

Brazilian prepaid card industry to consolidate in face of costly new compliance requirements - Analysis

The establishment of a legal and regulatory framework for the Brazilian e-payment industry is likely to spur consolidation within the meal voucher and prepaid card industries, advisors and executives said.

Small-sized companies will not be able to comply with the new requirements imposed by the Brazilian National Monetary Council (CMN) and the Brazilian Central Bank (BACEN), predicts Valerio Marega, CEO of the M&A boutique firm ASK Brasil.

If they do not merge with other small-sized peers or become incorporated by larger competitors, they could be forced to shut down, he said.

Potential buyers

Marega, who was mandated by a local player to prospect for suitable targets, believes the consolidation will unfold in two phases. First, regional players like **Policard**, **Sorocred** and **Valecard** are likely to start making acquisitions and initiate the consolidation movement. In a second phase, the sector's largest companies - **Alelo**, **Edenred** (EPA: EDEN) and **Sodexo** (PARIS: SW) – will likely become more proactive and begin a hunt for these regional peers, he suggested.

“It does not make sense for a large company to spend time and energy now to buy a small peer with only a few customers,” he noted. “On the other hand, regional players see small acquisitions as opportunities to enter new markets and diversify their portfolios,” he explained.

The vast majority of small players have a very limited portfolio, with only meal and food vouchers, while regional players are able to offer a broader array of products, such as prepaid gasoline and travel cards, Marega explained.

The advisor classifies regional players as companies with an annual transaction volume of around BRL 5bn (USD 2.1bn) from meal and food voucher operations, while large players generate more than BRL 10bn.

Policard's president told this news service in July that it had mandated two local M&A advisors to carry out talks with potential targets. One of the mandated advisors focuses on identifying suitable targets with annual revenues of less than BRL 20m (USD 8.8m), while the other concentrates on medium to large-sized peers.

Another potential bidder is the family-owned **Greencard**, which also wants to take advantage of the current situation to make key acquisitions. According to commercial director Jorge Elias Oliveira, the Rio Grande do Sul-based company has received several approaches from smaller peers hoping to associate with it since the regulatory framework was put into practice.

“Some of these companies made clear that they will not make the necessary changes to comply with the new rules, and came to us to see if we would like to incorporate them,” Oliveira highlighted. Some of these talks, he noted, are at an advanced stage and may be

concluded in 1Q15.

Greencard relies on its 25-year experience in the sector to internally carry out its M&A strategy, which mainly focuses on boosting its presence in the regions of Southeastern and Southern Brazil, the commercial director said. It expects to achieve BRL 820m in volume of transactions this year and projects to achieve BRL 1bn in 2015.

Greencard is part of **Grupo Greencard**, a holding company operating in several industries, including logistics, port operations and real estate.

Private equity funds are also carefully studying the sector, noted Bruno Balduccini, partner at the law firm Pinheiro Neto Advogados. Without providing names, he told *Mergermarket* that two local PE firms have recently consulted with the law firm to better understand the legal and regulatory framework for the sector.

Compliance requirements

Balduccini agrees that it will be very difficult for small-sized companies to bear the compliance costs related to the sector's regulation, as well as set up internal structures to provide the great amount of information demanded by CMN and BACEN.

Balduccini explained that the legal and regulatory framework, which was signed into law in October 2013, states that companies operating in the meal voucher and prepaid benefit card industries are subject not only to BACEN supervision, but also to the rules applied to financial institutions.

Another key rule includes the requirement to set up risk management controls, such as minimum net equity, minimum initial capital, anti-money laundering controls, and an ombudsman department, among other measures, Balduccini explained.

He added that the regulatory framework also demands companies to gradually allocate their balance of payment accounts to a specific account at BACEN, or invest that in federal government bonds. The percentage starts at 20%, but will increase to 100% in 2019, he noted.

“Even though some issues still need to be clarified, the regulatory framework has the potential to create a more favorable business environment and get rid of a few obstacles that prevented the further development of the sector,” Balduccini concluded.

by Thiago Barrozo in Sao Paulo