

PAGE ONE

## Brazilian Mining Titan Takes On Global Giants

Vale in Rare Stumble

As Earnings Drop;

Push Into Canada

By ANTONIO REGALADO

April 25, 2008; Page A1

RIO DE JANEIRO -- When [Companhia Vale do Rio Doce](#) arrived in the small Canadian mining town of Sudbury a year and a half ago, Mayor John Rodriguez recalls wondering: "Who are these Brazilians?"

As the Rio-based mining giant muscles its way to the front of the global business stage, more and more people outside of Brazil are finding out. In 2006, Vale swallowed Sudbury's biggest employer, nickel company Inco, for \$17.8 billion -- and set out on a campaign to win over the town's skeptical residents. Vale is now the world's second-largest mining company, and the biggest maker of iron ore, a key ingredient in steel.

Late Thursday, its push to diversify beyond iron ore came back to bite it. The company reported first-quarter net profit of \$2.02 billion, down 8.8%, which it blamed in part on a drop in nickel prices and losses from trading positions related to certain commodities. Vale's shares, which trade in the U.S. as American depository receipts, dropped 3.7% to \$35.95 in after-hours trading.

Like many mining companies, Vale is vulnerable to fluctuations in metals prices. But Goldman Sachs analyst Oscar Cabrera says Vale also struggled this quarter to boost production at the pace expected by the market, failing to produce as much iron ore and nickel as expected. During the second quarter, newly negotiated iron-ore prices are expected to boost revenue.

Emerging-market companies such as Vale have been climbing the ranks of the world's biggest and most successful firms in recent years. With China's booming economy boosting demand for raw materials and other commodities, companies like Russian steelmaker Severstal and Brazilian pork and poultry processor Perdigão SA have prospered. Prices for Vale's iron ore have risen by double-digit percentages in four of the past five years, and this year's price hike of 65% is expected to add as much as \$12 billion to annual revenue.

Using their new financial clout, these once-obscure emerging-market companies have been buying up firms around the world.

### Ahead of the Pack

Performance of Vale's American depository shares compared with the MSCI Emerging Markets index and the S&P 500.



\*In U.S. dollar terms through Wednesday  
Source: WSJ Market Data Group

1

Una cortesía de/Una cortesía do:

[DCabrera@TopExec.org](mailto:DCabrera@TopExec.org)

(011) 3711-2324 ou +1-954-382-6012 (FL, EUA)

# THE WALL STREET JOURNAL.

Last year, they struck \$294 billion of such deals, up from \$40 billion in 2003, according to research firm Dealogic. Brazilian steelmaker [Gerdau](#) SA bought Chapparral Steel Co. in the U.S. for \$4.4 billion. Mexican cement maker [Cemex](#) SA took over Australian construction group Rinker Group Ltd. for \$16.7 billion. Last month, India's Tata Motors Ltd. bought the Jaguar and Land Rover luxury brands from Ford Motor Co. for \$2.3 billion.

According to Dealogic, Vale's purchase of Inco is the largest-ever takeover by a Latin American company. In late March, Vale dropped its effort to buy Swiss rival Xstrata PLC for more than \$80 billion after the parties failed to agree on takeover terms -- a deal that could have made it the world's No. 1 miner, overtaking rival BHP Billiton.

Vale has been growing at a torrid pace. Last year, it hired 9,281 new employees in Brazil, leaving total employment world-wide at 124,013. It mined enough iron ore to fill 50,000 Olympic-size pools, and generated \$39.7 billion in revenue -- nearly 10 times what it did in 2001.

Between 2002 and 2006, Vale's average annual return to stockholders -- share appreciation plus dividends -- was 54.6%, tops among the public companies with market capitalizations of more than \$50 billion studied by Boston Consulting Group. América Móvil SAB, the cellphone operator owned by Mexican billionaire Carlos Slim was No. 2, followed by Apple Computer Inc.

## Commodities Bet

Until now, many investors have viewed Vale's stock as a way to bet on rising commodity prices. Vale was the third most heavily traded foreign company on the New York Stock Exchange in this year's first quarter, and the company says about two-thirds of its 420,000 shareholders are in the U.S. According to a February securities filing, Vale shares were the largest single holding of George Soros's Soros Fund Management LLC, which held \$238 million in shares.



**Roger Agnelli**

After Roger Agnelli took over as chief executive officer in 2001, Vale snapped up rivals in Brazil before the big run-up in iron-ore prices. When the boom arrived in 2004, the company was well placed to cash in.

Mr. Agnelli is a hard-charging executive known for his bear hugs and his penetrating stare. The company estimates he logs 800 hours a year on airplanes as he travels the world checking on operations and doing deals. Scott Hand, the former chief executive of Canada's Inco, said he offered the 48-year-old executive one piece of advice after the takeover: "Roger, stop and smell the roses sometimes."

Current and former Vale executives say Mr. Agnelli can be hard on subordinates. Some of them cite what they say is an autocratic style and a table-pounding temper. At least two dozen executives have left the company or been fired since Mr. Agnelli's

---

2

**Una cortesía de/Una cortesía do:**

[DCabrera@TopExec.org](mailto:DCabrera@TopExec.org)

(011) 3711-2324 ou +1-954-382-6012 (FL, EUA)

# THE WALL STREET JOURNAL.

arrival, former executives say. In internal company surveys, employees complain frequently that they are under too much pressure. Mr. Agnelli once told Exame, a Brazilian business magazine, that "it's very tough to convince a company that makes money that it should make even more money."

Mr. Agnelli declined to be interviewed for this story. Marco Dalpozzo, Vale's head of human resources, doesn't deny that Mr. Agnelli can be rough on people. "He's a tough guy," he says.

## **Sprawling Conglomerate**

Vale, whose full name means Sweet River Valley Co., was formed in 1942 as a state-run company, with loans from the U.S. government. It was part of a World War II deal in which Brazil agreed to supply minerals to Allied factories.

The state firm grew into a sprawling conglomerate. Brazil's government, dependent on the company's renowned technical skills, made Vale undertake projects unrelated to mining, such as pulping paper, according to several people familiar with the history.

In 1997, amid a wave of privatizations in Latin America, Vale was sold at auction for \$3.3 billion. The buyer was a consortium that included Brazil's largest steelmaker, Companhia Siderúrgica Nacional, or CSN, and banks and pension funds.

At first, CSN's chief executive, Benjamin Steinbruch, ran Vale as well, an arrangement that analysts say didn't result in a clear vision for Vale's future. In 2000, Banco Bradesco SA, Brazil's largest private bank and a major Vale shareholder, installed one of its own executives, Mr. Agnelli, as chairman. He helped engineer a share swap that eliminated CSN from the ownership group.

"Bradesco untied the hands of a giant," says J. Alberto Arias, a former stock analyst who now runs Arias Resource Capital Management, a private-equity firm specializing in mining.



Companhia Vale do Rio Doce's iron-ore mine in Carajás, Brazil

## Emerging Forces

Top 10 cross-border merger-and-acquisition deals announced since 2003, in which the acquirer was located in an emerging-market economy.

Deal value, in billions*	Announced Target (Nationality)	Acquirer (Nationality)
\$18.68	Aug. 11, '06 <b>Inco</b> (Canada)	<b>Companhia Vale do Rio Doce</b> (Brazil)
16.68	Oct. 30, '06 <b>Rinker Group</b> (Australia)	<b>Cemex</b> (Mexico)
14.32	Feb. 1, '08 <b>Rio Tinto</b> <sup>1</sup> (U.K.)	<b>Aluminum Corp. of China</b> (China)
11.60	May 21, '07 <b>GE Plastics</b> (U.S.)	<b>Saudi Basic Industries</b> (Saudi Arabia)
12.98	Oct. 17, '06 <b>Corus Group</b> (U.K.)	<b>Tata Group</b> (India)
9.50	Dec. 13, '07 <b>Dow Chemical</b> <sup>2</sup> (U.S.)	<b>Kuwait Petroleum</b> (Kuwait)
8.74	July 25, '05 <b>Ivax</b> (U.S.)	<b>Teva Pharmaceutical Indst</b> (Israel)
8.21	Nov. 29, '05 <b>Peninsular &amp; Oriental Steam Navigation</b> (U.K.)	<b>Dubai Ports World</b> (U.A.E.)
6.55	April 16, '07 <b>HSBC Holdings</b> <sup>3</sup> (U.K.)	<b>Saad Group</b> (Saudi Arabia)
6.55	July 1, '05 <b>Turk Telekomunikasyon</b> <sup>4</sup> (Turkey)	<b>Saudi Oger</b> (Saudi Arabia)

Note: Deals completed except where noted \*Excludes debt of target company  
<sup>1</sup>12% <sup>2</sup>Five Dow Global Businesses; pending <sup>3</sup>3.11% <sup>4</sup>55% Source: Dealogic

The company moved to develop a more focused strategy. Gabriel Stoliar, Vale's former executive director for planning, who retired from the company this week, recalls that during 2001 meetings of major shareholders, with consultants from McKinsey & Co. guiding the discussion, Vale adopted a straightforward plan -- become a global leader in metals such as copper, zinc and iron ore.

The plan didn't attract much attention at first. At that time, mining was seen as a sunset industry. Iron ore, in particular, was "very uneventful," says Mr. Arias. Annual negotiations between miners and steel companies rarely led to price increases of more than 3%, he says.

As a result, Vale faced minimal competition as it bought up Brazilian rivals in the iron-ore business. By 2005, Vale was responsible for 91% of Brazil's iron-ore production.

Vale's timing proved fortuitous. Steelmakers had long held the upper hand in price negotiations with ore producers. But booming demand from China turned the tables. Suddenly "there was a

Chinese on every corner looking to buy ore...and willing to pay any price," recalls Mr. Stoliar, Vale's former planning director. In 2005, the price steelmakers paid for ore rose 68.8%, nearly doubling Vale's profit that year. Ore prices have continued to rise, at a pace Vale executives admit they never imagined.

# THE WALL STREET JOURNAL.

The growing demand for metals plays into the hands of the biggest producers, which can make the investments necessary to open new mines, many in remote areas of politically unstable countries. The cost of mining also has been rising. Prices have leapt for everything from explosives to the big off-road tires used on mining trucks, which can cost about \$15,000 apiece. Vale estimates that the cost of opening Southern Range, a new Brazilian iron-ore mine that isn't yet open, has risen to \$10 billion, from \$2 billion several years ago.

"So you have got to be big," Mr. Agnelli said in February when discussing the company's 2007 financial results. "Small and medium can't grow production at the rhythm demand is growing."

To diversify beyond iron ore, Vale wanted to grow outside of Brazil, which has almost no coal and not much nickel. But the company couldn't raise money as cheaply as global competitors, Vale says, in part because rating agencies regarded its credit as riskier.

Mr. Agnelli courted rating agencies. Anita Saha, an analyst with Fitch Ratings, says Mr. Agnelli and his chief financial officer, Fabio Barbosa, were frequently in New York, ringing the bell at the stock exchanges and chartering planes for her and other analysts to visit mines deep in the Amazon forest. Fitch typically meets with companies just once a year, says Ms. Saha. Vale asked her for two additional meetings each year, she says.

In 2005, Vale received an investment-grade credit rating from ratings agencies -- something the Brazilian government still hasn't achieved. The rating enabled Vale to raise capital on the same footing as its rivals in developed economies. Vale swept down on Canada's Inco in 2006, breaking up a competing merger deal for the nickel maker with an all-cash offer.

Vale "came right out of the blue," recalls Mr. Rodriguez, the mayor of Sudbury, the Inco company town in Canada. "We knew nothing about them."

The Brazilians won over many in a town with a history of labor strife. The company donated \$375,000 to a local food bank and talked up the importance of employees. "You even had the accountants saying, 'If we are going to be taken over by anyone, it should be those guys,'" says Mark Cutifani, a former Inco executive who now heads miner AngloGold Ashanti Ltd.

At first, the Inco deal looked like a brilliant move, as nickel prices shot up early last year from \$15 to \$25 a pound. But since then, the price has fallen back to \$13. Adding to Vale's problems during the first quarter was a \$318 million loss on trades designed to hedge against price fluctuations of copper and aluminum. Add to that the dollar's rapid fall against the Brazilian real -- a decline of about 20% in 2007 -- which in effect made Vale's iron ore more costly to produce at home and less valuable to sell overseas.

## Port Accident

Thursday's earnings surprise wasn't the only setback in recent years. Last year, Vale missed its production target for iron ore for the first time, although the company said the shortfall was only

---

5

Una cortesía de/Una cortesía do:

[DCabrera@TopExec.org](mailto:DCabrera@TopExec.org)

(011) 3711-2324 ou +1-954-382-6012 (FL, EUA)

# THE WALL STREET JOURNAL.

1%. A port accident tangled exports for two months. Joaquim Martino, former director of Vale's huge Carajás iron-ore mine, says former co-workers tell him conditions at the mine are "less than ideal." Mr. Martino, who now works for a competitor, MMX, says he has seen photos of trucks stuck in mud in a mine pit, something he says he never saw during his 15 years there.

A Vale spokesman called Mr. Martino a disgruntled former employee. Mr. Stoliar says the company's production goals are aggressive, and despite problems including heavy rains, the company is producing more ore than ever.

Like many emerging-market companies, Vale can take advantage of low costs at home. It pays workers as little as \$470 a month.

But it also faces problems not shared by competitors based in more developed economies. As a former state enterprise, Vale is still viewed by many as a strategic asset of Brazil. Last summer, leftist politicians mounted a campaign called "Vale is Ours," calling for the company to return to state hands.

## **Farmers' Protest**

Last month, hundreds of poor farmers invaded Vale railway tracks, blocking transportation of 300,000 tons of ore. The farmers complained that the company's iron furnaces were polluting their village, and that a hydroelectric dam in which Vale is a partner was flooding their homes, among other things. Vale's policy: no negotiations.

Brazil's government still wields substantial clout over Vale. It holds "golden shares" in the company that gives it the power to veto such things as assets sales and any move of the company's headquarters from Rio.

So far, Mr. Agnelli has managed to navigate the domestic demands. The company spent \$251 million, or about 2% of its \$12 billion in 2007 profits, on social projects like sanitation systems, the vast majority of them in Brazil. It was the largest donor to the 2006 campaign of Brazil's leftist president, Luiz Inácio Lula da Silva.

Recently, Mr. Agnelli guaranteed that no matter what happens, Vale will "remain Brazilian."

**Write to** Antonio Regalado at [antonio.regalado@wsj.com](mailto:antonio.regalado@wsj.com)