good example is the decision made by Pacific Rubiales Energy to seek a secondary listing on BM&F/Bovespa and trading BDRs representing the company's common stock (2). Pacific Rubiales Energy is already listed in Canada and Colombia. "This additional listing will enable the company to expand its qualified investor base in a country with tremendous potential for access to capital," in the words of a company statement.





In fact, foreign investors are increasing their demand for financial mechanisms and products in the Brazilian market. This is where BDRs may be expected to show steady growth, though it will take some time.

### Other Initiatives

- BM&F/Bovespa has announced an agreement with the stock exchanges of the other three BRIC countries, Russia, India, and China. The initiative will provide trading in the principal stock exchange indexes on each country's market and in its local currency. The mechanism is expected to be operational in the first half of 2012. A second stage is envisaged, focusing on the trading of an index of selected stocks in each country. According to WFE data, the combined market capitalization of the BRIC exchanges is above US\$ 9 trillion, representing more than 9,000 listed companies. Their aggregate daily trading volume is around US\$420 billion.

- Manabi Holding has now been registered at the CVM as a publicly quoted company. It incorporated its Brazilian subsidiaries, Morro Pilar Minerais and Morro Escuro Minerais, which hold exploration rights in the Iron Quadrangle region in Minas Gerais. According to press reports, after finalizing the business plan for its iron ore exploration assets, the company will apply for a listing. Among the main shareholders are Korean Investment Corp. (a South Korean sovereign fund) and Canada's Ontario Teachers' Pension Plan (3).

- The IPO of Vale Fertilizantes envisaged last year did not go ahead as planned. Instead, Vale concluded a public offer to acquire the whole outstanding share capital in Vale Fertilizantes and decided to delist the company and incorporate it as a wholly-owned unit.

- Press reports also indicate that two international players, Direct Edge and Bats Global Markets, are considering the possibility of setting up a new stock

exchange to compete with BM&F/Bovespa. The two proposals are being drawn up independently of one another, it seems.

- Lastly, a very important initiative has to be mentioned: BRAIN, whose backers include Anbima, the Brazilian Association of Financial and Capital Markets; BM&F/Bovespa S.A.; the Brazilian Federation of Banks (Febraban); Cetip; the São Paulo State Federation of Commerce (Fecomércio); and eight top banks. BRAIN's mandate is to transform Brazil into a hub for international investments. This goal is totally aligned with the consolidation of the MILA market as a regional hub in the area where Bovespa is active. It can be accessed at <http://www.brainbrasil.org.br>.

### Final Remarks

The emerging countries are increasing their geopolitical power and their share in the global stock of capital. From a flow dimension perspective, the regional financial hubs that are in a consolidation process in some of these countries are important sources of new risk venture capital. Their international role will increase and grow stronger reflecting the evolution of global aggregates, such as stock and flow of capital, toward a more balanced profile. At the end of the day, the lion's share in the huge anticipated needed investments in resources, energy, infrastructure, urban poles, etc., is reserved for Africa, Asia and Latin America.

When thinking about funding, it is important to bear in mind that everything begins with savings. Most of the new global opportunities are to be developed in these regions. The regional hubs concentrated the inflow and outflow of funds making the global connections. The growing demand for products and facilities pushes the legal framework and technological platform, not to mention advancement of geopolitical interests and initiatives such as the BRICs. This holistic strategic vision of funding is shared by many companies around the world.

In Brazil a Norwegian company, Seadrill, is planning to attract over US\$ 500 million to finance the expansion of its local subsidiary (4). Parallel to pre-salt development, other foreign companies providing oil exploration services are expected to list in Brazil, seeking to raise local funding to support their endeavors in the region. Another good example is Karoon Gas Australia, which in October 2010 was implementing an IPO for its Brazilian subsidiary. The goal was to access about US\$ 1 billion, making adjustments to the evaluation approach in order to leverage its market capitalization. Among these initiatives were the spinoff and separate listing

of its South American assets. "Karoon believed that companies with South American exploration assets, whose shares were listed on overseas exchanges, achieved far greater value for their assets than that achieved by Karoon in Australia. [...] The company further stated that the value discrepancy arose from the different emphasis on the values given to its Australian and South American assets in different markets." (5) The process was halted to take account of general changes in the business climate. Karoon's operational attractiveness sustained a huge impact from the Petrobras mega capitalization.

For the mining industry, it is just a question of time. Taking into account the size and diversity of market capitalization, flow of funds, partnerships and interfaces with the rest of the world, for some mining companies Bovespa may already represent an alternative for a primary or secondary listing. In this sense, Manabi Holding's announcement of its planned Bovespa listing is of vital importance. In the near future operations such as IFC's investment in MBAC Fertilizer or the financing of the Tucano gold project (Beadell Resources) can be formatted in a new financial dimension when conceived by companies already listed on Bovespa. □

### References

1. VALE E. *Funding Brazilian Mining Projects: A New Design in Foreign Investors' Perspective*. Brasil Mineral. March, 1997. Special edition for Investing in the Americas' 97. Miami. <http://www.bamburra.com/Funding.pdf>;
2. RAGAZZI, A. P. "Pacific Rubiales Energy pede registro para listar BDRs." *Valor Econômico*. 10/10/2011. <http://www.valor.com.br/impreso/eu-investimentos/pacific-rubiales-energy-pede-registro-para-listar-bdrs>;
3. VIRI, N. "Novata Manabi recebe registro de companhia aberta na CVM." *Valor Econômico*. 14/09/2011. <http://www.valor.com.br/financas/1005848/novata-manabi-recebe-registro-de-companhia-aberta-na-cvm>;
4. VALENTI, G. "Norueguesa Seadrill planeja obter até US\$ 800 milhões para subsidiária brasileira." *Valor Econômico*. 15/12/2011. <http://www.valor.com.br/impreso/eu-investimentos/norueguesa-seadrill-planeja-obter-ate-us-800-milhoes-para-subsidiaria-bras>;
5. WESTPHALEN, A. L.; FREGONI, S. "Karoon inicia oferta para captar R\$ 1,8 bilhão." *Valor Econômico*. 28/10/2011. <http://www.valor.com.br/arquivo/854395/karoon-inicia-oferta-para-captar-r-18-bilhao>;
6. SWANEPOEL, E. "Australia's Karoon Gas may list South American assets in Brazil." *Mining Weekly*. 8th June 2010. *Mining Weekly.com*.

\* Eduardo Vale, DSc., is the Principal of Bamburra Ltda., [bamburra@superig.com.br](mailto:bamburra@superig.com.br)