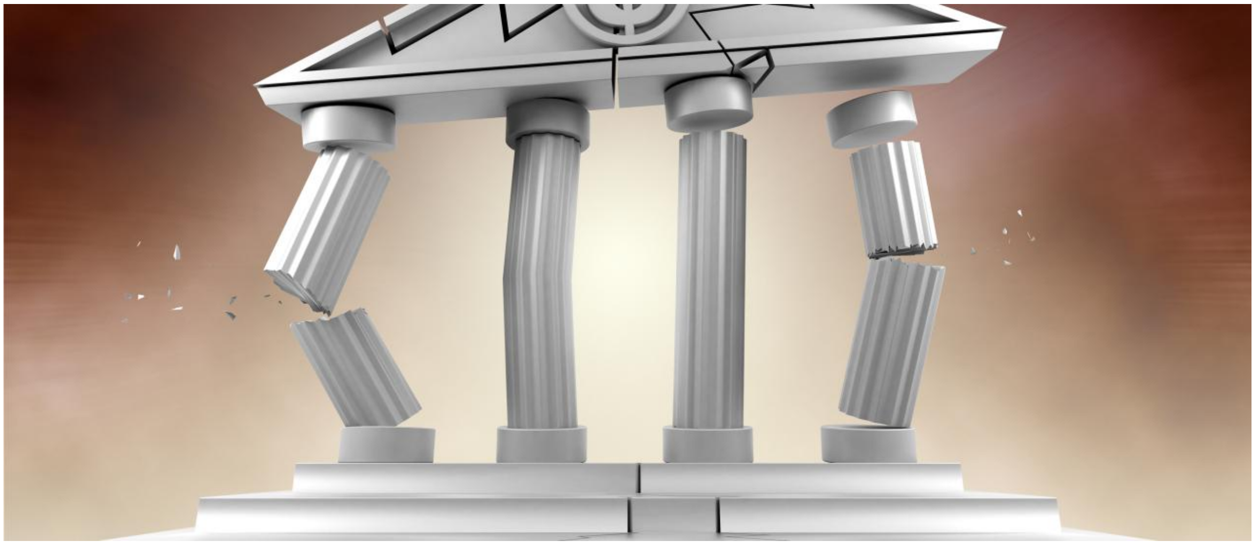
Brazil’s X Factor



By L. Felipe Monteiro , INSEAD Assistant Professor of Strategy

Building business groups too quickly can end in catastrophe.

Eike Batista, Brazil’s former “rock-star” entrepreneur, was the seventh wealthiest man in the world and a “strategic asset” for his country, according to his president. Starting with gold, moving onto iron ore, developing a super port and ending his amazing adventure with oil, Batista earned a fortune incredibly quickly and lost it just as dramatically. His was a story of big dreams and incredible growth. But it’s also a story of hubris and the hazards of growing too quickly, of believing that this growth can create a company that is too big to fail.

The son of a Brazilian father and German mother, Batista began without family wealth but with family connections and education. His father was president of the largest Brazilian mining company.

Batista studied metallurgy in Germany and at the age of 23 began working as a gold intermediary. Within 18 months he had US$6 million in capital and, in 1983, created the first alluvial mechanised gold mine in the Amazon. Batista had logistical issues in the wild west of the jungle – and was even shot – but he persisted and his mine made money. He expanded in 1986 to an even more remote mine in Chilean Atacama Desert. That too was viable.

From 1986 to 2001, he expanded operations into Brazil and was chairman of TVX, a Toronto-based gold firm.

Then things really started to take off.

Building an X empire

After selling TVX in 2001, Batista was back in Brazil. At this time the country was starting to recover from the economic problems which plagued the nation in the 1990s. But there were still many logistical problems – a lack of infrastructure and challenges with labour and finding talent. In 2004, he established MMX to mine ore – assisted by a big loan from a Brazilian bank – and took the company public in 2006, raising US$509 million. Batista continued, via M&As with other mining companies, to move from project to project.

He recognised the need for a large port to get his minerals to customers in China, so when the Brazilian government, which had unsuccessfully approached a number of big companies about developing a site 300km from Rio de Janeiro, came to him with the idea, he leapt at the suggestion. Excited at the prospect of transporting ore he foresaw an even bigger project, creating a huge pipeline and Açu super port. For this he created another company, LLX.

Finally, oil

By 2007, Batista was also investing in Brazil's burgeoning oil industry, creating OGX. Within six months, OGX was ready to make its IPO. It was the biggest public offering up to that time in Brazil, raising US$4.1 billion. Based on exploratory wells drilled between March 2008 and November 2009, the estimated oil and gas reserves mounted from 4.8 billion barrels to 10.8 billion barrels.

But the costs of running an oil company – leasing an oil rig cost more than US$500,000 per day – and enormous investments spread across other diverse business interests were starting to take their toll.

In 2010, Batista offered part of OGX's exploratory fields for sale. No-one was prepared to make an offer and between January and February 2011, OGX stock dropped 20 percent. In June 2012, OGX finally told the Brazilian National Petroleum Agency that they only had a quarter of what was promised and a run on all X companies began.

Finally admitting their oil fields were not economically viable in July 2013, the X business group collapsed. Companies filed for bankruptcy or were put under the management of their creditors.

How do you know when to stop?

In our case studies, **"EBX: Eike Batista and the X Factor"** and **"EBX Group: Autopsy of a Failure"**, we look at what happened to Batista and his business group, considering what could have been done differently. While some would like to blame his downfall on global markets and others claim illegal activity, we look at Batista's fall to earth as an example and wonder for future entrepreneurs: how do you know where to stop?

We see Batista as an incredible entrepreneur; it's amazing how much international support he was able to get. He was working with partnerships and investment from all over the world. He could have limited himself in Brazil, but he had big ambitions.

Emerging market multinationals

Business groups, like EBX, make a very important contribution to emerging markets. They have the power to do things on a large scale and can create infrastructure where none previously existed. Executives are able to take what they learn from one company to benefit other companies in the group. The Indian multinational **Tata** is a great example of how knowledge can be transferred across an organisation: where good managers identified in one company are assigned to lead the next company created or acquired by the group.

The problem EBX had was that the business group was built so quickly the new companies didn't have time to enjoy the benefits of experience. It was almost as if all their companies were starting simultaneously while just one of them, the mining company MMX had revenues. There was no large central company to support the others. By constantly expanding, the entrepreneurial DNA inherent in Batista meant that not enough time was spent executing strategy. While the scale of investment from outside Brazil was impressive, the timing and rapid growth, created a huge business without direction or focus or the ability to move nimbly and efficiently.

Personality or culture

Batista's story holds lessons in hubris and company culture.

In Brazil, he was seen as an icon of entrepreneurship. He was portrayed in the most important Brazilian magazines as the face of modern Brazilian capitalism.

This uniqueness gave him a phenomenal amount of financial support. He had access to investors all over the world for major projects. The opportunities seemed endless. Unfortunately his eagerness to grasp them all at once meant he was unable to make the transition from entrepreneur to general manager.

To run a large business group (including a new oil company) process and diligence are vital. The entrepreneurial culture at EBX meant the focus remained on expansion. For the group to succeed, it needed to transition to an execution-focused culture. This isn't a minor, incremental change, it's a sea change and particularly important in emerging markets where the environment is often volatile and shocks can be abrupt.

And they were. Just as Batista's business group grew at an incredible speed so did it collapse. Left with his overconfidence and his business group's inability to evolve away from entrepreneurial culture, Batista lost his X empire.

Felipe Monteiro *is Assistant Professor of Strategy at INSEAD.*

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About the author(s)

L. Felipe Monteiro is a Senior Affiliate Professor of Strategy at INSEAD and the Academic Director of the **Global Talent Competitiveness Index**. He is the Programme Director for INSEAD's **partner programme** with Fundação Dom Cabral, Advanced Management Program.

