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October 1, 2001
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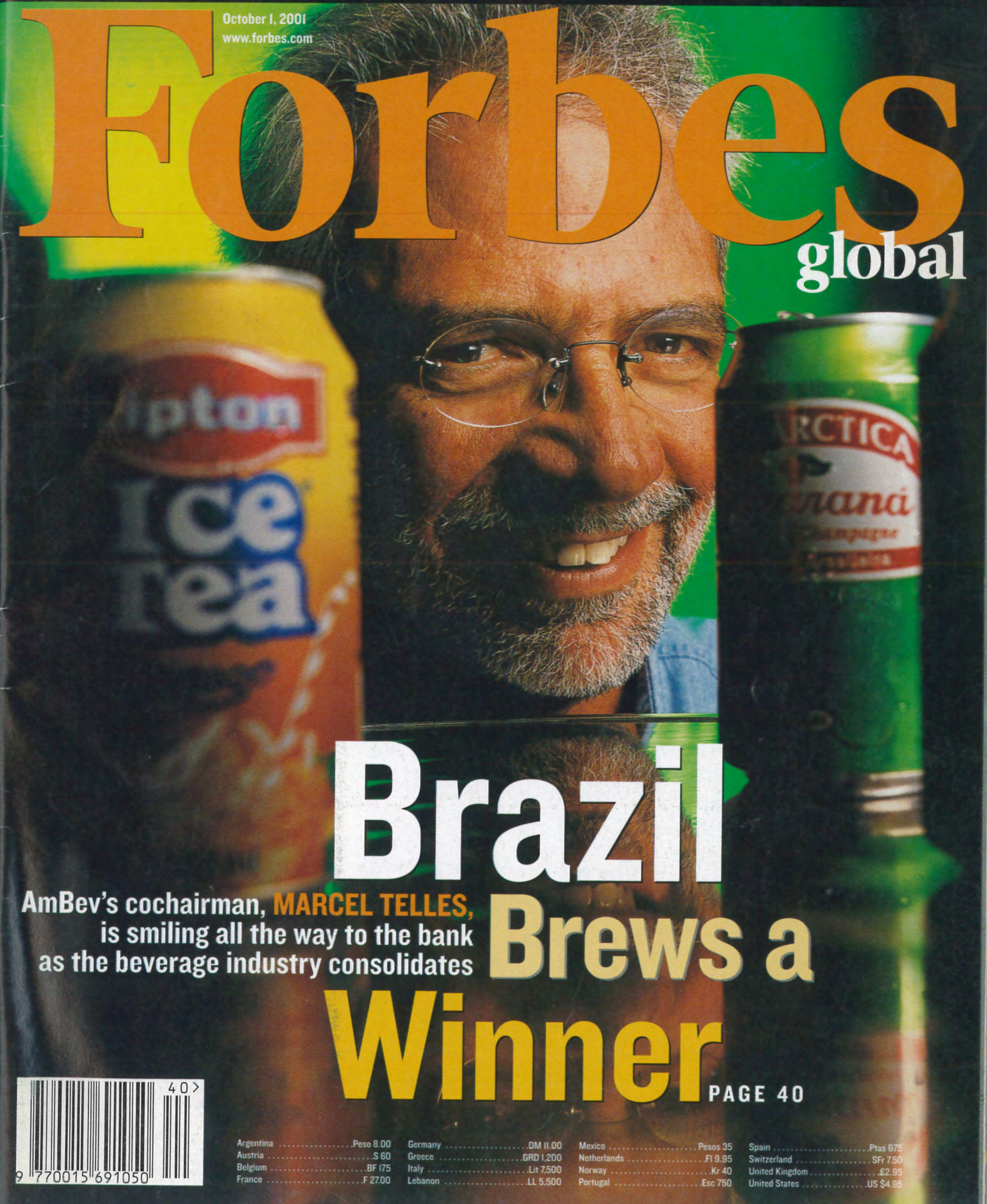

Brazil Brews a Winner

AmBev's cochairman, **MARCEL TELLES,** is smiling all the way to the bank as the beverage industry consolidates

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Brazil brews a winner

Marcel Telles wants AmBev to become the world's best beverage company. As the industry consolidates, he couldn't be in a better position.

BY ALEXANDRA KIRKMAN

Most investors would be hard pressed to name the world's third-largest beermaker (by volume sold in 2000). First comes Anheuser-Busch, then Heineken. Which is next? The answer is Companhia de Bebidas das Américas (known as AmBev), which is based in Brazil.

And here's another surprising fact: AmBev, with 2000 revenue of \$2.7 billion, sits on top of the largest beer market in one of the fastest-growing beer-drinking regions in the world. Anheuser-Busch predicts that 44% of the growth in the industry's profit between 1999 and 2005 will occur in Latin America, well above that in the other two fast-growing regions, Eastern Europe (23%) and Asia (19%). "Latin America is one of the great emerging markets that has not yet been infiltrated by anybody other than local operators like AmBev," says Nick Chaloner, director of communications for South African Breweries, a big international player.

As the global beer industry consolidates, AmBev could play a crucial role, as a partner, an acquisition or a purchaser.

Telles presides over a pressure-packed staff meeting.

The key for AmBev is to grow even larger in Brazil. "I see a huge undefined opportunity," says Marcel Telles, 51, the tall, jovial cochairman of AmBev.

Telles created the opportunity for AmBev. A Harvard-educated former partner at Banco Garantia, he was asked in 1989 by Brahma, a Brazilian brewery that was a client of the investment bank's, to join the board of directors and restructure the company. In the ensuing ten years, he turned the ailing Brahma, the largest beer company in Brazil, into a lean operation. He cut the work force by more than half, raised productivity sevenfold and lifted EBITDA (earnings before interest, tax, depreciation and amortization) eightfold, to $505 million on revenue of $1.8 billion, in 1999.

In July 1999, Brahma merged with its next-largest competitor, Antarctica, in exchange for $1 billion in stock, changing the company's name to AmBev. Telles became cochairman along with Victorio De Marchi, the head of Antarctica. The deal gave it 70% of the Brazilian beer market, which is worth an estimated $5.5 billion a year in sales. The takeover was passed by antitrust regulators because Brazilians make little distinction in their buying habits between soft drinks and beer: In beverages as a whole, AmBev has a less formidable 40% share.

That Brazil was creating a national champion in the global brewery industry also helped AmBev's cause. Brazil's population of 170 million makes it the world's fifth-largest country, but it has only a handful of internationally recognized companies.

AmBev is not some artificial company brewed up by politicians in Brasília. It is one of Latin America's best-run businesses, a further reason why any foreign beverage company wanting to do business in the region has to beat a path to its door in São Paulo. "AmBev is a strong, creative competitor with good brands that competes fairly in the marketplace," says Stuart Cross, president of Coca-Cola Brazil.

When Telles took over at Brahma, he realized that there was an important similarity between Garantia, his investment bank, and a brewery. "At Garantia, the only real asset besides the name was our people," Telles tells FORBES GLOBAL over a few cans of Ambev's Guaraná Antarctica soda in a conference room at the AmBev headquarters (a guaraná is a berry that grows in the Amazon jungle). "And the best way to keep good people is to give them a share of the business." At Garantia that meant partnerships for the highest achievers; at Brahma, a lucrative stock ownership plan for the company's top executives. Telles' turnaround formula was simple: "Hire the best people, have the right focus, give them the right motivation."

And it has carried through to AmBev, where more than 250 of its top managers participate in its stock ownership plan. Employees buy their shares up front (at a 10% discount) and contribute 70% of their bonus to maintain them. Shares become fully vested after five years.

Most of AmBev's 17,500 employees are paid only modest salaries by Brazilian standards, but half of them receive a bonus of 50% to 100% of their salaries at the end of the year if AmBev's performance goals have been achieved. Telles is aiming for long-term annual growth in economic value added (EVA) of 15%. (EVA is a way of measuring performance against the cost of capital.) If this goal is not met in a given year, there are no bonuses for anyone, even the executives. "It's impressive. AmBev has managed to align not only upper management but also salespeople and other employees with value-creation and therefore with shareholders," says Marco Vera, the head of Latin American equity research at Deutsche Bank in New York.

During the nine months that it took to gain antitrust approval for the merger of Brahma and Antarctica, the two companies established what Telles calls a "war room" to prepare for integration. Since the official approval, there have been savings of $200 million from reorganization.

There are no frills at headquarters. The 400 employees work together on one floor of an office building; senior managers sit at two long tables in one corner. "Our culture is a lot of leading by example," says Telles. "It's very important that when I go to or from an airport I take a yellow cab rather than a luxury car." Jeans and polo shirts are de rigueur, even for Telles, who is now in the midst of changing his business priorities. "The next ten years will be more fun because we can concentrate on revenue growth rather than cost-cutting," he says.

First task: to get Brazilians to drink more beer. Brazil ranks 29th in beer consumption *(see chart, p. 42)*, and it's 25th in soft drinks, so there's plenty of room to grow. One way Telles wants to increase sales is to use promotions and advertising to encourage people to consume more beer on weekdays. Another is to install more of their sub-zero coolers in shops that sell beer, because "Brazilians like their beer ice-cold," says Telles.

AmBev is a technological leader in mining the market for up-to-the-minute data. Each of the 12,000-strong sales force is armed with a personal digital assistant that can provide information on beer purchases at each of the million places where AmBev's products are sold. "Using the handheld devices, we know our exact market share at each point of sale. If we have a 70% share at one point of sale and 20% at another, the pricing strategy will be totally different," says Telles.

With this kind of market power and only $1.3 billion in total debt, it's natural that AmBev should be looking beyond Brazil, which accounts for 95% of its revenue. It already has small operations in Argentina, Venezuela and Uruguay and is thirsty for more. "It's a perfect opportunity to apply the lessons we've learned in Brazil," Telles says. He won't comment on market rumors that he's planning to bid for Quilmes, Argentina's top brewery, with annual sales of $1 billion.

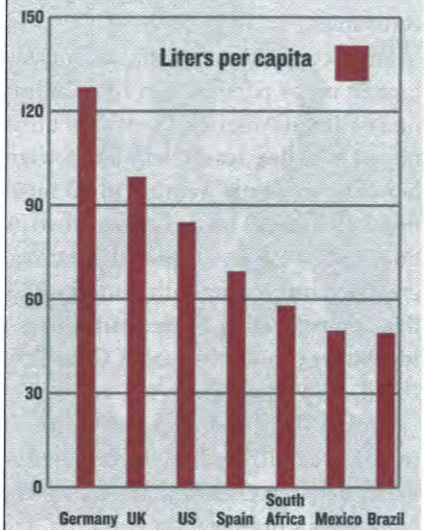
And there's plenty of opportunity for AmBev in soft drinks, too, where consumption in Brazil is growing by 6% a year, compared with 4% for beer. AmBev owns the No. 2 soft drink (behind Coke), Guaraná Antarctica, which has a 9% share in Brazil. AmBev brands have a combined share of 17%, a long way behind Coca-Cola's 50% share. Outside Brazil, AmBev has partnered with Pepsi to sell Guaraná Antarctica globally.

Such a partnership could presage more international ventures for AmBev, as the beverage industry rapidly consolidates. Adriano Seabra, a Latin American beverage analyst at Credit Suisse First Boston in Mexico City, says that only Anheuser-Busch, Heineken and Interbrew could pull off a takeover of AmBev. "I don't think that Anheuser-Busch or Heineken would pay the price that Telles would want, but I think he would sell for a big premium," he says.

Telles concurs. "The value of the number of opportunities we see will likely never be paid by anyone—they'd throw me out the window if they heard my asking price," he says, acknowledging merely that some global players have been looking for acquisition targets in the region.

Untapped potential

Brazil's per capita beer consumption has room to grow.



Source: World Drink Trends. 1999 AmBev.

The market already gives AmBev a rich valuation. With a 2001 estimated P/E of 22.8, AmBev is on a par with Anheuser-Busch and second only to Heineken's 25.9 *(see table below)*. Vera is not surprised by AmBev's high share price. "There are only three true growth markets for beer: Brazil, Mexico, and China. AmBev has the best competitive position in one of those massive long-term growth markets," he says. Vera expects net income to rise 30% to $311 million this year on sales of just over $2.7 billion.

Last year Anheuser-Busch made an unsuccessful bid for Bavaria, a Brazilian brand that AmBev was forced to sell to satisfy the antitrust authorities. In the end, it went to Molson of Canada for $200 million. But Anheuser-Busch is unlikely to stop there. Stephen J. Burrows, the CEO of Anheuser-Busch International, says: "Latin America is attractive for the implementation of both our brand and investment strategy. As the largest beer market in South America, Brazil would be consistent with this strategy."

Heineken, too, enthuses about prospects in Latin America. Manel Vrijenhoek, a spokesperson for the company, says that it is trying to expand its 15% interest in Kaiser, the fourth-ranked beer in Brazil, with a 14% market share. "We view Latin America as a very interesting and important growth market—absolutely," she says.

Telles is neither a military man nor a U.S. citizen, but he's fond of the U.S. Marine Corps's famous recruiting slogan: "The few, the proud, the Marines." He's certainly positioned his company as an elite business in Brazil. But can AmBev pack a punch beyond its home base? Our guess is that it can and will. FG

Bring on the brew

With Latin America one of the fastest-growing beer-drinking regions, AmBev is in position to gain on the big boys.

Company / country	Recent price (US$)	Est 2001 P/E	Dividend yield	Price/ book	Price/ EBITDA	EV/ EBITDA	5-yr price change*	EBITDA margin	Sales (US$bil)	Market value (US$bil)
Anheuser-Busch / US	43.04	22.8	1.7%	8.4	12	14	127.3%	26.9%	12,262	38,276
Heineken / Netherlands	41.92	25.9	0.7	7.6	15	14	47.2	21.3	6,611	16,432
Interbrew / Belgium	24.85	21.4	0.6	2.9	4	16	NA	21.4	5,211	10,622
Group Modelo / Mexico	2.39	19.1	0.5	2.7	4	9	106.5	32.8	3,042	7,769
AmBev / Brazil	189.31†	22.8	0.9	6.1	8	12	48.9	32.9	2,692	7,324
South African Breweries / UK	7.41	13.8	3.4	2.7	7	7	NA	24.6	3,482	5,744
Fosters Group / Australia	2.72	20.1	3.0	2.8	10	14	48.4	24.7	2,132	5,471
Scottish & Newcastle / Scotland	7.56	10.9	5.4	1.6	5	8	−28.6	17.2	5,745	4,893
Coca-Cola Femsa / Mexico	2.20	15.5	1.0	4.5	6	9	151.9	20.7	1,712	3,137
Carlsberg / Denmark	45.14	17.9	1.2	2.6	4	7	−23.8	21.2	3,529	2,876

All figures as of Sept. 4. *In US dollar terms. †Per 1,000 shares

Source: Worldscope via FactSet Research Systems.