

Savant: "Nobody should buy a company abroad just because it's cheap."



# Learning from the Crisis

For Karl P. Sauvant, professor at Columbia University, Brazilian companies need to think internationally if they are to take advantage of the current situation

NELY CAIXETA

**A**o During the three decades that he worked for the United Nations, before retiring in 2005 as Investment Director of the UN Conference on Trade and Development (Unctad), Professor Karl P. Sauvant gave special attention to matters related to developing countries. Sauvant, who is German, knows Brazil very well – and not just because of his work. As well as following the Brazilian market and companies for many years, he worked under Ambassador Rubens Ricupero when the Brazilian diplomat was Unctad's Secretary-General. And Sauvant's wife, Silvana, is from Belo Horizonte in Minas Gerais State – they met at the UN.

Savant is the father of the World Investment Report, an annual report produced by Unctad which has, since 1991, offered a detailed annual x-ray of foreign direct investment flows around the world, and he has dedicated the past three years to the same subject at Columbia University in New York. As well as lecturing there, he created and runs the Vale Columbia Center on Sustainable International Investment ([www.vcc.columbia.edu](http://www.vcc.columbia.edu)), a joint study center of Columbia Law School and The Earth Institute, supported by the Brazilian mining giant Vale, formerly known as CVRD.

In this interview with PIB – whose first six editions he swears he read cover to cover! – Sauvant

discusses the impact of the crisis on emerging markets, predicts a period of low growth for Brazil and offers a warning to Brazilian companies that have set off on the road to internationalization. In the wake of the financial crisis and recession, he says, there might be some good opportunities to acquire companies abroad. "But you have to be aware that it's very difficult to make an international merger and acquisition work well," he said in a phone interview with PIB. "There's a real need for professionals who are trained and experienced in international markets."

**Many analysts have said that the financial crisis could serve as a short cut to help companies from emerging markets establish themselves in global markets more quickly. Do you agree with that, or is it still too soon to know?**

In principle, yes. But during a financial crisis and recession, it's difficult to implement major expansion plans, including for firms from emerging markets. To be sure, for

**The relevant market is no longer just Brazil, it's the world. The option of staying home doesn't exist any more**

a short time it appeared that developing countries could disconnect or decouple from the rest of the world. Today, everyone knows that emerging markets, too, are suffering considerably from the effects of the crisis and recession. In Brazil's case, the IMF just estimated the country's GDP to decline by -1.3% in 2009 (the same decline as for the world as a whole); but I wouldn't be surprised if this percentage, like the others released by the IMF during the past few months, is revised downwards again. All the forecasts of the last semester have been revised downwards, every two months or so.

**These IMF forecasts have irritated President Luiz Inácio Lula da Silva enormously.**

His job, like that of politicians in all countries, is to be optimistic and do whatever is possible to avoid a deeper recession. I keep my fingers crossed and hope he's right. We all hope the scenario doesn't become worse. On the macro level, the crisis doesn't differentiate between developed and developing countries. However, on the micro level of foreign direct investment, I could imagine that some companies might be able to expand internationally with great success in the present circumstances – the opportunities are there. In a certain sense, it's a good time to grow your international presence. However, companies from developing countries need capital to un-

dertake cross-border mergers and acquisitions or to set up operations outside their home countries. But given the shortages of credit, many might find it difficult to find the required resources to do so.

**Which companies are managing to take advantage of the crisis to expand their international footprint?**  
Chinese companies, for sure, are taking advantage of their capacity to go international, of their financial strength and of the opportunities to buy cheap assets in other countries. China's foreign direct investment reached US\$26 billion in 2007. Last year, with the crisis already well entrenched, the country's outward FDI doubled to US\$52 billion, at a time when global FDI flows fell by some 20%. It's important to note, however, that between 80% and 90% of all Chinese outward FDI is undertaken by state-owned enterprises, in other words, firms that don't have financial problems. For Brazil and India, the situation is different.

**How do you see Brazilian companies doing after the crisis?**

It's very difficult to undertake a precise assessment at this moment, but I fear they are having difficulties getting the funding to finance their international expansion. Also, many have seen their profitability fall sharply. I'm talking especially about companies that supply raw materials, whose prices have suffered very badly in international markets. A tonne of iron ore, for example, was quoted in May this year at roughly US\$60, compared with US\$200 in March of 2008. That's less than a third of the price of a year ago. Obviously, such a drop affects the capacity of companies to finance their international expansion.

**In times of great turbulence abroad, companies based in countries with large home markets like Brazil tend to concentrate on domestic opportunities. Are they wrong, doing that?**

Well, it's a fact that Brazil has a large market. But the relevant market is no longer just Brazil, it's the world. The option simply to stay at home doesn't exist any more in a globalized world economy. Companies need to establish an international presence if they want to remain competitive – in fact, a network of foreign affiliates becomes an important source of the international competitiveness of firms. But Brazilian companies have a competitive disadvantage, which is the lack of a clear policy of internationalization on the part of the government. It would be good for the government to take a long, hard, systematic look at what other countries are doing in terms of offering support to their companies to expand internationally.

**Which examples should Brazil look to?**

All developed countries have an arsenal of tools in place to promote foreign direct investment by their firms. The same applies to a (small) number of developing countries. China, for example, has a government policy to train highly qualified international managers so that they can competently run companies established or acquired abroad. The country also supports outward FDI

**Brazil lacks a consistent policy to support the international expansion of its companies**

means, including by helping them to identify good business opportunities abroad. China also has more than 100 bilateral investment treaties to protect its investors. Compare that with Brazil. At the start of his first term in office, President Lula said he would like to see a dozen well-known Brazilian multinationals. But the country still doesn't have a consistent policy to support (and perhaps even encourage) the international expansion of its companies.

**Do you think the failure of so many financial institutions could represent an opportunity for Brazilian banks to assume a more important role in world finance?**

Brazilian banks are renowned for their efficiency, their capacity to overcome challenges and their ability to grow in times of high inflation. They will have good opportunities to expand their international operations, provided they manage adequately to evaluate the assets of the financial institution they plan to purchase. At this moment, however, it's difficult to know how much banks like Citibank, Bank of America or any other financial institutions are really worth. According to IMF estimates, a significant amount of toxic assets still have to come to light. It's very difficult to predict how much time is necessary for this situation to become clearer.

**Does this mean we shouldn't expect major international deals by Brazilian banks in the near future?**

I would be surprised if major deals happen just now. The atmosphere is still very uncertain. I believe that many investors will remain very cautious about investing in financial institutions just now – unless, of course, a company has a special target and is reasonably certain that it is heal-

thy and without problems. But here I would like to point out one aspect that demands great consideration and applies to companies in all sectors: no one should acquire an asset abroad just because it's cheap.

**What should a company consider when evaluating such assets?**

Above all, they must fit into the being acquired must make sense for the company in the long term, in terms of where it wants to be and what market segments it wants to serve. Companies also need to understand that it's very difficult making mergers and acquisitions work out well, in particular when they involve two major organizations. This is the biggest challenge for companies from emerging markets, including Brazil.

**What precisely is the challenge?**

Many companies lack sufficient experience to operate in international markets via the creation of integrated international production networks of foreign affiliates. To do that successfully, they need a pool of talent with experience in international markets. Many Brazilian multinationals still have difficulty in internationalizing their boards and senior management positions. This is a serious matter, and firms should pay much more attention to it.

Even large multinational enterprises from developed countries, companies that have lots of experience, have problems in doing this. The acquisition of Chrysler by Mercedes-Benz-Daimler, for example, was a disaster. An operation of this size involves questions such as the adaptation of different cultures, the meshing of different production systems and the creation of a company that is

**Brazilian banks will be able to buy overseas assets, provided they can evaluate them properly**

geared to integrated international production. Most Brazilian companies don't have the experience of doing that, and this means that they will have to make even bigger efforts to be successful in international mergers or acquisitions.

**Brazilian banker André Esteves, who recently bought back the Pactual bank from UBS, said that his ambition is to make Pactual into the Goldman Sachs of emerging markets. Is that feasible?**

There's no reason, at least in principle, why any bank or company should limit its activities to its country of origin – on the contrary. In a globalized world economy, everything is possible. If Esteves really wants to be ambitious, he shouldn't limit his goal like that: he should aim to make his bank the Goldman Sachs of the globalized world market. The key to doing this successfully will, naturally, be attracting talent from all over the world, and not just Brazil. He must construct the image of an investment bank that really does know what it is doing, one that is trustworthy and able to help both individuals and companies to be successful.

**What do Brazilian companies need to do to make consumers in rich countries want to buy their brands?**

Establishing a brand is a tough business, but it can be done. Just look at the Japanese multinationals. Forty years ago they were known as manu-

facturers of shoddy products. They were not seen as serious companies. Today they are global market leaders in various segments and have brands that are well established and respected. Companies from other countries can do the same thing, but it takes time and effort. The most essential thing is to have products that offer genuinely superior quality at reasonable prices.

**Some parts of Brazil's society object to internationalization because they argue that Brazilian companies are exporting jobs...**

That doesn't happen just in Brazil. We heard the same arguments in the United States at the end of the 1960s and even today, when people speak about offshoring. The same happens in Western Europe, where people speak about delocalization, the shifting of production facilities to other countries. Governments complain that companies move their factories to Eastern Europe and the Far East. The President of France, Nicolas Sarkozy, recently even encouraged a major automobile maker to bring some of its factories back to France in a move to create local jobs. However, as long as we have an open world economy, companies need to produce wherever they can do so most efficiently. If they don't do that, they will end up being less competitive and even go under. A national company isn't much use to Brazil or any other country if it goes bankrupt.

**When do you see the world economy starting to grow again?**

If I could answer that question, I might win the Nobel Prize, or at least I would make a fabulous play in the market. But it wouldn't surprise me if we don't see recovery until the second half of next year. ■