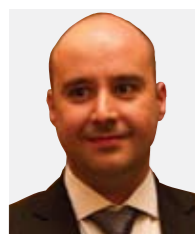


FOCUS ON

ACCESSING THE BRAZIL MARKET

Brazil illustrates how, in the long run, a fully regulated environment can prove to be beneficial for the funds industry. This is especially true for hedge fund managers, for whom Brazil's environment provides security, independence and a level playing field in which to operate



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For foreign investors attracted to the emerging global success of Brazil, the country's market environment is often regarded as one of the world's most complex, particularly for alternative fund managers. And in truth, there are a number of good reasons for such an assessment.

Since the 1990s, the Brazilian economy has experienced a series of changes that have substantially enhanced financial flows both into and out of the country, supported by regulatory improvements that have increased accessibility to the capital markets. However, it is important to understand these developments against the background of Brazil's consistent regulatory environment. The country has multiple regulatory bodies governing registration of all fund market participants and reporting requirements with associated daily processes (see table for a brief description of each entity).

First, the steps around registration requirements pose an initial cost to asset managers. All financial institutions in Brazil, from a single individual distributor to a large institutional custodian, must be registered.¹ In addition, the Brazilian market mandates additional reporting above and beyond the threshold that investors from other markets may not be accustomed to. For example, investors benefit from daily net asset value (NAV) calculations for all funds (including long-term private equity funds), as well as daily monitoring of all trades and respective compliance rules.

BRAZIL'S ENVIRONMENT: EXCESSIVELY CHALLENGING OR A MODEL ENVIRONMENT?

While some might argue that such an investment environment is excessively demanding, the overall trend in world markets towards a culture of increased regulation and disclosure contradicts this point of view. One illustration of this sobering reality is the fact that, in the wake of the 2009 conviction of Bernie Madoff, the self-regulatory nature of the global funds industry has been challenged.

HISTORICALLY HEALTHY INFLOWS

One ironic effect of this trend has been that Brazil has become a global model of how overall intelligent guidance and regulation does not necessarily limit business opportunities. On the contrary, the country's

domestic funds industry has grown consistently during the past 20 years. All of this has evolved reasonably smoothly.

Throughout the years, there has been a healthy inflow of investment into the Brazilian market. The country is quite open to foreign investment in its capital markets, and foreign investors enjoy an established environment in which to oversee portfolios.

RECENT REFORM IN REGULATING OUTFLOWS

In contrast, outflows have been more of a challenge. Today, however, sophisticated Brazilian investors can obtain exposure to non-Brazilian assets by using local feeder funds (though not yet through local Exchange Traded Funds).

While investors' ability to invest offshore has opened up, Brazil's regulators remain vigilant and have instituted significant precautions to protect the final investor. The local custodian is responsible for ensuring that all the positions are reconciled on a daily basis. This includes a daily substantiation process for any assets with offshore custodians.

With the still-high interest rates on local public bonds, outflows from Brazil have not yet demonstrated strong growth. This is also due to cultural practices, as Brazilian managers and investors still tend to view offshore investing as venturing into uncharted waters.

Nevertheless, for offshore alternative fund managers interested in Brazilian investors, the current timing is quite good. For example, private banking in Brazil has never been so vigorous, and high-net-worth individuals' interest in new products and partnerships is an important trend in this market. In addition, on the retail side, big local banks are offering funds with offshore exposure as part of their menu of typical investment products.

“SINCE THE 1990S, THE BRAZILIAN ECONOMY HAS EXPERIENCED A SERIES OF CHANGES THAT HAVE SUBSTANTIALLY ENHANCED FINANCIAL FLOWS BOTH INTO AND OUT OF THE COUNTRY”

CONCLUSION – THE BRAZILIAN OPPORTUNITY

From the point of view of a European or US-based asset manager, some new opportunities are now available. Together with the country's positive economic trends, this change has definitively upgraded Brazil's position on many asset manager CEO's list of next places to set up an office.

Today, US and European markets alike are struggling to understand and absorb the significance of new regulatory initiatives such as Dodd-Frank and Alternative Investment Fund Managers Directive (AIFMD). While some see these as a constraint on the industry, others point out that

“BRAZIL HAS BECOME A GLOBAL MODEL OF HOW OVERALL INTELLIGENT REGULATION DOES NOT NECESSARILY LIMIT BUSINESS OPPORTUNITIES”

the ultimate impact of new regulatory initiatives on these developed markets is unknown.

In contrast, Brazil's well-established environment has always been a part of the country's investment market and culture. In fact, in recent years – including the credit crunch – it has come to be regarded as quite beneficial to the financial industry.

Together with these outflow windows for funds, a whole new field of possibilities has opened up in Brazil, in the process shifting the market's overall complexity to a higher level. Combined with the country's significant and sustained upward economic trends, investing in the financial markets in Brazil has become an attractive proposition.

ABOUT J.P. MORGAN

With a presence in Brazil for more than 50 years, J.P. Morgan offers services across the Investment Bank, Global Corporate Bank, Asset Management, Private Banking and Treasury & Securities Services. The firm has a strong local presence, with offices in São Paulo, Rio de Janeiro, Porto Alegre, Curitiba and Belo Horizonte. Clients benefit from the firm's global expertise and strength across Latin America. Since September 2011, J.P. Morgan's global custody clients with interests in Brazil have used J.P. Morgan as custodian. ■

¹ Registration of a fund's market participants in Brazil requires compliance with all documentation and authorisation requirements with the CVM and Anbima (self-regulatory entity), apart from other specific regulatory bodies. Initial registration usually requires an audit report stating the current and planned state of the provider's systems, process and staff structure. Similarly, all funds also require registration, and the disclosure and documents requirements depend on the type of fund, target investors and distribution (public or restricted).

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AUTHORITIES	COMPETENCIES/FUNCTIONS
National Monetary Council (CMN)	CMN comprises the finance minister, the planning and budget minister, and the Central Bank governor. It was created with the specific purpose of formulating monetary and credit policies for the financial and capital markets. CMN policies address matters such as the availability of credit, payment for credit transactions, operating limits for financial institutions, and the rules governing foreign investment and foreign exchange in Brazil.
Central Bank of Brazil (BACEN)	The Central Bank is a federal agency attached to the finance ministry and is responsible for implementing the monetary and credit policies established by CMN, regulating the foreign exchange market and capital flows, authorising new financial institutions, supervising existing institutions, and overseeing the operations of public- and private-sector financial institutions, including the power to apply penalties. The governor of the Central Bank is appointed by the president of Brazil, subject to confirmation by the Federal Senate, for an indefinite term of office.
Brazilian Securities and Exchange Commission (CVM)	CVM is a federal agency attached to the finance ministry and is responsible for regulating and overseeing the Brazilian capital markets. Financial institutions and other institutions authorised to operate by the Central Bank are also subject to regulation by CVM when conducting business in the capital markets. One of CVM's key responsibilities is to oversee the activities of publicly held companies, organised over-the-counter (OTC) markets, exchange markets, and commodities and future markets, as well as members of the securities distribution system, such as fund managers and asset managers. CVM characterises a market as an organised exchange or organised OTC market, depending primarily on the pricing rules adopted for trading platforms or systems, the volume traded, and the type of investor targeted. BM&FBOVESPA falls under the organised exchange category.
BM&F BM&FBOVESPA (Brazilian Mercantile and Futures Exchange and São Paulo Stock Exchange)	The company develops, implements and provides systems for the trading of equities, derivatives, fixed income securities, federal government securities, financial derivatives, spot foreign exchange and agricultural commodities. It has a settlement bank and four clearinghouses for the registration, clearing and settlement of transactions carried out on its trading systems. It also acts as a central securities depository, and licenses software and stock indices. The company further manages social investments with focus on developing the communities with which it interacts.
Brazilian Financial and Capital Markets Association (ANBIMA)	Representing more than 340 institutions including commercial, multiple and investment banks, asset managers, brokerage houses, securities distributors and investment consultants. Helping Brazilian public institutions to regulate the activities of the financial and capital markets agents. Providing research and statistics about financial and capital markets.