IN THIS WEEK'S ISSUE...

Joanne Harris, special reports and Europe editor

Region: Portugal
Portugal has had a rough ride through the financial crisis. The P in the so-called 'PIGS' countries (Portugal, Italy, Greece and Spain), it has suffered from a severe recession and its sovereign debt has been downgraded. All bad news for the country's lawyers. Dealflow is sluggish, although a spate of big deals made 2010 better than it could have been. In place of M&A transactions there has been an increase in compliance and regulatory work as companies seek reassurance about their investments. Portuguese lawyers have also been looking outside the country for opportunities. They see Africa, Brazil and China as likely jurisdictions. Several firms have opened offices or established relationships outside Portugal in the past 12 months and more overseas ventures are likely in the next year. This week's Special Report speaks to Portugal's lawyers to gauge their feelings on the market and whether they think it will improve.

Practice area: Insolvency
Sovereign debt is under the microscope in the second of this week's Special Reports, which examines the potential effect of the crisis on businesses, finding that the chances of the recession continuing to create 'zombie companies' is high, particularly in the banking sector.

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On the brink

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Portugal has been a market in turmoil over the past year, with the necessity of a bailout from the EU hanging over its head. James Swift looks at how the legal market is faring

Linklaters' decision to axe six associates from its Lisbon office in May 2010, amid tumbling transaction levels and a frozen projects pipeline, was an ominous bellwether for Portugal's legal market.

In the grand scheme of things making six associates redundant might not seem like a drastic course of action, especially given the number of redundancies made at some UK and US firms. But the move went against the culture of law firms in Portugal, and it was not a decision that Linklaters took lightly (see box, page 26). News of the cuts came as a surprise, but was met with understanding by domestic lawyers at the time. Partners at Portuguese firms could see why Linklaters had made the decision, but remained optimistic about the market.

> "Every day the crisis is in the newspapers. One day it's good news, the next it's bad news"
> Manuel Santos Vítor, PLMJ

But now, with Portugal having passed its toughest-ever budget in a bid to convince investors that it will not be the next victim of Europe's sovereign debt crisis and work for lawyers at a painful low, Linklaters' decision seems regrettably prescient. Few now believe that simply riding out the crisis is an option for most firms.

Greece and Ireland both succumbed to Europe's sovereign debt crisis in 2010, requiring multibillion-euro bailouts from the EU and the International Monetary fund (IMF). For some time now Portugal

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has been tipped by investors as the next to fall.

There is no doubt that Portugal is in a bad way. On 17 December the yield on the country's 10-year bonds rose to 6.4 per cent, while in Germany sovereign bonds were yielding less than 3 per cent. Anecdotal evidence from within the country is just as gloomy.

"In restaurants at night you really notice the crisis," says one partner. "People aren't going out to dinner like they used to."

> **"We had to spend money to help the banks and we also had to spend a lot on social programmes. But Portugal never was very good at managing its budget – the state spends too much"**
> Luís Branco, MLGTS

Some are even painting Portugal's decline as a foregone conclusion. "The country's going to be bailed out early in 2011, by March at the latest," predicted Alastair Newton, senior political analyst at Nomura International, during an interview in Milan in December. However, at the time of writing there has been no concrete indication one way or the other.

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"Every day the crisis is in the newspapers," says PLMJ co-managing partner Manuel Santos Vítor. "One day it's good news, the next it's bad news. [In December] people were expecting the IMF to come in with a bailout any day. They haven't showed up yet, but that doesn't mean that they won't."

Slow going

While Greece was felled by its high public debt and Ireland by its fragile banks, the fears surrounding Portugal are driven by the country's slow growth rate and high level of private debt. Portugal must repay or refinance around €20bn (£17bn) by mid-2011 to avoid collapse.

"As a consequence of what happened in 2008 and 2009 with the financial crisis, we have an unbalanced budget," says Luís Branco, head of banking and finance at Morais Leitão Galvão Teles Soares da Silva & Associados (MLGTS). "First of all we had to spend money to help the banks raise money, and we also had to spend a lot on social programmes because a lot of people were losing their jobs as a result of the financial crisis. I should add that Portugal never was very good at managing its budget – the state spends too much."

Indeed, it would not be unfair to suggest that Portugal has been an economic underperformer for a long time. Since it joined the European Economic Community (now the EU) in 1986, Portugal has had the slowest real GDP growth of any country in Europe.

It was the first country to be threatened with sanctions after breaking the European Commission's stability pact on budget deficits. Rising labour costs have made the country uncompetitive compared with emerging markets, which have now overtaken Portugal in exports.

Media reports have even stated that EU member states are pressuring Portugal to take an EU/IMF bailout in a bid to save the euro. The risk is that, if Portugal needs a bailout, eurozone debt contagion will spread to Spain, which is heavily exposed to Portugal's debt. Some fear that Spain is too big to be bailed out, even with the support of the €635bn fund set up by EU leaders in December 2010.

Budget or fudge it?

Throughout all this, the Portuguese government has denied strenuously that it needs financial assistance. Of course so did Ireland's government right up until it accepted a £72bn rescue package in November. Nevertheless, Portuguese prime minister José Sócrates is confident that his government has taken sufficient steps to avoid a crash.

"Portugal's in the front line of countries that are consolidating their budgets rapidly," said Sócrates in an interview in November. "Debt, after 2013, will start to drop."

Certainly, Portugal's austerity budget was severe. It aims to cut the country's deficit to 4.6 per cent of GDP next year from its present 7.3 per cent and includes a raft of money-saving measures, including cutting public sector wages.

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▶ LINKLATERS' LAYOFFS: A SIGN OF THINGS TO COME?

For a relatively small market Portugal has seen a lot of change in the past 12 months, with a spate of mergers, restructurings and withdrawals.

The difficult economy was responsible for **Linklaters**' decision to make six associates redundant in May 2010. The move was driven by the firm's Portuguese office rather than its central management.

It was seen by the market as an indication that not everybody would survive the recession. The redundancies were the first and, to date, remain the only ones to be made public, although many Portuguese firms are more reticent about such things than their Anglo-Saxon counterparts.

Meanwhile, other international firms have been reconsidering their presence in Portugal. Linklaters remains the only UK firm with an office of its own in the country after **Simmons & Simmons** pulled out in 2009.

DLA Piper has reconsidered its strategy in Portugal. It announced in September 2010 that it would end its six-year non-exclusive arrangement with local firm **Miranda Correia Amendoeira & Associados** (MCA) at the end of November.

The firm is looking for an exclusive partnership with a Portuguese firm in the interests of improving the profitability of the relationship.

The 1 November 2010 edition of *The Lawyer* reported that DLA Piper was in talks with **Azevedo Neves Benjamim Mendes Carvalho & Associados Sociedade de Advogados** (ABBC).

The talks concluded this month with the signing of an exclusive referral relationship between DLA Piper and ABBC.

Last year also saw some consolidation among local firms. Simmons' former partner **SRS Advogados** merged with litigation boutique Soares **Machado & Associados** in September.

SRS partner Octávio Castelo Paulo said the firm had identified areas where it wanted to grow after splitting from Simmons.

"The first area was litigation, and we're open to other small mergers like this one," he told *The Lawyer* at the time of the merger (*The Lawyer*, 4 August 2010). Although SRS's partnership with Simmons broke down, the two firms maintain a referral relationship.

Iberian giant **Uría Menéndez** also expanded in Portugal in 2010, bolting on two-partner firm **Proença de Carvalho & Associados**.

Name partner Daniel Proença de Carvalho became the firm's local chairman, although managing partner Duarte Garin remained in his role.

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▶ GOING GLOBAL

Portuguese law firms are becoming increasingly international in an effort to diversify away from local work. Many of the favoured locations are ones in which it is difficult or even impossible for a foreign firm to set up its own office. In others the existence of established firms can often make it easier to set up a referral relationship.

Portuguese lawyers agree that the major jurisdictions in which to seek an international presence are Brazil and lusophone (Portuguese-speaking) Africa, predominantly Mozambique and Angola. The historic, cultural and linguistic ties between the countries makes cross-investment natural and law firms are seeking to make the most of this.

Raposo Bernado partner Joana Andrade Correira says the firm is looking to expand its network of offices into Brazil. It currently has offices in Spain, Romania, Poland and African countries Angola, Cape Verde, Guinea-Bissau, Mozambique and São Tomé. But its Latin American needs are handled through referral relationships with local firms.

Andrade Correira says the move is driven by an increasing amount of investment by Brazilian companies in Portugal and vice-versa.

Viera de Almeida partner Pedro Cassiano Santos also agrees that Brazil is a jurisdiction Portuguese businesses should be keeping a close eye on. "Brazil's a powerhouse," he says.

He adds that Viera de Almeida is happy with its referral relationship in Brazil with local firm Pinheiro Neto Advogados, but confirms that "our strategy is to intensify this relationship".

Viera de Almeida has a similar relationship in Mozambique with Furtado Bhikha Loforte Popat & Associados.

The partnership involves a Viera de Almeida partner based in Mozambique, although at present foreign lawyers are not allowed to practise Mozambique law. The relationship has helped the firm win work on a number of Portugal-Mozambique deals.

According to Cassiano Santos, Angola could well be the next hotspot in Africa for Portuguese companies seeking investment opportunities. Sérvulo & Associados partner Paulo Câmara agrees, noting: "What we see is a significant increase in Portuguese companies going to Angola and looking for law firms they know to help them."

Another trend last year was for Portuguese law firms to look even further afield – to Asia. PLMJ, CCA Avogados and Morais Leitão Galvão Teles Soares da Silva & Associados have all made inroads into the region. PLMJ tied up with Chinese firm Dacheng Law Offices in October and Morais Leitão signed a partnership in Macau with MdME in November.

CCA's decision to open an office in Shanghai was a first for Portugal, although many other European firms already have offices in China. Given the jurisdiction's significance and probable continued prominence, CCA is unlikely to be the last Portuguese firm to make a foray into one of China's big cities.

However and wherever international expansion happens, Câmara is certain it is now a fact of life for Portuguese firms and something more of them will be doing in the future.

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"In 30 years of being a lawyer I've never seen such a budget of such measures," says Branco. "No public officer would have thought that they would see their salary cut."

Raw deals

Few would have guessed that Portugal's year would end on such a low. The country began 2010 relatively strongly, say lawyers. There was promising dealflow and the banks looked to be in good shape. But the sovereign debt crisis soon made its mark on the legal market. Combined with austerity measures put in place by the government it caused financing to disappear, dealflow to dry up and projects to be put on hold.

"Everything's been marked with the effects of the sovereign debt crisis," says Santos Vítor. "Even if we started 2010 better than we did 2009, the rest of the year was determined by the nervousness of the markets. The implementation of government measures to cut spending has had, and will continue to have, a big effect on the Portuguese economy.

"As a result of cutting down on spending a lot of large PPP projects have been stopped: the third crossing across the Tagus River has been stopped and so have the airport projects. Also, the high-speed rail project [from Lisbon to Madrid], although it hasn't stopped, is progressing very slowly."

> **"The offer to purchase Finibanco was the only truly Portuguese deal last year. The rest were just triggered by outside events – there's no money to lend in Portugal"**
> Francisco Sá Carneiro, Campos Ferreira Sá Carneiro

There were a few headline deals in 2010, but these were mostly anomalous and said little about the Portuguese market. The largest deal was Telefónica's €7.5bn purchase of Portugal Telecom's 50 per cent stake in Brasilcel, which controls 60 per cent of Brazilian phone company Vivo.

The bidding war for Cimentos de Portugal (Cimpor), again involving Brazilian bidders, also kept a few firms busy (see box, page 32).

"There've been a couple of large deals in Portugal, but these don't represent the market as it stands," says Francisco Sá Carneiro, founding partner at Campos Ferreira Sá Carneiro & Associados. "These

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deals were triggered by international events. The whole Cimpor deal was a war among Brazilian bidders. The Portugal Telecom deal was again down to the Brazilians – it just so happened that the stake in the company was owned by a Portuguese player."

The only significant deal with any relation to the Portuguese market, according to Sá Carneiro, was bank and financial group Montepio's €341.25m takeover bid for Finibanco.

"The offer to purchase Finibanco was the only truly Portuguese deal [last year]," says Sá Carneiro. "The rest were just triggered by outside events – there's no money to lend in Portugal."

Instead, the type of work that firms have had to subsist on has been the usual downturn-related regulatory and compliance mandates.

"The type of legal services has certainly changed because of the sovereign debt factor," says Pedro Câmara, executive partner at Sérvulo & Associados. "The economic and financial conditions mean that the privatisations [which were announced by the government in March to raise public finances] didn't happen. People were counting on a lot of privatisations, but none happened. A major trend is the reduction of transactional work and a significant increase in regulatory work."

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Saviours over the sea

The consensus is, however, that regulatory mandates were not plentiful or profitable enough to make up for the dearth of deals. Fortunately Portuguese companies began looking abroad for opportunities.

"We've noticed a lot of the investment funds in Portuguese capital markets are leaving our country," says Joana Andrade Correia, a partner at Raposo Bernado. "Most of the opportunities are abroad. The banks and financial entities have had their capacity reduced, so they can't lend money to companies because banks need that money for themselves because they have to accomplish their solvency ratios.

> **"A lot of investment funds in Portuguese capital markets are leaving our country. Most of the opportunities are abroad. Banks can't lend money to companies because they need it themselves"**
> Joana Andrade Correira, Raposo Bernado

"The major companies that are dedicated to these areas [projects and infrastructure] are also starting to go abroad. Here in Portugal they don't have any projects. They don't have any alternative."

"Our clients have the clear idea that they must look beyond Portugal," adds MLGTS's Branco. "There just isn't enough happening for them in Portugal anymore. The most attractive jurisdiction, especially for service companies and contractors, but also for lawyers and accountants, is Angola.

"The country's growing and the political risks there are decreasing. We, as countries, understand each other well, and Angola's making large investments into Portugal and taking significant chunks of the Portuguese banks. A lot of money in Portugal at the moment is coming from the elite of Angola."

It is not just Angola, but the whole of Portuguese-speaking Africa, that has exploded as a market to be exploited by Portuguese firms and businesses, with the number of Portuguese firms with offices or alliance partners in the region reflecting this (see box, page 28). In October 2010 Abreu Advogados became the latest firm to establish links in the region, tying up with Mozambique's Ferreira Rocha & Associados.

The Africa connection has also prompted Portuguese firms to dig deeper into China, helping firms there to invest in the continent. PLMJ formed an alliance with China's Dacheng Law Offices, citing opportunities in lusophone Africa as one of the drivers behind the move, while in November CCA Advogados became the first Portuguese firm to launch an office in China with a Shanghai base.

The Chinese connection

While Portuguese law firms have been helping Chinese clients with investments, Portugal's government has in turn gone to China for assistance. In December Portugal's finance minister Fernando Teixeira dos Santos travelled to Beijing to persuade China to invest in Portuguese government bonds to help the country climb out of its financial crisis.

The trip was, by all accounts, a success. Teixeira dos Santos announced that China "has clearly shown it believes in Portugal" by increasing its financial assistance to the country. Unfortunately, it does not appear that the rest of the market shares China's confidence.

On 15 December 2010 Portugal issued €500m in three-month treasury bills to test the market. The bonds all sold, but the yield was incredibly high at 3.4 per cent – almost double the 1.82 per cent paid a month before.

Wasted for a year

The biggest fear for lawyers in Portugal is that the country's government will continue to refuse help and that things will not improve, forcing the country to accept a bailout later rather than sooner. This, they think, could lead to a wasted year for firms.

"If the government can't contain the country's debt problems with the austerity measures that have been introduced, at the earliest we won't see what happens next until May or June," says Branco. "This is because of constitutional limitations. We have presidential elections coming up [on 23 January] and we can't have general elections immediately before or after that.

"So the likelihood is that, if we do see international financial authorities stepping in and preparing a bailout, they'll only do so with a stable government in Portugal. We have a minority government at the moment, which is unlikely to withstand a confidence vote.

"We're all holding our breath to see if the austerity measures work. If they don't we'll be in limbo in the next few months and 2011 will be a wasted year. We'd probably only get the bailout in the third quarter after the elections and so only begin to see a semblance of order in the fourth quarter."

Eight months of stagnation would be a disaster for Portuguese law firms, which are already being tested to their limits.

"I'd imagine that 2011 could be a turning point for firms," says Santos Vítor. "Few law firms cut costs in 2009 or 2010 and just hoped that things would change for the better, but it doesn't look like that's happened and things will have to change. Firms will be under enormous pressure." ■

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▶ BIG TELECOMS AND CONSTRUCTION DEALS SAVE THE DAY FOR LAWYERS

Deal activity in Portugal in 2010 centred mainly around two sectors – telecoms and construction. Several of the biggest deals involved Portuguese cement company Cimentos de Portugal (Cimpor).

Activity kicked off in late 2009 when Brazilian steel company Cia Siderurgica Nacional (CSN) made a €3.9bn (£3.3bn) bid for Cimpor.

Cimpor rejected the bid, saying it was too low. However, the bid sparked interest from rivals. In early February Brazilian construction giant Camargo Corrêa swooped, buying a €968.3m, 22 per cent stake in Cimpor. Votorantim, another cement company based in Brazil, also acted, taking a 17 per cent stake in Cimpor from French rival Lafarge for €717m.

Both Camargo and Votorantim increased their stakes in Cimpor over the course of the year. In total the Camargo group spent almost €1.4bn on shares in Cimpor during the year. Viera de Almeida and PLMJ were the winners on the legal side, advising Camargo and Cimpor respectively.

The other particularly active sector during the year was telecoms. The biggest single deal of the year was the €7.5bn acquisition by Telefônica of Portugal Telecom's 50 per cent stake in Brazilian company Brasilcel.

The deal provided work for a host of firms from Spain, Portugal and Brazil. Cuatrecasas Gonçalves Pereira, Uría Menéndez and Brazilian firm Machado Meyer Sendacz Opice all advised Telefônica; Garrigues advised Portugal Telecom; and Sérvulo & Associados advised the Portuguese government.

Portugal Telecom was involved in a number of other major transactions as it entered into a partnership with Brazilian telecoms company Oi Telemar. Those included acquiring a 35 per cent stake valued at €2bn in LF Tel, while Telemar announced it was buying 10 per cent of Portugal Telecom, valued approximately at €730m.

The sheer size of the Portugal Telecom and Cimpor deals helped salvage deal value. M&A transactions involving Portuguese companies amounted to $22bn (£14.2bn) in 2010, the highest total since 2000 and quadruple the deal value of 2009. But volume was still relatively low at 166 deals, just a handful more than in 2009, meaning that work remains sluggish for Portugal's lawyers.

PORTUGUESE M&A VOLUMES SINCE 2000

Year	Total deal value ($bn)	Number of deals
2000	21.58	313
2001	8.02	247
2002	6.92	230
2003	5.56	134
2004	11.51	165
2005	11.11	185
2006	14.90	160
2007	13.51	225
2008	13.80	272
2009	4.63	152
2010	22.10	166

Source: Thomson Reuters

PORTUGUESE M&A DEALS 2010, BY VALUE

Value ($m)	Date announced	Target	Target nation	Acquiror	Acquiror nation	Target industry
9,742.79	11 May	Brasilcel	Brazil	Telefonica	Spain	Telecoms
2,655.97	29 July	LF Tel	Brazil	Portugal Telecom	Portugal	Telecoms
1,330.13	11 February	Cimpor	Portugal	Camargo Correa Portugal	Portugal	Materials
1,130.20	29 July	Tele Norte Leste	Brazil	Portugal Telecom	Portugal	Telecoms
1,010.61	12 May	Vivo Participacoes	Brazil	Telefonica	Spain	Telecoms
982.25	6 February	Cimpor	Portugal	Grupo Votorantim	Brazil	Materials
961.32	29 July	Portugal Telecom	Portugal	Telemar Norte Leste	Brazil	Telecoms
801.51	29 July	Naturgas Energia Grupo	Spain	Hidroelectrica del Cantabrico	Spain	Energy and power
438.08	31 July	Finibanco Holding	Portugal	Caixa Economica Montepio Geral	Portugal	Financial
384.76	13 February	Cimpor	Portugal	Camargo Correa Portugal	Portugal	Materials

Source: Thomson Reuters