

Brazilian Public Versus Private Companies: Current State of Affairs

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Brazil has grown steadily for many years. It is the seventh-largest economy in the world and remains the prominent power in South America even though the country is experiencing recent challenges. This analysis will provide insight into how privately owned companies are performing compared to their public peers in Brazil. By looking at the Brazilian company financial data, we can observe where opportunities exist and better understand the dynamics between privately owned and publicly traded companies. We reviewed privately owned companies spanning multiple sectors and sizes. Our sampling consists of 93 companies with more than \$1 billion in revenue, 637 between \$100 million and \$1 billion in revenue, and 1,862 companies with less than \$100 million in revenue as of February 17, 2015. From these companies, we analyze various key ratios including profitability, efficiency, solvency, and liquidity to see how sectors are positioned within Brazil. In addition, we look to some banking and energy ratios to better understand key metrics in these two industries as an example of the analysis this data set can support.

Key Findings:

- Private companies use assets to drive sales more efficiently but are not as good at managing costs.
- Publicly-traded industrials, consumer discretionary, and materials companies have median debt-to-capital ratios that are 10% higher than their privately-owned counterparts.
- Privately-owned banks are more conservative with a lower loan-to-deposit ratio and generate less revenue from other services aside from lending.
- Public exploration and production companies have better cash flow to asset ratio while managing lower exploration expenses as a percentage of revenues.

Average (mil. \$)	Consumer discretionary	Consumer staples	Energy	Financials	Health care	Industrials	Information technology	Materials	Telecom services	Utilities
Public-revenue	823	5,314	17,163	2,235	579	774	529	3,756	5,126	2,036
Private revenue	256	312	295	169	177	188	84	211	1,574	128

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Count	Consumer discretionary	Consumer staples	Energy	Financials	Health care	Industrials	Information technology	Materials	Telecom services	Utilities
Private	358	240	34	657	119	635	115	233	22	179
Public	76	26	11	55	11	56	10	40	9	45

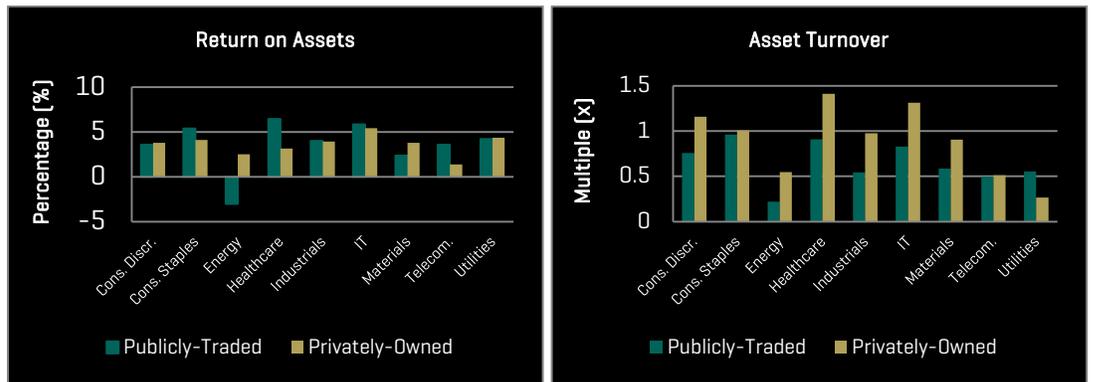
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Profitability, Efficiency, and Margin Analysis:

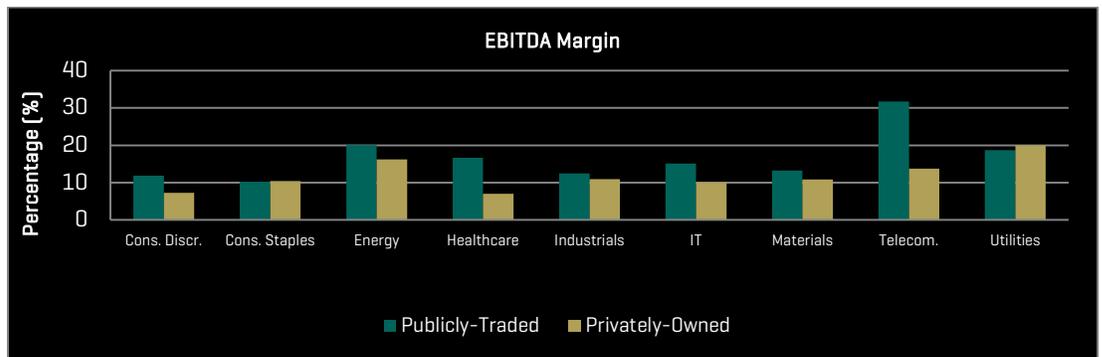
Public companies have a better median return on assets (ROA) in five of the nine sectors than private companies (we have excluded financials from this part of the analysis as their metrics are different from other non-financials). This provides an understanding of how profitable these companies are, normalized by their assets. The widest difference in ROA is within the energy space in which public and private energy firms have a ROA of -3.0% and 2.4%, respectively. Of the nine publicly traded energy companies with ROA data, five had negative earnings. The private company with the highest ROA and more than \$100 million in revenue in the energy sector is **Infineum Brasil Ltda** with an ROA of 17.2%.

However, when we look at median asset turnover to see how efficiently companies are using their assets to generate sales, private companies have larger multiples than their public counterparts. The largest difference in multiples is in the health care sector in which public and private health care companies have asset turnover multiples of .87x and 1.4x, respectively. **Santamária Saúde S.A.’s** 3.1x multiple is the largest of the private companies with more than \$100 million in revenue.

The health care, industrials, and information technology sectors have better return on assets percentages for public companies but private companies have better asset turnover multiples. This suggests that private companies in these sectors may be using assets efficiently to drive revenue but are not as good at managing costs.



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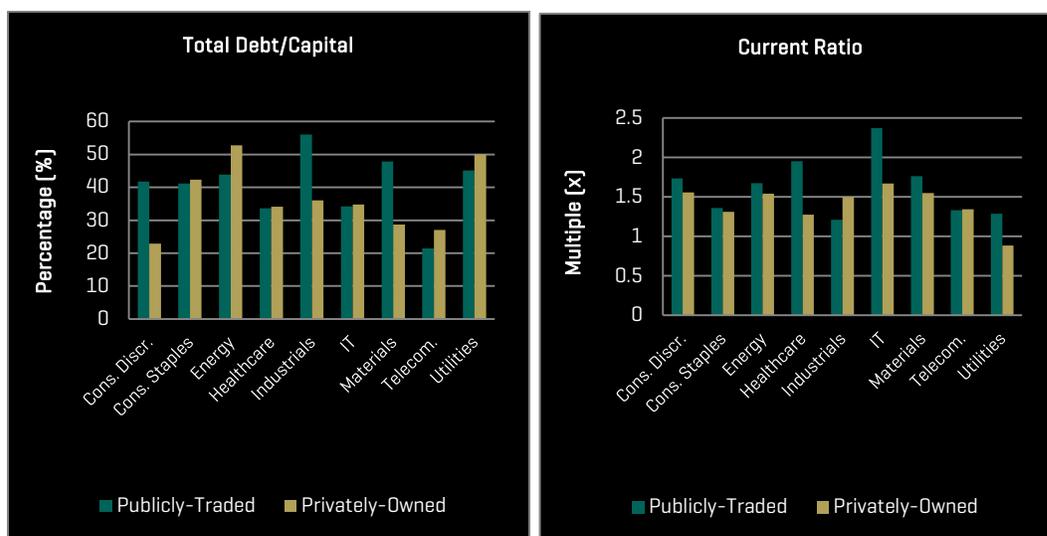
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From a median EBITDA margin perspective, the public sector has better median margins as well, which we observed in seven of the nine sectors. Utilities, telecommunication services, and energy have the best EBITDA margins for privately owned companies.

Solvency and Liquidity:

Solvency and liquidity ratios help us better understand the ability of companies to meet their long-term and short-term obligations. First, comparing the long-term solvency of these companies, we observe that private companies have higher median total debt/capital ratios in six of the nine sectors. Four of the nine industries have debt to capital ratios within 5% of each other. Industrials, consumer discretionary, and materials have more than a 10% differential in their public and private median debt/capital levels. The widest divergence in debt/capital is in the industrials sector. Public and private industrials have debt/capital levels of 56% and 36%, respectively. This may provide an opportunity to further lever up privately-owned industrials to be in line with their public peers. Publicly-traded industrials have the highest debt/capital levels of all types of companies.

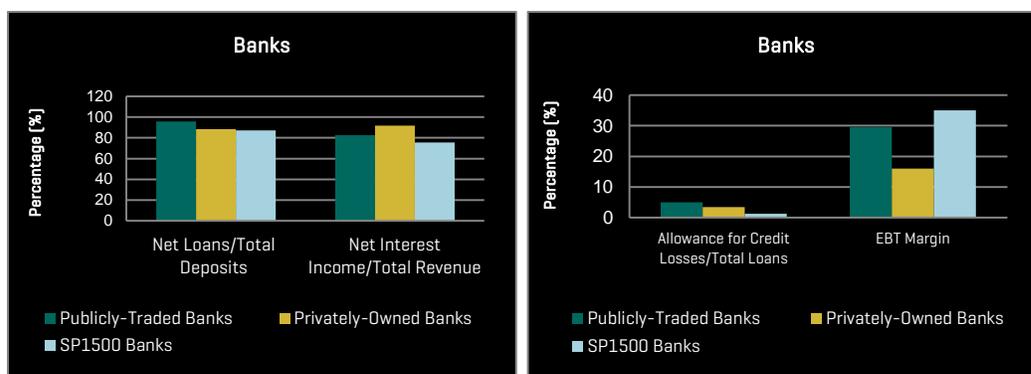
The current ratio gives an idea of a company’s ability to pay back its short-term liabilities with short-term assets. Public companies have more short-term liquidity in seven of the nine sectors as measured by the median current ratio [see charts below]. Most of these public companies are larger and do have access to more cash and inventory on hand to better cover their short-term liabilities. Information technology has the best overall liquidity. Two companies that have the best current ratio from the public and private space in this sector are **Linx S.A. and Digicon S.A.**, respectively. Privately-owned industrials have much better liquidity than their publicly traded peers. This may be because of the heavy debt burden public companies have relative to their private counterparts.



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Banks:

Financials is the largest sector in Brazil for both public and private companies. Specifically for banks, we look to understand key metrics driving performance, such as capital/funding levels, margin analysis, and asset quality. We also wanted to provide a relative comparison on how the Brazilian banks compare to U.S. banks in order to better understand the potential in this industry as the market matures. From median net loans to total deposits, we can see that publicly traded banks lend out more relative to deposits than their private counterparts. However, privately-owned banks get more income from loans than publicly traded banks, which have a more diversified revenue stream. In addition to having additional revenue streams besides lending, publicly traded banks have median EBT margins that are 13% better. These stronger margins suggest they are involved in other more profitable offerings. The two banks with the best EBT margins are from the publicly-traded and privately-owned sector are **Banco Alfa de Investimento S.A.** and **Banco John Deere S.A.**, respectively. However as shown in the charts, S&P1500 banks have stronger margins, lower allowances for credit losses, and more diversified revenues. This indicates that as the capital markets further develop in Brazil, margin expansion and product diversification can lead to stronger results.

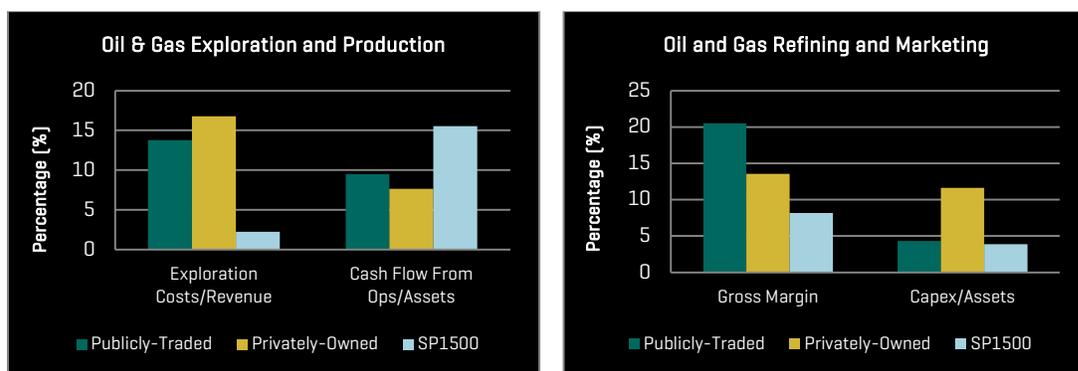


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Energy:

The energy sector has been in the spotlight recently as global oil prices have fallen drastically. Therefore, we wanted to look at two subindustries and better understand some key metrics behind their costs, as well as performance. Looking at exploration and production companies (E&P) companies, we see that exploration costs as a percentage of revenue are about 3% higher for private companies. In addition, E&P public companies are able to generate better cash flow from operations as a percentage of their assets. Comparatively to the U.S., these companies are not as efficient at keeping costs low and optimizing cash flows. The private companies with the lowest exploration costs to revenue and highest cash flow from operations to assets are **BG E&P Brasil Ltda.** and **Parnaíba Gás Natural S.A.**, respectively. Next when analyzing refining and marketing companies, it is useful to look at gross margins as a proxy for the crack spread between the raw inputs and fuel products extracted from it. Compared to U.S. companies, Brazilian refining and

marketing companies have better gross margins. Overall, Brazilian companies in this industry are refiners and marketers of ethanol and other biofuels to give perspective on their products. The private company with the best margin and more than \$100 million in revenue is **Liquigás Distribuidora S.A.** at 30%. Understanding capital expenditures is also important in analyzing how these companies are investing relative to their size. On a median basis, private companies are spending more on capital expenditures as a percentage of assets.



S&P Capital IQ financial data as of: February 17, 2015

Getting Behind The Data

S&P Capital IQ introduced private company financials for Brazil to its comprehensive database of standardized and comparable financial data for public and private companies. With the addition of timely, transparent, and comparable financial data for up to 9,000 Brazilian private companies, combined with our analytics and predictive models, S&P Capital IQ gives you the ability to assess risk and uncover opportunities in Brazil and across the globe.

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Getting Behind The Analysis

Our analysis included all companies that have a primary headquarters in Brazil. The data for the companies is sourced from their most recent financial filing, generally 2013 and 2014. Below are the definitions of all ratios used:

Return on Assets: $(EBIT * 0.625) / [(Total\ Assets\ (t) + Total\ Assets\ (t-1)) / 2]$

Asset Turnover: $Total\ Revenues / [(Total\ Assets\ (t) + Total\ Assets\ (t-1)) / 2]$

EBITDA Margin: $(EBIT + D\&A\ for\ EBITDA) / Total\ Revenues$

Total Debt/Capital: Total Debt / [Total Preferred Equity+ Total Common Equity + Total Debt + Minority Interest, Total (Incl. Fin. Div)]

Current Ratio: Total Current Assets/ Total Current Liabilities

Net Loans/Total Deposits %: Net Loans / Total Deposits

Net Interest Income/Total Revenue %: Net Interest Income - [Bank Template]/ Total Revenues - [Bank Template]

Allowance for Credit Losses/ Total Loans %: Allowance For Loan Losses/ Gross Loans

EBT Margin: EBT, Excl. Unusual Items / Total Revenues

Exploration Expenses/Revenue: Explorations Costs/ Total Revenues

Cash Flow from Ops/Assets: Cash from Ops/Total Assets [t]

Gross Margin: Gross Profit / Total Revenues

Capex/Assets: Capital Expenditure/ Total Assets [t]

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