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# Multilateral Financing for Companies in Latin America and the Caribbean

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In most Latin American countries, a broad range of companies possess risk profiles that inhibit their ability to raise capital through conventional channels such as bank borrowings or public securities issues. Some companies are too new to have a convincing track record, others are overburdened with debt, and still others have opaque financial statements. At a certain phase of growth, these firms can no longer compete effectively without raising capital—capital that is too large and costly to be financed internally. Multilaterals and private equity firms may fill the gap between self-financing and conventional capital market activities.

This article examines multilateral financing to small- and medium-sized companies through simple debt and equity financing; it will not discuss more complex forms of financing such as syndicated loan structures mostly reserved for larger infrastructure projects.

There are several multilateral organizations providing small and middle sized companies with programs to assist their financial needs while promoting private sector business development in Latin American markets. The International Finance Corporation and the Inter-American Investment Corporation are two of the regions' biggest investors, yet there are other significant organizations that are also addressed in this article. Following is a brief description of each including instruments and recent deals partaken.

## International Finance Corporation

The International Finance Corporation (IFC) is the private sector arm of the World Bank Group. The IFC operates on a commercial basis, invests exclusively in for-profit projects, and charges market rates for its products and services. A company or entrepreneur, foreign or domestic, seeking to establish a new venture or expand an existing enterprise can approach IFC for capital supply which he or she might receive through loans, equity finance and quasi-equity (quasi-equity financing is generally considered debt but having characteristics of equity capital, e.g., flexible repayment, expected higher rate of return and for the most part unsecured).

### *IFC in Latin America and Caribbean*

In a region where private capital flows have repeatedly proved capricious, the IFC is a long-term partner for good and bad times. This point is exemplified by noting that demand for lending was strong in fiscal year 2003, when there was a strong retreat of external financing in Latin America and the Caribbean. Committed financing in the region was $2.18 billion, an increase of $706 million from the previous year and the largest amount in recent years.

An example of the IFC's financing in the region is seen in Marcopolo, a Brazilian bus manufacturer. In September 2000, Marcopolo formed Polomex S.A. de C.V. (Polomex) through a 76/24 joint venture with Mercedes-Benz Mexico to assemble and sell buses in Mexico. Given the upsurge in demand and the growth prospects for exports and international operations, Marcopolo approached the IFC for a $40 million loan package out of the $80 million total project cost, which would help the company and Polomex maintain and upgrade equipment over the next three years; finance working capital needs stemming from both existing and expected growth in production; and refinance existing short-term debt.

An example in the telecom industry includes IFC's investment in the Caribbean, where it helped to break monopolies in the region through a notable investment in Digicel. Digicel is a provider of mobile telephone services which entered the Jamaican market in early 2001. Since then, Digicel has succeeded in attracting in excess of 700,000 subscribers, distinguishing itself from the incumbent provider through competitive rates as well as superior quality, functionality, and service. Total project costs were estimated at $120 million and the proposed IFC investment was up to $14.55 million, comprising a $10 million Senior Loan from IFC's account and up to a $4.55 million equity investment for IFC's account. After launching in Jamaica in 2001, expanding to the islands of Barbados, St. Lucia, Grenada, St. Vincent and the Grenadines, and Aruba in 2003, Digicel is pursuing opportunities in other Caribbean islands in its effort to build a pan-Caribbean network. In a recent news publication, it indicated that it did not disregard getting into other Central American countries.

***A-loans—Loans for IFC's Own Account***

For most A-loan issues (loans for IFC's own account) the IFC offers fixed and variable rate loans for its own account to private sector projects in developing countries. These loans are mainly lent in leading currencies, but local currency loans can also be provided. The loans typically have maturities of seven to 12 years. Grace periods and repayment schedules are determined on a case-by-case basis in accordance with the borrower's cash flow needs; in some cases these have been extended to as long as 20 years. Loans from the IFC finance both greenfield companies and expansion projects in developing countries. To ensure participation of other private investors, A-loans are usually limited to 25 percent of the total estimated project costs for greenfield projects, or, on an exceptional basis, 35 percent in small projects. For expansion projects, the IFC may provide up to 50 percent of the project cost, provided its investments do not exceed 25 percent of the total capitalization of the project company. Generally, A-loans range from $1 million to $100 million.

Interestingly, the IFC is willing to extend loans that are repaid only from the cash flow of the project, without recourse or with only limited recourse to the sponsors, which means that the loan is only or partially tied to the project's assets.

***Equity Financing***

The IFC takes equity stakes in private sector companies and other entities such as financial institutions, and portfolio and investment funds in developing countries. The IFC is a long-term investor and usually maintains equity investments for a period of eight to 15 years. When the time comes to sell, it prefers to exit by selling its shares through the domestic stock market in a way that will benefit the enterprise, often in a public offering. To ensure participation of other private investors, the Corporation generally subscribes to between 5 percent and 15 percent of a project's equity. IFC is never the largest shareholder in a project and will normally not hold more than a 35 percent stake and therefore does not take an active role in company management.

***Quasi-Equity Financing: C-loans***

The IFC also offers a full range of quasi-equity products with both debt and equity characteristics to private sector projects in developing countries. These products are called C-loans. Among other instruments, the Corporation provides convertible debt and subordinated loan investments, which impose a fixed repayment schedule. It also offers preferred stock and income note investments, which require less rigid repayment schedules. Quasi-equity investments are made available whenever necessary, to ensure that a project is soundly funded.

While it is beyond the scope of this article, the IFC also originates and participates in syndicated loans for larger projects.

***How to Obtain IFC Funds***

A foreign or domestic company can approach IFC directly or through a third party intermediary by submitting an "investment proposal." The investment proposal should contain a brief description of project as well as information about the sponsors and the company's operations, including: history and business of sponsors, including financial information; market and sales data; technical feasibility, manpower, raw material resources, and environmental issues; investment requirements, project financing, and returns and a timetable envisaged for project preparation and completion. After this initial contact and a preliminary review, the IFC may proceed by requesting a detailed feasibility study or business plan to determine whether or not to appraise the project. Should the project yield feasible results, a proposal will be drafted for approval by the Board of Directors. The time it takes for IFC to disburse funds for investments tends to vary on a project basis, on average from the initial contact to the disbursement of funds takes three to four months.

### Inter-American Development Bank Group: Inter-American Investment Corporation

Like the IFC for the World Bank, the Inter-American Investment Corporation (IIC) is the private-sector arm of the Inter-American Development Bank Group (IDB), together with the Private Sector Department of the Bank which mainly invests in larger infrastructure projects. The IIC promotes and supports development of the private sector and capital markets in its Latin American and Caribbean member countries by investing, lending, innovating, and leveraging resources.

The IIC provides long-term financing in the form of direct loans, direct equity or quasi-equity investments, lines of credit to local financial intermediaries in the form of smaller loans, agency lines with local financial institutions for joint lending, investments in local and regional private equity funds, and guarantees for and investments in capital markets offerings.

The IIC seeks to provide financing to companies that do not have access to medium- or long-term financing from the capital and financial markets. The IIC finances expansion projects in all economic sectors (except for arms manufacturing and trade, gambling, and real estate speculation). Its financing may be used for both local and foreign currency investments in fixed assets, permanent working capital, and pre-operating costs.

To obtain financing from the IIC, a company must be a profitable venture with growth potential requiring medium- or long-term funding to capitalize on its market potential. The IIC's target market comprises companies with sales ranging from $5 million to $35 million; however, it will work selectively with companies having sales in excess of $35 million. Eligible companies are typically majority-owned by citizens of any of the organization's 26 member countries in Latin America and the Caribbean, even though, on a limited basis, joint venture companies that are not majority-owned by citizens from the region. While profitability and long-term financial viability are a prerequisite for consideration for financing, other criteria related to the company's impact on factors that further economic development will be considered:

- job creation
- generation of foreign currency income or promotion of foreign currency savings
- transfer of resources and technology
- improvement of domestic management skills
- fostering of broader public participation in company ownership
- promotion of the economic integration of Latin America and the Caribbean

A recent IIC investment was done in Agrofértil S.A., of Paraguay, to finance its permanent working capital requirements and thus improve the company's debt profile. Agrofértil imports agricultural inputs and sells them in the Paraguayan market; it also purchases grain locally for export and provides its clients with technical assistance. The company also grows grain on its own land and holds a share of one of Paraguay's largest manufacturers of agrochemicals.

### Types of Available Financing Instruments

IIC loans and investments are denominated in United States dollars and may be up to 33 percent of the cost of a new project or up to 50 percent of the cost of an expansion project of an existing company. Based on cash flow assessment, repayment periods may range from five to 12 years, including a grace period of up to two years.

For equity investments, the IIC may invest up to 33 percent of an investee company's capital. The IIC will exit its shareholding through:

- sale on the local stock market if the company is listed;
- private placement with interested third parties;
- sale to project sponsors under a negotiated put option agreement; or
- redemption by the investee company.

The IIC may also participate as a co-financier of a loan when a project requires funding in excess of the its direct lending commitment; the additional sum may be arranged through a participation loan. The IIC would then fund one portion of the total loan, and participating financial institutions fund the other portion.

### Investment Funds

The IIC also makes equity investments in national, regional, and sector private equity funds that invest in Latin American and Caribbean companies that have no other appropriate source of such capital. These funds, which are managed by professional fund managers, are selected after careful consideration of their purpose, developmental impact, management quality, ability to mobilize resources for the region, and compliance with environmental protection and labor standards, among others. Eligible investment funds must meet the following minimum criteria:

- exclusive focus on Latin American and Caribbean companies
- partial or exclusive focus on companies with sales of $35 million or less
- experienced investment management team with demonstrated track records as investors and fund managers
- well-developed investment strategy and clearly defined investment parameters
- demonstrated ability to raise capital
- legal structure, investment return parameters, and expenses consistent with market practice

### How to Obtain IIC Funds

The IIC works very similar to the IFC in terms of the steps and activities necessary to obtain funds. When a firm seeks medium- or long-term financing to expand its operations, it must send a brief description of the company and a business plan to a regional office for the country in which the company is located, or directly to IIC headquarters.

If the project meets the eligibility criteria, more detailed information will be requested. After reviewing this detailed information, the IIC may decide to conduct an on-site project appraisal and arrange a meeting of the project sponsors with senior management.

If the results of the project appraisal are satisfactory to the IIC, a report with the proposed terms of the transaction is submitted for approval by the IIC's Board of Directors. If the transaction is approved, the terms of financing are finalized and legal documents are drafted and signed. On average it takes six months from the submittal of the application until the funds are approved for disbursement by the Board of Directors; however factors such as contract formalizations, can affect the time it takes for the actual disbursement to take place.

### Other Regional Multilateral Organizations

***CIFI (Corporación Interamericana para el Financiamiento de Infraestructura, S.A.)***

CIFI is a regional non-bank financial institution. Its objective is to promote and finance infrastructure projects and related services throughout Latin America and the Caribbean. It also provides long term debt financing and advisory services to infrastructure projects sponsored and/or operated by private sector clients. It provides term financing and advisory services to infrastructure projects located in Latin America and Caribbean countries.

CIFI provides financing and investment banking services in the following sectors: transportation and logistics, telecommunications, energy, water and sanitation, environment, social, tourism, and infrastructure related services. CIFI generally targets projects with total investment costs of up to $100 million, but may finance any size project.

Financing services of CIFI include credit guarantees and enhancements, leasing transactions, underwriting on a best efforts basis of corporate debt and quasi-equity instruments. The terms and conditions of CIFI's loans to a particular company will depend on the risk/reward profile of the proposed project. Loans will generally have maturities of between five and 15 years. Generally, CIFI's own financing amount will not exceed 25 percent of the total investment cost of a greenfield project; or 40 percent of the total investment cost of an expansion or rehabilitation project.

If a company seeks medium- or long-term debt financing from CIFI, it must complete and submit an application. After reviewing this detailed information, CIFI may decide to conduct an on-site due diligence. If the results of the due diligence are satisfactory a Project Report will be prepared and terms and conditions of the transaction agreed before submitting it to CIFI's Executive Committee for approval. Funds will be disbursed in accordance with the terms of the loan agreement.

***Corporación Andina de Fomento (CAF)***

Corporación Andina de Fomento (CAF) is a regional multilateral institution engaged in multiple projects in the Andean region to promote sustainable development mainly through the investment in debt or equity of public and private infrastructure projects for roads, transportation, telecommunications, power generation and transmission, water and environmental clean-up, as well as projects that foster the development of border areas and the physical integration of shareholder countries.

Through equity investments the CAF makes investments in strategic areas to support the development and growth of companies in its shareholder countries and their participation in securities markets, as well as acting as a catalyzing agent in attracting funds into the region.

The CAF invests in several ways:

- through investment funds that acquire, hold, manage and sell fixed- or variable-income instruments in companies and infrastructure projects represented by equity or the certificates of investment issued by them;
- directly or through equity investments in companies;
- through quasi-equity investments, such as subordinated loans, preference shares and convertible loans;
- CAF's basic criteria for selecting equity investments include: the external funds obtained as a result of the investment; impact on regional development; strategic character; presence in the decisions of the institution receiving the investment; exit mechanisms and profitability.

***European Investment Bank (EIB)***

The EIB supports viable public and private sector projects in infrastructure, industry, agro-industry, mining and services. EIB loans are project-oriented and linked to the financing of the fixed-asset components of an investment. Under the ALA III (Asian and Latin American) mandate, the EIB finances projects in Asia, Latin America and the Caribbean. In order to qualify under this mandate, projects financed by the EIB must present a mutual interest for both the country in which the investment is implemented and the European Union. Particular emphasis is given to investment projects that comply with one or more of the following criteria:

- subsidiaries of European companies
- joint ventures bringing together European and local firms
- private enterprises holding concessions to invest in and run public services
- transfer of European technology
- enhancement of the objectives of the EU cooperation agreements

Projects with a total investment above €25 million (approximately $32.5 million) can be financed through individual loans either directly to a project promoter or indirectly through a government or financial intermediary. The total investment of a typical project under the ALA III mandate is above €40 million ($52 million).

For example the EIB provided a €70 million ($90.75 million) loan for the extension of production facilities and upgrading of the existing plant for the manufacturing of passenger cars and engines in Puebla, Mexico. The EU nexus for this financing was that the loan would support the Volkswagen Group's strategy to maintain Mexico as the third largest production center of the Group and strengthening its position in the North America Free Trade Agreement market. ❏

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