Multilateral Investment Fund

Project Abstract
Small Enterprise Investment Fund

I. BASIC PROJECT DATA

Title:	Investment Fund for Emerging Technology-based Companies LatinTech Inovar
Country:	Brazil
Project Number:	TC-
Beneficiary/ Executing Agency:	LatinTech Capital, a Brazilian privately-owned management company.
Estimated Cost and Financing:	MIF Facility III-a: Grant up to USD 60,000 for three independent evaluations MIF Facility III-b: Equity up to USD 4mm. This amount is contingent upon "matching" funds from private investors
Date of Project Request:	October 2001

II. BACKGROUND[1]

2.1 The level of activity in the Brazilian venture capital/private equity (VC/PE) market during 2001 showed, according to the number of transactions made, a lower activity level than in the previous year. A total of 71 deals worth USD 678mm were announced for 2001; 43 of these can be considered venture capital deals: 33 related to technology and 10 non-technology related. The average deal size fell for the third consecutive year, and, for the first time, was below USD 10mm. The activity in 2001 was restricted by several factors, such as the Argentine crisis, the local energy shortage and the impact of weaker American economy fundamentals. Despite these uncertainties, investments above USD 670mm can be considered a solid development in the Brazilian VC/PE industry.

2.2 This assessment is reinforced when removing the impacts of the privatization process of 1997-98 and the Internet fever of 1999-2001. There is a consistent growth in the number of transactions related to diversified sectors, excluding privatization and Internet. There were clear trends in terms of average size –SMEs becoming increasingly relevant as a target--, and diversification. This fact may be considered the most important achievement in the sector, to the extent that it increases the chances of some success cases to be realized/publicized in the near future. This represents an opportunity for MIF to lead investments in this segment of the market.

[1] Brasil Venture Newsletter, Nov. Dec. 2001 and Jan-Feb. 20002

2.3 Going forward, VC/PE investments are expected to increase slightly in 2002, provided that the upcoming internal political events –presidential, state governors and congress elections are scheduled for October 2002—do not affect investors' confidence. In this scenario, we can expect investments between USD 800mm and USD 1bn, transactions reaching the 100 mark and, therefore, average deal size to remain below the USD 10mm level. It is important to mention that the border between venture capital and private equity doesn't have a consistent definition, which is one of the top challenges in assessing any VC market.

2.4 This fund, if approved, may be the third one resulting from the joint collaboration of MIF and the INOVAR partners: FINEP, SEBRAE and PETROS (ref. TC-00-11-04-1Br), through its Technology Investment Facility (TIF). The TIF partners have committed to perform a joint due diligence on a number of projects they will select, focusing on the ones which are more in line with the institutions' different mandates and investment criteria. Each institution, after completing the due diligence, is free to make its individual investment decision --there is no a priori investment commitment. The fund proposals will pass through normal internal approval processes, leaving the decision-making up to each organization's Board of Directors.

2.5 This project is, therefore, consistent with the goals set at the approval time of the INOVAR program and with the MIF's goal to promote the entrance of the private sector in the region, as well as to promote the emergence of an entrepreneurial, local class of fund managers that can compete internationally.

2.6 The first meeting of the TIF partners occurred in February 2001. The project team met with the three other partners to exchange investment criteria and analytical methodologies. Eighteen prospects for investment funds were presented, and several were considered for investment. The Stratus I fund, approved by the Donors Committee at the beginning of October 2001, was the result of this first call. The second call for funds was at the end of October 2001, and three out of the thirteen proposals presented were unanimously chosen by all the TIF partners to be pursued for due diligence. LatinTech Inovar was among these (see n. 2.7).

2.7 LatinTech Capital presented LatinTech Inovar in the first Call for Proposals made by the TIF in February 2001. At that time, it was not selected among the first proposals for immediate due diligence, but wait-listed with priority for the second round of proposals. The management team presented the fund again at the second Call for Proposals, and then it was unanimously recommended for immediate due diligence by all the TIF partners. The MIF, therefore, is starting its internal approval process by presenting this fund to the POC.

III. PROJECT BENEFICIARIES

3.1 The project will benefit the financing of 10-12 small and medium-sized companies which exhibit high growth potential, and are companies newly created or in early stages of development.

3.2 Another beneficiary of the project will be the management company itself. By receiving an injection of capital to start and operate a domestic fund, the management company,

which already has a track record regarding technology investments in Brazil and Latin America but not within the context of a domestic fund, will continue building its track record in the industry and in the country.

IV. PROJECT OBJECTIVES, COMPONENTS AND ACTIVITIES

4.1 The objective of the fund is to make equity investments in 10-12 companies throughout the life of the fund. The Fund will invest in small and medium-sized companies which exhibit high growth potential, in sectors related to solution providers in software for finance and back-office tools, and software for business intelligence tools and for enhancement of business productivity. Companies newly created and in early stages are expected to comprise the whole of the portfolio. Emphasis will be placed on companies that have already adopted --or are preparing to do so in the future-- the corporate governance standards necessary to become potentially listed in the Novo Mercado. The manager will seek to have a seat in the boards of the investees. The fund does not have a geographical focus, but it is expected that most of the investment possibilities will come from the South and South East regions, although investments in companies located in other regions might be considered as well.

4.2 The investment policies of the fund will comply with IDB/MIF and local environmental guidelines. Given the nature of the sector where the fund will be investing we do not foresee significant environmental issues.

4.3 LatinTech Inovar will not invest in Internet portals, information technology consulting firms, telecom infrastructure, or e-commerce platforms and solutions.

4.4 The exits will most likely be through sale to third parties. The companies targeted by LatinTech Inovar can be attractive to potential buyers such as bigger information technology (IT) companies looking for small companies dedicated to an specific area, that can be easily integrated in their existent businesses, and acquired at a lower cost than bigger IT companies. From the beginning of the due diligence on a potential portfolio company, LatinTech Inovar investments must possess a clear exit strategy.

V. PROJECT COST, FINANCING AND EXECUTION TIME

5.1 LatinTech Capital is asking the MIF for an equity investment (Facility III-b) of up to USD 4mm. The MIF would like to request an additional grant for USD 60,000 (Facility III-a) to perform three independent evaluations during the life of the fund. The equity amount is contingent upon “matching” funds from private sector investors.

POTENTIAL INVESTORS:	$R	USD
Private Investors		
Cell phone and land line companies	5 mm	2,222,222[2]
LatinTech Partners	8 mm	3,555,555
Individual investors and pension funds	7 mm	3,111,111
Institutional Investors		
MIF	9 mm	4,000,000
FINEP	6 mm	2,666,666
Other	5 mm	2,222,222
TOTAL (approx.)	40 mm	17,777,776

5.2 The fund will be constituted as a "*Fundo Emergente*" regulated by the CVM n. 209 and CVM n.302, a new regulation that modifies some of the requirements found in the CVM n. 209 for this type of funds. With respect to its funding, LatinTech partners are committed to invest up to 20% total size of the fund, although they think they will get enough money from other sources to reduce this percentage considerably.

5.3 The proposed terms of the fund are the following:

Size of the Fund:
R$ 40mm (approx. USD 17.7mm). Goal is R$ 50mm

Life of the Fund:
7 years, with one possible extension for two more years.

Investment Period:
Maximum of three and a half years.

Fund Investments Size:
Initial investments in the range of R$ 1mm to R$ 3mm (USD 444,444 up to USD 1.3mm) with an additional 30% reserve for refinancing rounds up to R$ 5mm (USD 2.2mm) for investment in a single company. In most of the cases, the fund will take stakes in the investee companies ranging from 15-35%.

Operating/Administrative Costs:
Management fee: 1.75% per annum based on committed capital, during the investment period, and afterwards, same 1.75% but based on invested capital (net assets of the Fund). Carried interest: 20% of the Fund's capital gain, being capital gain the distributed amount over preferred return exceeding inflation index (IGPM) plus 6% per annum.

Distribution Cascade
The fund will distribute 20% of the profits to the manager after having distributed 100% of the initial invested capital, adjusted for inflation plus an annual, cumulative preferred rate of return of 6% to investors.

[2] Exchange rate in this document is USD 1/R$ 2.25

VI. EXECUTING AGENCY

6.1 LatinTech Capital Ltda., headquartered in Rio de Janeiro, will manage the fund. The company was formed in 1998, but underwent different re-organizational stages until acquiring its definitive structure. LatinTech Capital started as a private corporation, changed to a public-held company in 2000, and to a limited liability company, adopting the name of LatinTech Capital Ltda. in June 2001. A year earlier, LatinTech Panamerican Inc. is formed as the investment vehicle for companies outside Brazil.

6.2 From June 1998 to August 1999, the company was not operational. In September 1999, in response to investment opportunities identified during this period by Mr. Christopher Meyn –who was working at the time as Director of Globalvest—and by professionals from Latinvest Asset Management, --both shareholders of LatinTech Capital--, the company raised its first round of capitalization in the amount of USD 29mm obtained alongside foreign investors, creating Latinvest Technology Fund I (LTFI). Later on, in March 2000, the fund was reorganized into a limited liability partnership adopting the name of LatinTech Capital Inc. Some of LatinTech Capital Inc.'s main shareholders are: GE Capital Equity Investments; CSFB Bahamas Ltd., Pactual Overseas Bank Ltd., Safra National Bank, Peter Gruber Charitable #1, Globalvest Investment Fund, and Darval Investments. John Templeton, George Soros, and Boston University Endowment Fund are minority shareholders.

6.3 LatinTech made its first investment in October 1999, and by the end of December 1999, USD 22.4mm had been already invested or committed, a 77% of the fund's capital at that point. In March 2000 there was a second round of financing that resulted in an additional USD 23mm from foreign investors, totaling USD 52mm in resources secured by LatinTech to date. To date, LatinTech's portfolio comprises 10 active companies and three exits (See Annex II). The portfolio has a mix of PE and VC deals. LatinTech's vision is to become a leader and source of reference for the market, in VC/PE in technology companies in Brazil and Latin America.

6.4 Globalvest and its related parties are the main shareholders of LatinTech. Globalvest is an asset management company started by Mr. Peter Gruber in 1989 with his own wealth –mainly realized through the buying and selling of shares in the Latin American market in the seventies--. Globalvest created other financing vehicles as well: Latinvest Fund, in 1991, with a focus on emerging markets; and Latinvest Asset Management LTDA. in 1994. In 1998 Latinvest starts managing third parties funds and funds of fixed and variable income. Two of its funds, Netuno and Jupiter, were given awards by *Revista Exame*. Globalvest and Latinvest together manage USD 0.9bn in third parties and their own money today. In Brazil, they manage R$ 225mm (USD 100mm).

6.5 The LatinTech Capital team has previous experience in managing VC/PE funds in Brazil and abroad. The key executives in the team have relevant experience, as indicated below:

- *Christopher Meyn*, Director, Executive Vice President and CEO, has been exclusively dedicated to LatinTech Capital since its beginnings, developing its deal flow, investment strategy, and strategic partnerships. He will be the person responsible for the Fund. Prior to this, he was director of Investments in Globalvest/Latinvest/Private Equity, in charge of business origination, execution

and portfolio administration, especially the telecom and infrastructure deals. Previously, he worked as Vice President of Dick Clark International Cable Ventures, specializing on mergers and acquisitions (M&A), as Vice President of Marks Group (a telecom holding company), and in the area of communications and media in Morgan Stanley Dean Witter;

- *Luiz H. Fraga*, Director and Executive President of LatinTech Capital, has ample experience in trading, corporate finance, capital markets, financial analysis and private equity investments. In 1994 he founded Latinvest Asset Management. Since then, he has been in charge of all PE activities in Latinvest, including cable TV and telecom investments. Prior to this, he worked in Bear Sterns & Co, Inc., as Emerging Markets Director (1989-1994), in Unibanco New York Branch as Director (1986-1989), in Citibank Rio de Janeiro in the Corporate Banking Division (1981-1984);
- *Eduardo Soares*, LatinTech Capital's Director, was dedicated exclusively to external audit work in Coopers & Lybrand and Arthur Andersen for 16 years. He has significant expertise in US GAAP standards and leading due diligence processes for technology-based companies;
- *Mariana Ribeiro*, Senior Investment Analyst at LatinTech Capital, has been working at the company since its foundation. Prior to that, she worked as investment analyst in Latinvest Asset Management.

6.6 LatinTech Inovar will be supported by: i) LatinTech Capital as its general partner and management company; ii) Latinvest as the portfolio's manager; iii) DreyfusBrascan, Bank of Boston or Banco Itau as the custodian-treasurer of the fund's reserves (decision on which of these three is still pending); iv) PriceWaterHouse Coopers as the fund's auditors; and iv) Vieira, Resende, Barbosa e Guerreiro Advogados as legal counsel for the fund.

6.7 The governance structure will be composed of a General Assembly (which replaces the usual Board of Directors structure used in other countries), and an Investment Committee, composed by the management company (two seats) and some of the investors (two seats for INOVAR investors), and one independent member, with proven knowledge of the industry and VC/PE, chosen by consensus between LatinTech and INOVAR. The decisions will be taken by simple majority. Each member will have a two-year term that could be renewed. MIF most likely will take an observer position in this committee, but preserving its right to become an active member in the future.

6.8 The TIF's members preliminary evaluation of LatinTech's proposal revealed the following:

Strengths	Weaknesses
Transparency and flexibility in their approach to potential investors	Lack of experience managing fundos emergentes (domestic funds ruled by CVM n. 209)
Good reputation in the market	
Experience in the whole VC cycle, track record with 13 investments made and 3 successful exits (See Annex II)	
Team wholly dedicated to VC	

Realistic vision of the market	
Excellent network	
Team has excellent qualifications and technological knowledge	
Management company committed to invest in the fund	
Sectors that are priority for investment in the fund are aligned with team's expertise	
Good relationship with entrepreneurs	
Good managerial skills during Internet crisis	

VII. EXPECTED PROJECT RESULTS AND JUSTIFICATION

7.1. The project's expected results are: i) to help in the consolidation of the venture capital industry in the country, by making SMEs financing attractive to private sector investors, local and international. For this, it is expected that the fund will obtain financial returns aligned with those in the industry in other countries; ii) to help SMEs attain profitable goals in their operations; and iii) to help SMEs conform to environmental and managerial standards that will make them more competitive in the domestic and international market.

7.2. The venture capital industry in Brazil is still in a developmental stage, in spite of being more advanced than in other countries in the region. In this process, the consolidation of a critic mass of fund managers is of utmost importance, to advance the discussion of certain aspects of the current regulation and market practices, and to assess what changes are needed in these areas. The INOVAR program has been so far a key element in this process. More than ten fund managers established their operations last year, in response to the TIF's Calls for Proposals.

7.3. The MIF not only adds credibility to the process, but also continues to play a catalytic role in attracting private sector money. The seal of approval it bestows upon the funds it invests in allows them to leverage funds from pension funds and other private investors, including individuals and international investors.

VIII. MAJOR ISSUES

8.1 Pre-operational Expenses: They need to be defined.

8.2 Technology Expertise. FINEP will conduct a special due diligence on the technological aspects of the companies in the pipeline, to assess LatinTech's capacity in the field.

8.3 Conflict of Interests. A clause to deal with potential conflict of interests will be negotiated by the team, since LatinTech Capital could potentially invest up to 20% of the fund's size. The team will negotiate which issues will be voted in the general Assembly without LatinTech's participation, --i.e., performance of the fund manager, its replacement, etc.--.

IX. ESTIMATED PROJECT PREPARATION AND ANALYSIS TIME

9.1 The timetable for decision-making is estimated as follows:

MIF Programming Committee	April 2002
Presentation to IIC Expanded Operations Committee	May 10th 2002
Donors Committee	June 19th or July 24th, 2002

Prepared by: Susana Garcia-Robles
Approved by: Sandra Darville
Date: 5/1/02

Annex I- LatinTech Inovar's Prospective Pipeline

Solution Provider Company with focus on Customer Relationship Management.
The company has developed a software with specific functionalities like call center, business intelligence, and sales automation among other features. The target market for this software is the big and medium-sized companies. The company has 50 employees and a clientele of 100. Potential investment ranges between R$ 2-4mm (USD 888,888-1,777,777).

Solution Provider Company with focus on Partner Relationship Management.
The company has developed its own software, targeted at big and medium-sized companies. The company has won several prizes, even in the US market, due to the quality of the software developed. Mc Donald's Brazil is one of its clients. Potential investment is on the range of R$ 4mm (USD 1,777,777).

Application Service Provider.
The company developed an Internet solution for marketing one-to-one and for supporting online clients. The latest version allows an operator in a call center work alongside with a website technician, helping the same client simultaneously. The company counts among its clients the largest e-commerce and financial institutions websites. Potential investment, which will be used for international expansion, ranges in the R$ 4mm (USD 1,777,777).

Software Developer Company with focus on Data mining products.
The company develops tools for market analysis via data mining. This software analyzes the results of marketing campaigns and special sales promotions, in a record time. The company has developed customized versions of the software for an extensive list of companies, including Coca-Cola, which aims at using this product in its branches in Latin America. The company needs a potential investment in the range of R$ 3-4mm (USD 1,333,333-1,777,777) to develop a new version of the product, and to expand its commercial department and develop new partnerships.

Interactive Software Developer.
The company develops software that allows an interactive communication between different cellular platforms in the market, hardly ever using the phone lines. This technology has been used since last year in the US market. The company is developing the first pilot products for the Brazilian market, and counts already with TIM and Telefonia Celular as clients. The potential investment is of R$ 3mm (USD 1,333,333), and it will be used for the expansion of the company's commercial department and the development of new partnerships in the Latin American market.

Company focused on infrastructure support for Internet Data Centers.
The company develops, installs and supports complex infrastructures in third parties Internet Data Centers, in companies located in Latin America and the US, using the Application Service Provider sales model. The company counts with clients in the US and Brazil, and they pay a monthly fee for the management of their Internet infrastructure. Potential investment ranges from USD 500,000 up to USD 3mm, depending on the speed of the company's expansion to new Latin American markets.

Annex II. Estimated ROI on LatinTech Capital's Portfolio.