BUSINESS

SPACs are back – with a Latin American twist

Special purpose acquisition companies are all the rage in the U.S., and sponsors are now beginning to eye up Latin American firms for mergers and acquisitions

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There is a curious convergence between financial markets and the fashion industry. Like seasonal clothing collections, trends in finance come and go and every now again old styles come back in vogue, with modern twists. In the U.S., the flavor of the month in 2020 was the so-called special purpose acquisition companies, or SPACs. And this season, they are all the rage once more, with added Latin American flair.

SPACs are publicly listed companies created with the sole purpose of acquiring other firms and bringing them into the market. Thus, they are often known as "blank check companies." SPACs begin life with a group of investors — or "sponsors" — who set up a shell company without assets, products, or services. This empty firm is then taken public, after which the SPAC has 24 months to acquire a target company using the proceeds of its stock offering. If all goes well, this target business also becomes publicly traded.

The SPAC model has become increasingly popular for companies looking to go public. Data from S&P shows that SPACs raised USD 88 billion in the first quarter of 2021, obliterating the USD 76 billion record for the entirety of 2020. Financial data company FactSet **points out** that SPACs were responsible for half of all IPOs in the U.S. last year, joining the list of heavyweights Nikola, DraftKings, and Virgin Galactic.

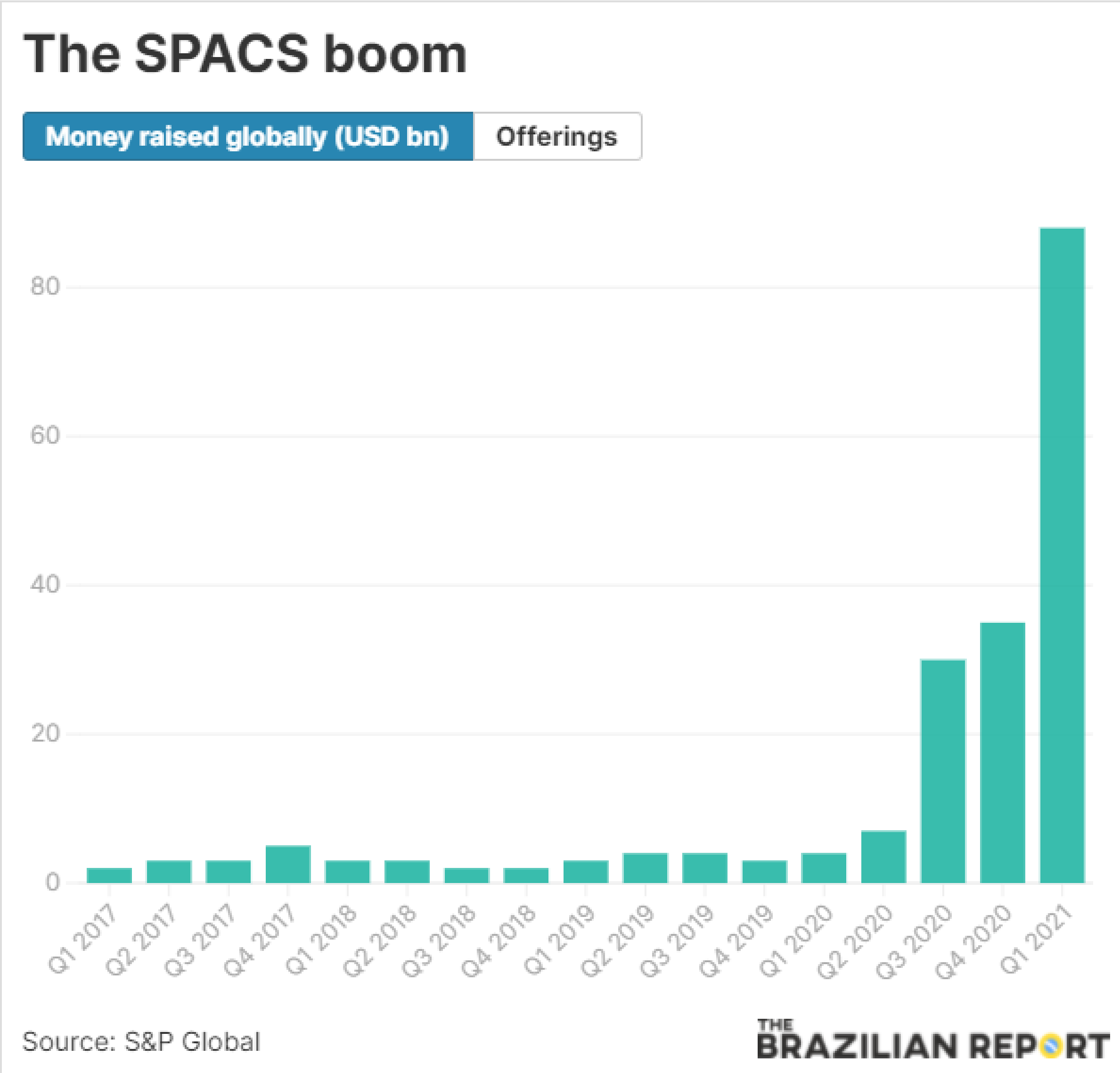
Indeed, going public by way of merging with a SPAC is a much simpler and quicker process launching a regular IPO. Furthermore, as the funds are already available, the entire process is more stable — the success of IPOs, meanwhile, are heavily subject to market conditions.

At the end of the day, however, SPACs are only as good as the reputation of their sponsors — which, so far, includes figures such as former **US House Speaker Paul Ryan**. On the one hand, investors place more trust in the decisions of esteemed sponsors, while the companies to be acquired can also benefit from the support of these executives in navigating the market.

And in an interesting development, sponsors are now casting their eye south of the Rio Grande in their search for target companies.

SPAC up your life

In 2021, a series of funds opened SPACs with their eye on Latin American companies. Among the most high-profile examples was **LDH Growth I**, a SPAC set up by the world's biggest tech-focused venture capital fund SoftBank. The blank check company raised a total of USD 200 million and will target sectors such as "mobile communications technology, artificial intelligence, robotics, and cloud technologies" in Latin America.



And the first success stories are beginning to surface. Colombian-based pharmaceutical firm Procaps had planned to go public for some time, and now hopes to do so before 2023.

Producing softgel in operations spanning 13 Latin American companies, Procaps was scouted by Union Acquisition Corp. II, a USD 200 million SPAC led by career investor Kyle Bransfield. The acquisition is expected to cross the finish line in Q3 of this year, funded by USD 100 million raised in an oversubscribed private investment in public equity (PIPE) transaction.

UAC II chief executive Dan Fink says that Procaps' long-term history and strong operational data played an important role in the deal's success, but governance is the key factor when it comes to any business in Latin America. "Latin American companies need great management to get this investor-base focused. (...) Ultimately, the common theme of the successful stories versus the non-successful ones will be great management," he tells **The Brazilian Report**.

Procaps CEO Ruben Minski notes that the company aims to capitalize on the possibilities of an IPO through a SPAC, including inorganic growth throughout South America, especially in Mexico and Brazil. "We have great expectations of becoming a USD 1 billion company in five years' time," he tells **The Brazilian Report**.

The China Hustle effect

The SPAC boom revived painful memories for regulators at the U.S. Securities and Exchange Commission (SEC). In the wake of the 2008 financial crisis, several Chinese companies joined the U.S. stock market by way of so-called "reverse mergers," which are similar to SPACs. Decades-long **securities fraud was later revealed** and stocks crashed, leading to massive losses that were particularly hard to swallow for retail investors.

Fast-forward to 2021, and the SEC has already **issued** several alerts to educate investors on the risks of SPACs, which include potential conflicts of interest between sponsors and the SPACs shareholders, fees, and sponsors' compensation. The SEC **stresses** that "it is never a good idea to invest in a SPAC just because someone famous sponsors or invests in it, or says it is a good investment."

Beyond mere warnings, Reuters reports that SEC regulators are **carrying out inquiries** on Wall Street and are seeking information about how underwriters are managing the risks involved.

In Mr. Fink's view, regulators are right to step in, as "the SPAC market became overheated and people were throwing money over a hope, a wish, and a prayer." In this sense, he believes stronger oversight can only benefit companies with a compelling governance case and will "protect the longevity of the SPAC market."

Brazilian SPACs in the pipeline?

As Brazilian private equity funds make their **first forays** into the U.S. SPACs market, questions have arised on whether the model could be replicated in Brazil — as the domestic market is in the middle of an **IPO boom** and venture capital for startups is abundant.

Currently, Brazil's securities commission (CVM) has put the matter to a public consultation, which will accept outside contributions until July. Brazilian regulators want to hear the opinions of market agents on initially limiting SPACs to qualified investors — namely, those who have over BRL 1 million in investment or are finance professionals — before opening them up to retail investors after 18 months.

"The justification for that is a potential regulatory overlap with Private Equity Investment Funds [FIP, in Portuguese] that, in a way, are similar to SPACs," wrote the CVM.

Self-regulatory organization Anbima already has a working group focused on the issue and plans to make submissions to the CVM's public consultation. As **reported** by newspaper Valor Econômico, one of the outcomes under discussion is the possibility of listing SPACs in Brazil as well.

Drafting regulation on the issue is key to preventing mishandling of the funds, according to Ricardo Rocha, a partner and finance professor at Finted Tech School. "SPACs are a very good idea, but you need to have solid regulation because people may not use the funds in the proper way," he tells **The Brazilian Report**.

"Will they issue them for qualified investors only? Will they regulate it as an initial public offering or a hybrid model between a publicly-traded company and a fund? There are several lingering issues on the subject."