By Jason Mitchell

Colombian entrepreneurs have turned more and more towards Central America as opportunities in Venezuela have dried up and investment bankers increasingly treat Central America and Colombia as a single market.

Ten years ago, Venezuela was Colombia's second biggest trading partner after the US. However, the strong tension between the former Colombian president, Alvaro Uribe, and the Venezuelan president, Hugo Chavez, led many Colombian groups to pull back from Venezuela. They turned their sights towards Central America, particularly Panama, Guatemala, Costa Rica and the Dominican Republic. In particular, the Colombians have invested heavily in financial services and energy in the region.

Today, investment bankers say that there is such strong integration between Colombia and Central America that banks that do not have a local commercial presence in the region increasingly regard the Andean and Central American region as one.

"It is no exaggeration to say that a single market is developing between the Andean region and Central America," says Ricardo De Bedout, country executive for Colombia at Bank of America Merrill Lynch. "Many investment banks that have representative offices in countries in the region increasingly see Central America and Colombia as a single market. Culturally, they have a great deal in common and also geographically they are in close proximity.

"Colombian companies have also realised that many industries in Central America are under-penetrated and see the opportunities in the region, which they look at as a whole."

Victor Rodriguez, president and chief executive at LatAm Alternatives, an independent third party advisory boutique based in Fort Lauderdale, says: "The tensions between presidents Uribe and Chavez led many Colombian entrepreneurs to reassess their business commitments in Venezuela. Venezuela has become closed to virtually every one, apart from China, Russia and the Middle East.

"Colombians understand the Central American culture and saw the opportunity to create a corridor that links south America with Mexico and the US. They are playing it smart."

For the year to 10 October, total M&A between Colombia and Central America amounted to USD821m with four separate transactions, according to Dealogic, the data provider. Total deals last year amounted to USD282m with nine transactions and in 2010 they added up to USD3.4bn with nine deals.

The biggest acquisition took place in July 2010 when Grupo Aval, the Colombian holding company engaged in a wide variety of financial activities, including banking, telecommunications and real estate, purchased BAC Credomatic GECF, the Panama-based financial services company with operations throughout Central America, for USD1.9bn. Grupo Aval owns Banco de Bogota in Colombia.

In January this year, Banco Davivienda, Colombia's third largest bank, acquired HSBC´s operations in Costa Rica, El Salvador and Honduras for USD801m. UBS advised Davivienda and Goldman and HSBC advised HSBC.

Since 2006, Bancolombia, another major Colombian bank, has owned Banco Agricola, one of El Salvador's most important banks.

Empresas Publicas de Medellin (EPM), the electricity, gas, water, sanitation, and telecommunications distributor owned by the municipality of Medellin in Colombia, has been one of the biggest investors in Central America. In January last year, it paid USD200m for Panama Distribution Group, the Panamanian electricity distribution company; in October 2010, it purchased Distribuidora Electrica Centroamericana, the Guatemala-based electricity distributor, for USD680m; and in the same month it acquired an 80.8% stake in Empresa Electrica de Guatemala, another Guatemalan electricity distributor, for USD635m.

For the year to 17 October, total Colombian and Central American (excluding Mexico) M&A -- including all cross-border and domestic deals -- amounted to USD11.2bn with 176 separate transactions. This compares with 235 deals last year valued at USD16.8bn and 189 transactions valued at USD12.7bn in 2010.

So far this year, Bank of America Merrill Lynch leads Dealogic's M&A advisory league tables for deals in Colombia and Central America (including cross-border and domestic) with a total of two transactions valued at USD2.4bn. Agora Corporate Consultants Ltda, a Bogota-based financial consultancy, is ranked in second place with one deal valued at USD2bn and Goldman Sachs is in third place with one transaction valued at USD1.7bn.

The strongest links are between Bogota, the Colombian capital, and Panama City: it is only one hour by aeroplane and their is a regular shuttle service between the two cities with flights every one hour. Colombians have invested heavily in real estate in Panama. Overall, they have seen the chance to create a 'gateway' between South America and North America. They are also investing to the south, especially in Peru, but that country has powerful domestic groups and it is difficult to penetrate its markets. Mexican entrepreneurs have focused more on developing links between the Mexican and US economies -- which are closely aligned -- rather than looking south to Central America.

"Most of the national champions in Mexico are just different from those in Colombia," says Bank of America Merrill Lynch's De Bedout. "For example, the financial services sector in Mexico is dominated by international banks, whereas the sector in Colombia is dominated by domestic banks. In particular, in the financial services and energy sectors in Colombia, the national champions see the chance to imitate their success in the domestic market in the Central American market."

Daniel Osorio, the chief executive officer at Andean Capital Management, an alternative asset management company based in Bogota and head of the Hedge Fund Association Colombia, says: "Traditionally, Colombians have seen many opportunities in Panama in banking, real estate and the development of tourism. It is a logical investment destination.

“However, in my opinion, Colombians do not view Central America as a single market: they see some countries such as Panama, Costa Rica, Guatemala, El Salvador and Honduras as attractive investment destinations and others such as Nicaragua and Belize less so, because of their worrying political and macroeconomic climates.”

Experts say they do not expect a convergence in the capital markets of Colombia and Central America but they do believe that banking regulation will become increasingly integrated between the south American country and the region.

“It would be extremely complicated to try to integrate the stock markets of Central America with the one of Colombia,” says Javier Vargas, managing director and co-head of investment banking for Latin America at Credit Suisse. “It would involve so many different currencies and different regulatory systems. It would be like the project to integrate the Colombian, Peruvian and Chilean markets, known as Mila, multiplied by three.

“However, I think we will see a convergence in banking regulation. Colombia´s biggest banks are now the main banking players in Central America and Colombia has a solid banking system. Central American regulators will speak more and more with their counterparts in Colombia.”

As well as financial services, experts believe the strongest links between Colombia and Central America will be in the energy and retail sectors. As a whole, Central America is a power starved region and relies heavily on fuel oil, which is highly damaging to the environment.

“We have already seen strong Colombian investment in the energy sector in Central America,” says Vargas. “I think that is set to continue growing. For European and US energy groups, their assets in Central America are of marginal interest. European companies are selling their assets and concentrating on paying down debt. American groups want to focus on other markets where they are able create greater scale. That creates opportunities for Colombian companies.”

Vargas adds that environment standards are likely to become more stringent in Central America and a new regional regulatory framework for energy developed by authorities from countries throughout Central America is a strong possibility. This could be closely aligned to Colombia’s regulatory standards.

The retail sector in Central America has been growing fast in line with greater consumption and the rise of the middle class. That trend is expected to continue and retailers from Colombia are increasingly turning their attention to the region. However, this sector is likely also to attract retailers from Mexico and around the world.

Colombia and Central America have also been witnessing growing international DCM activity. According to Dealogic, for the year to 17 October, there was a total of nine deals out of Colombia valued at USD7.3bn, compared with nine deals for the whole of last year valued at USD6.3bn and three deals in 2010 valued at USD1.9bn. This year there have been three deals out of Panama valued at USD1.19bn against two deals last year valued at USD545m and no deals in 2010.

In Honduras this year, there were four deals amounting to USD424m, compared with one deal last year valued at USD104m and two in 2010 valued at USD208m.

Guatemala this year saw two deals valued at USD890 whereas there were no deals last year nor in 2010.

The macroeconomic performance and business friendliness of Central American countries varies greatly. However, increasingly, Colombian companies are turning to the region - especially to Panama, Guatemala, Costa Rica and the Dominican Republic - as their home market is becoming saturated and there is limited room for organic growth.