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Corporate M&A 2022

Panama: Trends & Developments

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Trends and Developments

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Introduction

The fall and rise in gross domestic product (GDP) from 2020 to 2021 highlights the COVID-19 impact on Panama's economy. 2020 was marked by a fall of 17.9% in GDP as a by-product of the lockdown measures and temporary labour furloughs related to the pandemic. In 2021, GDP bounced back 16.2%, above the International Monetary Fund's estimate of 12.5%. Similarly, foreign direct investment (FDI) fell by 86% between 2019 and 2020, but also bounced back to 2017–18 levels in 2021. Panama continues to be the beneficiary of the majority of the FDI inflows in Central America. Furthermore, the government has engaged in anti-cyclic measures to push for further economic recovery, including a public works investment programme.

2021 was marked by a recovery not only in GDP but also in M&A activity. M&A activity in Panama is expected to continue the pace in 2022, as Panama's economy is projected to grow more than 5%, the second-highest growth in the region.

Notable acquisitions

Notable acquisitions in 2021 were in the telecommunications, retail, warehousing and logistics and distribution sectors. For example, Emergent Cold Latin America made its first investment in the Central American region in the acquisition of Galores Group, the largest 3PL cold storage facility in Central America and the Caribbean based in Panama City. Liberty Latin America also increased its foothold in Panama by acquiring, through its affiliate Cable & Wireless, the Panamanian operations (*Claro Panamá*) of América Movil, following recent legislation allowing for consolidation between mobile carriers. 2021 also signaled local investors' confidence in the future of the country, as the founders of Supermercados Xtra, the leading supermarket in Panama, reacquired the controlling stake previously held by a Southern Cross Group controlled entity. The recent acquisition of Fertica Panama, the leading agricultural input distributor, by Disagro/Abopac (based in Guatemala), marks the increased expansion of Central American groups in the country. This transaction in particular had to overcome COVID-19-related challenges which delayed the closing of this transaction. The banking industry, on the other hand, did not experience further consolidation in 2021 as buyers and sellers in this sector continued with a "wait and see" approach to gauge the impact that credit-relief measures and other temporary banking regulations had on banks' balance sheets. That said, the expectation is for consolidation to resume and M&A activity among small and mid players to increase in 2022.

A 2022 resurgence

As Panama's GDP and FDI is expected to continue to grow and recover in 2022, Panamanian companies will become more attractive targets for foreign buyers. Indeed, despite a pandemic-related credit downgrade in 2020, Panama continues to retain investment grade status and remains the only country in Central America with such rating (on January 2022 Fitch revised the country's risk outlook to "stable"). The government is also betting on public spending in infrastructure works, especially through a public private partnership law, which will facilitate FDI in public infrastructure projects, which alongside the usual multinational conglomerates, should entice new market entrants and stimulate FDI through private equity.

That said, some industries have also lagged behind. The construction and hotel and restaurant sectors suffered the COVID-19 pandemic the most. Construction, in particular, is one of the main private sector drivers of growth and makes up approximately 15% of the country's GDP and its recover is still well below the pre-pandemic levels of 2019.

Both have had a slow recovery in 2021 but such recovery should accelerate into 2022, considering that Panama is expected to soon lift mask mandates and reinvest in tourism.

June 2022 is bound to have an impact in the economic outlook of the country, which is deadline provided by the Financial Action Task Force (FATF) for completion by Panama, grey listed, of its action plan to strengthen its anti-money laundering and financial terrorism regimes. FATF has found in recent meetings that Panama has complied with eight of its fifteen action items. Countries such as France have acknowledged that its lag in the seven pending action items may be due to the effects of the pandemic.

Effects of the New PPP Law

The government is also aiming to drive the economic recovery with investments in public infrastructure projects by way of public private partnerships pursuant to the recently enacted PPP law. Such law was recently regulated in December 2020 with the technical assistance of the World Bank, and co-operation from multilaterals such as CABEI, CAF, and IDB. The first government tenders are expected in 2022. In particular, the first project under the PPP law will be the construction of 247 kilometers comprising the Cañita-Agua Fría-Yaviza component of the Pan-American highway for an amount of USD140 million, which would be undergoing public consultation in April 2022. Overall, President Laurentino Cortizo had announced in 2021 that in its first phase, three PPP initiatives will be undertaken: a 2,000 km road maintenance works, the costanera road in Panama Oeste and the Corredor Norte of David, Chiriqui, in the western part of the country.

It is expected that such initial projects, among others projected for 2022 will pave the way for many more projects in the coming years, which will provide opportunities for private investment, and M&A, to follow suit.

Start-Up Activity and Success Stories

Panama's position and a regional hub and business friendly climate has also proved to be attractive to foreign investors in tech-based companies and industries, and we expect a boost in strategic alliances and M&A activity in this sector to increase rapidly. Hotel platform Selina started in 2015 in a famous local beach Venao in Pedasi, province of Los Santos, and on December 2021 announced that it would go public via through a SPAC at a valuation of USD1.2 billion. It started with two hotels in Panama and, seven years later, now boasts 140 hotels in 23 countries. The transaction is expected to close in the first half of 2022.

Other start-ups have seen substantial cash injections from private equity groups, regional players, and international buyers looking to enter into the Latin American playing field. Encuentra24, an online classifieds and real estate platform first launched in Panama, has expanded to nine additional markets in the region. Appetito24, a food delivery app, was acquired by German conglomerate Delivery Hero, and in 2021 acquired and merged one its main competitors, Glovo jointly with PedidosYa, surviving the latter.

Other applications, such as Cuanto, a payment-processing service platform, Panadata, a background checks platform, and more recently in 2022, Panamanian start-ups Munily and PayCaddy, have received support from American seed accelerator Y Combinator. Munily is a proptech start-up that streamlines communications between members of residential or commercial communities and offers security solutions, and PayCaddy is a fintech which develops a Neo-Bank API that allows financial entities and companies to quickly deploy digital banking services and products. Nowports, another Y Combinator-backed start-up, opened in 2022 offices in Panama. It is a digital freight forwarder, mixing logistics with financial and technological tools to ship cargo in an efficient, transparent, and secure manner.

Other Regulatory Developments

In recent years, Panama's tax authority (DGI) has increased audit and enforcement measures for capital gains tax, focusing particularly on high-profile transactions. The DGI has also begun reviewing and, on occasion, conducting full audits of local targets, triggered by public announcements of deals being signed or closed. In addition, stricter criminal statutes for tax evasion were enacted in early 2019. The pressure on tax audits may increase in the following years considering the budget deficits that have been undertaken by the government following the COVID-19 pandemic.

ACODECO, Panama's antitrust and consumer protection agency, on the other hand, has also increased scrutiny in recent deals, resulting in potential buyers to demand stricter representations and indemnities. This has been focused on purely local deals than for deals where the buyer has no prior presence in the country. However, amidst the pandemic, the protection agency has, at least on one occasion, allowed for consolidation of a particular industry, which may hint at increased flexibility during these times.

Foreign Deals Impacting Panama

Consistent with Panama's historic FDI levels, foreign deals continued to have an impact in the country. Two examples in 2021 include the proposed acquisition by Canadian Pacific Railway of Kansas City Southern, the US-headquartered transportation holding company, which owns railroad investments in Panama. In addition, Stonepeak Infrastructure Partners acquired the Latin American operations of Lumen Technologies, formerly CenturyLink. Being Panama one of the main hubs in Latin America, increased regional M&A activity will continue to have an impact locally in 2022 and beyond.

Expectations for 2022 and Beyond

The administration of President Laurentino Cortizo continues its attempts to remove Panama from the tax havens lists. The government now faces the challenge of leading the economic recovery of a country that prior to the pandemic had been known for being a stable investment-grade economy, welcoming to foreign investment. But ongoing pandemic related challenges, such as growing unemployment (now at 11.3%), weaker consumer demand, together with an increased debt/GDP ratio (up to 63.7% in 2021 from 39.6% in 2018) may affect business valuations and have a negative impact on total M&A activity. Notwithstanding, giving the liquidity and growth of the US M&A market, Panama's stable and centrist government compared to other more troubled peers in the region, the expected economic recovery suggests FDI (and hence broader M&A activity) may well increase in 2021 and M&A deal flow will still be at or even higher than during pre-pandemic levels.

Again, the most active sectors for M&A activity in 2022 and the years ahead will likely continue to be in the logistics sector, followed by the banking industry, as further consolidation in the market is expected. A weaker than expected recovery in tourism and consumer spending will likely also drive acquisitions of distressed assets in the real estate, hospitality and retail sectors. Increased lending and technology upgrades and compliance costs specific to Panama's banking sector are expected to drive M&A and FDI levels in both these industries.

Arias, Fábrega & Fábrega has been advising leading international financial institutions and multinational corporations, as well as some of the largest domestic companies in Panama, for over 100 years. Highly specialised multidisciplinary legal teams enable efficient handling of complex M&A transactions, covering corporate law, antitrust, taxation, securities regulation, banking, environmental law, labour, real estate, regulatory work and IP. The M&A team consists of 13 lawyers with a wealth of international experience, and nearly half the team admitted to the New York or Florida Bar. Recently, the firm has counselled Grupo Rey in the sale of a 73% stake to Favorita, United on a complex joint venture deal with Avianca and Copa, shareholders of Cable Onda in the sale of 80% to Millicom, Assicurazioni Generali in an asset sale agreement to ASSA, and Inchcape in its acquisition of Grupo Rudelman.

AUTHORS

Andrés N Rubinoff is a partner in Arias, Fábrega & Fábrega and has acted as leading lawyer in some of the largest and most relevant M&A transactions in Panama. Worth mentioning are Grupo Rey's sale to Corporación Favorita, United complex joint venture deal with Avianca and Copa, Cable Onda sale's to Millicom, Assicurazioni Generali's asset sale agreement to ASSA, and Inchcape's acquisition of Grupo Rudelman. Andrés has worked as an associate with Greenberg Traurig (Miami) and for the Corporate Executive Board Company in Washington, DC. He is admitted to the Panama and Florida Bars.

Javier Yap Endara is a senior associate of Arias, Fábrega & Fábrega. Javier regularly advises clients on financing and M&A transactions, having participated in some of the largest and most relevant ones recently taking place in the country. In the financing working group, he advises purchasers/lenders in cross-border financing arrangements, and the financing and refinancing of major infrastructure work, including local ports, airports and subways. In the M&A working group, he has participated in the sales of Cable Onda (main telecom provider), Grupo Rey (leading supermarket chain), Suzuki distribution business, and Fertica (leading agricultural input distributor). Javier also regularly advises clients interested in setting up fintech operations in Panama.

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