# ACCESSING THE US CAPITAL MARKETS BY LATIN AMERICAN COMPANIES


REMARKS BY

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*The views expressed herein are those of Commissioner Schapiro and do not necessarily represent those of the Commission, other Commissioners or the staff.


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Good morning. It is a pleasure to be in Buenos Aires and an honor for me to participate in this important conference. In the last two years, I have enjoyed enormously working with Latin American companies and governmental authorities, particularly the Argentine Comision Nacional de Valores, on a wide range of issues related to cross-border offerings, trading and regulation. From the SEC, I have had a wonderful vantage point from which to view the renaissance of Latin American economic and financial systems. I admire the courage and vision of finance ministers like Domingo Cavallo, Pedro Aspe and Alejandro Foxley - to name just a few - who have put into place the far-reaching and fundamental reforms necessary to control inflation and instill confidence in the domestic currency, reduce foreign debt, privatize state-owned industry and re-attract flight capital.

As a regulator, I have probably seen these changes from a slightly different perspective than most of you. I know how hard it is to make governments change course - even slightly. I appreciate the effort it takes to build consensus within government, and then to sell a program of reforms to industry and the public. And most of all, I know how difficult it can be for public servants to make the hard

decisions that ultimately must be made, but which can cause, in the short run, real economic pain and social dislocation. In Argentina and many other countries of Latin America, governments are exhibiting the courage and creativity necessary to solve the problems of the last decade, to make those difficult choices and keep the ship of state on the course of economic deregulation. I applaud those efforts and assure you that they inspire us to try to be as creative and forceful when we deal with our own domestic economic issues.

The impact of the choices your governments are making are reflected in a variety of statistics which indicate that the 1990s are shaping up as the decade of Latin America. The positive reaction of domestic and foreign investors to economic reforms here is demonstrated by the successful privatization of state-owned industries; increases in market capitalization, growth of new issues, and the creation of at least sixteen Latin American country and regional funds in 1991 alone with the dedication of over one billion new dollars. A review of the IFC Index reveals that Latin American market advancements are not merely keeping pace with other emerging markets; in fact, the advances are much greater. During 1991, while the IFC Composite Total Return Index of Emerging

Markets increased a respectable 19%, the Latin American component increased an amazing 134%.

Despite recent market adjustments - felt virtually throughout the world - Argentina last year was the fastest growing emerging market in the world. It has become a leader in Latin America - it can be and indeed it is, a model for the nations of the region seeking to institutionalize the concept of free markets and acquire for their people the benefits and prosperity that open economies can bring. The importance of transmitting the benefits of economic growth to all levels of society was recently recognized at the Ibero-American conference in Madrid in July and by the Finance Ministers of the Western Hemisphere at their late June meeting in Washington, DC. The Ministers emphasized that there is no contradiction between economic stability and growth or between economic growth and social justice.

The results of that meeting were the recognition of a "New Partnership" between the countries of the Western Hemisphere, based on a mutuality of interests in stronger economies and financial markets, open trade through the successful conclusion of the Uruguay Round and the North American Free Trade Agreement, the

evolving and increasing importance of the InterAmerican Development Bank and the Enterprise for the Americas Initiative, and in the achievement of stable democracies.

On perhaps a more modest scale, but certainly also indicative of the pervasive sense of hemispheric destiny, the securities regulatory authorities from 16 countries in our Hemisphere also met in June of this year. The result of two days of meetings in Mexico was the formation of the Council of the Securities Regulators for the Americas, or "COSRA", chaired by SEC Chairman Richard Breeden. COSRA is based on the premise that securities markets are fundamental to the development of private enterprises, the formation of savings and investments, the efficient allocation of resources and the promotion of economic growth. It specifically recognizes the interconnection between the securities markets in the Americas and the need to promote continuing development of the markets for the benefit of all the people of the Western Hemisphere. The goals of its members are to propose and implement legal, regulatory and structural reforms to facilitate broad-based participation in securities markets, by fostering the basic protection of investors through the enforcement of sound accounting principles with standards for full and fair disclosure and ethical treatment of customers; by development of systems to ensure

market transparency and efficient clearance and settlement systems; by establishing linkages among markets to enhance liquidity; and finally, by identifying and working toward the removal of regulatory barriers that unnecessarily impede cross-border investment opportunities. The overwhelming commitment of the attending regulators was to a system of full cooperation within our hemisphere.

Why is all of this cooperation important? What is it that leads finance ministers and securities regulators alike to express so clearly and forcefully their desire to work together?

The answers to these questions are to be found in the evolution of the relationship between the markets and investors of North and South America. The need for cooperation on issues related to the capital markets is particularly acute when one considers that in 1991, Americans were net purchasers of 2.6 billion dollars worth of Latin American securities and the total international cross border transfer of funds into equities and bonds totalled $388.7 billion (according to BIS).

Because we are convinced generally that the cross-border flow of capital is such a positive development and one that will continue - in

fact, so far this year, companies have sold $14 billion worth of securities in public offerings outside their home market - the SEC has undertaken in the past few years, significant initiatives designed to facilitate cross-border offerings of securities. The centerpiece of these initiatives was the promulgation of Rule 144A.

The adoption of Rule 144A under the Securities Act has had a significant impact upon the accessibility of the U.S. market to foreign issuers. The Rule, which represents an attempt to free the flow of capital between nations, provides a safe harbor exemption from the federal registration requirements for the resale of restricted securities to "qualified institutional buyers", or "QIBS."

In promulgating the rule, the Commission hoped to attract more foreign issuers to the US private placement market, and also to improve the liquidity of that market. We believed that foreign issuers that previously may have foregone raising capital in the United States due either to compliance costs or liability concerns, or because of the discount and financing costs inherent in selling restricted, illiquid securities, might now find the U.S. private placement market more attractive as a result of this rule.

Rule 144A facilitates the growth of the foreign private placement market by permitting the resales of certain securities in the United States without requiring the registration of the securities with the SEC. The securities sold through the Rule can be any class of security, but may not be of the same class as securities already listed on a registered U.S. securities exchange or quoted on the National Association of Securities Dealers Automated Quotation system.

Securities of domestic issuers eligible for resale under Rule 144A generally are sold initially in private placements subject to an exemption to the registration requirements. Foreign securities resold in the U.S. pursuant to the rule generally are initiated as offshore public offerings which, pursuant to Regulation S, are not required to be registered under the Securities Act.

Securities sold in the U.S. utilizing the Rule 144A safe harbor must be sold only to so-called QIBs. As a general matter, in order to qualify, an institution must in the aggregate own and invest, on a discretionary basis, at least 100 million dollars in securities of issuers (excluding the US government) that are not affiliated with the institution. There are some different requirements for banks and broker-dealers. The largest purchasers of 144A securities typically

have been insurance companies, private and public pension plans, banks and investment companies or mutual funds. In general, US mutual funds have become some of the largest owners of foreign equity, public and private. As of May of this year, the assets of stock funds that invest primarily in non-US equity totalled nearly $42 billion, and the assets of global bond funds equalled more than $28 billion.

The Commission proposed only two weeks ago to expand the definition of Qualified Institutional Buyer to include collective trust funds (a trust fund whose assets consist of funds from multiple pension plans or other employee benefit plans of more than one employer; thus each separate plan need not qualify as a QIB in order for the trust to be a QIB); master trusts (multiple plans under the common sponsorship of a single employer); and insurance company separate accounts. These collective trust funds are a significant means of investing both private and government pension funds. While it is difficult to be precise, the inclusion of insurance company separate accounts which will increase the ability of insurance companies to participate in the 144A market, and the addition of collective and master trusts, potentially add a trillion dollars of new buying power to the 144A market.

By not being required to register, foreign companies availing themselves of Rule 144A are relieved of certain reporting and information requirements, and in particular, the reconciliation of financial statements to US GAAP. If the issuer of the securities is neither a reporting company in the US, nor providing limited home country information pursuant to the foreign issuer exemption (contained in Rule 12g3-2(b) of the Exchange Act), the issuer of the securities is required to provide a security holder with a brief statement of the issuer's business and most recent financial statements, preferably audited. This information requirement is sufficiently flexible and specific so as not to be a burden on issuers.

The data from the two years of the life of the rule is very positive, bearing in mind that this is a private placement market and will likely never have the liquidity of a public trading market. Nevertheless, Rule 144A clearly has attracted foreign companies to the U.S. capital markets. Since the rule's adoption, more than $7.6 billion of securities relating to 118 foreign issuers have been sold in 107 Rule 144A placements. ($11.8 billion of securities of 66 US issuers have been sold in 74 Rule 144A placements).

Latin American issuers and guarantors have been among the most active in this market. There have been 23 144A offerings by Latin American companies in the last two years, including four from Argentina (sovereign debt, Alpargatas S.A.I.C., Acindar Industria, Telefonica). The total value of these Argentine offerings (US and non-US tranches) is nearly $500 million of debt and equity.

Finally, we hope that foreign companies will use Rule 144A as a stepping stone to the U.S. public markets. Companies doing private placements can gain an understanding of the U.S. offering process, our markets, investors, broker-dealer community, and the SEC. Thus initiated, the step to registered public offerings should seem less bold. The recent efforts by Telmex, the Mexican phone company, first in the private placement market, and then in two substantial public offerings, are evidence of the success of this stepping stone approach.

The Telmex offering also was significant because it demonstrated the efforts the SEC is willing to make to facilitate cross-border transactions. In our efforts to encourage foreign issuers to access the US public markets, the SEC's Division of Corporation Finance works with foreign companies to facilitate the registration process and

in some cases to accommodate foreign issuers' accounting and financial reporting.

Given the success of the Telmex and other Latin American public offerings such as the Brazilian Aracruz Cellulose, I thought it might be helpful to summarize briefly the U.S. public offering process. Although the process at times seems complex, we perpetually are trying to maintain a balance between simplicity and the protection of investors and other market participants.

The vast majority of foreign issues in the US are offered in the form of American Depositary Receipts. The ADR arrangement provides several benefits to US investors in foreign securities over direct ownership of the securities, including the facilitation of share transfer and the conversion of dividends paid in a foreign currency to US dollars. ADRs have been used in connection with mergers and acquisitions, restructurings, foreign government debt offerings and the funding of employee benefit plans. ADRs are traded in the US in substantially the same manner as domestic issuers' equity securities. Some foreign issuers, such as Telefonica de Chile or Telmex, seeking to increase visibility and improve liquidity and access to US capital, choose to list on a stock exchange or to have their ADRs quoted on

NASDAQ. Other foreign issuers choose to have trading in their ADRs conducted in the US over-the-counter market through market makers that publish quotes in the "Pink Sheets" or the electronic bulletin board.

Under the federal securities laws, any securities transaction which involves the use of the U.S. mails or other facilities of interstate commerce is subject to the jurisdiction of the SEC, and the statutes and regulations that the SEC administers. The laws that the SEC administers govern the disclosure process for public offerings, and the reporting and registration requirements of issuers once a public offering is completed, to ensure that full and fair disclosure of information regarding the issuer and its securities is available to enable investors to reach informed investment decisions. It is important to remember that, in the federal context, the regulatory scheme is geared not to an evaluation of the merits or potential success of an issuer or its securities, but solely to whether the applicable disclosure requirements have been met.

As a threshold requirement, all documents and statements must contain no untrue statement of material fact, or omit to state a material fact whose omission would make the statements misleading.

Failure to adhere to this anti-fraud standard in the filing of disclosure documents can be a predicate for both civil and criminal liability.

Under the Securities Act, all offerings of securities must be registered with the Commission, unless an exemption is available. Two principal documents must be prepared in connection with a public offering; the prospectus and the registration statement. The prospectus describes the issuer, the securities being offered, and the terms of the offering transaction. The prospectus must be delivered to all persons who purchase securities from the underwriters, and generally is the only written document that may be delivered during the offering period. The registration statement is filed with the Commission, and includes the prospectus and other information and documents required by Commission rules. The offering may not legally go forward unless it has been reviewed by the SEC and the registration statement has been declared "effective". This is generally a process of give and take between the SEC staff and the issuer to ensure that all necessary information has been disclosed in the appropriate manner.

The Commission, to facilitate the registration of foreign issuers, has adopted a three tiered registration system for such issuers.

Foreign private issuers entering the US market for the first time file a form F-1, describing how the proceeds of the offering will be used, the terms of the underwriting, a detailed description of the issuer's business and financial information including audited financial statements and historical financial data. To facilitate the registration process, world class foreign issuers, or those that already have a presence in the US public market may register their securities on a shorter form (F-2 or F-3).

The registration of ADRs technically requires the registration of two securities, the underlying shares and the ADRs. The ADRs are registered by filing a Form F-6, which requires information concerning the depositary arrangement. The underlying shares are then registered on Form F-1, 2 or 3. Issuers may choose to establish an ADR facility without an offering by filing the F-6 form alone.

Accessing the US public markets brings with it other obligations on the part of foreign issuers, such as the information supplying requirements of the Exchange Act (Rule 12g3-2(b)), and the antifraud prohibitions of US law. But the increasing numbers of foreign issuers that come to the US markets find that while there are definitely costs associated with having a US presence, it is a cost that is justified by

the returns. And the SEC is continuously searching for ways to reduce these costs and open our markets to the widest array of foreign participants. The continuing world-wide competition for capital - especially in this era of reluctant bank lending - requires us to do no less.

The advent of the North American Free Trade Agreement between Canada, the United States and Mexico, and eventually a free trade agreement between the US and the Mercosur nations will likely increase the access of investors and companies in each country to all markets. It will become increasingly important for us to work together to successfully take advantage of the benefits this increased access can bring. The SEC, under the leadership of Chairman Breeden, is committed to working with the Argentine authorities and with our own industry and exchanges, to do our best to insure that the spirit of free trade and open access spreads to the financial markets and the capital formation process.

Thank you.