The Brazilian Economy
—With the gradual recovery of the U.S. economy and even a slow recovery in Europe, how do you think the global economic outlook will affect Brazil?

Paulo Stark—The resumption of U.S. growth and the European Union’s attempt to create an environment that fosters investments are very positive for Brazil. … Brazil is important for these countries; it has natural resources, commodities, and a large domestic market. Also, the U.S. recovery comes at a time when China is slowing down, which

What Brazil needs to really grow

Paulo Stark
CEO of Siemens in Brazil

Solange Monteiro
RESILIENCE AND FLEXIBILITY seem to be core beliefs of moderate optimist Paulo Stark, CEO of Siemens Brazil, when he talks about his business and Brazil’s economy. Stark, an engineer who began his career with Siemens more than two decades ago, sees investment intentions being rethought as a result of the escalation of the crisis of state-owned oil company Petrobras, which could benefit the logistics and electricity sectors. “That will cause a gap until new projects are developed, but it is not a permanent problem,” he says. However, to encourage new investments, he advocates both a concession model more open to private capital and longer-term planning for major infrastructure projects: “Sometimes we have the impression that Brazil needs a crisis to take a leap forward; now’s the time to jump to avoid being run over.”
A factor that most pessimistic scenarios are not taking into account is greater access to financing in the European Union because of credit easing, and the possibility that part of that capital will be invested here. It is noteworthy that foreign direct investment flows into the country have stayed at relatively high levels, despite all the changes Brazil has experienced in recent years.

What are the implications?
Brazil has one of the lowest rates of total productivity in the world. Why is it lower? Is it because we cannot work productively within an industry? Or are we not using the assets we have in the best way possible? A factory in China will be operating 21 shifts a week. The same asset in Brazil may only be working 7 shifts, one a day. Businesses are not investing in automation because there is no demand for higher production. This is the dilemma: I do not invest because I have no demand, and I do not demand because I do not invest. This means these companies are prevented from participating in global supply chains. The world market is 50 times greater than the Brazilian market. Here a small or medium business invests in a piece of equipment to produce just for the local market, which means investing to meet the demand of a market only one-fiftieth the size of the global market. Meanwhile, the Chinese competitor is investing to serve the larger market.

What stimulus for industry is feasible given the government tightening policies?
This is a complex issue that involves many variables, but there are some things that would have positive impact. One of them is
the question of scale, to enable companies to participate in the global market. A few years ago the National Confederation of Industry Brazil did a study that produced some good insights (Industry Strategic Map 2013–22). But it will not work, in my opinion, if there are exemptions and tax benefits at the end of the production chain. There are so many inefficiencies along the production chain that even though the government grants tax exemptions at the end of the production chain, [domestic industry] will still be light years behind its global competitors. Scaling up production has to happen from the bottom up, in the first value-added steps, and go forward, year after year, throughout the production chain. We need to replace the current policy by facilitations at the beginning of the production chain, so that the first value-added steps are competitive globally, so that companies return to buy from local suppliers, and thus we will be increasing the scale, gaining competitiveness, and suppliers can start to export, too, and not depend only on the local market.

What is your outlook for public and private investment in Brazil?
Foreign as well as domestic investment has kept up a good pace in recent years, but though it is good compared to previous levels it still falls short of what we consider necessary. And investment will be directed where there is growth. One focus should be public-private partnerships, which will largely depend on government policy, rules, and the concessions program. A revised concession program that is more open to private capital could dismantle many of the hindrances we have today and attract a lot of foreign investment in infrastructure, which is critical for the country’s growth, in areas like energy, logistics, and water supply. There is no doubt that there is interest in investing here. But a little easing is necessary to keep this capital coming and reduce the need for public investment.

The regulations for concessions have generated considerable debate. One of the most criticized points is the question of the rate of return on investment. Do you agree?
My company does not invest directly in infrastructure, so I will give my own view. You cannot have an absolute discussion on the topic because the rate of return is very dependent on the amount of risk the investor has to take. So a low rate of return for a low risk can be attractive, even excellent, compared to investments abroad. More importantly, however, is the long-term perspective of a
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particular concession and of the country’s development strategy. For example, when someone invests in a port, the business case is of no use if the investor does not have a clear sense of the country strategy that will make that port important in 20 years. Long-term signaling—a more nonpartisan development policy—matters. Lack of a development strategy generates uncertainty for investors, who then try to optimize the return on investment and mitigate their risks in the short term. If we had a social pact related to the country’s development strategy, it could change the game completely.

Your experience at Siemens includes time in Mexico and Germany. How do you see Brazil’s innovation environment in comparison to those countries?

I am convinced that innovation within industry is not done by passing a law, but by economic logic. And this logic is connected to several factors. The first is the existence of some kind of comparative advantage. An obvious area here is agribusiness, and another is mining. There are others that can be created in the long term, through investments in education, universities, and basic research, which is what many countries are doing. When I hear about innovation here, I sometimes get the feeling that we’re putting the cart before the horse. Choosing where to innovate through a decree might work in a protected market, but not in a free, global market.

We need to take the straightjacket off innovation and economic activity, and focus on identifying areas of comparative advantage. The Brazilian Corporation of Agricultural Research (Embrapa) created know-how without forcing farmers to use it. Farmers went looking for Embrapa when they realized that without this knowledge, they would be left behind. The same thing happens in industry. Entrepreneurs will only invest in R&D when they realize they need the knowledge to become more competitive. Brazil needs to improve education, identify more areas of comparative advantage, and make information available; then entrepreneurs will surely seek opportunities to build their businesses. Brazilians are good at recognizing business opportunities.

How does Siemens in Brazil see its operations in 2015?

Not just in Brazil but globally, we are drafting a business agenda based on three major aspects: electrification, automation, and what we call digitalization—business virtualization. What benefits does the agenda bring to Brazil? The entire infrastructure in every
industry obviously begins with bricks and mortar, but one of its foundations is electrification. In Brazil, there is an urgent need to expand electrification. Then we have automation, which allows companies to better use their assets. Finally, digitization allows for flexibility; it creates a virtual environment where I can plan, redesign, change flow, and then apply it, all in one operation. When we talk about smart grids, we mean reconfiguring the power grid by pressing a button. In Germany, and more widely in Europe, this process is called industry 4.0. Government agencies, ministries, and some companies, among them Siemens, are developing this technology and the necessary standardization for it to be widely used.

**To what extent is Siemens worried about the uncertainties involving the oil and gas sector given the investigations of Petrobras?**

Because of the diversity of our businesses, we have been seeing a clear shift in our customers’ focus of investment. The value supply chain will seek to develop other businesses that may have been in the drawer or lower on the priority list. This reallocation process will cause a gap until new projects are developed, but it is not a permanent problem. Today we see more focus, for example, on energy. The question is how long this reallocation trend will last. This will depend on management’s ability to get Petrobras beyond this situation so there is recovery before they turn off a large part of the production supply chain.

**Will energy and infrastructure be important for Siemens this year?**

The energy sector has risen in importance because of the electric power crisis. Today we are finally discussing pragmatically what kinds of energy we need in the energy matrix to solve the supply problem. We believe that there is also a good chance that logistics will heat up. No one is calm; no one is sailing in good weather. But sometimes we have the impression that Brazil needs a crisis to take a leap forward; now is the time to jump to avoid being run over.

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