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Strategy and innovation in emerging economies after the end of the commodity boom—Insights from Latin America☆

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ABSTRACT

This paper explores the economic trends of Latin America, highlighting their influences on the strategies and behaviors of different types of businesses. It introduces a Special Issue featuring a selection of the best papers presented at the Sixth International Conference on Strategic Management in Latin America, held at INCAE Business School in 2015. The theme for this Conference was: "Strategies for Growth, Regional Expansion and Global Competition". The Conference provided a big opportunity to exchange theoretical insights, empirical research results and applications of current Latin American strategic management issues.

1. Introduction

Between the early 1990s and 2014, Latin America went through a period characterized by positive economic performance, macroeconomic stability, and increasing visibility in the media (Ocampo, 2015). One of its two leading economies, Brazil, was included in the BRICS—the new emerging economic powers of the world—together with Russia, India, China and South Africa (Ciravegna, Fitzgerald, & Kundu, 2014; Stuenkel, 2014). Mexico and Colombia were included in other groups representing fast-growing emerging economies, the MIKTA [1] and CIVETS [2], respectively (Gonzales, 2014; *The Economist*, 2013). Both Brazil and Mexico are now members of the OECD. Poverty and extreme poverty have been reduced in most countries in the region, thanks to the positive effects of economic growth and targeted social policies, such as cash transfers (The World Bank, 2015). After several years of lethargic development, investments in infrastructure have increased, opening up new trade routes, with much-needed airports, railroads, ports, etc. Colombia's infrastructure, for example, was 25.4% higher in the first quarter of 2014 than in the same three-month period in the previous year (Nachiappan, 2014).

The consolidation of market reforms has supported the development of previously restricted markets, leading to a wave of acquisitions and the growth of multilatinas—Latin American multinationals, notably in banking, aviation, and energy (Dominguez & Brenes, 1997; Cuervo-Cazurra, 2016). Strong economic growth, driven partly by a commodity boom, fostered the expansion of domestic consumption markets, which generated opportunities for Latin American companies operating in a broad range of sectors, from food processing to retail to construction (Brenes, Metzger, & Requena, 2011; Carneiro, Rocha, & Silva, 2011; Ciravegna, Lopez, & Kundu, 2015). Building on their domestic fortunes, Latin American firms accelerated their internationalization to diversify their exposure, to achieve economies of scale and to conquer new markets. Several of these firms expanded in their neighboring VE countries, exploiting their understanding of regional consumer preferences, as well as the advantages of geographical and cultural proximity (Anand, Brenes, Karnani, & Rodriquez, 2006; Brenes, Montoya & Ciravegna, 2014). In industries not targeted to the final consumer, some global leaders, such as MarcoPolo and Embraer, emerged to challenge established competitors from advanced economies in the same way that Big Cola is challenging Coca Cola and Pepsi Cola in the Asian market (Bland & Schipani, 2014). Latin American firms changed their strategies, became more innovative, and contributed significantly to the region's growth and modernization by generating jobs, exports, and more-sophisticated products and services for Latin American consumers (Rowan et al., 2011; Brenes, Ciravegna & Montoya, 2015; Ciravegna, 2011).

By 2015, the context had changed dramatically. All emerging markets faced slower growth and different sources of instability. The

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slowdown of China's growth caused a dramatic fall in commodity prices, which affected Latin America's economy significantly. Brazil, once the powerhouse of Latin America, has entered its second year of recession in spite of hosting two of the largest sporting events in the world, the World Cup in 2014 and the Olympic Games in 2016. Oil exporters, such as Colombia, Mexico, Ecuador, and Venezuela, have suffered from the decline in oil prices from 100 US$ to 36 per barrel (Krauss, 2016). Although only a few countries, such as Argentina, Brazil, and Venezuela, entered into a recession in 2014, Latin America's economy is expanding at a much slower rate. Such a radical change in context sets the stage for the strategies and evolutionary trajectories that Latin American firms may take (America Economía, 2015).

Many Latin American businesses are in the process of successfully expanding their operations within and beyond their home country. This has been the result of both the firms' strategies and the critical factors that promote growth and internationalization of businesses. Improved access to capital markets has improved Latin American firms' ability to successfully introduce their operation and compete in global markets.

The Strategic Management Latin America bi-annual Conference (or SMLA), held for the first time at INCAE Business School in 2005 (Ketelhöhn, 2006), was established by a group of scholars and practitioners to study strategy, location advantages and environmental issues in the context of Latin America (Raventós & Ospina, 2013). The SMLA Conference also promotes research on Latin American firms, which remain, by and large, underrepresented in the management literature and, thus, not very visible to students, scholars, and researchers outside of Latin America (Gonzaléz, Jenkins and Lloret, 2016). This Special Issue is based on the 2015 SMLA bi-annual Conference held at INCAE Business School. That meeting provided an opportunity to exchange theoretical insights, empirical research results and applications of current Latin American strategic management issues. Scholars from many countries—including Bulgaria, United States, Chile, Colombia, Costa Rica, Germany, Nicaragua, Salvador, Spain, Venezuela, Brazil, Switzerland, Italy and Canada—contributed to the conference, illustrating that the region is attracting more interest within the academic community. The presented papers contributed to the state of business using three different formats: theoretical papers, empirical studies, and teaching cases. All the work presented was original and based on new research projects. The subjects covered included: 1) growth, opportunities and challenges in Latin America; 2) sources of value creation and growth in Latin America; 3) strategies to capture opportunities in Latin America; 4) investment selection in Latin American countries; and 5) financial market development and risk management in Latin America. The “Best Papers” were selected by a rigorous double blind review process and included in this Special Issue.

2. The context of emerging markets and Latin American economies

Capital inflows into EMDEs were originally fueled by the high liquidity and the comparative lower yields that investors obtained in developed markets (DMs) (Montiel, 1996). These “push factors” increased the appetite of investors willing to take more risk in exchange for higher yields and also offered them the possibility to diversify portfolio risk. The intensification of capital flows resulted also from the improved economic performance and the investment climate in EMs. These “attraction factors” were enhanced by the growth potential and improved competitiveness of companies participating in these markets, as well as by the reduction in the perceived level of the country risk associated with investment markets (Camacho, 2001; Goedhart & Hade, 2003; Agénor, 1998). The very definition of an emerging economy implies positive economic performance, and indeed stemmed from the financial industry (Ciravegna et al., 2014).

A significant proportion of capital flows has gone toward identifying companies that are either undervalued or/and have high growth potential, operating in expanding industries and in countries for which the perception of country risk and the currency exposure are low or can be controlled or mitigated. While during the global economic and financial crisis of 2007–2008, capital flows pulled out from EMDEs, in subsequent years, a strong return led EMEDs to account for a larger and growing share of global financial investment (Roxburgh et al., 2011). As investors continue to pursue opportunities that offer higher potential returns, it is clear that they also look for companies and projects that have the ability to manage the risks associated with economic fluctuations and to adapt to market and industry changes. The key question that emerged during the SMLA Conference is how the current slowdown of growth in Latin America and other emerging economies will affect the business environment (Ocampo, 2015). The high inflows of FDI have provided a broad range of new opportunities, fueling economic growth, and supporting infrastructure development in Latin America (O′Neil, 2014). However, FDI might have also crowded out domestic investors and increased costs as investors from advanced economies rushed to explore new opportunities in reaction to the US and European recessions of 2008 and 2009–2014. The rise in office space costs in countries such as Brazil underlines investments driven by an emerging markets craze, which fueled a real estate bubble that seems to have burst by 2014. The decline in office space costs caused by the 2014–2015 Brazilian recession might, for example, benefit service firms—assuming they do not lose their client base, that is (Reuters, 2013).

Another issue related to investment and capital flows is the increasing level of individual and corporate indebtedness that low dollar interest rates facilitated in Latin America. The expansion of consumer demand, which increased faster than GDP, is partially attributable to increasing indebtedness. The current threat of higher interest rates, together with an increase in the value of the dollar, has reversed the trend (Spence, 2015). This is bad news for firms selling consumer goods in Latin America, especially goods whose consumption can be postponed, such as cars and appliances or consumer durables. It is also bad news for credit providers and firms specializing in real estate, construction and entertainment. Higher interest rates and higher dollar values increase the cost of credit and reduce its availability. Thus, they threaten firms that incurred dollar denominated debts without hedging themselves against currency fluctuations, as well as firms that counted on their capacity to further access low interest credit to finance planned expansions. However, these factors might not affect all companies. For example, firms that have accumulated reserves in order to expand in the future and multilatinas should be better placed than domestic firms in this sort of environment (Robles, 2013). Firms that have debts denominated in domestic currencies should also be shielded from the current change in interest rates and exchange rates.

The dramatic end of the commodity super cycle also underlines the return of uncertainty to Latin America, though in a much more nuanced form—with inflation rates, debt, and currency stability deteriorating in several large economies. Politically, countries that rely the most on commodity exports suffer from the higher risk of instability, with Venezuela leading the ranking in terms of uncertain business conditions (Cárdenas, 2014).

Firms operating in Latin America are adapting to an environment that combines features typical of emerging economies and of their own past—such as having higher inflation rates than advanced economies—with features specific to the region—such as having achieved unprecedented levels of wealth. A large number of Latin American economies now qualify as mid-income economies, with a diversified industrial structure and a growing middle class. Poverty levels are at their historical low in most countries, while the diffusion of mobile telecoms has allowed a leap in connectivity, making the web available to an increasing proportion of the Latin American population (BBC Mundo, 2015). Yet, with growth slowing down, it is becoming harder to be profitable and expand in Latin American markets. The firms that achieve these goals are those that invest in innovation, differentiate