'THERE NEEDS TO BE MORE AGILITY, FLEXIBILITY, PROMOTION AND SUPPORT FROM REGULATORS'

Interview with Daniel Dancourt, Partner and Head of Asset Management HMC Capital

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What is HMC Capital?

HMC Capital is a Latin American investment and financial advisory firm, with offices in Chile, Brazil, Peru, Colombia and United States in order to effectively approach the most important markets and investment opportunities in the region. With $5 billion under distribution (third party funds) and $1 billion under management, HMC provides investment opportunities to institutional and HNW clients. The firm has more than 60 professionals with local experience and market knowledge. Main businesses are Third Party Distribution, Asset Management, Private Banking and Advisory, & Placement.

HMC's vision for Latam markets involves the creation of solutions for investors, and contribution in the development and scalability of asset classes in the alternatives investment spectrum, with focus on Credit, Real Estate and Private Equity. HMC has developed a complete platform of third party products and strategies, and proprietary Latam products maximising the risk/return for its clients in the region.

In essence, HMC believes in innovating and generating value added strategies, which requires in-depth knowledge of the local markets and understanding investor's portfolio needs and restrictions.

What has been HMC's approach to the region?

Latin America has been very challenging these past few years for investors. Uncertainties around macroeconomics and politics have affected economic growth, and have had an impact in markets performance. Also, considering a lower global growth scenario, we have experienced lower interest rates, generating a challenging environment for investors looking for returns and yields. We expect this scenario will continue for the foreseeable future.

HMC has been able to quickly identify emerging opportunities arising from the changing environment, not only economic and financial, but also regulatory and legal. We have developed attractive investment strategies on a risk-return adjusted basis, focusing in areas where traditional sources of capital have not played a significant role. Despite a challenging environment in the region, there are significant opportunities in the development of capital markets, improvement of access to financing, and connecting investor's capital to different segments of the economy.

When you mention improvement of access to financing, what opportunities and trends do you see?

Financing in Latam countries has been mostly provided by banks. Although banks have played an important role in our economies, their presence has been unequal depending on the size of the companies. Particularly, SMEs have faced more restrictions in terms of types and maturities of loans they can access, which could become even more restrictive given regulatory trends. Moreover, banks tend to be pro-cyclical, which leaves a financing void for these types of companies during economic downturns.

In developed markets, such as US and Europe, alternative sources of financing have taken an increasingly higher role throughout the years. Asset managers have been among the biggest participants, with strategies such as Direct Lending, Mezzanine, Credit Opportunities, among others. These types of alternative sources are significantly less developed in Latam markets, but we see a great opportunity given the need for yield from investors, and the appetite for companies to diversify their sources of financing, particularly SMEs.

Another critical difference is that developed countries have well-functioning capital markets, which can be a major source of capital for companies. This area is seriously lacking in Latam countries, where only large corporations have real access to capital markets. There is no breadth in our markets, which compounds issues like illiquidity and diversity of investors. We think that the asset management industry can play an important role in the development of capital markets.

What has HMC done regarding these opportunities?

From the asset management side, we have developed a regional credit platform. We have strategies related to Mezzanine Real Estate in Chile, and a Credit Fund in Peru, which has a significant focus in capital markets development. This Credit Fund, called HMC High Yield Peru, was possible with the participation of the main local institutional clients and the International Finance Corporation (IFC) as investors in the Fund.

The Fund focuses on investments in fixed income securities from Peruvian mid-sized companies, with local ratings below AA-. There was a lack of companies with this profile issuing bonds, so this segment of the credit spectrum had not been developed before. One of the main reasons was a disconnection between these types of companies and institutional investors, who could not access this segment efficiently or due to regulatory constraints. Our Fund has been able to bridge the gap between institutional capital and mid-sized companies, serving as potential anchor investor for some single 'A' local rating bond issues, which had not been in the market before.

For investors, this has presented an opportunity to access attractive risk-adjusted returns, and for companies it has provided an additional source of capital to improve their capital structures, diversify their funding sources, and free lines of credit with banks. This is also good for the economy itself, as it is helping develop the local fixed income market, bringing new issuers and increasing market breadth, which we believe in the medium term, will lead to higher liquidity and attract more investors. The focus has been in Peru, but we believe there's a similar situation and opportunity in other parts of the region.

What are the main elements you look for in companies you finance?

Being a credit fund, the main focus has to be on an in-depth analysis of financial credit risk. We have processes and internal methodologies that allow us to assess the main risk factors of each company, in order to avoid not only potential defaults, but to be able to adequately price these risks in a market that had no previous reference.

However, there are two key considerations that are embedded in our credit analysis, and that we think are vital for the sustainability of the capital markets and the companies themselves, particularly in the mid-sized segment. We look for good corporate governance, and for companies that are socially and environmentally responsible. This includes qualitative variables, such as independent directors, audited financial statements by a recognised firm, proven ownership and management experience, labour formality and security for workers, among other things.

What do you see as the main barriers for a capital markets development strategy?

We have identified three main difficulties. The first one is regulation. Although there are efforts being made, like the 'Mercado Alternativo de Valores', to make access to the market simpler and cheaper for mid-sized companies, the approval processes still take very long and sometimes with unnecessary restrictions to the bond structures due to standardised formats.

The second is education about capital markets. Several companies are aware of the bond market, but have never thought it was a possibility for them and are not fully aware of the benefits. Also, certain concepts are not easy to grasp for companies that are seeing the market for the first time, which is the case for many family-owned businesses.

The third one is cultural. Some business owners are not used to disclosing information to the public, and don't feel comfortable adhering to the standards of corporate governance and reporting of the markets. Although there are cases were there has been resistance, in general this difficulty can be addressed once the company understands the benefits of the market.

We have seen improvement, and we actively work with the companies to address these barriers. However, for a true development of the capital markets, there needs to be more agility, flexibility, promotion and support from regulators. Also, the educational process should come from across the board because it involves every entity that is involved in the market, including investment banks, securities brokers, rating agencies, media, investors and regulators. IFM

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