Speaker 1 (00:00):

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Arnaldo Rego (00:17):

And I think what you mentioned, the sustainability aspect of that is very interesting because we have seen, I think, some of the pushback we've seen with, for example, the electric car industry and battery-powered vehicles and alternative energy. The biggest, I think, argument, push back against those types of technologies becoming more of the norm is the sustainability of a lot of how these products are mined and then what it creates. Technology to help improve that would be very important.

Ivan Vera (00:52):

We are working towards a green copper and green nitrogen and green whatever because there is a huge opportunity because of the huge problem we have in climate change. That's reality. Climate change is reality.

Oscar Stephens (01:12):

So Ivan, you touched briefly on artificial intelligence, but outside artificial intelligence, FinTech, where do you see the opportunities? Where do you see there room for innovation, perhaps agriculture, things that deal with, for example, water, products on desalination or water purification? And I think as a follow-up to that, do you see right now that there's going to be still room for innovation and new companies coming out? Or do you think there's going to be a consolidation of the market when some of the larger companies are going to start acquiring the IP or the companies themselves that produce a new technology?

Ivan Vera (02:02):

Oscar, you know that VC investors are experts on selecting in which kind of technology and company invest. And then we are experts on how to support and properly help the founders to increase the value of their company. And then we are experts on getting exits from our investment and having a multiple of invested capital from 10 or 20 times the invested capital. So I see that in the US you have a wonderful technology ecosystems and Google have acquired some 150 companies. This is a perfect exit for the investors, for early investors and late investors, fantastic. But in Chile we don't have. You know that the VC industry in the US is exactly the same age as me because it was born in 1957. So your industry is 65 years old. Ours is 10 years old, as my granddaughter, my granddaughter, Dominga.

(03:25):

So we don't have technology titans acquiring those startups and having wonderful exits for our investors. But we have industries with large companies doing fantastic performance, but they are in danger of not surviving because of sustainability, because of productivity and so on. So I think you, Oscar, somehow you mentioned it. These companies, these big mining companies will acquire startups in not more than five years from now. So when our industry is 15 years old, we will have the maturity that we need to have a string of exits and getting money back to the investors and increasing the industry, because without exits, the industry won't increase, won't grow.

(04:36):

So I can give you an example. SQM. SQM is a fantastic company in Chile that is the number two in lithium in the world. It's a 12 billion revenue company with five billions in EBITDA. That's fantastic for a 12 billion revenue company. But they don't produce only lithium. They also produce nitrates and fertilizers. So I introduced to the VP of the fertilizers production vice presidency, I introduced them a startup that is agriculture, big data processing startup that helps farmers to reduce in 30%, 30% the use of water increasing 10% the yield in tons per hectare, but SQM is expert on fertigation. So delivering the fertilizer through the irrigation.

(06:04):

So I said this is a perfect match now because you can develop in SQM a chemical company, a digital big data business model, and if the pilot projects really are successful, bingo, you will have a digital arm to compete with another fertilizers producing companies. So they put money into that startup and they are right now having pilots in Chile and Mexico. But SQM is in 110 countries in the world. So if that pilot works, and you can bet that it will work, they will have a secret weapon to compete all over the world. You see? And then they will say, "Ah, I will acquire this startup because this gives us exclusivity on this technology." And exactly what the technology titans like Intel do, acquire the technology, acquire the customers, acquire the, it's a acqui-hiring. They acquire even the culture of the startup. And this beginning to happen in Chile.

Arnaldo Rego (07:39):

I've seen something similar to what Ivan mentioned. This was back in a transaction we did back in, I think it was at the end of 2021, where we had an Argentine payment processing company being acquired by a larger Brazilian payment processing company. Both of which were, I mean, the Argentine company was like mid-stage. The Brazilian company was kind of late stage, kind of getting prepped for potentially, I mean, I don't know because we were not representing them, but I think for potentially maybe an IPO push or something like that. And it was an acquisition within Latin America and it was an exit event for one fund that had invested in the Argentine company, and it was a roll-up event in order to prep to leverage itself to potentially IPO for the Brazilian company.

(08:42):

So I think that's very interesting because before I would think a lot of the acquisitions done were from foreign companies acquiring companies within Latin America. Now I think that the market within Latin America to consolidate and acquire and provide exits within the country itself, not having to depend on a international company in order to have an exit event is very good and will help develop the venture capital ecosystem within the countries in Latin America, I think a lot quicker.

Ivan Vera (09:19):

And some extraordinary innovations are being created in Chile and Argentina, in Peru, in Colombia. So I'm very optimistic of what large traditional companies are beginning to explore and beginning to notice in this new technology landscape of Latin America. And those large traditional companies are huge, have huge, deep pockets to invest in startups, and they are beginning to notice the opportunity.

Oscar Stephens (10:05):

So, Arnaldo, to wrap it up on the legal side now, are you seeing any trends and developments on legal technology on many of these investments? Tighter terms and conditions, different exit events, additional protections? Are you seeing any difference now than let's say couple of years ago?

Arnaldo Rego (10:31):

Definitely a lot of difference. And it's all related to what we've been speaking about, which is different market conditions, cost of financing, cost of funding. That has kind of shifted the balance from investments being much more issuer-friendly to now being much more investor-friendly as investors have been starting to get much more aggressive because there's less certainty that they had a few years ago with the potential of an exit event given the VC winter, as Ivan put it, that we are in right now. I mean, generally, as I mentioned before, transactions are still getting done. However, the investors I've seen are much more cautious with regards to the transactions overall. And they've been taking longer to do. A transaction that will normally take two, three months are taking four, five, six months even.

(11:28):

And in my experience, it's not only in the legal phase but also in the due diligence phase. Meaning I think business diligence itself before we even get to the LOI stage, letter of intent stage, has been taking longer due to the increased cost of capital, and not being a pro IPO environment, and the decrease that we've seen in M&A activity as well. The investors are being much more cautious even though they overall do have quite a bit of dry powder still to spend.

(12:06):

Transactions, not just in the diligence phase but also during the negotiation phase actually once you start preparing agreements and things like that, have also started to take longer. Like I mentioned, the conditions from 2020 to 2022 were much more issuer-friendly. Now investors will be much more aggressive, and that has caused the transactions to take longer to complete. I believe the decrease in potential IPO exit opportunities and also M&A exit opportunities in the near term have lowered valuations and significantly contributed to this.

(12:45):

What I have seen specifically are investors negotiating more forced exit provisions in agreement such as having IPO covenants, which essentially obligate the company to go public or work towards an IPO and go public within a certain timeframe. And I've also seen the inclusion of redemption provisions allowing investors to redeem at a premium following a time horizon, usually around five years. So the investors are now building in mechanisms so they can force an exit event as opposed to before where they just weren't doing it and were trying to get as many deals done as possible given the environment. And I've also seen as far as on the return side, them being much more aggressive in negotiating preferred returns, and some of which have been uncapped or with very high caps. So that's generally what I've been seeing be changes from even as early as Q3, Q4 of 2022 till Q1, Q2 now. I mean, this has happened very quickly, the shift from terms being much more issue-friendly to investor-friendly.

Ivan Vera (14:06):

But you that I find that this is very healthy because we need our investors to get their money back multiplied by 10 or 20 and we don't have 20 years to make that happen. At least in Chile, we don't have that time. So I guess, five, six years it's okay, but not 20 years. So imagining and translating that conditions for exits in our term sheets, it's very healthy.

Arnaldo Rego (14:46):

Well, I know my fund clients would be very happy to hear that and agree with you a hundred percent.

Ivan Vera (14:53):

Yeah, we are doing that, Arnaldo, and we say I don't care if the other 50 funds in Chile don't do that. I don't care. I just don't care. I am caring about my investors and also my founders, and also my founders. I will help them.

Arnaldo Rego (15:16):

No, yeah, I mean, that's exactly what I've been seeing too. When you're negotiating, sometimes the target, they'll be worried, but if you have an axe dangling over your head and saying, "Look, within five years we can exercise this," I mean, in practice we know that if you get close to that, things have been developing well, can we negotiate terms and be more flexible? I mean, that's how usually these things go. But if you're really close, then they'll give you some more leeway. But I think it helps to really motivate.

Ivan Vera (15:57):

You know which percentage of the startups that have been negotiating with us didn't accept the new terms? 20%. 80% accepted the new terms because they are reasonable. It was not the norm. I don't care. We are inventing the new norm.

Arnaldo Rego (16:25):

Yeah, I agree. I mean, it wasn't the norm from 2020 till mid 2022. I mean, I agree. It clearly wasn't the norm. But conditions change. Things change, and you have to adapt. If not, what's the alternative? You're not going to get the funding you need to help you grow and accelerate, and all the work you've put in might get stalled and you might get left behind. So I agree a hundred percent.

Oscar Stephens (16:54):

Well, thank you, Ivan, and thank you, Arnaldo. With this we conclude our podcast. Thank you, everybody, for listening and see you next time.

Ivan Vera (17:06):

Thank you, Oscar. Thank you, Arnaldo. Glad to meet you.

Arnaldo Rego (17:08):

Oh, it was a pleasure. Thank you.