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Pitting Latin Multinationals against Established Giants

by Paolo Pigorini, Arthur Ramos, and Ivan de Souza

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To succeed globally, "multilatinas" — and all aspiring international companies from developing nations — must make rapid strides in governance, transparency, and executive appointments.

by Paolo Pigorini, Arthur Ramos, and Ivan de Souza

Latin-owned companies such as Mexico's Cemex, Argentina's Arcor, and Brazil's Embraer and Petrobras have achieved remarkable success in their home markets, often against U.S. and European competitors. Building on this success, many of these companies have become "multilatinas," pursuing an aggressive strategy of regional and international expansion by acquiring companies and establishing cross-border joint ventures.

In 2006, 82 percent of M&A deals in Latin America originated with Latin companies. Brazil provides an excellent example: Its Gerdau Group acquired several international companies in 2007, including U.S.-based Quanex (Macsteel) and Chaparral Steel; CVRD acquired the Canadian Inco in 2006; and AmBev merged with Belgium's Interbrew, creating InBev, which recently acquired U.S.-based Anheuser-Busch. These moves and many other similar ones are creating a new corporate elite in Latin America. From 2002 to 2006, annual revenue for multilatinas grew 20 percent, compared with 12 percent for other multinational corporations. And in the mid-2000s, 59 percent of the 500 largest companies in Latin America were Latin-owned, compared with 52 percent at the beginning of the decade.

But the rise of these companies on their home turf does little to guarantee that they will be able to prosper on the global stage competing against established multinationals. Indeed, like many companies in emerging nations, these businesses face critical challenges relating to the necessity of more open governance procedures and transparency of information for internal and external stakeholders. And integral to the governance challenge is the need to seed boards and top management with new members who have an international perspective and experience.

Based on extensive interviews with dozens of executives in Argentina, Brazil, Chile, and Mexico, we found that access to international capital markets often hinges on good governance. Moreover, sustained long-term stock price appreciation is dependent on investor confidence in the company, which is frequently a reflection of the business's transparency.

One study of Brazilian companies generated results that we believe are relevant to the entire region. It identified three building blocks of corporate governance that are essential for emerging market multinationals to implement.

Shareholder rights. Investors should closely examine the relationship between controlling shareholders (typically wealthy families) and minority shareholders. To win investor confidence, these minority sharehold-

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ers must be protected through clear and fair dividend distribution and mechanisms to adequately compensate them in the event of a sale or merger.

Compliance. This is the basic building block of governance. It's critical to have an empowered audit committee acting on behalf of the board that evaluates financial statements before disclosure to the market and oversees internal audits.

Board and management composition. Because many multilatinas are still in the process of building a rigorous governance system, to boost investor confidence, it is crucial that they appoint board members and top managers with credible professional backgrounds and the confidence and experience to make key global strategic decisions.

Putting the right board and management dynamics in place not only improves access to capital, it also serves the very practical function of helping companies implement successful international management models. Many multilatinas were originally family-owned or still are, with high concentrations of equity held by a few family members. Hence, participation of nonfamily professional managers with deep knowledge of international aspects of the business in board-level strategy formulation is still an exception. As a result, many boards, dominated by members who may be trusted by controlling families but not expert in global operations, neglect the international activities that often represent new opportunities for growth.

To ensure the right balance between decision making by managers at the company's core and by its geographic, or country, managers, multilatinas must encourage global managers to participate in strategic decision making and perhaps to join the board. In addition, multilatinas should consider the creation of committees that involve solely the international business. For example, one Brazilian sporting goods company has established country-specific advisory boards to counsel international executives on unique cultural or political factors in their countries of responsibility. And decision rights must be clarified. In one successful implementation of this approach, executives at a consumer goods company identified which decisions had to go through headquarters (for example, those that may have an impact on the corporate image or introduce systemic risk) and which could be delegated to local managers (such as decisions in arenas that need local customization and faster market response).

Such steps are essential because most multilatinas — 85 percent of companies in one of our studies — provide their international operations with only the minimum of independence. Their ambivalence is clear. "Our main challenge is to speed up the international expansion, and we will be able to achieve this only by delegating more to the field," said one CEO. "But I am not sure I want to give [country managers] more authority."

Why this reluctance to empower? Many companies have enjoyed success with the centralized management style of an owner or CEO. This leader is often reluctant to share power or may simply enjoy playing a direct role in day-to-day operations. A disinclination to delegate is also often exacerbated by the company's limited experience with new businesses or geographies and by a shortage of managers with the necessary skills and consistent track records to lead international businesses. In addition, due to immature processes and systems, most multilatinas lack the minimum control mechanisms needed to manage decentralization. These factors tend to lead to inconsistent relations between headquarters and the field. Periods of delegation are often followed by periods of strong central control, especially when results fail to meet expectations.

The path to internationalization for multilatinas is demanding, often forcing them to fight in unfamiliar environments. But if they truly learn to master the complexities of governance, multilatinas will win access to capital to sustain expansion and at the same time increase their ability to navigate the myriad obstacles that stand in the way of their success. +

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