FINANCIAL TIMES

January 12, 2015 4:04 pm

Dealmaking puts Brazil at the centre of global telecoms war

Samantha Pearson in São Paulo

For Maria da Conceição Santos, a 49-year-old office cleaner in São Paulo, making a phone call is a complex operation. Like many poorer Brazilians, she has a mobile that holds two Sim cards, allowing her from one phone to use two pre-paid carriers — in her case, Oi and Tim, Telecom Italia's Brazilian subsidiary.

"When I call my father in the north I have to remember to use Tim because it's cheaper for national calls," she explains. "I use Oi for the rest of my relatives here who have Oi because it's free — we're a Tim/Oi family!"

But analysts say that the growing popularity of these phones, some of which can take up to four Sim cards, is an indication of why Brazil's telecoms industry needs to consolidate.

Bayard Gontijo, Oi's chief executive, agrees. "Consolidation will bring greater synergies and help improve the quality of services," he said.

The slowdown in Brazil's economy, which is expected to have grown less than 0.2 per cent last year, has only strengthened the case.

The four main operators, which also include Claro, owned by Carlos Slim's América Móvil, and Telefónica's Vivo, have become so desperate to hold on to market share that with careful planning and the right phone, Brazilians such as Ms Conceição Santos barely have to pay anything at all.

That could all change following the likely break-up of Italy's Tim — the final stage of a frenzy of dealmaking that put Brazil at the centre of the global telecoms wars.

But while the growth of Brazil's middle classes has prompted a surge in mobile phone ownership over the past decade — there are more mobile phones than people — this has not translated into higher returns.

The question is which of the four operators will disappear. Many analysts say it will be Tim. Regulatory pressures, price wars and Italy's stagnant economy have put pressure on Telecom Italia, its parent group, leaving it with €27bn of net debt.

In August, the company also lost out to Telefónica in its bid for Vivendi's Brazilian broadband business GVT — its last chance to compete with rivals as a "one-stop shop" operator in Brazil.

Oi is perhaps even more vulnerable after its merger with Portugal Telecom broke down when the group was linked to Portugal's crumbling Espírito Santo empire last year.

While Oi's €7.4bn deal to sell Portugal Telecom's Portuguese assets to France's Altice last month could give it more financial firepower, a €1.2bn bid for Portugal Telecom's holding company from Portugal's Terra Peregrin may jeopardise the sale. The CMVM, Portugal's stock market regulator, also suspended shares in Portugal Telecom last week, saying the group needed to provide more information to shareholders on the planned sale to Altice.

The Brazilian government will never allow Oi, the industry's only homegrown operator, to disappear, however, says Celson Placido at XP Investimentos. "The logical thing would be for Tim to buy Oi and break it up among the other three but that will never happen," he said.

46%

The combined share of the Brazilian market for Tim and Oi

The most likely scenario is for Tim to be divided up, says Juarez Quadros do Nascimento, a former Brazilian communications minister who now works at the consultancy Orion. A standalone acquisition by Oi is out of the question because of opposition from Brazil's competition authority Cade.

"Telecom Italia has a market share of about 27 per cent and Oi has around 19 per cent so together they would have 46 per cent — much more than Vivo, the market leader, with 29 per cent," he said.

In spite of Telecom Italia's insistence that Tim is not for sale, the industry has been consumed by rumours for the past few months that such a break-up is imminent. BTG Pactual, the Brazilian investment bank known for its aggressive dealmaking, is expected to mastermind the deal.

BTG may be anxious to make a preliminary announcement as soon as possible to seal Tim's fate before AT&T in the US begins looking for possible takeovers in the region after closing its acquisition of DirecTV. Analysts say, however, that it will take far longer to hammer out the details of any potential deal.

Not only will bankers have to get the relevant Italians, Brazilians, Mexicans and Spaniards to agree, they will need the government's rapid approval before any of them change their mind, says XP's Mr Placido. That will be no small feat, analysts say, given that the government is fundamentally opposed to consolidation and Congress is distracted by political infighting and a corruption scandal at state-run oil company Petrobras.

"On top of this you need to get Congress to change the LGT law the [General Telecommunication Law] that cites four players," Mr Placido said.

It is something that Ms Conceição Santos does not have to worry about. Along with the rest of her "Tim/Oi family", she is blissfully unaware of the frantic dealmaking going on behind the scenes and, if analysts are right, she will be for quite some time.

Additional reporting by Daniel Thomas in London

RELATED TOPICS Mergers & Acquisitions