

THIRD EDITION

# GOING GLOBAL FROM LATIN AMERICA

## THE ARCOR CASE

Bernardo Kosacoff - Jorge Forteza - María Inés Barbero  
Fernando Porta - E. Alejandro Stengel



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Prologues by:  
**Arnoldo C. Hax**  
**Juan J. Llach**

# **Going Global from Latin America**

The Arcor Case



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Third updated edition

**Bernardo Kosacoff**

**Jorge Forteza**

**María Inés Barbero**

**Fernando Porta**



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## **Going global from Latin America. The Arcor Case**

### **Third edition**

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## NOTE TO THE THIRD EDITION

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In this third edition of “Going Global from Latin America. The Arcor Case” a fifth chapter has been added. It describes the most relevant events of the company within the macroeconomic context from 2001 to 2012. It is worth mentioning that the substantive information and analyzes of the previous chapters have not been modified.



## PREFACE FOR THE FIRST EDITION

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Coinciding with one of the most significant moments in the life of our company, our 50th anniversary, these pages bring together details of ARCOR's rich history and evolution.

Proud of the achievement that is meriting this recognition, my wish here is simply to express gratitude:

Gratitude to all those who have worked or are working for ARCOR, and to their families, because our splendid team of workers have been the real strength behind the building of this company, and it is they who are responsible for its current success.

Gratitude to our consumers, who over the years have rewarded us with their preference, stimulating us to continuously improve our products and grow in Argentina, the region and the world.

Gratitude to all those companies and persons, whether public or private, who have worked and collaborated with us, because their confidence has enabled us to demonstrate that in Argentina and in Latin America, growth is possible.

And in particular, gratitude to that group of pioneers whose tireless search for growth and faith in the potential of our people has allowed us to cross frontiers around the world, taking advantage of the opportunities that have opened up as a result of globalization. In effect, the major achievements recorded by ARCOR in the last decade have continued along the path outlined by those pioneers, and in particular by that visionary Fulvio Salvador Pagani, my father, who guided the fortunes of the company until the end of 1990.

Since our foundation, the aim has been to contribute as far as possible to the progress of the country and the region, fulfilling our mission to help improve the quality of life of our peoples.

This book records the road we have traveled up to the present, and provides an indication of the course we will follow in future.

**Luis Alejandro Pagani**

*President of the ARCOR Group*



## P R O L O G U E

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*Going global from Latin America —The ARCOR case—* is a much needed and welcome contribution to management literature —both for the general business and academic audiences. This is so because it documents one of the most unique evolutions of a successful firm in Latin America. In the United States, where I have resided for the last thirty years, firms acquire real respectability when they break the barrier of \$1 billion in sales (one thousand millions in the Latin American measurement system). This goal, which is greatly aspired to by enterprises which want to assume real leadership in the world, is exceedingly difficult to realize and was achieved at ARCOR in 1999. It necessitates tremendous managerial competences, tenacity, a compelling vision, and firm strategic direction. Achieving this goal in a national company in Argentina, whose environment has been characterized by severe economic, political, and social turbulence is an extraordinary feat. For any Latin American firm this is the cause for both celebration and deep reflection, which is what this book is all about.

The uniqueness of the case is even more dramatic when we study the origins of ARCOR. We have to pay the deepest respect to the determined and extraordinary Pagani family who had a big dream and was able to convert it into a spectacular reality. They chose what at first sight seems a precarious location in Arroyito as the starting point. They transformed what could have been extremely unlikely conditions for the development of a world-class business into the foundations and the roots of its success. The critical assets of Arroyito was the presence of the Pagani family and their circle of friends that would convert this town into a vibrant engine for ARCOR's development.

The book admirably covers ARCOR's evolution from its modest origins to its legitimate claim to be a global corporation. The Four ARCORS described in the book constitute a model of enormous relevance for Latin America. This evolution is described using the most relevant academic frameworks, which adds to the quality of the presentation and makes it very appealing for possible classroom use.

ARCOR is exemplary not only for its economic success, but also for the fact that this is based on its industrial and technological competences — something which is rare on the Latin American managerial stage.

At the same time ARCOR has exhibited unmatched commitment to social responsibility which is also a rare quality in our hemisphere. Much of this is an expression of the values of Don Amos —the Patriarch of the family—, Fulvio Salvador —the Founder of ARCOR—, and his son Luis Alejandro —its current President.

The Pagani family has not only given us lessons in how to conduct a successful business practice, but they stand also as an example to other executives who have rushed into selling their firms to multinational corporations, reducing the national patrimony and risking a lack of alignment between business and national interest. The authors should be congratulated on carrying out this exciting project with impeccable professionalism.

**Arnoldo C. Hax**

Alfred P. Sloan Professor of Management  
Massachusetts Institute of Technology

## PROLOGUE FOR THE FIRST EDITION

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### **LET A HUNDRED ARCORS FLOURISH**

Argentina has just three large-scale industrial companies operating internationally, and one of them is ARCOR. If instead of three, there were to be thirty, or, why not, even one hundred, there would be no exhausting external and internal debate about the competitiveness and capacity for growth of the Argentine economy. Such is the strength of the leverage that sound companies exert on macroeconomic conditions.

Unfortunately, the reality is otherwise, and so two key questions arise. The first is how it was that ARCOR and its two colleagues became possible. The second, similar but not identical, is why there are not thirty or even one hundred ARCORS.

The book you are holding provides valuable answers to these questions. Nevertheless, the mystery will still remain after you have read it, through no fault of the authors, but rather because of the nature of the subject. Since Keynes coined the phrase “animal spirits” in reference to the deep underlying motives of entrepreneurs, and Schumpeter referred to their “creative destruction”, the theory of economic growth has been unable to clearly establish their determinants. If it is difficult to identify growth factors at macro level, how much harder will it be to determine them from company histories and macro level growth in general.

Explaining ARCOR therefore belongs to the field of atomic and sub-atomic economics and its interaction with society and culture, and is still not properly developed. All the institutional and behavioral bibliography used in this book, which has been essential in unraveling the history of the company, mostly dates back over the last fifteen years. When the true micro roots of macro growth are discovered, we will be in the presence of a revolution in economics of positively Einstein-like proportions, which will no doubt be worth a Nobel prize to its discoverers.

In Latin America, furthermore, our macroeconomies are sick. Certainly because our macroeconomies suffer from almost chronic ailments, but also because our energies have been centered on it to excess; as if we were hoping for a macro miracle that would cover up or repair all the mistakes and neglect



at microeconomic level. Hence the importance of this book, which shows that success is possible, and just how it is possible.

To understand ARCOR, as the authors have done, it is necessary to see both the text and the context. In the period under review our context was that of “magic Latin American realism”. As I outlined in “Another century, another Argentina”, this magic realism consists of considering that “the State” can in itself generate wealth, taking it from some place outside civil society. One of the consequences of the social practice of this belief was the creation of a society based on unearned income. Firstly income from the land, then state hand-outs and inflation itself. This created a society that did not plan for the future, being excessively short-term in its outlook.

In short, this was a context almost diametrically opposed to that needed for the birth and development of companies such as ARCOR. For this company to arise a form of counterculture was necessary, and this was the case in point. This is a story of sons of immigrants, creative and hard-working, with the outstanding figure of Fulvio S. Pagani as an emblem. Only children of immigrants imbued with a culture entirely contrary to the search for income (although knowing how to take advantage of it), a culture derived from a poor or overpopulated land, based on planning for the future and deferred gratification that led to work, saving, education and investment, were able to attain such achievements.

However, these are but modest hypotheses. Readers will find more precise answers in this book. Nevertheless, the questions as to why ARCOR, and why there are so few ARCORs, will continue to invite us to further study in the search for the keys that will turn the wheels of growth.

The ARCOR case is without a doubt outstanding, and beyond the celebration of the fiftieth anniversary, the publication of the book is very timely to ensure its history is known, and hopefully emulated. It has been a great honor for me to contribute with these brief lines to evoke the pioneers that created ARCOR, and all the entrepreneurs and workers that have contributed to its development. To all of them, as well as to the authors of this book, my warmest congratulations.

**Juan J. Llach**

*Director, Economics Department,  
IAE Universidad Austral*

## **Why is the ARCOR Case of Interest to Both Managers and Academics?**

Argentina is a country at an intermediate stage of development that is of particular interest to students of developing economies. There is abundant bibliography on the Argentine case, most of which attempts to explain why a country which in the first half of the 20th Century was considered to possess a vast potential for development should have performed so poorly over most of the last fifty years. In the context of an economy and a society that have gone through half a century of turbulence, losing ground in relation to other nations, it is important to analyze the behavior of its private sector, one of the keys to any explanation of such a performance.

At the end of the 20th Century, Argentina lived through a decade of major transformation of its institutions, accompanied by several years of growth and renewed hopes for the future; these changes are again coming under strong scrutiny. During that period, markets were opened up and the economy was deregulated, at the same time as the country experienced a major inflow of multinational corporations and a transfer of ownership of local companies on an unprecedented scale.

A significant proportion of Argentine business owners chose to sell their companies and find new uses for their assets. Few business groups decided to maintain their independence and develop as enterprises with global ambitions: ARCOR is one of the most significant exceptions. At the very moment multinational companies from emerging economies are attracting the attention of international researchers, the history of ARCOR has taken on particular academic interest. The case of ARCOR is also of relevance to those developing public policy, students of business strategies and those in charge

of implementing them, as well as to a wider public interested in recent history in general.

This book intends to provide an answer to the following basic question: By what means did a modest industrial undertaking set up by a group of descendants of Italian immigrants in 1951 survive and prosper through fifty years of political and economic turmoil, growing into a corporation with annual sales of \$1.1 billion employing approximately 13,000 people —30% outside its country of origin— exporting products worth over US\$ 200 million to over 100 countries? The research offers findings and conclusions that justify interest in the ARCOR case. Attempts to answer the question “how was it done?” point to a series of key aspects of particular relevance in illustrating this success:

- As always, in the beginning we have the entrepreneurs, a highly motivated group with complementary experiences and abilities, charismatic leadership, knowledge of the market in the interior of the country and the industry, as well as technical and engineering skills.
- During the various stages in the building of the company and throughout the succession of political and economic upheavals that Argentina has experienced, there was a constant commitment to ensure growth, investment and independence. Even at the most unfavorable times, the shareholders continued to innovate, acquiring machinery and investing, a behavior with few equivalents in the business community.
- During its strategic evolution, ARCOR focused on the search for positions in the market that tended to avoid direct confrontation with companies that were larger or which had greater fire-power. Whether faced initially by large domestic corporations or later by multinational corporations, ARCOR followed a policy of intelligent, indirect competition.
- Throughout its history, ARCOR has always been a company with a strong industrial and technological culture. From its early days in a closed economic environment, through a succession of attempts to open up the country's economy, the shareholders have regularly added state-of-the-art equipment and technology, developing the skills necessary to adapt them to local conditions and even to improve on them.
- The development of ARCOR has followed a series of stages making up what has been defined throughout this book as “the Four ARCORS”. Gradually coming to dominate the market in the interior of the country, the company then began to attack the Greater Buenos Aires market, subsequently starting to export and spreading throughout South America. Its

expansion strategy is another of the aspects of interest in the study of the ARCOR case.

- At the same time, ARCOR was able to make a successful transition from an informal model and culture based on strong personal leadership to a more complex management model that has been successful in attracting and developing Argentine and (gradually) international talent.
- Like many other domestic companies, ARCOR learned how to take advantage of the policies which provided for the support of industry by the Argentine State at various times over the last 50 years. It is interesting to analyze the contribution of these policies in the development of ARCOR as well as to explain why a company that was ranked 106th on the leading companies' list in 1973 (part of an extensive group of companies enjoying the same advantages) should end the century in the 26th place in the ranking, being one of the few domestic capital companies to retain its independence and preserve its strategic viability.

The story of ARCOR, like that of any other company, is the result of the interweaving of several interdependent histories. It is firstly the story of the people and the groups of people that have made it possible: the founders, owners, managers and workers of the company. It is also the story of social interaction, the relationships that developed between its components over time and the building of an identity and a culture, as well as the specific knowledge and skills on which its competitive capacity is based (Nelson and Winter, 1982).

It is also the story of a management structure (Williamson, 1989) which provided the environment for developing different strategies for growth and adapting to the conditions of its context: increased scale of production, vertical integration, diversification of production, building of a distribution network, search for new markets and the international expansion of the business. It is at the same time the history of a bureaucratic institution—in the sense defined by Weber—with a structure and functional organization that must match the strategies, dimensions and administrative complexities of the company (Penrose, 1959; Chandler, 1962, 1987, 1996).

It is a story to be measured and evaluated according to results and those elements and factors that have conditioned them. In so far as all companies have as their principal purpose the achieving of profit—although other motivations may also exist—their story must include their sources and methods of accumulating shareholder value and obtaining financing, specifically their evolution and performance. It must delve into the reasons for their successes and failures, interpreting them on the basis of internal strengths and weak-

nesses, as well as external factors that have nevertheless been of considerable relevance.

The story of an individual firm or business conglomerate cannot be understood in isolation from the environment —local, national, regional, international— in which it operates. The environment provides resources and opportunities, but also generates difficulties and restrictions affecting the development and growth of companies. Hence the need to consider, among other conditioning factors, the macroeconomic context, public policy, economic institutions and rules, characteristics and conditions of competition in the various markets, the productive and business structure and even the actions of competing firms.

As a result, this presentation of the “ARCOR story” is based around the dynamics of the growth of the firm, the identification of various successive stages of development around a predominant strategy and analysis of the circumstances, both internal and external, that have provided support to its development. Reconstruction of its development implies the need to identify the keys to growth over five decades on the basis of a perspective that considers not only its microeconomic behavior, its actions and decisions, but also the opportunities and the obstacles provided by the changing economic context in Argentina in the last fifty years.

The history of a company can also offer more than mere information on the events and reasons for its development. This history of ARCOR has been undertaken as a contribution to discussion of more general aspects of history and economic analysis.

It proposes to cast light on the modern history of industrialization in Argentina from a microeconomic perspective, based on the transformations that have taken place in the productive process and the organization of the firm, over a lengthy period covering the rise and fall of the import substitution model, the crisis of the Development-oriented State and the decline into hyperinflation, followed by the introduction of rules for an open, deregulated economy. Company histories and the picture from inside the enterprise provide views of aspects not generally covered by a more general panorama of reality, hence the originality of this contribution. Analysis of personal relationships, technology choices, management models and long-term strategies help to explain in greater depth the events and characteristics of the domestic economy.

Another particularly relevant field is that of the relationship between the macroeconomic contexts and enterprises, especially in external conditions that are highly unstable, such as those prevalent in Argentina over the whole period considered (Kosacoff, 1998 and 2000). One central premise of the

approach adopted is that responses by firms are not pre-established or mechanical and are not at all uniform. Any reading of the situation that does not highlight this variety of strategic responses will of necessity only offer a simplified and distorted view of reality. In this field, analysis of the ARCOR case may serve for discussion of both the processes and the strategies for the adaptation by companies to changing contexts, such as the nature of the relationship between the State and companies in contemporary Argentina.

From a historical perspective this case also offers valuable empirical evidence for the understanding of the birth and development of diversified economic conglomerates within the Argentine economy, where they have since become leading players. It is important to explain the reasons why, as in most late developing countries, “economic groups” have appeared as the most frequent format of major corporations. At the same time it is particularly relevant to establish why some take the form of conglomerates with diversified investments in sectors and areas that are unrelated technically and economically, while others on the other hand specialize in more narrow or related business areas, centered on a particular industrial activity.

Lastly, but no less significantly, histories such as this provide both their actors and readers with elements for reflection on the present and on the future. Obviously, no single individual case can be presented as a guide for action, nor can it provide grounds for a set of “best practices”, but there can be no doubt that analysis of such a case can be a source of information and conclusions that will foster debate and lead to improved practices and strategies. In this regard, a company history can also be a tool for use by business managers and leaders as well as public policymakers.

As this book is concerned mainly with a specific company, it is necessary to point out that the analysis outlined does not emerge out of —nor is it grounded in— any single line of theory. This is not just the product of a decision by the authors, more probably deriving from the fact that the field generally defined as the Theory of the Firm represents and combines various conceptual frameworks and cannot strictly be considered as an integrated corpus of theory on its own. Once the assumption and vision of a company as (always and only) the optimum combination of productive factors and perfect information to maximize results is discarded as simplistic and unrealistic, the field for debate is opened wide. Contribution to this debate will come from different approximations, formulated from approaches based on both company and institutional histories and economic and administrative theory.

Such approximations take into account the fact that the technical information summarized by the production function is not sufficient to provide an

understanding of the decisions and the evolution of a company (Tirole, 1990). Capacity for interpretation increases if a company is considered as an agent made up of other agents, as an organization with an inner life of processes that resolve repeating problems in a current manner (Hamel 1994). However, this approach in itself is incomplete; it must also be recognized that a company has the potential and ability to break out of its own inertia by means of the introduction of innovation and strategic changes. This would appear to be the key to an understanding of the reasons why not all companies behave or react in the same way to the same stimuli or contexts.

It is therefore valid to investigate the determinants of a company's configuration. Knowledge, even if only partial, as to why a firm tends to adopt some features and not others, in other words, information on its nature can provide an indication as to how it processes information and resolves problems. This "institutionalist" focus (Coase, 1937 and 1994; Williamson, 1975 and 1989; North, 1993), based on the concept of transaction costs and the alternative of either using or not using the market as the organizer of transactions, provides elements for reflection on the limits and the size of the firm on the basis of its function (producing or trading) and how it carries it out (the most economic manner of doing both things). However, this approximation is weak and unsuitable for dynamic consideration of the reactions of the firm over time in the face of unexpected changes in the environment.

The so-called "evolutionist" approach contributes to a more dynamic interpretation (Nelson, 1982, 1991 and 1996; Dosi, 1988). It considers that a firm is a combination of agents and resources and a network of interaction between them, with the ability to generate changes and adapt to them, following a trajectory that conditions it on the one hand and provides teachings and skills on the other. At the same time, this approach admits the inclusion between the skills and the attributes of the firm of the figure of the entrepreneur, the treatment of which is always difficult to set within a system. Evolutionists consider that it is such specific knowledge and accumulated experience that guides strategies and performance of companies, and —based on the groundbreaking ideas of Schumpeter (1983)— that their capacity for innovation is the principal source of their competitive advantages.

The ability of a company to formulate alternative strategies is therefore at the heart of the matter. Economic agents move in an environment of uncertainty, and their response is based on the design of strategies (Dixit and Pindyck, 1994). The range of strategies available to a company at any given moment is neither infinite, nor is it limited to a single option. However, it can be considered that the visible range of practical strategies will depend



on the company's evaluation of the most likely scenario and exactly what it considers itself capable of doing. It is not surprising therefore that in the face of conditions with uncertain outcomes, companies with different levels of capability should adopt different strategies. This book analyzes the successive strategies adopted by ARCOR, linking them to the evolution of its capacity to plan, decide on, implement and revise such strategies.

The globalization of companies in emerging economies is a growing phenomenon and source of increasing analytical interest. During the 90s, Latin American countries in general and Argentina in particular have played an active role in foreign direct investment (FDI), mainly as a destination but also as its source. It is estimated that companies and corporate groups from Argentina, Brazil, Chile and Mexico have invested some US\$30 billion outside their own countries during this decade. Evidently the consolidation of structural reforms and improved macroeconomic performance compared to the previous decade have helped redefine both the advantages of locating in those countries—which explains the size of the inward FDI flows—and the advantages of ownership by their companies—which in part explains their own process of productive globalization.

The first wave of outward foreign investment by Latin American companies had in fact taken place in the 50s and 60s. It mostly involved companies that were intensive users of natural advantages and, to a lesser extent, industrial companies that had successfully been gone through the import substitution phase and were carrying out marginal investments abroad. These undertakings were centered on other developing countries. In the 80s the countries of south-east Asia led a second wave of investment from developing economies, in this instance based on industrial skills and, unlike previous examples, also diversifying into developed countries.

Researchers have followed these movements and produced hypotheses to explain them. In the tradition of the product cycle theory, Wells (1983, 1986) has suggested that companies in developing countries are in a position to make use of their advantages in mature sectors and developed technology, which can be exploited in even less developed economies. Lall (1983) for his part has coined the concept of "localized technological change" to propose that companies in developing countries are better able to adapt their products and processes to the conditions in those countries, and are thus able to expand their activities into other similar economies.

While they accept this relatively evolutionary vision of the development of skills by companies, Cantwell and Tolentino (1990) state that such firms not only develop advantages from the use of techniques that have been for-



gotten in developed countries or have been better adapted to the conditions in developing countries, they do so following an innovative and relatively independent path, based less on science or R&D and more on various aspects of organizational knowledge and production and engineering technology. In turn, as part of their own process of globalization, these firms have built up new capabilities and skills in a typical learning-by-doing process.

Dunning (1988, 1997) has outlined a theory on the “development path of investments” claiming the existence of a link between the status of a country as a beneficiary and source of FDI and its level of economic development. As they develop along this path, countries will pass through various stages in their process of becoming international, evolving from being net beneficiaries to becoming a net source of FDI. In an intermediate stage, on the basis of the advantages provided by the country itself and on other advantages particular to the local firms themselves, they will develop an international strategy with a strong regional component (neighboring markets that are relatively similar), while at the same time including a growing global base that also involves significant and growing investments in developed countries.

The wave of investments abroad by Latin American companies in the 90s could be a reflection of this pattern. In general, the industrial firms involved did not participate in the investments made in the 50s and 60s, being relative latecomers in regional markets. In addition to their own skills, the impulse for this greater international presence was based on their dominant position in their relatively narrow domestic markets, on their improved access to voluntary credit markets, and on the search for improved scale, efficiency and quality to which they have been driven by increased competitive pressure.

The principal motivation of such companies has been to seek wider markets or those with strong growth potential, and with only a few exceptions, it has not reflected advantages closely linked to innovative or leading edge capabilities. The main attributes of these investments have instead been associated with management capabilities, the mastering of familiar process technology, an efficient quality and production management or strong sales and distribution skills. At this stage, therefore, companies tend to expand internationally as part of a necessary restructuring process aimed at consolidating competitive position in more accessible and open markets. The international expansion of the productive activities of the ARCOR Group can be placed within the context of such an analysis.

This book has been structured with the aim of presenting explanations on the ARCOR case from different angles, and has therefore been divided into four chapters with different objectives and themes:

- The first chapter: “ARCOR: fifty years building competitive capabilities” provides a summary of the development of the company. It begins with an outline of the methodological approach adopted —based on the interaction of factors from the political and institutional environment, the competitive dynamics of the industry, the intent of the shareholders and key actions— and then reflects on the performance and strategies of the company. It concludes with a series of findings that can be derived from the ARCOR case.
- The second chapter: “The early foundation to dominant local company: 1951 to 1990”, provides a detailed analysis of the first forty years of the company’s development. In particular, it presents a review of the factors and conditions that resulted in the transformation of ARCOR from a small single-production undertaking into a leading industrial conglomerate.
- The third chapter, “Building a regional company in a context of institutional transformation: the experience of the nineties” presents an in-depth analysis of ARCOR’s response to the abrupt change in the conditions for competition in Argentina in the 90s. Detailed examination is made of the strategic and operational responses adopted and the results achieved, contrasting them with the performance of the economy as a whole and the dramatic process of sales of national companies to international players.
- The fourth chapter: “Looking to the future: building a global enterprise from an emerging country” is an attempt to project ARCOR forward, presenting the outline of a “strategic agenda” for the development of the next stage of development of the company. In undertaking this effort, the author’s ambition was to contribute an analysis that meets the needs of both general readers interested in topics related to the development of Argentina and students and researchers seeking to understand the link between macro and microeconomics and specific business development strategies.
- Finally, the fifth chapter of this edition describes the Arcor case within the framework of the deep changes taking place in the regional scenario: from crisis management and the successful adaptation to the new Argentine economic context, to its integration into MERCOSUR and ARCOR’s business development in Brazil and the rest of the world. ARCOR’s evolution offers, once more, a model to be copied and key factors for the successful management of local and regional companies in developing countries that have to face challenges in increasing competitive contexts.



# CHAPTER 1

## ARCOR: Fifty Years Building Competitive Capabilities

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*Collaborators: Fernando Porta  
and María Inés Barbero*

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## **ARCOR TODAY. THE STARTING POINT FOR THE BUILDING OF A GLOBAL COMPANY**

In order to describe and understand a company's history and its performance it sometimes helps to begin at the conclusion, illustrating first where the company stands at present. A clear, precise image of the point reached provides a reference for each moment or landmark in its history and the establishing of the logic in its construction and the strategies that brought the process to its current state. A description of what makes up ARCOR today and where it stands is provided below.

In the first place, ARCOR is one of the few multinational groups made up of exclusively Argentine capital currently in existence. It is also the world's largest producer of hard candy, the leading candy exporter in Argentina and the Mercosur and the leading exporter of hard candy from Brazil.

Total group sales reached US\$1.1bn in 2000, 34% of which coming from its plants located abroad. Exports amounted to US\$217 million, going to a diversified total of 105 countries. It employs a total of thirteen thousand people in its various plants and enterprises, investing over US\$900 million during the 90s in the purchase of new plants, replacements and expansion of processes and the incorporation of new technology. This has resulted in a daily output of over 1.5 million kilograms of products, made up of some 1500 different items.

At present, the world candy market is worth some US\$ 100 billion and is at a relatively mature and stationary stage. As a result, competition between the main manufacturing groups is severe, and the challenge consists of creating and introducing successful new products, maximizing efficiency in plants and in the corporation in general and increasing penetration in existing markets. The market is relatively concentrated, the three largest producers (Nestlé (Switzerland) and Kraft Foods and Mars (USA)) being of similar size and accounting for 30% of sales world-wide. They are followed by a second group of eight companies (from Europe, the US and Japan) with a sales level of between US\$2bn and US\$5bn. In this ranking of the top 100 candy producers world-wide<sup>1</sup>, ARCOR ranks thirteenth at October 2000 and is the top-selling company in Latin America and all other developing countries, as well as being the only company that has diversified into all confectionery categories covered by the survey.

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<sup>1</sup> Prepared by Candy Industry Magazine (USA).

The ARCOR group currently operates 31 industrial plants, mostly using state-of-the-art technology, with manufacturing mainly falling into four large product groups: foodstuffs, confectionery, chocolates and crackers and cookies. In foodstuffs, it is the leading producer in Argentina of jams, corn meal and corn oil. In confectionery, it manufactures an extensive range of candies, chewing gum, nougats, lollipops and tablets. Outstanding aspects of its chocolate goods business include the plant at Colonia Caroya in Córdoba, Argentina, named Food Plant of the Year by Food Engineering International in 1994, and the new manufacturing installations completed in Bragança (Brazil). In crackers and cookies, an industrial plant making use of the latest technology located at Salto (Buenos Aires, Argentina) produces a wide range of wafers, fruitcake, snacks and buns, making it the second largest producer in the Argentine market, situated between the two largest multinationals in the segment.

ARCOR's production footprint is extremely diversified in Argentina and the Latin American region. In Argentina it has 25 industrial plants distributed in the provinces of Buenos Aires, Córdoba, Santa Fe, San Luis, San Juan, Mendoza, Tucumán, Catamarca and Entre Ríos. The remainder of the facilities are located in Brazil (Rio das Pedras and Bragança Paulista), Chile (Los Andes and Santiago) and Peru (Chancay). In support of its strategy for penetrating export markets, ARCOR has also opened sales offices in the USA, Canada, Mexico, Colombia, Ecuador, Paraguay and Uruguay.

Probably the most outstanding microeconomic characteristic peculiar to ARCOR is the extent and depth of the vertical integration of its production process, which in turn represents one of its principal differentiating attributes and competitive advantages. ARCOR has become actively involved in "upstream" activities related to its core business: container manufacture and the development of agro-industrial activities such as sugar, milk, glucose and fructose production. As a result of the growth of these activities, ARCOR is currently the largest manufacturer of corrugated cardboard and the largest printer of flexible packaging in Argentina.

In other words, from the production of raw materials and basic input through manufacturing of a wide range of different genetic categories of products, until the process is concluded with the final packaging, all aspects of the process are under the effective control of ARCOR. This integrated process coordinates autonomous production units certified under international quality standards such as ISO 9000 and ISO 14001 environmental standards. In turn, these standards serve to support the competitive capacity of the firm in the Argentine market and penetration in more complex and sophisticated markets.

It is precisely this diversification of its export markets that represents another of ARCOR's distinctive features. Leading regions and countries buying from ARCOR in addition to the Latin American region include the US, Saudi Arabia, Japan, China, Russia, India, Israel, Africa, much of the Far East and the European Union. This market diversification process is the result of an aggressive strategy over an extended period.

The great diversification of products and markets in Argentina is based mainly on a very effective sales and distribution structure, and is without doubt yet another of the competitive advantages of ARCOR. At present it has 160 official distributors and in total over one million visits a month are made to their customers.

This up-to-date snapshot represents far more than a cross-section at a given moment. It is the expression of an accumulation of practices, experiences, strategies and the effects of the interrelation with the economic, political and social context throughout the history of the company. That is why this history is important, and why it must be told and analyzed.

### Basic Data on the ARCOR Group

Variable	Date	Value
• Total sales	2000	US\$ 1.1 billion
- Sales in Argentina	2000	US\$ 703 million
- Sales abroad	2000	US\$ 397 million
• Consolidated investments	1992-1999	US\$ 906 million
• Exports to 105 countries	2000	US\$ 218 million
- Exports to South America	2000	US\$ 132 million
- Exports to the rest of the world	2000	US\$ 76 million
- Inter-group exports	2000	48%
• Employees	December 2000	13,000
• Industrial plants	2000	31
- Plants in Argentina	2000	25
- Plants in Brazil	2000	2
- Plants in Chile	2000	3
- Plants in Peru	2000	1
• Sales Offices abroad	2000	8
• Distributors	2000	160
• Daily production capacity	2000	1,500,000 kg
• Number of products manufactured	2000	1,500 items



- World's leading producer of hard candy
- Principal exporter of confectionery in Argentina and the MERCOSUR
- 13<sup>th</sup> in the *Ranking by Sales* for world confectionery manufacturers in 2000
- Brazil's leading confectionery exporter
- 1<sup>st</sup> Place in the *Ranking by Sales* for confectionery manufacturers outside the OECD in 2000
- Integrated production process for the manufacture of confectionery, chocolates, crackers and cookies and other foodstuffs
- The leading manufacturer of corrugated cardboard in Argentina



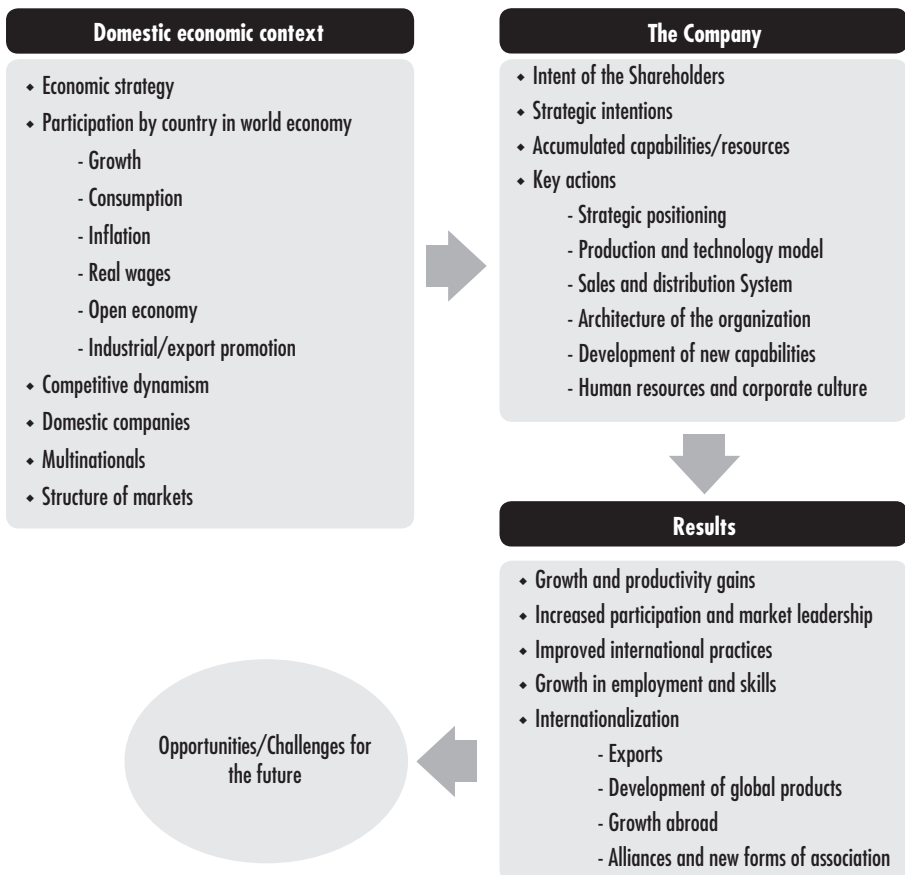
Rank	Company Name	Number of Plants	Number of Employees	Net Sale	Chocolate Bars	Moulded Chocolate	Enrobed Chocolate	Panned Goods	Soft Candies	Chewing Gum	Jelly Beans	Lollipops	Caramel	Licorice	Toffee	Gummies	Jellies
14	The Life Savers Company Parsippany, New Jersey	16	3N/A	1,000			✓	✓	✓	✓	✓					✓	✓
15	Stollwerck Aktiengesellschaft Cologne, Germany	N/A	2,721	932	✓	✓	✓								✓		
16	Lindt & Sprüngli AG Kilchberg, Switzerland	8	5,615	833	✓	✓	✓										
17	Lotte Confectionery Co., Ltd. Seoul, South Korea	N/A	N/A	781			✓		✓	✓							
18	Ulker Gıda Sanayi İstanbul, Turkey	2	7,000	600	✓	✓	✓			✓				✓			
19	Franz Zanetti GmbH & Co. Aachen, Germany	N/A	1,450	584			✓										
20	Brach's Confections Chattanooga, Tennessee	3	N/A	500				✓	✓			✓		✓		✓	
21	Elite Industries Ltd. Ramat Gan, Israel	1	7,000	500		✓				✓							
22	Russell Stover Candies, Inc. Kansas City, Missouri	6	6,021 Co	464	✓	✓	✓										
23	Chocolaterie Bouquet D'or S.A. Villeneuve D'Ascq, France	1	300	440		✓				✓							
24	Chupa Chups S. A. Barcelona, Spain	8	1,950	429.5													
25	Tootsie Roll Industries, Inc. Chicago, Illinois	6	1,000	396.7			✓		✓								

Source: Candy Industry, October 2000

## BUILDING THE HISTORY OF A BUSINESS. METHODOLOGICAL APPROACH

The international literature on the subject of corporate history, as well as the evolution of strategic thinking on company development (from the pioneering work of Alfred Chandler [1962, 1977, 1990] and Kenneth Andrews [1980] to the recent developments by S. Goshal [1997], R. Grant [1999] and P. Ghemawat [1999]) both point to the need to use a methodological focus that allows for the construction of a logical historical sequence and the explanation of the causal relationships between a series of determinant factors and the results obtained by the companies. In this instance, we have started from a summary of strategic thought to develop an analytical structure capable of interpreting the various stages in the evolution of ARCOR.

The outline used, shown on Table 1-1, is made up of four basic dimensions:



- The context: the institutional and economic “environment”
- Critical decisions taken by the company in the period under analysis: The competitive response
- Resulting performance
- Lastly —following the dictum of N.Tichy (1990) of “the past as a prologue to the future”— the situation of the company at the end of the period and the opportunities and challenges it faced for its subsequent development.

### **a) Context or Institutional and Economic “Environment” of the Country**

Most frameworks for strategic analysis coincide on the importance of analyzing the conditions of the environment that constrain or offer opportunities for the development of a company. The fundamental dimensions that are usually analyzed are as follows:

#### *The Institutional Situation of the Country and the Strategy Adopted*

ARCOR’s fifty years of development cover an extremely turbulent and agitated period of Argentine history. ARCOR took its first steps when Juan Domingo Peron’s first period of government was reaching its peak, in the framework of an economic strategy aimed at development based on the growth of the domestic market and support for local industry. Over the next fifty years, Argentina became a text-book case due to the evolution of its institutional context (periods of limited democracy, military governments and a recovery of democracy) as well as by the number and variety of different economic policies that were adopted. It is important to analyze for each period just how such institutional frameworks and economic policies have created opportunities or constraints affecting the development of the company. In particular, the impact of the following variables should be considered:

- Economic growth recorded during the period.
- Evolution of real wages, determining the evolution of consumer demand directed towards the company, as well as the behavior of its production costs.
- The behavior of inflation, due to its impact on real wages and the evolution of the real levels of other key variables such as the exchange rate, financial costs and the cost of services.
- Policies regarding openness to trade. This policy area should be analyzed from two standpoints: the level of protection that existed against the import of competing finished goods, and the level of protection for the importing of input, capital goods and new technology. The combination of these factors is reflected in the effective protection level, as well as leading to differing behavior regarding production and decisions to invest in new equipment.
- The possibility of gaining access to new technologies and their cost.

- Access to financing and its cost. Over these fifty years there have been dramatic changes in the level of access to credit (and its cost) for Argentine companies, with a switch from real interest rates that were low or even negative towards the end of the 70s, accompanied by strong subsidies from the public sector, to schemes involving the disappearance of subsidized credit and a high cost of financing. These changes have a strong impact on investment and borrowing decisions taken by the shareholders.

### *Competitive Dynamics of the Sector*

Having established the environment faced by the company, a more detailed analysis is required regarding the competitive dynamics of the sector or industry in which the company performs. This analysis is built on the following methodological basis:

- Analyses of the dynamics of industry, such as put forward by Michael Porter (1981) in his studies on the “Five Forces” and recent developments on the subject by Ghemawat (1999).
- Analyses based on different theories of business, particularly those related to the “Resource View of the Firm” (Collis and Montgomery, 1997) and those that view enterprises as a conjunction of economic rules for decision-making (D. Besanko, (2000), S. Oster (1999) and Brickley et al (2001).
- More recent analyses on the strategies of multinational businesses and their interaction with local companies in the context of processes of institutional transformation in emerging countries, in particular the notable contributions from T. Khanna (1997), C.K. Prahalad (1998) and N. Dawar (1999) and contributions from analysts of the development of multinationals and local groups (Gingrich, 1999 and Forteza, 1997 and 1999) and Latin American experts such as Bassi (2000).

In this area of analysis, we should be looking for answers to the following questions:

- How have the conditions of the context affected the evolution of the industry sector?
- How do value creation conditions arise from the interaction of suppliers, consumers and competitive rivalry?
- Which are the strategies that can be identified, and how are they defined?
- Which strategies were winners and which were losers?
- How can the strategy of multinational companies be interpreted? What have been its successes and failures?
- How did local companies react and defend themselves?
- How are markets evolving?
- How are distribution channels changing?

## **b) Critical Decisions Taken by the Company: The Competitive Response**

The two determinants previously analyzed—institutional and economic environment and the dynamics of the business sector—provide the backdrop to the actions taken by shareholders and senior company management. In this part of the analysis it is important to focus on the following subjects:

### *What were the Aims and the Aspirations of the Shareholders?*

As will be seen later, family enterprises are above all a reflection of the psychology and motivation of their founders. In general, in the early days there is a strong intent by the founder or founders to create an independent business project. It is therefore important to study these entrepreneurs to understand their motivations, skills and limitations. The literature on family companies also assigns considerable importance to the vital evolution of the founding or patriarchal process, how succession is defined and the skills and the motivations of the members of succeeding generations. In this case it will also be important to analyze, as María Inés Barbero does in a later chapter of this book, the psychology and sociology of the entrepreneurs descending from immigrants from the North of Italy, studied in depth by C. de Michele and others (1999).

### *What was the Strategic Intent of the Shareholders?*

G. Hamel and C.K. Prahalad, when coining the term “strategic intent” created a very valuable category for analysis for the study of business strategy. Other authors, such as R. Grant (1999) have advanced along this path, defining that the strategic intent can be defined by answering the following questions:

- How to shareholders analyze and evaluate the “strategic bets” available?
- What “game” did they decide to play?
- How well did they play the game?
- When/how did they decide to “change the game”, changing the rules for competition, in the phrase used by Hamel (1994) or Brandenburger (1996)?

### *What were the Critical Decisions Taken?*

Strategy can be summarized as a further checklist of decisions or “bets”. Principal among these are the following:

- Strategic positioning: the products offered, and their value proposition (quality-price-service).
- Production and technology model to be used: level of vertical integration and spatial configuration of the plant and production network configuration.
- Sale and distribution system adopted: how the company is organized to reach its consumers and the combination of channels used.

- The architecture of the organization: the structure of the organization and the decision-making and measurement processes followed.
- Human resource policy and the corporate culture created.

### *What Capabilities and Skills have been Accumulated?*

The various analyses based on the “evolutionist” view of companies support the claim that whether a company is more or less successful will depend on its ability to develop skills and resources and the manner in which they can be accumulated and used to improve its competitive position. In each period an attempt will be made to reflect how the company has innovated, “learning” and generating new capabilities for the following period. For this analysis we will base ourselves essentially on the analytical frameworks provided by Collis and Montgomery (1997), Besanko (2000) and Brickley (2001).

### *The Resulting Performance*

The combination of determinants and new opportunities and the context and decisions taken by the company give rise to a series of results. Although it is very difficult to establish a reliable connection between actions and results in each period, an evaluation has been made of the achievements in various dimensions:

- Sales performance in the company’s various markets
- Growth achieved
- Evolution of productivity and organizational effectiveness.
- Adoption or creation of new management practices
- Development of the international presence of the company.

## **c) Opportunities and Challenges Ahead**

At the end of any given period, it is interesting to try to provide an answer to the following issues:

What has the company achieved in the period under review?

What was the strategy adopted, and how successful was it?

What is the position of the company with regard to its main competitors?

What is the motivation and the aim of the shareholders and leading players?

In other words “what was in the minds of the leaders?” following J. Gartner (2001).

What changes can be detected in the environment that generate new opportunities or challenges for the company?

Is it possible to determine a company’s understanding of these changes in its environment and the process of discussion, analysis and decision-making aimed at facing up to such new conditions? In effect, is it possible to detect that a company has been “learning”, or is it persisting in incorrect strategic



behavior or conduct not adapted to the new rules of the game, as determined in their analysis by Broustail and Greggio (1999)?

### **Applying the Proposed Methodology. The “Four ARCORs” and their Development over a Lifetime of Fifty Years**

Applying the analytical framework that we presented in the previous section (see Table 1-1), it is possible to conclude that ARCOR has passed through a series of transformations over the course of its first fifty years of existence, making it possible to talk of “five ARCORs” or five company models that have developed successively, as illustrated in Tables 1-2 and 1-3.

*Origins in the Interior*, covering the period from foundation in 1951 to 1970, a time which saw the consolidation of a business project focused on the interior of the country and the steady construction of a growing range of products and nationwide distribution. Some key aspects of the company as it stood in 1970 were as follows:

- Sales of \$47 million (at 1995 prices)
- 1150 employees: 2.5 times the number in 1960
- A scale of production 12 times higher than that in 1960
- Exports of limited significance
- Ranked 18 by sales in the foodstuffs sector and 113<sup>th</sup> in the general ranking

#### *“A Multi-product Company with Nationwide Coverage and Incipient Exports”*

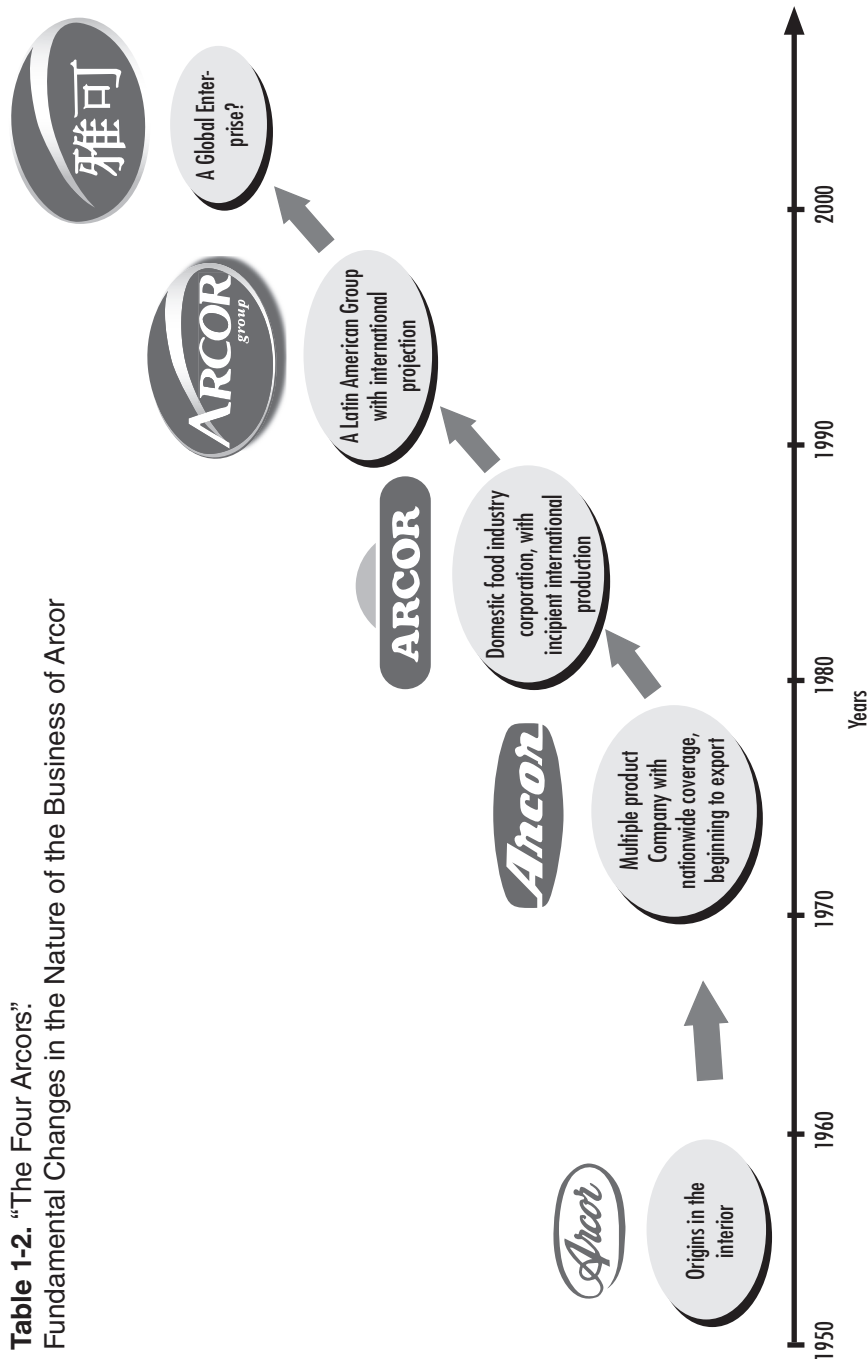
During this period, which covers roughly the 70s, ARCOR carried out a thorough transformation of its strategic focus and its competitive model. The company consolidated the expansion of its product range: in addition to its significant presence in the Interior, it began to make inroads into the markets of the greater Buenos Aires region. Its productive structure expanded, and it started to be managed as a production network. A sustained exporting effort was initiated, so by 1980 ARCOR had become a very different company in both quantitative and qualitative terms from that of ten years earlier:

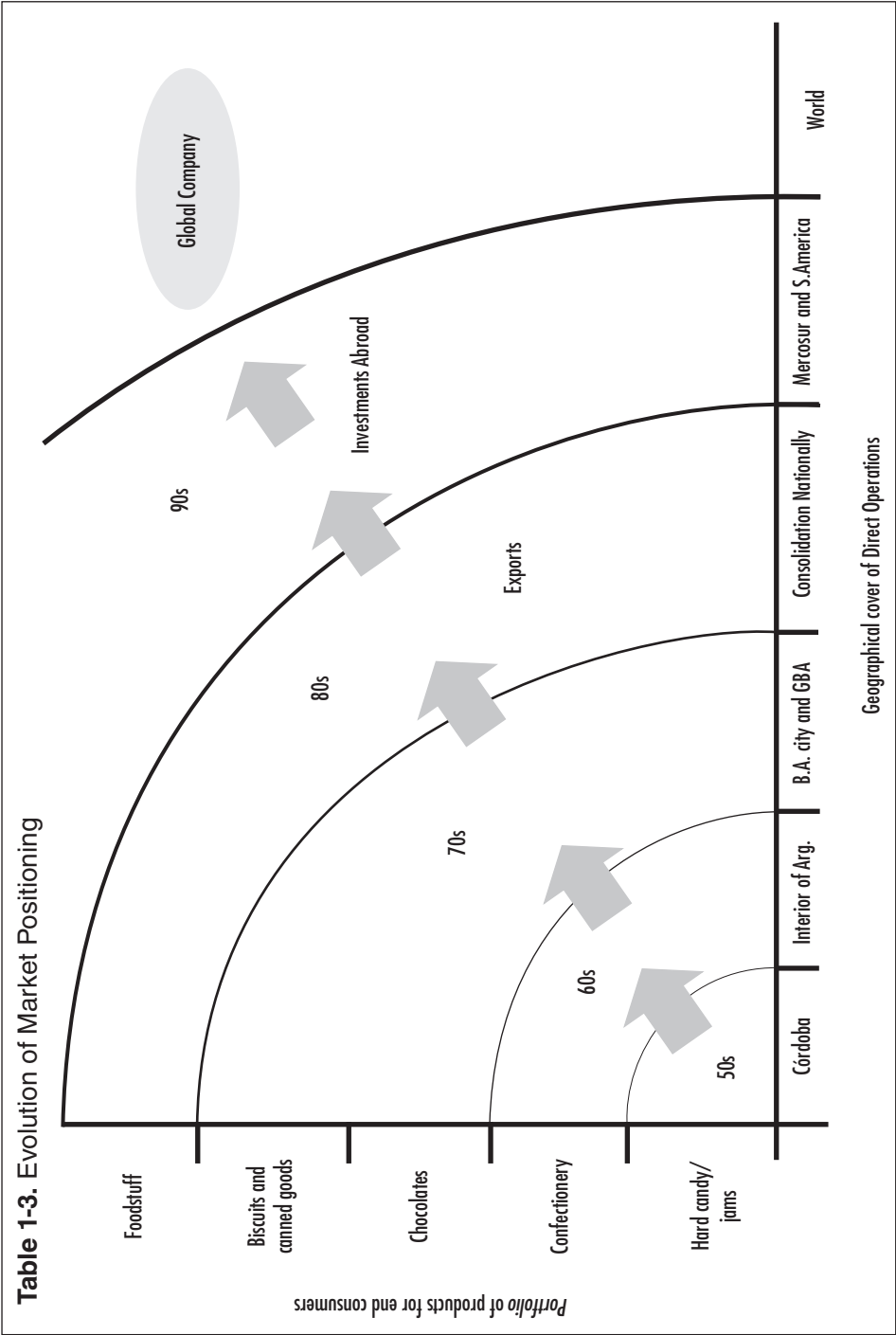
- Sales totaled \$280 million
- 2300 employees, twice the number in 1970
- Exports totaled US\$7 million
- Strong advancement in ranking of local companies: 9<sup>th</sup> in foodstuffs and 86<sup>th</sup> in the overall ranking

#### *“The National Food Group Goes International”*

In the 80s, a period of instability and stagnation for the Argentine economy, ARCOR made progress on several key fronts. Transition was completed from

**Table 1-2.** "The Four Arcors"  
Fundamental Changes in the Nature of the Business of Arcor





“company” to “group”, centered on foodstuffs, reinforcing its presence on the domestic market and beginning to build the foundations of a multinational corporation through the acquisition of companies and the setting-up of production facilities, mainly in neighboring countries. The group started to innovate not only in manufacturing practices (a specialty since its beginnings), but also in product development practices, marketing and management skills. By the end of the 80s, at a time when Argentina was struggling with hyperinflation and a major recession, ARCOR had taken a further significant step in its development:

- Sales reach \$420 million
- Employment totals 5400 people, of whom 21 per cent already work outside Argentina
- Exports are worth an annual US\$21 million
- The company continues to rise up the corporate ranking, standing in 5<sup>th</sup> place in the food industry and 40<sup>th</sup> in the overall list.

*“The Latin American Group with International Ambitions”*

The early 90s found ARCOR at a strategic crossroads, facing two fundamental strategic challenges: the need for a leadership transition caused by the traumatic loss of its founder and the launching of an unprecedented process of economic liberalization and institutional reform. During this decade, ARCOR was able to consolidate its position in the Argentine market and successfully defend its strategic position in the face of the disappearance or purchase by multinationals of other domestic companies. At the same time it achieved a qualitative change in its regional presence through its acquisitions and investments in Chile and Brazil. The company also consolidated its strong presence on export markets, and its operating parameters also reflected a great leap forward. By 1999, ARCOR had become a company with:

- Sales for US\$1.1 billion
- 13,000 employees (twice as many as in 1990) of whom 30% live outside Argentina
- Exports totaling over US\$200 million
- A first-place ranking among food industry companies and 26<sup>th</sup> place in the overall ranking

So far we have described the development of the **“Four ARCORS”**. Consideration should also be given to constructing a hypothesis regarding the future development of ARCOR, and this we have described as **“Moving towards a global enterprise”**, symbolized by the Arcor logo in Chinese char-

acters as it appears on the wrappers of the products that the company exports to China. We believe that ARCOR is entering a new decade in an enviable strategic position, but that it will have to work twice as hard to consolidate the creation of a **“Fifth ARCOR”**: the **Global enterprise**, to be built around certain fundamental dimensions:

- Defense of its position in the Argentine market in the face of increasing aggressiveness by multinationals
- Redefinition of the domestic market as that of a “Mercosur company” with a strong presence in Chile and the building-up of a leadership position in Brazil
- Building of an “enterprise for the Americas” with renewed efforts to establish a position in the NAFTA region
- Leadership of certain global export segments, built on the success already achieved in categories such as chocolates and candies
- Access to other major emerging markets such as that of China
- Development of an “international” corporate culture

These hypotheses regarding the potential shape of the “ARCOR for the new century” will be developed in depth in Chapter 4.

## THE “FOUR ARCORS” AND THEIR DEVELOPMENT OVER FIFTY YEARS. HISTORY AS A PROLOGUE TO THE FUTURE

In the Introduction and the previous section we have presented the analytical framework and its corresponding methodological approach. On the basis of both these two elements, it is possible to assert that the development of a company can be explained as the result of the evolution of four dimensions of analysis and their dynamic relationship. These four dimensions are the following:

- *The institutional and economic policy context* (both of Argentina and subsequently that of the region): where the company is born and takes its first development steps. Within this context, it is also important to highlight the dynamics of the sector (or the industry) in which the company carries out its business: how the competitive conditions and the strategies introduced by the competition evolve.
- *The aspirations and strategic intent of shareholders and Senior Management*: faced by the determinants and opportunities offered by the context, it is important to analyze the motivation of shareholders in initial stages as well as that of Senior Management in subsequent stages. This dimension seeks an understanding of the degree of aggressiveness and Schumpeter-type commitment of shareholders, their understanding of the context and key decisions they took on the strategy to be adopted.
- *Strategic actions and key operating decisions taken*: in each of the periods outlined the company's key players have taken a series of decisions that imply “bets” on the allocation of financial, production and human resources. Decisions are taken on strategic positioning, market pricing proposals, product ranges, production configurations, production volumes, distribution strategies, etc. At certain times decisions are taken that imply a qualitative change to the “strategic perimeter” of the company: new areas of business are developed, companies are bought or sold, new geographical areas are explored.
- *Performance during the period and opportunities and challenges for the future*: the combination of conditions of the environment, competitor actions and the company's own behavior lead to a series of results for the firm over the period under review. It is important to measure whether the company grew, whether it improved its profitability and its productivity, and more fundamentally, whether its positioning and strategic viability was strengthened or not during the period. A forward-looking analysis should also be made to outline

the changing trends in competitive conditions and the environment that represent opportunities and threats for the company; analyzing how the key players have perceived such changes and their strategic response (or lack of it).

In the previous section we also briefly mentioned that the first fifty years of ARCOR's history can be described in terms of the development of four stages known as "the Four ARCORs", which represent the "prologue" to what we have defined as the *prototype of a global enterprise*: the fifth ARCOR. These four ARCORs developed over clearly defined periods in the country's history, which can be summarized as follows:

- *A company specializing in the Interior*, developing during the 1950s and 60s.
- *A multi-product company with nationwide coverage and an initial export thrust*, consolidating during the 70s.
- *A domestic food industry group with a growing international presence*, during the 80s.
- *A Latin American group with international ambitions* that begins to take shape in the early 90s and which consolidated itself by the end of the decade.

In the following section we provide the results of our analysis of each of these four periods in greater detail.

### **Beginnings in the Interior in the 1950s, the Building of a Dominant Company in the Interior and Arrival in Greater Buenos Aires in the 1960s.**

- Argentina was experiencing a period of euphoria and apparently unlimited optimism: real wages were rising, there were ample job opportunities and popular consumption was increasing.
- The interior of the country seemed to offer even more tempting opportunities: most product innovation and large domestic and international brands were to be found in the Greater Buenos Aires region. The interior of the country was still a very fragmented area, made up of traditional distribution channels and local products and brands with limited innovation.
- The quality of the companies in the market and their management practices were at a very incipient stage, resulting in low entry barriers for this group of entrepreneurs of Italian heritage.
- The founders had already been active in the industry for several years, were familiar with the market in the interior and its key players.
- There was a severe lack of technology and input: Argentina was virtually a closed economy.

- Several areas in the interior of the country offered ample reserves of labor at an appropriate cost and reasonable industrial relations.

Building on this environment, we can imagine that at some point the founders began to converge on a *value proposal* and a *business model* as defined by M. Porter (1996) with the following features (for further details, see Table 1-4):

- We are going to manufacture and sell good-quality candy priced for popular consumption.
- We are going to focus on the markets of Córdoba and other nearby provinces, with distribution through wholesalers.

**Table 1-4. Origins — Period: The 50s**

**Strategic Intentions : “Building an independent business project”  
“Company specializing in candy with regional coverage”**

♦ Strategic positioning:

- Specialized range of products: candy on a growing scale
- Positioning in medium-quality goods for the mass market
- Focus on poorly-served markets in the interior - Córdoba and the rest of the provinces
- Search for leadership in costs
- Development of wholesalers

♦ Production/Technology Model

- Strong vertical integration from high transaction costs and insufficient access to input -glucose, cardboard, electricity
- Development, adaptation and manufacture of machinery-limited development of specialized suppliers and closed economy
- Plant located strategically to attend to the market in the interior (Arroyito)

♦ Architecture of the Organization:

- Team of entrepreneurs
- Distribution via wholesalers
- Functional but informal organization

♦ Accumulated skills and development of new skills:

- Capabilities of founders
- Entrepreneurs
- Knowledge of processes
- Knowledge of engineering/development of machinery
- Familiarity with markets in the interior

♦ Human Resources/Corporate culture

- A group of entrepreneurs with a charismatic leader
- A pioneering culture: hard work and building up of the business
- Strong links and commitment to surrounding community
- Cooperation in labor relations



- We are going to build a strongly vertically integrated plant, with equipment designed and ordered by us, that will enable us to provide large-scale production at very competitive prices.
- We will seek a site where we can build a “community” with an ample supply of labor at competitive costs.

It seems likely that these were the fundamental determinants of the decision, in addition to the desire for independence and the famous *voglia da fare* typical of Italian immigrants.

The early years of development can be defined as the implementation of this business concept. The results were encouraging: the interior of the country was prepared to accept ARCOR’s value proposition.

Towards the end of the 1950s the young ARCOR encountered a sudden change in its environment: the Arturo Frondizi administration adopted a more open economic policy, with greater freedom to import technology and capital goods, while maintaining high levels of protection for the import of consumer goods. ARCOR began to adapt to these new conditions, taking a series of strategic decisions that resulted in an acceleration of its growth process (for further details, see Table 1-5).

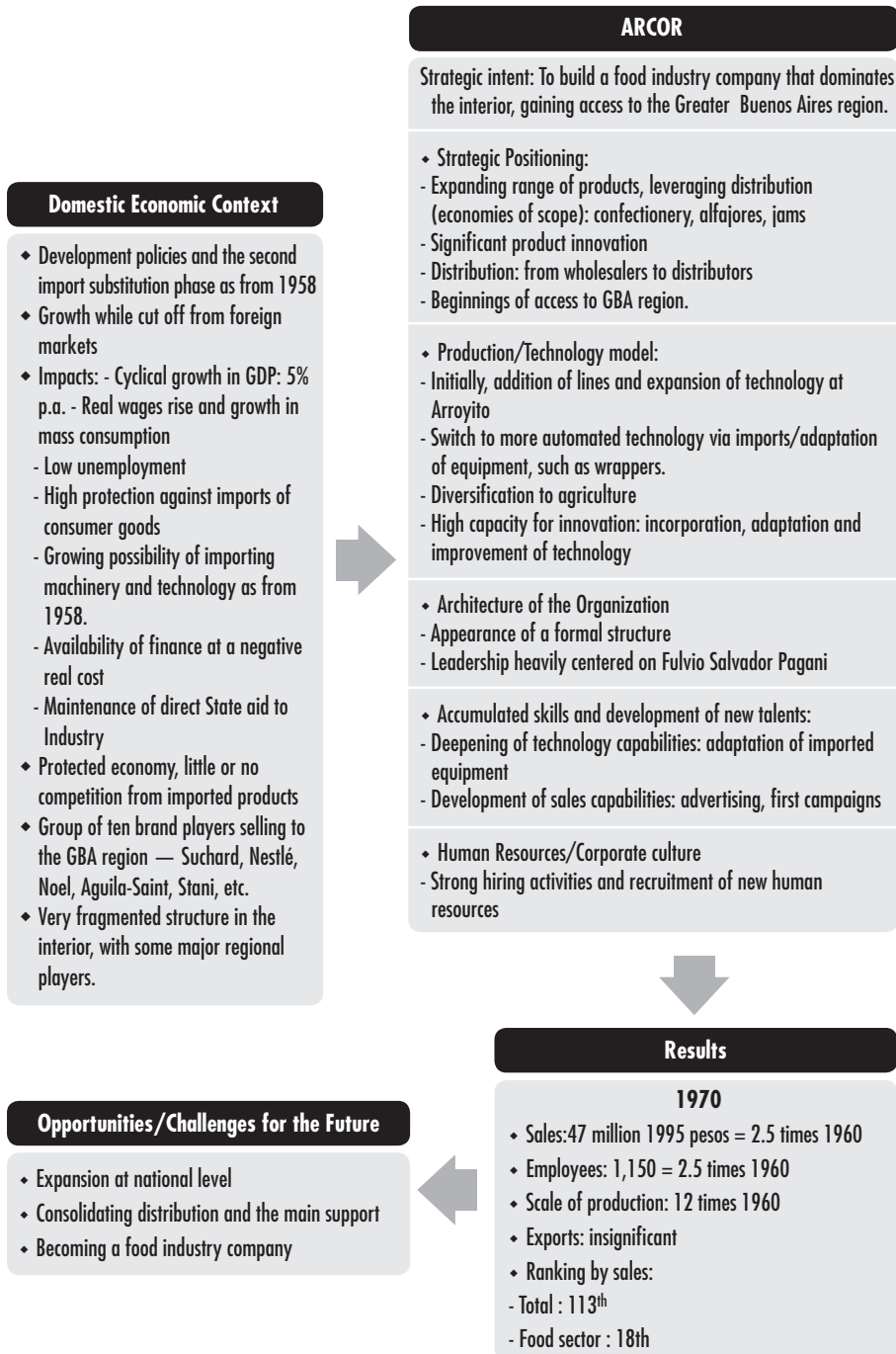
- A decision was taken to expand the product range so as to take advantage of the distribution capacity built up over the previous decade. Candy, alfajores (sweet biscuits with filling) and jams were launched.
- The transition from wholesalers to distributors begins.
- The first steps are taken towards penetration of the Buenos Aires metropolitan area.

At the same time, the new context offered an opportunity to evolve a new policy on technology and the productive model: equipment began to be imported for local adaptation, new product lines were added and technology at Arroyito was enhanced. The technicians and engineers who had worked miracles in the isolated Argentina of the fifties were able to rise to new heights once they had the opportunity to work with state-of-the-art equipment on which they could continue to innovate and adapt.

From a sociological point of view, ARCOR started to change dramatically: its work-force rose from around 400 employees in 1960 to almost 1200 in 1970. The leadership of Fulvio Salvador Pagani was indisputable, but a more formal organization structure was developed and new specialists and professionals were recruited. Transition from an entrepreneurial culture in the 50s to a more formal business structure was under way.

As a result, by the end of the 60s the situation of ARCOR was as shown in Table 1-3: it had expanded its line of products, becoming a leading competitor

**Table 1-5. Period: The 60s**



in the interior, and was beginning to make inroads in the Buenos Aires metropolitan region. The production model had also progressed: from single-product line plants in the 50s, Arroyito had become a diversified complex with various production lines and ARCOR was expanding its productive capacity by means of other plants in the interior. Its organization and its culture were moving away from its entrepreneurial origins to a more complex and formal model, still under Fulvio Salvador Pagani's strong personal leadership. ARCOR was therefore in the best possible position to face the 70s, a decade with strong signs of growing political turbulence and a still promising economic horizon.

### **Building a Multiple Product Company with Nationwide Coverage and Initial Export Efforts. The Experience of the 70s.**

In Argentina the 70s were a time of severe political turbulence and drastic changes in economic policy that placed considerable strain on companies operating in the country. Briefly, the decade can be divided into two main periods:

- *The 1970-1976 period*, during which the attempt to open up the economy by economy minister Krieger Vasena finally collapses and military rule ends, with a return to power by Peronism, followed by a dramatic end to the democratic experience. From this time onwards that the import substitution economic model and the role of the State as a business operator and major allocator of resources begins to be questioned.
- *The 1976-1980 period*, representing a rupture of the democratic system and the most ambitious attempt so far to open up the market and transform institutions during the administration of economy minister Martínez de Hoz. This model marked the beginning of the withdrawal of the State from business activities and involved a drastic financial reform that led to high borrowing costs and a sharp deterioration of the country's industrial fabric.

In a context that disheartened many businessmen and saw the disappearance of several Argentine companies, the group of founding shareholders continued to bet on the development of the company, as can be seen from Table 1-6.

- The product range continued to be expanded: more candy and chocolate categories, as well as totally new categories, such as foodstuffs, crackers and cookies, tomatoes and peas.
- Expansion into the Buenos Aires metropolitan region was consolidated, using the distribution leverage provided by the already existing cigarette distribution network.

- The foundations of an exporting focus and an export presence were laid with the ARCOPAR and Van Dam initiatives.
- The production model continued to evolve, with the addition of new plants in the interior that began to be managed as a network. Vertical integration was reinforced, with the production of containers, tinplate and enzymes.

The sociological aspect of the organization also continued to evolve: management was still based on a centralized model, but progress was made in the development of skills and functional resources in fields such as marketing, finance and logistics. A team was set up to develop exports and gradually acquired experience in serving channels and customers abroad. In 1980 the company recorded exports for around US\$ 7 million.

By the end of this very difficult decade for the country, ARCOP had become consolidated as an important Argentine business (see Table 1-3): sales totaled US\$ 270 million, it had grown threefold since 1970 and it stood in 86<sup>th</sup> place in the ranking of domestic companies.

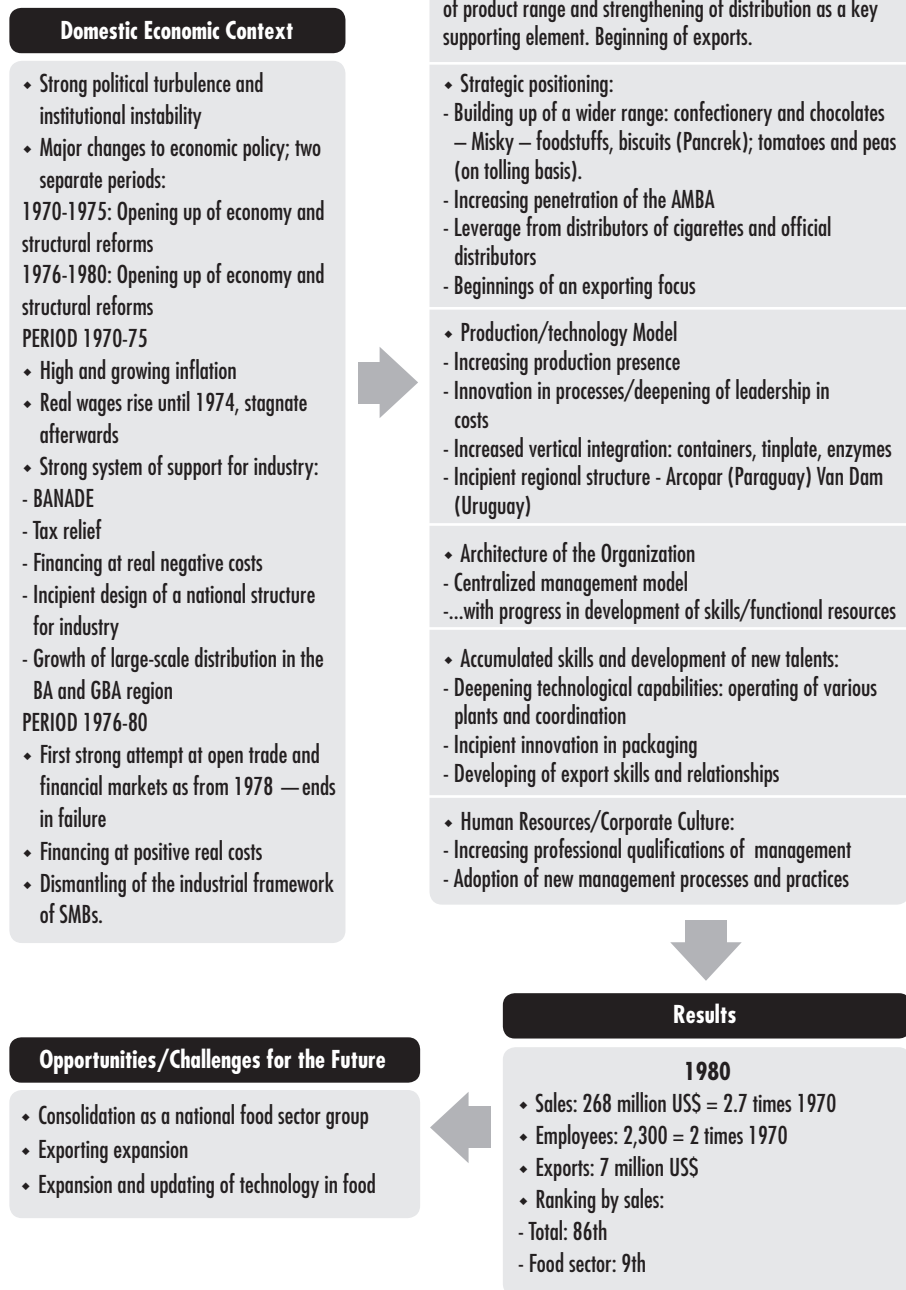
### **Towards a National Food Industry Group and Expansion into the Region and the World. The Experience of the 80s.**

The 80s also were turbulent times for the development of businesses in Argentina: a complex transition towards democracy was carried out in the context of an external debt crisis and failed attempts at stabilization. The macroeconomic outcome was extremely frustrating, with a persistent drop in per capita income and various hyperinflationary outbreaks during the decade.

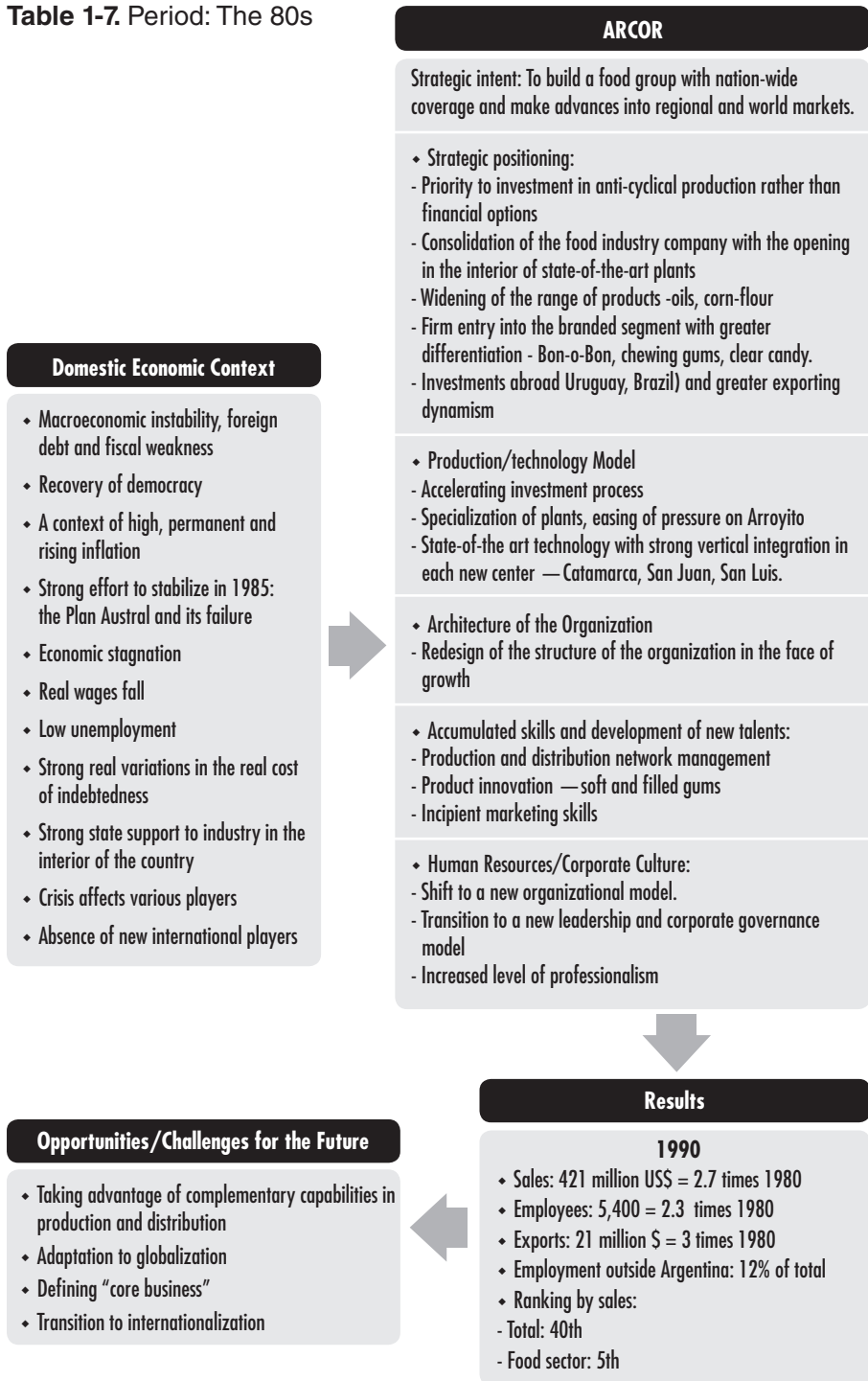
Within this framework, shareholders continued “deepening” their strategy, which could be defined on the basis of three basic elements:

- Expansion of the product range and transition towards a “group” model focussed on foodstuffs
- A counter-cyclical policy for continued investment in technology and production capacity
- A decision to grow internationally as a direct investor and as an exporter.

As shown in greater detail on Table 1-7, ARCOP continued with its growth plans in various strategic dimensions. In the first place, it sought to consolidate its position in the foodstuffs sector, at a time when various domestic players began to enter into a state of crisis and competitive pressures from multinationals were still limited. The product line expanded into oils and corn-flour, but even more significantly, a sharp change took place in competitive strategy with the launch of branded products with increased differentiation and a higher price positioning: chewing gums, *Cristal* caramels and *Bon-o-Bon*.

**Table 1-6. Period: The 70s**

**Table 1-7. Period: The 80s**



New skills were developed in brand building: design, packaging, promotion and communication.

Simultaneously, the production model of the company underwent a profound transformation. Backed by financial assistance from the official sector through the BANADE development bank, the company began to build a truly national production network, with state-of-the-art plants such as those built in Catamarca, San Juan and San Luis. Skills in the adaptation of technologies and industrial management were further developed.

In addition to development of the product range, presence on international markets and the new production model, the period was marked by the drive towards the transformation of the company's organizational model at the end of the decade by Fulvio Salvador Pagani. Don Fulvio was aware that, with sales of US\$400 million and 5400 employees, his company had achieved a level of complexity that required progress towards a new operating model. In the final years of the decade he led a process for the development of a new organizational structure, hiring new talent and advancing towards a more decentralized management model, based on a top-quality line management.

As a result, at the beginning of the 90s ARCOR found itself well prepared to take advantage of the new economic environment (see Table 1-3).

- It offered a wide range of products and a growing positioning in branded goods.
- It had a solid presence nationwide.
- It operated a network of modern plants with considerable production capacity.
- Its management had been renewed and staffed with new talent.

ARCOR was ready to embark on the most successful decade of its history.

### **The 90s. Building a Regional Leader at a Time of Profound Institutional Change.**

The 1990s in Argentina provides a case history of considerable interest to academics interested in studying the relationship between policies for macroeconomic transformation and the development of competitive strategies by local firms and multinationals.

Although the history of the 90s is well known, certain aspects should be highlighted, as they implied major discontinuities in the strategies adopted by companies such as ARCOR:

- Policies for stabilization and convertibility initially impacted in the form of a strong recovery in real salary levels and an accelerated expansion in consumption.

- At the same time markets were opened up to competition from imports.
- Argentina becomes an interesting destination for foreign investment: several multinational corporations decide to increase their presence in the country, in some cases by means of the acquisition of domestic companies.
- Factor costs record strong variations in their relative prices: labor costs grow sharply, while the incorporation of new equipment and technology becomes cheaper.
- Subsidized state credit disappears, to be replaced by bank lending and capital markets with high real costs and sharp volatility.
- Argentina, Brazil, Uruguay and Paraguay create the MERCOSUR common market, which results in a drastic change of the definition of the “home market” to which a local company can gain access.

Faced with such a drastic change in the competitive environment, ARCOR's shareholders could have lost heart and chosen (as many other businessmen did) to sell the company. They could also have failed, succumbing to growing pressure from the multinationals.

None of this occurred. The decade of the 90s became a period noted for a creative expansion in ARCOR that sharply accelerated its growth, reaching a sales volume of US\$1.1 billion in 2000, with exports for US\$ 218 million and 12,700 employees (30% living outside Argentina). How was this achieved?

The critical initiatives during the period (see Table 1-8) were as follows:

- The company strengthened its position as a manufacturer of “branded products with a good price-value positioning”, well placed in comparison to the multinationals.
- ARCOR became confirmed as an “industry consolidator” gaining ground on weakened domestic competitors (buying up some of them, such as Águila) and actively defending itself from multinationals still learning how to compete in the Argentine market.
- The company made strong progress in developing its ability to read the needs of consumers, segment markets and innovate rapidly. A significant advertising effort was made to establish its brands among the consumer public.
- Heavy use was made of the installed capacity created in the previous decade, and further modern plants were set up. A new approach regarding policies for vertical integration emerges and outsourcing initiatives were launched.

In addition, ARCOR completed its transition towards the adoption of the most modern management practices. The 90s saw considerable progress in



**Table 1-8.**

Period: The 90s



the hiring of talent and the development of skills and processes in the fields of marketing, logistics, finance and information technology.

ARCOR also became consolidated as a regional player, with a significant volume of exports and an active approach to embarking on strategic alliances:

- Expansion was completed with the installation of a plant in Brazil, the purchase of a company in Chile (Dos en Uno) and development in Peru.
- An active export program was developed, with strong growth in exports to Brazil (capitalizing on the opportunities offered by the Mercosur) and opening up new markets. By the end of the decade, ARCOR was one of the country's leading exporters, with sales of over US\$ 200 million.

As a result, by the end of the 90s those at the head of the company could feel satisfied (see Table 1-3): they had completed a difficult transition to a new generation and a new management model, strengthening the company as a leader in Argentina and one of the major companies in its sector world-wide. This diagnosis, justifying satisfaction with the past and providing grounds for reasonable optimism for the future, should be seen as the starting point for a new stage: the building of the “Fifth ARCOR”, which we will call “the global company”. In the following chapters we will reflect on the key insights that can be obtained from fifty years of history and will present certain hypotheses in relation to what this new opportunity for growth for ARCOR in the new millennium will imply.

## HISTORY OF THE COMPANY: CHRONOLOGY AND RESULTS

### History of the Company between 1951 and 1990

#### *The Entrepreneurial Event*

- As from the second half of the 1940s the boom in mass consumption and public policy for the promotion of Argentine industry provided an encouraging context for the rise of small-and medium-size companies established with domestic capital. It was in this macroeconomic environment, which was in fact already beginning to deteriorate because of imbalances in the external sector, that ARCOR began its operations in 1951 in Arroyito, 115 km. to the east of the city of Córdoba.
- The original partners in ARCOR (the Pagani, Maranzana, Brizio and Seveso families and other smaller shareholders) had earlier acquired certain experience in the business of selling and distributing candy in the provinces of Córdoba and Santa Fe, as well as in the manufacture of corrugated paper boxes and containers. Capital accumulated from these undertakings and knowledge of manufacturing activities and the markets in the interior of the country were the base for the setting up of this new company to manufacture candy.
- There were various reasons for setting up in Arroyito. The Pagani family had lived there and carried out business in the town for almost twenty years, giving them a network of contacts and relationships. In addition, the area offered significant cost advantages. The exhaustion of the carob tree forests—exploitation of which was the main activity in the region until the 40s—meant that much of the workforce had been left unemployed and housing infrastructure was unoccupied. The town was located on a highway and railroad intersection that facilitated distribution in a regional market with a strong demand capacity. It also enjoyed access to milk supplies and good water, key inputs for the activity being set up.
- The main difficulties included scarcity of skilled labor in Arroyito and deficient electricity supplies. The first of these was resolved by means of the hiring of technical personnel and specialists in other areas with a greater experience in industrial activities and machinery maintenance, or directly from the company in which the partners had been involved. In the case of electricity supplies, initially the plant was equipped with a generator that was steadily upgraded. Later, an electricity cooperative was formed and finally ARCOR installed its own generating turbine and power station that was also able to supply power to neighboring towns.
- There is a relative consensus among theorists that the process of creating a company—defined by Shapero (1978) as an “entrepreneurial event”—can

be studied on the basis of the influence of cultural, economic, sociological and psychological variables, considering the individuals involved as one of the relevant factors in explaining such a creation, although not the only one. From this perspective, the creation of a firm is not perceived as a predetermined event as from the birth of the protagonists, but as a process whereby the entrepreneurs begin to take shape on the basis of their interaction in society, within the framework of specific contexts.

- In the creation and subsequent development of ARCOR the figure of Fulvio Salvador Pagani stands out because of his personal qualities that included initiative, the ability to innovate, leadership skills and long-term vision, identifying him as an entrepreneur as defined by Schumpeter.
- However, the presence of the other partners and interaction with the local medium were also determining factors. All the members of the founding group were not only linked by their friendship, but also accumulated complementary experience and productive capacity. The relationship with the local environment facilitated the obtaining of material resources and made it possible to ensure that the starting up of the company and its operation in the first few years was the result of a collective effort implying a level of commitment and a capacity for hard work that compensated for the difficulties experienced in those first moments.

### *The 1950s and 1960s. Increase in Scale and Development of Vertical Integration*

- During the fifties and sixties the growth of ARCOR was based mainly on increases in scale, integration of production and the creation of a distribution network for the nationwide market. The key to the strategy of the firm was to compete with low costs and products aimed at a mass market. By the end of the 60s the company was already supplying 50% of the domestic market for candy.
- Since the end of the 50s increases in scale were supported by growing technical innovation in production, with a leap in technology between 1958 and 1960 —stimulated by the possibility of importing capital goods without paying import duties— as well as by heavy investment in equipment throughout the 60s.
- Unlike the large candy manufacturers at the time, which mainly manufactured for segments with higher purchasing power, concentrating on the big urban centers, ARCOR aimed at the mass market and consumers in the interior. Candies were a product accessible to all sectors of the population and their consumption was very widespread.

- In the early years production was basically manual. In 1958 state-of-the-art manufacturing machinery was purchased in Germany, with machines for wrapping being acquired in Italy, and processes were automated to significantly increase production speeds. With this new machinery the company took its place at the forefront of international technology, increasing its efficiency and competitiveness, and its scale of production rose significantly: from the five tons per day in the early stages to sixty tons at the beginning of the 60s.
- Integration of production had as its purpose the reduction of costs in the supply of raw materials, input and machinery. Raw materials and input were produced locally, but supply was hindered because of price problems—particularly in the case of input—and delivery times. Machinery was built in the early years to overcome restrictions on imports, and since the end of the 50s to cut costs—given the high price of imported equipment—avoiding any increase in foreign currency debt.
- Historically transaction costs have always been high in Argentina, and vertical integration was a common strategy adopted by most companies during the import substitution period. Difficulties tended to arise in the obtaining of supplies of raw materials and input, either because of shortages or monopolistic local supply or because of restrictions on imports from fluctuating exchange rates or changes in tariff policy.
- In the case of ARCOR integration of production became one of its principal strengths, allowing it to lower production costs, offer competitive prices and diversify risks. Through this process of integration the company was transformed into an industrial group in which the various production plants sold their surpluses on the market, complementing the sales of the core activities. In some cases the scale required and determined for the plants manufacturing inputs amply exceeded ARCOR's needs, so that sales to third parties were higher than their intercompany transactions.
- Surpluses from the glucose plant, for example, were sold to other companies making drinks and jams, and in the early 60s these sub-products also began to be exported. Corrugated paper was sold to local companies and gradually, as ARCOR increased the number of its plants and its volumes of production, this category of product began to assume a significant role in the group's total sales.
- Initially machinery used was second-hand and the technology was obsolete. However, by the end of the 50s the company's directors and experts were traveling regularly to Europe to acquire new technology and renew machinery. ARCOR's strategy consisted in combining imported items with those it

had manufactured itself. Key machinery (such as cookers or wrappers, for example) was bought for adaptation and improvement, and other machinery was manufactured using the latest foreign models as a reference.

- This engineering capability was developed into the company's own workshop for construction and adaptation of equipment which steadily increased its personnel and design capabilities. In 1953 the workshop had a single lathe, kept fully in use by two technical operators in two shifts. By the end of the 50s the design office had hired a couple of draftsmen, and by the 60s it had become a full work-team made up of mechanical draftsmen, engineers, designers and architects. This team was responsible for most of the group's plant expansion projects.
- At this stage therefore the company had acquired the features of an integrated multiple plant company with its activities centered in Arroyito in the city of Córdoba, although it continued to operate as an individual company and not as a group. By the 1960s it had begun to invest in companies in related activities in various agricultural and industrial sectors, as well as in the production of input.
- At the same time, as from the mid-60s ARCOR started to diversify its output, manufacturing other types of candy, *alfajores* and jams. However, the principal feature of this stage was the company's diversification into non-industrial activities, mainly the purchase and exploitation of land for agricultural activities that were not necessarily linked to the core business. One such activity was cattle-raising, covering the full cycle of breeding, fattening and sale of livestock.
- In 1953 a first farm of 111 hectares was purchased to begin planting quince trees and for the fattening-up of pigs. By 1988 the group had 180,000 hectares located in several provinces —Córdoba, Salta, Santiago del Estero—, developed using modern techniques on a capital-intensive basis. In general cattle raising was predominant, although later other activities gained importance, such as forestry plantations and exploitations and dairy farming.
- Strategy regarding agriculture was two-fold. Farming activities represented a diversification in the activities of the firm to take advantage of business opportunities, lower risks, improve availability of financing and ease access to bank credit. To a lesser extent it formed part of the process of integration, as the company's land produced raw materials such as sorghum and maize for the manufacture of glucose, quinces for the making of jams and wood for paper pulp.
- At the same time as it increased its production capacity, the company began to build a distribution system that became one of its strategic advantages,

thanks to its reach and the methods implemented. From the beginning, sales were made to wholesalers, and in the 60s new channels began to be added. One of these was the cigarette distribution system selling to kiosks. Another, used as from 1967, was sale through official distributors. By the end of the 60s, ARCOR had an efficient distribution network covering the entire domestic market, although its main area of influence was the market in the interior of the country, where conditions were less competitive than in Buenos Aires and the Greater Buenos Aires region.

- Direct sale to wholesalers was a strategy that set ARCOR apart from many of its competitors, which sold to retailers in very small volumes with high transport costs. The company weeded out its customer list, demanding minimum orders from its smaller customers, with the aim of making better use of transport and loading and unloading of goods. Subsequently, sale through official distributors enabled a significant reduction in the cost of sales and speeded deliveries.
- The company used the two distribution systems in parallel, selling some brands through wholesalers and others through official distributors. In the 50s and 60s the company's production was almost entirely for the domestic market, in particular in the interior of the country. It began by developing a regional market —Córdoba, Santa Fe, Entre Ríos and Tucumán— and then expanded into other provinces. Its first sales were made in Buenos Aires in 1953, but its effective participation in this market dates back only to the 1970s.
- In this first stage advertising investment was low, and very rudimentary resources were used. The ARCOR brand was less well-known than its products. Nevertheless, during the sixties some minor developments and investments took place in the field of packaging.

### *The 1970s. Diversification and Decentralization of Production*

- Throughout this decade the economic performance of this company was severely conditioned by a context marked by instability, rising inflation and far-reaching economic policy changes as from 1976. ARCOR was not much affected by the opening up of the economy in 1977, but did feel the impact of the financial reforms, which caused a drastic increase in its borrowing costs. During these years the company grew at a lower rate than in the previous decade, and in general its performance fluctuated.
- In the 50s and 60s ARCOR's expansion had been based on increased scales of production and vertical integration, and only very slightly on diversification. In the 70s, however, the company's growth was a result of the develop-

ment of new markets for its products and the search of new geographical markets inside and outside Argentina. During this stage ARCOR diversified and decentralized its production and widened its distribution radius, advancing on the city of Buenos Aires and the Greater Buenos Aires region. At the same time it began to develop an international presence through its exports and the first direct investments abroad.

- Although ARCOR's core business continued to be confectionery, the process of diversification meant that it gradually became transformed into a food-producing company. In addition to candies and jams, it began to make crackers and cookies, maize derivatives and canned and pulped fruit. There was also a diversification in the confectionery line itself, with the start of chocolate manufacturing. At the same time there was a stronger focus on the process of vertical integration in the production of input, with the addition of plants manufacturing flexible packaging and tinplate and the production of enzymes.
- Diversification was a response not only to the dynamics of the firm but also to the search for economies from product range in distribution, in particular because the official distributors required a wider variety of products than wholesalers.
- Whereas in the 60s the increases in the scale of production and the manufacture of new products was mainly carried out through the addition of plants and lines at the Arroyito complex, during this second stage the physical expansion of the company was accompanied by a process of geographical decentralization and the creation of a growing number of related companies.
- New companies were either acquired or set up in various provinces of Argentina —Tucumán, Mendoza, Buenos Aires, Santiago del Estero— and in other regions of the province of Córdoba. A confectionery company was formed in Tucumán (Misky); a firm for the production of enzymes was established in Arroyito (Milar) in association with Miles Laboratories (USA); two companies were set up at Villa del Totoral (Córdoba) —Pancrek (crackers) and Vitopel (plastic film)— and an ARCOR plant was built in San Rafael, Mendoza, for the production of fruit pulp. In 1979 the assets of a distillery, the firm of Guillermo Padilla, were acquired to act as a basis for the setting up of a plant at San Pedro to produce maize derivatives. Much of this investment was financed through loans from Banco Nacional de Desarrollo benefiting from the use of provincial industrial promotion regimes.
- With the growth in investment in related companies the company began to evolve from an individual entity into an economic group, with ARCOR SA



- at the head of a series of firms that were legally independent which were either wholly or majority owned.
- During the seventies the company aimed at improving its competitiveness and costs by means of increased productivity, either through investment in machinery and equipment or improvements in the organization of production, with reforms in plant layout, the introduction of quality control and the setting up of an industrial safety department.
  - At the same time changes were made in the organization to make management more efficient and make operating and administrative controls more agile. As from 1977 measures were adopted to improve and update internal organization structure and procedures, including the introduction of a dynamic organization chart for all executive levels and an increased spread and use of computer systems, which in 1978 led to the opening of the company's own data processing center.
  - The steady expansion of production was backed by gradual improvements in distribution systems and resulted in a considerable increase in the firm's market share both in Argentina and abroad. In the domestic market, the most significant advance was an increasing presence since the beginning of the decade in the city of Buenos Aires and the Greater Buenos Aires region, where ARCOR's penetration had previously been very limited, given the company's initial strategy of gaining strength in markets in the interior of the country, holding the metropolitan region in reserve.
  - Exports, which began to be made at the end of the sixties, gradually increased their share of total sales, until reaching a level of 8% in 1979. Although sales abroad helped to support the increase in the scale of production and moderate the effect of fluctuations on the domestic market, their principal contribution in the seventies was to ensure improved logistics and quality standards. For this reason the first foreign sales were made to the United States. In addition, during the 70s the process of internationalization of production began with investment in a company in Paraguay (ARCOR-PAR, 1976) and the approval for investment projects in Uruguay (Van Dam) and Brazil (Nechar).

### *The 80s. Internationalization and the Building of a Multiple Division Corporation*

- In the 80s, ARCOR gained in strength as one of the country's main economic groups, its rate of growth being far higher than in preceding decades, generating a significant change in the magnitude of its assets and its sales. It maintained a strongly industrial profile, without diversifying into activities

unrelated to its manufacturing output, a trait that set this group apart from most domestic conglomerates.

- Its expansion was based on a dual process of decentralization —with the installation of manufacturing complexes in various provinces— and internationalization —with investment in a confectionery plant in Brazil and the purchase of 50% of Van Dam in Uruguay. At the same time ARCOR further developed its diversification into the food sector. Local investment was mainly made taking advantage of industrial promotion regimes set up in various regions in the interior of the country. By the end of the 80s, the company operated 23 manufacturing plants located in eight provinces.
- Between 1985 and 1988, ARCOR set up industrial complexes in San Juan, San Luis and Catamarca. Each of these plants manufactured both end products and input for local firms and for the group, thus becoming decentralized manufacturing centers.
- It also continued to re-equip existing plants, installing automatic lines for the production of confectionery, expanding the machinery workshop and the paper manufacturing plant and diversifying production at the San Pedro plant with the addition of dry milling and oil manufacturing facilities. The Milar plant was also enlarged with the addition of machinery built in the company's workshops, and silos were purchased to increase grain storage capacity.
- Throughout the 80s it became increasingly apparent that there was a widening gap between the size and complexity that the group had acquired and its organizational structure. Whereas production had become increasingly decentralized, management continued to be highly centralized and based on individuals. Since the seventies changes had been made to the organization, with the adoption of a departmental structure and professional management, but this was proving inadequate one decade later. The company also evidenced a lack of resources and management in certain areas, such as personnel, finance and, to a lesser extent, marketing.
- At the end of the eighties ARCOR carried out a far-reaching restructuring of the organization, which culminated in 1990 with the adoption of a multidivisional structure in the nature of a holding company, organized on the basis of business units, geographical areas and functional entities, each division being headed by a manager with a high degree of autonomy. This restructuring eased transition to a new stage of collegiate leadership following the death of Fulvio Salvador Pagani, in December 1990.
- The company significantly increased investments in organization and management with the development of an offensive strategy with the aim of im-

proving competitiveness in a context in which the levels of protection by the state of the manufacturing sector were declining and rising interest rates encouraged the search for increased levels of efficiency.

- Efforts were made to improve information systems and obtain greater facility for analysis, operating flexibility and coordination of management levels, with the aim of ensuring a more appropriate environment for decision-taking. Adaptation of systems and methods and procedures was the subject of continuous analysis and in 1985 a working group was set up at executive level to plan the information systems for the company and its related firms.
- At the same time it was sought to lower costs through a reduction in expenditure and increased efficiency and productivity, with constant improvements in the organization of production and distribution and steady investment in state of the art machinery and workshop equipment. The company continued to manufacture much of its machinery in its own workshops, importing the most complex elements such as those required for numerical control.
- In the case of distribution, during this stage efforts were centered on making the network more efficient and innovations were introduced in selling systems, with direct sales to supermarkets, in line with the increasing importance that this channel was acquiring in the Argentine market. In turn, the new sales systems required increased investment in packaging and advertising to make the presentation of products more attractive and strengthen brands.
- Exports remained at high levels throughout the decade, and since 1985 their volume rose at a faster rate than local sales. Lines were diversified (with exports of input and machinery being added to sales of confectionery) and new geographical regions were opened up. Exports and investments abroad began to be part of a single, coordinated strategy.
- The international structure of production advanced significantly, with the purchase of 50% of Van Dam (1980, Uruguay) and the acquiring of a confectionery company in Brazil (1980). A sales office was also opened in the U.S. It should be noted that the growing international development of ARCOR was part of a more widespread process of international expansion by several large Argentine manufacturing groups. In the case of ARCOR, its international expansion was based mainly on its technical and production skills and distribution facilities.
- The company's performance was severely affected by conditions on the domestic market, particularly the episodes of inflation and hyperinflation

and the rising cost of money. During this stage ARCOR borrowed heavily —because of the increase in its investments— at a time when the cost of financing was very high.

- Nevertheless, the increase in assets and sales was constant throughout the decade and ARCOR recorded a notable improvement in its position both within the ranking of leading Argentine companies and in the food sector itself. In the ranking of leading Argentine companies published by Mercado magazine on the basis of sales, the company rose from 70th in 1980 to 44th in 1989, the year in which it held 6th place in food companies, with sales higher than all other producers of confectionery and biscuits. By the mid-eighties it supplied 70% of the domestic confectionery market.

## **Performance and Development of Competitive Capacity in the Nineties**

### *Performance During the Nineties*

- ARCOR's performance during the 90s compared very favorably with any indicator of economic behavior and of the Argentine industrial sector. This evidence is a sign of the successful strategy and appropriate decisions taken by the company in the face of the changes made in macroeconomic design and the overall competitive environment. The company correctly judged and understood the scenarios that arose as a result of the introduction of structural reforms and the success of the 1991 stabilization program, taking advantage of the knowledge and infrastructure built up during the course of its own development.
- The new economy of the nineties in Argentina found ARCOR in full maturity after a development process that had taken place over 40 years, during which time it had developed specific competitive advantages as seen in its strong production, sales and distribution capabilities —principally in the interior of the country— and in the skills of its human resources in the operating management of the company. It was equipped with modern, highly integrated manufacturing processes, large-scale low-cost production, backed by continuous addition of best international practices.
- This infrastructure placed the firm in an unrivalled position when domestic consumption soared in the period immediately following the introduction of the Convertibility plan and the sudden stabilization of internal market prices. At that moment the relative positioning of ARCOR benefited from weaknesses in the process of investment by its local competitors and the limited activity in the domestic market of the branches of the major international manufacturers. This initial advantage was maintained even when the big players arrived in the market in the middle of the decade, given the time

it took them to learn the peculiar characteristics of the market for this type of product.

- Although the company suffered from organizational and management method defects, by 1990 it held a fairly precise diagnosis of these problems and a proposal for the redesign of administrative and decision-making structures. This enabled it to approach its restructuring and respond to the demands of an increasingly complex organization, including the attaining of an increased level of professionalism in its leadership and management, attempting to ensure that the levels of excellence achieved in the production and distribution environments could be replicated in other areas of the group —development of human resources, marketing and administration. Just as Fulvio Salvador Pagani was the key figure during the first forty years of the firm, during this stage the leadership of Luis A. Pagani was essential in the implementation of these new strategies.
- Economic rules and institutions and the conditions for competition altered drastically in Argentina during this decade. From a situation noted for high inflation, a fairly closed economy, markets that were quite inaccessible and financing that was relatively cheap, the country advanced to an extended period of price stability, open economy, more competitive markets and the high cost of money. This set of conditions defined a productive scenario in which extraordinary profit margins could no longer be expected, with the need to pay special attention to the problems of market development, expanding sales channels and product offer.
- ARCOR decided to consolidate its position in the markets that represented its basic strength (confectionery and jams, in the interior of the country) developing other areas where its presence was less significant, but which could guarantee sustained growth in the medium and long term (chocolates, *alfajores*, crackers and cookies, Buenos Aires and the supermarket channel).
- To assure this strategy it was proposed to make rapid progress with a new organizational model, developing a new corporate image and strengthening marketing capabilities —with an aggressive development of new products— strongly developing the process of internationalization —through exports and direct investment abroad—, lowering the level of productive integration —outsourcing activities— and modifying the system of specialization —centering on core businesses.
- Through its retail point of sale distribution system, the structure and control of which was always one of ARCOR's competitive strengths, the firm developed and took advantage of strong economies of scope during this stage of the 90s. Its wide range within the different product categories allowed

it to combine mass distribution and volume in food and biscuits with high relative margins on confectionery and chocolates. This last attribute in particular was beneficial in its negotiations with supermarkets, a sales channel that was essential to carry out any expansion strategy.

- At the same time, the process of gradual occupation of various international markets, particularly in the region of the MERCOSUR and Chile, assumed a key role. A plan for integrated commercial expansion was adopted, which resulted in rapid growth and diversification of exports and new markets. This process was complemented by the development of a truly multinational Latin American company, through an aggressive strategy in Chile—with the purchase of candy company Dos en Uno—and in Brazil—with the development of a greenfield investment in the chocolate sector.
- During the 90s, the rate of growth in sales by ARCOR was three and five times higher respectively than the rise in total production and industrial production in Argentina. The contrast is equally notable in terms of the number of employees. Whereas in the ten years under review the Argentine economy as a whole generated an increase of barely 10.1% in employment, the manufacturing sector lost 22.4% of its workforce and the food sector lost 12.9%, ARCOR increased its workforce by 85.3%. In this context, the firm's productivity evolved even more favorably than national aggregates.
- Export sales by ARCOR increased five-fold between 1991 and 2000, while in the same period Argentina's total exports did not even double and those corresponding to manufactured goods recorded a rise of close to half that shown by the company. This performance accentuated the already comparatively greater exporting focus of ARCOR, with an exporting ratio which rose from 9.5% in 1991 to 17.4% in 1999, levels that once again are far higher than those estimated for Argentina as a whole (3.7% in 1991 and 5.2% in 1999) or those of the industrial sector (7.9% in 1991 and 12.2% in 1999).

### *Incorporation and Generation of Technological Capability*

- Until the 90s the situation of ARCOR with regard to technology was conditioned on the one hand by the nature of its principal market—mass consumer and relatively unsophisticated—and on the other by a context marked by restrictions on the offer of capital goods, given limitations on imports and the relative lack of development by local industry. As a result, during its first thirty years ARCOR's main efforts in the field of technology were centered on the process area, leading to acquiring a reserve of skills and internal capability that was used by the company to adapt, develop and even construct equipment.

- In the exceptional conditions of the 90s, ARCOR decided to outsource certain activities, extend the reach of plant efficiency programs and position a wider and more differentiated range of products. The new microeconomic strategy of the company led to taking a new look at its traditional approach to technology. It could be seen that although the staffing of technical personnel and the way its activities were organized showed adequate generic technical knowledge, the capabilities and specific advantages shown were not the most appropriate to immediately adapt to this transformation.
- It became necessary for the focus of development activities to switch to the area of product technology. Organizational improvement processes were rapidly introduced and through increasingly professional management and intensive training programs a renewal of management methods was achieved. ARCOR began to make use of consultants and work by outside experts to resolve certain specific matters.
- R&D activities showed a trend towards decentralization into the new business units. This change enabled greater agility in the detection of needs and opportunities in the company's various different markets, where competition relies heavily on the constant launching of new products.
- At the same time, the principal in-house efforts were centered on the adoption of soft technologies. Programs were introduced systematically for quality improvement, inventory management, reduction of idle time and minimizing of scrap. All plants saw the incorporation of ISO 9000 standards, and some also adopted ISO 14001.
- Prior experience and the knowledge contributed by personnel added during ARCOR's expansion stage—through the absorption of other companies and the hiring of personnel from formerly domestic firms taken over by transnational corporations—proved to be a valuable asset in the development of new and different products, businesses and capabilities. In this regard, the overall restructuring of the food sector provided a source of positive externalities to the firm.
- Among the most significant technological developments carried out or implemented by ARCOR during these years was the new filled hard candy plant. This plant—almost entirely designed by ARCOR—is considered to be the best of its kind in the world and is the leading expression of the knowledge and know-how developed by the company.

#### *Development of Capabilities in Marketing and the Sales and Distribution Process*

- Towards the end of the 80s, although ARCOR benefited from its extremely competitive prices and total control over the productive process, it was ex-



periencing problems in the sales process. On the one hand, there were too many official distributors operating in a not very sophisticated manner. On the other, the company needed to increase its penetration into the important markets in the metropolitan region, dominated by supermarket operators. Full development of this latter channel seemed to be a requirement if ARCOR was to improve its positioning, particularly in the food segment.

- Its products were considered by consumers to be of high quality, although lacking in brand image. Prices were low, and although they generated volume their contribution margin was also reduced. In general packaging was outdated and advertising support was weak. Because of this, as well as its lack of brand names, ARCOR was less recognized in the large urban centers.
- These problems were likely to be aggravated by the transformations in the domestic economic system. Local brands were having to compete against international brands and corporations, offering products of a recognized quality, with a considerable product innovation capacity. At the same time, self-service was gaining importance in the purchasing habits of the population, reinforcing the negotiating position of supermarkets. In these conditions, companies such as ARCOR which had not developed sufficient brand capital, might have begun to see a weakening of their other competitive advantages.
- ARCOR strengthened its strategic decision to position itself as a food and confectionery company with an international outlook, emphasizing its quality and price attributes. To this end, precise objectives were set for its competitive positioning, its strategic markets, its brand policy, its distribution systems and the attention to foreign markets.
- In just the first five years of the decade ARCOR launched 300 new products on the market including over 500 different items, changed almost 100% of its packaging, created 83 new brands, backing them with an intensive communication activity and an investment under this heading of over \$150 million, a level that was 15 times higher than that previously recorded. This innovation in the area of marketing continued in even greater depth subsequently, with the launch of approximately 100 new products every year, so that by 1999 ARCOR produced more than 1500 food and confectionery items.
- In general, all the objectives outlined in the design of the strategic plan at the beginning of the nineties were more than achieved over the course of the decade, with sales and market share rising faster than expected in the case of both confectionery and food. This positive performance was based on a



total marketing strategy, to gain maximum leverage from attributes such as quality and price which had always been present. At the same time a specific corporate communication strategy was developed to position the main ARCOR brand-name as an effective umbrella for the remaining individual brands.

- During these years performance was noted for: i) a significant increase in the cover provided by product distribution, both physical and weighed by value; ii) an increase in share in all markets; iii) improvements in product quality and brand development, enabling an increase in average prices until 1995-96, partly reversed subsequently because of the recession.

### *Development of Human Resources*

- By the early 90s ARCOR's payroll already totaled over 6000, with approximately 12% working for the company in plants and undertakings abroad. The main attribute and principal strength of this assets was its good level of technical training of the production personnel. This capability was completed by a notable disposition to innovate and be creative in the same area. Producing is what ARCOR personnel knew how to do best, and in effect they did it very well.
- ARCOR had a Human Resource manager, but lacked infrastructure and resources to fully develop the area. As a result, the operating capacity of management appeared weakened because of this deficit, which was a reflection of the lack of any specific human resource strategy. There was also a lack of training in management skills at various levels.
- The ARCOR Group workforce grew significantly throughout the nineties, doubling in size. The main strategic change in this area can be summarized by two principal actions: i) development of an integrated Human Resource management; ii) an increase in the level of professional Human Resource management. These actions led to the adoption of specific strategies and the definition of organizational aspects, development of resources, personnel administration, selection and hiring, training and education and industrial relations.
- Personnel administration systems were modernized by means of the computerizing of processes and the establishing of a complete system of performance indicators and performance evaluation based on international benchmarking. An aggressive procedure was developed for identifying and hiring university graduates for areas of the firm that had not previously had components with such a high level of formal education: Sales, Human Resources, Quality Control and the first line of supervision in the industrial area.

- The selection of university graduates, middle management and managers led to the incorporation of novel tools. Formal educational requirements for production-line personnel were also raised. As a result of the new profiles that were established the average age of personnel tended to decline, to stand at 35 years old for the group as a whole and 25 in the case of newer plants. All these actions were accompanied by a purposeful strategy for the development of human resources based on three fundamental pillars: training, evaluation and incentives based on results.
- The remuneration system was redesigned at the same time. A system of salary bands based on average market values was gradually introduced, as were various forms of compensation based on performance. In the case of management levels, variable remuneration was related to the objectives and results of the specific area, while in the case of operations personnel it was linked to productivity. This system of remuneration was approved by the union authorities.

### *Developments in the Financial Area*

- In the context of the macroeconomic instability that existed in the eighties, in particular following the consolidation of the pattern of high inflation and widespread monetary indexation, financial management by companies in Argentina assigned priority to short-term movements and the situation in the immediate future. Companies based their actions around a constant search for opportunities for the placing of investments in highly liquid assets. This context and the predominant strategies strongly conditioned the type of skill developed in the financial administration areas of companies, and ARCOR was no exception.
- Although a financial information and operations center had already been set up and the group's finances were being handled on a centralized basis, which enabled better use to be made of short-term opportunities, the firm showed weaknesses in the matching of its process of growth to an adequate long-term financial strategy. To this substantial shortfall certain failings in the administration of the area, such as the lack of information mechanisms and internal supervision and weaknesses in communications systems and computer technology could also be added.
- ARCOR had taken decisions regarding the expansion of its productive capacity that ran counter to the traditional business practices of the period. In this context the results of the strategy—an apparently excessive company structure—appeared as a weakness. The first response by the company was to place its indebtedness ratio on a sound footing, disposing of certain assets not directly related to its principal business.

- At the same time the recovery of the domestic market and a sharp rise in consumption since the third quarter of 1991 found ARCOR with sufficient productive capacity working at a level of efficiency that enabled a rapid increase in sales and absorption of fixed costs, so the higher sales income that was generated restored the company's liquidity.
- The reorganization and increased level of professional skills in a finance area that was to be centralized at group level became a priority if operations were to be carried out efficiently at the same time as ensuring longer term financial planning capability. The hiring of skilled professionals for the sector from outside the company and the increased importance assigned to the area within the company through its links to strategic planning, ensured it became possible to overcome the existing limitations.
- The evolution of the financial position and strategy of ARCOR in the 90s shows two distinct phases. During the first stage, which ran through to approximately 1997, the debt was relatively low with a predominant strategy for the self-financing of investment projects or the taking of loans from international financial agencies. At a second stage investments for the development of new plants or the acquisition of other companies tended to be financed with an increased proportion of borrowing from the private bank system.
- The priority assigned to self-financing strategies was to a large extent a response to the features of the domestic capital and lending markets. In comparison to other international manufacturers, a company such as ARCOR had to face higher borrowing costs and severe restrictions on the raising of capital on equity markets. It is interesting to note that while its debt to capital ratios are quite similar to those of its global competitors, its self-financing ratio is much greater, while the "income/interest paid" ratio is substantially lower.

*Penetrating World Markets. Exports and Manufacturing at International level*

- Since its first exports to the United States at the end of the 60s, ARCOR has been developing a steadily increasing presence in international markets, a trend that accelerated in the 90s. This performance was a reflection of a corporate decision to preserve its positions in markets that had already been opened up, regardless of the changes in circumstances and fluctuations in terms of trade.
- Export sales reached a peak in 2000, when they totaled US\$ 217 million, 20.2% of the company's total sales. Investments currently being carried

out with the specific purpose of increasing shipments in coming years will ensure that exports will play an even more important role in the overall performance of the company.

- This performance has led to ARCOR becoming the leading confectionery exporter in the Mercosur and the largest exporter of confectionery in Brazil. It currently sells to 105 countries, with a notably strong presence in the Mercosur and the United States, a significant share of the market in Israel and a growing penetration in Asian markets —especially China— and in Africa. Most export sales are made from its plants in Argentina.
- The company's strategy for achieving a greater presence on international markets has been complemented and reinforced by the decision taken to substantially increase productive capacity outside Argentina. ARCOR's development of a multinational manufacturing and sales network is playing a key role in the prospects of improved penetration of foreign markets with own brands and differentiated products. In the 1994-1999 period, intra-firm exports represented almost two thirds of its total foreign sales and in 2000 accounted for 72% of its exports.
- Gains in competitiveness require comprehensive advantage be taken of economies of scale, while the opening of new markets makes it possible to overcome the limitations of size and dynamism of the domestic market. In turn, the international spread of productive capacity eases access to certain markets that otherwise would not be able to be served. It should be emphasized that this aspect not only involves growth in the physical volumes of exportable offer but also assumes a process of product upgrading.
- This strategy for the building of ARCOR into an international company based on its principal objective of reaffirming its position within the Mercosur, becoming the leading confectionery and chocolate manufacturer in Latin America with a growing share of markets outside the Mercosur, required the strengthening of the organization as a whole, the permanent review of its areas of specialization and steady gains in efficiency.

### **Overall Context and Specific history. Distinctive features.**

- Two aspects of the evolution of ARCOR are particularly relevant when viewing comparative histories. One relates to the shape taken by large corporations in late developing societies, where integration of production, diversification and the forming of economic groups are a response to contexts in which a high degree of uncertainty predominate, with high transaction costs, scarcity of management resources and small markets. The ARCOR case shows signs of these defining traits, but also other aspects specific to

the company, such as its lack of diversification into other manufacturing activities and its family business structure with a very centralized management during much of its existence. These characteristics —evidence of a predominantly industrialist culture and strong personal links— reveal the variety of strategies and organization models out of which successful companies can be built.

- A second important aspect is the way in which a competitive company can be built up in a context of high protection and subsidized industry, such as that of Argentina during the period of import substitution. In the case of ARCOR it can be seen that the company grew by combining its innovative capability with the use of various public subsidies, including loans, industrial promotion, tax exemptions, rebates and other measures intended to benefit companies in the private sector. In this case, the two strategies —the obtaining of advantages from the protection provided by the state and the creation of competitive capacity— worked together in a positive manner. In a context in which lax design of promotion instruments and weakness in the State's ability to monitor and control encouraged widespread rent-seeking practices by local entrepreneurs, other types of response were also possible that were intended to install genuine competitive capacity.

These two strongly distinctive aspects of ARCOR compared to the development of other large companies and conglomerates in Argentina came into play in the 90s when, in the context of profound changes in the principal economic regulations and thus in market and conditions for competition, the strategies of economic agents also altered. Two features are particularly noticeable during this decade: the considerable extension of the growth of transnational companies —particularly in industry— and the decided preference shown by local groups for taking positions in the widespread process of privatization of services and public assets —generally transferred in the form of captive markets in monopoly conditions. Competitive capacities built up by ARCOR over its history and its decided vocation as an industrial concern enabled it to continue to expand, concentrating on its core manufacturing business, competing successfully in the context of an open economy and developing its own process of productive internationalization.

## **LESSONS LEARNED FROM THE ARCOR CASE**

Three aspects of this singular case are particularly relevant to business executives, entrepreneurs, designers of economic policy, regulatory authorities and academics.

- First, the decisions made by company executives and its subsequent performance challenge commonly-held assumptions in the field of business management.
- Second, the Group's evolution enables assessment of non-traditional strategies for business growth and development.
- Last, the firm's reactions and adjustments to sudden changes in the business context allow for the examination of alternative development paths of companies in emerging markets, where strong macroeconomic turbulence and changes are frequent.

The combination of these aspects provides an example that illustrates microeconomic theories explaining the successful performance of domestic corporations when competing against multinational groups in emerging markets.

Below we detail some of the key elements of the ARCOR Group's strategy over its history that are decisive in explaining both the specific nature of the company and its success. These attributes can be grouped into six basic topics:

- How to achieve a market position with minimum efficient scale in small markets.
- How to secure viability and enhance market leverage via greater control of the value chain.
- How to drive growth of the firm via an evolving distribution strategy.
- How to acquire and maintain world-class competitiveness under capital constraints and restrictions on capital goods imports.
- How to develop a winning competitive strategy against larger, entrenched incumbents.
- How to develop a sustainable export capability in a constrained and erratic context.

### **How to Achieve a Market Position with Minimum Efficient Scale in Small Markets**

Most business operating principles and accepted best practices have been developed in regions with strong contrasts with those of emerging countries. Among these differences we find the former have much larger markets, consumers with greater purchasing power, availability of capital to carry out innovation and investments and well developed infrastructure. In this context the formulation of commercial strategies in consumer goods starts from an understanding of consumer needs to achieve their segmentation or re-segmentation.

The number, size and differentiating features of consumers in developed markets results in the need to focus on some segments when developing a competitive product or service offering to meet specific needs and provide benefits. In these markets focus is a fundamental aspect of any commercial strategy and is a fundamental requirement for achieving economic viability. In other words, the potential provided by each segment assures a minimum efficient scale.

Typically this is not the case in emerging markets, and certainly it was not the case of the interior of Argentina in the 50s, when ARCOR emerged. Carrying out a traditional market segmentation and the subsequent focusing would have confined the company to a value proposition with limited potential, making its sales and distribution structure more costly and constraining its future growth. The intent of creating products (candy) for the consumer public at large in its region of influence led ARCOR to develop a business system that emphasized low-cost production and distribution capabilities, taking advantage of economies of scale. This path would in turn influence its later growth, diversification and integration strategies.

### **How to Secure Viability and Enhance Market Leverage Via Greater Control of the Value Chain**

Having defined the initial business scope as the production of candy for markets in the interior and having achieved the first volume targets, company executives found they had problems in the supply of key raw materials. The end cost of a product such as candy is strongly determined by the cost of its raw materials. Unreliable supply, low negotiating power and lack of alternative suppliers raised a significant issue. This situation is not unusual in semi-closed economic environments, where supply through imports is difficult and market sizes are relatively small, leading to scarcity in domestic sources of supply and high transaction costs.

ARCOR's reaction was to integrate vertically into critical inputs: a viable and consistent solution at its stage of the development and low product diversification. An alternative response could have been to maintain the focus on the initial product, deepening the search for economies of scale and attempting to compensate partially for cost disadvantages, however, dependence on key inputs posed a strong risk. It should be noted that the resulting integration strategy is well aligned with widely accepted business theories that predict this kind of adaptive behavior as firms strive to reduce transaction costs.

A key feature of the development of the vertical integration strategy adopted by ARCOR was the systematic effort made to ensure that the produc-



tion scale of the various undertakings should provide competitive positions in their respective markets. Hence, the companies created were able to supply other customers at market prices, and those were used to determine transfer prices. During the time the described market conditions continued to prevail, basically up to the end of the 80s, this strategy provided ARCOR with significant advantages. In addition, and more fundamentally, it created a path to growth through vertical integration on an efficient scale, as well as providing increased control over the value chain in which it participated, allow for greater margins and multiple points to realize them, increasing autonomy and “end-to-end” profitability.

Later macroeconomic changes and a more open Argentine economy in the early 90s significantly altered this situation. A new, more open business environment and the arrival of specialized players lowered many transaction costs substantially and led the ARCOR group to take another look at its vertical integration levels, placing emphasis on the need to focus on its core businesses. ARCOR’s ability to interpret and consequently adapt to changes in its context has been one of its outstanding strengths and underlines the decisive impact that macroeconomic and institutional conditions have on microeconomic behavior.

### **How to Drive Growth of the Firm Via an Evolving Distribution Strategy**

A factor that frequently limits company growth of companies is the lack of access to a distribution network with appropriate coverage, capillarity and critical mass. Over time, direct distribution costs can only be justified under conditions of high customer or points of sale density with orders above minimum levels. Such conditions are not usually present in the early development stages of a company. However, faced with the lack of a distribution network, many companies are forced to serve customers directly over long periods, incurring in high costs that impact on their profitability. ARCOR’s initial situation did not escape this reality and the company, as in other areas, quickly adapted to this restriction, developing an effective distribution system that it expanded and strengthened over the years.

Initially, small size and limited products assortment made it hard for ARCOR to set up its own distribution, so it used wholesalers who were able to place a small range of products in limited volumes. As the company grew, the wholesaler channel presented restrictions to volume and coverage, which led to developing distributors. They differed from the former in that their area of influence was larger and they were able to handle a broader assortment



of products. To increase its significance for distributors, ARCOR decided to widen the range of its initial offering, supplying products such as *alfajores* and jams, and later with chocolates and biscuits. The sequence in which new products were introduced to the system was key to their success. Initially, new products were manufactured by third parties, thus avoiding risky and sub-scale investments. Once product volumes warranted it, ARCOR would begin in-house production.

The combination of scale and assortment created an offering that qualified to be channeled through the distribution system of tobacco companies, thus reaching a vast number of points of sale with products that complemented cigarettes. This development provided ARCOR with extensive territorial coverage throughout Argentina, at significant capillarity levels.

As ARCOR broadened its product range, their products began to account for a greater portion of kiosk and store purchases, indirectly competing with cigarettes. This factor, coupled with increased scale and sales volume, finally led the company to set up a network of official distributors stretching across the whole country. The continuous interaction of production and distribution strategies is a key feature of ARCOR's development and has been leveraged to strengthen its market position.

### **How to Acquire and Maintain World-class Competitiveness under Capital Constraints and Restrictions on Capital Goods Imports**

Since the beginning of its activities and up to the early nineties (with two brief exceptions at the end of the 50s and in the second half of the seventies) ARCOR faced severe restrictions that hindered and added cost to the import of capital goods. This situation added to limited availability of funds (typical of companies in their early stages) the absence of capital markets for financing and an international supply of state-of-the-art equipment at high prices, made it very difficult to acquire production equipment for long periods. At the same time, the success of the strategy pursued by ARCOR was to a large extent based on achieving low cost production capabilities.

In a local context marked by shallow markets and relative factor prices in inverse proportion to those of developed countries, ARCOR solved the described tension by identifying critical points along the production chain and updating machinery that determined overall efficiency. Having set the priorities, those responsible for technology kept updated and internal workshops were developed for in-house manufacture or adaptation of equipment.

In line with these actions and at an early stage in its growth, ARCOR decided to export in a systematic and regular manner to developed markets, in

spite of the effort that this represented for a company of its size. This policy ensured that the company constantly updated quality standards for its products and adopted innovations for its equipment. It should be noted that when the opening up of the economy eased imports of capital goods, the activity of internal workshops declined until it was outsourced, but it preserved its excellent equipment purchasing skills, which resulted in more efficient investment. Once again it can be seen how ARCOR redirected the application of its accumulated abilities, adapting them to new institutional and regulatory contexts.

The trend towards adaptation followed by ARCOR is a reflection of the fact that in a context of production organization and markets that are significantly different from those of industrialized countries, it is possible to develop a configuration for production that involves the co-existence of machinery and equipment of different technology maturity levels. This is perhaps the best response to the conditions under which operation takes place in some emerging markets, and supports the argument that the best local manufacturing plant is not necessarily a replica of “the best plant in the world”.

The incorporation of technology and its regular updating took place in the context of an innovation path particular to the company, leading to the manufacture of equipment within the firm as well as introducing adaptations and improvements (even in the case of recently acquired equipment); a typical example of *learning by doing*. The problem resolution, introduction of changes and improvements and the incorporation of additional innovation developed considerable internal technical production skills at ARCOR, which ensured the company was kept up-to-date as to best practices and could count on the necessary skills to rapidly incorporate important technical innovation. These activities were complemented by quality certification processes under international standards and continuous improvement following Japanese techniques. The results achieved in terms of quality and productivity have been very significant, making ARCOR’s practices comparable to those of other world-class players and at the same time providing it with a competitive cost position making its global export program viable.

### **How to Develop a Winning Competitive Strategy Against Larger, Entrenched Incumbents**

The development of small-and medium-size companies is frequently hindered by premature competition with a strong player or dominant sales channel that influences its margins and growth. In many cases market dynamics does not allow the young company to control the level of competitiveness to which it is exposed. This is generally the reason given to justify steps taken to protect

infant industries and recommendations for a regulatory framework that contemplates adequate levels of protection during launch and incipient development. This framework, as well as decisions at company level that allow for management and mitigation of the level of confrontation with competitors and the relationship with its channels, can turn out to be decisive for survival. Throughout its history, ARCOR has paid particular attention to these aspects, allowing it to develop its capabilities appropriately before it was required to face intense competitive pressure.

The start-up of activities and the initial focus on markets in the interior of the province of Córdoba, benefited ARCOR with a “natural barrier” represented by its position in markets that were far from major centers of consumption, and therefore less attractive to leading national competitors. During much of the 60s and 70s, ARCOR’s expansion was centered on the development of markets in the interior of Argentina, avoiding a massive, frontal and costly entry into the market of the capital city. At the same time as progress in those markets increased the scale of the business, the company’s management strengthened its capabilities as a low-cost manufacturer and established an effective distribution system that emphasized traditional channels and kiosks (vs. supermarkets), creating a very robust business model, in spite of existing competitive pressures and restricted sales channels.

The deliberate strategy of focusing on poorly-served, less approachable markets, together with its clearly-defined business model, provided a two-fold benefit for ARCOR’s expansion. It gave it time to develop competitive skills in the areas of production, distribution, innovation, product development and management, as well as to become familiar with the possibilities and prospects of promotional regulations. In addition, it enabled it to gradually dominate those markets and thus establish a robust fortress in the interior of the country. In the following decade it was to use this base to launch an attack on Argentina’s main consumer center, where it would have to face the rise of the supermarket channel and the arrival of leading competitors in ARCOR’s own territory. However, this increase in competitive intensity found ARCOR with strong production and distribution capabilities, competitive costs and a critical mass of business provided by markets where it was not easy to make inroads into its position.

These microeconomic decisions were a distinguishing feature of ARCOR, although the conduct that would make it stand out sharply from most other Argentine companies came in the 80s. While most companies concentrated on managing the financial aspects of their business in response to the inflationary context and the behavior of interest rates, ARCOR persevered with its

policy of investment in production and distribution capabilities. Although this strategy had a significant cost, almost leading the company to a difficult financial situation at the end of the decade, it served to position it to take advantage of the consumption surge that took place during the first part of the 90s.

The stabilization of the Argentine economy with the introduction of the Convertibility Plan (1991) and its impact on disposable income gave rise to strong growth in all consumer goods categories, which had been suffering from considerable repressed demand. Growth in consumption in the first years subsequent to stabilization was such that in many categories installed capacity proved insufficient. In this context, investments made in productive capacity and distribution enabled ARCOR to respond efficiently in the face of demand increase and gain market share. However, this position was challenged by the opening up of the economy, the entry of multinationals lured by the strong growth, and the notable expansion and concentration of the supermarket channel.

In the new competitive environment that arose, many local companies found themselves faced with the dilemma of having to choose between three basic options: to position themselves as secondary players, running the risk of gradual loss of market share; to sell out, or to double the stakes and go head to head against the multinationals, which were equipped with better financial resources, advanced technology, superior products and strong brands. ARCOR opted for the latter path, on the basis of its strengths in production and distribution and recent improvements in marketing, innovation, packaging and research and development, which had begun in the previous decade, driven by the demand caused by the company's increased presence in the competitive and sophisticated market of Buenos Aires. At the same time, part of its development in this decade benefited from certain strategic mistakes by incoming multinationals that extrapolated business assumptions of their home markets and hence suffered delays in their adaptation to local market conditions and infrastructure.

At the same time, the company further developed its strategy for international expansion that enabled it to take advantage of economies of scale and accelerate its innovative processes in production, product and quality. These actions, added to a selective acquisition of key assets from certain local competitors, made it possible for the company to expand its product range and cover a multiplicity of market positions. Through an effective communications strategy, an evolution was achieved in the perception of its products from "economic" to "best value", at the same time as the launch of premium products took place, competing successfully with the multinationals. Simulta-

neously, and unlike other consumer goods businesses that found themselves in the same circumstances, the company preserved a balanced portfolio of channels, strengthening its distributors, negotiating access to supermarkets and looking after its presence in its traditional channel and kiosks, thus achieving better protection for its margins. One key factor in this strategy was the ability to have a diversified product portfolio which enabled it to make sales to supermarkets (oils, canned goods, flours, etc.), achieving volume and scale in distribution although at lower margins, at the same time as other products (confectionery, chocolates) provided higher margins through kiosks and traditional channels, with lower volumes.

### **How to Develop a Sustainable Export Capability in a Constrained and Erratic Context**

Except for sectors and companies based fundamentally on natural competitive advantages for which the export of raw materials or commodities has always been their main activity, the development of an import substitution model was not matched by any clear strategy for the generation of a sustainable flow of exports. In general terms, during the development of industrialization in Latin America manufacturing exports have been based on counter-cyclical actions (occasional exportable balances) or required circumstances and exchange policies that were especially favorable and explicit promotional instruments that are increasingly challenged in a multilateral trading context. Under these conditions very few local firms have developed and subsequently maintained a significant position in foreign markets.

ARCOR is one such exception, and over its history it is possible to identify the evolution of its export strategy, based on its experience and the increasing sophistication of its capabilities. It is possible to recognize in this evolution various of the elements generally present in textbook cases of successful exporters, which are not often evident in the case of most domestic companies: prompt use of sophisticated markets as quality signals for own production, continuity of operations abroad relatively independent from price fluctuations, so as not to lose customers and positions that have been gained, taking advantage of opportunities and preferential access to regional and neighboring markets to gradually gain volume and experience and the progressive development of production activities abroad to strengthen brands and make progress with strategies for specialization and complementation.

ARCOR's first exports, made as early as the end of the 60s, consisted of relatively small volumes placed in the North American market. In this stage the key contribution to the company from these exports was the identification of

potential improvements to quality and presentation, rather than sales revenue or scale advantages. Concern with volume and the consequent establishing of a relatively significant export flow began subsequently, with the development of a distribution network in the markets of neighboring countries —Paraguay, Uruguay, Chile and lastly Brazil—, taking advantage of trade preferences negotiated under the framework of the LAIA trade association, which were subsequently extended and deepened during the process of negotiation and setting up of the Mercosur. Key aspects of this stage of exporting strategy include the nature of the products exported (the same as those produced for the domestic market, so there were no problems of scale or organization of production caused by the set up of special lines “for export”), and the deployment of the company’s own network of service centers to handle demand in these markets.

At an early stage ARCOR also consolidated its brand and its presence in the regional market, developing production capacity abroad through direct investment in companies, allowing it to combine and benefit from location advantages. This process accelerated and made major progress in the 90s in the context of a significant export development strategy that involved multiplying productive installations and widely diversifying markets served. The progress made and the experience acquired during the process enabled ARCOR to reach its current position as a global enterprise that produces and exports differentiated goods.

Specifically, the export of differentiated products requires a strategic positioning that implies: i) development of products that are recognized globally; ii) production capacity and flexibility to adapt to requirements of demand; iii) development of own distribution and sales systems in leading markets; iv) negotiating capability of strategic alliances that allow the undertaking of specific projects. As a result of its performance, ARCOR has not only become consolidated as a manufacturer and exporter of confectionery in South America, but also it has generated a dynamic flow of sales towards important markets outside the region. Penetration of the market in China and the development of long-term alliances to make strong inroads into the North American market constitute two of its most significant achievements.

## Conclusions

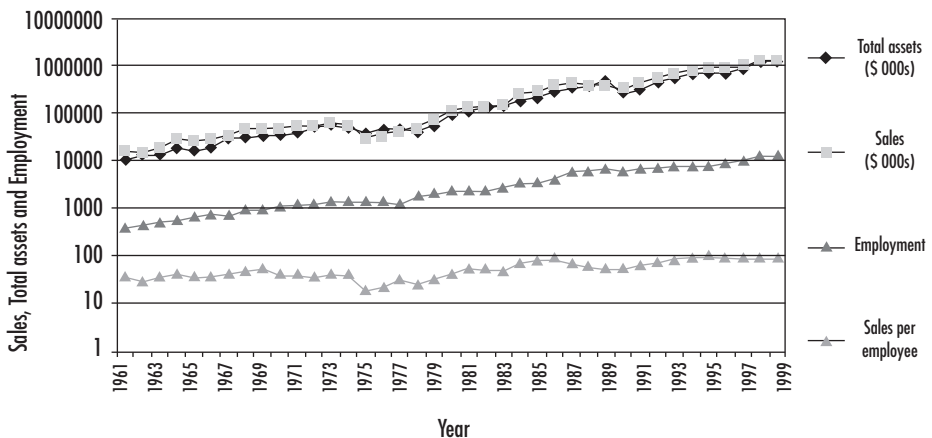
The ARCOR case is a clear indication of the fact that globalization does not necessarily imply the domination of local or regional markets by multinational companies, in line with similar cases presented by academics and students of the matter such as J. Gingrich (1999); N. Dawar, T. Frost (1999); C.K. Pra-

halad, K. Lieberthal (1998); and T. Khanna, K. Palepu (1997). In particular, it indicates that superior market understanding often allows local groups to out-perform multinational corporations that extrapolate successful models or formulas from their countries of origin without making the necessary adjustments to the local scene. This situation highlights the fact that pressures for globalization are not uniform in all industries and are greater in so far as the key competencies for the business and its success factors are transferable and can be replicated in other geographies. In consumer categories where the local tastes of consumers are a determining factor, such as snacks, beer, pasta and confectionery, there is a viable and profitable positioning possible for local brands and products, leveraged by business systems with strong sales and distribution capabilities.

**EXHIBIT.****A QUANTITATIVE VIEW OF THE DEVELOPMENT OF THE COMPANY**

The purpose of this exhibit is to provide an aggregated and summarized review of the evolution of ARCOR from its beginnings through to the present. To this end an analysis has been made of the financial statements of the main company (1961-99) and those of the Group (1984-99), surveying the main economic indicators arising from them, such as Sales, Total Assets, Shareholders' Equity, Additions of Fixed Assets, Employment and Profitability, among others. To be able to make use of comparable information, data at current values was transformed into constant 1995 pesos (using the wholesale price index) and constant dollars in the same year (using the average annual exchange rate and the U.S. retail price index). Both adjustments generated convergent trends and behaviors.

Analysis of the information provided by the annual balance sheets discloses the evolution of some of the basic elements behind the forming of the group, giving an indication of its financial and production behavior and the conditions of its performance over a long period. The evolution of sales, assets and personnel employed give an idea of how its size developed; the relative evolution of liabilities and shareholders' equity, together with the evolution of the various measures of profitability summarize the results of its management and its performance. At the same time the evolution of the relative ratios for sales and investment per employee can be used as approximate indicators of aggregate productivity, which thus indirectly reflect elements of productive strategy.



**Graph No. 1.** Evolution of sales, total assets and employment.



To provide an overall picture and outline the most general traits, the following graph summarizes the evolution of the main size and performance variables for the ARCOR group over an extensive period of almost forty years. It should be noted that for the 1961-1983 period the information corresponds to ARCOR alone, while for 1984-1999, consolidated figures for the group have been used.

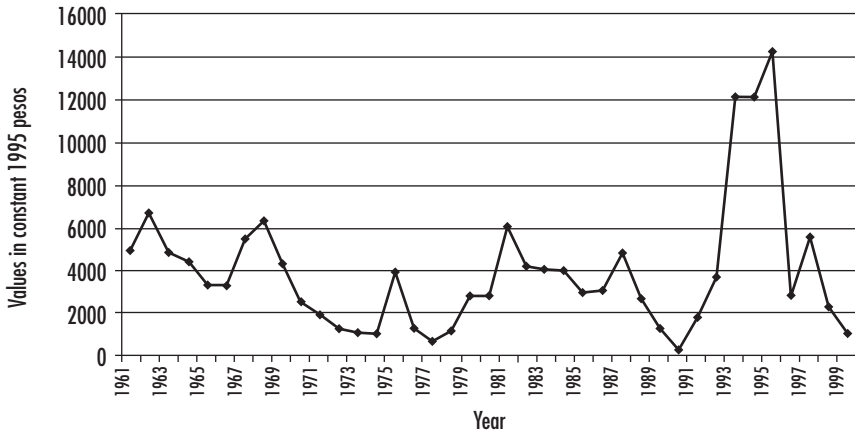
In terms of trend, Sales and Total Assets grew continuously and strongly over the period, showing an average annual rate of change (end-to-end) in the order of 11.9% and 13.1%, respectively. As a result of this performance the size of the company was multiplied by 107 times (by Assets) or 71 times (by Sales) in four decades. Similarly, Employment shows a continuous annual growth in the order of 9.4% on average, which translates into an overall increase of the 31 times in the workforce since the levels at the beginning of the period.

The differences in the rates of growth in the workforce on the one hand and sales on the other suggest a significant positive variation in the firm's productivity levels, which according to the approximate indicator used would have multiplied almost 2½ times. It can be seen that as the rate of addition of personnel has been relatively constant the long-term trajectory of productivity entirely reflects the cycles of the Sales variable<sup>2</sup>. The performance of the Investment indicator has been notably cyclical, as might be expected, but has also been relatively irregular. However, as in the case of the other dimensions considered, its average annual level of growth has grown strongly, having multiplied by seven in relation to the first years analyzed.

As a result, capital intensity, estimated by means of an indicator for additions of Fixed Assets (equipment and buildings) in relation to personnel employed, shows a highly fluctuating behavior, with sharper peaks towards the end of the period. In the first three decades the amount of annual investment per employee ranged between 2 and 6 thousand pesos, being particularly low during the 70s and at the end of the 80s, picking up strongly between 1992

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<sup>2</sup> In general terms, assets, sales and net equity of the group record a trajectory similar to that of the main firm and show a very similar average annual rate of growth. In the case of these variables the main firm represents approximately 75% of the consolidated figures for the group. The main difference between the two lies in the evolution of the level of employment, as on the one hand the firm's personnel accounts for less than 50% of the total for the group and on the other the rate of hiring of personnel by the group has been significantly faster. As a result, in comparison to the group the productivity indicator (sales per employee) of the main firm records a higher level, a greater rate of growth and a less notable cyclical trend.

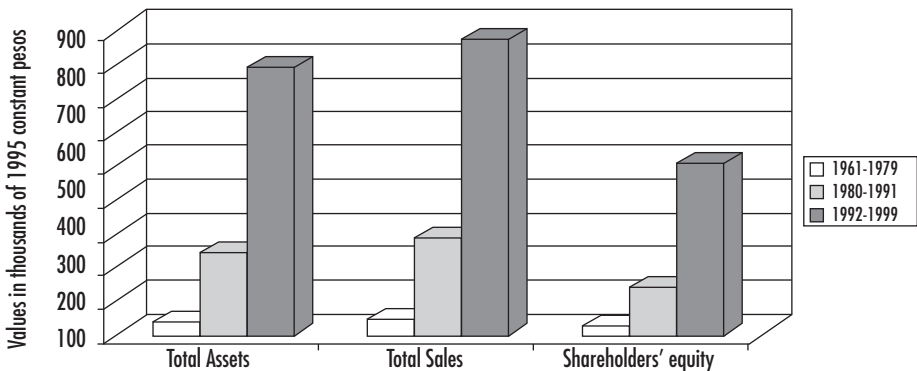


**Graph No. 2.** Increase in fixed assets per employee.

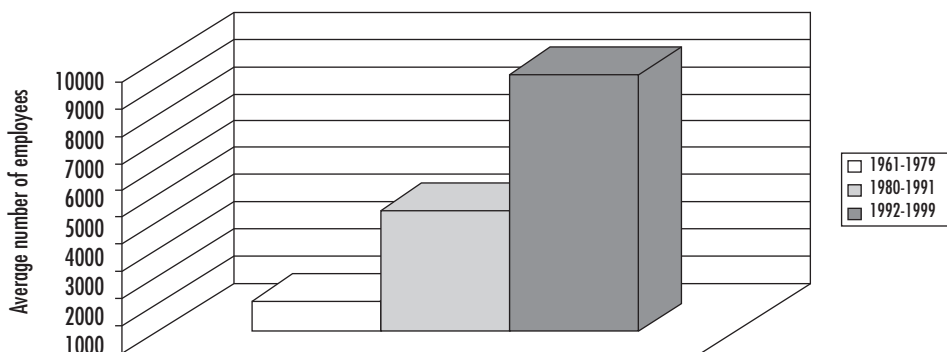
and 1995, more than doubling previous maximums. Towards the end of the 90s however, it returned to minimum levels.

The behavior of Assets and Total sales suggest the existence of three main stages in the evolution of ARCOR. The first covers the period 1961 to 1979, the second runs from 1980 to 1991 and the third from then until the end of the decade. In general terms these stages are ended by periods of recession for the group that interrupt relatively prolonged phases of steady growth. Each of these periods is in turn noted for a considerable difference in the size of the variables involved, so that calculations of respective average values shows the company has experienced several distinct growth phases. It should be noted that in comparative terms, it is during the last of three phases that ARCOR demonstrates the greatest growth.

**Graph No. 3.** Comparison of the three stages : Total assets, sales and shareholders' equity



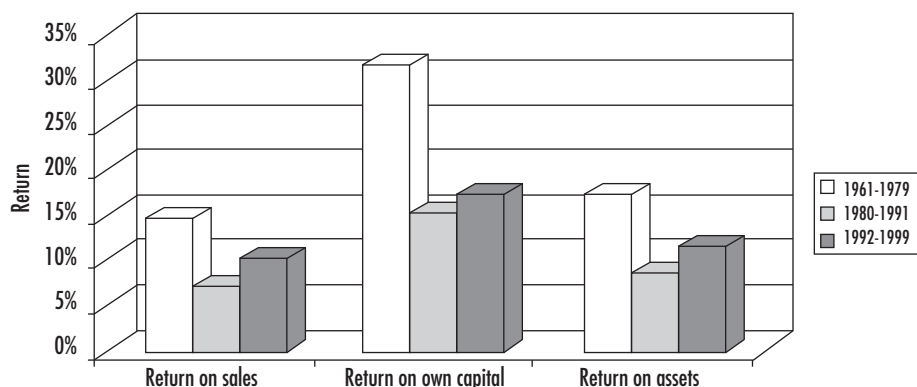
During the first period, assets and average sales were slightly under \$40 million (in constant 1995 peso terms) and shareholders' equity was close to \$20 million; during the second period both assets and sales were more than six times the level of the former, reaching a level of an annual average of around \$250 million. Finally, in the last period, when relative growth was comparatively lower, (3.2 and 3.1 times, respectively), assets amounted to around \$700 million and sales were in excess of \$800 million, while equity for its part had risen from \$130 million to \$500 million. It is interesting to note that investment in property, plant and equipment performed in a similar manner, reaching average annual values of \$2.5 million, \$8.5 million and \$25 million in the three respective stages.



**Graph No. 4.** Average number of employees in the three periods.

The different average employment levels have been another indicator of the changes in the size of the business group during the four decades under analysis. In this case, the number of workers increased fourfold between the first and second stages, reaching a total of almost 4500. In the 90s, although the rate of hiring of personnel was lower (total growth of 112%) absolute growth was considerable and the annual average level of employment was over 9500.

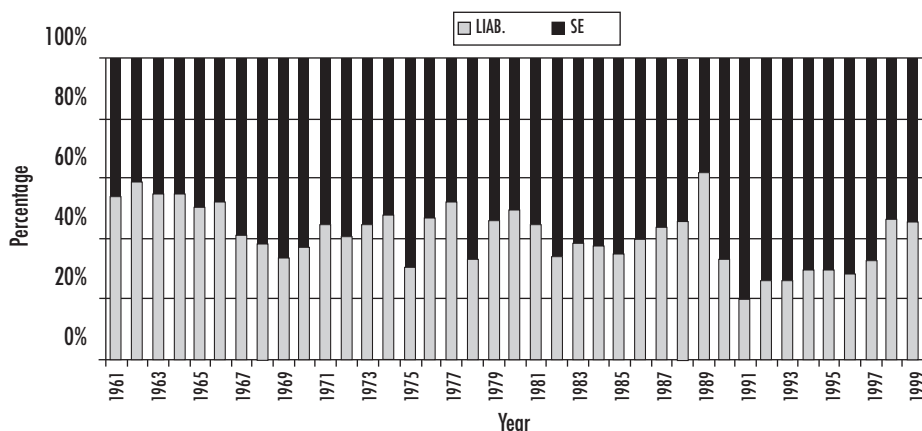
These various phases of growth recorded by ARCOR in the context of a history of continuous growth, were accompanied by differing trends in the group's operating results, as can be seen from the various estimated profitability indicators.



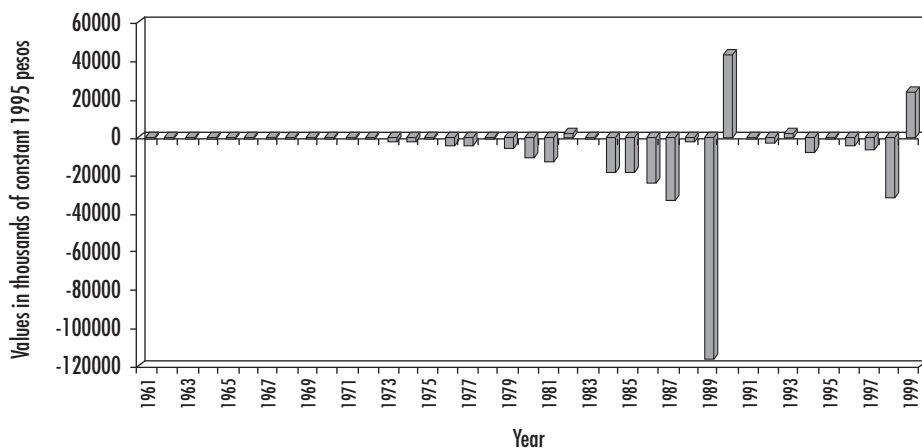
**Graph No. 5.** Comparison of return between periods.

In effect, average profitability in the first stage is in all cases the highest and tends to decline considerably, although remaining positive, in the next phase corresponding to the decade of the 80s, which was also the period of greatest macroeconomic instability when recession predominated on the domestic market. Subsequently, matching the general trend of global economic variables, all ARCOR's profitability indicators showed a significant recovery.

Analysis of the evolution of the composition of assets in relation to liabilities and shareholders' equity and financial income and expense in the various periods provides an indication of how the company has financed its activities and results. Shareholders' equity accounts for between 40 and 80% of the Total Assets during the whole period, with predominant values of between 40 and 60% during the first 30 years and between 60 and 80% during the last 10 years. Two years that stand out in this regard are 1962 and 1989, when the proportion of Total Assets accounted for by liabilities reached maximum values of 60% and 62% respectively.



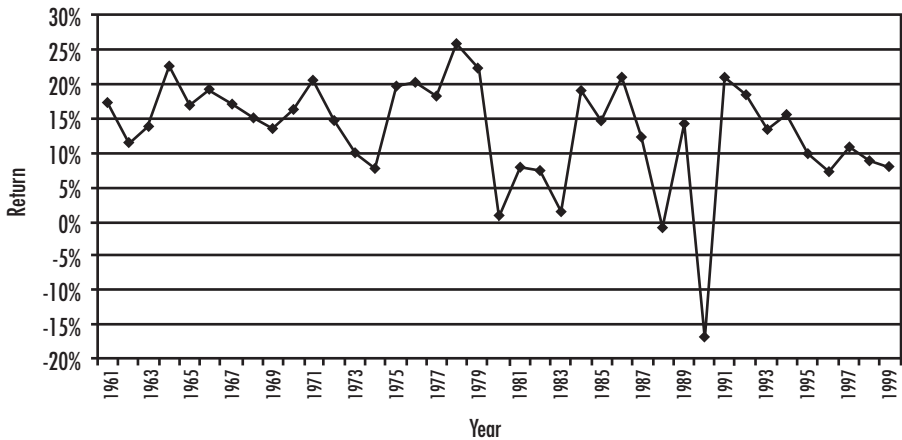
**Graph No. 6.** Evolution of the composition of total assets.



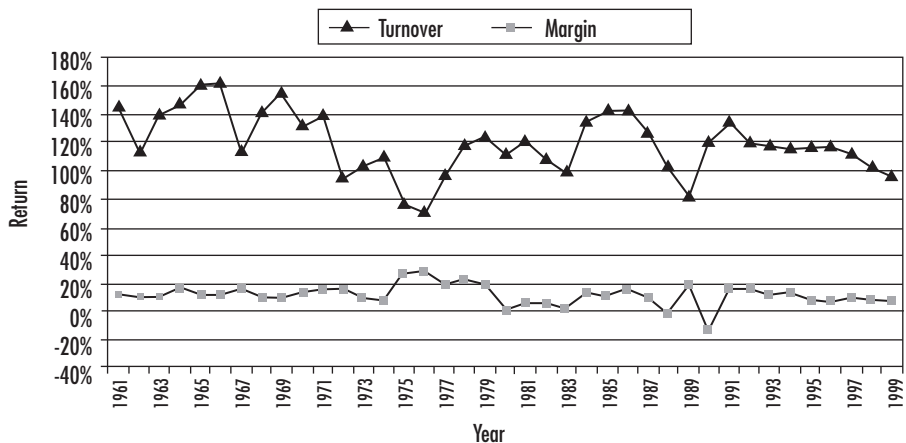
**Graph No. 7.** Evolution of Financial Income and Expense.

The negative effects of financing in absolute values tend to rise over the whole period, although the proportion of liabilities that finance assets declines. The only years in which financial income consistently exceeds expenditure, leaving the company with a positive balance, are 1990 and 1999. After a period in the eighties during which they rose steadily, financial expenditure reached a peak in 1989, the year in which the company had to absorb the greatest costs (around \$ 120 million). The size of the liabilities also grew in that year. In addition, in the second half of the nineties an increase in the cost of liabilities was also recorded.

Evolution of the group's profitability can also be followed by means of two indicators: return on assets and return on shareholders' equity. In turn, the evolution of the components of the two indicators —asset turnover, costs of liabilities and the indebtedness ratio- provide the basis for analysis of the behavior of the factors that explain the profitability achieved. Return on assets indicates the profitability of the company's activity, regardless of how it is financed, while return on net equity taken into account the financial effects.

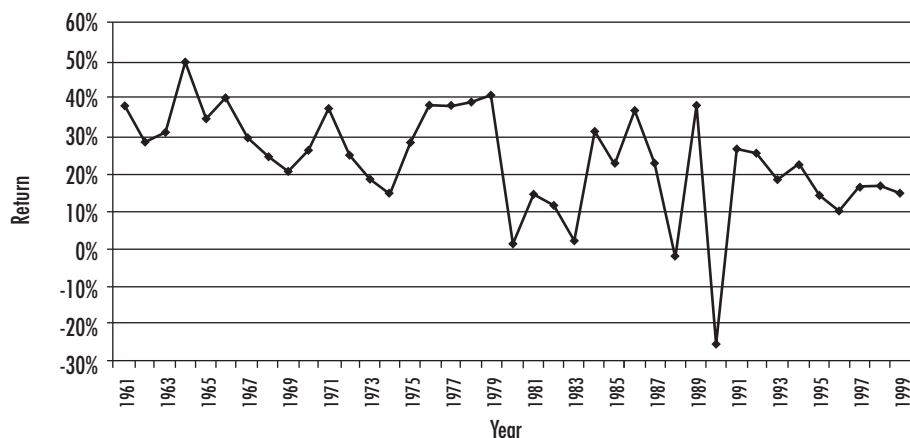


**Graph No. 8.** Evolution of return on assets.



**Graph No. 9.** Evolution of components of return on assets.

The return on assets ratio<sup>3</sup> for the ARCOR group shows high and increasing fluctuations. It ranges between 12% and 22% until 1971, between 7% and 26% until 1979 and between 0 and 22% during the decades of the 80s and 90s. It reaches a maximum level of 26% in 1978 and a minimum of 17% in 1990. However, a slight downward trend can be observed for the period as a whole, explained both by a drop in the average for asset turnover as well as a declining trend, particularly in the 90s, in margin on sales (from around 15% in the eighties to 8% in the following decade). For its part the turnover indicator begins the long period at levels of between 1.8 and 1.2 in the sixties, fluctuating between 0.8 and 1.5 in the seventies and eighties and ending at levels of between 1.2 and 0.9 in the last years of the period.



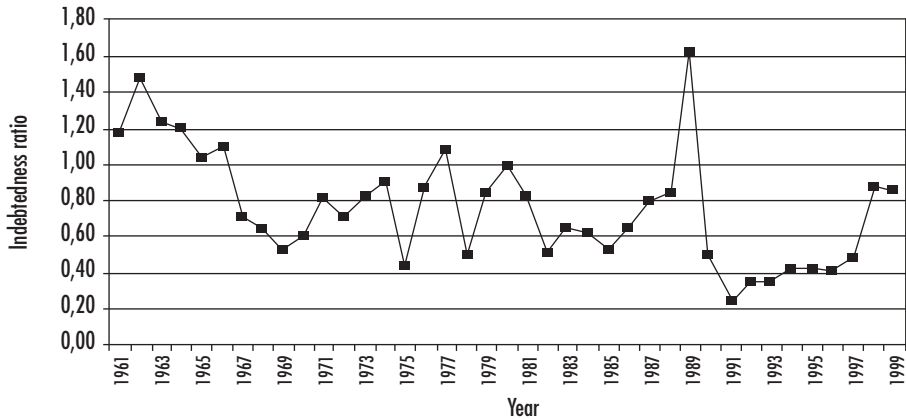
**Graph No. 10.** Evolution of return on shareholders' equity.

Return on shareholders' equity indicates the return that shareholders obtain on their own resources. In the case of ARCOR, the return on shareholders' equity, like the return on assets, records a slightly downward trend over the long term within the period analyzed. In turn, the high profitability on own capital during the first decade can be explained by the considerable difference between profitability on assets and the cost of liabilities (based on the high cost of borrowing) combined with a significant indebtedness ratio<sup>4</sup>. When

<sup>3</sup> Profitability on assets can be divided into two components: margin on sales (profit before financial costs on sales) and turnover (sales over assets).

<sup>4</sup> Return on shareholders' equity can be broken down into  $RAT + (RAT - CL) * IR$ , where  $CL$  = cost of liabilities and  $IR$  = indebtedness ratio. However, to calculate this indicator the effects

Return on Assets is higher than the cost of liabilities, it is profitable for shareholders to borrow, as the resources received on loan generate a return that is higher than their cost.



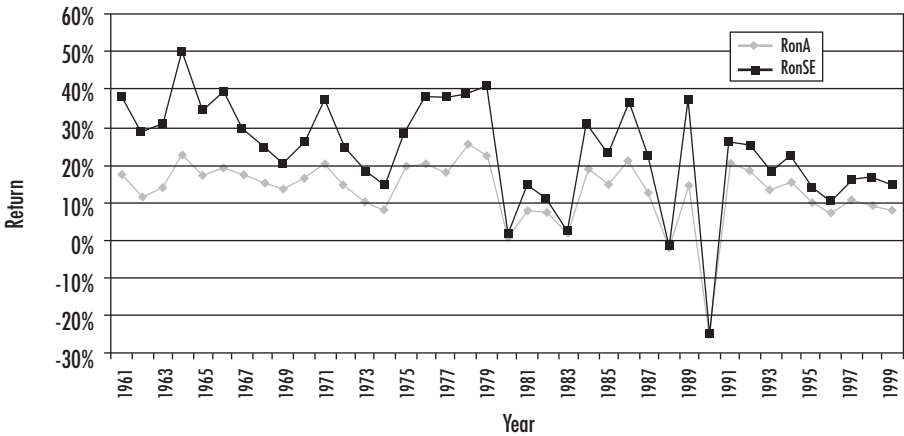
**Graph No. 11.** Evolution of indebtedness ratio.

Towards the end of the 70s and during the 80s shareholders' equity tended to decline. Costs of borrowing recorded a rising trend<sup>5</sup>, in some cases approaching the return on assets, and the reduction in the indebtedness ratio was insufficient to compensate for this trend. During the first half of the 90s, on the other hand, the return on assets was again well above the costs of liabilities. This circumstance is not reflected in an increase in the return on own capital allowing maximum historical levels to be achieved, as there was no similar increase in the indebtedness ratio. Lastly, it should be noted that the two years of negative return on shareholders' equity (1988 and 1990) can be explained by a combination of large differences between the cost of liabilities and the return on assets and high levels of indebtedness. In such situations the company still borrowed, even though the resources obtained in the form of loans obtained a yield that was below their cost.

*of financing were taken into account, that is to say, net financial costs. It is for this reason that negative costs arise in the years in which financial income was higher than financial costs.*

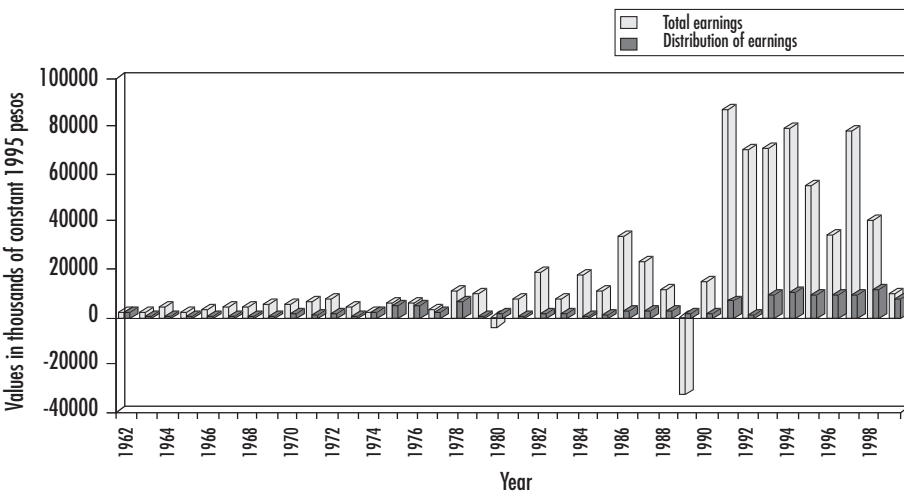
<sup>5</sup> With exceptional years in which the firm received financial income that was higher than its financial costs.



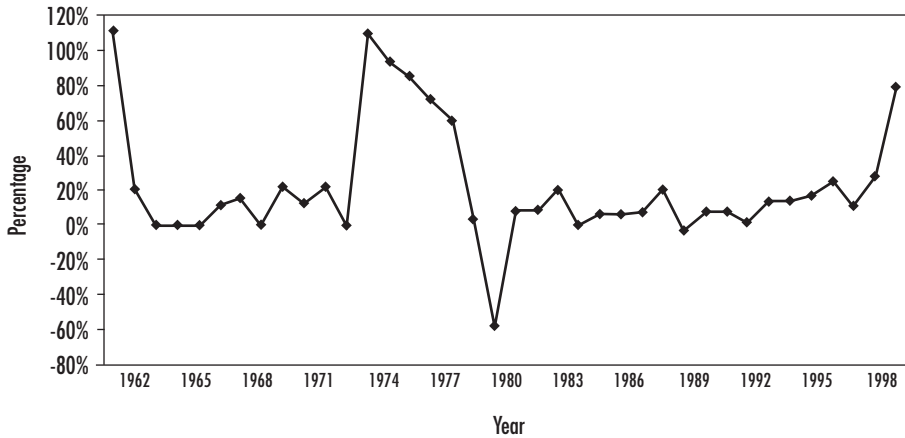


**Graph No. 12.** Evolution of return on equity and assets.

To sum up, in its early years ARCOR recorded a significant positive difference between the return on own capital and that on assets, an indication of the existence of adequate financial conditions. However, this difference tends to decline considerably as from the end of the eighties and during much of the nineties, explained fundamentally by an increase in financing costs and to a lesser extent by a reduction in the inclination to borrow funds on the market.

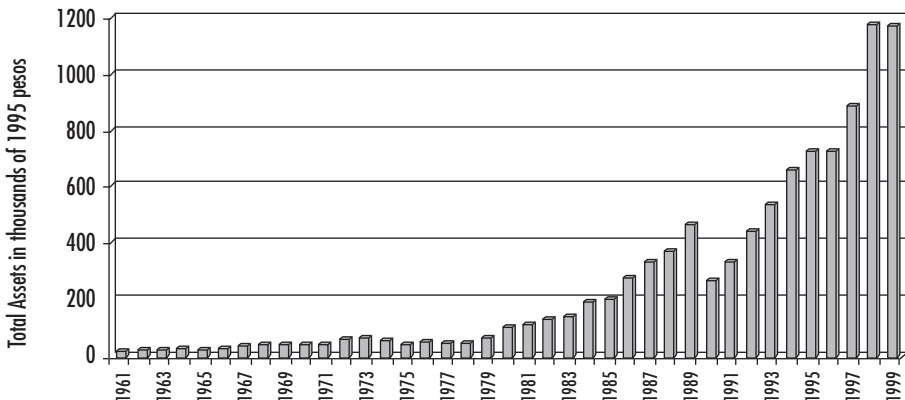


**Graph No. 13.** Distribution of earnings .

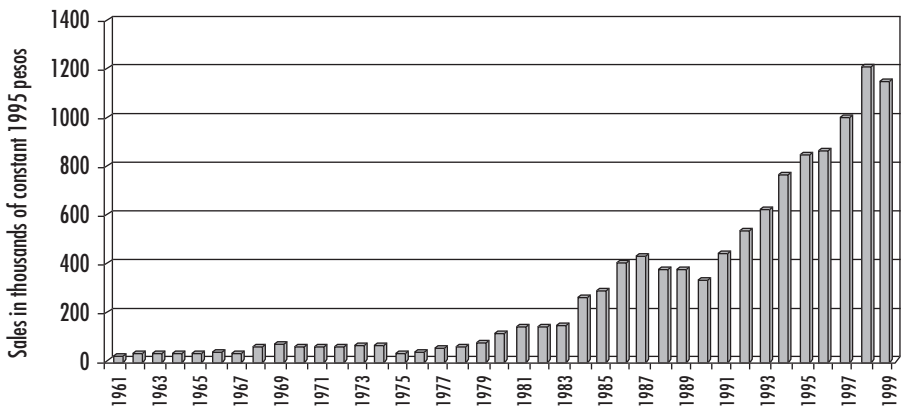


**Graph No. 14.** Distribution of profits as a percentage of total earnings.

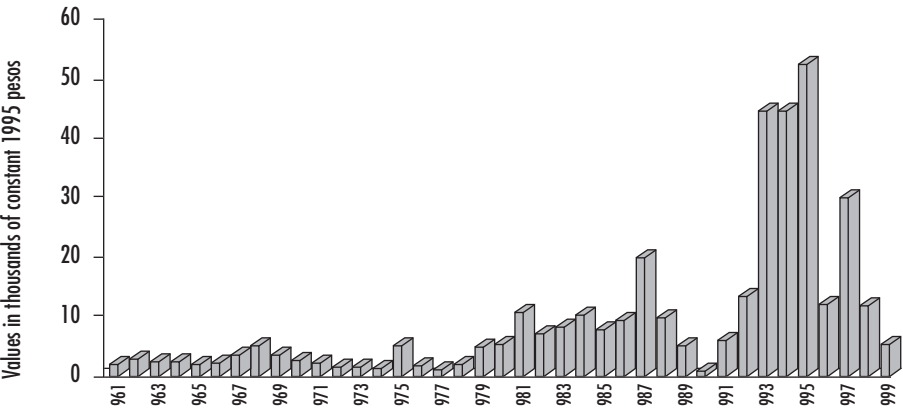
Lastly, it is interesting to consider the trend in the distribution of earnings process. In general terms the ARCOR group has been noted for austerity in this regard, assigning priority to reinvestment. Over the period considered, it can be seen that the amount of earnings distributed remains fairly constant in the various different stages, remaining in most years at a level of between 5% and 20% of total net income.



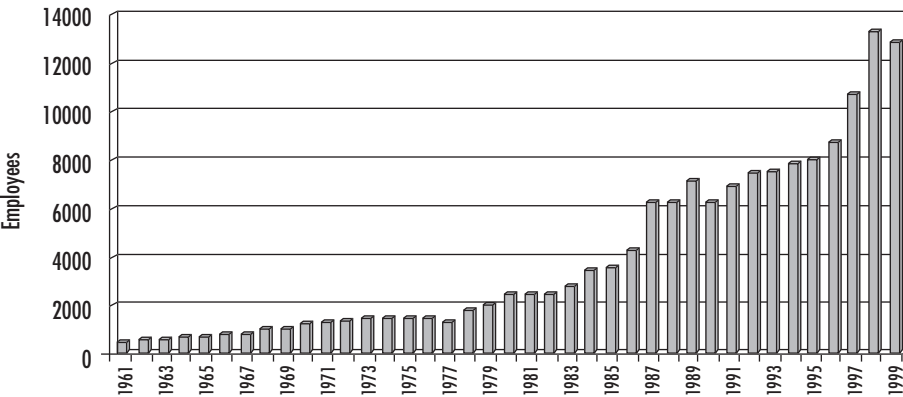
**Graph No. 15.** Total assets.



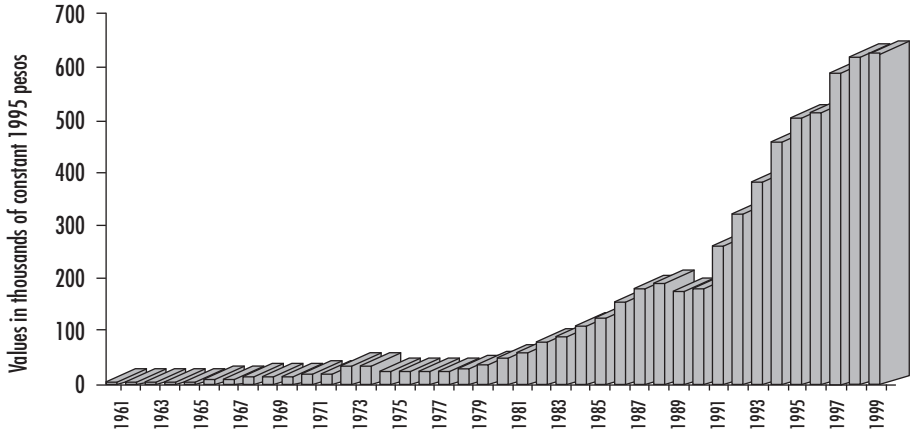
**Graph No. 16.** Sales.



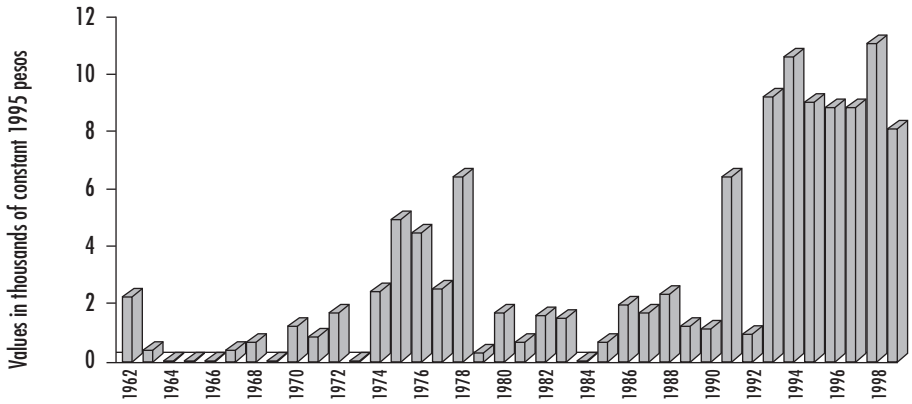
**Graph No. 17.** Increase in fixed assets.



**Graph No. 18.** Employment.



**Graph No. 19.** Shareholders' equity.



**Graph No. 20.** Profit distribution.



## CHAPTER 2

# From Foundation to the Development of the Dominant Local Enterprise. The Years from 1951 to 1990

*María Inés Barbero  
assisted by Anabel Marín*

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> Origins

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> The Development of ARCOR Between 1951 and 1990

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> Stage One: The 50s and 60s

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> Stage Two: The 70s

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> Stage Three: The 80s

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> Summing up Four Decades



## ORIGINS

### Argentine Industry in the Early Fifties

At the time ARCOR was established in 1951, Argentina was experiencing a period of profound transformation. The 1946 elections which had made Juan D. Perón President of the Republic were a political expression of new economic conditions and the emergence of new social structure. From an economic standpoint, the most notable features were the development of industry—which since the thirties had become the most dynamic sector of productive activity—and the growing role of the State as a regulator.

Industrial development in Argentina was a gradual process that began at the end of the 19th century, stimulated by the modernization that accompanied the boom in the agricultural exporting system. Between 1875 and 1912 the annual rate of per capita GDP increase was almost 4% thanks to the successful participation of Argentina in world markets as a producer of foodstuffs and raw materials, with strong competitive advantages because of the availability of vast expanses of fertile land (Cortés Conde, 1997).

Although the farming sector was the force behind the growth recorded until 1930, the development of primary activities had an impact on the rest of the economy from the point of view of both supply and demand. The growth in production and export of agricultural products, the increase in population—which thanks to immigration rose from under two million inhabitants in 1869 to almost eight million in 1914—development of transport and services and the process of urbanization contributed to the generation of a growing demand for manufactured goods and created a suitable environment for industrial development.

Increases in manufacturing output were stimulated by the supply of raw material, the rise in exports and increased domestic demand. Although the latter was mainly satisfied by imports, as the century progressed the degree of substitution rose and the local production of industrial goods increased. In the period 1900-1904 the ratio of imports to total demand for manufactured goods stood at 58.6%, falling to 51.1% in 1925-29 (ECLAC, 1958).

According to data from the national census, the number of industrial establishments doubled between 1895 and 1914, and the number of workers they employed grew by 145%. On the eve of the First World War manufacturing industry already accounted for over 16% of GDP and during the 20s the development of local industry accelerated even further, encouraged by the growth of the economy and a rise in import duties.



Throughout this stage industry was dominated by light or traditional activities, with a strong predominance by the food sector, which in 1914 represented 53% of the total value of output. Towards the end of the twenties the largest industrial enterprises were the meat packers, sugar mills, large flour mills, wineries and breweries.

The crisis in 1929 and the depression during the thirties significantly modified the conditions on world markets and within the Argentine economy. The fall in volumes and the prices of export goods restricted the country's importing capacity, accelerating the substitution process. Between 1930 and 1950 the import of manufactured goods fell from 45% to 15% of the total supply of industrial goods (Mallon and Sourrouille, 1973).

The thirties have been described as the age of industrialization through import substitution, not only because of the increase in the substitution coefficient but also because manufacturing industry became the most dynamic sector of economic activity, with a rise in excess of that of GDP and a share in total product that reached 23.7% in 1940 (ECLAC, 1978).

Substitution also benefited from public policy on restriction of imports, implemented by means of exchange controls and increased duties, as well as through an expansive fiscal and monetary policy as from 1933. The Second World War further reinforced the difficulties in importing manufactured goods, accelerating the development of local industry.

There can be no doubt that such growth would not have been possible without the existence of a prior industrial base and idle installed capacity, as between 1930 and 1945 production increased at the same time as gross fixed investment and net capital stocks declined (Díaz Alejandro, 1975).

The structure by sector of industry evolved, with a relative decline in the food segment, which dropped to 32.7% of total production in 1946, and significant progress by the textile, metallurgical and chemical branches, which in that same year contributed 13.5%, 7.6% and 7.4%, respectively (1947 *Industrial Census*).

As from the early thirties State intervention in economic activity began to increase, with a bias towards rising industrial protection by means of tariff and exchange rate measures, as well as through credit policy as from the forties. Measures adopted to restrict imports and moderate the effects of the crisis benefited the manufacturing sector, although the development of the industrial sector was not explicitly intended. However, as from the beginning of the forties, industrial promotion became Government policy. This was largely due to the importance that industry had gained as a source of employment, pressure from the sectors involved and also the pro-industry position of the

armed forces, which were starting to play a growing political role which crystallized in the revolution of June 1943.

The forties also saw the development of the business State, with the setting up of *Dirección de Fabricaciones Militares* and a group of public enterprises formed by companies created or expropriated during the war and those nationalized in the post-war period.

Government policies adopted as from 1930 generated a transfer of resources from agriculture to industry and severe distortions in relative prices. The share of GDP accounted for by the primary sector fell significantly, from 33% in 1925-29 to 16% in 1947-49 (Díaz Alejandro, 1975). This process had a negative repercussion on farm output, particularly grain production, and gradually limited the exporting capacity of the country by creating imbalances that grew sharper in the early fifties.

The crisis in agriculture and the development of industry had a strong impact on society. The agricultural crisis drove population away from rural regions, giving rise to internal migration towards the large urban centers on the coast. As a result of these migrations and the growth of the manufacturing sector the number of industrial workers rose from 796,700 to 1,185,600 between 1940 and 1945, at the same time as union membership rates increased. Import substitution also favored the birth and development of small and medium-sized domestic capital firms, and industrial enterprises were set up in the littoral region and in the interior of the country.

With the rise to power of a Peronist government a strong income redistribution stage began that benefited salaried workers and reached a peak between 1945 and 1949. In those years real wages went up by 60%, and in 1948 the salary component of national income reached 53%, for the first time exceeding income from profits, interest and income from the land (Gerchunoff and Llach, 1998). Workers significantly increased their consumption capacity, which led to a rise in demand and the creation of a mass market in non-durable and durable industrial goods supplied by local production.

In spite of the fact that the early years of the fifties were critical to the Argentine economy because of the imbalances in the external sector, the circumstance in which it developed were especially favorable to the rise of domestic capital firms. The domestic market was protected by high tariffs, the demand for mass consumer goods was very high thanks to the level achieved by wages and government policies were directed towards promoting local industry.

Between the industrial censuses of 1947 and 1954 the number of establishments almost doubled, and this was due mainly to the creation of small-and medium-sized domestic firms. ARCOR was one such firm.

### **Immigrants and the Development of Industry**

*Immigration played a decisive role in the early days of industrialization. Between 1870 and 1930 over three million immigrants settled in Argentina, making it the country that took in the greatest number of immigrants in proportion to its total population. In 1914 one out of three inhabitants of Argentina had been born abroad, but as distribution was not uniform, in some areas, such as farming colonies and the large cities on the littoral, the proportion was much higher. The main flows arrived between the end of the 19th century and 1914. Immigration halted during the First World War and picked up again in the twenties, although without reaching pre-war levels. In the period prior to 1930 almost all immigrants came from Europe, with a strong component of Spanish and Italians, followed far behind by immigrants from Central and Eastern Europe. There were various forces at work behind the decision to emigrate. At a macro level, there was a combination of factors that drove people out of their countries of origin (economic, social, political and religious) and the attractiveness of Argentina (demand for labor, wage differentials, exchange differences, availability of land, opportunities for business). On a micro scale, networks of personal relations played a decisive role, as many immigrants chose their destination and obtained their first jobs thanks to the help of relatives, friends or people from the same region who had arrived earlier. In general, the decision to emigrate was part of a family strategy, whereby some members of the family group became expatriates in order to provide support to those remaining behind, or to act as a vanguard for subsequent emigration by other members of the family. These immigrants contributed actively to the development of industrial activity as workers, entrepreneurs and consumers. In 1914, 64% of all owners of industries were foreigners, as were 49% of the workers employed in industry. In 1935 foreigners owners were still numerous, making up 55% of the total. The high participation by foreigners in the manufacturing sector is explained in part because their proportion within the economically active sector of the population was very high, as well as because industry was a sector in constant growth that was not sufficiently attractive to the native population, and immigrants could have certain advantages. Generally speaking they were very versatile and adapted to different types of work. Although most were originally agricultural workers, they tended to have some experience in craft industries. Some immigrants were craftsmen who resisted joining the proletariat and continued to work at their craft in their country*

*of destination, others were technicians seeking better opportunities and the possibility of becoming established as independent businessmen. In most cases immigrants acquired a skill in Argentina as a result of their work experience. This process was facilitated if they had contacts that offered them work opportunities, instructing them in new skills and competencies. Almost all immigrants that founded industrial establishments began as workers or craftsmen who later set up their own businesses, or tradesmen who invested in industry when they had built up sufficient capital. In general they set up family businesses, with the participation of brothers, parents, sons and other relatives. The network of parents and friends that supported emigration also served as a base for the setting up of companies, various individuals often coming together in order to gather the capital required to set up a firm. The contribution by immigrants to the growth of industry was also a product of the role they had played in the development of agriculture. In the regions of agricultural colonization —particularly the “pampa gringa” that extends across the province of Santa Fe and the east and south-east of the province of Córdoba— the expansion of grain farming required the development of business skills, generated a rising demand for industrial goods and gave an impulse to urban development and the diversification of local economies. The location of suitable land, decisions on the adequate size of agricultural units or the type of machinery most suitable for the exploitation were not easy or automatic processes, requiring adaptation and experiments that were carried out by immigrant settlers. This encouraged the birth and development of entrepreneurial capacities that to this day constitute a characteristic of the region. At the same time demand for inputs and machinery, the offer of raw materials and growth of the population stimulated the development of local industries in agricultural regions, and by the end of the 19th century some towns in the wheat belt had been transformed by the setting up of small and medium-sized work-shops.*

## **The Birth of ARCOR**

ARCOR was established on July 5, 1951 at the initiative of a group of young people led by Fulvio Salvador Pagani, the son of an Italian immigrant who had arrived in Argentina in 1924. They each had on business experience and had worked together previously. Putting together this association had much to do with the entrepreneurial capabilities of Fulvio Salvador Pagani and the potential for complementation that existed with his partners. As can be seen on previous pages, this association took place in a national context that encouraged industrial activity, with a closed, protected economy in a regional framework in which immigration and the development of agriculture provided a suitable environment for the flourishing of new undertakings.

### *The Pagani Family*

Fulvio Salvador Pagani's father, Amos, arrived in Argentina in 1924 from the region of Friuli, in north-eastern Italy. He came among the contingents of emigrants who left Europe in the early twenties after the end of the First World War, and headed to Arroyito, a town located 115 km to the east of the city of Córdoba, where one of his brothers had settled in the previous year. As in the case of most other Italian immigrants, he chose to settle where he already had a family network.

Amos Pagani had been a baker in Italy —like other members of his family— and during his first year in Argentina he worked in agricultural activities and as a bakery employee in order to raise the capital he needed to set up his own business. In 1925, once he had achieved this objective, he brought his parents and brothers over to Argentina and taught them his trade. Later on he left them the Arroyito bakery and opened another at La Para, 60 km to the north, where he moved with his wife, María Fabbro, in 1927.

Ten years after having set in motion his first bakery, Amos Pagani decided to diversify his business and began making soft milk candy, manually at first and, as from 1936, using an automatic press, enabling him to increase production and extend the range of sales to a radius of 200 km from La Para. Distribution was carried out using a delivery truck. Candy manufacturing represented an integration of activities, as it was common for bakeries to sell confectionery and other similar products.

In 1940 the Pagani family moved to the city of Córdoba so that their children could continue their education, as the school in La Para did not go past the fourth grade. His three boys —Fulvio, Renzo and Elio— began to work

with Amos, dividing-up candy and biscuits that they bought in bulk in Buenos Aires.

Fulvio studied at the local Commercial High School, looked after the administration of the company and helped in the distribution of the candy. Amos was in charge of sales and Renzo made deliveries with the help of a driver.

As a result of this business the Pagani family began to forge links with other confectionery manufacturers in the interior. In 1946 they made contact with a group of investors who were setting up a candy and biscuit factory at Sastre, a town in the province of Santa Fe close to the border with Córdoba. The partners in that company—which they had named SASORT—were interested at first in buying a machine that Amos Pagani used for wrapping candy at La Para, but once they got to know him they proposed that he should join them in their new venture.

### *New Companies and New Partners*

Amos Pagani joined SASORT as a partner, contributing his machine and the capital represented by his warehouse in Córdoba. In addition he worked as a travelling salesman, as did Renzo. Fulvio studied in Córdoba and worked for SASORT from there, but shortly afterwards he moved to Sastre to take direct charge of matters concerning costs and selling.

In Sastre the Paganis got to know another group of young people—Mario Seveso, Enrique Brizio and Modesto “Tito” Maranzana—who had been hired by SASORT but who had previously worked for the Córdoba firm of Boero and Sebaste in Las Varillas (60 km from Arroyito), at that time the largest candy factory in the interior. Seveso was a mechanic and Brizio and Maranzana were travelling salesmen. Within a few years they had all joined forces with Fulvio Salvador Pagani to found ARCOR.

That same year (1946), Amos Pagani, together with his sons and a group of friends, set up a cardboard plant in Córdoba. Meanwhile Fulvio Salvador, who was 18 years old, continued to work at SASORT, where he proposed to the owners that they should expand the scale of the company, concentrating on the manufacture of candy and increasing production to 10,000 kg per day, reducing costs and increasing the competitiveness of the firm. The partners in SASORT did not accept this proposal, which was to be the idea behind the creation of ARCOR a few years later.

In 1948 the Pagani brothers together with Enrique Brizio and the brothers Tito, Pablo and Vicente Maranzana purchased a cardboard company in Tucumán. They had in fact traveled to that city to purchase a machine for sewing

cardboard boxes, but the owner refused to sell single machines, as an alternative offering to sell all the installations on easy credit terms over ten years at an annual interest of 6%. This company was several times larger than the cardboard company in Córdoba, and initially seemed to be beyond the reach of the potential purchasers, but the insistence of the owner and the terms offered finally led to the deal being closed. This was the birth of Sociedad Industrial del Envase —SIDE—, which became managed by Fulvio Salvador Pagani and Pablo Maranzana.

Both the experience at SASORT and that provided by the cardboard company served to build up capital and experience that would later make it possible to create ARCOR. In these companies the future partners became familiar with manufacturing activities and began to make contact with markets in the interior of the country, and the investment in cardboard manufacturing was the basis of the future links of ARCOR to the packaging sector.

Between 1948 and 1950 SIDE grew to cover a market ranging from Rosario to Jujuy. As part of this expansion, Fulvio Salvador Pagani, Enrique Brizio and Mario Seveso traveled to Buenos Aires with the intention of buying a machine to manufacture cardboard trays. At this point Fulvio Salvador Pagani again raised his project for a candy plant producing 5000 kg per day, proposing using the profits from SIDE and contributions from partners and family to raise the initial capital for the new business.

This time his proposal was favorably received, and the partners agreed to set up a new firm which they called ARCOR, in reference to its location in Arroyito, in the province of Córdoba.

### *The Creation of ARCOR*

In May 1950 the building of a new plant began on a 10,000 square meter site in Arroyito. In June of the following year ARCOR SRL was set up as a company to manufacture candy, and production began almost immediately.

Start-up capital was provided by a group of partners formed by the Pagani brothers (Renzo, Fulvio, Elio), the Maranzana brothers (Tito, Pablo, Vicente), Mario Seveso and Enrique Brizio. There were also other smaller partners, making a total of 23 stockholders. They were all from Arroyito or the surrounding area and were relatives, friends or neighbors of the main partners.

Arroyito is set in an agricultural and livestock-breeding region. In the 1800s the local carob wood forests were exploited for charcoal and wood for paving blocks for use in Buenos Aires. The arrival of the railroad in 1888 and the beginning of immigration saw the forests being exploited on a large scale, with an era of prosperity that lasted for several decades. Saw-mills were es-



tablished, the population increased because of the demand for labor and small industries emerged to process raw materials of agricultural origin and to meet local needs.

Intensive carob-wood exploitation and indiscriminate felling led to the gradual disappearance of the forests. Towards the end of the twenties the crisis in the wood industry led to a period of decline that grew stronger during the depression of the 1930s. Part of the population had to emigrate and the number of inhabitants fell to almost half, with numbers dropping from 5000 to 3000 between the end of the twenties and the early fifties.

The choice of Arroyito as the place to set up ARCOR was based on several reasons. In the first place, it was a site where the Pagani family had already acquired business experience and a locality where the founders of the company had a network of friends and neighbors who together with the inhabitants of neighboring towns were actively involved in the setting up of the firm.

Arroyito also offered cost and location advantages. There was plenty of available labor, and for those wishing to work at the factory there was cheap housing at hand that had been vacated by workers who had emigrated when the carob forest exploitation ended. The main problem affecting recruitment of labor was the lack of skilled workers, which had to be hired in other urban centers.

Localization advantages included closeness to the provincial capital and the agricultural and industrial area in eastern Córdoba and central Santa Fe, traversed by the Belgrano railroad and a paved national highway (Route 19) linking the capitals of the two provinces. Both the location and the communications links facilitated the distribution of production in a regional market with a strong demand capacity and reinforced contacts with locations in the so-called "*pampa gringa*" where technical personnel and specialized labor were hired and where the company acquired its first machines. The railroad facilitated the supply of sugar from the province of Tucumán and also provided links to the cities of Córdoba and Santa Fe.

Location in Arroyito also guaranteed supplies of milk, used as a raw material in the manufacturing of candy, as dairy farms had been set up after the crisis in the wood industry. Lastly, good water quality represented yet another advantage, as it was an essential requirement for the proper operation of the machinery and was not available in other local towns, where high salinity was harmful to pipelines.

One of the main disadvantages was the insufficient supply of electricity. Power was cut off at midnight, so the factory required its own generator,



which was replaced by larger units as time went by. In 1955, at the instigation of Fulvio Salvador Pagani, the *Cooperativa Eléctrica de Arroyito* was set up to operate a 750 hp power plant. Later ARCOR set up its own turbine generator.

### *An Entrepreneurial Event*

A company is born as a product of a decision taken by an individual or a group of individuals that choose one path over other alternatives. For the purposes of economic theory as well as other disciplines, models have been designed with alternative explanations, highlighting either the personal traits of the entrepreneurs or the characteristics of the contexts within which new companies are created.

The focus on personalities explains the birth of companies taking individuals as the basic unit for analysis, highlighting either the roles that the entrepreneurs have played within the economic system —innovating, assuming risk, acting as a stabilizing factor— or certain particular aspects of their personality considered to be relevant, including the desire to succeed, the need for independence, the need to control, etc..

These approaches of a highly psychological nature have been challenged by various analysts who have upheld the position that analysis of the birth of a new business ought not to be centered on the individuals responsible for it but on the combination of events and situations that surrounded the entrepreneurial event. In this regard Shapero (1978) has proposed the study of the creation of a company —which he defines as an “entrepreneurial event”— as a result of the influence of cultural, economic, sociological and psychological variables; considering individuals as one of the relevant factors, although not the only explanation. From this perspective the creation of a firm is perceived not as a predetermined event since the birth of the protagonists themselves but as a process whereby the entrepreneurs are molded on the basis of their social interaction in the framework of specific contexts.

Social interaction is also emphasized by the networking approach, in which relations between players have a precise, defined role, and extra-economic factors, such as trust and commitment are considered to be relevant in the formation and functioning of enterprises. The entrepreneurial group concept, for its part, underlines the importance of the complementing of the skills of various individuals as a central element for the analysis of the rise of new companies.

The creation of ARCOR was the result of action by a group of individuals linked by bonds of friendship, with prior industrial experience who had previously participated in joint undertakings. On the basis of such experience

they decided to set up a new company in a context favorable to the establishing of new industrial companies.

Fulvio Salvador Pagani was one of the outstanding figures in this group, having been the force behind the creation of ARCOR and the president of the company until his death in December 1990. Pagani combined personal traits and a family history that served as a stimulus and model for his performance as a businessman. His personal qualities included initiative, the ability to innovate, leadership skills and long-term vision, identifying him as an entrepreneur, as defined by Schumpeter.

In addition to his personal qualities, Fulvio Salvador Pagani had the advantage of being the son of an entrepreneur and having his father as a role model. He also had experience working in the family business and benefited from the resources that his father contributed towards his education and the setting up of ARCOR. The history of the Pagani family reflects many of the traits common to immigrant families that achieved successful integration in the local economy, including: the skill acquired by Amos in Italy, his decision to emigrate based on family networks, the accumulation of capital from work on an employment basis during his initial stage of residence in Argentina, the setting up of the first bakery in Arroyito and the association with members of the family and other Italian immigrants in the region of the *pampa gringa*.

However, in the birth and development of ARCOR, the presence of the other partners and interaction with the local medium were also determining factors. The existence of partners, particularly if they are friends, can help to transform a possibility into an action, providing the entrepreneur with funds, moral support, work and skills and the possibility of sharing the risks. All the members of the founding group had previously taken part in other confectionery industry businesses and had work experience, skills and knowledge regarding production matters. In addition, there was a high degree of complementation between Fulvio Salvador Pagani (the driving force behind the project, with experience in administrative areas), Mario Seveso (who had outstanding mechanical skills) and the partners who contributed their knowledge of the market and their abilities as salesmen (such as Enrique Brizio, Tito Maranzana and Renzo Pagani). The members of the group also had their credentials as independent businessmen in other fields, such as the soda plant at Sastre (belonging to Brizio and Maranzana), the Córdoba cardboard plant (Fulvio Salvador Pagani and his brothers) and the Tucumán cardboard plant. These earlier undertakings also provided an opportunity for hiring skilled labor, such as ARCOR's first master confectioners, who had previously held the same position at Boero y Sebaste and SASORT.

SASORT was also the environment in which the idea of forming a new company first arose, as a result of the lack of satisfaction from having to work for others, aggravated, in the case of Fulvio Salvador Pagani, by the refusal of the owners to accept his proposal to specialize in the manufacture of candy to increase the scale of production.

The structure of the group and the relationship between its members in the local environment provided economic feasibility for the project, combining personal, family and community contributions. Initial capital was provided by the founders and their families, as well as by friends and neighbors from Arroyito and other nearby towns, particularly Las Varillas, which provided the partners that had worked for Boero y Sebaste there. The fact that they were all immigrants or sons of immigrants from Italy also reinforced the bonds of solidarity, as they all shared an ethnic and cultural background.

Interaction with the local environment not only made it easier to obtain of material resources, it also ensured that the company start-up and its operation in the early years was to be the result of a collective effort that implied a level of commitment and a capacity for work that, to a large extent, compensated for the difficulties of the initial moments. The stories told by the protagonists of that stage are full of references to the feverish rate of work in the early days, without timetables or weekends, with permanent contact between partners and company workers. In the eight months prior to the start-up of ARCOR, Fulvio Salvador Pagani traveled constantly from Tucumán (where he was based) to Arroyito, Las Varillas, Sastre and Buenos Aires. The cult of personal effort was typical of immigrant culture, at a stage when upward mobility was one of the distinctive features of Argentine society, and has been perceived by the company as one of its strengths.

Families were also very much involved in the project. Wives helped in the plant, performing tasks such as candy-wrapping, cleaning of machinery, preparing food for visiting customers or lodging business visitors to Arroyito, as the local hotel infrastructure was inadequate. As ARCOR was one of the few sources of employment in Arroyito and the economic life of the community depended to a large extent on the success of the company, the population as a whole had an interest in its success.

There can be no doubt that the combination of all these elements explains the success of the undertaking, which has involved many of the personal and contextual factors that have been identified, in case studies and in the entrepreneurship theory, as providing an impulse to the incubation, formation and early development of new companies.

## THE DEVELOPMENT OF ARCOR BETWEEN 1951 AND 1990

Over the course of its first forty years of existence, ARCOR grew steadily, with the adoption of strategies for expansion in response to both the internal dynamics of the firm and changes that took place in the macroeconomic context.

Although segmenting into periods could be considered arbitrary, it is possible to define three stages in the evolution of the company between 1951 and 1990. The first covers the fifties and sixties, during which time the firm developed its competitive capacity in production—through scale integration and distribution—establishing a sales network in the interior of the country. Growth was based on a constant increase in candy production—a segment in which the company gained a high market share as a result of competitive pricing—and an incipient diversification during the sixties. In this period ARCOR became a multiple plant integrated company, with its center of operations in Arroyito—where new plants were gradually added to the existing installations—and some production facilities in the city of Córdoba.

A second stage took place during the seventies, when the basis of expansion for ARCOR became diversification, geographical decentralization and progress in new markets. Although candy manufacturing remained the firm's main business, it also developed as a foodstuff producer, and both the process of integration and the generating of economies of scale were translated into a growing diversification of its product offer. The firm's process of diversification and integration took place largely through the setting up of related companies, ARCOR becoming the head of an economic group made up of legally independent companies in which it held a controlling interest. Geographical coverage increased during the seventies with entry into the metropolitan region and a steady rise in exports, which had begun in small quantities at the end of the sixties. It was at this stage that the company began to manufacture on an international scale, with investment in branches in Paraguay and Uruguay, the first steps in the setting up of a multinational corporation.

The eighties were years of consolidation for the economic group, on the basis of the establishing of new subsidiaries, decentralization and internationalization. To support this growth the company continued to diversify both products and geographical coverage, significantly increasing its output and its share of the domestic market, supplying 70% of the local confectionery market. The setting up of a manufacturing facility in Brazil was a decisive

step in the development of the company's international presence, reinforcing the multinational profile that ARCOR had acquired at the end of the seventies.

While in previous decades investment had been aimed mainly at production and distribution, the eighties saw investment in other areas, mainly marketing and finance. During this stage there was a steady search for increased competitiveness in costs through improvements in organization, reaching a head with the restructuring carried out in 1990, when the group took the form of a *holding* company with a multidivisional structure.

## Stages in the Development of ARCOR

### **The fifties and sixties**

Development of a multiple plant company. Building of competitive advantages: scale, integrated production, domestic market distribution network, with focus on the provinces in the interior of the country. Steady growth and high profitability.

### **The seventies**

Birth of the economic group. Diversification and decentralization of production. Distribution: progress towards the metropolitan region and increase in market share. Exports and beginnings of manufacture at international level. Lower rate of growth than in the sixties, with strong fluctuations, in an economic context that was less stable than in previous decades.

### **The eighties**

Consolidation of ARCOR as an economic group and international expansion. Increased diversification of products and markets. Setting up in other provinces of the interior: decentralized industrial complexes in the framework of industrial promotion regimes. Restructuring of the organization in 1990: adoption of a multidivisional structure in response to the decentralization of production and increased management complexity. Strong growth in sales and assets, although with marked fluctuations in profitability, in a very turbulent context, with high inflation.

## STAGE ONE: THE 50s AND 60s

### Macroeconomic Context

*Strong growth in the second half of the forties came to a halt in the early fifties, and the first twenty years in the life of ARCOR took place in a context of political, social and economic instability, although as from 1963 economic conditions did improve significantly. Overall economic performance was poor during the 50s, with an average growth in GDP of 2.9% p.a., and much better in the 60s, when the average growth rate was 5.5% p.a. Growth was not constant, as periods of expansion alternated with stagnation and recession (1952, 1959, 1962-63), making stop-go cycles one of the distinctive features of the period. In comparative terms, the rate of growth for Argentina was lower than that of the world economy and that of the most developed countries of Latin America. As regards the industrial profile, in the mid-fifties the first or “easy” substitution phase based on the consumer goods industry was exhausted and a second substitution phase was begun, based on chemical and petrochemical complexes and the metals-to-machinery sector, led by the automobile industry. From a political and social point of view these were unstable decades, with alternating civilian and military governments being a feature of the whole period from 1955 to 1983. In 1955 Perón—who had begun his second mandate in 1952—was overthrown by a civic and military revolution known as the “Revolución Libertadora”, which was followed by the presidencies of generals Lonardi and Aramburu. At the elections in 1958 a civilian government led by A. Frondizi (UCRI) took power, only to be overthrown by another military coup in 1962. Following the presidency of Guido (1962-63), elections in 1963 established a civilian government under A. Illia (radical), who was in turn overthrown by the military coup that took place in June 1966. That was the year of the start of the so-called “Argentine Revolution” during which time three military presidents ran the government: J.C. Onganía (1966-70), M. Levingston (1970-71) and A. Lanusse (1971-73). It was only in 1973 that the prescription that had been imposed on the Peronist party at the elections in 1958 and 1963 was lifted. From a social perspective the decades of the 50s and 60s were years of strong tensions and struggles for the distribution of income, with periods of strikes and mobilizations during the presidencies of Frondizi and at the end of the Onganía years. In the field of the economy, since the fifties there were a series of measures and counter-measures conditioned by imbalances in the foreign sector which exposed the fragile nature of the first substitution phase, based on the manufacture of consumer goods for the domestic market. One of the structural weaknesses of this industry was that it obtained a high proportion of its*

raw materials, input and machinery from abroad but aimed all its output at the domestic market, without generating the necessary currency earnings to continue to grow, as export earnings continued to be provided by agricultural exports. By the end of the forties installed capacity was being fully utilized, and it was impossible to reduce imports without affecting local industrial production. During the period, macroeconomic policies alternated between expansion and more or less orthodox stabilization plans implemented one after the other for very short periods, generating a considerable instability in the rules of the game. The overall economic situation had already begun to deteriorate because of the increasingly complicated picture in the external sector. Falling exports following the droughts affecting the harvests in 1949/50 and 1951/52 severely restricted import capacity. In 1949 both imports and exports declined by almost a third, and remained at that level during the following three or four years. As from 1952 the government introduced a stabilization plan with the aim of resolving the problem of the foreign trade deficit and fighting growing inflation. Changes were made that affected income policy, exchange policy and controls on imports and the handling of foreign capital, with measures that encouraged foreign investment. In 1953 an economic recovery took place as a result of the austerity measures adopted and improved export levels, but until the end of the fifties the balance of payments deficit and inflation were a recurring economic problem. Between the fall of Peronism and the assuming of the presidency by Frondizi in May 1958, various stabilization programs of an orthodox nature were adopted, in a climate of growing political and social tension. The Frondizi government itself, after its first months of expansive policies, resorted to orthodox measures to control inflation and spending and balance the trade accounts. Notwithstanding such changes in course and cyclical fluctuations, this development-minded government initiated a period of industrial promotion based on the attracting of foreign capital and the search for vertical expansion in the industrial sector, providing support for the development of basic branches of industry. The aim of this policy was to take advantage of natural resources and achieve equilibrium in the balance of payments through an intensifying of the import substitution program in the context of self-sufficiency in areas such as oil, steel, paper and pulp etc.. The intention was to overcome the limitations of the first period of substitution, during which industry remained highly dependent on the import of input. The measures implemented since 1958 had a profound impact on the manufacturing sector, which gained in visibility as the sixties progressed. There was a massive installation of multinational companies —benefiting from Law 14780— which



started to play an increasingly significant role in the local economy. Industrial expansion was led by dynamic new branches headed by the auto industry, with a significant presence by basic metals, chemicals, machinery and equipment. Industrial promotion Law 14781, passed in 1958, encouraged the import of machinery and equipment as it allowed the unrestricted import of capital goods not manufactured locally and had a great impact on local industry in terms of re-equipping and updating of technology. The Frondizi government fell in March 1962, in the midst of an acute recession that lasted during 1962 and 1963. There was a recovery as from 1964-65 and the economy continued to grow during the rest of the decade. The radical party government applied a monetary, fiscal and wage program that was expansive and promoted strong growth until the end of 1965. In 1966, the economy continued to grow, although at a lower rate and accompanied by a rise in inflation. Expansion returned as from 1967, keeping up a steady rate in subsequent years. The stabilization program introduced by the military government in 1967 (the Krieger Vasena plan) differed from those applied previously in that it combined a wage and price freeze with a shrinking of the fiscal deficit with a heavy program of public investment that acted as a recovery mechanism. The economy performed well until 1969, combining growth with stability, but the worsening social and political tensions during the year—which reached a peak in July with the Cordobazo disturbances—had a very direct impact in economic spheres. The last years of the military government were times of growing inflation, exchange rate instability and deteriorating public accounts, in a context in which the priority of the authorities was not economic but political. One factor making a decisive contribution to economic growth in the sixties was the rise in exports, which doubled between the beginning and the end of the decade. Between 1963 and 1970 the trade balance was positive, and terms of trade were more favorable than in the fifties. The most distinctive feature of this stage was that the increase was due not only to the rise in sales of agricultural products but also to exports of industrial goods, which between 1962 and 1972 doubled their share of total exports, from 10% to 20%. Growth was also based on the relatively new industrial structure that emerged following the investment boom in 1958-61, with a strong presence by branches of trans-national companies that grew in strength and market share as part of their long-term rise to maturity. In the ten years between 1964 and 1974 the annual rate of growth for industry from the beginning to the end of the period was almost 8%, one of the highest in Argentine history, with a simultaneous increase in industrial productivity, employment and exports.



## Introduction

The first twenty years of the history of ARCOR were a time for building competitive advantages in production and distribution by means of increased scale, integrated production and the creation of a distribution network within the domestic market.

The basis for this strategy adopted by the company, which was significantly different from that of other companies in the sector, was its specialization in the manufacture of a single item —candy— on a large scale, with cost competitiveness because of the economies of scale, the company's own production of its basic input and distribution system. ARCOR manufactured medium-quality goods aimed at the mass market, and by the end of the 60s it supplied 50% of the domestic demand for candy.

Since the end of the fifties increases in scale had been based on raising the technical component of production, with a leap in the level of technology between 1958 and 1960 —encouraged by the possibility of importing capital goods with zero duty during the Frondizi administration— and heavy investment in equipment throughout the sixties.

Integration of production was carried out with the aim of reducing costs in the supply of raw materials, input and machinery. Raw materials and input used by the company were produced locally, but supplies were affected by price problems —in particular in the case of input— and delivery times. In the early years machinery was built to overcome import restrictions, and since the end of the fifties for cost reasons —given the high price of imported equipment— and to avoid foreign currency debt.

At the same time as it invested in production, ARCOR was putting together a distribution system that represented one of its strategic advantages, thanks to its scope and the methods used. Since its beginnings the company developed sales to wholesalers, and during the sixties it began to add new channels. One of these channels was made up by cigarette distributors supplying kiosks. Another, which began to be used as from 1967, was sale through official distributors. By the end of the sixties, ARCOR had an efficient distribution network for the entire domestic market. Its main area of influence, however, was in the provinces in the interior, where there was less competition than in the city of Buenos Aires and its metropolitan area.

During this stage it acquired the features of a multiple-plant integrated enterprise, with its activities centered on Arroyito in the city of Córdoba, although continuing to operate as a single company and not as a group. Never-

theless, in the sixties it had already begun to invest in related companies, in agricultural and industrial businesses and in the production of input. It was still a medium-size, family-owned business, without any separation between ownership and management, with leadership strongly centered on the figure of its president, Fulvio Salvador Pagani. It began operating as a limited liability company (SRL), turning into a corporation (SA) in 1961.

### **Economic Performance of ARCOR During the 1960s<sup>1</sup>**

As can be seen from the information included in Chapter 3, the company grew constantly throughout the decade. The main increase was in shareholders' equity, which went up fourfold, rising from \$5 million in constant 1995<sup>2</sup> pesos to almost \$22 million in 1970, at an annual rate of growth of 16%.

Total sales and assets grew evenly. Assets rose from around \$11 million to \$35 million, with an annual growth rate of 12%, and sales went up from \$16 million to \$46 million, an annual rate of growth of 11%. Personnel numbers increased from 368 to 952, at a lower rate than sales. ARCOR increased sales from \$40,000 per worker (on average for the first three years) to \$60,000 on average for the last three years: a 50% increase in productivity, attributable to the constant investment in machinery and equipment.

Profitability indicators based on both assets and company capital recorded a decline over the decade, except for 1964 and 1966, when the initial values were maintained or increased. Profitability on assets, which at the beginning of the period was in excess of 20%, had fallen to 17% in 1970, and that corresponding to its company capital fell by almost half, from 50% to 26%. However, the most notable aspect of these figures has been the reduction in the gap between these two indicators, with a shrinking in the difference between the profitability on resources and that corresponding to the company.

The return on sales ranged between 15% and 9% without any clear trend, following the fluctuations in profitability of the main business, showing the limited impact of other activities on total profitability.

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<sup>1</sup> Information on the economic performance of the company as shown on the financial statements is available since 1961, when ARCOR became a corporation.

<sup>2</sup> All monetary values are stated in millions of constant 1995 pesos.

**Table No. 2-1** Evolution of principal accounting and profitability aggregates (monetary values stated in millions of constant 1995 pesos).

Year	Total Assets	Sales	Workers	Return on sales	Return on Assets
1961	10948	15930	368	15%	23%
1962	13146	15086	413	13%	18%
1963	13171	18498	454	10%	18%
1964	17947	26569	518	16%	26%
1965	15945	25862	568	10%	18%
1966	18061	29594	636	12%	22%
1967	28512	32731	609	14%	18%
1968	31749	45542	747	12%	18%
1969	34290	53160	785	9%	16%
1970	34848	46277	952	12%	17%

Source: Prepared on the basis of information from the company's financial statements. Information is stated in thousands of constant 1995 pesos.

## Technology and Production Aspects

### *Economies of Scale*

The strategy of manufacturing a single product —candy— on a large scale was intended to increase the competitiveness of the company through an increase in the volume of production and a reduction in unit costs. This was an innovative proposal in the category, as the remaining confectionery firms in the interior manufactured a very wide range of products, but all on a very small scale. In a speech at the end of the eighties, Fulvio Salvador Pagani said that he decided that “a way had to be found to manufacture a product on a massive scale and achieve a more competitive price than that of the remaining companies. At that time there were over one hundred candy manufacturing plants in Argentina”<sup>3</sup>.

Unlike the main confectionery manufacturers at the time, which made products directed at segments with a higher purchasing power, ARCOR aimed at the popular end of the market. At the same time it emphasized distribution in the interior of the country, while the big players concentrated on the metropolitan area and the main urban centers. This strategy was in harmony with the development of mass consumerism that had taken place since the mid-for-

<sup>3</sup> Quotes from Fulvio Salvador Pagani included in this chapter are taken from a speech delivered to an ACDE forum held in Buenos Aires in 1987. It was published in F. de la Rúa (comp.), Fulvio Salvador Pagani. A life in the service of his Country, Buenos Aires, 1991.

ties, as a result of the income distribution policies adopted. Candy was a low-price product, accessible to all, with widespread consumption in households.

Manufacturing candy was a simple, profitable business, and in the early years most tasks were manual. The process was performed on a batch basis, the paste was made with a lot of manual input, and products were largely wrapped by hand.

Two types of machine were used: equipment from the thirties purchased and fixed by Mario Seveso, and milk candy wrapping machines that were developed in Argentina, having been manufactured by a workshop in San Francisco in the province of Córdoba.

In 1956 Fulvio Salvador Pagani traveled to Europe for the first time, visiting candy manufacturers in Italy and Germany. He noted that comparatively speaking ARCOR was behind in the mechanization of work, as many of the tasks the company was performing manually were automated in Europe.

In Argentina the import of capital goods was restricted until the end of the fifties, which hindered the modernizing of the technology used by companies. ARCOR began procedures to obtain permits to import machinery that took two years. Only in 1958, during Frondizi's government, was it able to begin to renew its equipment as a result of newly introduced policies to promote the import of capital goods implemented by the development-minded authorities.

Modern equipment was purchased, from Germany to make the candy and from Italy to wrap it, making it possible to automate processes and significantly increasing the speed of production. This new machinery placed the company at the forefront of international technological development, increasing its efficiency and competitiveness, which translated into a significant increase in the scale of production. At the beginning of the 60s 60,000 kg of candy were being manufactured every day, 12 times more than the initial volume of 5,000 kg.

Imports of machinery and equipment continued to be carried out throughout the sixties. The introduction of the latest technology was one of the basic principles of the firm's policy, with the aim of lowering costs and competing in price. The increase in productivity in the sixties compared to the fifties can be measured indirectly by that fact that between 1951 and 1960 production grew at a rate similar to that of labor, while between 1961 and 1970 the workforce went up 2.5 times and sales (in dollars) increased 3.3 times.

Thanks to the increases in production and productivity, in the sixties ARCOR achieved an outstanding position among Argentine candy manufacturers, with a share of 50% of the domestic market in 1963, although its radius of action continued to be mainly confined to the interior of the country.

Some competitors began to fall behind, while others such as Stani matched the company for growth. According to Fulvio Salvador Pagani “most of the one hundred companies that existed at that time —many of which, located in the north of the country, were customers of the cardboard company we had purchased in Tucumán— had to close down as they were unable to compete”.

As from the mid-sixties the company began to diversify, adding other forms of confectionery to the manufacture of candy, such as *alfajores* and jams. The decision to widen the range of products had as its purpose the need to achieve economies in distribution, as the introduction in 1967 of a system of official distributors required the offer of a wider mix of items. In any event, the scope for diversification at this stage was limited, with a significant change only taking place in the following decade.

There was however diversification into non-industrial activities, fundamentally the purchase and exploitation of land for farming, whether or not related to the core business. The most important activity was a complete cycle of breeding, fattening-up and sale of livestock.

### *Integration of Production*

Integration of production was another of the keys to the competitiveness of ARCOR since its beginnings, based on the need to reduce costs and increase the internal value in the chain of production. This policy made it possible to cut the cost of raw materials, input and machinery, which were a source of problems caused by price fluctuations, inadequate production levels, monopoly positions and in the case of machinery, lack of local supply and the high price of imported equipment.

Vertical integration has traditionally been a strategy adopted by growing companies in all types of economies, and one of its purposes is to reduce what theory has defined as transaction costs, that is to say the frictions faced by companies when they perform transactions in the market. Through integration such transactions are replaced by operations between different plants of the same company or between different companies in the same group, with the aim of reducing the cost of raw materials and input, guaranteeing an adequate flow and improving the efficiency of the exchanges.

In Argentina transaction costs were traditionally very high, and vertical integration was a strategy common to most major companies during the import substitution period. Difficulties in obtaining supplies of raw materials and input worsened when supply was limited, when companies that supplied them were in a monopoly position or when it was necessary to import such products and they were subject to international market prices, fluctuating exchange rates and tariff policies.

In the case of ARCOR the integration of production was one of its principal strengths, enabling it to reduce production costs, offer competitive prices and diversify risks. In the confectionery manufacturers and food products (derived from bakery) sectors, most large companies were only partly integrated, as was the case of Canale, Terrabusi, Noel and Águila. Stani diversified and became automated but did not integrate. ARCOR not only integrated its activities, it began to become transformed into an industrial complex, a path that none of its competitors followed.

Integration, in so far as it implied diversifying the activity of the company into new branches, required a learning process that was not exempt from cost. Fulvio Salvador Pagani, referring to the manufacture of machinery, has said that “our closed economy, enabled our company, which did not specialize in the sector, to enter the market and compete... because we were provided with a margin within which we could make mistakes”.

### *Integration in the Production of Raw Materials and Input*

The purpose of achieving self-sufficiency in these items was explained by Fulvio Salvador Pagani as follows: “once a certain volume of candy production had been reached on the basis of very effective competition, profit margins were 5 or 10%. We realized that if we produced some of the raw materials we needed ourselves we could achieve margins of 30% or 40%. As a result, we decided that instead of increasing the production of candy, we would aim for the production certain raw materials”.

### **Glucose**

In 1956 ARCOR began to manufacture glucose, entering into the chemical process industry. Glucose is one of the basic inputs for confectionery manufacture. It is obtained from corn and other grain such as sorghum. Glucose is also used to produce fructose syrups used as sweeteners for beverages and jams.

At that time there was just one company that held a monopoly on production, a situation that resulted in insufficient supply and high prices. ARCOR therefore decided to install a glucose production plant at Arroyito, alongside its candy plant. Because of existing restrictions on the import of equipment, it was built with second-hand equipment and very basic technology, a situation characteristic of Argentine industry in the fifties. An old plant in Río Segundo (Córdoba) that was not in operation was purchased in order to make use of the equipment, and machinery was also acquired from a sugar mill being dismantled in Jujuy. The vacuum pump was manufactured in the company's

own workshops. In his words of F.S. Pagani, “we began to produce glucose in a very precarious manner”.

Until 1965 glucose was made on the basis of sorghum (grown in the region of Arroyito and much cheaper than corn) and improvements were made to machinery and processes. That year the company hired a chemical engineer for the first time, with the aim of modernizing and expanding the plant. Imported machinery was installed, and corn began to be used as raw material, improving the quality of the product. This plant continued in operation, with partial improvements, until 1980, the year in which it was replaced by an entirely new high-technology plant.

### Packaging Material: Corrugated Cardboard, Cartons and Paper

Corrugated cardboard cartons were another basic input for the company, but in the early fifties supply was insufficient and prices were very high. As from 1954 ARCOR began to manufacture its own corrugated cardboard boxes, as it was more profitable to produce the input and sell it as part of the product than to sell the end product on its own.

In the case of carton packaging, ARCOR had an advantage in that its owners had prior experience in the product from their involvement with SIDE. In fact they had begun to manufacture packaging before they owned their own candy factory, operating plants in Córdoba and in Tucumán. Their output, however, was insufficient to supply ARCOR's needs.

The corrugated paper plant was set up next to the candy plant at Arroyito. Its machinery was built in the company's workshops, and a paper-making technician was hired who had already built a corrugating machine for another company. As from 1958 ARCOR began printing its own packaging material at Arroyito, with the purchase of a flexographic printer.

During the first few years the corrugated cardboard plant was supplied with paper from the market, but in 1959 it began its own manufacturing, with a small plant that was also set up in Arroyito. As F.S. Pagani was to say later, “we encouraged the same mechanic who built the corrugated paper machine to build a paper plant. On the basis of trips to Europe and having read magazines and catalogs, he built us a paper manufacturing facility that continues to operate at our Arroyito plant”. Nevertheless, the new plant served to supply only a part of the paper requirements of the company, the rest being met by purchases from third parties.

The paper plant began by using rag as its raw material. In the sixties it began to make use of wood to produce a small proportion of cellulose. Wood



supplies came in part from ARCOR's own forests in areas close to Arroyito. By 1990 Arroyito's paper was 85% recycled and 15% made from pulp derived from its own eucalyptus plantations.

During the sixties integration in the packaging and printing sector continued. In 1960 ARCOR set up a new company, —IDEAL (Industria del Envase Argentina Ltda.)— to print flexible materials for packaging. This company was the first in Argentina to use rotogravure, a technique that was more modern than flexography. It was developed in Italy in the fifties and required metal printing cylinders instead of rubber plates.

Through this process of integration the company was, in the 1950s, becoming transformed into an industrial group. Several of its production plants were selling their surplus output on the market, complementing sales of the principal line of business. Both the glucose plant and the corrugated paper factory manufactured not only for ARCOR but also for third parties. Surplus production from the glucose plant was sold to other firms producing drinks and jams, and in the sixties some sub-products began to be exported. Corrugated paper was sold to local companies, and gradually, as ARCOR began to increase the number of its plants and its production volumes, paper and cardboard began to assume a significant role in group total sales. As from the seventies the scale required by the input plants far exceeded the needs of the company, so that in some cases sales outside the group exceeded intra-firm transactions.

### *Manufacture of Machinery*

Since its founding ARCOR had been manufacturing machinery in its own workshops, which continued in operation until the end of the 1980s. As F.S. Pagani said in 1987: "we have continued to build between 70 and 80% of our machines; the rest we import and try to copy. The machines we built are on a par with the most modern in the world".

Until the end of the fifties the main problem for the purchase of imported machinery was the restriction on imports, which was resolved by in-house manufacture, the reconditioning of old equipment or manufacture to order at workshops in Santa Fe and Córdoba. Local production of machinery and equipment was insufficient, technologically backward and made to low quality standards. These problems affected industry in general, not just ARCOR alone, and began to be resolved following the opening up of the market to imports during the government of Frondizi. Until then it was frequent for companies to manufacture their own machinery and spares.



As from 1958 ARCOR began to import, but in-company manufacturing continued, with the aim of lowering costs and holding down foreign currency borrowing. The price of imported machinery was very high, as there were few manufacturers, and sales conditions were monopolistic. Until the end of the eighties the strategy of the company consisted in combining imports and its own production. Key machinery was purchased (such as cookers and wrappers) and the rest was made in the company's own workshops or under contract, by means of copying foreign models. As a result, machinery was obtained at below market prices.

Even in cases where equipment was imported, production lines were manufactured and assembled. Workshops were also used to adapt and improve imported machines, steadily introducing innovations to equipment and processes.

One of the advantages on which ARCOR could count in the manufacture of its own equipment was the presence of Mario Seveso among the founding partners. Seveso had left primary school after fourth grade, but had an innate technological ability and great mechanical ingenuity. He began working for a forestry company, and then joined Boero y Sebaste as a mechanic, where he learnt about confectionery manufacturing machinery. He served his apprenticeship with the head technician of the firm, who was German, and replaced him following his retirement. From Boero y Sebaste he moved to SASORT, and from there to ARCOR, where he was the partner responsible for the technical area until his death in 1965, at which time he was a vice-president of the company.

On their first trip to Buenos Aires, when it was decided to set up the company, the founding partners purchased the basic equipment they needed: a lathe, a filing machine and a welder, as well as four candy-making units and their moulds. They stored all of this in a shed in Las Varillas and Seveso took charge of building the machinery for the confectionery plant. He assembled the first facilities recycling machines from the thirties and ordering machines from third parties' workshops in the provinces of Córdoba and Santa Fe.

At first second-hand machinery and obsolete technology had to be used, but when Fulvio Salvador Pagani began to travel to Europe with his colleagues they were able to copy foreign machines. In visits to international fairs and confectionery factories they studied the machinery and gathered brochures, which were used to build machines, as they were too expensive to buy. On his first trip to the Milan Fair together with Pagani, Seveso sketched a kneading machine, and on the basis of his sketches and brochures he was able to con-

struct a similar machine in the workshop in Arroyito, incorporating certain improvements of his own.

In 1953 ARCOR inaugurated its corrugated paper plant. It was designed, manufactured and assembled at Arroyito under the direction of a technician hired for the purpose with the help of local labor, and in 1959 the first paper-making machine was built.

Initially the machinery workshop was a very modest affair: in 1953 it used a single lathe, and operators took turns using it. At the end of the fifties, when the paper plant was built, it was expanded and equipped with used machinery from a machining business in Santa Fe, which was upgraded by the technical personnel at ARCOR.

In the 1950s the company had a design office and a couple of draftsmen, but as from the sixties a work team was formed, staffed by mechanical designers, engineers, draftsmen and architects. Since then it has carried out various jobs such as building the glucose plant, IDEAL, the Kraft paper machine and several industrial complexes in Argentina and abroad. On the basis of this team an Industrial Infrastructure Department was created in 1978, with its headquarters in Córdoba. And, in 1991, following the restructuring, a General Engineering Coordination Department was set up.

In addition to the Arroyito workshop, during the sixties ARCOR invested in other companies for the manufacture of machinery that were set up in the city of Córdoba: Fripack —packers and similar equipment— and Industrias Mark —automated packing machines and ice-cream making and pasteurizing equipment.

### *Agricultural Activities: Diversification and Integration*

Since the beginning of the fifties ARCOR had been investing in land, and in 1957 it set up an Agricultural Division. This began to gain in importance as from 1960, headed at first by Pablo Maranzana and then by Tito Maranzana, two of the founding partners.

This division, which accounted for an important proportion of investment until the end of the sixties, fulfilled two functions. It was above all the product of a diversification strategy with the aim of taking advantage of business opportunities, reducing risks, improving financial availability and facilitating access to credit. Owning land provided a form of insurance, as its sale could help resolve liquidity problems, and in addition, in the words of one of the founders “owning land and livestock helped in obtaining bank credit”. Furthermore, Arroyito was located in a rural area, where most immigrants tended to buy or farm land.

At the same time, although to a lesser extent, the exploitation of farm land was part of the process of integration, as the company's land was used to produce certain raw materials such as sorghum and corn for the manufacture of glucose, quince for jams and wood for paper pulp.

The annual reports and balance sheets of the sixties clearly show the importance of land purchases and agricultural activities to the profitability of the company, particularly in the case of the sale of livestock. In the following decades, as industrial production and the company's assets grew, agricultural activities began to decline in relative importance.

The company's decision to include agricultural activities within the company's lines of business was explained by Fulvio Salvador Pagani: "Each time I traveled to Europe I could see that industries ceased to be competitive when they were overcome by other companies that were more advanced either in terms of technology or for other reasons (...). This never happened in the case of farm production. This led me to consider the comparative advantages of Argentina in the agricultural sector, and we began to purchase land, first one hundred hectares, then another thousand, and so we began to grow in the agricultural sector also. Most of the land we bought had been unproductive, and we gradually transformed it. It is true that we must be competitive in world terms, but I think we should seek to become so in areas where we have competitive advantages, which in my mind is especially the case in the farming sector".

In 1953 they purchased a plot of 111 hectares to begin planting quince and fattening-up pigs. By 1988 the company owned 180,000 hectares in various provinces of the interior —Córdoba, Salta, Santiago del Estero—, with a highly technical, capital-intensive operation. Livestock raising had become the principal activity, covering the complete cycle from breeding to sale. Other activities included the planting and exploitation of trees for paper manufacture and, since 1985, dairy farming.

### *Electricity Generation*

Integration of production at ARCOR was completed by the generation of electricity. One of the problems with Arroyito when ARCOR set up there was the shortage of electricity supplies, as power was available only until midnight. This was a fairly widespread problem in Argentina in the early fifties.

The company acquired a generator, which was gradually upgraded over the years. In 1955, at the instigation of Fulvio Salvador Pagani, the *Cooperativa Eléctrica de Arroyito* was set up, based on a 750hp power plant. Later still, ARCOR installed its own turbine generator, which together with the power plant supplied power to neighboring towns.

## Sales: Building of a Distribution Network

A strategy based on a constant increase in the scale of production required an appropriate sales system to meet the demands of a growing market share. At the same time the building of an efficient distribution system became one of ARCOR's strategic advantages, because of its market reach and its contribution to price competitiveness through reduction in selling costs.

Over its first twenty years ARCOR assembled a distribution system that offered capillarity and covered the whole country, progressing from its own regional market to a nationwide market; with a strategy for keeping the markets of the city of Buenos Aires and the Greater Buenos Aires in reserve.

The company always aimed at large-scale production for the mass market, standing out from other major candy manufacturers which preferred to manufacture for segments with a higher purchasing power and focused on the main urban centers. At an early stage it competed mainly with small and medium-sized companies in the interior, with increasing advantages thanks to the scale of its production and distribution system. Since the seventies, however, ARCOR began to make inroads into markets dominated by the so-called *major players*.

Whereas most of the firms in the interior sold directly to retailers, ARCOR opted from early on to sell to wholesalers, with consequent advantages in terms of the cost of transport and shipping. In the sixties two new sales channels were added. One was cigarette distributors, who sold to kiosks. The other, used since 1967, was a system for sales through official distributors, which was better adapted to the company's scale of production. One of its main advantages was that it enabled economies through diversification in sales, as the official distribution network could be used for the sale of a growing range of products. These channels were used in parallel, with some brands being sold through wholesalers and others through official distributors.

In the seventies sales offices were set up at various points around the country, and as from the eighties a strong push has been given to sales through supermarkets.

### *Sales in the Early Days*

The company began operating in provinces in the interior of the country through wholesaler traveling salesmen. The first of these were three founding partners: Renzo Pagani (who covered the area from the north of Córdoba up to Santiago del Estero) and Tito Maranzana and Enrique Brizio (who were responsible for the region from the east of Córdoba to Entre Ríos). All of them had worked as salesmen for SASORT, providing ARCOR with the advantage

of being able to make use of their experience and knowledge of the regional market and their contacts with retailers.

Since the early years the sales system was supported by competitive prices and the preference for sales to wholesalers on very favorable terms, with the offer of credit and significant discounts.

During this first stage decisions began to be taken according to “news from the street”, and salesmen were in constant contact with the shipping department. In the sixties the company purchased an aircraft, which helped increase the radius of action and the speed of transactions. Several provinces could be covered in one day, and the sales staff closed deals at airports, in fields or on roads, wherever they were able to land.

Direct sales to wholesalers formed part of a strategy that differentiated ARCOR from most of the competition in the interior, which sold directly to retailers in small volumes with high transport costs. The customer base was purged, with minimum orders being required from smaller customers, to ensure better use of transport and efficiency in the loading and unloading of goods.

The system of official distributors was established in 1967. Previously the company had dealers that sold to wholesalers in certain cities (Mendoza, Jujuy, Goya), and as from the early 1960s sales had begun to be made through cigarette distributors that had added confectionery to their lists. Sales through official distributors, selected by company wholesaler traveling salesmen required an expansion of the supply of products and faster deliveries.

In the fifties and sixties the company's output was sold almost entirely on the domestic market, in particular in the interior of the country. It began in the regional market —Córdoba, Santa Fe, Entre Ríos and Tucumán— expanding from there into other provinces. Although sales began to be made in Buenos Aires in 1953, large-scale expansion into the Federal Capital only took place as from the 1970s.

In this first stage advertisement spending was limited and use was made of very basic resources. The ARCOR brand was less well known than its products; official distributors often did not have good sales personnel and competition was hard, particularly in the soft candy segment. Until the mid-sixties, as the company only manufactured one type of low-cost, high volume product, it did not justify a significant marketing investment.

Nevertheless, since the end of the fifties nationwide campaigns began to be carried out using radio, cinema and television. The first was for Bocaditos Holanda, in 1958, which included the organizing of a competition on one of the most popular radio programs. It was supported by radio ads and a small

amount of cinema advertising. In the mid-sixties ARCOR acquired the license to manufacture a brand of U.S. candy —Charms— seeking growth in the fruit-flavored acid drop segment, and commercials were made for cinema and radio, with considerable use of both media. The campaign was based on soccer, to ensure it reached a mass audience.

## STAGE TWO: THE 70s

### Macroeconomic Context

*In the seventies the Argentine economy grew at a slower rate than in the sixties, at an annual rate of 4%, although with strong fluctuations over the decade and very high levels of inflation, well above those of any previous period. Politically it was a very unstable period, which saw a second era of military governments under the presidents Levingston (June 1970-March 1971) and Lanusse (March 1971-May 1973), a Peronist government from May 73 to March 76, with four presidents (Cámpora, Lastiri, Juan D. Perón and Isabel Perón), followed by the Videla dictatorship after the military coup in March 1976 which saw the start of the so-called “Process of National Reorganization”. It was also a period marked by violence and union conflicts. The economy was severely affected by political conditions. During the presidencies of Levingston and Lanusse the economic situation deteriorated as the public sector deficit and inflation rose threefold. The early years of the Peronist government were relatively stable, with economic growth that benefited from a boom in exports in 1973 and price and wage controls agreed under a Social Compact reached that year. The situation began to deteriorate in 1974 because of rising inflation and a worsening of external accounts, accompanied by growing political destabilization worsened by the death of Perón in July. In the twenty months of Isabel Perón’s government the country had six ministers of economy, in a context of internal struggles and worsening economic and social problems. As from 1975 the situation began to slide out of control. Economic activity levels dropped, the situation of the balance of payments became desperate, the fiscal deficit reached unheard-of levels and inflation ran out of control, reaching a rate of increase in March 1976 that qualified as hyperinflationary. The consumer price index rose by 182% in 1975 and 444% in 1976. During the time Martínez de Hoz headed the Ministry of Economy (March 1976-March 1981) a series of profound changes took place in the rules of the game that had served as a framework for economic activity during the whole import substitution phase. Economic policy, which since the end of 1978 had been based on a monetary balance of payments focus, became centered on market liberalization, opening up of the economy and the elimination of subsidies and state regulations. The Martínez de Hoz administration was unable to stabilize the economy, except for a few partial gains, and ended in a recession that had a severe impact on all productive sectors. Inflation fell compared to the peaks during the government of Isabel Perón,*

*but between 1976 and 1981 it was never lower than 100% per year. At the same time, the financial reform of 1977, which implied the freeing of interest rates and the de-nationalizing of bank deposits, lead to soaring rates and a grave crisis in the system in 1980. The opening up of the economy provoked a flood of imports as a result of a combination of lower duties and exchange rate lag, and since 1980 the trade balance, which had been positive between 1976 and 1979, turned negative. The sector most affected by the new economic policy was manufacturing industry. With the opening up of the economy the protectionist system that had been built up since the thirties began to be dismantled, and following the financial reform real interest rates, which had historically been negative because of the effect of inflation, became positive. The appreciation of the peso and the lowering of duties encouraged the massive import of industrial goods, severely harming local manufacturers. The opening up to imports, the rise in interest rates, high levels of borrowing, an overvalued peso and the lack of incentives for productive investment, added to a shrinking of markets, had by the end of the seventies generated an unprecedented crisis in the industrial sector. Between 1975 and 1982 industrial output dropped by over 20%, and the share of industry in GDP fell from 28% to 22%. The most affected sectors were those most exposed to international competition, particularly textiles, footwear, wood products, metal products, electrical machinery and transport material. The area less affected was that of basic industry, which benefited from industrial promotion regimes before and after 1976. The food industry maintained its levels of activity, and in the face of declines in other areas, increased its relative share of manufacturing output.*



## Introduction

Whereas in the fifties and sixties ARCOR's expansion had been based on increased scale of production, a process of integration and development of distribution in the interior of the country, in the following decade company growth was centered on the development of new product markets and the search for new geographical markets within and outside Argentina. The company diversified and decentralized its production, at the same time as expanding the radius of its distribution towards the area of the Federal Capital and the Greater Buenos Aires area. At the same time it carried out a process of internationalization through exports and direct investment abroad.

Although confectionery continued to be the core business of the company, it was gradually becoming a manufacturer of food products in general. In addition to confectionery and jams it began making chocolate, cookies and crackers, marmalades and corn derivatives. There was also increased diversification within the confectionery category, with the starting of chewing-gum lines and other products.

At the same time the process of integration continued to be developed, with the addition of new input production facilities such as the start of enzyme manufacturing and the making of flexible packaging and cans.

Increases in and diversification of production were carried out by means of the purchase or setting up of new companies located in various provinces in Argentina (Tucumán, Mendoza, Buenos Aires, Santiago del Estero) as well as in other regions of the province of Córdoba (Villa del Totoral). Whereas in the 60s increases in the scale of production of candy and the manufacture of new items were achieved mainly through the addition of plants and lines at the Arroyito complex, as from the seventies onward the physical expansion of the company was accompanied by geographical decentralization and participation in a growing number of related companies.

Although ARCOR had already begun to invest in related companies in the previous decade (for example, in firms making machinery in the city of Córdoba), the number of related companies increased substantially in the seventies, with the addition of companies manufacturing candy and input and the first direct investments abroad. During this decade the company began to develop from a single entity into an economic group, with ARCOR S.A. becoming the head of a series of legally independent firms in which it held all the capital or a controlling interest.

The setting up of new subsidiaries began in 1970 with the creation of Misky, a company manufacturing chocolates and confectionery in the province of Tucumán, and continued with the formation of Pancrek —a biscuit manufac-

turer—in 1976, Milar—an enzyme plant—in 1979, and Vitopel—transparent film and flexible packaging—in the same year. Also during the seventies, ARCOR began to purchase assets of existing companies, such as Guillermo Padilla Ltda., which served as a basis for the starting up of the San Pedro plant for the production of alcohols and corn derivatives. At the same time new manufacturing establishments were set up at other locations, such as ARCOR San Rafael in the province of Mendoza, for the making of fruit pulp, which began operating in 1972.

A new approach adopted in the seventies was the entry into associations with other companies, such as those done with a US firm at Milar and with a company from Córdoba at Pancrek.

The main investments took place at the beginning and end of the decade, falling significantly in the period from 1973 to 1978 because of the unstable macroeconomic context and the intensity of political and social conflicts. A major portion of such investment was financed through loans from the Banco Nacional de Desarrollo, and the company benefited from provincial industrial promotion regimes that offered tax exemptions and deductions.

Growth in output was underpinned by steady improvement to distribution systems and participation in new markets, both in Argentina and abroad. On the domestic market, inroads were made into the markets in the metropolitan area, where ARCOR's presence had been very limited.

As regards foreign markets, exports, which had begun at the end of the sixties, increased their share of total sales reaching a maximum of 10% in 1978. Although they contributed to a certain extent to support increased scales of production and temper fluctuations on the domestic market, their effect was more important on the qualitative level, because they helped to improve logistics and controls on the quality of products.

During the second half of the decade the process of internationalization of production began with investment in a company in Paraguay (ARCORPAR, 1976) and the approval for investment projects in Uruguay and Brazil.

During the seventies the company made efforts to improve its cost competitiveness through increases in productivity by means of investment in machinery and equipment as well as through improvements in the organization of production, with changes to layouts, quality controls and the creation of a department of industrial safety.

At the same time the company implemented changes to the organization in order to make management more efficient and improve the response of operating and administrative controls, which culminated in the adoption of a multi-departmental structure. As from 1977 steps were taken to improve

and update the organization, including introduction of a dynamic organization chart for all executive levels and increasing investment in computer systems, leading to the setting up of the company's own data processing center in 1978 for ARCOR and its related companies.

ARCOR's growth and its leading position among companies in the interior of the country was reflected in the leading role played by Fulvio Salvador Pagani in the creation in 1977 of the *Fundación Mediterránea*, an institution founded by a group of companies in Córdoba to promote research into the Argentine economic reality and the drafting of proposals for action.

### **Economic Performance During the 70s**

Over the decade as a whole the economic performance of the company was strongly conditioned by a context marked by instability, growing inflation and the profound changes that took place in economic policy as from 1976. ARCOR was not very much affected by the opening up of markets in 1977, but was impacted by the financial reforms, which led to a very sharp increase in borrowing costs.

In the seventies the firm grew at a much lower rate than in the sixties, and performance fluctuated. The years 1970 to 1974 saw growth, but in 1975 there was a sharp decline. A recovery took place in 1976, although it was conditioned by inflation, which continued at a high rate in spite of the stabilization policies implemented, as well as by high interest rates, which, as a result of the financial reforms in 1977, became positive in real terms.

The financial statements for the period reveal both the lower rate of growth and the fluctuations that existed. Taking averages for the first and last three years of the decade, in constant terms total assets and net worth fell by 1% and investments were down 19%. In spite of fluctuations, sales remained at a level of around \$ 60 million. The number of workers grew by an annual average of 3% and increases in fixed assets doubled.

This performance is largely explained by the events that took place during 1975, a year in which sales fell by 50% and assets were down 30%, reflecting the effects of a highly unfavorable context (this was the year of the so-called "rodrigazo") with high rates of inflation, shrinking demand, labor conflicts and political instability. Investment grew in 1972 and 1973, but fell sharply in 1975 and continued to fall until 1979, as from when it began to pick up again.

Over and above the economic context at the time, the behavior of variables such as employment and the increase in fixed assets reflected relative stability in the company's long-term growth strategy, as not only did they not decline

compared to previous values, they grew. Even in the most critical years the firm continued to invest in equipment.

Profitability trends were not as clear during this stage as they were previously. Both the return on assets and that of own resources fell until 1974, when they reached their lowest rate (9%), then rising until the end of the decade, reaching levels higher than those at the beginning of the decade. On average, profitability during the seventies was higher than in the sixties—except for the return on company capital—but fluctuations were much higher. Returns on sales ranged between a minimum of 4% in 1974 and a maximum of 24% in 1978, while in the sixties it had ranged between 9 and 16%. Profitability on company capital fell significantly, the annual average falling from 35% to 26%. The explanation for this lies on the one hand in the increase in Shareholders' Equity financing assets, and on the other in the rise in the cost of liabilities attributable to the economic policy adopted as from 1976.

The largest falls in return on sales were seen in 1973/74, as a result of the maximum price policy introduced by the Peronist government. This fall was however moderated by the company's own production of basic input that made it possible to reduce manufacturing costs.

In the last years of the decade borrowing costs increased significantly as result of the switch from negative to positive interest rates. In 1977 the company sold part of its livestock herd to reduce its liabilities, and the following year it began to convert its bank debt into dollars, to reduce the cost of financing. Control of the cost of borrowing was a recurring theme in annual reports from 1977 onward, becoming a critical problem at the beginning of the eighties.

**Table No. 2-2.** Evolution of principal accounting and profitability aggregates (monetary values stated in millions of constant 1995 pesos).

Year	Total Assets	Sales	Workers	Return on sales	Return on Assets
1971	37187	51979	1033	13%	21%
1972	54576	51601	1100	15%	16%
1973	56935	59771	1217	8%	11%
1974	51938	57423	1177	4%	9%
1975	36636	28110	1236	23%	22%
1976	45848	32721	1177	22%	24%
1977	42634	41795	1058	11%	21%
1978	41875	49977	1618	24%	33%
1979	54685	68715	1641	16%	32%

Source: Prepared on the basis of information from the company's financial statements. Information is stated in thousands of constant 1995 pesos.

## Technology and Production Aspects

### *Diversification and Decentralization: from Confectionery to Foods*

#### Confectionery and Chocolates: Misky

In the confectionery segment, production was increased as a result of the re-equipping and reorganization of the Arroyito plant and the building of a factory in Tucumán.

At the beginning of the decade new machinery and equipment was installed at the Arroyito candy plant—with heavy investment between 1971 and 1973—and changes were made in the organization of production through alterations to plant layout. Installations were redistributed, with a more rational layout intended to increase productivity and ensure a more fluid manufacturing process.

However, the most important change was the installation of a chocolate and confectionery factory in the province of Tucumán, in the district of La Reducción, which was given the name of Misky. Through Misky the company began its installation of plants in provinces in the interior where it could benefit from industrial promotion schemes, a policy which it continued to follow throughout the seventies and which it expanded during the eighties. The new firm functioned as a subsidiary until 1986, when it was absorbed via merger.

Investment was financed by loans from Banco Nacional de Desarrollo in very favorable terms in the context of a policy for the promotion of diversification in production in the province that was instituted at the end of the sixties (Operativo Tucumán), and thanks to which various industrial concerns (including Scania, BGH and Alpargatas) were set up.

The setting up of Misky was also a decisive step towards the forming of a group made up of legally autonomous companies, as, until then, the growth of ARCOR had been based on continuous expansion of the Arroyito complex, through the addition of new lines and new production plants. Previously, in the sixties, three subsidiaries had been set up in the city of Córdoba for the manufacture of input and machinery (Ideal, Mark and Fripack), but most production took place at Arroyito.

The Misky plant in Tucumán gradually integrated and diversified production, following a path similar to that of Arroyito: in 1970 the confectionery plant began its operations and in 1975 a glucose, starch and derivatives plant was inaugurated. In 1973 this plant began to manufacture chocolates and chewing-gum, categories in which ARCOR had not been previously involved,—a very significant step in the process of diversification within the principal activity of the company.

### Cookies and Crackers: Pancrek

The second key event in the diversification that took place in the seventies was the start of cookies and crackers manufacturing. In 1975 Pancrek S.A. was set up in association with LIA S.A., a firm from Córdoba that was established in the early seventies. At the end of the decade ARCOR acquired part of the capital stock of LIA, and in 1997 it purchased the remainder of the company.

This new company was located in Villa del Totoral in the province of Córdoba, also in the context of an industrial promotion scheme. It began to operate in 1978, three years after its creation, with production lines for sweet and semi-sweet cookies and crackers.

### Alcohol and corn derivatives: the San Pedro Plant

In February 1979 ARCOR acquired the fixed assets of Guillermo Padilla Ltda. SAIC, a company that owned an alcohol plant located at San Pedro in the province of Buenos Aires. According to the Annual Report for that year, the intention was to “put the facility into competitive operating condition and complement it with other industrial activities appropriate to the commercial structure”.

ARCOR was already processing corn at its glucose factories in Arroyito and Tucumán. The purchase of Padilla was a diversification within this sector, as it implied incorporating the manufacture of new derivatives. The alcohol distillery came into operation in 1980, producing various types of grain alcohol for sale on the market to be used as input by various different branches of industry.

The main product was 96° ethyl alcohol used as a raw material in the chemical industry and in the manufacture of liquors, perfumes and disinfectants. Liquid sub-products (alcohols for the chemical industry) solids (animal feed from the by-product of sorghum distillation) and gases (carbon dioxide for soft drinks) were also manufactured.

During the eighties the San Pedro plant was diversified and integrated. Diversification consisted of the adding of new plants for the manufacture of other corn derivatives: in 1982 a mill was installed for the manufacture of corn-flour and corn meal (dry milling) and in 1986 corn oil began to be manufactured, refined from germ derived from wet milling in Arroyito, Tucumán and the San Pedro mill.

Backward integration by the plant included the manufacture of its own plastic containers for oil and other products, with sales of surplus production to third parties.

### Jams, Fruit Pulp and Canned Products

The other sector into which ARCOR diversified in the seventies was that of jams and prepared fruit, following a common development pattern among

candy and biscuit manufacturers. The company had already been making jams at one of its plants in Arroyito, which was expanded in 1970.

In 1972 the company opened a plant for the preparation of fruit pulp for use in jams and marmalades in San Rafael, Mendoza. During the same year the company began producing peaches and tomatoes for canning at installations belonging to third parties.

### *Integration of Production*

#### Packaging: Vitopel SA

During the 70s new items began to be manufactured in the packaging category: transparent film and flexible packaging. The prices of cellophane on the local market were very high, 40% above international prices. The manufacture of PVC film as a substitute helped lower costs and promoted the modernizing of company packaging.

In 1978 the Vitopel SA subsidiary was set up with a plant at Villa del Totoral, alongside Pancrek, in an industrial promotion area. In 1980 this company began to manufacture and print PVC film, and since 1988 it has been doing the same with biaxially-oriented polypropylene (BOPP). The company, which manufactured both for ARCOR and the market in general, was equipped with state-of-the-art technology from Italy and Germany and inks and printing cylinders manufactured by Ideal, another of the firms in the group, created in 1960.

By the end of the eighties the plant at Villa del Totoral, as well as manufacturing PVC and BOPP, was also making stretch films and self-adhesive film for fruit, vegetable and meat packing and satin film (for heat-formed trays and blister packs).

In addition to the production of flexible packaging, during the seventies ARCOR began to manufacture cans at a line set up at Arroyito.

#### Manufacture of Enzymes: Milar SA

One significant innovation in the seventies as regards the production of input was the setting up of Milar SA in 1979, a firm that manufactured enzymes. Participation in Milar meant not only the ability to develop in the field of biotechnology but also the entry into the company's first strategic alliance with a foreign firm that was a leader in research and development.

In the mid-seventies ARCOR had already begun to invest in biotechnology research with the founding, together with the *Universidad Nacional de Córdoba*, of the CABI (*Industrial Biological Catalysis*) working group—the purpose of which was to study and promote the use of enzymes and cells in industrial processes.



In order to set up Milar the company formed an association with Miles Laboratories from the USA, contributing 50% of the capital. Miles—which in the eighties was to be acquired by Bayer—was one of the top three producers of enzymes in the world. At the time it was created, Milar was the only industrial scale enzyme producer in South America. In the nineties it was to form an association with leading Belgian chemical firm Solvay, also active in biotechnology research and development.

The company began to manufacture enzymes with a range of industrial applications, and at the end of the eighties it also produced IGI (immobilized glucose isomerase), a multi-purpose sweetener for the food and beverage industry.

## **Sales and Marketing: Advancing Towards New Markets**

### *From the Interior to Buenos Aires*

Whereas in its first twenty years of existence ARCOR had been growing strong in the market in the interior of the country, as from the early seventies it gradually increased its presence in the Federal Capital and Greater Buenos Aires region. In 1966 the company purchased land for a warehouse in the Federal Capital and opened its branch there in 1969. The following year Hugo D'Alessandro, one of Fulvio Salvador Pagani's main collaborators, took up residence in Buenos Aires. He was later to become vice-president of ARCOR between 1981 and 1990 and its president in 1991 and 1992.

The metropolitan area was the most difficult and competitive market, making greater demands in terms of marketing and packaging, and the leading confectionery producers in the country were all active in this region (Águila, Nestlé, Noel, Stani, Suchard and Warner Lambert). Sales were made through candy wholesalers, complemented as from the eighties by direct sales to supermarkets.

At the same time, beginning in the early seventies the distribution system began to be upgraded and investments were made to improve logistics.

At the end of the decade increasing use of television advertising campaigns designed by agencies, began to be made such as that carried out for Bang Bang chewing-gum manufactured by ARCOR in association with General de Confitería—a Spanish firm—, which contributed its experience in marketing and advertising.

### *From the Domestic Market to Export Markets*

#### **The First Exports**

Since the sixties Fulvio Salvador Pagani had been emphasizing the importance of gaining foreign markets, underlining the need to seek out opportuni-



ties in the rest of the world. The first foreign sales were made in 1964, to just a few markets and in limited quantities, and the company also took part in international trade fairs.

Early exports consisted of the sale of glucose sub-products to European countries in 1964 and confectionery to the USA in 1968. The experience of the first export of confectionery was an indication of the difficulties that existed in expanding to new markets when the company was unfamiliar with basic details such as how to prepare products for export. Two containers of soft milk candy were shipped in the ordinary hold of a vessel. The goods melted when crossing the equator, arriving in the USA in a solid block.

In spite of the cost to the company Fulvio Salvador Pagani made good the importers' losses, thus gaining credibility and ensuring that a few months later he would receive visits at Arroyito from those same importers. It seemed audacious to select the USA as the company's first export market. According to one of his aides, Pagani chose the most competitive market in the world because of the high demands it made in terms of quality and delivery dates, in order to improve the logistics and quality of products and ensuring company personnel became equipped to handle such requirements.

In the mid-sixties ARCOR also began to participate at international fairs. Initially it did not even have a stand of its own, so suitcases full of samples were carried and sales deals were closed in hotels. By 1970, when the first international confectionery fair (ISM) was held in Cologne, Germany, ARCOR had its own stand and it is currently the only Argentine company with an uninterrupted presence at the ISM up to the present.

### The Seventies

As from the seventies the company adopted a strategy aimed at increasing exports, which Fulvio Salvador Pagani explained in the 1977 Annual Report as follows: "We are driven by a desire to build an efficient domestic industrial complex to compete in the local market, but equally, or even more importantly, we aim to conquer markets abroad".

The penetration of new markets served various purposes. On the one hand, as already mentioned, it provided a quality benchmark. On the other, it helped to maintain a steady rate of growth in production, smoothing out the fluctuations in domestic demand, especially as from 1975, when the macroeconomic context became increasingly complex.

Export sales only began to reach significant volumes as from the mid-seventies. Exports of confectionery rose from US\$ 1 million in 1974—equal to 0.6% of sales—to over \$ 6 million in 1979, 8% of total sales. In 1978 they

**Exports (in thousands of dollars)**

Year	Value of exports
1974	1,238
1975	510
1976	2,125
1977	4,422
1978	4,164
1979	6,279
1980	7,067

Source: ARCOR, Annual Reports and balance sheets for years in question

were lower in value (\$4.1million) but higher as a percentage of sales (10%).

Exports were encouraged by official promotion and subsidy policies that had been implemented by governments since the end of the sixties. The main obstacles noted in the company's annual reports in those years were the changes in domestic prices, the fluctuations in the exchange rate, and the ab-

sence of any official measures to help compensate for the consequences.

**The Beginnings of International Manufacture**

Exports were the first step in the firm's process of international expansion, which continued with the setting up of manufacturing plants in neighboring countries in the mid-seventies through investment in companies making confectionery in Paraguay (ARCORPAR) and in Uruguay (Van Dam). In 1976 a distributor was opened in Chile for the sale of biscuits, but it was closed down four years later.

The process of opening up sales and manufacturing facilities abroad continued throughout the eighties and accelerated in the nineties, transforming ARCOR into a multinational corporation.

Foreign direct investment by Argentine companies in general increased at the end of the seventies, encouraged by an over valued peso, more open markets—helping to increase business contacts abroad and evaluate the possibilities of doing business—and by the lack of incentives for domestic investment in production. The food industry was well positioned for this process, and the confectionery sector was one of its most dynamic components, as could be seen by the opening of manufacturing subsidiaries by ARCOR, and sales branches by Stani in Brazil and Felfort in Paraguay.

In the case of ARCOR, initial foreign investments were in neighboring countries, either through association with local companies (in Paraguay and Uruguay) or through the acquisition of businesses (Brazil).

**Paraguay: ARCORPAR**

The decision to invest in Paraguay was mainly a defensive strategy. The Paraguayan market, unusual in that it did not have a confectionery industry of its own, had traditionally been supplied from Argentina, largely by ARCOR. Since the middle of the decade policies resulting in overvaluation of the peso

adversely affected exports from Argentina- to the benefit of goods from Brazil, which were backed by competitive prices and an aggressive market penetration policy. The setting up of ARCORPAR sought to halt the advance by Brazilian companies into the Paraguayan market (aggravated by a project for a plant backed by Brazilian capital) and at the same time use Paraguay as a launch pad for moves into other countries—including Brazil—in the context of LAIA (Latin American Integration Association) agreements that eliminated tariffs on regional exports to assist those countries that were relatively less developed.

ARCORPAR was set up in 1976 and began to manufacture in 1978 at a plant located in Puerto Villeta, 30 km from Asunción. ARCOR made an initial investment of US\$ 300,000 to establish, build and equip the company. The plant was exported on a turn-key basis, with Argentine-made machinery and equipment, much of which had been manufactured in the company's own workshops. The company specialized in the manufacture of hard candy, a line in which Brazilian competition was strongest. ARCOR continued to export soft candy from Argentina and supplied the new factory with input. In 1987 ARCORPAR was the only candy manufacturer in Paraguay, fully supplying domestic demand, with a daily output of 8 tons, employing 54 workers.

### *Uruguay: Van Dam*

In Uruguay ARCOR formed an association with Industrias Van Dam, a local manufacturer of confectionery and chewing-gum which was seeking a partner to provide financial assistance for its development. The project was approved in 1979 and began to become a reality in the following year. Van Dam sold 50% of its capital stock to ARCOR, which made an investment of US\$600,000 for the share purchase and provided a further US\$200,000 in working capital and the purchase of machinery. Management remained in the hands of the previous owners.

This company was well positioned on the Uruguayan market through its products and a sound distribution network, as well as being an importer of ARCOR products. The decision to participate in Van Dam was taken, at a time when the flow of exports to Uruguay had increased considerably, with the aim of achieving a larger share of the market.

The decision was also based on the prospects provided for trade liberalization and intra-regional integration and bilateral trade in particular, as well as the possibility of lowering the threat from the setting up in Uruguay of companies from other countries (Europe, the United States or Brazil).

In 1987 it had an installed capacity of 250 tons per month at its candy and chewing-gum plant in Montevideo. The company also distributed Rowntree McIntosh products (Smarties and After Eight).

## STAGE THREE: THE 80S

### Macroeconomic Context

*The 80s were a highly critical decade for the Argentine economy, with negative GDP growth that averaged an annual decline of 1.52%. The 1981-83 three year-period, which coincided with the final stages of military rule, were extremely unstable both politically and economically. Since the fall of Videla in March 1981, three presidents (Viola, Galtieri and Bignone) and four economy ministers (Sigaut, Alemann, Dagnino Pastore and Wehbe) followed in quick succession. The heirs to Martínez de Hoz had to take charge of an economy showing signs of strong imbalances, including an exchange rate lag, a balance of payments deficit, high foreign debt levels and a recession, all of which were aggravated by political instability and the Malvinas War (April-June 1982). During the Sigaut administration (1981) most of the main measures adopted by Martínez de Hoz were abandoned, leading to a period of devaluation, increased import tariffs and interest rate control. Since 1981 the most pressing problem was the external debt, worsened by the rise in international interest rates that affected not only Argentina but all countries in Latin America. The debt crisis blew up in 1982, following the threat of a moratorium by Mexico that shut off all possibility of taking new loans abroad. Both the public and private sectors had borrowed more than they could repay, placing the economy as a whole at risk. Corporate debt to local and foreign creditors affected both the productive and financial sectors, and successive governments between 1981 and 1983 took various measures whereby the State gradually assumed responsibility for private sector debt. Under Sigaut, exchange rate insurance was provided to Argentine private sector debt, and in 1982, during the administration of the economy by Dagnino Pastore (at a time when D.Cavallo was President of the Central Bank) debt was refinanced at a regulated interest rate, well below the expected rate of inflation. From then on, public sector debt, which had risen as a result of these measures, generated growing imbalances in fiscal accounts, accentuated by the difficulty the State experienced in obtaining resources. In 1983 democracy was restored with the election victory of the Unión Cívica Radical, and in December Raúl Alfonsín assumed the presidency. The democratic government inherited a stagnant economy with a US\$45 billion foreign debt, a growing public sector deficit —aggravated by commitments abroad— and a rate of inflation of 343% for 1983. The debt crisis reversed the net flow of resources transferred from abroad because of the interruption of capi-*

*tal flows and the increase in international interest rates. After an initial stage in which expansive policies were applied, the government introduced a stabilization program —the Plan Austral— which for several months was successful in containing inflation and reactivating the economy, but in the middle of 1986 there was a surge in inflation and as from the end of that year the public sector deficit began to be financed through monetary printing. The situation grew worse in following years in spite of new stabilization efforts, with a combination of growing inflation, an external crisis and a fiscal crisis leading to hyperinflation in 1989. The economic balance sheet for the 80s was strongly negative. Industrial GDP fell by more than 10%, consumption fell 15.8%, investment was 70.1% lower and per capita income fell by 25%. Real wages also shrank (by 24% in the manufacturing sector) and unemployment rose from 2.3% in 1980 to 7.4% in 1990 (Kosacoff, 1993). Following the changes in the local environment and regulatory framework, as well as the new international economic conditions and the different strategies adopted by companies, a new pattern of industrial development arose that replaced the import substitution model that had been in force since the thirties. The macroeconomic conditions led to a general stagnation in manufacturing activity, which recorded a decline in its share of GDP. However, at the same time industry underwent profound structural reforms with widely differing behavior both at sector level and by individual companies. On a sectoral basis there were some areas that increased output and relative share (intermediate input, especially basic metals and chemicals), others that while not growing increased their share (food and beverages) and those that recorded significant falls in their level of activity and in their share (principally machinery and equipment, as well as industries linked to consumption and construction: textiles, wood, non-ferrous minerals). In general capital or natural resource-intensive activities grew, compared to a relative loss by metalworking industries and labor-intensive goods-producing industries. At company level, small and medium-sized businesses were more severely affected than large companies, but once again, behavior was not uniform. The most notable change was the rise or consolidation of economic groups of predominantly local capital that evolved into conglomerates. Company performance varied according to the ability to diversify activities, but also according to skill in coping with a context of high inflation and considerable uncertainty, developing appropriate financial policies or taking advantage of industrial promotion systems and credit lines for equipment purchases.*

## Introduction

In the eighties ARCOR gained in strength as one of the country's leading economic groups, with a rate of growth considerably higher than that of previous decades, so that the transformation in its size was significant, measured in terms of both assets and sales, which in 1990 passed the \$200 million mark, without taking into account sales by related companies. One feature that set it apart from other domestic conglomerates was its heavily industrial profile, with no diversification into areas unrelated to its manufacturing output.

Growth was backed by decentralization —plants were opened in various provinces—and an international presence, with the start of operations in Brazil and Chile. At the same time ARCOR increased its diversification within the food sector.

Local investment benefited from the industrial promotion regimes that existed in various regions in the interior of the country. By the end of the 80s the firm operated 23 plants located in eight provinces. At the same time it continued to expand internationally, increasing its exports and making direct investments in Brazil —acquiring a confectionery plant— and in Chile, with the acquisition of a food distributor.

Whereas in previous decades the company's management had assigned priority to investment in production and distribution, in the eighties it significantly increased its investments in other areas, particularly marketing and finance. It also carried out a far-reaching restructuring that was completed in 1990 with the adoption of a multidivisional structure organized into business units, better suited to the size and complexity that the group had acquired.

At the same time it looked for ways to lower costs and increase efficiency and productivity, with constant improvements in organization, production and distribution, and a steady flow of investment in state-of-the art machinery and equipment. It continued to manufacture the bulk of the machinery required in its own workshops.

The performance of the firm was severely affected by the conditions prevailing on the domestic market, particularly the episodes of inflation and hyperinflation and the high cost of money. During this stage, because of the increase in investment, the level of indebtedness increased, with very high borrowing costs and a decline in profitability.

Nevertheless, throughout the decade there was a steady rise in both the company's assets and its sales, and ARCOR significantly improved its position within the segment of large domestic companies in general and among those in the food sector in particular. On the ranking of the country's largest firms based on sales published by *Mercado* magazine, the company rose from

70th place in 1980 to 44th in 1989, the year in which it occupied 6th place among food companies, with higher sales than all other producers of confectionery and cookies and crackers. By the mid-70s ARCOR was supplying 70% of the domestic confectionery market.

Although the excessive size of its assets had a negative impact in the last part of the 80s, it positioned the company favorably for the opening up of the market in the nineties, when it was found to be a modern company with available capacity.

The death of Fulvio Salvador Pagani in an accident in December 1990 was without doubt a traumatic moment in the company's history, as he had been mainly responsible for the strategy followed by ARCOR since its foundation. The restructuring already carried out that year served to lessen the impact and eased the transition to a period of professional management.

### **Economic Performance in the Eighties**

This decade was marked by a clearly-defined change in the dimension of the company, as it grew at a faster rate than in the sixties and at a far higher rate than in the seventies. Total assets, sales and net worth all increased almost fourfold. Whereas in 1979 total assets amounted to around \$55 million, in 1980 they had almost doubled to \$96 million, and by 1990 their value had risen to \$243 million. Net worth had also recorded a significant increase, rising from almost \$30 million in 1979 to \$48 million in 1980 and ending the decade at \$178 million. The average annual growth rates for the period were 10% for assets and net worth, 6% for sales and 14% for investments, reversing the trend of the previous decade, which was noted for negative growth rates.

The increase in assets, net worth and investment reflects the policy for strong growth adopted by the firm at the end of the seventies, although results only began to be seen during the following decade. The result of this expansion policy was the incorporation in only a few years of a large number of investors companies and a change in its nature, acquiring the features of an economic group with an increasing geographical decentralization.

Almost all the companies created in the 80s were established under the umbrella of industrial promotion regimes that granted tax benefits to businesses located in certain specific areas of the country. The use of these regimes accentuated ARCOR's geographical expansion, so that by the end of the eighties it operated manufacturing plants in eight provinces. The addition of new companies was reflected in the notable increase in investments, which rose from \$17 million to \$113 million in 1990, recording an average annual increase of 14%.



Sales grew at a lower rate than other indicators (6%) but sales per worker almost doubled compared to the average for the 70s, reaching \$76 thousand.

Although end to end the number of workers rose from 1828 to 3142, it should be noted that there were reductions in 1981, 1982, 1988 and 1990 in response to declines in the company's sales and profitability.

Profitability followed a contrary path. For the first time there were years of negative profitability from sales (1980 and 1989), and the profitability of the main business was positive in only four years. Simultaneously, there was a rise in the importance of income generated by other headings. The worst year in the history of the company was 1989, when the return on sales reached a negative 13% and profitability on own capital was a negative 18%. Undoubtedly hyperinflation was one of the variables of the economic context that most affected the company's performance.

The behavior of the various profitability measures wavered, fluctuating around values far lower than the averages for previous decades. Average return on sales, for example, was 15% in the seventies, 12% in the sixties and just 5% in the eighties, and the return on assets in the same periods was respectively 21%, 19% and 11%.

The most notable decline was recorded by return on shareholders' equity, which had fallen 9 points in the seventies and a further 17 points in the eighties. As in the last years of the 70s, this period was noted for high borrowing costs and debt levels, with an impact on the return on ARCOR capital. Although the company took advantage of the measures adopted by the authorities in 1981 and 1982, which provided exchange insurance for debts in dollars and regulated rates that were below inflation levels, costs of borrowing were high over the whole decade.

### **Technology and Production Aspects**

In the 80s the company continued to diversify and integrate, adding new confectionery and food products and starting to produce milk at its own dairies. At the same time it carried out a considerable expansion of its manufacturing capacity through the setting up of related companies.

The company also continued to equip existing plants, installing automatic lines for the manufacture of paper and diversifying production at the San Pedro plant, which began dry milling and oil crushing. The Milar plant was also expanded, with machinery built in the company's workshops, and silos were acquired to increase grain storage capacity.



**Table No. 2-3.** Evolution of principal accounting and profitability aggregates (monetary values stated in millions of constant 1995 pesos).

Year	Total Assets	Sales	Workers	Return on sales	Return on Assets
1980	96493	108781	1828	-2%	9%
1981	109280	132802	1754	6%	20%
1982	121743	132715	1689	16%	16%
1983	139805	140340	1998	6%	6%
1984	177753	206036	2521	9%	13%
1985	185712	218602	2543	5%	12%
1986	257449	292394	3044	12%	20%
1987	293630	325795	4083	7%	16%
1988	317817	280988	3683	4%	4%
1989	398938	241890	3865	-13%	7%
1990	242768	224272	3142	7%	0%

**Source:** Prepared on the basis of information from the company's financial statements. Information is stated in thousands of constant 1995 pesos.

### Integrated Industrial Complexes in Areas of Industrial Promotion

Between 1985 and 1988 ARCOR installed industrial complexes in San Juan, San Luis and Catamarca. Each of these complexes manufactured end products and input for local firms and for the group, becoming “decentralized production centers”. All these investments were carried out under industrial promotion programs, which during the eighties represented one of the main sources of state subsidy.

In his Annual Report for 1986 Fulvio Salvador Pagani explained to shareholders that “the policy for the creation of development centers in industrial promotion zones has encouraged the setting up of specialist businesses. These in turn are integrated within a global context leading to the harmonious development of the group”.

Frutos de Cuyo, a tomato canning plant and tin can manufacturer, was set up in San Juan.

At the Villa Mercedes industrial plant in San Luis four companies were set up that operated as independent businesses with a central administration. These companies manufactured food products for sale on the market and input for the group.

The companies set up were: Converflex, manufacturing flexible materials for food packaging (for ARCOR and the market); Dulciora, a manufacturer of jams and marmalades (using as raw materials fruit pulp from San Rafael and syrups and glucose from Arroyito and Tucumán); Productos Naturales,

manufacturing essences, and Metalbox, maker of cans and tin lids for ARCOR and third parties. Tinplate manufacture was essential if the cost of input of canned goods was to be lowered, because at the beginning of the decade locally-manufactured tinplate was both expensive and of poor quality.

At Complejo Recreo, in Catamarca, a further four companies with a joint administration were set up, following the Villa Mercedes model: Carlisa (bakery products: bread-sticks, fruit-cake, alfajores); Candy (candy made using starch and gelatin); Alica (powdered mixes); and Flexiprin (printing of flexible packaging for food products, for both ARCOR and others).

## **Integration: Production of Input and Raw Materials**

### *Corrugated Paper and Packaging*

In 1980 Cartocor was formed as a new company making corrugated cardboard and packaging, with a plant at Paraná in Entre Ríos, —a strategic location for sales of cardboard boxes across the whole country. The project for this plant began to be studied in 1976, as the Board of ARCOR foresaw a significant increase in its packaging needs and was anxious to ensure self-sufficiency. A technical analysis indicated that the recommendable module volumes would considerably exceed the company's own demand, so it was decided to embark on a larger module that would be obliged to make sales to third parties as well as to ARCOR. In this case sales outside the group were in excess of the business between members of the group.

Cartocor started manufacturing in 1981 with the production of cartons for different types of packaging and the manufacturing of boxes in various sizes for other customers. In the early nineties it covered part of the needs of the group that could not be met by the corrugated paper plant at Arroyito, also making sales to third parties and exporting to Chile and Cuba.

### *Milk*

In 1983 ARCOR began to produce milk from its dairy installed close to Arroyito. By the end of the decade it had four such establishments producing milk for use in the manufacture of milk candy.

### *Sugar*

Fluctuations in sugar prices have always had a direct impact on ARCOR's production, as it is a basic raw material for confectionery manufacture. In the 60s there were some years when the price rose very high, hindering export projects, and by the early seventies the company had managed to ensure that

the sugar mills would sell sugar at international prices when it was to be used to manufacture goods for export. Nevertheless, sugar prices were continuously being mentioned in ARCOR's Annual Reports as a problem, and not even during the open economy years from 1977 to 1981 was it possible to obtain a lifting of restrictions on imports because of the lobbying by local producers.

In 1980 the company acquired an interest in a sugar mill, but it was not until the nineties that it began to produce sugar for its own use, with the purchase of the La Providencia mill in Tucumán, which by the end of the nineties supplied almost 100% of the group's needs.

### **Diversification**

During this decade ARCOR became transformed into a mass consumption food group, as a growing number of food industry lines were added to its production. Confectionery lines were also diversified with the addition of chocolate bars, wafers, new types of chewing-gum and other products, including the Bon-o-Bon bites, which became a great success.

In the case of food manufacturing, progress in diversification took place with the setting up of decentralized centers of production in the provinces, which added new categories such as powdered food (gelatins, powders for ice-creams), bakery products (fruit-cake, bread-sticks) and tomato processing ("the red line"). New corn-based products were also introduced, including flours, corn meal and oil produced at the San Pedro plant.

### **Distribution**

During the 80s ARCOR carried out investments to speed the distribution system and made innovations to its sales system, opening distribution centers in provincial capitals (Córdoba, Santiago del Estero) and starting direct sales to supermarkets, in view of the growing importance that this channel was acquiring in the Argentine market.

In 1981 the company inaugurated its distribution center in Buenos Aires, on the Acceso Norte in General Pacheco (district of Tigre) and in 1983 a new shipping and dispatch facility was built at Arroyito.

Another distinctive feature of the decade was the increasing investment in packaging and advertising on the basis of the type of products offered by the company and the sales channels used. Supermarket sales required visual communications techniques to attract customers, with special packaging and display cases, and brands needed to be reinforced. Investments in marketing were also based on the type of market to which the products were addressed and the need to compete with other large confectionery companies.

## Internationalization: Exports and Direct Investment

### *Exports*

During the decade export sales were generally at a high level, and as from 1985 volumes rose at a faster rate than domestic sales. As in the seventies, exports served to compensate for the fluctuations in domestic demand, but were increasingly affected by instability in the exchange rate and changes in economic rules.

ARCOR's policy was based on keeping up exports even in years when they were not profitable, in order to preserve the company's position in the markets. Export sales picked up as from 1982, steadied in 1983 and 1984, rose between 1985 and 1987, grew a little in 1988 and fell in 1989.

One notable development during the eighties was the increasing diversification of the goods exported, as in addition to confectionery, input materials began to be sold, as well as machinery and equipment. Exports of input (enzymes, glucose, starch, pellets, base gum, coloring essences, flexible packaging) made it possible to take advantage of excess production capacity in the group's local plants, and were favored, as well as those of machinery, by the installation of manufacturing branches in neighboring countries, (which were equipped with machines and production lines built at the workshops at Arroyito and by other related companies).

The main destinations for exports were North America (USA and Canada), neighboring countries and other countries in Latin America. By the end of the decade sales to the Middle East and Europe were rising, although in the case of the latter they were hindered by high duties, which ranged between 38% and 50% (while Argentina's tariff rates were 20%). New markets began to open up, with exports to Japan and countries in Africa.

### *Direct Investment Abroad. Production and Distribution*

In the eighties the internationalization of production made significant progress with the purchase of 50% of Van Dam in Uruguay and the acquisition of a confectionery plant in Brazil (1980).

The growth of direct investment abroad—which had begun to take place in the seventies with ARCOPAR although it gained considerably in strength during the eighties—reflects the process of spreading of assets and the maturing of the company. At the same time it formed part of a wave of growing internationalization by Argentine manufacturing companies, backed by capabilities accumulated in production, distribution and management.

In the case of ARCOR the reasons for internationalization were several, and can be analyzed on the basis of the model designed by Dunning—the “eclec-

tic paradigm". This claims that decisions by firms to begin production internationally are based on the location advantages offered by a given country or region, making use of advantages of ownership, or rather, the company's own skills that enable it to position itself better than other investors in the receiving market.

The advantages of ownership of a firm could derive from the possession of intangible assets (patents, brands, technological and management skills) and/or benefits arising from operating in various complementary activities. Exploitation of such advantages can take place through the export of goods and services, the granting of licenses to other firms, or through the installation of the company's own plants in other markets. In general, companies follow a route that begins with exports, continues with the installation of sales branches and is completed with the setting up of manufacturing subsidiaries. There are also other possibilities, such as for example when manufacturing subsidiaries are set up that also distribute products manufactured by the parent company in its country of origin or by other subsidiaries. This was the case of ARCOR in Paraguay, Brazil and Uruguay, where there was no previous investment in distribution subsidiaries, while in Chile and other Latin American countries the classic path was followed

Advantages of locating in a receiving country justify direct investment as an alternative to exports. These include the possession of natural, human and institutional resources, as well as their cost and quality; the size and features of the market; the degree of political and economic stability; the availability and cost of infrastructure; the cost of transport; the rate of exchange and public policies.

At the time ARCOR established its branches abroad its principal ownership advantages derived from its skills in technology and production and its experience in distribution. In the area of technology, the company was capable of supporting productive developments in favorable conditions compared to local competitors, and in the commercial area, it had a long-lasting experience in exporting and a well-oiled distribution network in Argentina which served as a model for those countries towards which investment was channeled.

There were various reasons for the decision to operate plants abroad. The first of these was the saturation of the domestic market, which meant that any production growth strategy had to be based on investment in other countries. Secondly, one of the objectives of direct investment was to strengthen the exporting focus of the company, as branches combined local production with the distribution of products imported from Argentina. These products included consumer goods (confectionery, etc.), but also input manufactured by ARCOR

in Argentina and machinery, equipment and spare parts manufactured in the company's workshop. Factories in other countries not only manufactured for domestic markets but also for export. To do so, location advantages played a key role. Paraguay, for example, served as a base for sales to other countries under the terms of trade treaties such as LAFTA and LAIA.

In addition to the specific advantages offered by each of the countries in which investment was made, international expansion was part of a strategy for the consolidation of a regional market involving growing integration with neighboring countries which received institutional reinforcement through the creation of the MERCOSUR.

### *Brazil*

The establishing of the company in the Brazilian market took place through the purchase of Nechar S.A., a small confectionery manufacturer located at Rio das Pedras, in the State of Sao Paulo. ARCOR purchased the entire capital stock for US\$825,000 and invested a further US\$1 million to increase its capital and carry out re-equipping.

There were various reasons for this decision to invest in Brazil. It was a market of 120 million inhabitants —four times bigger than that of Argentina— and it had a high annual rate of growth. In addition, the company considered the investment in Brazil as part of its regional integration strategy in the context of policies to bring the two countries closer and various Latin American trade treaties.

The investment in Nechar was ARCOR's first experience in a large, competitive foreign market, very different from the markets in Paraguay and Uruguay. Commercial practices were different, there were cultural differences (starting with the language) and there were companies that were very strong in chocolate production (Nestlé, Kraft, Garoto). The most fragmented market was that of confectionery, where there was no established leader. ARCOR's position here was stronger than in the chocolates segment, and its main share was obtained in the chewing-gum segment.

Overall the experience of those early years in Brazil was not entirely satisfactory, because of the nature of the market and the initial difficulty in adaptation.

The Nechar plant was expanded and modernized using machinery and equipment designed and manufactured by ARCOR in Argentina. Between 1980 and 1987 production rose from 4 to 100 tons per day. Sales were made both on the Brazilian market —giving the company a 10% share of the market by the end of the eighties— and on export markets. Distribution in Brazil was carried out using the same system as in Argentina, with sales through whole-

salers initially and the use of official distributors at a second stage, and direct sales to supermarkets. Nechar also imported and sold products manufactured by Arcor in Argentina.

### **Birth and Development of the Economic Group.**

By the end of the 90s ARCOR had become one of the major economic groups in Argentina with diversified investments and a structure in which the parent operated as the head of a group of legally independent firms.

The creation of these related companies, independent businesses in which ARCOR held full or majority control, had begun in the sixties with the setting up of firms to manufacture input and machinery (Ideal, Fripack, Industrias Mark) and continued in the seventies with the establishing of Misky, Pancrek, Vitopel and Cartocor, the purchase of a jam factory in Santiago del Estero and participation in ARCOPAR and Van Dam abroad. Milar was also set up in the seventies (in association with a foreign company) and ARCOR acquired a cold storage plant in Córdoba (Colcar) and also set up a construction company (Constructora Mediterránea).

In the 80s the number of related companies increased with the setting up of eleven new companies in Argentina in industrial promotion regions and new branches abroad (production units in Brazil and sales units in other countries).

The basis for the establishing of the group was the strategy for integration and diversification followed by ARCOR since its birth. Although, until the end of the sixties, the firm had grown mainly by adding production plants to the Arroyito complex, in the following decades it began to take control of other companies. This process was matched by a growing geographical decentralization, so by the end of the eighties ARCOR operated in eight provinces in Argentina and had manufacturing facilities in three neighboring countries.

The setting up of independent companies was a product of the dynamics of the expansion of the company, in so far as the decentralization was a requirement of its increasing size, and can also be explained by the various ways in which such expansion was achieved. The use of promotion systems required the setting up of new companies that could claim the promotional tax exemptions. In addition, investments abroad in both manufacturing branches and distribution also required the forming of companies. Lastly, association with partners, such as the case of Milar, required establishing legally independent firms.

Graph 2-1 shows the expansion of the firm through plants and related companies within Argentina and the structure of the group at the end of the eighties.



## **Organization of Production and Management. Restructuring of the Company**

One distinctive feature of the 80s was the increased investment in management and a sustained policy for cost reduction through improvements to the organization of production and the company's information and communications systems.

ARCOR developed a proactive strategy in this area with the aim of increasing competitiveness within an environment with shrinking margins of state protection for the manufacturing sector and a rise in interest rates that encouraged the search for greater levels of efficiency.

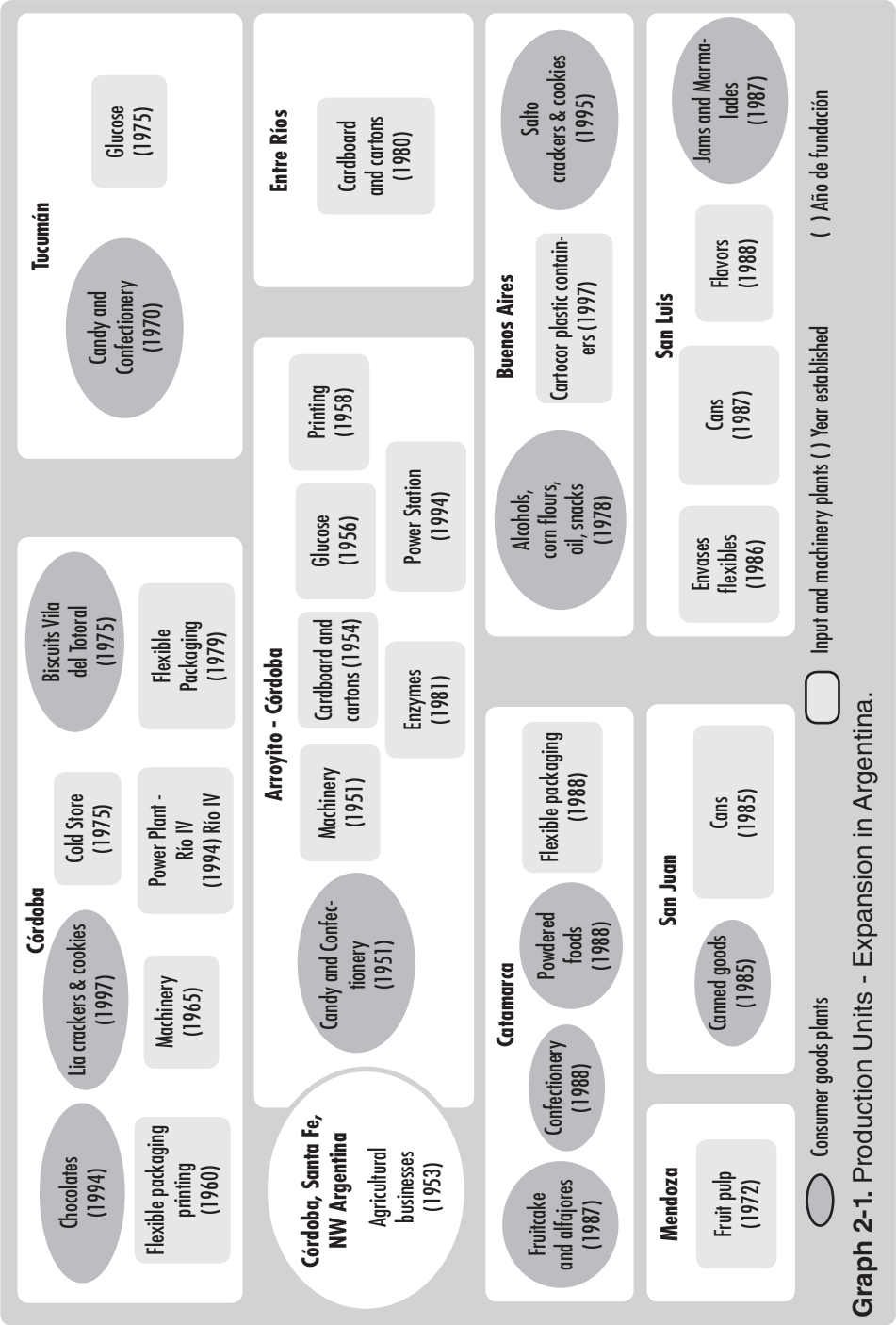
Since the end of the seventies measures had been taken to improve and update the organization of the firm, obtain sound data on costs, implement quality control systems and speed communication with related companies. Two key measures were the adoption of a new organization chart (1977) and the establishing of a data processing center for use by all the companies in the group (1978).

During the eighties the preoccupation with improvements and changes to increase productivity was constant. At the beginning of the decade the manufacturing lines at Arroyito and Misky were reorganized, and costs were lowered as a result of economies of scale. Production was also restructured, with products transferred from one plant to another and manufacture of certain products being discontinued. In 1985 the sales structures for ARCOR and Misky were unified, and the following year Misky was merged into its parent company.

Other key actions included improvements to information systems and the search for fluid analysis, operating flexibility and coordination of management, with the aim of ensuring that the right decisions were being taken. Methods and procedures were constantly monitored to ensure their appropriateness, and in 1985 an executive-level working group was set up to plan information requirements for the company and its subsidiaries. Annual reports from that period constantly indicated the search for means to ensure that "the right decisions were taken at the right time" (1987) and "to adapt the structure to the new context" (1988).

During the eighties it became increasingly evident that the structure of the group was not in accordance with its size and complexity. By the end of the decade the company had 23 manufacturing plants in eight provinces and manufacturing branches in four Latin American countries, and between 1961 and 1988 assets were multiplied by thirty. This growth had not been matched by equivalent changes in structure, leading to a strong imbalance between the





**Graph 2-1. Production Units - Expansion in Argentina.**

size and decentralization of the group on the one hand and the centralized structure and very personalized management that existed on the other. The firm had evolved from its simple structure into a multi-departmental organization. But, as the 80s progressed, this structure ceased to meet the requirements imposed by the company's expansion strategy, as it had been transformed into an increasingly diversified economic group.

ARCOR remained a family-owned company, with a very personalized management centered on the person of Fulvio Pagani, who "discussed matters with every last salesman" and "came up with ideas on every topic", in the words of this collaborators at the time.

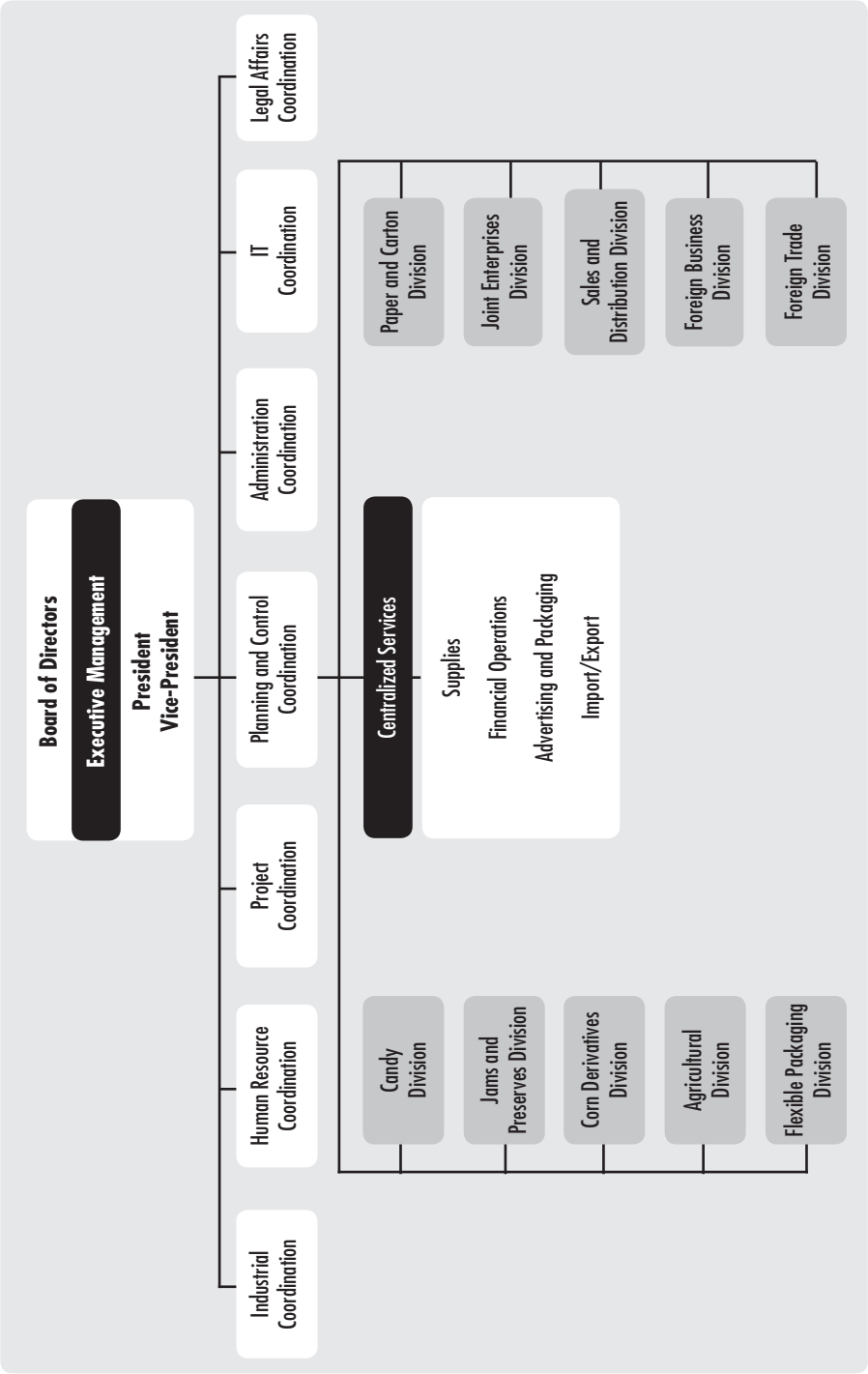
At the end of the decade a consulting firm was hired to perform a diagnosis of the situation of the company, and in 1990 a new structure was adopted more in accordance with the size and features that ARCOR had acquired (see Graph 2.2).

The new organizational structure, announced in early December of that year, was based on increased decentralization. The structure chosen was a multi-divisional holding-company format, organized on the basis of business units, geographical areas and functional units, each division headed by a general manager operating with considerable autonomy. In turn, some common functions were centralized in two sectors, Coordination and Centralized Services.

Various changes were made in management during the 80s, as in some areas there were signs of shortfalls in performance and in resources. Until that time the company had concentrated mainly on the management of production and distribution, whereas other areas —finance, human resources and marketing— were, in comparison, given less attention.

Marketing gradually adapted to the changes generated by the growth of ARCOR and the expanding of the markets in which it competed. Initially, until the mid-sixties, investments under this heading had been limited, which was justified because the company's strategy was based on production at low cost in high volumes. From the seventies onward the situation began to change as production diversified, requiring an investment in marketing more in line with the new features of its product portfolio. In the 80s the company increased its investment in this area as it grew, and such spending intensified in the 90s in a context that was more competitive than in preceding decades.

In finance the main changes were made as from 1987, in response to the difficulties posed by the macroeconomic situation and the crisis generated by over-investment in assets which led to the hiring of new management and a reorganization of the sector.



**Graph 2-2.** Structure of the Organization of ARCOR, December 1990.

On December 29, 1990 Fulvio Salvador Pagani died in an accident, just three weeks after having announced the restructuring of ARCOR. With the death of the company's president since its creation, a new stage began in the history of the company. This included the adoption of a new structure and the challenge of continuing the work begun by Fulvio Salvador Pagani. And it would have to be done in conjunction with profound changes in the economic environment, —which became noted for a process of restructuring, deregulation and opening up of markets, convertibility and progress towards regional integration in the context of economic globalization.

## **SUMMING UP FOUR DECADES**

This overview of the first forty years of the history of ARCOR takes us back to the question asked in the introduction namely, how to explain its steady growth from a small business into a multinational economic group in a complex and changing economic environment in which many of the major players of the fifties and sixties were to encounter very severe difficulties in the following decades.

The answer to this question requires identification of the particular strengths of the company and the elements of its strategy that awarded it its differentiating features.

Production on a large scale of a single product —carried out steadily over the company's first fifteen years— can be seen as an innovative strategy in the confectionery business, as was the integration of input production and the manufacture of machinery. Since the beginning the company's productivity was based on economies of scale and its own production of input and machinery, keeping down costs and prices. A second distinguishing feature was the constant improvement in technology as from the end of the fifties, through the purchase or copying of the latest developments in machinery and equipment. This not only enabled a leap to be taken in production at the beginning of the sixties, it was a strategy followed by the company across the whole period. Another notable feature of the history of ARCOR was its constant reinvestment of profits at the expense of dividend declarations, and that the investments were made in productive activities even at times when the economic context was encouraging other firms to bet on financial investments. In the second part of the eighties this over-investment in assets placed the company in a critical situation, but it was a weakness that became a strength at the beginning of the nineties, as the company found itself well prepared to compete successfully when the economy was opened up.

Integrated production was an appropriate response in the context of an Argentine economic system based on import substitution, but it was not adopted by other companies in the sector to the same extent as it was by ARCOR. It was not the only strategy to guarantee growth, and other firms were able to grow and compete by following other paths. However, ARCOR was the only confectionery company that was able to grow into a diversified economic group and one of Argentina's leading domestic capital corporations.

This combination of integration and diversification is often a feature of company growth, as the manufacture of new products is one response to market saturation. Diversification by ARCOR reflected certain features specific to the company. It was due not only to the search for new markets but also to the need to expand the range of products to develop the distribution system on the basis of economies from the offer of a wider range of items. Another notable feature was the investment made in agricultural activities, which until the early seventies were significant as a source of both risk diversification and finance.

Another strategic advantage seen since the beginning was the building up of a distribution network with a nationwide scope based on sales through wholesalers, cigarette distributors and official distributors in the early days and direct sales to supermarkets as from the 80s. Sales through wholesalers, through cigarette distributors and official distributors gave it an advantage over its first natural competitors, which were other small and medium-size companies in the interior of the country. The building of a multiple-level distribution structure in the provinces also gave it an advantage over other large players, which focused mainly on urban centers.

In the area of distribution there were three other distinguishing elements. One of these was the idea of keeping the metropolitan area in reserve, concentrating sales efforts on the market in the interior, with mass consumer products at accessible prices. The second was the strategy for evolving from unidentified products to branded goods, with a growing emphasis on packaging and advertising beginning in the seventies.

A third differentiating element was the early adoption of an export policy, targeting very competitive markets such as the U.S. as well as neighboring countries and the rest of Latin America, with the aim of obtaining quality benchmarks. By the 1970s exports were running at 10% of total sales, a proportion which was to double in the eighties. Since the seventies ARCOR has been one of a group of Argentine companies that operated manufacturing branches abroad, initiating its multinational era. ARCOR was also early in targeting the regional market that was to develop into the MERCOSUR, as the first direct investments were made in Paraguay, Uruguay and Brazil.

One significant aspect for comparative history purposes is that the company maintained a highly centralized and personalized management, based around the figure of Fulvio Salvador Pagani until his death on December 29, 1990. This remained the case even during the eighties when ARCOR's size meant it was a major Argentine corporation, with decentralized production facilities; effectively an economic corporate group made up of related companies.

The main advantages of this situation were the strategic vision provided by Fulvio Salvador Pagani and his recognized leadership skills. These were in evidence since the early days and continued to be seen over four decades, notwithstanding the complementation that existed with the range of skills contributed by the remaining partners.

Nevertheless, towards the mid-eighties there were growing signs of asymmetry between a strategy based on constant expansion and a structure that was not adapting at the same speed. This asymmetry, outlined in a consultant's report at the end of the decade, led to the restructuring that took place in 1990, on the basis of a multi-divisional structure that adapted the organization to what was already a reality: the existence of a corporate group for which ARCOR's role was to act as a holding company.

At the same time, ARCOR was placing emphasis on investment in production and distribution, while other aspects received less attention, generating an imbalance between the functional areas. Part of the success of the company in the nineties is explained by the ability shown in reversing this situation, particularly in the areas of marketing and finance, in response to internal changes, changes in context and, in the case of the finance area, to the crisis at the end of the eighties.

Two aspects of the evolution of ARCOR are particularly relevant to any comparative history. The first relates to the forms taken by large corporations in late developing societies, in which the integration of production, diversification and the forming of economic groups are a response to contexts that include a considerable degree of uncertainty, high transaction costs, lack of management resources and small markets. The ARCOR case presents some features that are typical and others that are specific to the company, such as its lack of any diversification into unproductive activities or its structure as a family business with a very centralized management until the end of the eighties. These aspects—linked to the existence of an industrialist culture and very strong personal relationships—clearly reveal the variety of strategies and organizational models on the basis of which successful companies could be built.

A second key aspect is the way in which a competitive company can be built within a context of high levels of protection and subsidized industry, such as

Argentina during the import substitution period. In the case of ARCOR, it can be seen how over a period of forty years the company grew thanks to its capacity for innovation but also thanks to the subsidies offered by the State in the form of credits, promotions, tax exemptions, rebates and other measures intended to benefit private sector companies. These two strategies protection by the State and creation of competitive capacity- in this specific case were not alternatives but complementary.

## CHAPTER 3

# Building of a Regional Company in a Context of Institutional Transformation: The Experience of The 90s

*Bernardo Kosacoff*  
*Fernando Porta*  
*E. Alejandro Stengel*

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- Performance During The 1990s
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- Incorporation and Generation of Technological Capability
- 
- Development of Marketing Capabilities and the Sales and Distribution Process
- 
- Human Resources
- 
- Financial Developments
- 
- Involvement in Foreign Markets. Exports and International Production
- 
- Action in The Community
-





## PERFORMANCE DURING THE 1990s

### Starting-point for the Corporation

The performance recorded by ARCOR during the 90s compares very favorably with any performance indicator for the Argentine economy and its industrial sector in particular. This fact is a reflection of a successful strategy and a series of correct decisions by the firm in the face of the changes that took place in the macroeconomic context and overall conditions for competition. Undoubtedly the company was quick to interpret and understand the new scenario and the challenges arising from the introduction of structural reforms and the success of the stabilization plan in 1991, partly explaining its positive development. Another major reason for its success was the knowledge and infrastructure accumulated over the company's history.

The new economy of the nineties in Argentina found ARCOR at full maturity after evolution over a period of forty years during which it had developed competitive advantages that were soundly based on strong production, sales and distribution capabilities —mainly in the interior of the country— and on the skills of its human resources in the operating of the company. It was equipped with modern, highly integrated manufacturing processes, with large-scale production and low cost, reinforced by constant incorporation of best international practices.

During the 80s in particular, it had experienced a strong process of investment and growth, diversifying in terms of production and geographical location to take advantage of regional industrial promotion programs, setting up seven new plants in the provinces of Catamarca, San Juan and San Luis. In an environment overshadowed by stagnant demand and macroeconomic disorder, the return on these investments was much lower than expected and the company found itself in a delicate financial position. However, once financial health was restored through the sale of certain assets, ARCOR was able to call on its strong, restructured and technologically up-to-date production capacity.

This infrastructure placed the firm in the best possible position when domestic consumption soared in the period immediately following the introduction of the Convertibility Plan and the sudden stabilizing of domestic prices. At this point ARCOR's relative positioning benefited from the weakness of the investment process in the previous period by its domestic competitors and limited activity in the Argentine market by the branches of major international producers. This initial advantage was maintained even after these large international competitors set up in Argentina in the middle of the decade, and

were given the time required to adapt to the peculiar characteristic of the market for this type of product. To a certain extent it could be said that in the nineties ARCOR reaped the benefits of going against the trend in the previous decade that favored assigning priority to short-term financial investments.

Its differentiating features also included a sales area with vast knowledge of the market, particularly in the interior of the country, and excellent daily operating management skills in fields from distribution to procurement. Furthermore, although it suffered from organization and management system shortfalls, in 1990 it already held a precise diagnosis of these problems and a proposal for redesign of administrative and decision-making structures. This enabled it to undertake restructuring and respond to the demands of an ever more complex organization. It raised the professional quality of leadership and management with the aim of ensuring that the levels of excellence achieved in production could be replicated in other areas of the group, through development in the field of human resources, marketing and administration.

The drive behind this decision and the will and capacity of the company to carry it through were severely challenged by the tragic disappearance, at the onset of the process, of Fulvio Salvador Pagani, who had without doubt been the person mainly responsible for the growth of ARCOR since its beginnings and had provided the impetus for the proposed reorganization. In spite of this traumatic event, and bearing witness to the cohesion of the firm's leadership, this transition was implemented successfully. At this time the figure of Luis Alejandro Pagani rose to the fore, taking over as president of the company at the age of 35 in 1993, consolidating the transformation and directing strategy and strong growth for ARCOR during the decade.

### **The New Economic and Institutional Context**

In general terms it can be considered that microeconomics, understood as the technical, productive, organizational and management practices of any company, responds to a large extent to the signals and incentives arising out of the general situation and the macroeconomic rules and regulations and actions by control authorities and the prevailing forms of competition. This context, not necessarily always perfectly understood by companies, conditions strategy before-hand and validates it afterwards. In addition, in the face of significant changes in context, a company will require learning time before adapting its strategy, altering its routines and selecting the best procedures.

In Argentina the economic rules and institutions and conditions for competition changed drastically at the start of the new decade. In evaluating the

new strategic focus adopted by ARCOR and its subsequent performance it is therefore necessary to summarize the principal macroeconomic changes that took place at the beginning of the nineties and their potential effects on microeconomic behavior in general.

From hyperinflation to price stability: i) explosion in food consumption (mainly in the rising cycle in the period 1991-94) and strong increase in demand experienced by the company; ii) reduction in transaction costs and a new look at links to the market and the level of integration of intra-firm businesses; iii) recovery of domestic and foreign credit markets and a widened range and availability of loans for large, well positioned companies; iv) disappearance of inflationary impacts on taxation and increase in the effective tax burden experienced by taxpayers.

From a relatively closed economy and protected markets to an open economy and more competitive markets: i) greater competitive pressure from imports and a reduction in the mark-up margin for firms already in the market; ii) reduction in the cost of imported capital goods, with facilities for the modernizing of machinery; iii) arrival on the scene of major international manufacturers and increased competition from product and specialty differentiation; iv) integration within the MERCOSUR common market and relative advantages for firms which could already count on a developed regional presence; v) the need for increased participation on world markets and the limited *know-how* of local firms regarding exporting and international business.

From relatively inexpensive financing to more costly credit: i) switch from negative interest rates to strongly positive rates in real terms, deepening the effects of the 1977 financial reform; ii) elimination or reduction of investment promotion regimes and greater need for self-financing for the development of new projects; iii) rigidity in the nominal rate of exchange and elimination of changes in parity as a means of diluting financial liabilities.

Briefly, it could be said that this combination of conditions meant that a company based on industrial production such as ARCOR now had to face a scenario that differed from the past because high or extraordinary profits could no longer be expected. Also, particular attention had to be paid to problems of demand and market development, with a rapid expansion of sales channels and product offer.

## Challenges and Landmarks in Development

In line with this diagnosis, ARCOR decided to consolidate its position in markets that constituted its basic strength (confectionery and canned goods

in the interior of the country) and develop other markets where its profile was low, but where steady growth could be ensured in the medium and long term (chocolates, *alfajores*, cookies and crackers, Buenos Aires and the supermarket channel).

To guarantee the viability of this strategy it was decided to progress rapidly with the introduction of a new organizational model, developing a new corporate image and improving marketing capabilities. This was to include an aggressive development of the market on the basis of emphasis on product innovation, increasing its international scope—via exports and direct investment abroad—, reducing the level of integration of its production through the outsourcing of activities and modifying its pattern of specialization, concentrating on its core business.

From the point of view of its microeconomic operations, these actions represented a three-fold change in its previous approach: i) the company moved from a predominantly family business model to one based on a professional skill-based structure, now under the leadership of Luis A. Pagani; ii) it changed its main focus from production and distribution aspects to marketing and demand-based actions; and iii) it switched from concentrating on mass products to differentiation based on quality and variety.

The strategy defined by ARCOR implied mainly paying attention to product markets where there was the greatest potential for growth and where its share was relatively weak, generating both higher volume and better prices. The prestige of its “Bon O Bon” brand (which dated back to the early eighties) and the success achieved with the launch of its Cofler brand of chocolates, as well as its penetration of the market for fine chocolate (1990) represented the first steps in this new strategy. The acquisition of Águila (1993), with its prestige brands and excellent craft skills and the development of a greenfield plant equipped with the latest international technology at Colonia Caroya (1994) were two landmarks along the path to the building of significant achievements in the chocolate, *alfajor* and fine chocolates segments.

The manufacturing of crackers and cookies was another strategic growth area. This was a market in which ARCOR held a minor share, and although it was agreed that there was potential for growth on the basis of the increasing sophistication of consumers, the market appeared to be dominated by two main leaders—domestic in origin—that controlled the strategic Buenos Aires market. However, there was initially a certain slowness to respond by both these companies, as they were in the process of negotiating their sale to two giant multinational corporations. Subsequently delays by one of the latter in adapting to the Argentine market provided an opportunity that was

well capitalized by ARCOR. It built a state-of-the-art plant at Salto (1995, Buenos Aires), took control of its associate LÍA —a medium-size company with a leading presence in the interior— and launched a significant variety of products and brands.

Through its retail point of sale distribution system, the structure and control of which was always one of ARCOR's competitive strengths in the domestic market, the firm developed and took advantage of strong economies of scope during this stage of the 90s. Its wide range within the different product categories allowed it to combine mass distribution and volume in food and biscuits with high relative margins on confectionery and chocolates. This last attribute in particular was beneficial in its negotiations with supermarkets, a sales channel which were essential for carrying out any expansion strategy.

At the same time the process of gradual occupation of various international markets, particularly in the region of the MERCOSUR and Chile, assumed a key role. A plan for integrated commercial expansion was adopted which resulted in rapid growth and diversification of exports and new markets. This process was complemented by the creation of a truly multinational Latin American company, through an aggressive strategy in Chile —with the purchase of candy company Dos en Uno in 1998, (this being a company that already had a significant presence in other Latin American countries)— and in Brazil with the development of a greenfield investment in a modern technology chocolate plant (1999).

### **ARCOR 1991-99: Development Compared to the Industrial Sector and the Economy as a Whole**

ARCOR's performance throughout the nineties in comparison to the evolution of the principal economic aggregates for Argentina, local industry and the food and beverage sector in particular has been extremely dynamic. The behavior of various representative variables is analyzed in detail below.

Measured over the whole period, ARCOR's sales rose by 296.4 %, compared to an increase of 38.6% and 23.5% in the gross value of national output and the output for the industrial sector respectively. This performance represents an average annual rate of growth of 12.8% by the firm, three times that for total national output (4.2%) and five times higher than the average annual rate of growth recorded by industry (2.7%). In the case of the confectionery aggregate, for example, growth in physical output volume recorded by ARCOR was 76.8% for the whole period, an annual rate of 7.4%. This is much higher than that estimated for the comparable variables at country

level (4.2%), in the manufacturing sector (2.7%) and in the food and beverage industry (3.8%).

The contrast in the evolution of workers employed is equally notable. Whereas over the ten years the Argentine economy was responsible for an increase in total employment of 10.1% and manufacturing industry lost 22.4% of its workforce, with the food industry in particular suffering a decline of 12.9%, employment at ARCOR went up by 85.3%, an 8% annual job creation and hiring rate.

Viewed on the basis of productivity per worker, the growth shown by ARCOR (77% end to end) also compares very favorably to that recorded at national level (25.9%) and in the industrial sector (59.2%). In addition, it should be considered that in addition to showing higher productivity, such growth took place at a time of a significant rise in the company's employment levels. This trend is in marked contrast to national aggregates, particularly in manufacturing industry, where a significant part of labor productivity is explained by net job losses.

Undoubtedly this dynamic evolution in ARCOR's productivity was related to the changes in organization and management that had been introduced, the steady modernization and improvement of productive processes, and the incorporation of new equipment and the development of state-of-the art plants. The firm's investment rose strongly in those years, with a total increase for the period of 723.1%, a rate almost eight times higher than that experienced at national level (93.1%), which was in itself generally considered promising. Peaks in investment by the company (measured in relation to sales invoicing) were recorded in 1992/93 and 1997/98. During the rest of the period the process was upheld by relatively lower flows.

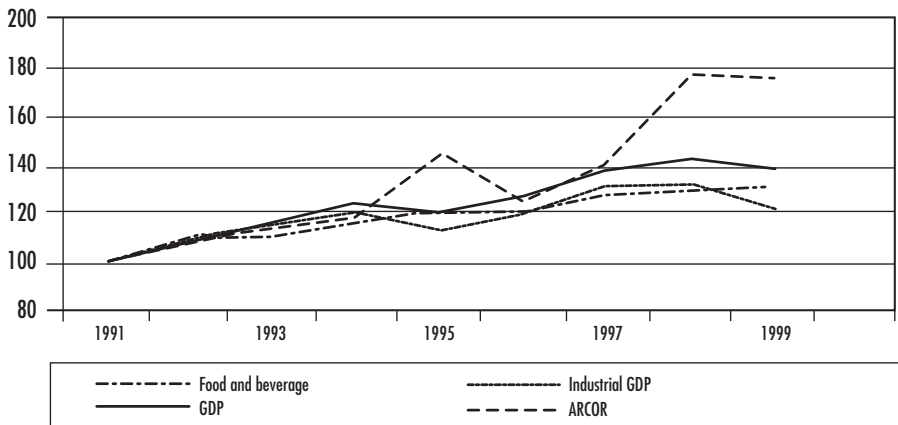
Comparison of exporting performance leads to similar results. Export sales by ARCOR increased at an annual average rate of 24%, accumulating a total variation of 454.5% between 1991 and 1999. In the same period Argentina's total exports did not even double, growing by 94.5%, and those corresponding to manufactured goods, which increased by a faster than average rate (158.5%), nevertheless recorded a rise of under half that shown by the company. This performance accentuated the already comparatively greater exporting focus of ARCOR—with an exporting ratio which rose from 9.5% in 1991 to 18.1% at the end of the decade—, levels that once again are far higher than those estimated for Argentina as a whole (3.7% in 1991 and 5.2% in 1999) or those of the industrial sector (7.9% in 1991 and 12.2% in 1999).

It should be noted that if ARCOR's performance is compared to that of a sample of large companies and conglomerates, the signs are similar to those

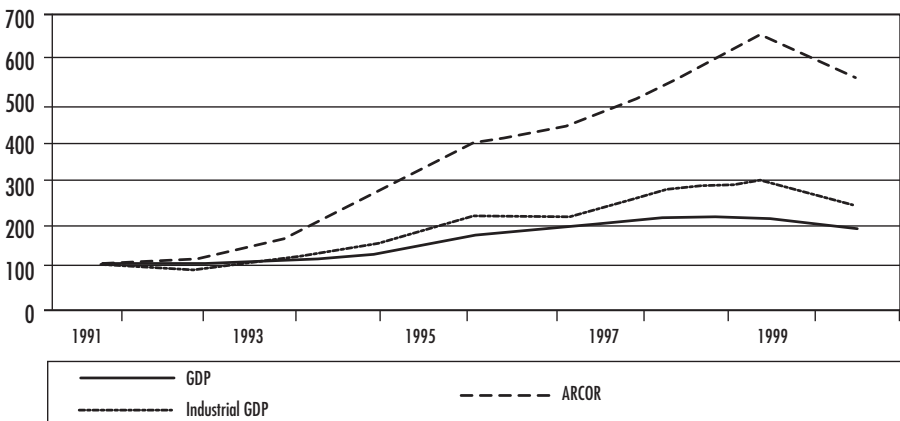
indicated in the preceding paragraphs. The company's outstanding performance is not explained by any excess representation by medium-size or small companies in total aggregates. In effect, if comparison is made only against the top-selling 500 companies in Argentina, ARCOR doubles the relative growth in value of output (total sales) of this select group. In turn, the growth of its work-force as indicated above contrasts with a 10.5% fall in employment by the group of 500 companies as a whole.

### Performance by ARCOR in the Argentine Context (1991-1999) (1991 = 100)

#### Physical volume production index

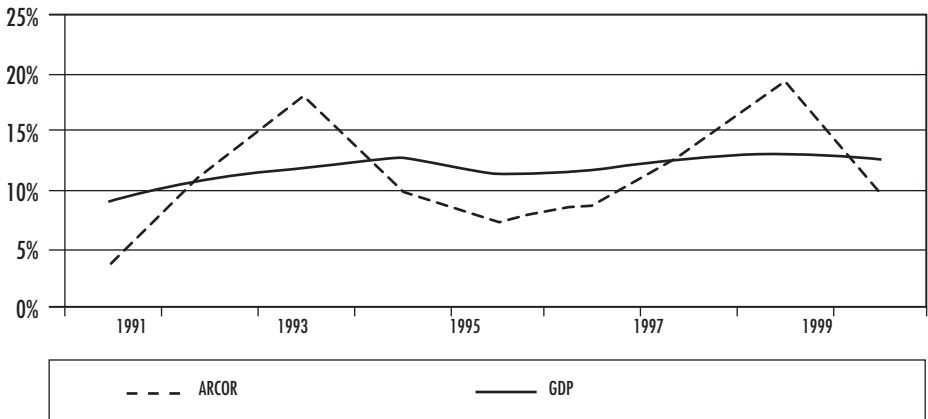


#### Export index

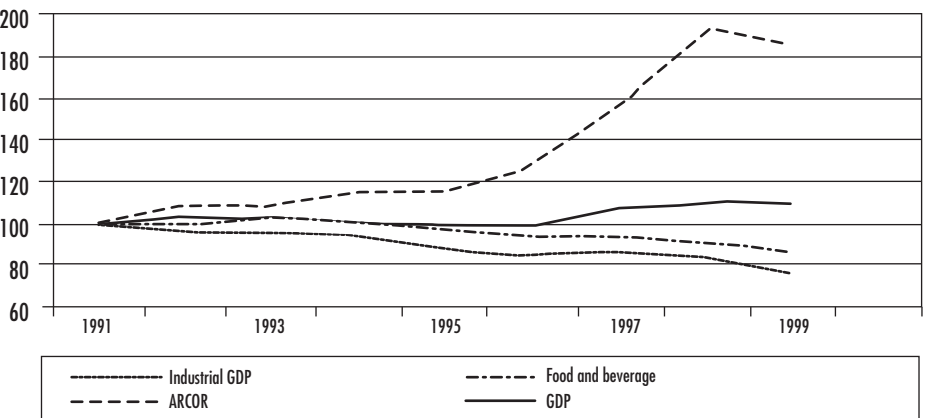




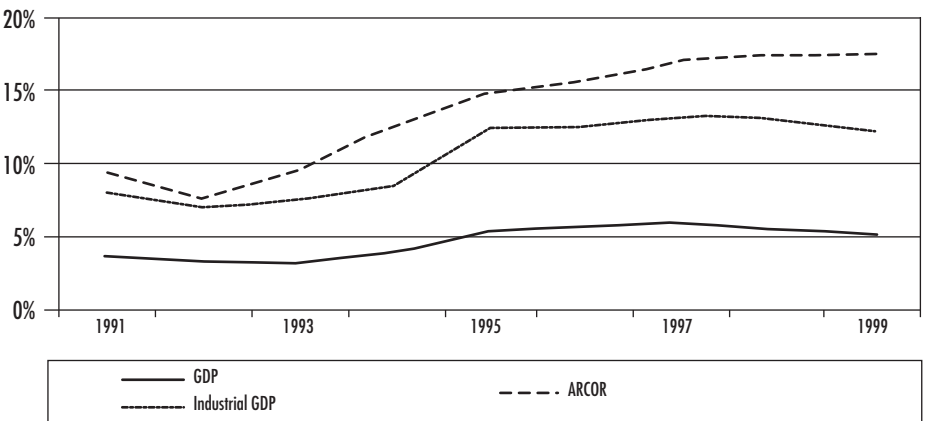
**Ratio of investment to production**



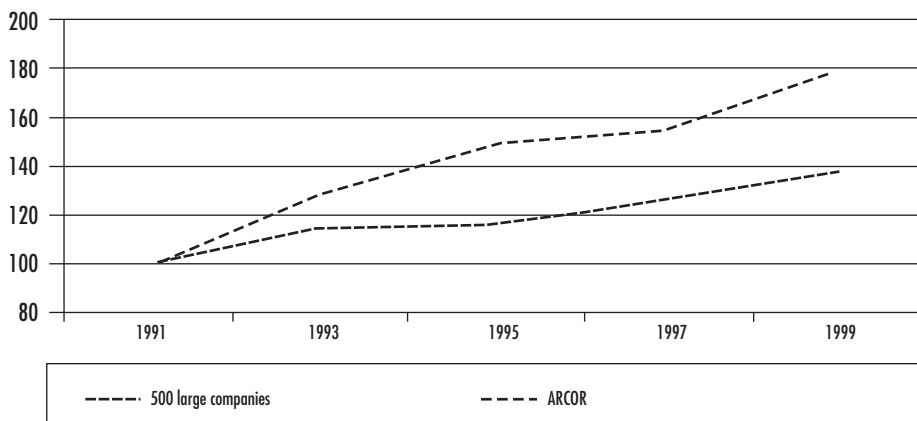
**Employment**



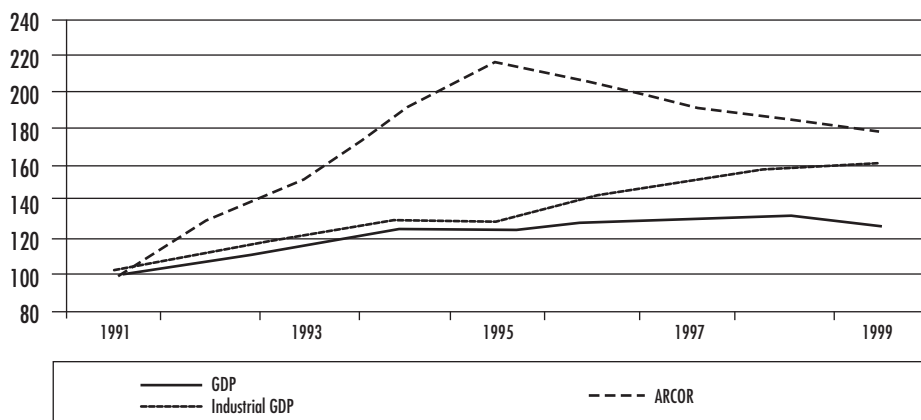
**Ratio of exports to production**



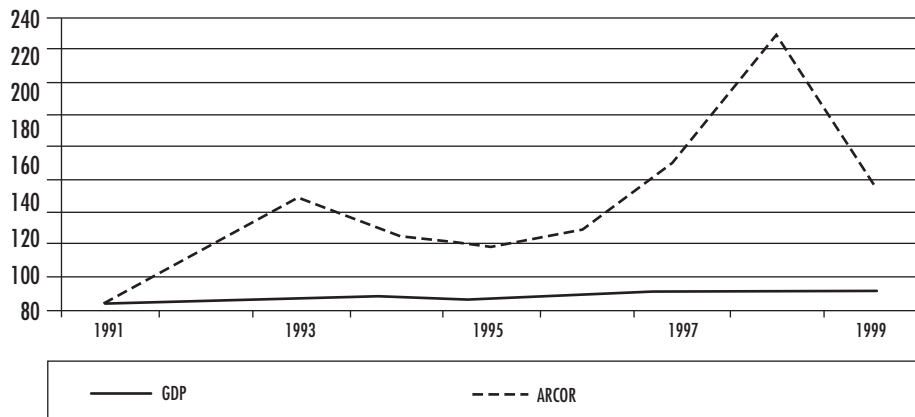
### Production value index

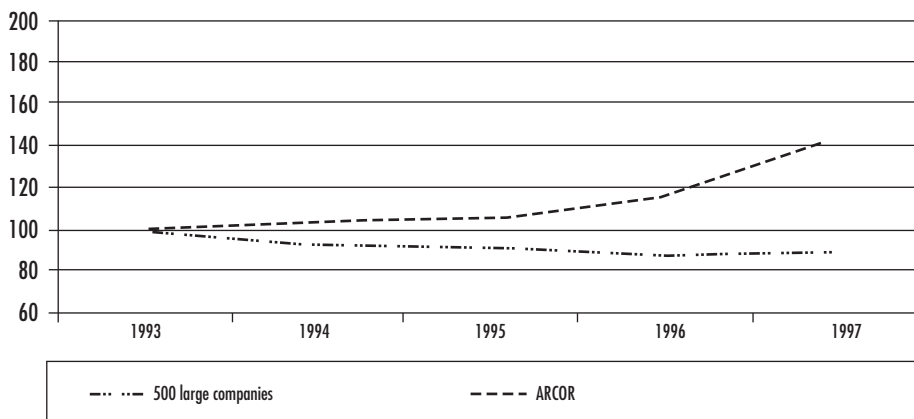


### Labor productivity index



### Investment index



**Investment index****Physical production volume index**

	Food and beverage	ARCOR	GDP	Industrial GDP
1991	100.0	100.0	100.0	100.0
1992	109.8	107.8	110.3	110.2
1993	110.0	114.3	117.2	115.8
1994	118.3	118.0	124.1	121.0
1995	120.2	143.9	120.6	112.4
1996	120.7	124.8	127.2	119.6
1997	127.2	139.7	137.5	130.6
1998	130.0	177.7	142.9	132.7
1999	131.0	176.8	138.6	123.5

**Employment index**

	Industry	Food and beverage	ARCOR	Country total
1991	100.0	100.0	100.0	100.0
1992	99.2	100.6	108.1	102.2
1993	96.2	101.8	108.8	102.7
1994	93.5	101.8	113.7	100.4
1995	87.9	96.9	115.2	98.1
1996	84.8	93.3	126.2	99.6
1997	86.0	93.3	155.3	106.5
1998	83.9	90.0	192.6	109.0
1999	77.6	87.1	185.3	110.1

## Labor productivity indicator

	Country total	Industry	ARCOR
1991	100.0	100.0	100.0
1992	108.0	111.1	130.9
1993	114.2	120.3	153.5
1994	123.6	129.5	190.1
1995	122.9	127.9	216.9
1996	127.7	141.1	206.0
1997	129.2	151.7	192.6
1998	131.1	158.1	184.4
1999	125.9	159.2	177.0

## Exports indicator

	Country total	Industrial goods	ARCOR
1991	100	100	100
1992	102.2	97.7	115.6
1993	109.3	119.5	168.8
1994	132.2	149.9	287.5
1995	175.0	217.4	393.8
1996	198.8	225.1	431.3
1997	219.0	293.5	534.4
1998	220.7	304.3	656.3
1999	194.6	258.5	554.5

## Exports at value of production indicator

	Country total	Industry	ARCOR
1991	3.7%	7.9%	9.5%
1992	3.4%	7.0%	7.7%
1993	3.4%	7.4%	9.6%
1994	3.9%	8.6%	12.6%
1995	5.4%	12.5%	14.9%
1996	5.8%	12.5%	15.7%
1997	5.9%	13.3%	16.9%
1998	5.7%	13.1%	17.5%
1999	5.2%	12.2%	17.4%

**Investment indicator**

	<b>Country total</b>	<b>ARCOR</b>
1991	100	100.0
1992	133.5	446.2
1993	154.9	776.9
1994	176.0	553.8
1995	153.0	469.2
1996	166.6	592.3
1997	196.0	1053.8
1998	209.0	1776.9
1999	193.1	823.1

**Investment at value of production indicator**

	<b>Country total</b>	<b>ARCOR</b>
1991	9.0%	3.8%
1992	10.9%	12.1%
1993	11.9%	17.9%
1994	12.7%	9.9%
1995	11.4%	7.2%
1996	11.8%	8.8%
1997	12.8%	13.6%
1998	13.1%	19.2%
1999	12.5%	9.6%

**Value of production indicator**

	<b>500 large companies</b>	<b>ARCOR</b>
1993	100.0	100.0
1994	114.4	129.5
1995	116.7	149.7
1996	125.9	155.8
1997	137.6	179.2

**Employment indicator**

	<b>500 large companies</b>	<b>ARCOR</b>
1993	100	100
1994	92.7	104.5
1995	90.3	105.9
1996	88.8	116.1
1997	89.5	142.8

## **The Convertibility Law and Macroeconomic Conditions in the Nineties**

*The monetary system established in Argentina in 1991 arose as a consequence of a long history of acute price instability and failed attempts at stabilization. The experience of the successive hyperinflationary episodes in 1989 and 1990 and the subsequent economic upheaval, which interfered with the performing of even basic daily transactions, reinforced social awareness of the high costs of inflation and made the search for long-term stability an overriding objective. The flight from domestic currency reinforced the role of the dollar as a financial asset, as the currency of reference for contracts and prices and even as a means of payment in certain transactions. This substitution of the currency also strongly eroded the capacity of the public sector to generate resources through seigniorage. In addition, confidence in the Central Bank as an efficient administrator of monetary policy was severely eroded unless it operated under heavy restrictions.*

*On a scale of alternatives ranging from rigid monetarist rules to fully flexible policies, convertibility clearly belongs among the former. The system was designed to generate simple, specific signals for both the public and private sectors on the performance of monetary policy. A structure similar to a traditional currency board was created, with a nominal anchor that validated the existence of a dollar-based economy, as well as various mechanisms to reduce the government's monetary financing. The Central Bank was obliged to sell currency at a fixed parity and to hold foreign assets for at least 80% of the monetary base (the remaining 20% could be backed by government securities in foreign currency). Severe limits were placed on the transactions that the Central Bank was allowed to perform involving government securities and the granting of rediscounts, and the Central Bank was forbidden to pay interest on bank reserve requirements. In addition, it was established that private sector contracts could not include indexation mechanisms.*

*The importance of the convertibility system as the central element in the stabilization program, designed to provoke a sudden interruption in inflationary conduct, was clear. It remained to be seen if the rigid monetary regime was to be a temporary measure or would be long-term. In any event, the necessary condition to preserve a fixed parity would be for inflation to converge on international levels. In addition, although reserve requirements added solidity to the system, there was still a risk that any*

*run on banking system deposits could lead to the need to decide whether to support convertibility in the terms established or to provide liquidity to the financial system. Within this scheme there were however still certain margins for maneuver available for monetary policy (for example, for steps of a restrictive nature, and even for expansion measures if surplus reserves were to exist).*

*The behavior of markets (and in particular the credit market) confirmed the view that instead of declining gradually the “exit costs” for the convertibility system would remain at a high level. In particular, the density (in both volume and terms) of financial contracts, most of which were denominated in dollars, increased. This implied that any eventual change in exchange policy could lead to a sudden shift in the real values of the commitments entered into between the parties, with potential effects not only on the distribution of wealth among them, but also on the predisposition of economic agents to offer and demand credit in future.*

*During the first half of the nineties the Argentine economy underwent considerable change. Especially noticeable was the sharp fall in the rate of inflation. In addition, there was a strong rise in domestic spending and the rate of production, while labor demand rose much more slowly. The increased predisposition to spend by local agents, added to a fluid availability of foreign credit, led to a sharp widening of the balance of payments current account deficit. This behavior resulted in discussions on the sustainability of the macroeconomic course during the period that were never fully settled: in the final instance it was a case of determining if the plans of the economic agents were based on expectations adapted to the true potential for future growth by the economy. In any event, shrinking availability of external financing in 1995 suddenly altered the operating conditions of the economy and highlighted the dilemmas faced by economic policy.*

*During the recovery that followed this crisis, the Central Bank made efforts to reinforce prudential regulations for the financial system, especially in relation to minimum capital requirements for banks and the holding of liquid assets (minimum reserve requirements were replaced by liquidity requirements that entities can comply with by holding various types of paper). The structure of the banking sector was modified by numerous merger and acquisition transactions, as a result of which the control of many of the leading private entities passed into the hands of foreign investors. Subsequent turmoil originating on Asian markets had a visible impact on local*

*stock markets but did not affect the rise in deposit volumes or lending by the banking sector.*

*In general terms Argentina's experience with convertibility indicates that it has become a very significant element as a point of reference for forecasts and for the system of contracts. In effect, the design of monetary and exchange institutions presents dilemmas, and in practice there does not seem to be any solution that has optimum qualities, independently of the features of the economy, its history and the disturbances to which it will presumably be exposed. However, in the specific circumstances prevailing in Argentina there is a fairly widespread consensus that the perception of macroeconomic stability is closely associated with expectations that the convertibility scheme will continue in operation.*



## The Industrial Sector in the Nineties

*Increased domestic demand for manufactured consumer goods and investment was the main driver behind the growth in output in the sector during the 90s. This trend was caused on one hand by the strong negative impact on GDP from the import substitution process and on the other by the limited contribution from export growth. Nevertheless, in the ascendant phase of the industrial cycle in 1996-98 foreign sales of manufactured goods played a slightly more important role in the growth of manufacturing output. This would appear to indicate that at last there has been some progress in increasing the competitiveness of industrial production following efforts to increase productivity and reductions to employer payroll taxes.*

*During these years there was a change in the ranking of manufacturing activities with a loss of influence by the sectors producing intermediate goods and a relative advance by manufacturers of consumer durables. Branches manufacturing consumer durables maintained their relative importance. In other words, the drop in participation in industrial GDP by tradable goods, excluding vehicles, was due mainly to the negative impact on production of increases in imports. It is therefore evident that problems of competitiveness in the segments exposed to imports meant that local industry was not able to confront the pressures of external competition. In effect, one feature of this period is the large and growing currency deficit evidenced by the industrial sector. In the context of the operating methodology imposed on the economy by currency convertibility, the presence of recurring and rising foreign deficits highlights its vulnerability in the face of fluctuations in goods and capital markets.*

*On the other hand the process of investment in industry was without doubt more intense than in the 80s, giving rise to a steady flow of imported capital goods. There are signs that most of the recent capital formation process in the manufacturing sector has been centered on the incorporation and replacement of equipment, and to a lesser extent on the installation of new production plants. At the same time, changes in the rules for the operating of the economy in response to the new competitive challenges established saw the rise of so-called "soft technologies". This trend was particularly evident in the case of most large domestic and foreign firms and among a smaller nucleus of small and medium-size businesses. Both processes tended to generate improvements in the productivity of resources applied to production and their more efficient use.*

*The actions taken by different companies revealed the existence of a variety of situations and approaches. Broadly speaking, there were two types of attitude or behavior. One more aggressive approach involved heavy investment and thorough organizational changes to productive models, achieving rises in productivity close to international levels; another was of a more defensive nature, with a lack of significant investment or the incorporation of any productive or management innovations, leading to indications that efforts were insufficient to close the productivity gap. In the latter instance in particular the shortfalls, difficulties and restrictions in performance suffered by companies facing the new environment were accentuated.*

*Even if recognizing the significance of these varying conducts, it must be said that there are new microeconomic features that became widespread. In general terms most firms adopted production methods that are relatively less labor intensive, there was a trend away from the local adaptation of technology and an abandonment of local technological efforts for the generating of new products or processes. There was a relative interruption in vertical internal production, encouraged more by a substitution of domestic added value by increased imported content than in any processes of local sub-contracting. There was also a growing complementation of local supply by a range of imported goods, and in a far less generalized manner in an industrial context, a greater participation by external markets, especially the MERCOSUR.*

*The fact that these changes have not caused any revival of the industrial sector in aggregate terms is a sign of either the still insufficient maturity of the sector or problems of adaptability and design, and leads to debate on the need to continue to wait for the potential benefits or to deepen and adapt the required transformations. When reviewing the ever decreasing relative importance of manufacturing activities in driving overall growth there are evident signs of strong dependence on external financial cycles and a changing pattern of leadership in the sector in favor of branches of MNCs and such mutations of a microeconomic nature that have taken place have not been sufficient to create a new industrialization model nor to establish the basis for a more sustainable growth over the long term.*

## **INCORPORATION AND GENERATION OF TECHNOLOGICAL CAPABILITY**

### **The Evolutionary Path in a Closed Economy**

In its early days at the beginning of the fifties ARCOR's business and main activities were essentially aimed at gaining a market that was still underdeveloped and insufficiently supplied, driving demand by means of excess product offer. Its production strategy was therefore based on large-scale production of low-cost mass consumer products. In a context of severe restrictions on the import of capital goods and relative prices that encouraged hiring, highly-labor intensive production processes were implemented.

In this context ARCOR resolved its production equipment needs through the purchase of used machinery from troubled food industry companies or companies pulling out of the market. These machines were generally based on pre-war technology and there were problems of technical compatibility and adaptation to the firm's particular production processes. To ensure the integration and the optimizing of productive capacity of these machines, which were based on a variety of technologies, a specialized work group was created within the company with the principal purpose of adapting equipment, introducing improvements by means of the copying of the designs of foreign machines and the setting up of a single production line.

It is interesting to note that the technological path followed by the company was conditioned on the one hand by the nature of its principal market —unsophisticated mass consumption— and on the other by a predominant context in which supply of capital goods was restricted, given the limitation on imports and the low level of development of local industry. For this reason ARCOR's main efforts in the field of technology during this period were concentrated on the area of processes rather than products, leading to the generation and accumulation of capabilities that were incorporated within the company for the adaptation, development and even construction of equipment.

These attributes developed into one of the company's strengths when the import of capital goods was eased as a result of the introduction of various industrial promotion measures by a development-minded government in 1958. Without interrupting its evolution, ARCOR was able to take advantage of its engineering resources to reinforce its technical and productive capacity and move towards international best practices. In this new context, building on its accumulated experience, the firm was able to simultaneously articulate steps

to: a) make selective purchases of imported machinery, b) copy and manufacture certain equipment, usually at a lower cost than imported equivalents, and c) develop innovative adaptations. As a result, the company was able to modernize its equipment and optimize the integration of productive lines with the existing plant and new additions.

It became a regular practice for the company's technical personnel to attend international machinery and technology trade fairs, enabling them to keep abreast of the latest developments and subsequently implement their own improvements—constantly upgrading their adaptation and design skills. At the same time the company confirmed its intention to adopt state-of-the-art technology without delays. Production began to be switched from batch processing to continuous production, enabling better advantage to be taken of economies of scale and therefore achieving a significant increase in the company's productivity standards. In line with this substantial change in technology, ARCOR's efforts during the 70s and 80s were aimed at increasing plant automation and lowering manual intervention in the chain of production.

ARCOR took advantage of the setting up of various promotion programs to locate industrial activities in several Argentine provinces in order to diversify geographically as well as in its production. Its first experience in this regard took place as from 1971, with the installation of a confectionery plant in Tucumán. This was a greenfield investment built by the company from scratch. Once again its own capabilities in technology—mainly the selection and development of equipment and operating improvements—enabled ARCOR to assemble its own production lines instead of opting for a turn-key solution, optimizing their performance and reaching levels higher than previously obtained in excess of manufacturers' specifications.

Taking advantage of other regional incentives and the experience acquired in Tucumán, ARCOR replicated the same financial and technological strategy on various occasions, increasing its level of vertical integration and consolidating its technical and production skills. Specific undertakings worthy of note included: i) the adoption of photogravure simultaneously with its introduction in developed countries; ii) replacement of cellophane (a product with a very high transaction cost in the Argentine market) by PVC for wrapping and work together with Italian vendors of machinery and technology for its manufacture in Argentina; iii) development of new packaging materials.

In short, the evolution of the technological capabilities of ARCOR in its first four decades of existence was strongly conditioned by the closed

economy in which it acted and by its overall business strategy—which combined concentration on relatively unsophisticated low-price products with a continuous search for lower manufacturing costs and expansion of its distribution network. In this context its main capabilities were developed in the area of processes along the entire chain of production, allowing it to reduce installation costs and increase the physical yields of the investments made.

### **Transformations in Approach to Technology in the 90s**

The abrupt change in conditions for competition in the early nineties, derived from the introduction of a program of structural reforms, forced the redefinition of ARCOR's production strategy. Specifically, the stabilization of the economy diminished the importance of transaction costs and challenged the degree of vertical integration of the company. At the same time the elimination of industrial promotion tax programs added to the cost of financing for additional investment and tended to depress profit margins. Lastly, with the opening up of the economy and the consolidation of large manufacturers and international sales chains, price competition was exacerbated at the same time as increased differentiation was required for products and brands.

This situation, which was entirely new in the history of the company, was also noted for a sharp rise in domestic consumption in the first half of the decade and implied that ARCOR had to consider outsourcing certain productive activities, further improving the efficiency of its own plants and positioning a wider and more differentiated range of products. The new microeconomic strategy of the firm and changes in the way it served its markets led ARCOR to review its traditional attitude to technology. At this point it should be mentioned that although the company's own technical personnel and the organization of its activities included ample knowledge on the subject, many of the skills and specific advantages were not the most appropriate for immediate adaptation to this transformation.

To a certain extent the technological history of ARCOR, as in the case of most other Argentine firms facing the same circumstances, appeared to be a limitation in this new context. For this reason adequate response to these novel problems required new skills and significant changes in traditional values and company culture. It became necessary for the focus of development activities to be shifted to the area of product technology. In addition, organizational improvements were rapidly introduced and increased levels of professional qualifications and intensive training efforts helped to transform management

processes in all departments. In addition, the practice of hiring external consultants to resolve specific matters instead of using the company's own internal specialists, as had been standard until then, began to be adopted.

In line with the new emphasis on the development and attention to the various individual markets in which ARCOR was active, the company adopted an organizational structure based on large divisions by generic product type or business. As a result, research and development activities tended to become decentralized, being carried out within each of these divisions. This change helped to provide greater agility in detecting needs and opportunities in the various markets, where the main form of competition is centered on the constant launch of new products.

As well as developing new products, the company made efforts to implement organizational technologies. Programs were introduced systematically at all plants for quality improvement, inventory management, reduction of idle time and minimizing of scrap. All plants also saw the incorporation of ISO 9000 standards and *Hazzard*-type systems for analysis of critical control points. The results with regard to improvements in productivity were very satisfactory, especially and more intensively in the new industrial plants (such as Colonia Caroya —province of Córdoba— and Bragança Paulista in Brazil, for example), where standards of equipment and performance were set, since the outset, on the basis of best international practices<sup>1</sup>.

In addition, several of the group's plants have already received certification under ISO 14001, while others are in the process of obtaining such certification. In the case of the Flavors Division, ARCOR was the first company of its type in the world to receive such certification. In addition, the changes made to the production process at the hard candy plant at Arroyito resulted in a 60% reduction in steam consumption and a cut of 26% in plant waste, with the generation of less waste water and a greater recovery of the remaining technical energy.

The introduction of new management criteria has been one of the most significant changes made to the organization. The Total Product Maintenance (TPM) methodology developed by the Japanese Institute for Plant Management (JIPM) was adopted to improve the performance of human resources through their own actions to achieve increases in the level of competitiveness

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<sup>1</sup> The chocolate plant at Colonia Caroya in the province of Córdoba was named food plant of the year in 1994 by specialized magazine *Food Engineering International*, the world's leading food engineering publication, published by Chilton Publications (USA).

in the framework of existing installations. TPM is described as incorporating: i) the creation of a corporate organization that maximizes productive efficiency; ii) plant management in order to ensure zero accident, defect and fault rates; iii) the involvement of all departments, including those performing development work, sales and administration; iv) the involvement of all personnel, from senior management to plant operators.

TPM required the design of a master plan for each plant and its full implementation over a period of approximately three years, with visible results in terms of reductions in costs, accidents and faults, improvements in product quality and process efficiency and greater interdepartmental cooperation.

There has also been a significant contribution in the form of new knowledge and qualified human resources incorporated during ARCOR's expansion process, through the absorption and acquisition of other companies. In addition, an important contribution was made by personnel from local firms taken over by multinationals and subsequently hired by ARCOR. In this regard, the general restructuring in the food sector came to represent a positive external influence for the company. The knowledge and skills contributed by this new personnel turned out to be a very valuable asset when it came to developing new products and varieties, as well as new businesses and capabilities. ARCOR's expansion into the chocolate business, for which, in addition to the company's own efforts, the acquisition of Águila was a decisive factor, represents one of the clearest examples of this process.

### **Some Significant Developments in Technology**

A few interesting examples of the new practices and developments by ARCOR in the 90s are provided below. These examples place in evidence both the importance of the technical and production capabilities built up by the firm as it expanded and those acquired as it adapted to the new conditions.

#### *The Case of Soft Center Hard Candy*

The plant manufacturing ARCOR's principal product, candy, suffered from serious shortfalls that affected the firm's ability to compete. The main building was on several floors and it was difficult to fully implement a continuous production-line system. The candy was manufactured and stored unwrapped in baskets that were then carried in an elevator to the upper floor for wrapping. Once the candy was wrapped, it was again put aside to await the packing of the mix. This layout led to a large amount of unproductive time, waste, an



excessive work-force, overcrowded premises and lack of order. Not only was productivity low (approximately 31.5kg per man hour) because of the interruptions to production, the system for preparing and dosing the filling manually meant that the product was not uniform and raw material consumption was excessive, increasing costs.

In 1994 it was decided to invest in the construction of a new plant and the incorporation of modern technology. From the point of view of process design and layout —performed almost entirely by ARCOR's own design department— the new plant is considered the best of its type in the world and is a clear expression of the knowledge and know-how developed by the firm.

The building has a floor space of 7,200 square meters in a single volume on one level uninterrupted by columns, allowing an appropriate conditioning of the various sectors in the production chain according to the needs of each stage of production. Currently three production lines are in operation, although there is space for a total of five, and the site and the design contemplate future expansion of the building without loss of design attributes. The large increases in production that were experienced derived not only from the effective implementation of a continuous process but also from the company's history of improvements to equipment that often ensures machinery works at above specification. This was possible because of continuous improvements to some parts of the process and the overcoming of the various bottle-necks that arose. In this process of optimization and improvement the experience gained with the old plant was decisive.

The principal technical features of the new plant are as follows:

- Automated packaging: Bosch (Germany) bagging machine, Wedside (USA) case erectors and Blue Print packer.
- Automated preparation and mixing of filling and syrup. Addition of a multiple-head Ishida high-precision scale.
- Automated cooking processes.
- Addition of a tempering conveyor (based on the circulation of water at four different temperatures).
- Addition of larger cold tunnels (enabling longer cooling periods required for the switch to continuous processing).
- Improved air-conditioning with ventilation at each stage of the process.
- Improved organization and use of space (reduction of idle time and accidents) and fewer raw materials movements (reduction in waste).

In addition, a new technique was developed to make use of the waste materials generated in the manufacturing process. To ensure uniformity in end-



product quality it is not advisable to add such waste back into the productive process, as not all candy constituents react in the same manner to a second melting. For this reason hard candy waste is usually sold as animal feed to the livestock sector, preventing its accumulation at the plant as it cannot be reprocessed. Originally this ground waste was shipped out of the plant in burlap sacks, a costly and time-consuming procedure. As from 1999 this waste has been melted down and concentrated at around 65° Brix for shipping in tanker trucks to storage tanks at dairy farm and cattle feed lots.

### Rise in production from increase in installed capacity

Line	Description		Evolution (installed capacity)	
	Before	After	Before	After
Line 1	—	Continuous	—	1350 kg/hm
Line 2	Discontinuous	Continuous	800 kg/hm	1300 kg/hm
Line 3	Continuous	Continuous	1.100 kg/hm	1350 kg/hm

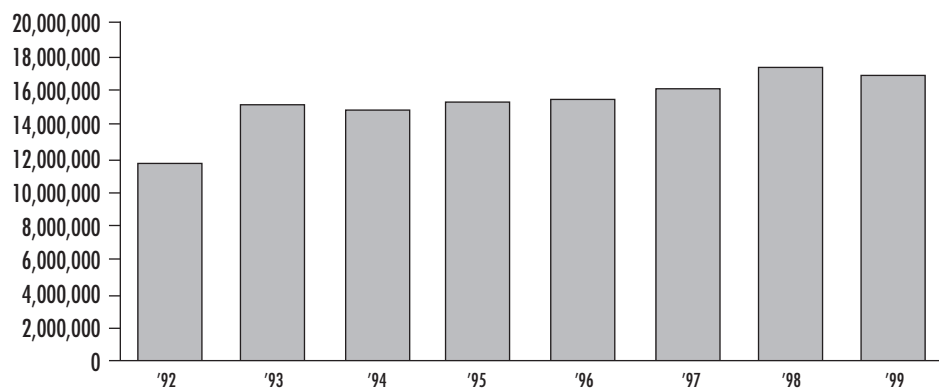
### Improvements (increases in production)

Year	Process	Bottle-neck	Improvement	Indicators
1998	Line 1 – A	350mm stamp press	450mm stamp press	360 kg/mh – 550 kg/mh
1997-99	Line 3	—	Continuous improvement	1,100 kg/mh – 1,350 kg/mh (20% increase)
1994-1999	Direct labor	Large numbers	Reduction	Cut from 290 to 166 workers to produce same volume

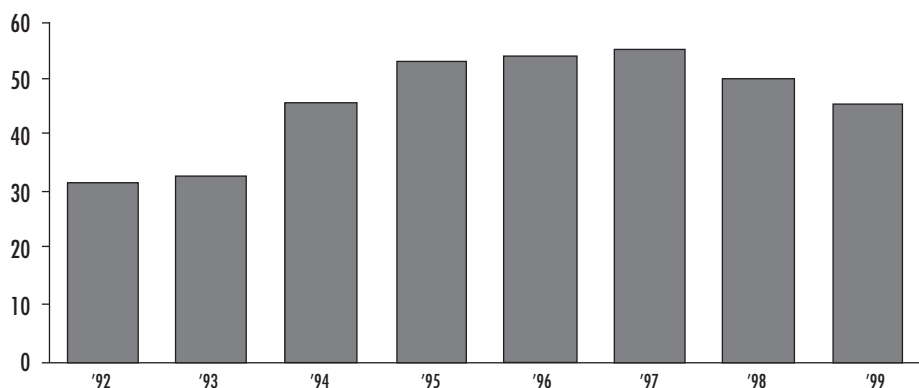
### Hard Candy Plant

Year	Kilos Produced	Hours worked	Installed capacity tn/month	Kg/h	% waste	Fixed direct labor
'92	11569156	366576.5	1000	31.56	no data	no data
'93	15196266	473256.5	1000	32.11	3.96	no data
'94	14825357	327626.5	1200	45.25	3.94	290
'95	15311891	317304.3	1200	52.62	3.04	no data
'96	15543291	345516.4	1200	53.3	3.58	no data
'97	16046447	293729.5	1600	54.63	2.49	224
'98	17287269	350441.3	1700	49.33	3.36	no data
'99	16872777	375785.7	1800	44.9	2.65	166

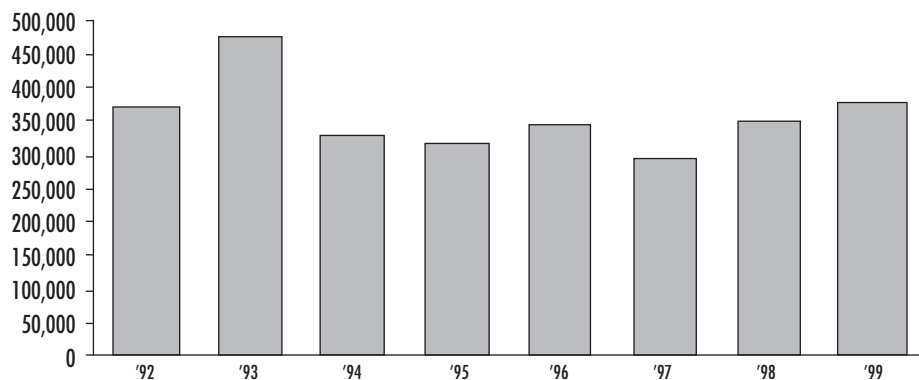
### Kilos produced

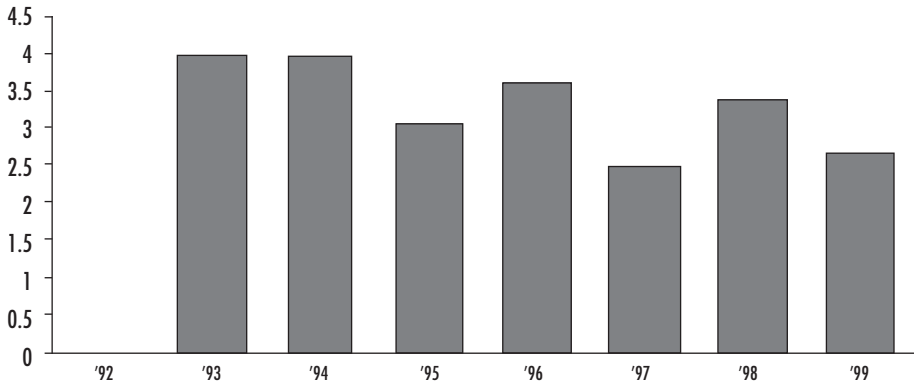


### Kg/hour



### Hours worked



**% Waste***Outsourcing the Industrial Workshop*

The industrial workshop for the design and manufacture of machines was created in the early years of ARCOR's growth as an effective response to the high cost of imported equipment and the lack of available machinery manufactured locally. Most employees had some technical experience and basic knowledge, and training was carried out on the job through the steady transfer of knowledge from supervisors to the rest of the personnel. Motivation was generated by the successful accomplishment of difficult objectives.

The industrial workshop was made up of a technical office and the workshop itself, formed by several sections —Machining, Fitting and Assembly, Boilers, Painting, Cutting of Materials and Moulds— employing as many as 128 workers in 1985. This structure represented a high fixed cost, justified by the unfavorable conditions for importing of equipment and extended delivery terms. Given this situation the workshop was competitive and provided a rapid response to the continuous requirements of the company in terms of adaptation and improvement of equipment.

As from the opening up of the economy these conditions altered. Following drastic cuts in duties on imported capital goods and an easing of credit terms, the company began to gain fluid access to suppliers and developers of equipment built according to the latest technology. The company's own workshop, not dedicated exclusively to development and the latter not being a core activity for ARCOR, was unable to match these new levels of performance. As there was a consequent reduction in internal demand, it was decided to undertake a restructuring that would enable a cut in the high fixed costs in this sector. The first step, begun in 1989, was the relocation of most of the per-

sonnel to the various growth areas of the group, strengthening the staffing of divisional R&D departments organized according to product, so by 1992 the number of employees in the workshop had fallen to 50.

Nevertheless, the firm continued to assign great importance to the service provided by the workshop, because of its ability to maximize the performance of the machines acquired abroad. The intention was to create a smaller, more competitive workshop that would achieve efficiency and quality gains through a process of specialization. With this aim in mind, in 1994 it was decided to outsource the area through a contract signed with those responsible for the Machining, Fitting and Assembly workshops. The purpose of this outsourcing was to transform fixed costs into variable costs, lower the cost of the machinery itself, reduce delivery times and improve the quality of work. Currently, goods and services for ARCOR represent 95% of the billing of this new company (FAMEQ).

## **DEVELOPMENT OF MARKETING CAPABILITIES AND THE SALES AND DISTRIBUTION PROCESS**

### **Diagnosis of the Situation at the Beginning of the Nineties**

Until the end of the eighties ARCOR had mainly worked towards resolving production problems and adapting productive resources. Through a continuous process of profit reinvestment, purchase of leading technology and the setting up of new industrial plants, the company sought to gain an international foothold based on the comparative advantages of its integrated production process. By that time ARCOR, a complex of 20 plants which in addition to foodstuffs and confectionery also produced corrugated paper, packaging, tinplate, flexible goods, paper and wrapping machinery, encompassed the full supply cycle, completing a strong process of vertical integration. Although it benefited from its highly competitive prices and full control over the productive process, it nevertheless suffered from sales difficulties.

In the context of the instability of those years, control over distribution of food and confectionery was a key factor, as it allowed regulation of the market and provided greater flexibility in the face of frequent changes in prices. Based on a structure of official distributors and far less dependent on the retail channel than the rest of the companies in the sector, ARCOR had developed advantages, in particular a very superior coverage of the domestic market. Even so, the system had some failings. There were large numbers of official distributors operating in a not very professional manner, and the company needed to increase its penetration in the markets of the Buenos Aires metropolitan region—which were increasingly being dominated by a supermarket sector still insufficiently served by ARCOR.

Beginning in the late fifties, ARCOR ran advertising campaigns to promote some of its products and brands in the confectionery, chocolate, candy and chewing gum lines. However, at the end of the 80s its advertising investment and marketing activities were less significant than those of its direct competitors in the domestic market. In general terms the company was perceived to be a second-rank firm with good quality products that lacked consumer image. Its prices were low, and although volumes were high the contribution margin was also low. Its products suffered from out-of-date packaging and weak advertising support. Although it had a strong leadership position in the interior, in the metropolitan region it had yet to develop a firm competitive position.

In the confectionery area its main strengths were in candy and in the chocolates segment—where its Bon-o-Bon brand had developed an entirely new

type of product— but it held a lower share in other categories. In the candy segment volumes had remained stable over the whole decade. ARCOR was the leader in this traditional and mature market, benefiting from its distribution advantages in the interior, with 57% of sales by volume but only 48% in terms of value. At the same time, and because of the same advantage, ARCOR led the market for lower-price chocolates (9g and 25g sizes). However, in the overall chocolates segment its market share reached barely 10%, with products at prices 50% below those of the competition and with a lower image.

In the chewing gum market the product offer by leading competitors was noted for variety and very active marketing. In this segment ARCOR ranked behind the two market leaders, weakly positioned in the traditional segment with its Cowboy brand, a far lower-priced product distributed almost exclusively in the interior.

In the case of foodstuffs, the process of strong vertical integration implemented by ARCOR provided it with advantages because of its lower prices in the commodities segment. However, the lack of any well positioned brands and an adequate institutional umbrella such as those of its competitors relegated ARCOR to a brand distributed almost exclusively in the interior. Because it is a price-driven market, ARCOR led in the canned goods segment, although without any major innovations in either products or packaging. In the case of marmalades, oil and corn flour, crackers and cookies, food mixes and ice-creams the firm's products were all at the low end of the price range, resulting in a reduced market share at the same time as compromising the image of the mother brand.

ARCOR's institutional image did indeed suffer from various weaknesses. Consumers valued its variety of products and low prices, but it was considered to be mainly a children's brand. Wholesalers clashed with ARCOR's system of official distributors, and the latter, although recognizing the quality of the products, complained of a lack of advertising and promotional support. Kiosks, particularly in the metropolitan area, although positioning ARCOR at a higher level than other retailers, did not give its products a preferential place on the displays, again because of lack of advertising and rotation.

This diagnosis of the potential and problems of ARCOR at the beginning of the 90s acquired particular relevance in the context of the transformations that began to be seen in the domestic market environment. In a context of economic liberalization, local brands and products had to compete with international corporations and brands offering products of recognized quality at

a good price ratio, and in particular benefiting from a considerable capacity for product innovation. At the same time it was evident that self-service was the growing trend in consumer shopping habits, reinforcing the negotiating strength of supermarkets and large retail distribution chains. At a time when companies were required to be business and market oriented, those firms such as ARCOR that had not developed sufficient brand capital could have found their other competitive advantages severely weakened.

In short, given this scenario the strategic matrix for ARCOR in this regard was based on its strengths in distribution capacity, its good image and leadership in the interior of the country, the spread of certain important brands (Bon-o-Bon, Menthoplus, Cowboy) and the control of various plants in MERCOSUR countries. At the same time it also showed certain weaknesses such as a relative lack of institutional image, a product image mostly associated with candy and a deficit in the area of brands, advertising, packaging and presence in the Federal Capital and Greater Buenos Aires. The arrival and installation of powerful international brands represented a potential threat, and at the same time the formation of MERCOSUR and the opening up of Latin American markets represented a significant opportunity.

This means that ARCOR had many valuable attributes but also several aspects that needed correcting. In particular, it needed a surge in marketing effort to leverage its remaining competitive advantages and benefit from the opportunities in each market. The development of its brand capital and institutional image became an absolute priority for facing up to future scenarios and maintaining and consolidating a policy for the launching of a large number of products on the market.

### **Strategic Decisions and Objectives Established**

At the beginning of the decade the decision to turn ARCOR into a food and confectionery company with an international reach and top-quality products at the best price was reinforced through the setting of specific objectives at various levels:

*a) Corporate positioning:* The aim was to demonstrate that ARCOR's low prices were not a consequences of any lower quality. It was necessary to advertise a reality: the company worked on the basis of an integrated production process that, as well as being unique, was intended to ensure that supplies, from raw materials through to packaging, should be made with the best raw materials, using the most advanced technology certified under ISO 9000. It was necessary to highlight this microeconomic characteristic that ensured

constant quality, lower costs and effective control at each of the manufacturing stages.

The Objectives Established were as Follows:

- To offer consumers products with quality they could rely on, recognized brands and competitive, accessible prices.
- To create within the organization a market-based culture, with strong awareness of the importance of quality and excellence.
- To ensure permanent care of the environment and total quality in all processes.
- To achieve an increase in total sales.
- To increase exports at a faster rate than the increase in domestic sales.

**b) Strategic markets:** Both confectionery and food markets were very competitive and predominantly stagnant, with low contribution margins and fashionable products that required a heavy investment in advertising. Given the particularities of each segment, markets defined as having a high level of potential were: i) confectionery, stressing the nature of ARCOR as a leader; ii) chocolates, developing new brands and entering new segments; iii) chewing gum, developing a wider range of products; iv) *alfajores* and fine chocolates, evaluating the possibility of extending the “Bon-o-Bon” brand into both markets; v) marmalades, canned goods and corn flours, stressing the company’s quality control as from the raw material; vi) biscuits and snacks, with an increased penetration planned as from 1993 or 1994. It was considered necessary to increase integrated production processes, installing new plants and production lines for candy, chocolates, *alfajores* and chewing gum, all under strict ISO 9000 and 14001 standards. In addition, it was also possible that certain established brands might be bought to strengthen positions in those markets considered to be of interest.

Once the strategic markets had been defined the decision was taken to adopt a new structure for the organization, creating four business units —confectionery / foodstuffs / chocolates / crackers and cookies— each of which faced different competitors in their various markets. When one looks at the excellent results obtained during the nineties it is evident that this process of specialization by business unit has been largely responsible for the growth achieved.

*Some of the Objectives Established for the Confectionery Segment were as Follows:*

- To revitalize the candy market with new flavors and product variety, increasing sales by 30% and average prices by 20%.



- To develop a senior brand to achieve leadership within 5 years in sugar-less gum and a new brand in the children's and adults gum categories with the ability to dispute leadership, increasing sales by 100% and average prices by 50%.
- To develop a lollipop brand that will enable the placement of this product in new markets.

*Some of the Objectives Established in the **Chocolates** Segment were as Follows:*

- To develop the market for *alfajores*, using all the company's brand capital and purchasing new brands.
- To develop a leading brand in the chocolate bar segment and deepen overall development of the market for chocolates, launching new products with a higher contribution margin, using new or acquired brands, increasing sales by 100% and average prices by 10%.
- To participate in new categories, especially in candy-coated chocolates, chocolates for the child segment with surprises and seasonal markets such as that for Easter.

*Some of the Objectives in the **Foodstuffs** Sector were:*

- To develop associations with agricultural product suppliers, providing them with technical, commercial, economic and financial assistance.
- To develop a highly innovative line of jam and marmalade products as a leader, under the company's own brand or through the purchase of a brand, increasing sales by 30% and average prices by 25%.
- To innovate in canned goods and sauces, launching new products and brands, increasing sales by 50% and average prices by 20%.
- To develop the corn-flour market, increasing sales by 50% and prices by 70%.
- To reposition the "Godet" brand as the leading brand in powdered mixes and desserts.

*Some of the Objectives in the **Crackers and Cookies** Sector were:*

- To enter the biscuit market with own brands as from 1994, increasing sales over the first two years by 30% and prices by 15%.
- To develop the snacks market as from 1995 with new or acquired brands, leading the market by 1997.

**c) Brand policy:** Strategy in this area was aimed at: i) creating identities or sub-brands for all new products, leaving only candies for the longer term

because of their traditional identification with the ARCOR brand; ii) in the long term using the ARCOR umbrella for as many brands as possible; iii) not using it, however, for those brands that strategically operate as a strong barrier against advances by the competition (such as Águila, Misky, Cabsha, Noel), which at some time in the future could be brought under the ARCOR umbrella; iv) taking advantage of certain brands to extend them to other generic products (Bon-o-Bon, for example).

**d) Development of distribution and sales:** Within the framework of an overall reorganization of the sales structure it also became essential to define the evolution of the company's own distribution system and develop sales in the city of Buenos Aires and the Greater Buenos Aires region. It was therefore decided to: i) organize and train a sales structure to serve supermarkets, although with the idea that this channel should not account for a major proportion of shipments; ii) modify the traditional structure based on the assigning of sales personnel by geographical area, transforming it into a network of businessmen and women specifically selected according to customer profile; iii) having analyzed the different requirements of each link in the chain, set up a sales organization with professionally-qualified staff specializing in Major Accounts, Supermarkets and Wholesalers.

The Objectives Determined were:

- To ensure more aggressive penetration in the city of Buenos Aires and the Greater Buenos Aires region through direct handling of sales to large chain stores.
- To improve the development of distribution, reorganizing the system on the basis of the business profiles defined, upgrading distribution company capabilities, training its personnel and creating an area for services to distributors.
- To generate and promote new systems for distribution: convenience stores, maxi-kiosks, shopping malls, creating a special sales division in 1994.
- To develop catering system sales through the creation of a specialized division in 1994.
- To increase market share in the Greater Buenos Aires region by 5% on average for all products.

**e) International growth and foreign markets:** The foreign sector was considered a key area for development. Based on the advantage provided by its existing network of plants in neighboring countries, it was decided to take advantage of the new conditions provided by the MERCOSUR to increase interchange between them, developing more efficient strategies for special-

ization and complementation. Naturally MERCOSUR was considered a priority and maximum strength area, but the strategy also contemplated the development, in the short term, of markets in Chile, the rest of South and Central America and the United States, and, more gradually over the medium term, markets in the Middle East, Africa and South-east Asia.

### **Actions Taken**

Between 1991 and 1995 ARCOR launched 300 new products and over 500 separate items on the market, changed virtually 100% of its packaging and created close to 100 new brands, supporting them with intensive advertising campaigns. It invested over US\$ 150 million in this area, equivalent to growth of 1500% as compared to the previous five years. This activity continued in the second half of the decade, during which the company launched approximately one hundred new products per year on the market. At present the company manufactures over 1500 separate food and confectionery items.

Numerous actions were taken in various business areas to carry out this overall strategy for the development and positioning of new products, brands, packs and image. The most significant included:

- The launching on domestic and foreign markets, of the *Butter-toffee* candy line, an international-quality product that created a new category of soft-centered milk candy products, and the development of the *Topline* brand of sugar-free chewing gums.
- The launching of the *Cofler* brand, positioning it as a line with a wide variety of quality chocolates and innovative packaging.
- Repositioning of the *Aguila*, *Cabsha* and *Tofi* brands (acquired with the purchase of *Aguila*), launch of candy-coated Rocklets, (halting the entry into Argentina of world-leading “M&M”), full-scale development of the prestigious “Bon-o-Bon” brand, expanding its product varieties, and the extension of several of these brands to promote products in the very dynamic *alfajor* segment.
- Launching of a new line under the ARCOR name for high-quality *premium* jams and new presentations of canned vegetables, manufactured using the latest technology for the aseptic treatment of fruit pulp for better preservation of natural flavors.
- Launching and development of the *Maná* brand in the crackers line, backed by production from the new plant at Salto (in the province of Buenos Aires) equipped with the latest in international technology, and the launch of the *Saladix* line, strategically supported by its range of flavors.
- Launching of the *Mr. Pop’s* brand, a line of lollipops to compete on international markets.

- Launch and development of the *Arcor Cereal Mix* brand to compete in the cereal bar market.

These actions, taken to diversify products and markets, were complemented by changes and the introduction of new practices in the sales and distribution area, the most significant of which were:

- Reorganization of the direct distribution system, making it more professional and cutting the number of official distributors, with a US\$20 million investment in distribution logistics systems, optimizing the transport system, lowering costs and delivery times.
- Sales force specialization by customer profile and improved training of order-takers in the supermarket channel so they can become skilled merchandisers with career plans and negotiating powers.
- Setting up of the International Division, providing specialized attention to each foreign market, with persons directly responsible for marketing, administration and logistics in each geographical zone and the planning of a global supply strategy based on synergy with ARCOR plants abroad and the consolidation of more than 1700 trade-mark registrations around the world.
- The development of the Brazilian market, with direct distribution systems in the main states, the purchase and development of plants in Brazil, Chile and Peru and increased presence in the US market through the opening of a branch in Miami.
- Opening of new branches in Mexico, Colombia, Ecuador and Canada, consolidating the commercial structure at continental level.
- Development of the Israeli market through importers, obtaining of a *kosher* certificate and developing packs in Hebrew for chocolates and corn oil, and markets in China, Vietnam and South Korea for the *Butter Toffee* brand and soft-center candy.

## Results Achieved

In general terms, all the objectives established in the design of the strategic plan at the beginning of the nineties were more than fulfilled over the course of the decade, with a rise in sales and market share in excess of forecast in the case both of confectionery and chocolates, crackers and cookies and foodstuffs. In the stable environment for growth experienced in Argentina since 1991, ARCOR's market and organization strategies received a boost, ensuring that the company was able to take maximum advantage of its competitive advantages. It continued to carry out its policy for constant innovation in the development of new products, with a work-force that was increasingly

qualified and professional. In addition, the incorporation of marketing and institutional communication as added value for its productive strengths also made it possible to maximize its earnings on capital invested. The strategy for expansion and the occupation of Latin American markets also positioned it as one of the leading players in both segments in the region. Furthermore, not only did ARCOR's market share rise significantly, so have its prices and contribution margins.

Information provided by Nielsen y Asociados confirms the market performance of various representative products made by ARCOR in the period 1991-99. The overall trend has been noted for: a) a significant increase in product distribution scope, both as regards the number of stores selling the brand (physical distribution) and in the supply of those with the highest level of sales (weighted distribution); b) increased share in all markets; and c) improvements in product quality and brand development, implying a rise in prices until 1995-96. This increase was reversed in recent years because of the impact of the recession and the drop in income that affected the Argentine economy—leading to price deflation and the growing participation of sales channels with lower margins (supermarkets).

- In the market for bite-size and individually-wrapped chocolates, the company continued to lead in a segment in which it competed with firms such as Suchard, Felfort, Ferrero, Nestlé and Garoto. ARCOR's market share grew from 35.5% in 1991 to 56.7% in 1999. Over the same period, physical distribution increased from 47% to 70% and weighted distribution went up from 95% to 98%. In turn, prices increased by 18% between 1991 and 1995, falling by a slight 2% until 1999.
- ARCOR's growth in the market for *alfajores* was significant, gaining ground on or overtaking competitors such as Bagley (Danone), Terrabusi (Nabisco), Suchard, Nestlé, Jorgito, Fantoche and Guaymallén. In the period 1991-1999 its market share rose from 5% to 23.8%, physical distribution increased from 11% to 46% and weighted distribution was up from 11% to 76%. Prices increased from a minimum of \$4.83 a dozen in 1991 to a maximum of \$9.02 in 1995, falling back subsequently to \$6.39 in 1999.
- In the cracker and cookie market the company reached a share of 23%, taking over second place and gaining on the leader, Nabisco. In the case of cookies, in which there was a notable penetration by the Maná brand, in the period 1992-1999 as market share rose by 11.1% to 14.4%, physical distribution increased from 62% to 69% and weighted distribution increased from 69% to 82%—while prices went from \$ 3.34 in 1992 to

a maximum of \$ 3.91 in 1996, falling to \$ 3.28 in 1999. In the market for assorted biscuits, in the period 1992-1999 the share went from 22.2% to 24%, physical distribution rose from 22% to 33% and weighted distribution increased from 38% to 50%. In turn, prices varied from a minimum of \$ 3.76 in 1992 to a maximum of \$ 4.19 in 1995, falling later to \$ 3.50 in 1999.

- In the snacks market the performance of ARCOR's Saladix line has been very successful. Competing with similar products manufactured by Danone and Nabisco the company managed to increase its market share from 3.6% in the year of its launch (1995) until reaching its market leadership position with 40.9% in 1999. That year its physical distribution was 57% and its weighted distribution 91%.
- In the markets for the various types of chocolate products performance in the nineties has been a notable success, as out of the 8 categories into which this market is divided in Argentina, ARCOR is the leader in 7 (bite-size items and chocolates, *alfajores*, tablets, candy-coated, child and Easter) and is second in wafers. As an example, in the coated candy segment the introduction in 1994 of Rocklets gave the company the lead over M&M so that in 1999 it controlled an 89% market share and 99% of the weighted distribution. In the case of drinkable chocolate and topping chocolate, with its Águila, ARCOR and Godet brands the company is the absolute leader with 67.5% of the market in 1999.
- In the foodstuffs segment, with its Arcor, Noel, Titán, Versailles, Presto-pronta, Godet and Dulciora brands the company leads in 11 of the 17 segments in which it participates, such as "traditional jams" (44.6% market share), "tomato products" (with market shares of 23.6% for tomato puree and 21.6% for peeled tomatoes), in "corn meal" (68.9% share in instant polenta and 54.7% in traditional polenta) and in the case of "corn oil" (38.2% market share). In the canned vegetables segment the company leads in "peas" (25.7%), "corn" (30.3%) and "mixed vegetables" (27.4%).

One final aspect to be highlighted is the share held by ARCOR in volume terms of the total market and the structure of the sales channels used by the company in comparison with the total market in 1999. ARCOR leads with 16.2% of the total market, followed by Nabisco-Terrabusi (11.9%), Danone-Bagley (10.5%), Kraft-Suchard (7.4%), Molinos (5.6%), Cadbury (3.9%), Warner Lambert (3.7%) and Canale (3.4%).

Markets in the interior accounted for 71.2% of ARCOR's domestic sales, against 28.8% accounted for by Buenos Aires. These figures clearly indicate the company's greater penetration in the interior and differ significantly from

the share of the total market accounted for by the Interior, which is 53.8%. Such discrepancies can also be seen in the various sales channels, as kiosks, traditional stores and convenience stores in the interior have a relatively higher participation in ARCOR's sales, compared to its lesser relative weight in supermarkets and convenience stores in Buenos Aires.

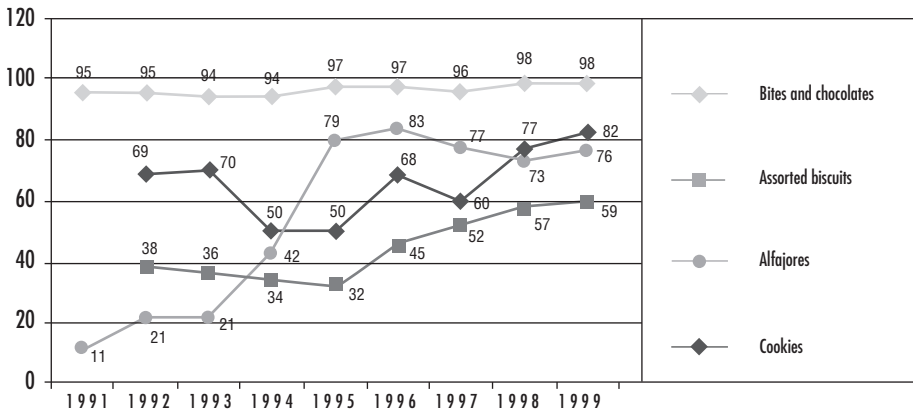
This successful performance was backed by two further elements. On one hand, effective, aggressive marketing actions were developed, enabling the repositioning of the company and the achieving of very strong brand values. This activity involved total marketing strategies, gaining maximum leverage from the price and quality attributes that were always present. In addition, a specific institutional communication strategy was carried out to position the main ARCOR brand as an effective umbrella for the rest of the individual brands.

As a result, ARCOR's institutional image improved significantly, as the company became widely recognized as a leading brand in the market. In a survey of 350 executives published by Clarín newspaper on May 28, 2000, ARCOR obtained first place in the overall ranking for the company with the best image in Argentina, as well as maintaining this position in 6 of the 8 categories considered, being the only domestic firm in the top ten positions (followed by Coca-Cola, Repsol-YPF, Unilever, Telecom, Citibank, Telefónica, Microsoft, American Express and Mercedes Benz).

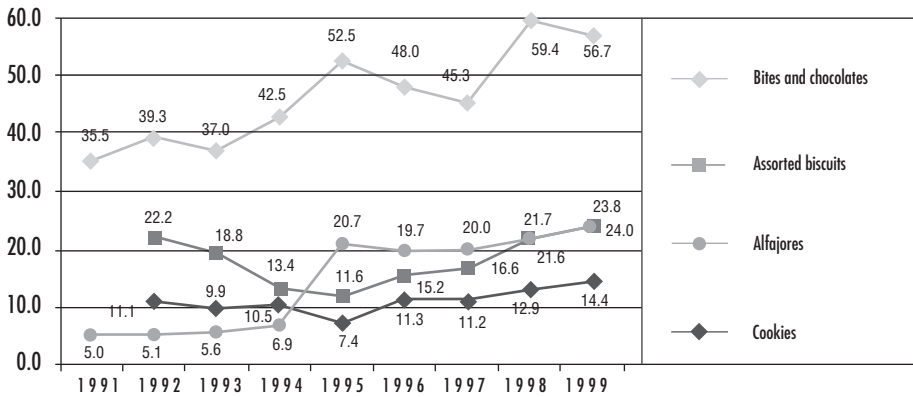
Overall ranking	1
Quality of products and services	1
Creativity in sales management and marketing	1
Economic solvency	6
Honesty and business ethics	1
Adaptability to changes	1
Quality of management	1
Evolution	2
Relationship with community and environment	1

In conclusion, it is worth pointing out that in a similar survey by the same media in 1994, ARCOR had occupied 47th place.

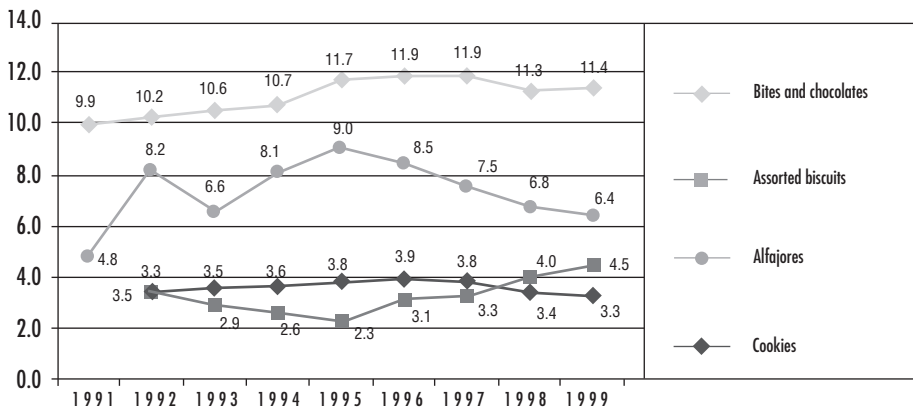
### Evolution of market share of certain products (1991-1999)



### Share in volume



### Price per kilo

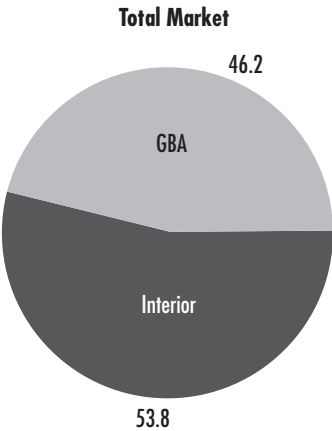
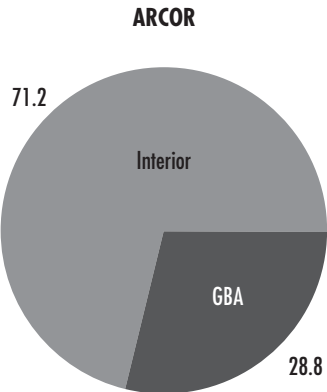


Source: Based on data from Nielsen y Asociados



ARCOR’s Sales Channels and their Comparison with Total Market  
(1999) (by volume of sales)

Sales channel	Total market in 1999	ARCOR 1999	Performance compared to market
Supermarkets in GBA	17.1	9.1	-46.9%
Supermarkets in Interior GBA	15.6	14.0	-10.1%
Convenience stores Interior	6.6	3.8	-42.0%
Convenience stores	9.7	11.1	14.9%
Traditional stores in GBA	9.9	4.5	-54.5%
Traditional stores in Interior	13.5	18.7	38.6%
Kiosks and Mini-stores in GBA	12.6	11.4	-9.3%
Kiosks and mini stores in Interior	15.0	27.3	81.9%
Total	100.0	100.0	-



Source: Based on data from Nielsen & Associates

Share of Market Volumes - ARCOR and Leading Competitors

Companies	Total market share
ARCOR	16.2
Nabisco	11.9
Danone	10.5
Kraft Suchard	7.4
Molinos	5.6
Cadbury	3.9
Warner Lambert	3.7
Canale	3.4

Source: Based on data from Nielsen & Associates

## Some Awards Received During the 90s

- **No.1 in CEOP corporate image and prestige ranking in 2000** (*Clarín* newspaper)
- **Roll of Honor - Candy Hall of Fame 2000**, Luis Pagani (National Confectionery Sales Association, U.S.A.)
- **“Businessman of the Year Award -2000”**, Luis Pagani (*Prensa económica* magazine)
- **“Mate.ar de plata 2000”** Award for the best web sites, for [www.ARCOR.com.ar](http://www.ARCOR.com.ar) in the “Economy and Business” category.
- **“Ciudadanía empresaria 2000” Award**, for the company’s “Overcoming limits” program (AmCham)
- **“Eikon 2000” Award** for “Excellence in institutional communication” in the General Communication Campaign category (*Imagen* magazine)
- **“Puma de oro 2000”** Award to the food company with the highest prestige in the Cuyo region (*Mercado* magazine)
- **“Puma de oro 2000”** Award to the company with the greatest prestige in the province of San Luis (*Mercado* magazine)
- **“Business leader of the year 1999”**, Luis Pagani (Company Directors Association)
- **“Eikon 1999” Award** for “Excellence in institutional communication” in the Communication of Corporate Identity category (*Imagen* magazine)
- **“Ciudadanía empresaria 1999” Award**, for the company’s “Overcoming limits” program (AmCham)
- **“Konex de platino 1998” Prize**, ARCOR “Company of the decade” in the Business and Community category
- **“Konex de honor 1998” Prize**, Fulvio Salvador Pagani.
- **“Eikon 1998” Award** to “Excellence in Institutional Communication” for the ARCOR website (*Imagen* magazine)
- **“Exportación argentina 1998” Award** (*Prensa Económica* magazine)
- **Recognition as “Largest exporter among mid-size companies, 1998”** for LIA (Government of the Province of Córdoba; Foreign Commerce Chamber, Province of Córdoba)

- **Distinction “for contribution to bilateral trade and productive investment”** between Argentina and Chile, 1998 (Argentine-Chilean Chamber of Commerce)
- **“National Unity Award, 1998”**, to Grupo ARCOR “Source of employment for thousands of families” (Movimiento Familiar Cristiano)
- **“Businessman of the Year”**, Luis Pagani (*Punto a Punto* weekly, Córdoba)
- **“Businessman of the Year 1997”**, Foodstuffs Category (Security)
- **“Mercurio 1996” Prize**, for ARCOR Institutional Advertising (Asociación Argentina de Marketing)
- **“Entrepreneur 1996” Award**, Luis Pagani (*Mañana Profesional* magazine)
- **“Expoinnovador 1996” Award**, Luis Pagani (*América Economía* magazine)
- **“Invertir 1995” Award**, Colonia Caroya Plant (Invest Argentina Foundation)
- **“Latin American Food Processing Company 1995”** (*Alimentos Procesados*, USA)
- **Award for “Best Food Plant in the World - 1994”**, for the Colonia Caroya chocolate plant (*Food Engineering International* magazine)
- **“Mercurio 1993” Award**, for Cofler (Asociación Argentina de Marketing)

## HUMAN RESOURCES

### **Accumulated Strengths and Weaknesses**

By the early 90s ARCOR's personnel already numbered more than 6000, with approximately 12% employed in undertakings developed by the company abroad. The attribute and principal strength of this asset was the high level of technical training of the production work-force. As mentioned previously, the evolution of the firm has been based since its creation on the development and constant improvement of manufacturing aspects for all its many production lines, and this approach was clearly evident in the skills of company human resources. Production was what ARCOR's personnel knew how to do best, and they did it very well.

This capability was complemented by an innovative and creative vocation in the same areas which had grown to become part of standard management practice. The existing work-force included a large number of young people with skills and potential for generating and leading team initiatives. Although teamwork methodologies were not formally implemented within the firm, management tended to encourage them in their respective areas, with mixed results. This spirit of innovation in middle-rank management allowed them to interpret changes in the conditions of the environment and accept the necessary internal adaptations.

In the case of the organization and development of the Human Resources area, strengths were restricted to ensuring high levels of efficiency in Personnel Administration aspects —with an adequately staffed and equipped department for the performing of tasks such as payroll services, attendance control, health and hygiene matters, accident prevention, medical services and union matters in general. At that time ARCOR employed a functional Human Resources Manager, but lacked infrastructure and resources to fully develop the area.

This shortfall had the effect of weakening management operating capacity. To begin with, there was a problem with the definition of competencies and functions among managers and, in addition, these same managers concentrated more on day-to-day operating aspects than on planning and the definition of strategies and objectives. This situation reflected the absence of specific policy regarding personnel selection and hiring, structure, description and evaluation of job positions, training, performance and potential assessments and career and promotion plans. There was also a training and preparation deficit at some management levels in certain areas.

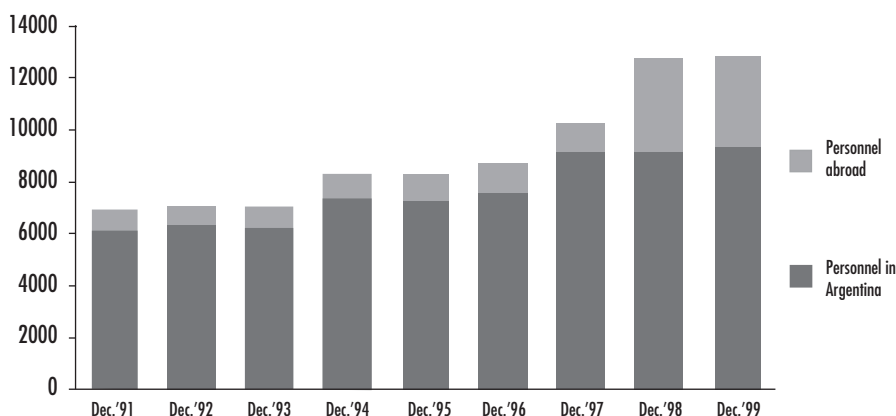
## Strategy and Evolution in the 90s

ARCOR's personnel increased considerably during the 90s, almost doubling in numbers. This trend was a result of both the growth of the company's traditional activities and the process of absorption of other businesses as well as the strong increase in the operations of the company itself and its subsidiaries abroad.

The principal, strategic change in this area can be summarized in two main actions: i) the developing of an integrated Human Resource management; ii) adding of professional skills to Human Resource management. These ac-

### Growth in Personnel Numbers at ARCOR. 1991-1999

Personnel	1991	1992	1993	1994	1995	1996	1997	1998	1999
Argentina	6,108	6,342	6,287	7,379	7,291	7,601	9,190	9,158	9,283
Abroad	773	689	757	905	1,002	1,061	1,100	3,580	
3,537									
Total	6,881	7,031	7,044	8,284	8,293	8,662	10,290	12,738	12,820



tions took place by means of the adoption of strategies in specific areas and the definition of organizational, resource development, personnel administration, selection and hiring, training and development and union relations aspects.

A significant change at the outset took place in the organization of the area itself, with the forming of a sector able to deal with the planning and develop-

ment of all these aspects. The main features of the new organization can be summarized as follows:

- Setting up of Business Units led by general managers with responsibility for the results of their area (strong process of delegation).
- Generation of a matrix structure with strong functional areas in Administration and Finance, Industrial Activities and Human Resources.
- Introduction of systems for administration of positions and salaries intended to achieve uniformity within the company and market competitiveness.
- Setting up of Human Resource managements for each Business Unit.
- Creation of the position of Human Resource Analyst for each Business Unit, to focus on training aspects.
- Creation of a Marketing function and area for consumer businesses.
- Introduction of new management tools, such as Strategic Planning, Management by Objectives and Budgeting.

Administration systems were modernized through the computerizing of processes and the establishing of a complete system of performance indicators and evaluation. Here the main purposes pursued by such changes were:

- Standardization and integration of all Human Resource processes.
- Facilitating and optimizing the handling of information to provide timely and reliable service to all internal customers.
- Defining of a Policies and Procedures Manual for the whole Group.

At the same time a system of performance indicators was established based on international *benchmarking* developed with the assistance of the Saratoga Institute. Through the calculating of some of these indicators, it is possible to measure the degree of professionalism reached by Human Resource management in the final years of the decade.

**Human Resource Staff compared to total personnel  
(number of personnel per Human Resource employee)**

ARCOR indicator: 117

Market indicator: 96

**Human Resource Administration Staff  
(number of personnel per Personnel Administration employee)**

ARCOR indicator: 189

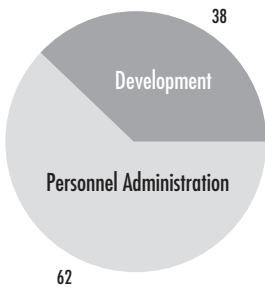
Market indicator: 206

**Human Resource Development Staff  
(number of personnel per Personnel Development employee)**

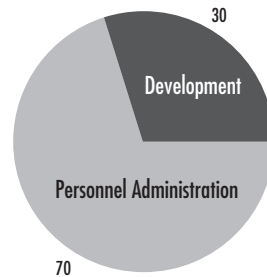
ARCOR indicator: 310

Market indicator: 393

**Composition of the Human Resources  
Department July 2000**



**Composition of the Human Resources  
Department July 1999**



As indicated in its “Benchmarking 2000” report, the ratio of ARCOR personnel to each Human Resources employee has remained constant in the last 2 years. On the other hand, analysis of the distribution between Development and Administration of Personnel shows the increase in productivity of the Personnel Administration function, mainly as a result of the improvements made to the systems adopted in the area and a greater assignment of internal resources to the Development function. It is evident that management in this area has been able to make efficient use of the economies of scale available in Human Resources functions: as the number of internal customers grows, increased productivity can be obtained from each one of those functions.

In the area of **recruitment and selection** of personnel an aggressive process of identification and incorporation of university professionals was developed for those areas of the firm with a lower content of employees with such a level of formal education: Sales, Human Resources, Quality and the first line of supervision in the industrial area. Without desisting from its usual direct recruitment of personnel for the industrial areas from the School of Engineering of the Universidad Nacional del Litoral and for administrative areas from the School of Economic Sciences of the Universidad Nacional de Córdoba, the search was extended to universities across the whole country by means of a systematic forming of links with various public and private universities. Selection and hiring gradually began to be channeled through specialist consultants.

The process of hiring of university graduates, middle management and managers led to the incorporation of tools such as psychological technical aptitude tests, Hermann profiles, Disc profiles and value tests. The Assessment Center technique was introduced to evaluate the development potential of the candidates for the young professionals programs (see box later in chapter). Advanced knowledge of English became an essential requirement when selecting such young professionals. The incorporation of highly-qualified personnel from companies acquired during these years also contributed to the process of improving the standard of company resources. As a result of the new profiles that were established the average age of personnel tended to decline, currently standing at 35 years for the group and 25 years for the newer plants.

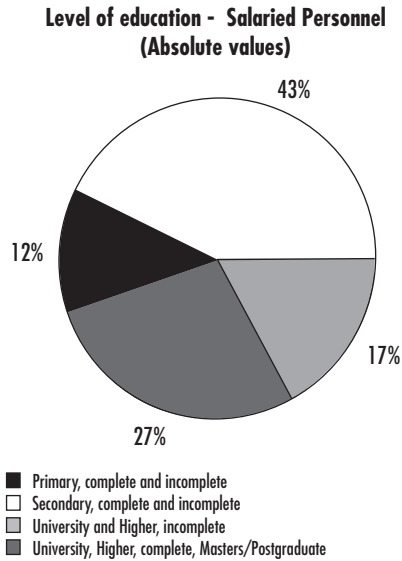
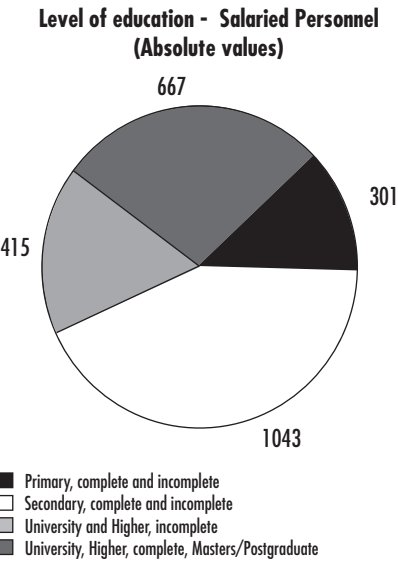
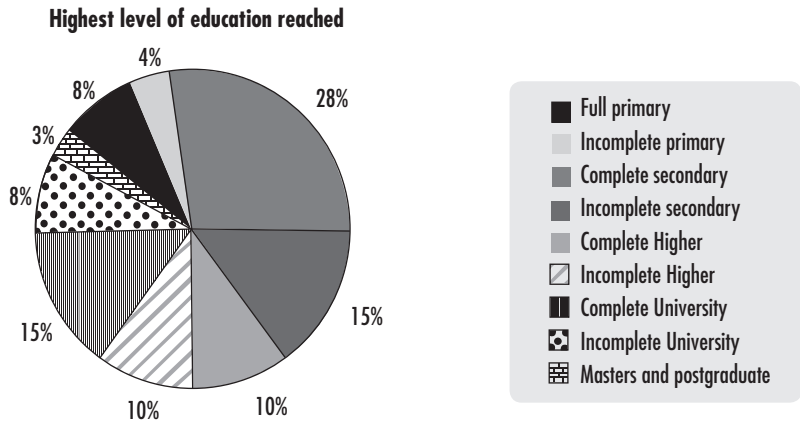
Formal educational requirements for production line personnel were also raised, generating a visible change in profile in direct labor. Until the 80s workers were only required to have completed their primary education. Changes in technology at the various group plants during the following decade meant that production worker vacancies were required to be filled by candidates recording a completed secondary education in technical subjects or at technical institutes.

All these actions were accompanied by a purposeful strategy for the development of human resources based on three fundamental pillars: training, evaluation and incentives based on results.

In the field of **training**, emphasis was placed on management courses for supervisors and managers. Training based on visits to trade fairs was complemented by postgraduate courses for professionals, with a minimum number of three to five participants. This initiative included participation on *Master's in Business Administration* programs in Argentina and abroad for personnel



Level of education reached	Total
Low	10
Full primary	205
Incomplete primary	96
Complete secondary	685
Incomplete secondary	358
Complete Higher	248
Incomplete Higher	232
Complete University	355
Incomplete University	183
Masters and postgraduate	64
<b>Total</b>	<b>2,436</b>



considered to be of high potential, and the application of Management Development programs carried out in-company or at business schools for management levels.

At the same time a program was developed to improve the professional skills of the sales force by means of training plans aimed at developing selling capabilities directed at modern sales channels. In addition, the introduction of new production and management techniques led to the need for intensive retraining of direct labor. In particular, programs were developed for training in automation and computerizing of production lines and the implementation of industrial standards such as ISO 9000, ISO 14000, Total Productivity Maintenance, 5 “S” and IRAM 3400, among others.

**Performance evaluation** systems were introduced for each type of competency, adopting processes such as People Review, identification of K Positions, identification of K People, Evaluation of Performance and Appraisal of Potential, Replacement Charts and personalized training and development plans for Strategic Resources.

The **remuneration** system was redesigned at the same time. A system of salary bands based on average market values was gradually introduced, as were various forms of compensation based on performance. In the case of management levels, variable remuneration was related to the objectives and results of the specific area, while in the case of operations personnel it was linked to productivity. This system of remuneration was approved by the union authorities—with ARCOR being the first company to reach such an agreement—and is in force in most of the establishments of the group. It combines an individual bonus with a bonus based on increases in the performance of the production line.

Lastly, the rapid process of **internationalization** experienced by ARCOR provided an impulse for the definition of a strategy for forming professional teams for developing operations abroad. At present around 1% of personnel working in manufacturing plants, branches or sales offices abroad are employees who have been transferred from their bases in Argentina, Chile and Peru.

Two strategic objectives are fulfilled by these transfers. Firstly, they are a way of transmitting ARCOR’s corporate culture to the various different countries; secondly, advantage is taken of the opportunity to meet the personal development needs of staff with potential for growth within the organization. Countries currently hosting personnel from other branches are Brazil, Chile, Paraguay, Peru, USA, Uruguay, Ecuador, Colombia, Mexico and Canada. The positions most often filled by expatriates are those of branch managers, administration managers and sales and marketing functions.

**ARCOR Personnel - Domestic and Expatriate Personnel 1991-1999**

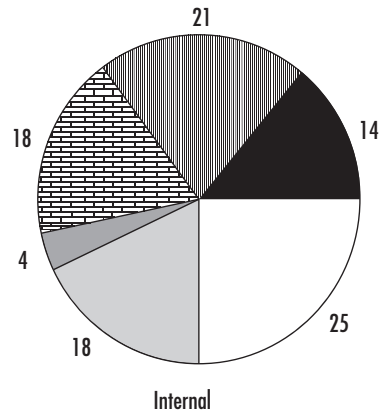
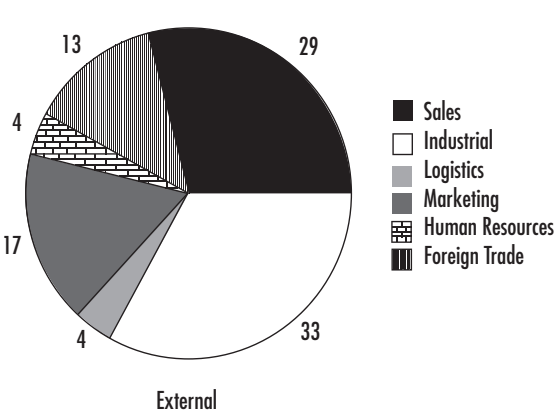


**Summary of the process of external selection. Plan 2000**

Location	Number of candidates pre-selected	CV in line with profile sought	Intake
Federal Capital	427	376	10
Interior of country	289	199	12
Abroad			2
TOTAL	716	575	24

**Relationship between the professionals hired and the areas of specialization**

**Young professionals: selected from the market for the 2000 program**



### **Young Professionals Program**

*This program was started in 1994 and was restructured and strengthened in 1998. Initially prior knowledge of English was not required for joining the program. Candidates submitted a project, agreed to by those responsible for the area, to be carried out while continuing to work at the company. Once a project had been approved, each area drew up a rotating work schedule. Later, responsibilities related to compliance with the tasks assigned were incorporated on a gradual basis.*

*The program was redesigned in 1998 on the basis of the project for growth and internationalization of the Group. This definition of new values led to the recruiting of young persons with the skills required by this new professional profile. The program is corporate and is carried out together with the countries where ARCOR has branches. Each Business division is assigned a quota on the basis of total vacancies. Since the beginning, these young professionals fill a specific position in a real job, without rotation in the various areas.*

*In addition to the overall growth of the company, this program has been another factor contributing towards a better positioning of ARCOR as an employment opportunity for university graduates. According to the annual Mercado-Mori survey, the ARCOR group is among the top five most popular places of employment for graduates, with a particularly good showing in the careers of Administration, Marketing and Advertising, Physics and Chemistry and branches of engineering.*

*General features; the full program lasts 12 months and basic requirements for participation are a University degree with a good academic average, up to 27 years of age, an intermediate to high level of English and willingness to transfer to the interior of the country or abroad. Previous work experience is not mandatory.*

*Basic Purpose: hiring, training and career development of young professionals with high potential who in the future will be responsible for carrying out ARCOR group business strategies.*

*Coordination: The training process and its contents have been suggested and approved by the company Board. They reflect strategic growth needs. As a business need, the direct superiors of the participants are responsible for implementation. Coordination of activities is the responsibility of Human Resource Corporate Management.*

*Candidates for training: Young professionals selected on the basis of their performance, potential and possibilities of growth within the company.*

*Purpose of training: i) to satisfy the training needs of this group of professionals; to provide tools and operating techniques to contribute to the development of the young professionals within the organization; iii) to support the incorporation and integration of these young people, giving them a sense of belonging to a project that is undergoing growth, internationalization and acquiring increasing complexity.*

*The training process is divided into various stages:*

- a) Training of supervisors: workshops will be held in order to provide them with tools for coaching and performance evaluation.*
- b) Training of the young professional: 5 modules will be offered during the year, dealing with the following aspects: Teamwork, Induction into the Corporation, Professional Performance, Culture of the Organization and Self-development. All these modules are residential, to encourage exchanges and so that participants can get to know each other. Activities are designed to allow supervisors and managers to be visible as teachers, so they are called upon to teach some of the courses. Furthermore, in order to receive input representing different perspectives on market and economic reality, external specialists are invited to give lectures during each module.*
- c) Follow-up of the evolution of the young professionals: made by means of work plans, regular interviews and performance evaluations. The latter are designed to provide information on potential as well as past performance.*

*Development of the program: in 1998 and 1999 36 and 50 young professionals participated in the program, recruited internally. In 2000 the intake was 53 people, located through both internal and external searches.*

## FINANCIAL DEVELOPMENTS

### The Crisis at the End of the 80s

In the context of the macroeconomic instability that existed in the eighties, in particular following the consolidation of the pattern of high inflation and widespread monetary indexation, financial management by companies in Argentina assigned priority to short-term movements and the situation in the immediate future. In the first place, capital markets and long-term loans were virtually non-existent, and secondly, companies concentrated their efforts on a constant search for opportunities for the placement of investments in highly liquid assets, either to exploit immediate gains in terms of financial value or simply to preserve the real value of their holdings.

This context and the predominant strategies strongly conditioned the type of skill developed in the financial administration areas of companies, and ARCOR was no exception. In addition, because of the type of market to which most of its output was directed, its treasury was almost entirely liquid, increasing the need and opportunity for very short-term investments. To provide a more efficient response to this situation, in 1987 an area specifically responsible for Finance began to be formed, staffed by finance professionals.

The strengths and weaknesses of ARCOR in this field in the early 90s included the hiring of an overall Finance Coordinator at Group level, with a strong professional profile and considerable experience in business conglomerates of large size by local standards. The main purpose was the development of a unified management in the financial area. Considerable progress had been made with these objectives through the setting up of a financial information and operations center and the developing of a system of centralized handling of group finances, which enabled a better use of investment opportunities. The results of this administration were strengthened by the definition of financial objectives and policies for the term of one year.

This latter feature was an indication of the weakness of the firm's ability to match its process of growth with an adequate long-term strategy. To this substantial shortfall could also be added certain failings in the administration of the area, such as the lack of information mechanisms and internal supervision and weaknesses in communications systems and computer technology. In particular, the company did not have on-line financial information for all the group's units, which weakened the effectiveness of decisions regarding the application of funds.

In spite of these internal organizational and functional weaknesses, ARCOR's financial situation during most of the 80s was relatively sound, and debt remained at levels that were not significant until 1988. Nevertheless, the commitments assumed because of strong expansion—fundamentally through the development of projects in industrial promotion regions—and the sharp fall in sales in the severe recession of 1989, precipitated a liquidity crisis. This crisis peaked in December 1989, when the financial debt/net worth ratio reached 1.3, seriously compromising its development.

It is interesting to note that in a domestic context in which a recession predominated, with weak demand, lack of long-term financing and high volatility in relative prices, (and therefore a time when companies adopted strategies to strengthen their financial position), ARCOR took decisions regarding the expansion of its productive capacity that ran counter to the traditional business practices of the period. In this context the results of the strategy—an apparently excessive company structure—appeared as a weakness. The first response by the company was to place its indebtedness ratio on a sound footing, disposing of certain assets not directly related to its principal business—mainly land and agricultural establishments. Proceeds from these sales and the fact that the banks with which the company operated never cut off their credit lines made it easy for ARCOR to find a way out of the crisis situation.

In any event the main factor explaining the reversal in the company's situation and its full return to financial health was the abrupt change in market conditions and recovery in domestic demand as from the success of the Convertibility Plan in stabilizing the economy. In effect, a position that in a period of recession and volatility appeared as a heavy burden for the company, hindering its development, was transformed into one of its main attributes and advantages enabling it to take advantage of a new growth phase. The recovery of the domestic market and a sharp rise in consumption beginning in the second quarter of 1991 found ARCOR with sufficient and efficient productive capacity that allowed for a rapid increase in sales with a clearly defined strategy to position it as a leader in many different segments. Significant increases in production enabled absorption of fixed costs, so that the higher sales income that was generated restored the company's liquidity.

### **Financial Strategy in the 90s**

The evolution of the financial position and strategy of ARCOR in the 90s shows two distinct phases. During the first stage, which lasted up to approximately 1997, the debt was relatively low with a predominant strategy for the self-financing of investment projects or, particularly as from 1994, the taking

of loans from export credit agencies located in countries from which equipment was supplied. During this phase the financial debt/net worth ratio was 0.145 and 0.115 in December 1995 and 1996, respectively. During a second stage, however, investments for the development of new plants or the acquisition of other companies, whether in Argentina or abroad, tended to be financed with an increased proportion of borrowing from the private banking system. Here the debt/net worth ratio rose to 0.528 and 0.461 at the end of 1998 and 1999, respectively.

## ARCOR – Consolidated Investments

*Period 1992-99 (in millions of pesos)*

Year	Investments
1992	58
1993	101
1994	72
1995	61
1996	77
1997	200
1998	230
1999	107
<b>Total 92-99</b>	<b>906</b>

## Acquisitions and plants

*Major acquisitions*

1993	Águila – Argentina
1997	Lia – Argentina
1997	Koppol – Brazil
1998	Dos en Uno – Chile
1998	Van Dam – Uruguay

*Latest plants built*

1994	Chocolates - Colonia Caroya, CBA. Arg.
1995	Crackers and cookies - Salto, Bs. As. Arg.
1996	Candy - Chancay, Peru
1997	Corrugated cardboard - Luján, Bs. As. Arg.
1999	Chocolates - Bragança, Sao Paulo, Brazil



From an internal aspect, the reorganization and increased level of professional skills in a finance area that was to be centralized at group level became a priority if operations were to be carried out efficiently and at the same time ensure longer term financial planning capability. The hiring of skilled professionals for the sector from outside the company and the increased importance assigned to the area within the company through its links to strategic planning, made it possible to overcome the existing limitations. In any event, the emphasis placed on self-financing decisions and strategy, in addition to being an obvious sign of the availability of liquidity, should also be seen as a product of the company's traumatic experience during the hyperinflationary crisis.

During 1991 and 1992 there was a steady reduction in the level of the company's liabilities, with the use of economic results to finance the investments made and working capital increases needed to support the growth in the company's level of activity. Although not abandoning its priority strategy for self-financing, ARCOR began to negotiate with domestic and international financial institutions to obtain long-term credit lines to finance its future investments. In general, the good performance of the Argentine economy in that period and the fairly widespread optimism among analysts regarding the prospects for growth meant that local companies were again considered creditworthy.

The situation at the end of the decade saw ARCOR without any major financial problems, although limited by a bank debt maturing in eighteen months on average. In this context, the main problem was the combination of simultaneous cycles of stagnation in Argentina as well as in Brazil and Chile, which were of course its main markets. Shrinking levels of consumption in these markets meant that the effective return on investments and the positions developed in recent years was lower than expected, affecting the overall profitability of the company and the levels of available liquidity.

Two separate tension factors can be determined within this scenario affecting the prospects opening up for the company's development, one a reflection of the particular nature of ARCOR and another originating in the specific environment in which it carries out its business. The former consisted of two elements: on the one hand, the firm faced the need to rationalize its asset structure, stressing its specialization in those areas making up its *core business*. This meant a careful evaluation of relative contribution margins and the sale of some facilities that were justified as part of a vertical integration process, but which were not strategic in the current global context. Another required giving consideration to strengthening and consolidating the interests

and objectives of the principal shareholders to ensure that demands for dividend distribution did not weaken the process of reinvestment in the business.

The second source of tension was provided by the economic and institutional context in which ARCOR was active, which implied conditions that were very different from those affecting the principal *global players* in the sector. In effect, the assigning of priority to a self-financing strategy to a large extent responds to the differences that existed in their respective capital and financial markets. In the case of a company such as ARCOR these have meant higher financing costs (as a result of the country-risk premium) and strong limitations on capitalization and the possibility of obtaining funds on stock markets, compared to the situation facing international manufacturers. It is interesting to note that whereas debt to capital ratios are quite similar to those of its global competitors, the self-financing ratio is much greater and the “income / interest paid” indicator is substantially lower. In this case, the challenge for ARCOR was to develop its participation on international stock markets.

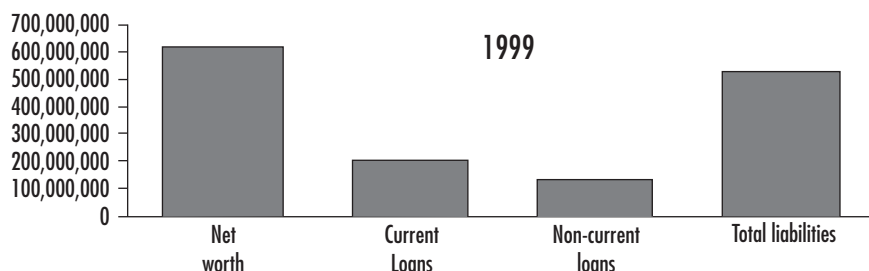
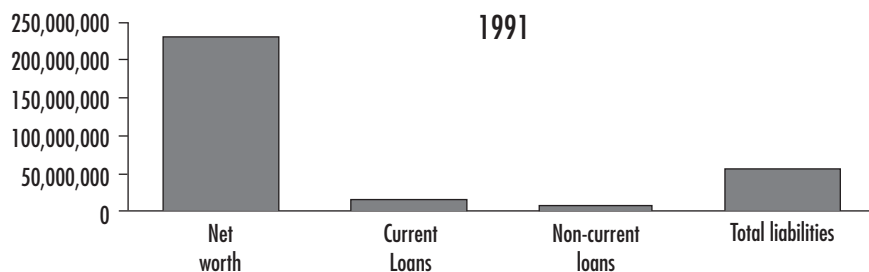
### Comparison of financial indicators for ARCOR and its principal competitors/benchmarks at world level

	ARCOR	Cadbury	Hershey	Nabisco	Nestlé	Philip Morris	Warner Lambert	Campbell Soup
FS used (year)	1999	1998	1999	1999	1999	1999	1998	1999
Current ratio	1.43	0.97	1.80	1.01	1.22	1.16	1.27	0.41
Quick ratio	0.74	0.73	0.66	0.47	0.86	0.52	0.71	0.22
Cash ratio	0.09	0.30	0.17	0.13	0.30	0.28	0.28	0.04
Operating cash flow ratio	0.12	0.39	0.45	1.41	0.37	0.63	0.61	0.30
Liabilities-to-equity ratio	0.85	1.33	2.05	2.78	1.38	3.01	1.56	22.50
Debt-to-equity ratio	0.55	0.56	0.99	1.50	0.92	1.10	0.42	16.29
Debt-to-capital ratio	0.35	0.36	0.50	0.60	0.48	0.52	0.30	0.94
Interest coverage (earnings)	3.20	10.44	10.82	43.06	8.05	16.97	—	7.34
Interest coverage (cash)	—	7.57	8.04	10.04	—	14.51	—	—
% of Current over Total Liabilities	73%	46%	32%	23%	66%	39%	57%	60%

Source: FS for ARCOR, FS for other companies, Analysis Booz Allen & Hamilton

### Financial data - 1990s

Date	Net worth	Current Loans	Non-current loans	Total loans	Total liabilities
31/12/1991	229.765.703	15.697.611	6.833.846	22.531.457	55.957.351
31/12/1992	291.204.959	20.958.970	4.127.738	25.086.708	100.529.783
31/12/1993	347.922.346	35.894.120	4.143.284	40.037.404	121.005.030
31/12/1994	334.760.056	49.809.726	26.220.710	76.030.436	183.271.411
31/12/1995	502.131.343	68.842.720	35.879.627	104.722.347	210.296.616
31/12/1996	552.337.163	54.664.027	29.114.539	83.778.566	212.166.463
31/12/1997	597.411.264	62.491.300	88.916.087	151.407.387	289.389.316
31/12/1998	617.825.715	172.279.221	190.853.171	363.132.392	541.810.074
31/12/1999	617.356.787	203.870.484	133.447.985	337.318.469	524.627.181



## INVOLVEMENT IN FOREIGN MARKETS. EXPORTS AND INTERNATIONAL PRODUCTION

Since its first exports to the United States at the end of the 60s, ARCOR has been developing a steadily increasing presence in international markets, a trend that accelerated in the 90s. This performance was a reflection of a corporate decision to preserve its positions in markets that had already been opened up, regardless of the changes in circumstances and fluctuations in terms of trade. This early definition of a clear exporting strategy was a decisive element in the company's long-term evolution. Recently this strategy has been consolidated through the developing of an extensive network of commercial offices and distribution channels, as well as through a process of international production through direct investment abroad. Currently ARCOR operates six industrial plants abroad (two in Brazil, three in Chile and one in Peru) and six commercial offices in various countries in Latin America in addition to sales units in the USA and Canada.

A pioneering experience in 1968 involved the U.S. market, in an attempt to test the company's competitive abilities in a relatively sophisticated market, searching for a catalyst for the quality and productivity improvements that were necessary. From there on export sales rose steadily, with the nineties in

particular being noted for very significant increases in the values of exports, penetration of new markets, consolidation of products with a global capability and the development of specific export strategies. Export sales reached a peak in 2000, when they totaled US\$ 217.8 million, 18.8% of the company's total sales. Investments currently being carried out with the specific purpose of increasing shipments in coming years will ensure that exports will play an even more important role in the overall performance of the company.

This performance has led to ARCOR becoming the leading confectionery exporter in the Mercosur and the largest exporter of confectionery in Brazil. It currently sells to 105 countries, with a notably strong presence in the Mercosur and the United States, a significant share of the market in Israel, a growing penetration in Asian markets —especially China, where the company is present in more than forty cities— and in Africa. Most export sales are made from its plants in Argentina, although there is a growing participation by its branches in Chile and Brazil as from 1997, currently accounting for 24% of total exports. This trend is a result of the process of expansion of these branches and the strategy for the efficient organization of the international productive capacity of the group. Confectionery and chocolate figure predominantly in the *mix* of exported products.

As part of its exporting strategy, ARCOR has in recent years established agreements with other companies to develop products on their behalf, notable cases being the supply of the U.S. Wal Mart chain and French Carrefour outlets. At present a strategic alliance is about to be concluded with a leading U.S. confectionery manufacturer that has decided to limit part of its production capacity and supply itself to a significant extent through ARCOR. In addition, several production lines have been expanded to be able to meet foreign demand. This expansion has included work on the Arroyito plant —doubling milk candy output to satisfy the rising demand from China, South Africa, India and Mexico— and the process of investment and restructuring derived from the need to attend to the new requirements in the U.S.. These trends represent the consolidation of a growing share of non-Mercosur sales in the company's export business.

The company's strategy for achieving a greater presence on international markets has been complemented and reinforced by the decision taken to substantially increase productive capacity outside Argentina. The development by ARCOR of a multinational manufacturing and sales network is playing a key role in the outlook for improved penetration of foreign markets with its brands and differentiated products, which enable an improvement in the

profitability margin of the export business. In the period 1994-1999 intra-firm exports represented almost two thirds of its total foreign sales and in 2000 accounted for 72% of its exports.

The building of a multinational corporation has been one of the most relevant aspects of ARCOR's history, particularly in recent years. The process began in 1976 with the opening of a branch in Paraguay (ARCORPAR) and continued in Uruguay with the acquisition of 50% of the capital stock of Van Dam SA in 1979. Subsequently, international development was extended into the Brazilian market with the take-over in 1981 of Nechar Alimentos (now ARCOR do Brasil). In the 1990s the company's presence in Brazil was significantly strengthened with the building of a modern chocolate factory at Bragança Paulista. In addition the company acquired Chilean business Dos en Uno, the leader in confectionery and chocolate in that country, with a production pattern very similar to ARCOR's. This latter acquisition helped the group to consolidate its presence in Chile —dating back to 1989 and based on the operation of three manufacturing plants— as well as in several other Latin American countries through the investments that had already been made by the Chilean firm. The production network was completed with the plant at Chancay in Peru, a *greenfield* investment inaugurated in 1996.

This intensive international expansion by ARCOR in the last decade has been a key component of the company's process of modernization and restructuring within a relatively novel context of open markets and competition with leading multinational corporations. Competitiveness gains required taking full advantage of economies of scale, and the opening up of new markets made it possible to fully overcome limitations in the size and dynamism of the domestic market. At the same time, the international deployment of productive capacity has facilitated access and penetration to certain markets of high strategic importance which otherwise could not have been served. It should be noted that this aspect not only concerns growth in physical volumes of exportable offer, as it also acquires an absolutely determinant qualitative dimension in so far as it also supposes a product *upgrading* process.

The increased facility for the sale of its brand products and goods with increased market value provided by a productive presence in certain markets in effect helps to overcome the problems caused by excessive specialization in the trade of so-called *commodities*. Closeness to the various segments of demand, complementing of production with marketing, the providing of services together with product sales, the development of regional sales and distribution networks, adaptation to domestic cultural factors, the possibility of

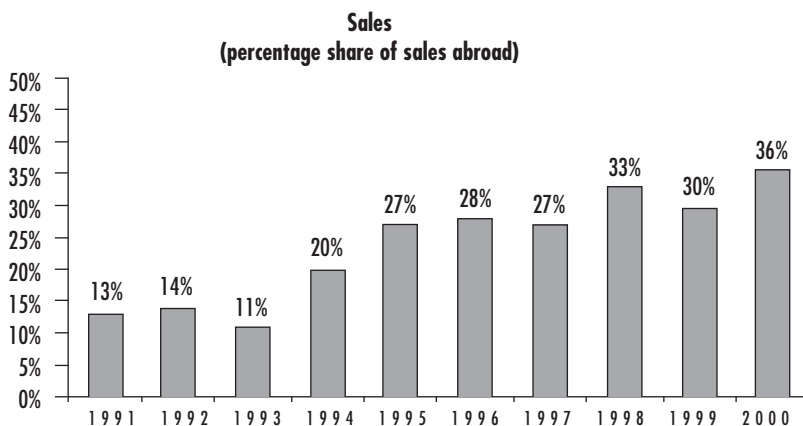
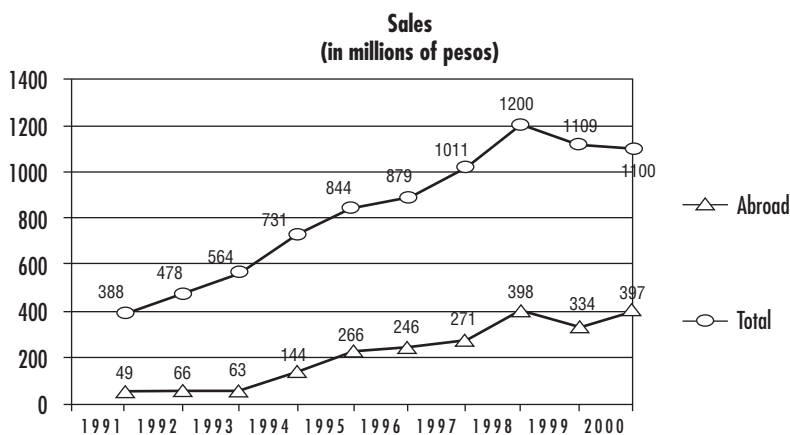
avoiding tariff and non-tariff barriers in the various markets and the purchase of companies with recognized brands and distribution channels are all attributes that promote greater and better commercial penetration from outside the market by differentiated products with a high added value.

Progress along the path to an international presence by an Argentine company is often hindered by the difficulties and limitations of its own overall development context. Financing of any such investment process suffers from the narrowness of the domestic capital market and the instability and size of the country risk premium, which generally obliges companies to commit higher volumes of their own capital and liquidity. Furthermore, macroeconomic contexts and demand cycles in Latin American countries are affected by highly unpredictable fluctuations that affect the anticipated return on investment, with very negative consequences on the handling of flows of indebtedness. At the same time, human resources are a basic element in any international expansion process, and it is not easy to harmonize the availability of personnel from Argentina and the peculiarities of domestic cultural values.

As a result, ARCOR's strategy for international expansion, based on the main objectives of strengthening its leadership in MERCOSUR, becoming a leading manufacturer of confectionery and chocolate in the Latin American region as a whole and achieving a greater share of the market in areas outside MERCOSUR, requires the strengthening of the overall organization, continuous analysis of its patterns of specialization and a steady increase in efficiency.

### **Share of Total Sales Accounted for by Sales Made Abroad (in millions of dollars)**

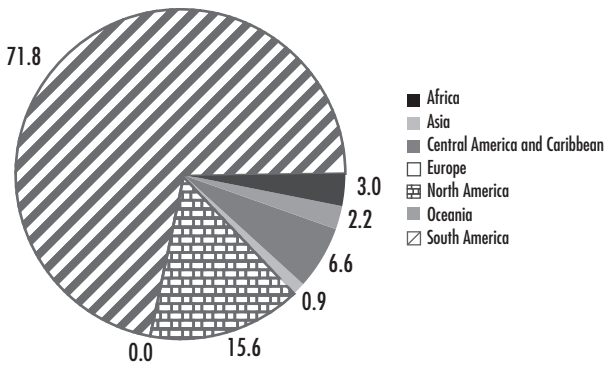
Year	In Argentina	Abroad	TOTAL
1991	339	49	388
1992	412	66	478
1993	501	63	564
1994	587	144	731
1995	618	226	844
1996	633	246	879
1997	740	271	1.011
1998	802	398	1.200
1999	775	334	1.109
2000	703	397	1.100



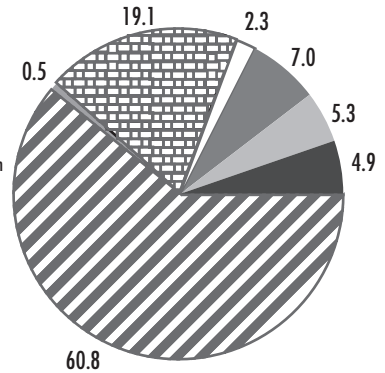
### Exports by Destination 1994-2000 (in thousands of dollars)

Destination	1994	1995	1996	1997	1998	1999	2000
Africa	3,021.0	3,275.1	3,471.7	5,844.7	4,863.6	4,340.3	10,768
Asia	2,225.1	5,878.5	4,676.7	8,803.1	7,942.8	14,417.1	11,590
Central America and Caribbean	6,779.2	3,669.6	2,665.5	4,723.8	13,207.3	16,572.3	15,199
Europe	883.2	702.9	979.2	1,124.5	1,452.9	2,300.7	5,024
North America	15,901.2	16,849.8	16,064.0	14,470.5	21,323.6	20,688.6	41,608
Oceania	36.0	43.4	73.8	273.3	246.8	687.8	1,162
South America	73,404.3	120,185.7	130,302.6	134,750.5	187,670.0	141,022.6	132,403
<b>TOTAL</b>	<b>102,250.0</b>	<b>150,635.0</b>	<b>158,224.5</b>	<b>169,990.4</b>	<b>236,713.9</b>	<b>200,029.4</b>	<b>217,754</b>

**Total exports by destination  
1994**



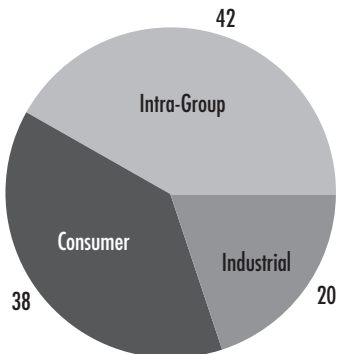
**Total exports by destination  
2000**



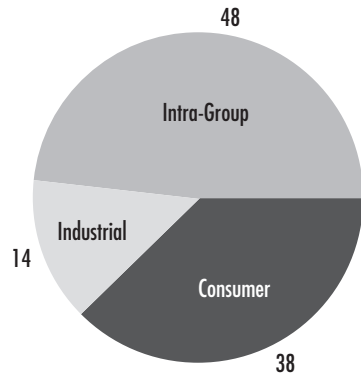
### Exports of Industrial and Consumer Products by Production Units 1994-2000 (in thousands of dollars)

Year	Consumer	Industrial	Total third party	Intra-group	Total
1994	39,295.0	20,260.0	59,555.0	42,695.0	102,250.0
1995	37,427.0	36,064.0	73,490.0	77,145.0	150,635.0
1996	31,668.2	28,572.7	60,240.9	97,983.6	158,224.5
1997	47,748.2	36,834.4	84,582.6	85,407.8	169,990.4
1998	80,043.5	33,087.7	113,131.2	123,582.7	236,713.9
1999	78,171.6	30,811.7	108,983.3	91,046.1	200,029.4
2000	83,595.0	31,506.0	115,101.0	102,653.0	217,754.0

**Total exports by customer  
1994**



**Total exports by customer  
2000**

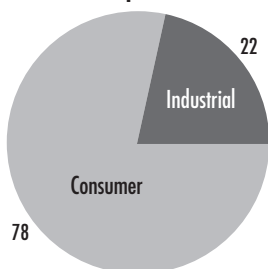




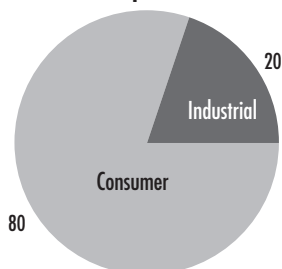
## Exports of Industrial and Consumer Products by Production Unit 1994-2000 (in thousands of dollars)

Year	Industrial	Consumer products							Total
		ARCOR	Lia	Styrene	Versalles	Brazil	Chile	Branches	
1994	22,847.0	52,542.0	0.0	0.0	0.0	26,861.0	0.0	0.0	102,250.0
1995	39,587.0	88,106.0	0.0	0.0	0.0	22,942.0	0.0	0.0	150,635.0
1996	41,184.2	98,504.3	0.0	0.0	0.0	17,994.0	0.0	542.0	158,224.5
1997	45,164.6	98,064.1	8,960.1	0.0	339.3	16,649.0	0.0	813.3	169,990.4
1998	46,939.8	128,115.8	8,830.2	17,746.1	499.9	13,769.3	22,921.3	894.4	236,713.9
1999	42,557.0	90,650.4	5,804.2	17,388.6	145.6	17,234.5	25,420.2	828.7	200,029.4
2000	42,876.0	93,146.0	4,784.0	28,780.0	19.0	23,475.0	23,021.0	1,653.0	217,754.0

Total exports 1994



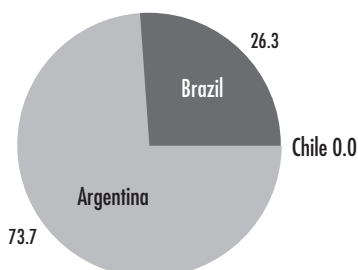
Total exports 2000



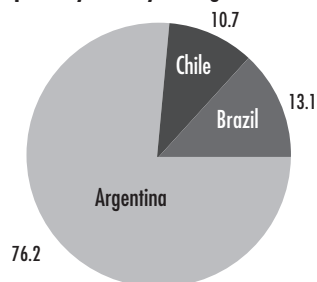
## Exports by Country of Origin and Type of Product 1994-2000 (in thousands of dollars)

Year	Argentina			Brazil			Chile	Other countries	Total
	Industrial	Consumer	Total	Industrial	Consumer	Total			
1994	28,847.0	52,542.0	75,389.0	0	26,861.0	26,861.0	0.0	0.0	102,250.0
1995	39,587.0	88,106.0	127,693.0	0	22,942.0	22,942.0	0.0	0.0	150,635.0
1996	41,184.2	98,504.3	139,688.5	0	17,994.0	17,994.0	0.0	542.0	158,224.5
1997	45,137.1	107,363.5	152,500.6	27.5	16,649.0	16,676.5	0.0	813.3	169,990.4
1998	43,805.3	155,192.1	198,997.4	131.5	13,769.3	13,900.8	22,921.3	894.4	236,713.9
1999	39,912.0	113,988.9	153,900.9	2,645.1	17,234.5	19,879.6	25,420.2	828.7	200,029.4
2000	38,029.0	126,729.0	164,758.0	4,847.0	23,475.0	28,322.0	23,021.0	1,653.0	217,754.0

Total exports by country of origin 1994



Total exports by country of origin 2000



## ACTION IN THE COMMUNITY

The ARCOR Foundation was created in 1991 and is active in four main areas: **economic research, education, health and culture**, as a matter of preference acting where possible in the population segment aged between 0 and 17, on matters relating to nutrition, growth and development. Its activities have been carried out on the basis of **programs** defined according to these guidelines established for the interests of the institution and the social demands received by or perceived by the Foundation. The programs operate by providing **funds for financing**, allocated and paid out according to a combination of methodologies: a) through project competition in the framework of an explicitly defined basis, and b) through the submitting of projects for consideration.

Both procedures involve an exhaustive analysis and objective evaluation of the initiatives submitted. The principal criteria for the selection of projects are based on ensuring the greatest social benefit is obtained from the resources allocated, promoting concepts of efficient administration among those carrying out not-for-profit activities, assigning priority to projects showing potential for replication, self-supporting capabilities and the possibility of multiplying benefits, and supporting initiatives that propose to achieve tangible, measurable results.

To obtain maximum benefit from its activities in this area and increase scope and efficiency, the ARCOR Foundation has promoted and entered into various strategic alliances with other important entities of a similar type. It also forms part and leads a Group of Foundations (GDF) designed to assist in continuously improving the performance of donor foundations through the sharing of ideas and experiences. The GDF is guided by three basic objectives: to be a qualified source of reference for other existing or new foundations as well as for the targets of assistance, offering systematized services that can be communicated among potentially interested candidates and increasing the number of participating entities.

### Areas and Programs

#### *Economic Research*

To encourage research by Argentine economists into different aspects of the economic reality of the country, the Foundation grants its “Fulvio Salvador Pagani” Award annually. The competition requires the presentation of papers on a set topic, the winner being determined by a jury of experts. These topics are usually based on the ARCOR Group’s vision of the priorities and princi-

pal challenges facing the Nation, and candidates should base their research on the Argentine situation.

In recent years the topics that have been developed during the competition have been as follows: “Fiscal Federalism” (1996), “The role of education and training in growth” (1997), “Economic analysis of prevention and treatment in healthcare” (1998), “Economic analysis of crime prevention and control” (1999) and “Productivity and competitiveness for Argentina’s insertion in the global economy” (2000). Given the relevance of the topics and the growing prestige of the competition, interest by researchers is considerable, as can be seen from the large number of submission received each year. Winning papers are provided with a monetary prize, a trophy and the publication of the work.

### *Education*

In this area the Foundation runs various programs aimed at encouraging activities for well-rounded education of children and young persons at various levels. Through training for the formulation of projects, **annual competitions** are developed with participation by primary schools and disabled infant and adolescent care centers. To promote greater environmental awareness in new generations, various different initiatives in this regard have been sponsored.

#### **“My School Grows” Program**

The system defined for this program is based on the existence of a Fund for the Financing of Projects directed at primary school establishments that submit proposals for the setting up or expansion of educational school workshops to improve teaching and learning potential. All educational establishments in the country can take part, doing so by means of a Project Competition, following a call for candidates made in a different region each year.

Once the competition has been announced, special workshops are held to assist potential beneficiaries with project preparation techniques. When the projects have been selected on the basis of feasibility and impact, an agreement is signed with the beneficiary school, which will be responsible for executing the project. The program contemplates monitoring visits by the Foundation to follow up on the project and offer technical advice for the carrying out of the initiatives. Lastly, once the project has been completed, communication of its achievements is arranged through the holding of meetings to exchange information and evaluate performance, with the publication of the results and teachings that were developed.

Since its beginnings in 1996 and including the competition organized in 1999, the program has selected and financed a total of 68 projects at the same number of schools, with the allocation of Foundation resources for a total of approximately \$175,000. It should be noted that beneficiary schools and communities have provided their own resources to match this amount. Carrying out these initiatives involves a growing number of school-age children every year, with beneficiaries to date totaling a school population of 21,000 children between 6 and 13 years of age. As a working strategy, assurance of nation-wide coverage has been proposed so three provinces are chosen every year, with a total of 17 having been covered by 2000.

The projects selected cover a very wide range of improvements for the educational community, including computer equipment, job training, organic market gardens and animal breeding, theater workshops, handicraft manufacture and the setting up of sports clubs, among others. In general terms, all these initiatives aim to resolve difficulties faced by schools in developing such actions, reflecting the needs of each individual location, and are intimately linked to the reality of the social situation in the community. Many of the projects are designed as a response by the public schooling system to the economic problems of families, and others have been noted for their positive results in keeping down school dropout and academic failures.

### **"Overcoming Limits" Program**

The main purpose of this program is to provide technical and financial assistance carrying out projects for the setting up or expansion of workshops for the social integration and job training of children and young people with special needs. The methodology is similar to that of the program described above and includes the establishing of a financing fund and the selection of initiatives by means of the holding of competitions.

Through the four competitions held between 1996 and 1999 the program financed a total of 94 projects for a similar number of institutions helping those with special educational requirements. Beneficiaries have included almost 3,900 children and young persons with some degree of disability of one kind or another (mental deficiency, Down syndrome, physical handicap, hearing or sight impairment) attending special schools run by the public system or non-government charitable entities.

In this instance the resources channeled by the Foundation during the period totaled \$240,000, while the respective counterparts contributed more than \$510,000. The projects selected and financed are located in rural or urban zones in nine provinces and coverage for the entire country is anticipated in the short term. They have involved a very wide range of initiatives, includ-

ing jam and canned goods production workshops, bakeries, welding, sewing, cooking, fruit processing and IT equipment. Lately efforts have been made to ensure that those carrying out manufacturing projects are also trained in business aspects.

### *Health*

On the grounds that prevention is one of the main components of an adequate health policy, the ARCOR Foundation supports and channels resources towards community initiatives in the field of education and prevention, nutritional guidance and the training of human resources for communities at risk.

#### Program for Healthcare and Prevention.

##### Support for Research and Publication of Scientific Knowledge

The purpose of this program is to encourage the development of activities concerning **healthcare, illness prevention and applied research**, specifically directed towards anticipating infant and child health problems, dealing with elements of social, family, recreation, sanitary and dietary containment.

One of the principal projects supported by this program is the CLACyD Study, a full-scale analysis of various aspects concerning the health/illness process in mothers and infants. This inter-disciplinary research arose at the initiative of a group of professionals at academic institutions and service providers, and has involved a long-term study of the profiles of nutrition, growth and development in the infant population in the city of Córdoba. The result of this research is published with the support of the Foundation at leading congresses and seminars, as well as in national and international publications.

Other long-term activities receiving financial support from the ARCOR Foundation include: i) assistance for local programs in relation to mother and infant health; ii) promotion of mother and infant health programs through the production of informative material and teaching aids and organization of a Documentation Center on breast feeding, nutrition, growth, development and reproductive health; iii) setting up of the Córdoba Breast Feeding Support Group with full-time training functions, advice to mothers, organization of a network of community promoters and participation on courses and congresses; iv) assistance for the “Integral health of adolescents” research and action project to define and combat risks to health among this age group.

#### Program for Community Support

By means of the donation of products, the Foundation supports a significant number of institutions carrying out actions in the fields of nutritional assis-

tance, recreation, training and prevention in relation to infant health, directly benefiting families with limited resources located mainly in the central and northern regions of the country. This activity is complemented by the financial support provided to not-for-profit organizations for the printing of information materials and organization of events linked to healthcare and health promotion.

### *Culture*

In this area the Foundation provides its support to the work of institutions and organizations that promote excellence in cultural events, with particular emphasis on proposals involving children, adolescents and young people.

#### **Program for the Support of Cultural Events**

This program encourages cultural manifestations that include active participation by children and young persons. Initiatives that have been supported are noted for promoting the setting up, expansion or improvement of cultural workshops, as well as involving the organization and holding of events and support for artistic expression in various forms. Support has included contributions for advertising projects, obtaining of the necessary equipment and the development of training activities.

#### **Program of Cultural Activities for Families of Company Personnel**

The Foundation organizes a Drawing and Literature Competition as a means of promoting integration between the ARCOR group of companies and the families of their personnel, at the same time as developing creativity and interest in such artistic expression. Annually over 4000 children and young people in Argentina, Brazil, Chile, Peru, Paraguay and Uruguay participate with drawings and poems on subjects set when launching the competition.

### *Alliances – Cooperating Funds*

The steady and systematic development of activities by the ARCOR Foundation has led to the forming of several strategic alliances with other important donor institutions, carrying out coordinated collaborative actions and the exchange of learning experiences.

#### **Infancy and Development Program. Fundación ARCOR / Fundación Antorchas**

This program was set up to support projects aimed at improving care for infants, adolescents and young people in disadvantaged sectors of society,

seeking to promote innovation in the administration of policies, programs and projects with emphasis on preventive and educational aspects. These two foundations have contributed in equal amounts to a financing fund that makes contributions to projects distributed around various Argentine provinces. So far the projects being financed have reached 215 disadvantaged communities and almost 23,000 children and young people belonging to families of limited resources, a total of \$ 1,500,000 having been invested in the program, of which 45% was contributed by the two foundations.

#### **FEPIC Fund – Forming, Educating, Preventing and Integrating into the Community. Fundación ARCOR / Fundación Interamericana**

This fund was set up in 1996 to direct financial resources to projects concerned with nutritional health, children and young persons at risk, rural education and non-formal technical education. Funds are intended for use by non-government organizations and not-for-profit institutions working among the disadvantaged sectors of the population. Some 22 projects have been financed covering 222 communities and more than 15,000 young persons in Córdoba, Mendoza, Salta, Buenos Aires and Jujuy. The FEPIC has participated with 30% of the \$ 1,600,000 invested in these projects.

#### **Infancy and Rights Program. Fundación ARCOR / UNICEF Argentina**

This program plans for the setting up of a financing fund for a total amount of \$150,000 made up of equal contributions from the two sponsoring institutions. Its purpose is to select, finance, evaluate and communicate projects by non-government organizations working with groups of children and young persons whose rights are threatened or violated. It intends to protect development beginning with early infancy by means of ensuring appropriate child-raising practices by families and institutions.

## CHAPTER 4

# **Towards the “Fifth ARCOR”: a Global Enterprise from an Emerging Country. New Challenges for ARCOR. Suggestions for Future Research**

*Jorge Forteza*

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➤ Towards the “Fifth ARCOR”: A Global Enterprise from an Emerging Country. New Challenges for ARCOR. Suggestions for Future Research

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## **TOWARDS THE “FIFTH ARCOR”: A GLOBAL ENTERPRISE FROM AN EMERGING COUNTRY. NEW CHALLENGES FOR ARCOR. SUGGESTIONS FOR FUTURE RESEARCH**

This book has attempted to summarize fifty years in the history of a company that, from its beginnings in the interior of an emerging country, has experienced a process of steady growth in spite of major turbulence in its environment and has succeeded in becoming a leading business in the region and a relevant player in the global industry.

We believe that the ARCOR case is of particular interest for students of globalization processes and their impact on emerging countries. For over fifty years this organization has demonstrated the possibility of building a viable business model, competing first against large domestic firms and later against dominant multinationals. Which have been the recurring themes of this strategic trajectory? We believe the following points summarize the key dimensions that help in understanding the ARCOR case and provide insights of interest.

- *A strategic intent in constant evolution and “re-invention”*, that has made it possible to follow a “growth path”, beginning with accessible markets and growing steadily in geographical coverage and product range, but in general avoiding direct confrontation with the strongest competitors. In other words, an interesting application of the “indirect strategy” also analyzed by Lidell Hart (1954). This course, which has consisted of focusing on less contested markets or “sustainable niches” is also reflected in recent analysis on multinationals from emerging countries performed by Khanna, T. (1997), Goshal, S. (1999) and Dawar, N. (1999)
- *The ability to identify and take advantage of successive discontinuities in context or the industry*, evidenced at an early stage in the reaction to the development policies of the Frondizi government and on numerous subsequent occasions: benefiting from regional investment promotion structures to build a network of modern plants and taking advantage of the weakness of local competitors to make acquisitions. ARCOR was also able to take advantage of such processes to make purchases of businesses in neighboring countries, and capitalized on the deregulation process that took place in Argentina in the nineties to radically transform itself. The launch of MERCOSUR also provided a platform for extending its presence in the Brazilian market through exports and direct investment.
- *The ability to capitalize on strategic or operating weaknesses of multinational corporations*. ARCOR was able to identify several of the limitations suffered by multinationals and was equipped to wage an effective “surrounding action” against them. The company developed branded

products that were better positioned in the middle of the market; it found a way to create magic for its brands, set up efficient distribution channels and in general was able to design a policy for rapid development of products. Its light structure and entrepreneurial culture also provided it with speed of response and an exciting organizational environment that few of the multinationals with the limitations already analyzed by Gingrich, J. (1999) and Prahalad, C.K. (1998) could offer.

- *Continued emphasis on the development of technical and functional capabilities and continuous learning.* Since its beginnings in Arroyito, when the founders designed and manufactured their own machines, down to the modern plants of today, ARCOR's culture has included a strong technical bias, with the development and adaptation of capital goods and productive processes. This tradition, considered to be a true resource in studies by Collis and Montgomery (1997) and Peteraf (1993), has allowed the company to maintain a high level of innovation. Even today, although ARCOR has become integrated to world equipment markets, its excellence in terms of processes has meant its costs are highly competitive.
- *A culture and organizational model that have adequately combined leadership and control by family shareholders and a growing professionalism and the attraction of quality human resources from Argentina and subsequently from abroad.* We have seen that ARCOR is the product of the creativity of a few partners with very uniform culture and values. This point of departure was centered around the personal leadership of Fulvio Pagani during the first forty years of the company's life. Nevertheless, during traumatic periods in the nineties the shareholders demonstrated their vitality by carrying out a successful transition and a process of reorganization that resulted in an accelerated evolution in the quality of management. ARCOR has become an attractive place to work for Argentines, and is in the process of developing capabilities to reinforce its management teams with talent from Brazil, Chile and elsewhere.

Lastly, there is another distinctive aspect to this story: the continuity in the strategy followed by group of shareholders that suffered all the vicissitudes experienced by the country and yet continued to bet on investment, developing plants, exporting and opening up new markets. In a decade such as that of the 90s, during which time a significant sector of the Argentine business class decided that "the game was over" and sold their businesses, this group of shareholders persevered with a dedication worthy of detailed analysis.

Now, in the early days of a new decade, the question for industry analysts and students of economics must be: How does the story continue? Are we seeing the ARCOR case at its zenith, prior to a slide into decline, or are we truly at the threshold of the building of the “Fifth ARCOR”, a global food company that will continue to do battle with the giants in the sector?

Obviously this question cannot yet be answered, but in this chapter we would like to contribute with some thoughts that can help us in imagining the possible evolution of the ARCOR case. We propose to begin this analysis with a vision of what the “Fifth ARCOR”, a global food industry company, could look like by the middle of the decade.

*We Imagine this “Fifth ARCOR” as Follows:*

- ... A global food industry company with sales of over US\$2 billion ...
- ... a leader in the Mercosur, where it makes half its sales,
- ... but which is also a “local player” with distribution and production capability in key emerging countries such as Mexico and China, and in developed markets such as the United States.
- A strong contributor to Argentina’s development as an exporter: ARCOR leads a group of exporters in foodstuffs and related products and services that generates exports for the country nearing US\$ 1 billion.
- ARCOR continues to be a strong innovator, having also developed an excellent capability for the forming of strategic alliances, which it has used to launch initiatives such as the development of new categories of products in MERCOSUR, the entry with branded products into the U.S. market and the developing of joint ventures in India and China.
- ARCOR has continued migrating towards the construction of a global company, but has managed to avoid much of the rigidity of its oldest competitors. It has in effect built a “confederation of production and management units” that are interrelated. Buenos Aires is not the headquarters, just one of four management centers together with Sao Paulo, Miami and Shanghai. At the same time ARCOR has made progress towards the construction of a global culture: the Chairman of the Board is Argentine, but several senior managers are Brazilians, Chileans and U.S. citizens.

This is no doubt an inspiring vision, that will make it possible to say in ten years’ time that “ARCOR has re-invented itself once again”. However, it should be noted that in this new stage in its development ARCOR will have

to face a series of changes in its environment that will create growing challenges for the Group: in the food industry the process of concentration will accelerate as companies search for scale and world-wide presence. In these conditions players of intermediate size based in emerging countries such as ARCOR will face intensified competition. We should also consider that all the limitations affecting multinationals that have been identified in economic texts will gradually be corrected. Multinational companies are immersed in institutional transformation processes intended to make them more agile and innovative, developing their learning capacity (see Forteza and Neilson [1999], Arnold, D. [2000] and Birkinshaw, J. [2001]).

The great frontier in theoretical and practical analysis in coming years will be the determination as to which are the categories of global, regional or local products, and thus how mid-size players such as ARCOR will be able to build geographical portfolios of products and positions that will be viable in the face of pressure from multinationals. ARCOR's experience would seem to indicate some promising currents for analysis with regard to "defensible" segments.:

- Categories of branded products aimed at consumers in the mid to low income segments offer positions that are hard for multinationals to gain access to.
- Some geographical markets, such as mid-size or small countries, which the multinationals consider of limited strategic importance, offer a promising basis for the shareholder value creation for dominant players.
- Some segments of world export markets where the brand is not a key aspect, but where alliances are to supply private brands or to gain access to distribution channels.

This analysis is interesting because it will offer a perspective on how players such as ARCOR develop strategic portfolios that combine dominance in their natural market and certain minor markets with incursions into defensible segments on world markets, and the few "major bets" that could be placed on large country markets such as Brazil's, or in global segments dominated by multinational brands.

ARCOR is a company with a strong presence in the whole of South America, but its center of gravity is still strongly based in Argentina, Brazil and Chile. Following the years of accelerated growth in the nineties, Argentina seems to be facing a less dynamic horizon, and will probably not be a market offering major growth opportunities. The great challenge for ARCOR will be

Brazil, a major emerging nation which does appear to offer reasonable prospects for growth, although increased attention from multinationals and some local companies will make it challenging to build a significant position.

Another fundamental aspect to be considered will be how to finance this growth. If we accept the premise that ARCOR should at least double its size in the next few years to maintain its independence, it calls for an analysis of the capital structure required to fund this growth. The shareholding families have time and time again shown their commitment to the project for the enterprise, but it would be reasonable to suppose that their investment capacity has limits. Looking forward, ARCOR should follow a path of strategic alliances and increasing openness to capital markets to be able to pursue its development process.

Lastly, regardless of the will of the shareholders, what defines the future of a company is its attractiveness to talent, which no longer will be just Argentine but also Brazilian, Chilean, U.S. and why not, Chinese... The evolution of a management and governance model and the development of a global culture that is friendly and welcoming to citizens from widely differing cultures will be one of the challenges for the leaders of the company.

The nature and magnitude of the challenges faced by ARCOR could at first glance seem overwhelming. However, we have seen in this book how in similar situations ARCOR has repeatedly been able to “re-invent” itself and managed to protect its independence, progressing to a new stage in its development.

We would like to propose to readers and analysts a “strategic agenda” for the establishing of the “Fifth ARCOR”, encouraging further study of the company’s development in coming years. In our opinion this agenda will be built around four major themes:

- Consolidation of a leadership position in South America and particularly in the Southern Cone.
- Building up positions in major world markets and the development of new “games”.
- Moving from a management model centered on Argentina to a global model.
- Developing of a culture that is attractive to talents from all around the world.

Let us consider some of the key issues in each of the four strategic dimensions indicated.

### **Consolidation of a Leadership Position in South America and Particularly in the Southern Cone**

ARCOR is currently the dominant player in several categories in Argentina and Chile. In Argentina over the last decade various multinational companies have invested heavily, mostly with disappointing results. These disappointments have had as their cause the market recession and difficulties encountered in competing with companies such as ARCOR. Multinationals have undergone a learning experience that will make them tougher competitors in future, which implies that it will be necessary for ARCOR to make a significant effort to maintain its position in existing categories at the same time as being strongly innovative, introducing novelties onto the Argentine market either before or shortly after the multinationals do so.

However, the key battle is to be fought in Brazil. That country is one of the world's five largest emerging markets and is a privileged focus for multinational investment (see Gartner, J. [1997], Kennedy, P. [1996] and OECA [1997]). In coming years Brazil will be transformed into one of the world's most competitive markets, with all the multinationals including it in their world-wide expansion programs; local firms will try to defend certain viable market segments and it will be essential for ARCOR to build up a sustainable position in this market. It should be noted that ARCOR will not be starting from scratch, as it has a significant presence in sales and production, but its presence will probably need to make a quantum leap through an acquisition or a strategic alliance in order to consolidate its position.

Another matter of considerable interest is ARCOR's potential for the building up of a privileged position in the Southern Cone through increasing integration of its presence in Argentina, Brazil and Chile, building up a true "manufacturing and sales network" with specialized plants and a regional vision. This will enable it to obtain a strong strategic position, in terms of costs and strategic flexibility based on its position in the three key Southern Cone countries.

### **Building Positions in Major World Markets and the Development of "New Plays" in these Markets**

In addition to the urgent need to build a dominant position in its "expanded domestic market" (the Southern Cone), the Global ARCOR must build up significant positions in other markets outside the region. This approach should be based around the major categories of countries in the world economy:

- The NAFTA bloc, and USA and Mexico in particular.

- Other large emerging countries, such as India, China, Indonesia, Turkey and other Asian countries.
- Developed countries in the European Union.
- Global export markets.

Each of these segments offers different opportunities and entry barriers, but it is probable that over the next few years ARCOR will need to make additional efforts to build up a position in NAFTA. It will need to do the same in certain emerging markets such as China, as well as developing certain global export initiatives such as those already taking place with confectionery and chocolate products.

It is very likely that several of these initiatives will require the forging of strategic alliances, and we believe that ARCOR will need to significantly reinforce its capacity and its corporate culture in order to stand out as the “best partner” for alliances.

These alliances could take many forms, including the following:

- Joint development of new categories in the Southern Cone with companies that have products and brands in the main countries.
- Development of its brands for major distribution chains,
- Agreements for specialization in the value chain whereby ARCOR carries out some activities and the partner some complementary activities.
- Alliances to enable entry into markets with high potential that are difficult to gain access to, such as India and China.

ARCOR has already built a promising experience in the area of alliances, and this will become a key skill for its development in the coming decade. In this regard, a good example of how alliances are effective vehicles for penetrating extremely competitive markets is the agreement recently concluded with Brach’s Confections Inc. Brach’s is a leading manufacturer and seller of high-quality candy in the North American market and its portfolio of products includes fruit snacks, chocolates and hard candy. Under this agreement, ARCOR will manufacture 30,000 tons of confectionery annually for Brach’s, increasing exports by an annual US\$ 40 million.

The synergies achieved by the two players are significant: Brach’s will considerably improve its cost structure compared to its U.S. competitors and ARCOR will achieve better use of its capacity and a major increase in its exports, with potential for a further rise in future.

Looking forward, the development of e-commerce capabilities will be essential for the strengthening of competitive positions in its markets and will become an effective vehicle for growth and projection internationally.



ARCOR will need to extend its innovative *business to business* (B2B) offerings that are already in progress, which in a first stage will enable:

- Improving customer attention and achieving their loyalty.
  - Permanent availability of information (current, historical)
  - Customized products and services (order acknowledgement, price quotes, shipping and follow-up)
  - Added value services
- Expanding of local and international scope to new customers.
  - New sales channel
  - Advertising support and promotion
  - Association programs
- Generating deeper awareness of customer needs through the sharing of information.
- Reducing times and costs for acquisitions, transactions and delivery to customers.

Steps taken in this direction will enable the inclusion of the value chains in which ARCOR participates as part of an “extended company”, establishing efficient links between suppliers, transformation processes and integrated customer supply management. Combination of e-commerce skills and strong delivery capabilities in research and development, production, distribution and sales and marketing will promote a more robust business model and the development of one of the most important business communities in the food industry in Latin America.

### **Moving from a Management Model Centered on Argentina to a Global Model**

ARCOR is today only a “prototype” of a global enterprise. Its organization and operation makes it more of a multinational company with its central headquarters in Buenos Aires. This model is still appropriate for its current stage of development, but in order to adequately manage a global company twice the size of the current business, ARCOR will have to evolve in various directions, and will need to face and resolve the classic dilemmas that confront multinational corporations: how to leverage capabilities across countries and at the same time maintain a local identity and the ability to anticipate and respond adequately to local competitive realities. Here it would be of interest to study how ARCOR will develop the key elements in its organizational model:

- Architecture of the organization (production units, sites, matrix or functional structure, autonomy and integration of country units, etc.).
- Production model (plant configuration, shared services and specialization)
- Management processes, such as planning, evaluation of results, incentives and career development.

In addition, ARCOR will no doubt have to reconsider the relative roles played by Buenos Aires and other key geographical centers such as Brazil and the United States to decide on the location of decision-making centers and their relationship to each other.

### **Development of a Culture that is Attractive to Talents from all Around the World**

Today ARCOR is an attractive organization for Argentine talent, and increasingly for human resources in neighboring countries such as Brazil and Chile. Its culture is still predominantly Argentine, and should probably evolve towards the creation of a “Southern Cone” culture that will continue to be its “base identity”. It should be mentioned that few multinationals possess a “global culture”, as they carry strong domestic cultural traits on which they later expand, as indicated by Doremus et al (1998).

As ARCOR grows it will be interesting to analyze the opportunities offered to non-Argentines for growth and development; it will be interesting to follow, for example, the increase in the number of key positions filled by non-Argentines over the coming years.

When opening up to capital markets, issues regarding ARCOR’s corporate governance will begin to gain in importance, such as the composition of its Board of Directors and its relationship to line management. This will be another innovation that ARCOR will no doubt have to carry out in the next few years.

To conclude, we would like to point out that ARCOR will no doubt continue to be an interesting subject for study in coming years, as it makes progress towards building a global enterprise, and we would like to encourage new generations of analysts to further pursue this study and apply it to other cases in emerging countries.

Analysis of the history and development potential of our companies, as well as being a highly satisfying professional exercise, is also a duty to our com-

munity. In developed nations names such as Peugeot, Mercedes Benz, Intel, Fiat, Telefónica and others are part of the heritage of their societies: citizens are proud of these companies and clearly understand their importance to the development of their respective countries. It is also for this reason that we hope this work will represent a small contribution towards increased awareness (and pride) of Argentines, Brazilians, Chileans, etc. of “national” companies such as ARCOR and the contribution they make to the development of the region.

## CHAPTER 5

# **Consolidating its Competitive Position (2001-2012) From Candy to Food Products, from Arroyito to the World 2001-2012 Update**

*Bernardo Kosacoff*

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➤ Introduction

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➤ Successful Adaptation to a new Business Environment in Argentina

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➤ The Rules of the Game Change: The Argentine Macroeconomy

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➤ Development of New Competitive Capabilities

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➤ A Place in The World

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➤ Final Comments

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## INTRODUCTION

The beginning of the new millennium has been characterized by the existence of fluctuations in the performance of the economy with a greater negative impact on the so-called emerging economies. The corporate agenda has changed completely, focusing on: short-term streamlining, the development of methods to restore credibility to the Corporate Management and Government, and adapting the business model to the new setting. Latin America was reached by this turmoil which converged with a macroeconomic performance in decline and sparked off severe institutional and financial crises in several countries. The new scenario posed strong challenges to all the companies operating in the region and especially to the local business groups. In Argentina particularly, many local groups had to undergo difficult and lengthy forced restructuring processes which often implied a change of shareholders with controlling interest.

However, this global scenario favorably changed during the years before the 2008 financial crisis when a noticeable dynamism of the international economy was appreciated. This dynamism included growth in, the activity, foreign trade and investments, and the spread of new production practices in the generation of goods and services, all of which had a highly favorable impact on the performance of the economy and welfare improvements. The growing participation of China and India has brought about a significant change in the global economy. In an international context of greater growth, this period has been very favorable for Latin America. The combination of the expansion of the activity level, the growing volume of exports, and improvement in the terms of exchange gave rise to the most distinctive feature of this period of economic growth: its coincidence with a current account surplus in the balance of payments (an unprecedented event in the economic history of the region). The governments took advantage of this new context to improve public accounts and macroeconomic consistency, to pay their debts, to accumulate international reserves, and to improve social conditions and poverty.

The 2008 financial crisis, which originated in the developed countries, was a turning point that strongly gave rise to uncertainties and changes of the expectations about the perspectives of economic performance. Still in an incomplete stage, the operation of the international economic organization and the sustainability of the development models have been reconsidered. Developing countries have not only evidenced their recovery process but also appear to be stronger than developed countries to face the growth and development process.

The ARCOR Case, which in the previous edition of this book had been studied till the year 2000 as an example of a company which managed to develop, grow and regionally integrate into emerging markets, faced crucial questions in this changing context, including aspects such as:

- How would the changes in the business environment affect ARCOR?
- Would it be able to successfully overcome the crisis in its core markets?
- How would it respond in terms of priorities, strategies and key decisions?
- Would its regional exposure and development towards a global company from Latin American markets be hindered?

We believe that these questions and the magnitude of the challenges posed deserve an update of the case for the 2001-2012 period, addressing the following issues:

1. Successful adaptation to the new business environment in Argentina.
2. The rules of the game change: Argentine macroeconomy.
3. Development of new competitive capabilities:
  - 3.1. Conceptual framework
  - 3.2. Value-added chain in the food industry
  - 3.3. Technological capabilities and operations management systems
  - 3.4. Human resources
  - 3.5. Environmental management
  - 3.6. From corporate social responsibility to sustainability
4. A place in the world
  - 4.1. Mercosur integration process
  - 4.2. Business development in ARCOR do Brasil
  - 4.3. Towards a global company
5. Final comments

We aim at addressing these issues in the following pages and drawing new lessons from this case which is essential to understanding and implementing successful business strategies in Latin America.

## **SUCCESSFUL ADAPTATION TO A NEW BUSINESS ENVIRONMENT IN ARGENTINA**

Since 1998, the Argentine economy has been simultaneously affected by several negative impacts. Its most striking examples include: the effects of the Russian crisis on the access to external financing, the devaluation and the modification of the exchange rate regime of Brazil (Argentina's main trade partner), the unexpected drop in the prices of the country's export products, the persistent strength of the US dollar with respect to the other currencies and the continuous advance of the public sector over the private one in the internal financial markets. By the end of the decade, a lengthy period had begun which was characterized by recession and price deflation. It subsequently generated mounting tensions and modified the expectations about the growth potential of the Argentine economy and the solvency of the public sector, which eventually led to the final collapse of the economic system.

This negative economic environment worsened in the case of companies with investments or interests in several South American countries, as the turmoil of the international economy was slowly leading to an expanded regional crisis. Events such as the East Asian and Russian crises in 1997-1998, the 1999 Brazilian devaluation, the problems of the Argentine economy, and the likely world recession caused serious financial and commercial disruptions all over the region. The sudden reduction of international capital flows aimed at emerging economies and the growing interest rates they faced constituted particularly major restrictions.

In the aforementioned period, the negative trend of the main (economic) aggregates of Argentina, of the local industry, and of the food and beverage sector in particular exerted a huge impact due to its magnitude. After four years of recession and sudden contraction, the product registered a fall of almost 20%, industry was reduced by 27%, unemployment and poverty reached all-time highs and Argentina took on the challenge of redesigning the key rules of the economic game, regarding its exchange, monetary, tax, and financial aspects.

Due to the return of extreme volatility to the environment, decisions on production and investment changed and increasing doubts were raised as to the solvency of a leading group of companies operating in the country. The negative consequences in the corporate sector spread rapidly while the economic agents' possibilities to prevail upon the return of great macroeconomic uncertainty were unclear. Thus the question that immediately arises is: How does a company walk through a period of such negative economic and insti-



tutional context? How did ARCOR's strengths help it overcome the collapse of the convertibility system and the regional crisis?

In the first place, and like many other times, the business history counts. On the one hand, during a great part of the nineties the company had developed an aggressive strategy for capital investments (of almost one billion dollars) and for sustained improvement in the technical/production and organizational management. These transformations facilitated the consolidation of its position in the markets (which were its core business) and gave the final boost to the internationalization process. Eventually, this behavior turned out to be, *ex post*, decisive in facing an acute and lengthy crisis. A clear example is illustrated by the results of the systematic development policy of the export market, which had been adopted in the preceding years. Even when the most disruptive effects of the crisis had spread, the company's policy acted as a reliable insurance, guaranteeing them an invaluable diversification of risks in view of the dismantling of the Argentine domestic market. On the other hand, the knowledge gained (from half a century of existence) of how to act in view of changing economic scenarios, provided ARCOR with a better understanding of what could happen once the crisis worsened and turned into a depression. Furthermore, it brought ARCOR greater flexibility to adapt itself to the changes in the environment, from both a financial and a commercial perspective.

But not everything is history. By the end of 1998, when the 4-year recession period had just commenced in Argentina, ARCOR started getting ready for a more difficult scenario through the implementation of structural adjustment programs and through a greater focalization of the investments on mass consumption business lines. Throughout this period, thanks to a group of measures which had been implemented, the crisis had found the company at a time where it was pretty advanced in its process of production and financial adaptation to a new environment. Some decisions that can be mentioned include; achieving a reduction of fixed costs, applying adjustments in production and input stocks, reorganizing a great part of the retail distribution chain (which had been a key asset in the previous stage of growth with convertibility) and achieving synergies and savings in the costs of sales through the unification of mass consumption commercial structures, acquiring the right to use licenses of well-known brands within its main business units (for instance, the agreement with Kraft to use the candy brands Sugus and Suchard in Argentina and other countries of the region), intensifying the strategy of development of new international markets outside the region, and finally, the shedding of some assets which were no longer strategic for the company (selling

the assets of a thermo-electrical power plant, exiting Vitopel [a polypropylene film manufacturing company] and the sale of some fields and agricultural and livestock farms).

On the other hand, some investments that had been made in the mid-nineties foreseeing more optimistic scenarios in terms of economic return, and the internal restructuring process of shareholdings which demanded a strong application of funds had brought about an increase of the financial debt which, at that time was difficult to manage in the context of a greater load of interest as a consequence of the tight restriction on financing in general. Although a significant part of the non-operational financial revenues were redirected towards said destination and the necessary financial engineering was applied in order to improve the structure and profile of the loans, the financial liabilities constituted an additional fragility factor which had to be dealt with amid the increasing turmoil.

Nonetheless, in times of crisis as the one Argentina lived through at the end of the nineties, where the horizon excessively narrowed, business mistakes in short-term decision making directly related to the everyday operation (and which in other fields only imply a fall of annual profitability, economic losses or the change of a subsidiary manager of a country representing less than 1% of the total sales) could irreversibly imply the forced sale or merger of the company or even its permanent closure. Consequently, apart from structural strengths, the company relied on business capacities for day-to-day crisis management. This was evidenced in ARCOR's speed of reaction in the time prior to and subsequent to the collapse of the convertibility regime.

In a highly uncertain scenario, the disappearance of credit, the rise of relative prices in favor of internationally tradable goods, the sudden fall of the real salary and the increase of unemployment and poverty appeared as inexorable features of the immediate post-devaluation economic scheme. However, the level at which the exchange rate would stabilize itself and the reaction of internal prices upon the raise of the nominal anchor of convertibility, were just some of the key questions that remained unanswered. In view of these circumstances, a package of short-term measures was implemented in order to minimize the impact on the financial position and on the result of the operations. The priority decision adopted by ARCOR was to fully protect the working capital and the profitability of the company, respect the contractual obligations and maintain the quality of the products.

The aim set by the company to protect its working capital initially resulted in a necessary adjustment of customers' purchase and sale financial condi-

tions. The purpose of prioritizing the cash flow (precautions had been taken in that sense since mid-2001) brought about, by the end of 2001, a reduction of the tax credit magnitude from more than 90 days in average to just 7 days. This process of financing reduction and of working capital recovery took place during the most critical times of the crisis in a period of just 40 days.

The financial policy was aimed at increasing the liquidity level in order to meet the funding requirements of operations and the financial obligations considering the markets lack of credit and liquidity. Financing restrictions put pressure on commercial policies. In this sense, ARCOR also decided, in direct connection with the aforementioned decisions, to redefine its commercial relationship with the large retail sales centers (supermarkets, hypermarkets). These retail distribution channels which had developed since the mid-eighties and forcefully grew during the nineties, operated in terms of product delivery time and loan settlements which had become strongly unfavorable in context of a worsening crisis and a dim future.

With the new exchange scheme which had been implemented since January 2002, the criterion adopted by some multinational competitors of delaying the increase of prices in the domestic market in the expectation of obtaining greater volumes of sales, was totally contrary to the goals ARCOR had set. To protect the working capital meant to sell on the basis of "cash only". This implicitly entailed lower sales and, consequently, the loss of part of the company's products market share. Regardless of the reasons, to accept the loss of market share in favor of competitors was unusual behavior from a strategic point of view as it might imply market situations that could turn out to be difficult to reverse later on. Undoubtedly, in shrinking markets, these decisions generate high internal tensions in any company that needs to strike a proper balance between the financial and commercial aspects of the business.

Taking on the role that a leading company shall play in critical times for its production structure basically means not to transfer the various negative effects of the crisis onto the multiple small and medium enterprises that regularly act as suppliers and customers. In this sense, ARCOR implemented measures to cushion the impact of the global fall such as providing certain suppliers with access to inputs or collaborating with the weakest links of the distribution network which would allow ARCOR, once the most troubled times of the crisis had elapsed, to find the answers for a quick recovery of the activity level. Fulfilling the commitments previously taken on with the supplying companies guaranteed the preservation of the reputation built up over decades. Avoiding, even at the expense of losses in the short term, the unilat-

eral breach of the contractual obligations was a prime objective in order to maintain the company's good name intact.

As mentioned above, the crisis rewarded ARCOR's dedication in the search of foreign currency outside the region through the penetration of its products. Upon the dismantling of the domestic market and the subsequent change in the relative prices, many Argentine companies decided to redirect their sales towards the global market. However, exporting is not just a matter of expression of the business will. In order to meet the international demand of goods and services, it is necessary to carry out systematic activities for the development of customers and markets in foreign countries during usually lengthy periods of time. In ARCOR's case, these slow and long-term processes were evidenced by the fact that its products reach more than one hundred and twenty countries of all latitudes. But they were mainly recognized when (with the Argentine economy facing serious difficulties in 2001) a production and exports agreement (that was enforce till the end of 2007) was entered into with one of the main U.S. confectionery manufacturing and trading companies, or when sustained external sales were achieved due to the quality of the products and the reliability attained in the trading channels.

Finally, the supply of the company's products was redefined based on the new purchasing power of Argentine consumers. The regional experience was a key factor to adapt to and have a quick reaction to the new habits and purchasing power of consumers. In this sense, ARCOR also tried to reduce advertising investments in favor of intensifying promotional activities. With this package of policies ARCOR could dramatically reduce the collection terms and achieve greater financial autonomy. Furthermore, the uninterrupted supply of products was guaranteed and the exports volumes favored a good marginal contribution with respect to the company's core business.

The gradual normalization of the Argentine economy since the second half of 2002 and the subsequent sustained recovery throughout 2003, allowed ARCOR to obtain positive profitability levels, to increase liquidity, and achieve financial soundness. ARCOR's adequate reaction to the Argentine crisis favored the quick use of the greater sales volumes in the domestic market. The situation began returning to normal in particular regarding those items which had suffered sharp falls and in less than one year ARCOR had recovered its market share in most business units. The features of the post-crisis consumption favored the increase of sales in the retail channels in relation to those of supermarkets, thus ARCOR benefitted from the greater commercial penetration it had in the aforementioned channel. The protection of

the working capital was still a goal, so in 2003 the trade conditions were maintained in spite of the higher demand.

With the refinancing of financial liabilities with bank creditors and the profitability level reached, the perspectives for 2004 were positive again and the year carried good news; greater sales, new increases in the profitability levels and strengthening of the market share. Furthermore, another milestone worth to be mentioned was the agreement with the French group, Danone (world leader in fresh dairy products and bottled water, and at that time one of the leaders of the cookies & crackers global market), for the creation of an alliance which merged the activities in the cookies & crackers business in Argentina (with the incorporation of the centenary company Bagley), Brazil (with well-known brands Triunfo and Aymoré) and Chile. Since 2005, ARCOR has started operating with the companies which emerged from the regional association, where ARCOR held a 51% share and was in charge of the management and control of the unified operations. The reputation (expressed in numerous local and international awards) and the experience of ARCOR in the region (particularly in terms of distribution and wide coverage of its points of sale) turned out to be key assets to successfully achieve the said collaboration. This transaction allowed the creation of one of the largest cookies & crackers companies of South America. The operational performance of the new companies in Argentina, Brazil and Chile is very successful, evidenced especially by its growing market shares and profitability improvement.

Bagley's performance in Argentina showed a sales increase from USD246 million in 2005 to USD645 million in 2012. This dynamism allowed for an increase in the cookies & crackers market share from 40% to almost 50% in 2012, with a growing share in higher value segments. The alliance defined medium-term strategies. In this way, a new organizational structure was implemented adapting the already existing roles to the development, integration and training of human resources, tending towards greater multiskilling and leadership, stimulating innovation, relationships with the community and continuous development. At the same time, the positioning in marketing and sales was strengthened thanks to a flexible organization and distribution, and prioritizing the entry of new differentiated products and markets supported by communication actions and events. Its great capacity to adapt its distribution systems to the changing choices of consumers stood out. By taking full advantage of Danone's prior abilities in innovation and marketing issues, new solid skills were picked up in knowledge management, supported by a research and development area for continuous improvement and development

of new products, especially focusing on the nutritional improvement of its components. The new business base relied on a strong reorganization and efficiency gain of its 4 industrial plants in Argentina. Between 2005 and 2012 more than USD120 million were invested. The results of these measures meant a significant improvement of the EBITDA, which increased from USD3.7 million in 2005 to USD87 million in 2012.

In order to be consistent with the strategic purposes, between 2010 and 2012 a new model plant was built in the complex located in Salto, Province of Buenos Aires, with an additional plan to annually manufacture 260,000 tons of products up to 2015. This plant has state-of-the-art technology and lines with the highest productivity available, and seeks innovation in products packaging, as regards to both speed and automation and the protection of the useful life of products, thus changing the historical and traditional packaging of the brands' products. The keys to running this project were; the abilities ARCOR Group had and maintained in order to adapt to the constant changes in the economic context and the market, organizational and team work capacities; profound knowledge of the engineering of its plants and production lines, relationship and joint work with suppliers of global first class technology, full development of equipment and services suppliers on a local level, experience in the setting up and starting-up of different lines and technologies, research and development for the creation of new products and improvement of the existing ones, recruitment and constant training of human resources, and the development of relationships with the community and with the national authorities to solve restrictions on infrastructure (gas pipelines and electrical power generators). The production area in the Salto Plant doubled, thus covering an area of 79,000 m<sup>2</sup>, with 7 production lines and 10 industrial ovens, subsequently increasing production capacity up to 107,000 tons annually and increasing employment up to approximately 900 people in 2012. The crackers production line, 9 (familiarily called "Jumbo"), is currently one of the greatest and world class lines of crackers. In turn, Salto became the largest manufacturing plant in Argentina and one of the most important of Latin America. The facilities actively follow ARCOR's sustainability policy regarding a low environmental impact and rational use of energy and water.

The success of the Group in forging the alliance with Danone provided it with immense strength to take on new challenges. In addition, in 2005, ARCOR asserted its leadership in the food products market through the acquisition of Benvenuto (owner of the well-known brand "La Campagnola"). The purchased company had been in the country for almost 100 years, therefore had consoli-

dated its position in several markets relying on specialized human resources, also enjoying the prestige of a well positioned brand equity of its “Premium” products of a high value and differentiation, all of which facilitated the positioning of food products that offered increasing margins. The decision to go on with the purchase of La Campagnola faced, in principle, the danger of shifting the focus of attention onto the internationalization process as it implied the allocation of the available resources and the efforts to develop abilities to strengthen the domestic market. However, this apparent dilemma of alternative strategies was quickly forgotten due to the successful process which this new acquisition meant, which implied an increase of its leading position in key markets of the country as well as competitive earnings which enabled it to rely on greater strengths to make progress in its business strategy.

The progress made in the Danone Alliance and the acquisition of La Campagnola had an impact on the whole development model of the ARCOR Group business base. An example was the redefinition of the marketing strategy with a new managerial policy which prioritized the development of brand equity of the products which offered greater differentiation and margins. At the same time, regional brands with growth potential were identified and as a result investments were made in advertising, design, internal and external communications, market research and technological innovation to realize their potential. This produced very dynamic results with an increase of physical volumes, margins and EBITDA. These aforementioned increases were associated with the consolidation and increase of market positions and the aggressive entry into new product categories with a higher added value such as, breakfast cereals, nutritional products lines, impulse ice creams, and powdered juice. In turn, other measures were reconsidered such as the organization of the industrial production with the growing participation of new plants of international efficiency, the restructuring of the distribution systems which facilitated cost cutting measures and efficiency gains, the redefinition of the administrative and management areas and the human resources policy, all of which have developed more modern competencies and programs for talent detection, development and retention.

In the case of ice creams, ARCOR entered said market in 2005. The business development strategy focused on a heavy investment in marketing and an active support of the distribution channel including the sale of products during winter. New products associated with those brands which are highly recognized in the market by consumers of chocolate and confectioneries have been permanently introduced into the market and new products aimed at chil-



dren have been launched. The development of the ice cream market coincided with the financial turnaround of distributors which has allowed them to invest in refrigerated chambers and refrigeration trucks that are essential to develop this activity. At the same time, ARCOR entered the market after Nestlé and Unilever's leadership. Unilever's closure of its operations in the ice cream line provided ARCOR with a quick market gain since its beginnings, achieving an ice cream market share of about 50% in Argentina. With the development of first class suppliers, the constant investment into marketing, distribution and new freezers as well as prioritizing its visibility in its points of sale, ARCOR consolidated its position in this market with a specific nature very different from that of chocolate and confectioneries.

The development of the packaging area, a key strategic input in its productive integration process has been another prominent feature of its business base. In 2012, the packaging sales represented about 12% of its total billing as compared to values around 8% in the mid-nineties. Initially, in order to manufacture corrugated cardboard containers, Cartocor S.A. began its production activity in the Paraná plant in Entre Ríos in 1981. Its purpose was to meet the needs of cardboard packaging markets focusing mainly on customer service, permanent innovation, productivity, quality and preservation of the environment. Its constant growth and the diversification of its products and markets resulted in a fierce rhythm of investments. At present it has six manufacturing plants, five of which are in Argentina: four for the manufacture of corrugated cardboard and boxes, and one for the production of paper. And in 2007 a world class corrugated cardboard plant was inaugurated in Chile, becoming the third manufacturer of boxes in said country. With a production capacity of 40,000 m<sup>2</sup> per month in Argentina and 15,000,000 m<sup>2</sup> per month in Chile, Cartocor S.A. is the greatest corrugated cardboard manufacturer of Argentina and Chile. Ten to fifteen percent of its production meets the needs of ARCOR Group, while the remaining percentage is used for other markets such as fruit and vegetables, industrial, large containers, and cardboard sheets and packaging in Argentina and other countries. It is characterized by offering an integral service while sharing with its customers the development of its packaging, design and logistics.

On the other hand, since its origins in the sixties, progress has been made on Converflex S. A. within the flexible containers market, achieving in the last decade a leading position in the Argentine industry. 70% of its production is integrated into ARCOR Group's production process. It has plants in Villa del Totoral, Province of Córdoba (10,500 m<sup>2</sup>); Villa Mercedes, Province of San



Luis (4,775 m<sup>2</sup>); and Luján, Province of Buenos Aires (7,900 m<sup>2</sup>) with an installed capacity of 12,000 tons per year. It manufactures gravure cylinders and rigid PVC blown film and carries out the conversion of flexible material. Apart from its previous landmarks, in the last decade it has consolidated a highly integrated production process and has incorporated the latest technology. In 2004, the third industrial plant was inaugurated in Luján and in 2005 the plants at the Villa del Totoral complex (for the conversion, extrusion and engraving of the cylinders) were expanded inaugurating the second industrial building within the complex and introducing new equipment to increase its capacity. In 2011, the area covered by the Luján complex was expanded and the latest Fischer & Krecke, high resolution flexo press (one of the pioneers in Latin America to incorporate this technology), was installed therein. Furthermore, additional lamination and cutting equipment was acquired in order to balance the increased production capacity of the complex. It is important to highlight the constant investment in technology, with the development of special applications, research of new packaging technologies, sustainable containers and studies for replacement of containers.

In 2006, the joint production agreement with Bimbo Group for the elaboration of sugar and chocolate confectionery entered into in Toluca, Mexico, presented another landmark in recent history. This agreement promoted ARCOR's presence in a market of crucial importance in Latin America, providing a much larger support base in order to achieve an increasing participation of ARCOR in Mexico and of said country into ARCOR's structure. Cooperation with Bimbo is much more than a simple partnership as it offers the advantage of the association between a Mexican world leading company and ARCOR's competition skills in a significant domestic market with strong export possibilities to compete with the best transnational companies. Between 2001 and 2005 ARCOR supplied the market through imports and sales by means of wholesale channels. In 2007, Mundo Dulce began manufacturing ARCOR and Bimbo products. The dynamic results are shown in the growth of domestic sales by more than USD100 million, the manufacture of products with efficiency gains and low transformation costs, and the consolidation of an exports platform which in 2012 represented more than one third of total sales.

In 2010, an agreement with *The Coca-Cola Company* was entered into through which ARCOR gained the right to commercialize some confectionery products and ice creams with the use of certain Coca Cola brands. All these events emphasized one of the most relevant aspects of ARCOR's performance in the last decade which had been the successful forging of alliances

with world class players which had brought about the consolidation of the company in a process of sales increase and the use of synergies with strong efficiency gains in the administration, logistics, distribution and marketing areas. This successful building of alliances based on the company's lengthy and evolutionary process during which it not only showed its competitive abilities but also generated significant social capital based on its reliability, respect of contracts, and its commitment to social inclusion and environmental sustainability. As seen below, these alliances have been expanded in the last few years to include technological liaison projects and others for the generation of innovation activities; the development of systems areas and sustainability actions jointly pursued with other companies, organizations and the public sector. These cooperative advances on the creation of business knowledge and development networks have potentiated (through a joint process) ARCOR Group's performances.

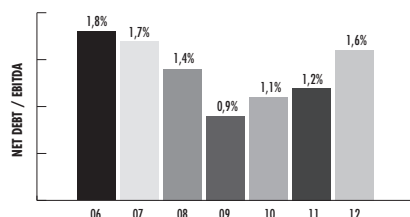
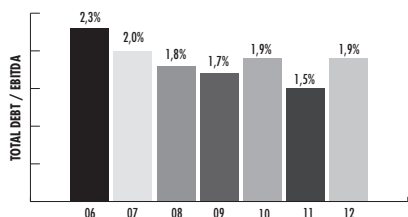
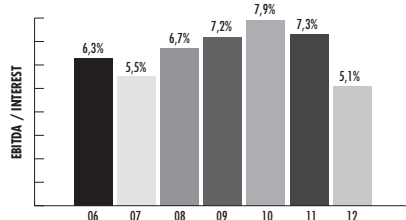
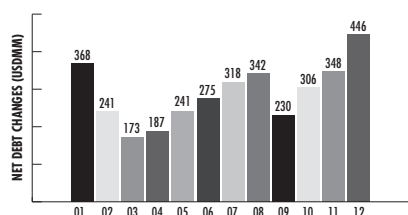
Furthermore, apart from the building of alliances, (which strengthened ARCOR's presence in the domestic market, Brazil and Mexico) world class operation plants were opened. In 2004, in Luján, Argentina; a new Converflex plant was built for packaging production. In 2006, the Mundo Dulce plant in Mexico was developed to manufacture confectioneries. In 2007, a confectionery plant was inaugurated in Pernambuco, Brazil; and the Cartocor packaging plant was opened in Chile. In 2010, a new cookies & crackers plant was built within the Salto Complex in Argentina. In 2011, a new Van Dam distribution center was opened in Montevideo, Uruguay, and in 2012 the construction began of a chocolate and sugar confectionery manufacturing plant in Chile. This process involving acquisitions and the construction of new plants could be carried out thanks to the development of a significant investment process which was in the region of USD700 million between 2002 and 2012.

In 2005, in a context of increasing sales, employment and investment in Argentina and abroad, ARCOR enrolled on a financing program with the International Finance Corporation-World Bank Group tending to extend debt maturity dates. The execution of this loan agreement with the IFC for a total amount of USD280 million implied a substantial improvement in the capital structure and financial cost of the Group. Firstly, in order to receive this financing ARCOR had to pass certain examinations in terms of its contributions to corporate social responsibility, the preservation of the environment, and the generation of dynamic competitive abilities which contribute to the economic development of the country. Secondly, the grant of the loan reflected not only an improvement in the economic situation of the country but

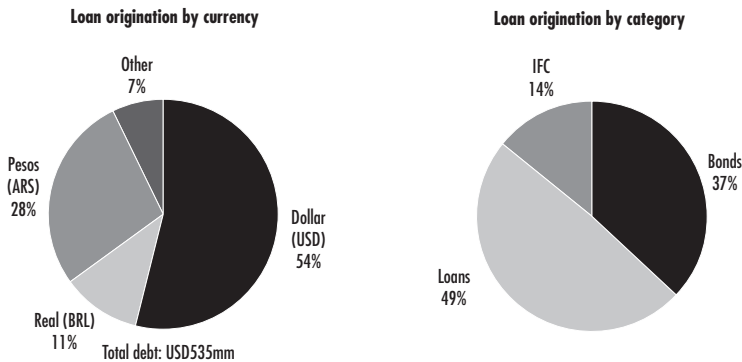
also the chance to develop an integral business strategy within a medium term working scheme. While in the transition stage, short term financial agreements had been achieved, this loan symbolized a shift from short term uncertainty to adequate financing to develop long-term business strategies.

In 2007 a new loan for USD130 million was taken out with the IFC and in 2009 an additional loan for USD100 million was also arranged with the institution. Following that, in November 2010, for the first time in the Group's history, corporate notes amounting to USD200 million were issued. This placement was very successful and had an important oversubscription proving ARCOR's solid financial position, and their well-known and reliable image among national and international investors. The final maturity date is in 2017, with a 7.25% annual interest rate, which is a highly competitive rate for the Argentine capital market. These opportunities of new financial funding lines with multilateral organizations within the international capital markets facilitated the extension of the consolidated debt terms, which in turn generated the funds necessary for the development of the operations and the financing of the investments. In addition, a capitalization policy of the subsidiaries in foreign countries was established in order to face their investment and operation programs. The debt indicators show ARCOR's solvent situation as seen in the following charts.

**Debt changes. 2001 – 2012**  
In millions (mm) USD and percentages (%)



**Consolidated debt as of December 2012**  
**In millions (mm) USD and percentages (%)**



**Financial Indices**

Net debt (USD)	445.5 MM
EBITDA/ Interest	5.1x
Total debt / EBITDA	1.9x
Net debt/ EBITDA	1.6x

### Brief Quantitative Evidence of Successful Performance

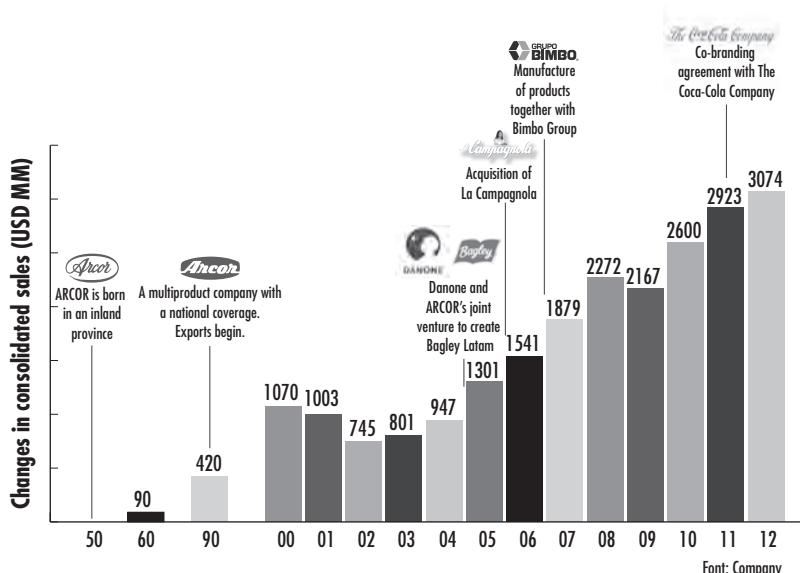
The development of ARCOR's business strategy has consolidated its leadership in the food industry, and is holding a very significant presence as of end 2012. For example, some of ARCOR's indicators include:

1. Total sales went up rapidly from USD1.003 billion in 2001 to USD3.074 billion in 2012. A growth was observed in sales outside Argentina, where they decreased from 79% to 67% between 1996 and 2012, however were offset by the growth in Brazil, Mexico and the Andean Region (Chile, Peru and Ecuador). At the same time, confectionery sales fell from 61% to 52% in this period, with increases in cookies & crackers and packaging. In terms of physical volumes manufactured, production increased from 850 thousand tons in 2002 to slightly over 1.5 million tons in 2012. ARCOR is the leading foodstuff company in Argentina, the world's main candy manufacturer and one of the leading cookies & crackers companies in South America. In the turnover ranking, it is one of the leading confec-

- tionery manufacturers in Latin America and is ranked in the world's top 12. It is the main producer of corrugated cardboard and ethyl alcohol from cereals in Argentina.
2. Exports increased from USD193 million in 2002 to almost USD400 million in 2012. The dynamism of exports generated in Chile, Mexico and Brazil stands out, with exports from these countries having increased by more than USD50 million during that decade. ARCOR exported to more than 120 countries, in an increasing process of diversification, opening of new markets and growing participation of Africa and Asia. These destinations accounted for, in 2012, USD80 million in exports. Around 50% of ARCOR's exports are within the intercompany network. It is the first confectionery exporter in Argentina, Brazil, Chile and Peru.
  3. Employed staff increased from 13,000 members in 2002 to around 20,000 members in 2012, with total payroll costs of approximately USD 550,000,000. In Argentina there are 13,000 employees, in Brazil around 4,000, in Chile slightly under 2,000, in Mexico around 1,000, and there are almost 1,000 staff members in offices located in the rest of the world. All of which proves the strengthening of the internationalization process through direct investments abroad within the context of a "multi-Latin" company. It also has over 10,000 suppliers, most of them SMEs.
  4. ARCOR has 39 industrial plants: 29 in Argentina, five in Brazil, three in Chile, one in Mexico, and one in Peru. Its main manufacturing plants are certified under ISO 9001 and ISO 14001 standards. It also has 19 distribution centers in Latin America and commercial offices throughout the five continents.
  5. In Argentina, it is a model due to the implementation (through ARCOR Foundation, Brazil ARCOR Institute, and the comprehensive management of its business base) of policies on Corporate Social Responsibility (especially its commitment to education), Sustainability and Environmental Protection. ARCOR has received many of the most prestigious awards which are granted to companies and managers in Argentina for its actions and achievements.

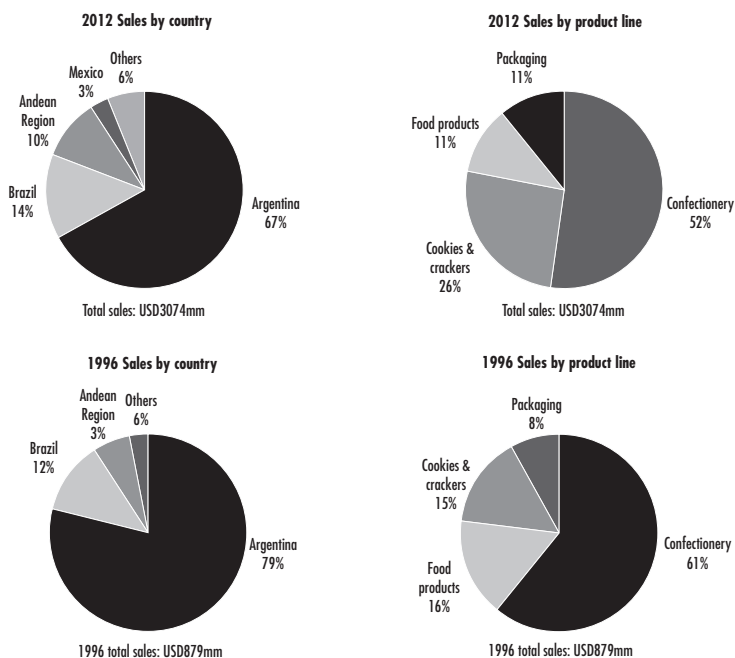
# Changes in consolidated sales. 1950-2012

In millions (mm) USD



## International Scope and Diversified Sales. 1996 and 2012

In millions (mm) USD and percentages (%)



## THE RULES OF THE GAME CHANGE: THE ARGENTINE MACROECONOMY

### The 1998 Recession and the Collapse of the Convertibility System

*Since 1998 the Argentine economy had been simultaneously affected by various negative shocks. Some of the most prominent examples of what happened at the time include; the effects of the Russian crisis on the access to external financing and on interest rates in developing countries, the subsequent devaluation and modification of the exchange-rate regime in Brazil (Argentina's main trade partner), the sharp drop in prices of the country's export products, the persistent strength of the dollar with respect to other currencies, and the continuous advance of the public sector over the private one in the internal financial markets.*

*By mid-1998, which was the onset of a long period of recession and price deflation, the system was affected by a growing distrust of the economy's growth potential and of the solvency of the public sector, thus recreating a negative cycle of rising interest rates, deterioration of fiscal results and additional losses in credibility levels. In this context, falls in bank deposits and capital flight took place which led to the introduction of constraints both on financial system funds and on foreign payments. However, such measures were not enough to prevent the end of the system.*

*Between 1998 and 2001, the return to extreme volatility of the market greatly affected the decisions on production and investment, and raised increasing doubts as to the solvency of a large number of companies. The difficulties of the Argentine economy caused significant financial and commercial turmoil. The negative consequences in the corporate sector had spread quickly. Furthermore, there was no clarity as to what would be the dominant response from the economic agents upon the return of a high macroeconomic uncertainty. The macroeconomic scheme by late 2001 showed a highly indebted economy without political instruments to withstand external shocks, namely; a fixed exchange rate, a passive monetary policy, and an unsustainable tax scheme due to the exponential rise of interest on debt.*

### Main Features Associated with the Change in the System (2002 - 2007)

*The 2001 crisis derived in the exit from the convertibility system and the devaluation of the exchange rate by early 2002. This caused a generalized termination of agreements and a radical change in the relative prices of the*

*economy, modifying the profitability of the different sectors compared to the rates of the previous decade and tending to favor the production of tradable goods. With the partial suspension of payments of public debt (and its subsequent restructuring), the partial pesification (conversion from dollars-USD to pesos-ARS) of local financial and bank debts along with the implementation of a floating exchange rate scheme controlled by the Argentine monetary authority, the country recovered the ability to use its exchange, monetary and fiscal policy instruments. Though the cost of exiting the system was high in economic and social terms, due to the rise in prices and the termination of agreements, there was an intense and fast recovery, starting a few months later, in the second quarter of 2002. Such a recovery was also favored by the international price rise of raw materials (associated with the expansion of China and India), the drop in import prices and low interest rates.*

*In this context, both the domestic (final and intermediate) and external demands fuelled the production of goods and services. Among the different economic sectors, the manufacturing industry showed a significant performance within this generalized context of recovery, by reverting (at least partially) to the previous deindustrialization process. In addition, some policies were implemented in order to separate (at least partially) the sharp initial drop in real wages from the purchasing power of the aggregate demand. In particular, it is also worth mentioning the implementation of the Unemployed Household Heads Program (Plan Jefes y Jefas de Hogar) with the duty to settle currency, the withholding of tax on certain products included in the consumer basket and the gradual consolidation of the income policy.*

*In this way, a process of high economic growth was triggered, with the creation of jobs and a gradual recovery in real wages. Initially this recovery was only for formal employment however it later reached the informal employment sector, due to the restoration of central items such as minimum wages and collective bargaining. In aggregate terms, there was a sharp increase in GDP that continued to exceed 8% per year (except in 2009 due to the international crisis) thus allowing a rise in average well-being indicators and in the main variables of the social structure without restrictions from fiscal or external areas. In fact, the payment of both the external debt and interest had a significantly lower effect in terms of the exported values. With regards to public debt, its renegotiation and subsequent restructuring*



*led to a less risky debt profile in comparison to that of the last decade. In this sense, the public debt-to-GDP ratio shifted from 53.7% in 2001 to 40% in 2010—with a 166% peak in 2002. Another key factor in the restructuring process was the conversion of the debt from dollars into pesos. Furthermore, within the period analyzed, there was a sharp reduction of the external debt to exports ratio, from a high of 5.4 in 1999 to 1.6 in 2008. These elements meant a favorable transformation in the dynamics of the foreign exchange market and a larger leeway for exchange policies.*

*Moreover, the net position in international investments changed from negative to positive and Argentina became a creditor to the rest of the world. In addition, the savings rate increased to, in 2007, about 25% of GDP (the highest in decades), whereas in 2001 it constituted 14.2% of GDP. In this period, there was a significant rise in investments financed by an important increase in domestic savings, which allowed high surplus in the current account of the balance of payments. The rise in investments was not due to the previous flow of external capital but to the expansion of aggregate demand associated with a competitive exchange rate. Thus, the discontinuity in the generation of national savings to finance investment seemed to have been broken, and the country's ability to generate surplus and increase its wealth was evidenced.*

*In this context, the solid initial recovery and the rise in activity levels led to a significant drive in the labor market, particularly in formal employment. Between 2002 and 2007, more than 2.5 million job positions were created, of which 435 thousand were in the manufacturing industry, which represented 17% of the total new jobs. As a distinctive feature of this process and reversing the previous trend, there was a rise in the full employment rate from a low 25% in May 2002, to an average 38% in 2007. This encouraged a decrease in unemployment rates (from 21.5% to 8.5% in the same period), poverty rates (from 53% to 23%), extreme poverty rates (24.8% to 8.2%) and undeclared employment rates (47% to 37.8%).*

## **The International Crisis and its Impact on Argentina**

### ***The Pre-crisis Background and the Emergence of Structural Tensions***

*In 2007 some tensions relating to the macroeconomic scheme began to surface, together with structural deficiencies that shaped the production matrix of the country slowed down the recovery of the productive sector.*

*Thus new dilemmas for economic policy emerged, which recreated negative expectations about the evolution of the economy as of late 2007. Some dilemmas worth mentioning include the accelerating inflation and the energy supply problems, both of which required concrete actions, to eliminate negative expectations, give credibility to public information, and to ensure the infrastructure that brings growth. Skilled labor restrictions for the most dynamic sectors were added, together with the practically nonexistent long-term credit supply, whether from the banking sector or the capital market. All these elements combined to narrow the horizons of the agents, hindering long-term investment decisions, particularly in the segment of transnational companies.*

*The long-enduring conflict with the agro-industrial chain triggered by the increase in the rate of export duties under Resolution 125, the subsequent drought, the appreciation of the Argentine peso, the outflow of deposits from the financial system, the rise in the interest rate, the increase of subsidies and their growing influence on public spending, the federal distribution of public resources, and the nationalization of pension funds were some of the central issues in the context prior to the impact of the international crisis. These negative expectations also created an excessive preference for the dollarization of portfolios.*

*Consequently, the dynamics of the different industrial sectors began to show an increasing heterogeneity, especially in mid-2008. On the one hand, the blocks linked to the domestic market experienced a slowdown. On the other hand, the evolution of certain capital-intensive sectors with export output remained exceptionally good, so much as to offset, on average, the modest performance of the former. Such was the case that only two sectors –automotive and steel industries– experienced more than 65% of cumulative growth, in contrast to the relatively homogeneous evolution of previous years. In addition to the increasing concentration of growth, there was also a slowdown in the investment process.*

### ***The Impact of the International Crisis***

*The crisis spread worldwide, initially from the United States and then through the financial channel, affecting mainly the developed nations and the developing countries that had greater integration in world markets. Later, the decline in aggregate demand and international trade in general spread the impact to the rest of the world through the real channel. Early*

*in the fourth quarter of 2008, the Argentine economy received the impact of the international crisis. Although the country had higher margins in order to face a negative external shock than on other occasions, the situation was not as strong as two years earlier, so the initial blow was felt heavily, mainly by the real side of the economy.*

#### The Financial Channel

*Unlike past events in Argentina, the impact on the financial side had a limited scope. This was due to a number of factors that served to cushion the blow, thus avoiding a crisis in the balance of payments and the banking system. This is a significant development considering the country's economic history, marked by the typical crises of foreign exchange settlement that deprived the activity of its growth potential. Among the elements associated with this reality, it is worth highlighting the relative strength of the macroeconomic fundamentals, particularly the strong trade surplus and the low public debt. From the point of view of the external and fiscal sectors and in relation to the liquidity and solvency indicators of the financial system, the situation was significantly more solid than on other occasions. In the case of the financial system, it is worth stressing the liquidity levels, the change in sign of the average equity exposure of the system, and the reduced delinquency rates, along with the significant decline in dollarization of bank portfolios.*

*In addition, the favorable terms of trade for Argentina and the accumulation of international reserves played a significant role in relation to the external gap. Furthermore, the public debt restructuring, which involved a significant reduction of foreign currency borrowings, gave the government leeway to control the exchange rate against a run on the currency and foreign exchange outflows. In fact, there was an intense capital flight (of about USD 45 billion between the second quarter of 2008 and the third quarter of 2009) before the impact of the crisis, as a consequence of the political conflict with the agricultural sector; doubts regarding the CPI and the nationalization of the Retirement and Pension Plans Administrative Bureau (Administradora de Fondos de Jubilaciones y Pensiones).*

*Another factor that contributed to neutralizing the harmful effects was the companies' low debt. Paradoxically, the low multiplication of credit (which is, under normal conditions, a factor that adversely affects the full development of production) and the relative isolation of the international*

*capital markets caused the financial turmoil to generate secondary effects at the aggregate level. Argentina is the only halfway developed country where both public and private sectors were oblivious to the extraordinary growth of financial derivatives. This occurred in a context of persistent positive flows of private surplus during the post-crisis years, which was reflected in an increase in the inventory of assets belonging to Argentine residents abroad. This increase was so important that the private sector became a creditor to the rest of the world.*

#### The Real Channel

*Regardless of the factors that eased the impact, the Argentine economy was not immune to the external crisis. The main affected channel was the commercial trade, with a significant deterioration of external demand and consequently, there was a sharp drop in prices and in quantities exported. This was coupled with the drought suffered by most of the agricultural sector and with the lower depreciation of the Argentine peso relative to our major trading partners, which set a challenging scene. Within the industrial sector, this retraction stage involved the fall of the two most dynamic branches sustaining the growth of the manufacturing sector having had a high export output; namely, the automotive and primary metals industries. Both of these industries suffered declines exceeding 40-45% year-on-year during 2008 and in the first months of 2009, all of which began to reverse gradually more than a year later. The fall in external demand, combined with lower liquidity in capital flight and retraction in productive sectors leading the aggregate growth, resulted in the first contraction in activity levels after almost 20 quarters of continuous expansion.*

*In this context of high uncertainty, domestic demand also fell. Investment suffered a sharp setback, in view of the worsened sales expectations and the upsurge in financial constraints, which multiplied the initial effects. The decrease in activity continued to deepen until February 2009, the most critical moment for the industrial sector in recent years. Numerous plants halted production and reduced shifts. There were also suspensions and dismissals of staff. Thus the labor market situation worsened, with the destruction of around 200,000 jobs, taking into account registered employment only. This decline in production and investment was reflected in a sharp drop in imports (especially in intermediate and capital goods), which made it possible to maintain loose external constraints, even in the face of*

*declining exports. In this context, the year 2009 ended with a drop in exports of 21% and a decrease in imports of 32%, which is why, contrary to what might be expected, there was a record trade surplus as a result of the activity adjustment, particularly in sectors with high import content (automotive), which funded an acceleration in capital outflows.*

#### **Economic Policy Response to the Crisis**

*In the context of the international crisis, the Argentine government authorities adopted a series of policies in at least four areas: monetary and exchange, fiscal, trade, and social policies. Regarding the first issue, it should be mentioned initially that in the context of the capital flight previously said, the thought of an expansionary monetary policy was complex, even though there was an injection of liquidity (buying of bills and notes by the monetary authority, open market operations and easing of some legal provisions for calculating minimum liquidity), this was not enough to offset the increase in the preference for liquidity by the banking system, which strongly reduced the credit and money multipliers. In this way the net result of the policy was contractionary, initially generating a sharp rise in benchmark interest rates, with particularly damaging effects on the chain of payments and the working capital financing to small and medium enterprises. Although for a few months the situation reached a critical point, the payment chain fortunately failed to be interrupted, thus recovering degrees of freedom which led to the gradual reduction of interest rates. Additionally, considering the economy in real terms, there was a slower depreciation rate of the Argentine peso, compared to what happened in other countries, particularly those having had a greater exchange of goods with Argentina. This, in part, fuelled capital flight, due to the growing expectations of depreciation.*

*Only in late 2009 was there some correction in the trend, even though the appreciation of the Real and the Euro played an important role in it. Additionally, the role of the public banking system was also very active: it sold more than AR\$12.5 billion of its holdings of Central Bank Bills (Lebacs) and Central Bank Notes (Nobacs) in order to inject them later into the financing of both the public and private sectors, thus balancing the restrictive policy guidelines of the Argentine Central Bank. In fiscal policy, it played a very active role, although limited by the absence of an anti-cyclical fund and the difficulties to finance new debt. However, the net effect was*

*expansive, since the growth rate of primary expenditure was maintained despite the downturn shown by the tax revenue (of 32% and less than 10% in current values, respectively). This move would not have been possible without the resources from the pension reform introduced by Act 26.425, which established the Argentine Integrated Pension System (SIPA), a pure PAYG system that removed the individual capitalization component, which has been effective since 1994. This reform implied, on the one hand, a monthly flow of 1.1% of GDP for the Argentine Social Security Administrative Bureau (ANSES), and on the other hand, the transfer to the bureau of a resource stock equal to 10% of GDP, composed in many cases (almost 60%) of government bonds, which allowed a better management of liabilities. Another measure that played a significant role in mitigating the impacts of the international crisis was the increase in public works. Along the same lines, there were also tax cuts, higher subsidies and tax benefits, like the extension of the moratorium for all obligations due on December 31, 2007, the reduction in employer contributions to new or formerly undeclared jobs, the removal of income tax deductions effective for employees since 2000, and the extension of the investment and infrastructure promotion system, among others.*

*During 2009, an active foreign trade policy was implemented in order to promote the monitoring of foreign trade in an international context of inventory liquidation and trade diversion. But it is worth mentioning that some measures, such as non-automatic licenses imposed on bilateral trade, though they may be relevant in some specific product segments, did not have a significant impact on foreign trade as a whole: the fall in imports during 2009 was mainly due to the sharp decrease in industrial activity (particularly in the automotive sector) along with the decline in investment, an activity where most capital goods are still imported.*

*Finally, regarding social policy, it is worth highlighting the implementation, by the end of 2009, of the Universal Child Allowance Program (Programa de Asignación Universal por Hijo), extending social security coverage to the unemployed, informal workers and maids. Its impact affected the offsetting of the fall in aggregate demand produced by the international crisis, by encouraging private consumption in a segment of the population that has historically fallen behind. Furthermore, it served to cushion the negative effects of inflation on the rise in poverty and extreme poverty. On the other hand, the implementation of the Productive Recovery Program*



*(REPRO) of the Ministry of Labor, which helped many of the companies pay a portion of the wages and thus overcome, without much turmoil, the worst of the international crisis, was also important. Even without developing a productive and social comprehensive program to overcome the impact of the crisis, the significant differences in the macroeconomic framework and the implemented public policy measures proved to be stronger against the impact of the international crisis than on other occasions, preventing the triggering of an economic depression. The administration of foreign trade and the stimuli to employment sustainability (coupled with the reluctance of companies to lay off skilled labor) and consumption were key factors to moderate the decline and to accelerate recovery.*

### **Recent Developments and Challenges**

*After the 2010 crisis, by the end of that year and during the first three quarters of 2011, there was a significant recovery in activity and an increase in the investment process, which reached a historical peak of 24% of GDP in 2011. The Argentine economy faced, in late 2011, new problems in the management of the economic policy that allowed it to hold the sustainable development path and generate a dynamic process of structural change. Included in the challenges; were inflation issues, which require specific actions to defuse inflation expectations and give credibility to public information, rationalization of increasing subsidies mainly in the areas of transport and energy, involving simultaneous effects on efficiency and distributive progress, and the loss-making external balances of trade in the manufacturing sector, which posed an acceleration of competitiveness gains in productivity, together with the creation of a significant external trade deficit in the fuel sector. These new dilemmas recreated negative expectations about the evolution of the economy, generating excessive preference for the dollarization of portfolios, which amounted to around USD 75 billion between 2007 and 2011. Despite these difficulties and the reduction of looseness in the management of the economy, corrections can be implemented without the need of a crisis: there are political and technical margins to administer a new path of sustainability of the sources of growth.*

*The energy constraints led to the nationalization of YPF, which is the main company of the Argentine economy. In addition, the negative trend projected on the results of the current account led to the implementation of a strong administration process in foreign trade and restrictions on the*

*purchase of foreign currency. These measures made it possible to maintain a strong trade balance of USD12 billion in 2012. However, combined with the uncertainties of the international economic context, these measures resulted in restrictions of; the activity level, which only rose slightly more than 1% in the year; the investment process, which fell by about 5 points of GDP; the creation of jobs; and the higher value-added exports.*

*Major warning signs emerge from inflation which affect, investment decisions, the purchasing power of informal workers, the execution of contracts and the competitiveness of the economy. Export sectors are affected by strong increases in production costs and a greater tax burden, while the exchange rate is set far below such increases. In the domestic market, there is a moderate recovery in the activity. It is important to consider that the domestic market has doubled in the past six years, with a growing wage bill during the last decade. In addition, the existence of a negative real interest rate, an increase in public spending over tax revenue growth, and a monetary expansion, together with increasing dollarization restrictions, are all associated factors that strongly encourage domestic consumption, in a context of growing distribution resistance. Among the positive aspects, there is still some looseness in the external sphere and a continued growth of aggregate spending, so a moderate growth in economic activity is expected in 2013. The good prices of export products, the levels of grain harvest favored by good weather conditions, and the recovery of automotive demand by Brazil are crucial factors to support the performance of the economy in the short term.*

*The strength of the macro policy is necessary but not sufficient to overcome the current challenges. The second path the country should take is an inclusive development agenda. Some of the key criteria to define such an agenda should include, in an interrelated manner, the definition of a production policy focused on innovation, qualified human resources and productivity gains, financing schemes to channel national savings (collectively, to improve the financial system and the capital market), the development of adequate infrastructure, the strengthening of enterprise development, and fundamentally, a social assessment of public spending to reverse social and regional inequalities.*



## DEVELOPMENT OF NEW COMPETITIVE CAPABILITIES

### Conceptual Framework

*in the new millennium, ARCOR has developed a set of coordinated actions for a long-term strategy aimed at the constant generation of higher value. This process is characterized by a move towards a more “intensive” pattern of specialization in the use of skilled labor, based more on domestic technological efforts while focusing on production of greater added value and differentiated goods. The results allow broad social inclusion, with the creation of new jobs and a significant contribution towards economic development.*

*Companies look for more flexible and innovative strategies, forms of organization, and production in order to deal with the increase of globalization and changing consumer preferences. To achieve this goal, it is not enough to incorporate modern technologies, but rather, it is generally necessary to adopt new forms of organization in research, design, management, production, branding and commercialization processes simultaneously. This transformation process is complex, proceeds unevenly, takes specific characteristics depending on the sector, region and country, and involves causalities and interactions not yet fully understood. However, different analyses have shown, in the empirical field, that there is a link between the adoption of new forms of productive organization, skills training and human resource training, and gains in productivity and competitiveness.*

*Competitiveness is an ongoing challenge for the company. The possibility of accessing increasing levels of competitiveness and keeping them in the long term cannot be confined to the action of an individual economic agent.*

*According to international experience, successful cases are explained by a set of variables which clearly prove that the overall performance of the system allows the achievement of a sound basis for the development of competitiveness. Thus the “systemic notion” of competitiveness replaces individual efforts, which, though they are necessary to fulfill this goal, must be accompanied by countless aspects composing of the entire business environment (including the physical infrastructure, the technological-scientific system, the network of suppliers and subcontractors, the distribution and commercialization systems, cultural values, institutions, and the legal framework). Competitive capabilities are characterized by the product of a collective and cumulative process over time.*

*Techno-productive capabilities are not only the technologies “incorporated” into the hardware or into manuals and patents acquired by the company, though these are the tools through which the capabilities are put to work. Such capabilities are neither the educational qualifications of the employees (though a receptive base for the acquisition of capabilities depends largely on the education and training of the personnel involved) nor are they isolated skills and training of individuals within the company, although these are the building blocks of capabilities at a micro level. They are the way in which a company combines all of the above to function as an organization, with a constant interaction among its members, effective flows of information and decisions, and a synergy greater than the sum of individual knowledge and skills. It is conceptually useful to consider the development of competitiveness in the company as an investment in “incorporated” technology, accompanied by investments in skills, information, organizational improvements, and interrelationships with other companies and institutions.*

*These considerations also serve to extend further and deepen local integration including the development of local suppliers and subcontractors. Apart from the production benefits, these interrelations accelerate the diffusion of technology, increase specialization and manufacturing flexibility and generate employment. Due to these externalities, the related chains of activities fuel economic development. This systemic notion of competitiveness is relevant for each of the markets in which it is considered. Therefore it must be obtained in export markets and in relation to potential imports.*

*The international scene shows the increasing importance given to knowledge networks regarding the development of dynamic competitive advantages. In recent years, while a new paradigm was consolidated (intensive in knowledge and information), there was a discussion on the competitiveness of agents acting in an interrelated manner, as opposed to those who act individually. In this regard, a review of recent works confirmed the complexity of developing these networks, partly due to the increasingly less public nature of knowledge and the learning process carried out by agents. The new networks are characterized by a large flow of information and specific knowledge, not only among their members, but mainly with companies and institutions that do not belong to them.*

*One crucial aspect is the fact that learning processes do not arise automatically over time. They are precisely the positive outcome of deliberate*

*and explicit efforts aimed at generating technological assets and training human resources. This implies the development of a technological and productive strategy associated to investments aimed at creating/adopting permanent technical changes, leading to a non-automatic or instantaneous development which requires permanent and conscious efforts. The adoption, diffusion, adaptation and generation of scientific and technological knowledge are neither automatic nor individual processes. They require deliberate efforts in a complex, collective and cumulative process over time, involving (in an interactive manner) companies, public and civil society institutions, businessmen, workers, research institutions and universities, and among others, all of which constitute the so-called National Innovation System (Sistema Nacional de Innovación).*

*Thanks to the conceptual developments of the “new theory” of economic growth, such growth is explained largely by the ability of economies to generate and incorporate knowledge and technology. This is done by, the education and training of the work force, the changes in the organization of production, and by the institutional quality. A significant part of the production competitiveness is based on the way in which the various stages of production and commercialization, from the basic input to the final consumer, are coordinated. For this reason, it is necessary to build and strengthen production networks in the following ways; firstly, by encouraging the development of linkages of suppliers and commercialization chains; secondly, by coordinating investments in complementary assets within the networks; and lastly, by promoting greater product and service differentiation, and incorporating quality improvements along the production chain. All of which can be achieved by means of the interaction among companies, the information shared, and the joint identification of improvements in production, since it is not always easy for companies to notice the benefits arising from networks and cooperation, especially when they are focused on the problems of short-term competitiveness. This leads to an expansion of the markets, with increases in productivity and creation of jobs.*

*In general, the actions taken so far by the different countries in order to increase the competitiveness of their economies seek to directly attack the so-called “price factors” (cost of capital, labor, tax, and exchange rates). However, they do not consider the elements that make it sustainable in the medium and long term and that are key to sustained growth, such as policies that promote technological innovation, investment coordination, pro-*

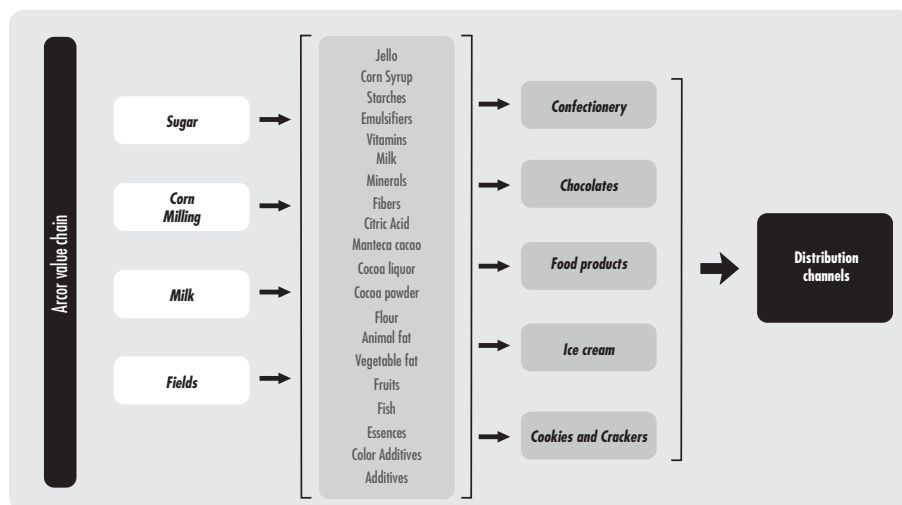
*duction and trade specialization, improved differentiation, quality of the production of goods and services, and institutional infrastructure; that is to say, the variables known as “non price” of competitiveness.*

*In the following sections, some aspects of the performance of ARCOR Group in the development of dynamic competitive advantages will be discussed, showing the possibilities that developing societies have of taking an active role in the globalized world.*

### Added Value Chain in the Food Industry

Argentina is a worldwide leader in the production of raw materials for the food industry. However, one of the remaining challenges is to increase the use of those materials in chains of greater added value and in product differentiation, thus strengthening its industrial platform and creating more wealth, more skilled labor, and more availability of foreign currency. ARCOR Group has proven the feasibility of advancing in the creation of value with food products, brands and product differentiation, and shifting from “the grain to the trademark” and from “the commodity to the product offered in the aisle”.

#### Value chain

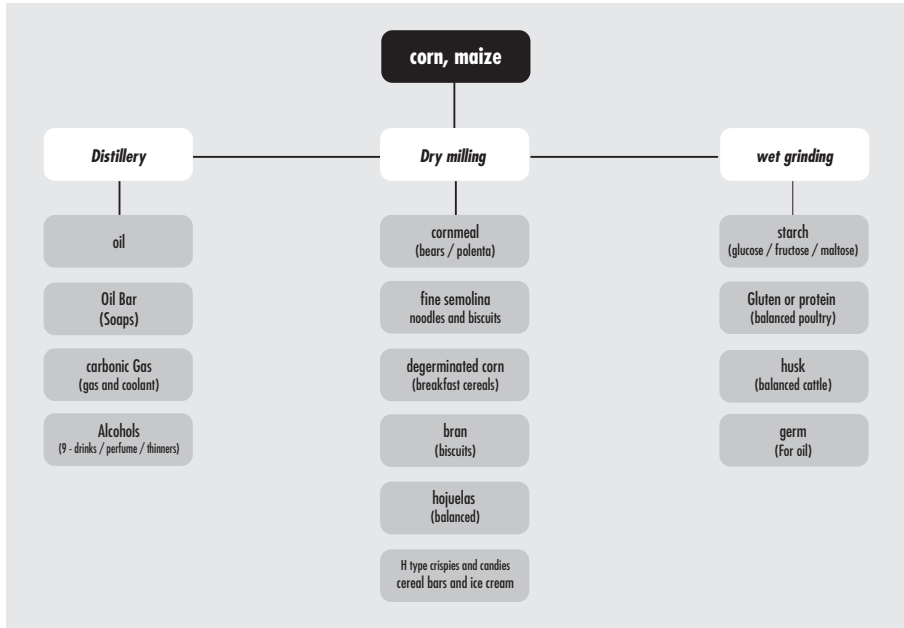


One of ARCOR's strengths is its vertical integration in Argentina, achieved by the production of strategic raw materials such as corn, sugar, milk, and corrugated cardboard and by the printing of flexible containers. Its self-supply of raw materials complying with international and technical standards of efficiency and sustainability is boosted by, its network of 29 industrial plants (all of which are certified under the ISO 9001 and ISO 14001 international standards), by the hiring of over 10 thousand small and medium enterprises (SMEs) as suppliers (thus fully availing the division of labor with economic specialization), and by its sophisticated world-class distribution network. All this allows the ARCOR Group to take a leadership and competitive position. Today, the company produces over three million kg of food products per day and is regarded as the No. 1 company in the commercialization of food in Argentina.

Taking into account some representative cases, it is possible to evaluate ARCOR's remarkable progress towards the production of differentiated food products. Hence, in the case of corn which goes through a wet milling process, the four essential components of that grain are separated to be transformed later (mainly with the company's own manufacturer) into other by-products. Glucose and fructose corn syrups (basic ingredients for candies) and maltose (used for the brewing industry) are produced out of starch. Balanced dietary food for birds and cattle is produced out of gluten and corn grain pericarp. Corn germ is sent to the distillery located at ARCOR's plant in San Pedro, and then transformed into oil and oil dregs to produce soap. From the corn distillation process, carbon dioxide (to prepare soft drinks) and 9 varieties of ethanol (alcoholic beverages, beauty products and diluents) can also be obtained. At the dry milling plant, the following products are manufactured; corn flour (useful to manufacture polenta and for the brewing industry), fine semolina (noodles and crackers), degermed corn (breakfast cereals), bran (crackers), pellets (balanced dietary food for birds and cattle), and type h krispies and confectionery (cereal bars and chocolate/ice-cream stuffing).

Another example is the transformation of tomatoes and peaches at four industrial plants: ARCOR, San Rafael; Frutos de Cuyo, San Juan; La Campagnola, Choele Choel; and La Campagnola, San Martín (Mendoza). These plants process 122,000 t of tomatoes on 1,500 ha, transforming them into 69,500 t of goods, they also process 16,000 t of peaches on 650 ha transforming them into 10,900 t of goods.

## Corn Scheme



Moreover, ARCOR Group:

1. Has seven dairy farms equipped with automatic milking systems with 2,800 cows, producing 28,000,000 L of milk per year, for the production of chocolates and candy.
2. Owns a sugar mill, milling 1,500,000 t of sugar cane from 25,000 ha, obtaining 138,000 t of sugar per year, and thus being the 4<sup>th</sup> largest sugar producer in Argentina.
3. Transforms wheat at its cracker production plants (Salto, Villa Totoral and Campinas) where 180,000 t of wheat flour are used to manufacture 236,000 t of cookies & crackers per year.

Cartocor and Converflex, companies initially created as part of ARCOR's vertical integration process to ensure packaging for its products (since packaging is a strategic raw material for its productive integration), have turned into separate businesses. Cartocor, a company that produces cardboard boxes (main manufacturer of corrugated cardboard in the country, today using 10% to 15% of its capacity to satisfy ARCOR Group's needs), places the rest of its production in the national and regional markets, mainly for wine and fresh

fruit exporters. On the other hand, Converflex, a company that produces flexible containers, sells 20% of its products to third parties.

### **Technological Capabilities and Operations Management Systems**

One of ARCOR's characteristic features is that, since its origins, it has been an innovative company. This has reinforced its position as a leader and competitive company. Between 2002 and 2012 its way of operating was consolidated through the systematization of work in long term innovation projects having basic and applied science as pillars, in order to achieve an increasing progression towards differentiation, with greater added value and sustainability. The innovation process has been integrated into ARCOR's business management culture as an essential element. Its goals are represented by an inclination towards nature, shown by functional food products and dietary supplements (innovation in products and food ingredients technology), by the use of renewable resources in packaging (innovation in packaging, design, new polymer technologies and additives), by primary production and more efficient manufacturing processes (innovation in fields, agribusiness management, genetics, pesticides, industrial processes, new technologies regarding equipment and control, management innovation), and by the approach to every consumer (innovation in logistics, sales, data). In order to achieve these goals, ARCOR has around 140 employees engaged in research and development (R&D). They are approximately 100 people in Argentina and the other 40 are distributed across Brazil, Chile, Peru and Mexico.

The work guidelines are set up by the Technological Liaison Corporate Management area (*Gerencia Corporativa de Vinculación Tecnológica*). On the one hand, it develops activities of constant **Technological Vigilance and Competitive Intelligence**, so as to be permanently updated and to be able to understand events, scientific publications, competitors' actions in the scientific and technological fields, and patents developed internationally. It has a plan of systematized reports defined as the strategic axis of the company, performing requested searches, developing the company surveillance platform design to be implemented, defining search engines and data analyses and takes part in new business projects. It has fostered two Business Cooperation Projects (*Proyectos de Antena de Vinculación*), one of them in the plastics area jointly with the Argentine Industrial Union (*UIA*), and the other jointly with the Argentine Ministry of Science and Technology extending through several related sectors.



On the other hand, in the last decade the **Technological Liaison Corporate Management** has been deepened as a mechanism to generate technological capabilities within the company itself. Seventy projects were created jointly with other companies. Among them, 37 were carried out through strategic associations with multinational innovative companies (for example, Basf, 3M, Cargill, Dupont) and national leading companies (such as Bagó, Gador, Sidus), thus supplementing this new essential aspect which characterizes this stage of the company. This type of integration facilitates and accelerates innovation, thus being able to enter into exclusivity and technology exploitation agreements. Moreover, its interaction with the National System of Science and Technology has been increased, comprising over 30 projects, being worth mentioning the permanent activities with the following institutions: the Argentine Ministry of Science and Technology, the National Universities of Córdoba, del Litoral, Luján, La Plata and Cuyo, the National Institute of Industrial Technology (*INTI*) and the National Institute of Agricultural Technology (*INTA*). These activities are related to technology and products, as well as management and processes, which are strategic matters that have a positive impact on the company. As a supplement, the creation of internal, external and mixed work networks have been increased. ARCOR takes part in the company's innovative activities in different influential spaces, such as chambers, forums, congresses, fairs, decision making tables regarding innovation policies, courses and conferences, thus proving to be a trustworthy model clearly identified as a leader in the consolidation of the innovation climate.

Moreover, the most important aspect in this area is the **Administration of Innovation Projects**, which in 2012 amounted to 42 initiatives. The management area supports the business units that adopt projects previously conceived and with major probabilities of success, by executing the corresponding agreements, forging alliances and protecting the intellectual property rights that may arise or be exchanged between the different parties. These projects comprise actions aiming at: health and nutrition, environmental protection, agricultural management tending to certified agriculture and to the consolidation of the value chain, imports substitution, and quality and differentiation improvements.

Some of ARCOR's examples of innovation include the following:

Topline Chewing Gum containing fresh gel. The freshness line is used to turn it into gel, thus taking advantage of ARCOR's experience with gelatin and pectin-based candies. It is the first chewing gum with such characteristics.

Isomalto-oligosaccharide syrup (*IMO*) is a corn syrup developed at ARCOR, with soluble fiber with low molecular weight, prebiotic effects and low in cal-



ories. This project was carried out jointly with the CERELA (Reference Center for Lactobacillus- CONICET), the University of Buenos Aires, CEPROCOR (Center of Excellence in Product and Processes of Córdoba), among other institutions belonging to the Argentine Scientific Technological System.

The company uses compostable and renewable resources-based containers to progressively replace PVC containers, which generate dioxin. They also produce flexible containers by Converflex, jointly with NatureWorks (Cargill subsidiary, resin supplier), and with Dupont, Basf, and 3M (special additives suppliers).

On the other hand, ARCOR Group has created the ARCOR National Award for Food Innovation in 2009, as part of its Technological Vigilance and as a means of linkage with the National Innovation System. This prize is to be awarded on a biennial basis, which is why it has been presented only twice (2009 and 2011), being a success both in participation and federalization since more than 25 projects were exhibited and institutions from all over the country took part in each contest. This award is supported by the National Agency for Scientific and Technological Promotion of the Argentine Ministry of Science and Technology.

In a supplementary way, ARCOR Group is characterized by its leadership in the use of IT applied to business management and to the consolidation of its competitive advantages. In this context, one of the most significant events has been the implementation of integrated and modern tools for the management of its operations.

In 2009, ARCOR defined a program of strategic actions so as to transform and improve efficiency and to add value to technological solutions. Prior to this program, in 2002, ARCOR had created the Single Payment Center (*CUP*), a shared services center where all the company's payments are processed with high traceability, control and efficiency. Moreover, between 2002 and 2006 the industrial processes and costs of the entire group were integrated into a single process map with JDE technology.

By 2008, after purchasing La Campagnola and entering into a joint venture with Danone to create Bagley, it was necessary to provide a better support to its business lines in order to prepare them for permanent improvement and value solutions that the industry would demand in the years to come.

This gave rise to a strategic transformation plan called Antares Program. The various industrial plants and offices had different versions of JD Edwards (the company's ERP), some had internal development applications and a very complex but poorly integrated data map. Following Antares aim, the company therefore decided to globalize processes and to homogenize technology, as-

simulating the best practices for each stage. Thus, all systems were unified into the latest ERP (JD Edwards) version, with a single and comprehensive model that complied with every business requirement and legal regulation of each country. Four hundred staff members from all the areas of the company took part in the development of this program, and global consulting firms with experience in solutions for mass consumption industries were hired. These consulting firms were from the United States, Canada, Colombia and Australia, and joined the internal team in order to face the challenge. Besides, a strategic partnership with Oracle was consolidated, for both software supply and hosting and operational services. ARCOR Group joined the Oracle Development Direct Customer Program for JDE clients, as well as three Oracle Advisory Boards specialized in industry capabilities, thus showing once more progress in alliances to manage ARCOR's businesses.

Among the newly introduced tools the following stand out; JDE E1 9.0, Siebel, Demantra, and Oracle's BPEL. The reporting and consolidation of strategic information and the company's business intelligence continued to be based on MicroStrategy. With regards to infrastructure, since Antares was launched the company decided to *climb the cloud*, also known as cloud computing: that is, to take all productive and administrative movements to a virtual net located outside the company's limits, therefore allowing users to have a workplace, regardless of their location. A net of virtual servers were set up, managed by third parties thus minimizing operations and the impact of updates. The cloud contains all transactions made by the industrial plants and business offices in the country, extending from purchase orders of a supplier to picking (code reading) of an order prepared for a client, as well as the weighing of trucks that transport goods. It also keeps the company connected to banks, tax agencies from every country and with customers and suppliers for the electronic exchange of data. To sum up, the Antares Program is an integrated and modern tool for the management of ARCOR's operations, generating synergies through the integration of processes and data centralization and the ability to come up with global business solutions. The actions it has developed are vital to build competitive capabilities that may support ARCOR's consolidation as a world-class company. Thanks to Antares, ARCOR Group has defined and implemented a strategy to attain such progress in consistency with its innovative and cutting-edge history.

## Human Resources

The deep changes that the company has suffered during this new millennium have redefined and strengthened the significance of its human resources as a

fundamental pillar of its business strategy. Thus, it fosters the well-being and progress of its work team, which is essential to the competitive advantage of the company. Alliance formation processes, international operations in different environments, acquisition of companies and ARCOR's growth have presented major challenges. Thus, employment growth was very dynamic: in 2011 ARCOR had 12,880 employees, whereas in 2012 that number increased to around 20,000. These changes and increments meant multiple and coordinated endeavors. The review of overlapping duties, needs for new skills, the spread of the best practices aiming to harmonize existing heterogeneous features, the redefinition of the organizational structure, training programs, and the internationalization of employees, among other elements, required systematic actions based on a strategic point of view.

The main challenges in human resources were faced consistently with ARCOR's business goals. In the first place, a value proposal was outlined in order to attract, train and retain professionals to support and foster growth, particularly abroad. Besides, a development and succession plan was conceived so as to design replacement charts in leading positions. There was a search for efficiency and growing profitability, which meant training employees to sustain it. One of the goals was to ensure that corporate culture be in line with the reality of the markets and the company's values and strategies, introducing the concept of economic, social and environmental sustainability into business management.

The value proposal was grounded in the development of a global remuneration policy based on the adjustment to the market average and on the sorting out of "key" employees. Moreover, the creation of a company attractive to professional development with opportunities of growth, strong investment in internal communication, improvement and training, organizational stability, management autonomy and full implementation of meritocracy, was contemplated. In turn, special attention was placed on the creation of an inspiring work environment, fostering participative leadership in cooperative, diverse and innovative work conditions as well as creating a balance between an employee's personal life and work. Social responsibility and ethics have always been priorities in every action. The aim was to develop practices based on the company's values and that may promote an adequate working atmosphere and a corporate culture that facilitates its strategy to attract and retain talent.

In 2012, ARCOR had more than 20,000 employees, being one of the main industrial employers in Latin America. 13,000 people worked in Argentina, 4,000 in Brazil, around 2,000 in Chile, almost 1,000 in Mexico, and about 1,000 in the rest of the world. In Argentina, more than half of the employment concen-

trates were in the cookies & crackers, candies and food products business units. In 2012, the annual payroll exceeded USD550 million. On a national level, as a consequence of the different production organization models and economic conditions of the countries, it was possible to verify heterogeneous levels as regards to productivity and wages and salaries. In this case, Argentina stood out due to its greater figures for both indicators. It kept employee turnover at a lower level than that of the market, with relatively young staff members and a progressive professionalization, all this evidencing its transition from a family company to its consolidation as a world-class company.

Obtaining a job at ARCOR is possible through reliable and clear procedures that include; advice from consulting firms, advertisements on web sites, trainee programs and agreements with Universities. In 2011, the “ARCOR Internal Search” program (*BIA*) was launched in all the companies belonging to the Group in Argentina, international business units and southern subsidiaries. This program aimed at the development of human resources, by identifying the best talent for a certain position and at the same time addressing the employees’ concerns regarding promotion prospects. Simultaneously, it was consistent with the objective of considering all employees as part of the company as a whole and not limited to their current job positions. With this system a high coverage rate has been achieved; particularly in Brazil, where due to the Internal Opportunities Program, a coverage rate of almost 80% has been attained in recent years. In addition, the principles of equality of opportunities for disabled people are being considered during the processes of selection and employment of workers. This project also makes provisions for the gradual adjustment of buildings, equipment, systems and processes under the universal services principles. In 2012, six industrial plants set specific objectives for the employment of disabled people, and the company kept on supporting the labor inclusion program carried out successfully in Brazil and in the Salto plant (Province of Buenos Aires).

ARCOR created many key tools to align its employees’ professional development with the company’s strategic goals. The Strategic Resources Planning Program (*PRE*) was launched in 2007 to train and retain significant talents, contributing to the long-term sustainability of the business. The talent pool comprises of more than 430 employees; it is a biennial process that has given very positive results, where the substitution of managers has been analyzed and the critical positions and possible replacements have been identified, thus favoring the progress of staff members inside the company. In 2012, 85% of job vacancies were occupied by workers inside ARCOR.

On the other hand, 100% of the employees annually receive a performance evaluation, which affects their wages and their development plan. Such evaluation is conducted through the Performance Management System (*SGD*), which since 2011 has incorporated the sustainability variable within the managerial and executive levels of the Group. Thus, those employees who were trained in this matter had to include in their annual performance plan at least one specific sustainability goal contributing to the Policy adopted by the company. As a result, more than 600 employees from managerial and executive positions included around 700 sustainability goals in their annual plans, convinced that their work could contribute to making ARCOR a sustainable company. Some of the ideas presented as performance goals were: reduction in the use of water and energy; promotion of sensitization and awareness-raising on sustainability; substitution of packaging materials, reuse and recycling; nutritional improvement of products; promotion of healthy lifestyle habits; relationships with the community; inclusion; and diversity. The *SGD* evaluation of the personnel outside the collective agreement is supplemented with a performance management system implemented by each business unit for the employees under the collective bargaining agreements. In this context, employees receive an annual recognition for their performance in relation to their evaluation results, thus answering to the employees' concerns with regards to their prospects of growth.

In relation to the job position, performance and development plan of each employee, ARCOR implements training programs that address the needs of each business unit, plant or country, in line with the company's strategy. Through ARCOR University, launched in 2008, the company has a strategic tool to consolidate the capabilities of the Group, promoting classroom and e-learning training programs aimed at all employees. Activities have been carried out in more than 20 programs for capabilities development, leadership and training, and the program's evaluations showed a satisfaction rate of 85%. Specialization schools were created, extending across the management, industrial, commercial, administration, human resources and finance areas. At the management school, a range of programs were conducted, from top management programs to leadership programs for employees. One of the most recent projects is the creation of the technical school organized by specialties. To mention a few which stand out include: the "Industrial School", which started with a focus on maintenance and quality areas, and will extend to the rest of the specialties; the "Packaging School" (particularly regarding flexible containers) and the "ARCOR-Mode Marketing Academy". Considering train-

ing indicators, in 2011, training courses for a total of 392,967 man hours were run, with an attendance of 14,843 people; an average 22 training hours and 85% coverage of employees.

Within this framework, and based on ARCOR's sustainability strategy's second pillar, apart from the corporate training programs, education spaces related to sustainability were created. This includes the Leadership Program, the Induction Program, the Sustainability Mini-site within ARCOR University's website, and the training of 35 multipliers. The latter facilitated the development of a network of sustainability facilitators in the entire group so as to communicate its policy in a top-down manner. The internal training and sensitization on sustainability represent a fundamental axis for the Group's strategy. This is why the company has been working since 2005 in the development of different corporate and specific sustainability programs as a key element for the construction of a corporate culture committed to that matter. With this goal in mind, during 2011, 2,963 employees took part in 11,199 training hours, amounting to 19,865 participants in 44,628 hours since 2005. On the other hand, the formation area provided by ARCOR University is supplemented with different training programs and courses (a major part of them offered at an industrial level within the context of the Integral Management System), that cater for the specific needs of each country and business.

Another significant event worth mentioning is the creation of the Corporate Communication Management in 2006, aimed at harmonizing communication within the organization and developing all channels (on-site and digital) required to achieve fluid communications between the various levels of the organization, reinforcing the Group's strategic goals in every stage. Thus, a group of over 30 experts in internal communication was set up and can be found in all organization bases, ensuring an adequate flow of communication.

In order to deeply understand this subject in general and ARCOR's strategy in particular, and to increase the generation of initiatives to promote sustainable development, the company launched the second stage of the Communication and Sensitization Program in 2011. Within this framework, a group of 35 staff members called "multipliers" was formed and trained, and the group was entrusted with the coordination of communication meetings about ARCOR's Sustainability Strategy and Policy, addressed to analysts and supervisors. As a result, 1,858 people were sensitized in Argentina, Brazil, Chile, Mexico, and the international division. The next steps will be to continue with its diffusion so as to reach every plant in the Group.

Moreover, within the Work Environment Management process which started in 2007, several internal communication meetings were conducted in the industrial plants as a channel to listen to concerns and suggestions and to foster communication and integration among the different hierarchical levels of the company. The goal was to develop practices based on the company's values and that promoted an adequate working atmosphere and a corporate culture that facilitated its strategy to attract and retain talent. In 2011, more than 3,200 employees attended 256 meetings, with a 98% satisfaction rate, proving the employees' high approval of this channel of communication. The Group moved forward with the communication of the Organizational Environment Survey results. Thanks to the results of the survey *and of different surveys made by other areas, plans of action to be worked on were defined, in line with the following pillars: Quality of Life, Leadership, Recognition, and Rewards. Almost 80% of the plans of action set for 2011 and 2012 were fulfilled or are under way.*

#### Human Resources – 2012 Average

Region	2012 Average
Argentina	13,034
Brazil	3,808
Chile	1,945
Central – Mexico	139
North and Overseas	57
Southern Subsidiaries	202
Peru	258
Ecuador	83
Mundo Dulce	865
<b>Total</b>	<b>20,391</b>

The position of *Corporate Executive* Director of the company was created in 2010, consolidating the professionalization process of the Group. The company has a multidivisional structure, of the holding type, organized in business units, geographical areas and functional units; and a manager with great autonomy power is in charge of each area. There are 12 general managers



who report to the director, who, in turn, reports to the Board of Directors of the company. The result is a growing decentralization of roles, within the concept of integral company, constantly working for the creation of interaction for the construction of a wholly articulated business strategy. The creation of competencies, professional development and the recruitment of the best talent are part of the company's constant change. The company must be inserted in the local and global contexts of business strategy development. The way to go is paved with enormous challenges and it is necessary to constantly redefine the organizational structure of those responsible for the high management in order to achieve articulation with the company as a whole. International careers and the regular change of high management executives are essential to renew, in an appropriate way, the growing competition. The recruitment of the best human resources, the young professionals' plans, the care of work relations, a management culture, and constantly assessing the Group's sustainability are a few of the challenges appearing in the near future.

### **Environmental Management**

Since the establishment of ARCOR Group, its pioneers understood that economic progress was necessarily tied to social development and to the conservation of natural resources. That firm belief evolved and took different forms as time went by, and it was marked by certain facts which may be considered key in the achievement of the development of the environmental management that it enjoys today.

This process has two precedents in the 1990s. In 1992, the Group joined 10 leading companies in founding the Argentine Corporate Council for Sustainable Development (*Consejo Empresario Argentino para el Desarrollo Sostenible - CEADS*), as a replica of the World Business Council for Sustainable Development, with the aim of promoting, contributing to and spreading sustainable development in our country. In 2012, *CEADS* included 69 leading Argentine companies. The second milestone took place in 1994 with the creation of the *MAHPI* Management (Environment, Hygiene and Industrial Protection) with the aim of defining and coordinating environmental and work safety management, in the corporate sector, with the aim of becoming a world model regarding good hygiene, safety, environmental and plague control practices.

*MAHPI* is a way to manage the environment (disposal or reduction of adverse impacts), hygiene (healthy and comfortable work environments) and industrial protection (people's safety). The main scope of action is in factories, warehouses and the communities where the factories are located. The management has three pillars that support it: 1. compliance with environmen-



tal and work safety legislation; 2. eco-efficient industrial operations, and 3. work risk control.

In 2004, ARCOR became part of the promoting group (holding a leading position) which created the Global Compact local network, committed to the United Nation's 10 corporate social responsibility principles. By 2012, 370 organizations had joined, shaping the country's biggest network and one of the main networks internationally.

Considering the mentioned facts as a frame of reference, the organization and the defined work methodology were used to complete an approach which allowed the development of an environmental management system considering constant improvement in its widest sense. This organization is contemplated in the Integral Management System (*SGI*) which the Group designed and adopted as a methodology for industrial management.

The system is based on six components which constitute the main pillar on which it is structured: 1. Commitment and Leadership in Management, 2. Customer and community orientation, 3. Process Management, 4. Committed Human Resources, 5. Reliable suppliers, and 6. Constant improvement.

The company's aim is to use the SGI in all plants in order to achieve the best results regarding efficiency and loss, environmental care, the best quality possible for the consumer, a workplace free of risks for the staff, and the personal and professional growth of our people, based on continuous learning. In 2012 there were 33 plants which had obtained and maintained the ISO 14001 International Standard for Environmental Management Systems certification, and 18 with the OHSAS 18001 Occupational Health and Safety Management certification.

The signing of the ARCOR Sustainability Policy in 2011, as analyzed in the next section, provided the structure for activities and in depth planning, while taking into consideration, the commitments taken on and the entire value chain. The starting point was the creation of the Risk and Opportunities Matrix, which summarized the critical sustainability issues considering a medium-term scenario, which led to the definition of the five specific commitments. Three out of the five commitments were directly related to environmental management; namely, rational use of water, energy efficiency and the minimization of impacts that contribute to global climate change, and rational use of packaging.

In the corporate sector, specific initiatives have been defined to be developed and completed in the next five years. Some of them include; calculation of carbon inventory for the whole company, energy efficiency program to reduce the emission of greenhouse gases, environmental analysis of packaging, and calculation of the water footprint (the only program which has not been launched yet).

## From Corporate Social Responsibility to Sustainability

### *Corporate Social Responsibility*

Social responsibility has been part of ARCOR's identity since its creation. Already in those times, a development model which balanced economic achievement with the contribution of social and environmental value was a priority. Sustainability measures have been consistent with the Group's origins, which refer to its founding identity and are characterized by its family origin, social sensitivity, entrepreneurial spirit and effort culture. ARCOR's history of growth and success is defined in its values and principles, which reflect the company's way of being, thinking and doing. In all its corporate documents; integrity, commitment, respect, reliability, and leadership are laid out as essential values, which have led to a business development in daily practice with consistent ethical principles.

This decision of the Group to be a relevant and responsible member of the community motivated the concern for the implementation of socially responsible practices, and the creation of ARCOR Foundation in 1991 was a significant milestone in this process. In an organized and corporate way, the Foundation focuses its work on social interventions which promote better education opportunities for boys, girls and teenagers in Argentina. In its long history: it has supported 2056 projects which had, as main beneficiaries of their initiatives, 2.6 million boys, girls and teenagers throughout the country; it has combined its work with more than 2,000 organizations; it has been awarded 18 prizes and honors for its work; and the Group has supported and published 172 childhood-related publications.

The main focus of the work with children, through private social investment (which implied the company's voluntary contribution of its financial, human, technical, managerial and/or in-kind resources, in a planned and evaluated form, for the public interest) has been based on:

- Contributing to the integral development of childhood from a perspective based on rights.
- Placing emphasis on education: choosing education as a key tool in the creation of better opportunities.
- A community approach, turning each community into an educational opportunity haven for the integral development of its children.

In 2004, ARCOR started working with the aim of creating a shared vision regarding corporate social responsibility (CSR) throughout the company. In that same year, the Group created Brazil ARCOR Institute, which also fo-

cuses its efforts on the support of children through education. Since 2004, the Institute has accompanied 316 educational projects and has reached more than 1 million children and youngsters from 16 Brazilian states.

In 2005 ARCOR decided to systematically include CSR at all company levels: from its business policies and management to the relationship it has with each one of its target audiences. Two key milestones set the basis for the consolidation of socially responsible practices in its activities: the start-up of the Corporate Social Responsibility Program in 2005 and in 2006, the creation of a specific corporate management team to manage it. Since 2006, all ARCOR's efforts have been aimed at aligning and integrating existing practices, promoting co-responsibility of the parties involved and establishing a management system. Another important milestone arrived in 2006, when the Corporate Social Responsibility Management succeeded in systematizing, for the first time in 55 years, the Group's history and its aims in a sustainability report, an annual report which accounts for the manner in which the company works on different CSR initiatives. In 2007 ARCOR gave a great step towards the systematization of its community actions: it developed and approved ARCOR's Social Investment Policy (*ISA*), which established the criteria that guide the channeling of resources destined to the integral development of the communities where it operates.

### *Sustainability*

In 2009 ARCOR Group set a new challenge: going from the concept of CSR to that of Sustainability. From this evolution onwards, two main challenges were sought to be faced: on the one hand, having a clearer view of the value and the advantages of sustainability for the business, and, on the other hand, promoting a cross and integral management of these issues in the company. This implied knowing the main risks and opportunities of sustainability for the business in the long term, developing innovative initiatives according to the business needs, and creating a context which favors the development of business in general. Within this framework, we have worked on the elaboration of the Sustainability Plan and Strategy for the coming years and on the definition of ARCOR's Sustainability Policy.

ARCOR's Sustainability Strategy is made up of three pillars: sustainability of business strategy, staff performance and management system.

- Sustainability in business strategy: to integrate environmentally and socially responsible actions throughout the value chain, in an innovative and proactive way.

- Sustainability in staff performance: to promote, support, monitor and assess the performance of the company's employees from the perspective of sustainability.
- Sustainability in the management system: to set up a sustainability management system across all areas of the company.

The Sustainability Policy consists of a general commitment to sustainable development and five specific commitments to the most relevant and primary issues; rational use of water, energy efficiency and the minimization of impacts that contribute to global climate change, rational use of packaging, respect and protection of human and labor rights, and active life and healthy nutrition. All these achievements, apart from creating value for ARCOR's interest groups and society as a whole, have had a positive impact on business management. They have contributed to brand value and to the company's reputation, to the improvement of the economy of costs and productivity, to the strengthening of the company's human capital, to facilitating the access to new markets, and to the management of risks and reinforcement of the operating license.

By means of sustainable management, the company develops bonds with the different groups it relates with, promoting long term and reliable relationships (stakeholders):

- Employees: Occupational safety, health and environmental management, training, strategic resources development program, internal searches program, actions addressed to staff members' children, inclusion programs for disabled people, and a gender project.
- Suppliers: Training and sensitization actions, responsible inclusive purchasing project, project against child labor, supplier strengthening and development actions. Agro sustainable program.
- Customers: Training and sensitization actions. Strengthening and development. Inclusive business projects in stores ("almacenes"). Sustainability plans for distributors.
- Consumers: Customer services, meetings with consumers, adherence to advertising self-regulation codes. Marketing projects with social impacts.
- Community: Relations with more than 14,000 social organizations. ARCOR Foundation, Institute and Community Relationship Program actions (in 22 communities in Argentina and Chile).
- Participation in public spaces: Active participation in more than 60 chambers and business organizations. Active members of the UN Global Compact, RedEAmérica, International Food Bank Network, and Business Network against Child Labor.

## A PLACE IN THE WORLD

### **Mercosur Integration Process**

*The economic integration process between Brazil and Argentina started in the mid-1980s with a set of regional agreements. Later, both countries decided, together with Paraguay and Uruguay, to create the Mercosur. Initially a free trade area, Mercosur soon became a customs union when a common external tariff came into force in 1995 (although the countries could still apply special duty regimes to a set of excepted goods). Towards the mid-nineties, the continued growth of intra-regional trade since the beginning of the decade, the initial success of the stabilization program for the Brazilian economy, and the fast recovery from the Argentine financial crisis in 1995, encouraged a hopeful outlook regarding the economic performance of Mercosur. Mercosur member economies expanded production, trade boomed, and local and foreign investments in the domestic market increased. This outlook changed abruptly due to the effects, on the region, of a series of financial and trade disturbances derived from events such as the East Asian crisis in 1997, the Russian financial problems in 1998 and the Brazilian devaluation in 1999. The management of the crisis and the recovery process in the new millennium modified the context once again. So, economic relations may be divided in three periods: firstly, the period of the Argentina-Brazil bilateral approach and the democratization of the second half of the 1980s, secondly, the period of the opening and ongoing expansion of trade up to the end of the 1990s, and lastly, the crisis and recovery period.*

### ***Democratization and Bilateral Approach in the Second Half of the 1980s***

In the mid-eighties, political incentives played a catalyst role in the process of economic approach between Argentina and Brazil. Particularly, the Argentine democratic government that took office in December 1983 saw the rejection of the hypothesis about a conflict with Brazil and Chile as a key step towards limiting the influence of the armed forces in national public life. This transition to a cooperative view was facilitated by the Corpus-Itaipú tripartite agreement (1979) and by other initiatives from the early 1980s (such as the agreement for the development and pacific application of nuclear energy in May 1980), but it grew stronger with the launch of the

Economic Cooperation and Integration Program (*PICE*) in 1986. The conclusion that both countries shared similar economic problems (stagnation, macroeconomic instability, productive specialization patterns and external strangulation) also helped to consolidate a vision that underlined the existence of converging interests. This more cooperative environment was strengthened by the almost simultaneous transition to democratic governments in both countries.

Asymmetry in the business share in the respective markets had been a consolidating feature since the 1960s: in fact, between 1981 and 1985 Argentine imports from Brazil already represented 14% of total imports, while Brazilian purchases in Argentina represented less than 3% of the imports, with a clear asymmetry in the specialization patterns. Additionally, in the late 1970s, primary products (especially temperate climate agricultural products) made up almost two thirds of Argentine exports to Brazil, while Brazilian exports to Argentina were, essentially, manufactured products (72.5%). As a result, the *PICE* set in motion instruments for gradual liberalization, trade administration and productive complementation which would ensure a more balanced expansion of trading and would reverse the prevailing tendencies toward inter-industrial specialization.

At the beginning of the process for bilateral economic integration, economic determining factors showed a positive net balance magnified by the expectations that the Brazilian economy might play the role of an “engine” for Argentina, and by the attraction exerted from a large and protected market. On the other side, the reserves that might arise as a consequence of the dissimilarities in size, market share, and specialization were at first withheld by integration instruments which emphasized the administration of trade flows, economic complementation, intrasectoral specialization, and the dynamic balance of trade. These economic considerations were boosted by political factors which granted additional attraction to the development of a more intensely cooperative bond with Brazil.

### *Opening and Expansion of Trade in the 1990s*

*Towards the end of the 1980s, PICE implementation problems had already outlined two alternative visions among those encouraging a deeper economic integration with Brazil. On the one hand, a “commercialist” vision which encouraged the gradual liberalization of bilateral trade and the restructuring conducted by the market, prevailed. On the other hand, an “in-*

dustrialist" vision which complemented the trade liberalization with active industrial and technological policies coordinated between both countries, consolidated. The new Argentine government that got into power in 1989 was the prime mover of a new "commercialist" orientation which, from then on, defined the bilateral cooperation process. The Buenos Aires Act (July 1990) brought about a radical change in the integration methodology and coincided with a period of reform and unilateral opening in both countries. The act and its methodology of automatic and generalized liberalization were adopted without changes by the Treaty of Asunción (March 1991) which created Mercosur and incorporated Paraguay and Uruguay.

In this reformed atmosphere at the turn of the decade, Argentina also appeared as a "modernizing" country, by means of an ambitious reform program which contrasted with a neighbor who could not get rid of its heavy "developing" baggage. The differences in the Argentine and Brazilian visions about the evolution of the integration process were clearly reflected in the debate regarding the customs union. The Treaty of Asunción set a deadline for the constitution of the "customs unions". An influential government sector and private actors did not like the adoption of a common external tariff and the loss of autonomy to develop preferential business negotiations with third parties which was implied in the agreement for the customs union. During this period, Argentina and Brazil's positions regarding the international trade agenda such as the Initiative for the Americas and, later, the FTAA, showed differences. Finally, in 1994, Argentina accepted the adoption of a CET which reflected the Brazilian tariff, subject to exceptions and long transition periods.

During the first years of the Mercosur, the negative aspects of the intensification of the economic bond with Brazil were softened for various reasons. On the one hand, the general framework of unilateral opening and domestic reforms cushioned the impact and the visibility of the effects of preferential liberalization. Furthermore, many low productivity sectors in Argentina were protected by a list of sensitive items (temporarily exempted from the liberalization program) or the introduction of safeguards. Specific decisions such as the modification of sources of energy or wheat supply on Brazil's part were also useful to reduce the instability of a bilateral balance of trade which was an increasing deficit for Argentina, in a context where Argentine exports to Brazil doubled in a five-year period.



*Asymmetry in the specialization patterns of both countries did not suffer modifications during this period, which was consistent and compatible with the general tendency towards “primarization” which Argentina’s total exports showed. Nevertheless, trade in Mercosur did not only show higher intra-industrial trade rates than the rest of the regions, but Brazil also appeared as a destination for the exports of some fast-growth manufactured products (such as automobiles and chemical products). The fast growth period of bilateral trade during the mid 1990s matched the beginning of a stage of regulatory paralysis and a growing “implementation gap” in Mercosur. Soon after the beginning of the implementation of the customs union, the difficulties to adopt the common external tariff and to “deepen” the business negotiation agenda of the countries were clear.*

*Asymmetry in size had a particularly beneficial influence in the mid-nineties, when the real appreciation of the Brazilian currency and the strong recovery of economic activity which followed the implementation of Plan Real had a very positive impact on Argentine exports, helping the country to recover from the effects of the “Tequila crisis.” In fact, the consequences of this fast expansion would dominate the bilateral bonds for the next three years: As a result, in 1998, Argentine exports to Brazil represented more than a third of total Argentine exports and improvements were registered in the Brazilian market share in virtually all production segments. Therefore, the asymmetries in market share and specialization also softened their most negative impacts, eclipsed by the fast growth of bilateral exchange.*

*After the de facto convergence of macroeconomic policies caused by the Plan Real, asymmetries in production policies played, once again, a central role in the bilateral agenda. In fact, the restoration of active sectorial and horizontal policies by the central government and sub-national administrations broadened the gap with the policies’ system prevailing in Argentina. Besides, after the Russian and South East Asian crises, costs for the maintaining of the currency board system became higher and more evident; in a time when both economies were facing, for the first time since the beginning of the integration, a strong recession. The result was that this set of asymmetries had very distorting effects on trade and investment incentives, which remarkably expanded after the devaluation of the Brazilian Real.*



### Crisis and Recovery

*Generally, the devaluation of the Brazilian Real in January 1999 is considered the starting point of the most troubled period in bilateral economic relations of the last two decades. After the crisis, in December 2001, and especially after the new government of President Lula came to power in Brazil, political understanding between both governments remarkably improved. However, interest in finding political balances to the relationship with Brazil did not disappear: during Kirchner's administration, the search for a privileged relationship with Venezuela became one of the ways to shape that strategy. As attempted with Chile a decade before, the Argentine government activism was looking for the incorporation of Venezuela to Mercosur.*

*During this period, the negative impact of dissimilarities in size, market share, and specialization became particularly important. The increase of inter dependency seen in the 1990s and its asymmetry magnified the effects on Argentina of the subsequent macroeconomic crises which struck the region since the end of the 1990s. Furthermore, after the collapse of the currency board, Brazilian imports share in the Argentine market reached much higher levels than before the crisis. At the same time, Brazil's share as a destination market for Argentine exports fell and Argentina's share in the Brazilian market systematically decreased.*

*The increasing share of imports from Brazil in some industrial sectors (worsened by the fast recovery of domestic demand in Argentina after 2002) encouraged defensive responses by means of the implementation of mechanisms such as the trade flow monitoring, the application of voluntary restrictions to exports, and the implementation of ad hoc protection measures. During this period, concern about the offshoring of industrial plants to Brazil grew enormously. This emphasized the fear of an aggravation of the inter-industrial profile of specialization in Argentina in comparison with Brazil.*

*Dynamism in Brazilian investments in Argentina in recent years has been a relevant microeconomic phenomenon. The modes of arrival of those flows had mostly to do with M&A transactions and on a lower scale with production capacity expansions. Among the motivations of Brazilian transnational companies for settling in Argentina, the following ones stand out; the need to accompany the transformation processes of the sector on an international scale, the possibility of reaching new markets (which are, besides,*

*relatively protected) and raw materials in good quantities and quality, access to new consolidated distribution channels, and the utilization of the advantages offered by a wider market. Beyond the quantitative magnitude of the process, a limited degree of productive integration is seen, which implies a low level of business specialization and complementation.*

*Despite the new ideological convergence regarding the role of active policies, the sharply defensive interventions adopted in Argentina and the prevailing institutional inertia made regulatory asymmetries (especially regarding their efficacy) not to be materially modified. The identification of common interests in an agenda of “productive” integration and the recognition of Argentine demands for “reindustrialization” did not materialize in concrete instruments, but in practice, they legitimized a strongly defensive agenda. Instrumental divergences in a context of global ideological convergence were even expressed in dissimilar positions in international forums such as the Doha Development Round, in which Argentina adopted a much more defensive position than Brazil.*

*In summary, during the most recent period, economic constraints acquired a more negative slant than in the past. Although size asymmetries did not increase, those regarding market share and specialization remarkably did. Even though the prevalent vision of today is that Brazil continues to be a key economic partner for Argentina (a vision magnified by the increase of direct investments in the last few years), the Argentine agenda has become essentially defensive.*

*The factors that condition the dominant perspectives about Brazil in Argentina are related not only to the bond between both economies but are also related to the wider international context. Although the global context has changed dramatically in recent years, it has not altered a fundamental principle: the bond with Brazil will continue being essential for Argentina in the future. If anything has changed in these last 20 years, it would be that such bond has become more relevant and complex. For these same seasons, a strategic vision to grasp opportunities and minimize risks is needed. In turn, Argentina is a fundamental space for a successful insertion of Brazil in the world.*

*It is widely accepted that the main source of dynamism of the world economy in the future will come from a few developing countries, and, especially, from some large economies which are going through strong demographic and productive transformations. Brazil is one of the countries in*

*this sub-group. In the last two decades its production apparatus has become more complex, new capacities have been developed in non-traditional areas (such as agro-industry and energy), and its macroeconomy has become less volatile and more sustainable. As a result of its geographical, population and economic dimensions, Brazil has also become a relevant international actor with a voice in several fields which include business, finance and the environment. Nevertheless, and despite the growing asymmetries, Argentina keeps a strategic interest boosted by the development and consolidation of new interests in the business and investment sectors. The long-term interests that must be promoted to strengthen Mercosur should be pointed out.*

### **Development of Business in Brazil**

Since its origins, ARCOR Group has considered Brazil as a strategic market. This long-term vision gave an impulse to the first export efforts in the 1970s. In 1981, the Group acquired Nechar Alimentos Ltda.; a candy company located in Rio das Pedras, Sao Paulo, which was considered a traditional Brazilian factory that manufactured 5,000 kg of goods per day. Three decades later, in 2012, as a result of this focus and strategic commitment, ARCOR Brazil became a competitor established in the Brazilian food market; as an example, producing 240,000 kg of sugar confectionery goods per day. The company manufactures more than 300 products, in the four categories in which it participates; food, sugar confectionery, cookies & crackers, and chocolates. All of which, amounts to 163,000 tons per year, with a leading position in many market segments. It is a leader in the children chewing gum market; the fourth brand name and the third chocolate manufacturer, competing with the main global companies. It is one of the most significant cookies & crackers competitors and the main exporter of confectioneries from Brazil. In order to develop this active presence in the Brazilian market; the company has five manufacturing plants, around 4,200 employees, four distribution centers, six regional offices, and a network of 93 distributors which cover the whole country. To face the challenges this growth brings along, it was necessary to make important efforts and follow basic teachings, which include:

- A thorough understanding of the national market, its constituent segments, consumption culture, needs, habits, attitudes, prime movers, occasions, and channels.

- The development of new value propositions (brands and products) which should be innovative, different, recognized, and suitable for consumption characteristics.
- The need to reconcile the ideas of fast growth and those of profitability and self-financing.
- The creation of a distribution network with competitive service levels and costs, covering the regions and channels which are consistent with the strategic goals.
- Critical mass and efficient scale, permanently in line with the business model.

From this perspective, ARCOR Brazil's evolution may be understood as the answer to the challenges presented by the market and to competitive dynamics. So, during the first stage in the 1980s, the focus was on the candy and chewing gum markets, doubling candy production after the acquisition of Nechar. As part of this strategy, sometime later, sugar-coated chewing gum lines were installed and, a few years later, a complete chewing gum plant was built, where the base gum was produced. At the same time and following the practices and teachings of the exports strategy of Argentine operations, the first exports were encouraged. As a result of these efforts, at the end of the said decade, overall production volume went from six to one hundred tons per day.

Since the 1990s, factors such as the gradual knowledge of the market, the constitution of a distribution network, and the need to widen the client portfolio versus local and multinational competitors, all stimulated the entrance into the chocolate category. The development of ARCOR's competitive position in this segment started with an import process, which then allowed the diversification of the products line. Having achieved a great success, in 1999 the Group opened, the region's most advanced chocolate manufacturing plant situated in Bragança Paulista, thus consolidating itself as the fourth largest chocolate competitor and strengthening Brazil's exporting platform. A better knowledge of consumers and innovation allowed ARCOR, at this stage, to provide a better response to the market, by means of the insertion of products such as chocolates (bonbons), tablets, Easter eggs and children's chocolate. With this, revenues reached almost USD100 million by the end of the 1990s.

The innovation rhythm would be kept during the 2000s, including 20 launches per year, with the initial focus on chewing gum and then on chocolate, moving towards differentiated products in line with the defined strategy. At that time, the process of growth and diversification made the company face strong and protected competitors in several sub-segments of many categories

throughout Brazil's extensive territory. The challenge consisted of matching, profitably and growth to the investment levels needed to obtain the expected positions by developing brands. ARCOR responded by strengthening and extending its brands to reach efficiency with investments and by acquiring Kid's, Poosh, 7 Belo and Amor, which would ease access to a better presence and distribution in regions like Sao Paulo, in the center and south of the country. Additionally, the chocolate lines Chokko Snack were incorporated into the market. At the beginning of the decade, the company reached a leading position in the children chewing gum category. It also succeeded in regionally positioning itself with brands and products with global potential such as Butter Toffees candy, Big Big chewing gum and Tortuguita chocolate. Thus, the company reached a 90% market share in the milk candy category.

ARCOR's innovation processes in this period did not limit themselves to the development of products and brands, but implemented new and innovative marketing forms, linking consumer needs of products and brands with social causes. In this sense, since 2003, the company has joined an environmental project for the preservation of sea turtles and of aquatic life in general (TAM-AR-IBAMA) with the 'Friends of the Sea' campaign, an environmental education initiative to raise awareness of the protection of this species. The project's voice is a character called 'Tortuguita Tamar,' a sea turtle-shaped chocolate especially created for the campaign.

The strong expansion and growth process in this period was based on an important development in the customers-distributors network. This movement allowed ARCOR to go from 60 customers-distributors in 2000, to 93 today, covering 150,000 points of sale, with 750 distributors, being the key to balance its channel portfolio by increasing sales through customers-distributors. In 2005, when ARCOR entered the cookies & crackers market, activity levels reached 80 thousand tons per year and annual billing was of USD150 million.

Regional association with the Danone Group in the cookies & crackers business opened a significant opportunity in the biggest market in the region and the one with the biggest potential, being of special importance for ARCOR Brazil. The constitution of the new organization, in which ARCOR took on the operational management, included two production plants and enlarged the number of staff by almost 2000 people, which doubled production. The integration process secured synergies through the use of commercial strength, the attention to the supermarket channel, the incorporation of new customers-distributors to the network, an increase of the importance of the Group regarding sales, and the incorporation of valuable marketing skills. Bagley Brazil's

performance between 2004 and 2012 showed an increase in sales from USD77 million to USD150 million; in terms of Brazilian Reals (BRL), the growth was from BRL227 million to BRL353 million and volumes sold went from 69 thousand to 83 thousand tons. Within the Brazilian cookies market, which in 2011 had a production of 388,123 tons, ARCOR's share, with its Bagley-Aymoré-Triunfo-Danix and Break Up lines, was 6.7%. All this can be summarized as a remarkable dynamism in sales, which provided the Group with an essential critical mass in a market with minimum margins and which presented constant future challenges of value incorporation in order to achieve a dynamic revenue/profit equation.

In order to consolidate its presence, in 2005 the company entered into, the *Panettones* market. In 2007, the Campinas Distribution Center was inaugurated and the Recife Plant (in the state of Pernambuco) started operating for the manufacturing of chewing gum, lollipops and candies, which allowed the company to cater for the growth in the markets in the North and Northeast of the country. In addition, efforts for the promotion and valorization of the brands were made, including the participation of very well-known artists. Significant efforts were also made in the human resources area, recruiting young executives with previous experience in key positions in first-level transnational corporations and a strong entrepreneurial motivation, who were encouraged to participate with greater freedom in the strategic management of the business base, strengthening the sales and marketing divisions and the management team. These incorporations went hand in hand with the creation of a company which should be one of the best workplaces in Brazil. Training was reinforced, including a corporate post graduate education program. An important asset of the group is the multitasking aspect of the work done by the staff, which requires great motivation to deal with the efforts necessary to act in a market with strong competitiveness on the part of world leading companies.

During recent years, there has been a significant strengthening of the Brazilian domestic market, boosted by very favorable international exchange terms and an upward social mobility process, which implied that an additional 50 million people reached a purchasing power previously unknown, creating in Brazil, a powerful and massive domestic market. In this context, ARCOR's competitive response allowed a very positive performance. Some of the most relevant indicators for the 2001-2012 period were:

- Sales in BRL multiplied four times, going from BRL232 million to BRL970 million. In dollars, numbers showed a growth from USD99 million to USD553 million. In actual volumes, the increases went from

56,630 tons to 162,976 tons. This dynamism in sales was associated with a greater penetration in the domestic market, keeping export levels above USD30 million per year.

- The opening of new plants, distribution centers and acquisitions were possible through a vigorous process of investment, of almost USD140 million in each stage. In addition, occupation doubled, reaching almost 4,200 employees. Chocolate production grew from 8,000 tons to 19,000 tons, maintaining a 5% share in the dynamic and competitive Brazilian market. Chewing gum production went from 17,000 tons to a maximum of over 25,000 tons, with a market share around 45%. In candy, a maximum production of 16,000 tons per year was reached, with a market share of around 16%. As mentioned before, cookies sales in dollars tripled, with a 6.7% market share.

This performance allowed ARCOR to start enjoying positive profitability results in 2012, after three decades of competitive efforts. Brazil is a key market in the company's strategy. In order to achieve a competitive position, it is necessary to develop strategies which allow the company to stay and grow, with increasing profitability, within the privileged group of the five or six highly professionalized global companies operating in the country, together with around 300 smaller companies. Organic growth is not enough. The challenge is to combine volumes, but focusing on a growing market share of more differentiated products. Brazil's particularities, because of its size, the active competition of the largest world competitors, and the particularities of the market imply the development of a business model in a highly competitive context.

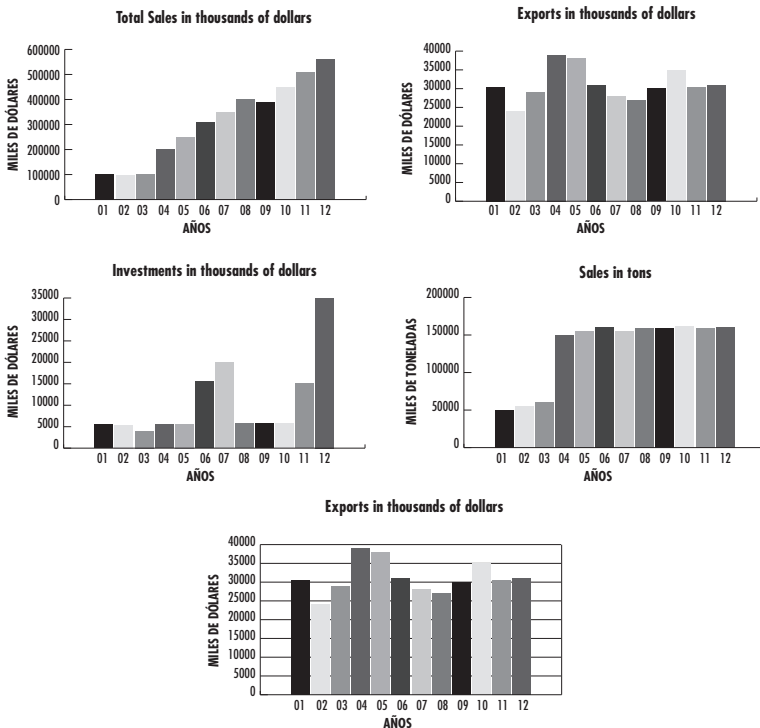
In this context (highly competitive and in which the company tried to position itself in the highest segments with growing positive results recently), systematic actions were taken, in 2012, which were materialized at the end of the year with the strategic strengthening of Bon o Bon, one the emblematic brands of the company. 70 staff members in a multifunctional team worked together for several months systematizing tasks for: 1. marketing, with a USD15 million investment for the development, of the brand, of flavors, and of knowledge of market features; 2. packaging, with the development of a more environmentally friendly container, with a high percentage of renewable sources, with an ultrasound seal to achieve excellence in the preservation of the product, and with an easy-opening system, and 3. an investment process which, together with other products, reached USD85 million, for the improvement of efficiency and increase of production in industrial plants.



ARCOR Brazil's success will mostly depend on the consolidation of its market position based on its historical innovation and distribution skills; searching of efficient strategies; and cost and capital available to deal with local and multinational competitors in the great Brazilian market. Thus, the strategic agenda of ARCOR Brazil includes important challenges and opportunities. It becomes necessary to maintain and deepen its insertion in Brazil by means of the development of its business and corporate social responsibility initiatives, like the ones ARCOR Brazil Institute has been developing in the educational field. Progress achieved in the last decade is auspicious for the long-term consolidation of the Group in Brazil, but, at the same time, experience teaches us that competitive challenges allow no pauses. Challenges consist in collective practices with permanent focus on enhancing the development of critical skills, training and recruiting human resources, innovating, developing marketing and distribution, and investing in order to position the brands and differentiated products. All of which are sustained by an international topflight production model.

### ARCOR main indicators-Brazil. 2001-2012

*In millions USD and tons*





## **Towards a Global Company - International Expansion**

With an early urge to export and having been one of the first companies from the developing world to go international through foreign investments in industrial plants and distribution-commercialization channels, and together with the vision of the world as its market, ARCOR Group succeeded in consolidating itself in the international market and has a brand presence in more than 120 countries in 5 continents. ARCOR is a leading multinational group with 39 industrial plants in Latin America (10 of which are outside Argentina) and 13 commercial offices around the world. The international expansion of the business is still a central pillar for its growth. The company maintains its strategy for expansion of international markets; positioning ARCOR as the Argentine group with the highest number of open markets in the world; the biggest sugar confectionery exporter of Argentina, Brazil, Chile and Peru; going global and forging strategic alliances with leading companies. Comparing the 1996 and 2011 sales, a growing relevance in international presence can be observed. The Argentine market share decreased from 79% to 63%, while the Brazilian market share increased from 12% to 18%, the Andean Region from 3% to 9% and Mexico represents today 4% of world sales.

Export values just about doubled between 2002 and 2012, from USD200 million to almost USD400 million. Nearly half of these exports are destined for South America, with an outstanding growing market share in Africa and Asia, which today represent almost 20% of exports, with values in dollars having grown around 300% in the aforementioned period. Also, around half of the exports are made into the international production and distribution network of the company (intercompany), while the rest of the sales correspond to third parties. From Argentina, around 50 million products for industrial use are exported (mostly containers), and the remaining values correspond to sugar confectionery, chocolate, and cookies & crackers, for final consumption. Two thirds of exports have their origin in Argentina, while the remaining third is divided between Brazil, Chile and Mexico.

### *Actions Beyond Latin America*

With the ability to carry out business in a highly competitive framework, to meet the local needs and to integrate globally, the North–Overseas Division (which includes the United States, Canada, Europe, Africa and Asia) bases its strategy on reaching the markets, with global brands, with the ability to adapt, with competitiveness, and while working together with the best distributors.

The business strategy guidelines arise from the definition of a combination of strategic countries: Angola, Congo, Mozambique, USA, Canada, South Korea, China, UAE, Philippines, Vietnam, Thailand, Eastern Europe, Israel, India, Saudi Arabia and the Iberian Peninsula, with core brands such as: bon o bon, Butter Toffees, Blow Up!, Rocklets, Plutonita, Mr. Pops, Menthoplus.

In its process of bringing markets together, ARCOR's strategy has been to create human groups made up of expatriates able to transmit ARCOR's know-how in the operations abroad and of local staff members who, based on the knowledge of the local market, help bridge the cultural gaps. Thus, in 2002, ARCOR added (to the already existing commercial offices in Miami, USA [1993] and Ontario, Canada [2001]) a branch in Barcelona, Spain, as a means of giving special emphasis to Europe and the Iberian Peninsula, being the first office opened outside the Americas. In 2006, after three years with a home office in South Africa, a new commercial office opened in Durban, attending, mostly, to the sub-Saharan Africa markets. In that same year, ARCOR established a representation office in China, a key location in order to start a period of regional exploration. The said office would, in 2011, evolve into a subsidiary to operate directly in the local market, without intermediaries, achieving a greater flexibility and control over operations. Furthermore, in China, ARCOR carries out the repackaging of products from Argentina, Brazil and Mexico to be commercialized in the domestic market. In this way, the subsidiary keeps the added value of the repackaging, which the importer used to keep. The result is much more customized presentations for the Asian consumer in general, but with the original quality of the products. Additionally, still with the aim in mind of settling in the markets in order to achieve closer relationships with customers, home offices are opened in; Dubai, United Arab Emirates (2006); Casablanca, Morocco (2007); Bangkok, Thailand (2008); Lucknow, India (2009); Luanda, Angola (2010); Ho Chi Minh, Vietnam (2010); and most recently, Accra, Ghana (2012), incorporating the trade marketing and country managers figures.

Revenues evolved from USD68 million in 2002 to USD173 million in 2012, which implied a cumulative growth at a compounded 10% annual rate. This was made possible thanks to a sustained growth in the different regions in which the business operates, facing different contexts of economic, political, and social crises, with the following estimated annual revenues for 2012: the Iberian Peninsula, USD4 million; the USA, USD50 million; Africa, the most dynamic region, over USD53 million; Europe, USD11 million (93% growth as compared to 2002); India and the Arab World, USD18 million; and Asia

Pacific, USD30 million (440% more than in 2002). The reasons for this growth are based on the company's presence in the main markets, through offices and periodical visits; with the focus on those products with a greater potential in each region, and special attention on the core brand names and the marketing investment for each portfolio.

Within the milestones, the following are worth mentioning:

- The massive advertising campaigns in Africa and the Arab World, which included TV, radio, press and outdoor advertising.
- The regionalization of the actions in trade marketing throughout the African continent (19 markets).
- The development of special packaging to compete in the gift pack category in the Arab World.
- ARCOR's first participation in Dubai business fair "Gulf Food 2010".
- The customization of production lines and flavors to suit the Asian palate, for example, a less sweet white milk candy.
- Regionalization of the Butter Toffees business in Asia, with China-HK basis.
- The successful commercialization and positioning in Japan, Korea, Thailand and Vietnam.
- In 2003, the beginning of a direct business relationship with the ALDI (a leading discount chain in Europe) to meet the needs of the markets in Holland and Belgium.
- In 2009, the opening of processes in the CIS countries (Georgia, Ukraine, Azerbaijan, Armenia and Uzbekistan).
- ARCOR's first participation in the Russian business fair "Prodexpo Russia 2009" and "World Food Russia" in 2010.
- The launch of the peninsula project, in which Spain, Portugal and Andorra became an independent unit.
- In 2011, mass distribution of Bon o Bon and "Alfajores" in Walgreens stores in the south of Florida.
- Contracted manufacturing operations in the USA: 1. With Nabisco in 2004, a business which ensured 3,000 tons of "Cream Savers." 2. With General Mills in 2004 for 3 years for the development and production of fruit snacks in Catamarca. The agreement implied an investment of USD2.5 million on the part of General Mills in equipment and infrastructure in the plant in Recreo, Catamarca, as well as the creation of 135 jobs at the plant. 3. ARCOR USA became the only supplier of hard candy lines for the three main discount stores when it acquired the private firm, Family Dollar business. Annual market value of these products is estimated to be USD25 million.

### *Chile and the Andean Region*

ARCOR Group started operating in Chile in 1989 with the setting up of a fruit preserve production plant. Ten years later, by means of an important investment, ARCOR consolidated a competitive position in Chile through the acquisition of Dos en Uno, a leading local company of sugar and chocolate confectionery, with an important international projection. This strategic operation positioned ARCOR as the main sugar confectionery company in Chile and as an important player in the chocolate and crackers industries. Besides, it allowed the company to significantly expand its product portfolio and strengthen its continental presence. Thus, between 2002 and 2012, sales went from USD94 million to USD212 million and exports grew from USD21 million to USD34 million.

Such dynamism was based on a brand strategy, in which certain key brands were chosen, mostly those with a higher contribution in value, in order to place focus on them. An important investment in advertising led to a very positive performance, which allowed for making a profit and increasing market share. Bon o Bon, Bigtime, Selz, Nikolo, Rocklets, Alka, Dos en Uno, Miti Miti and Cofler were among the most important brands sold. In the 2002-2012 period; the crackers market share went from 11% to 22%; the chocolate market share, from 21% to 24%; the candy market share, from 37% to 38%; and the chewing gum market share kept its leading position with over 90%.

Measures were taken to improve the distribution networks which replicated the Argentine model, starting with the Normandia project (2007-2008). An important modification of the incentives and the development of 57,000 points of sale were carried out, with a stable 75% coverage and weekly follow-up. Points of sale were massively modified with 20,000 items of furniture, for sales through impulse purchases of chocolate and sugar confectionery. In order to leverage this growth, ARCOR Group has planned a large investment into the opening of a high technology distribution center and for the development of a new distributors' channel, with growing professionalization; which has included a Business Development Program, given by professors from Adolfo Ibáñez University.

In 2007, a corrugated cardboard plant opened in San Francisco de Mostazal, with excellent facilities and equipment which allows the company to meet the growing needs of the Chilean market in a more appropriate way, relying on a production capacity of 80,000 tons of cardboard per year. Additionally, the execution of the strategic agreement with the Danone Group in 2005,

through which operations for cookies & crackers, “alfajores”, and cereal bars were unified, facilitated the creation of new opportunities for the development of the company in the country.

In 2012, the company had three industrial plants for the manufacturing of chewing gum, candy, cookies & crackers and chocolate. With the aim of increasing production capacity related to productivity improvements, the company has worked in spreading new processes for the automation and efficiency of industrial processes. The DoyPack packing line and ISO 14001 certification stand out, adding to the strong environmental commitment which, only in 2011, allowed an 8% reduction of energy consumption per ton produced. In 2012, the company set in motion the Bicentenary Project, focusing on the construction of a modern plant for sugar confectionery, chewing gum and chocolate. This plant will, cover a 22,000 m<sup>2</sup> area, involving an investment of USD50 million, and will be located next to the Cerrillo Distribution Center, the integration of which will generate efficiency gains. The project, the engineering, and the planning of this work have been developed by ARCOR’s own capacities. Also, systematic actions for recruiting and retaining the best talents have been developed.

In addition, the investments in Peru stand out in the Andean Region. Activities started in 1994, and in 1996 the Group opened the Chancay Industrial Plant, which originally produced candy and then expanded its production to chewing gum, chocolate and lollipops. The main brands commercialized are Topline, Privilegio, Golpe, Nikolo, Sapito, Bon o Bon and Mogul, which have allowed the company to achieve a preferential position in the competitive national confectionery market. Furthermore, a dynamism in Peru’s exports has been seen, increasing from USD3 million to USD5 million in the last decade, especially towards the Pacific basin. Systematic actions to recruit and retain the best talents were also carried out.

### *Mexico, Venezuela and Central America*

Activities in Mexico started in Monterrey in 1994. Later, in 2000, operations were centered in Mexico DF. Between 2001 and 2006, activities consisted of the import of products and wholesales. In 2006, the joint ventures agreement with Bimbo Group was signed, which included the construction of an industrial plant and, in 2007, Mundo Dulce started operating. The strategic alliance with Bimbo Group included industrial activity in Mundo Dulce as well as trade and distribution of Bon o Bon. Achievements were very significant. Consolidated sales increased, between 2002 and 2012, from USD11 million

to 112 million, with the participation of more than one thousand employees. Also, Mexico consolidated itself as the Group's exporting platform, for both customers and subsidiaries, representing, in 2012, 38% of revenues.

Mundo Dulce is the result of a strategic alliance arising from a solid business relationship between the companies, with the aim of coordinating their production and distribution capacities and of being able to meet, more efficiently, the market's needs. A new plant was built in the city of Toluca, specializing in the production of chocolates (bonbons), filled candies, chocolate bars, chocolate figures, lollipops, different kinds of chewing gum and recently incorporating the Butter Toffees and Wafers lines. It required a USD60 million investment and created nearly 900 jobs directly and 400 jobs indirectly. It covers an area of 30,000 m<sup>2</sup>, relies on 14 production lines with an installed capacity of 52,000 tons per year and produces more than 150 products, making it a leading plant in Mexico in the confectionery sector, and one of the largest in Latin America. It is an efficient industrial plant, with low transformation costs, which has allowed ARCOR to increase its exports to values close to USD50 million per year. These exports were originally directed to the USA and Central America but have since been expanded to 60 countries, from South America to Africa and Asia. Some of the main brands commercialized in the region are Bon o Bon, Nikolo, Sapito, Poosh and Butter Toffees.

Altogether, achievements since the beginning of operations in Mexico 12 years ago have been very positive. Sales have grown by more than USD100 million, it has consolidated itself as one of the Group's exporting platforms, for both customers and subsidiaries in a six year period, the industrial plant operates with price competitiveness, and a product like Bon o Bon has achieved a 35% market share in 5 years. Specific challenges include; increasing sales in the supermarket channel, consolidating existing brand names, strengthening the development of Butter Toffees as core brand of the Group, and continuing with the industrial development process. Also, all efforts are being made to strengthen distribution capacity, in a wide market, where demands are still much smaller than their potential and with strong competitive presence of the main world class companies.

Venezuela was a market supplied by means of the operations of importers. In 2002 the opening of the subsidiary was decided, but it was put off because of the "oil strike" and the institutional climate in the country, so the importers model continued until 2006, divided between the ARCOR and Dos en Uno business lines. Between 2006 and 2007 the subsidiary opened its doors with

the aim of managing both business lines. From this moment onwards a clear dynamism in sales has been noticed and sales have gone from an annual average of around USD5 million between 2001 and 2005 to USD38.7 million in 2012. In said year, candy sales reached USD7.8 million. These sales allowed a 7% market penetration. Furthermore, chewing gum billing was up to USD5.6 million. Chocolate lines sold USD15.1 million, which allowed the company to have, in the chocolate (bonbons) and chocolate tablet lines, around 13% of the Venezuelan market. This good performance led to a fast positioning of the brands in the local market, reaching important positions in the categories where it competed, supported by a remarkable distribution network.

In the Central American and Caribbean markets, ARCOR Group started exporting products to the region in 1996. In 2000 the company changed its model and became an import company, training local distributors, which turned it into one of the best copies of the model applied in Argentina. In recent years, with a consolidated distribution model, a new process for the development of brands started, involving important communication investments. The region has also been marked by its dynamism in the last decade. Sales, which in 2000 amounted to USD15 million increased to USD32.4 million in 2012. These revenues were distributed in the two regions in a very similar way. This achievement was based on the transition from the market management on the part of importers to the development of a distribution network. The huge recognition of ARCOR's brand name was a key supportive element: especially in the candy category (seen as high quality candy) which held, in 2012, almost 9% of the market; and in the chocolate category, which had a market share of 7%, the chocolate (bonbons) sector stood out as it had doubled. The candy segment generated 40% of sales, and the rest of the sales were divided in equal parts between the chocolate and chewing gum lines. Honduras is the market with the biggest sales, followed by El Salvador and Guatemala, with a strong presence of Cuba.



## FINAL COMMENTS

Sixty-two years have gone by since ARCOR Group went into business. Its evolutionary path of competitive capacity building has been characterized by a business strategy that advances firmly on the strengths previously developed, as well as change assessments within the economic context. In this long period, it has left the candy manufacturer behind and turned itself into, the main diversified foodstuff company in Argentina, a first world candy manufacturer, and one of the most important cookies & crackers companies in Latin America. From its original location in Arroyito, today ARCOR has a place in the world. This strategy has translated into an economic performance with outstanding achievements during the period of 2001-2012, which can be summarized as: three times more sales in dollars, two times more tons of products manufactured, and the opening of nine industrial plants.

The period analyzed in this section began in 2001 with a greater challenge. The Argentine economy was immersed in the decline of convertibility (one of its greatest historical crises) in a context marked by growing uncertainties, high volatility, and a deep social crisis and indebtedness, which reduced the economic horizons to the fullest extent. ARCOR Group showed an outstanding capacity to weather the storm and successfully get through it. Two business behaviors were essential to get through these hard times. Firstly, the Group's complete fulfillment of its agreements. Secondly, always taking all stakeholders into consideration in order to overcome these difficulties together, and understanding that business success goes beyond its own walls and involves its staff members, value chain and customers.

Once the company and the country could overcome this highly uncertain period, the Group implemented, from 2003 onwards, a strategy of growth and competitive consolidation with very significant achievements. A key milestone has been its capacity to develop highly complex strategic alliances in the business world, particularly those forged with Danone and Bimbo Groups, and many other examples included in this section. Apart from that, the acquisition of companies, the most important being the acquisition of La Campagnola which has strengthened its position in the diversified foodstuff industry. ARCOR Group has proven its high capacity to successfully manage these alliance and acquisition processes. It has deployed comprehensive reengineering in a highly professional manner to complement and adapt these new areas and human resources to its existing capacities and to promote its development with an increasingly competitive position in the foodstuff markets.



Regarding strategy development, it continued strengthening its internationalization process as a priority. The significant advances of its presence in the Brazilian economy are one of the major events of the last decade. Important investments, recruitment of human resources, the strategic alliance with Danone, and the strengthening of the distribution chain were some of the factors that have allowed ARCOR to develop new successful value proposals. At the same time, the strengthening of its international presence was accompanied by significant actions in Chile, Mexico (leveraged by its relationship with Bimbo) and the rest of Latin America. Simultaneously, its articulated export network throughout the world continued to grow, regardless of the situation, with total belief that foreign trade is the backbone of its long-term strategy. In 2012, ARCOR was still the Argentine company that sold to the greatest number of countries.

ARCOR's new production profile as a foodstuff manufacturer for the world was achieved through an articulated process for the development of its value chain. New products have been incorporated on an ongoing basis, and in the last few years the most notable products have been ice creams, powdered juice, cereals, and healthy products. The first step was a strong investment process into machinery and manufacturing organization models within the world's highest quality levels. And this was achieved by adopting a policy of profit reinvestment and successfully turning to the international capital market, where long-term financing was obtained. The development of different value chains were carried out with ARCOR's characteristic philosophy in mind. A vertical integration process included strategic supplies manufactured internally and produced with efficiency and sustainability levels within international technical frontiers. At the same time, it has relied on strong product differentiation with a brand capital developed through a truly remarkable marketing strategy. Its leadership position arises from the development of increasing projects on technological innovation, sustainable environmental management, and the implementation of up-to-date management operating systems. The marketing and distribution channel is also one of the key assets that were strengthened.

The manufacturing of differentiated food products has set the company as a concrete example on how to move forward in one of the key challenges of the Mercosur: shifting its specialization pattern to differentiated products with greater added value, use, and generation of foreign currency. The region is the main supplier of raw food materials in the world. ARCOR is an example of the possibilities of shifting from the "grain to the trademark", from the "com-

modity to the product offered in the aisle”, with world-class quality, efficiency and competitiveness.

As regards to its business model, it moved towards a decentralized organization with a multi-divisional scheme, similar to a holding company, articulated in business units, geographical areas and functional units, and the progressive professionalization of the company which was reinforced by the appointment, in 2010, of an executive director outside of the family structure. ARCOR’s staff members are the soul of the company and the increasing importance of the actions taken in the human resources area, articulated within an integral management system, has been central to the achievements obtained. Competence building, professional development, recruitment of the best talent, international careers, and among others, are the strong challenges which are faced while taking care, of the Group’s labor relationships and cultural values.

Finally, it is worth noting the creation of ARCOR’s Sustainability Strategic Platform, which strengthens relationships as a basis for development and protection of the environment, the community, and its people. The commitments taken on are: rational use of water; energy efficiency; rational use of packaging; respect for human and labor rights; and more recently, active life, nutrition, and healthy lifestyles. In Particular, it develops and promotes a balanced relationship with the environment by preventing and controlling pollution in the manufacturing processes and by implementing good practices in the value chain. At the same time, reliable and long-lasting relationships are encouraged, promoting a diverse organizational culture as well as the integral development of the communities with which it interacts, and generating childhood opportunities. The aim is to be identified as an exemplary group regarding sustainability matters, believing this to be an investment that strengthens both the value chain and business benefits, generating social benefits that nurture social and economic development.



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**The book analyzes** the evolution of ARCOR's development. Since the beginning of its operations in 1951, its road in the building of competitive capacities has been characterized by a business strategy that firmly advances on the strengths previously developed and an intelligent adaptation to the changes in the economic context. Throughout its long history, the original candy manufacturer turned into the main diversified foodstuff company in Argentina, and from its original location in Arroyito it has found a place in the world. Its evolution towards a world-class company is the evidence of the huge challenges and opportunities found in the lay-out of a business basis in a halfway developed country. The macroeconomic context, the institutions, the competitive features and conditions of the different markets

and the articulation of its value chain are just some of the decisive factors that explain its successful performance. At the same time, it is an example of the role companies play in inclusive economic development in Latin America. Its commitment to industrialization, technological innovation, the qualification of its human resources and environmental and social sustainability have provided Arcor with effective answers to contexts often characterized by volatility and uncertainty. Part of its success is explained by the fact that it has always taken into account all parties involved in its activities in order to overcome difficulties in a joint manner and develop its business strategy, stressing that its business success is possible when all players get involved: its staff members, its value chain, its customers and its consumers.



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