



“We must work to reduce the size of the government”

Laercio Cosentino

CEO of Totvs

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AS HEAD OF the leading business management software company in the Brazilian market, serving sectors ranging from agribusiness to logistics, Laercio Cosentino closely follows the mood of investors and considers the current crisis the deepest since he founded Totvs in 1983. “For the first time ... virtually every industry somehow has been penalized,” he says. However, he is optimistic that the economy can recover—provided there is willingness to carry out reforms that will bring the business environment to a par with competitive economies. For the information technology sector, Cosentino says that on the reform agenda there must be laws that allow a more flexible relationship between companies and workers, and tax reform. “What we need first,” he says, “is a clear, definite, and sustainable course, and then create rules that allow Brazil to become more competitive. If the country is competitive, companies will be competitive, and things will happen.”

Before the recession began in 2014, how did the Brazilian economy affect the Totvs growth strategy?

It took over 50 mergers and acquisitions to build what Totvs is today. We understand that when you talk about technology, you talk about scale. So what Totvs did was exactly that: it grew from a turnover of R\$300 million in 2003 to net income of R\$2.4 billion last year. Through this process, we saw the private sector in general learning a lot in order to thrive. We went through all the presidential reforms and plans: one opened up Brazil’s economy, another stabilized the economy,

another passed the Fiscal Responsibility Law, which allowed sustainable growth, another helped to advertise Brazil around the world.

When the economy was opened up, we began to prepare the company to compete in the software development technology market. When the economy was stabilized and companies started to grow, we had products to offer to these companies. When higher growth attracted investors, we opened up our company's capital in 2006 to structure the process of consolidation and grow together.

But then we saw the government increasing its spending without carrying out needed reforms. And now we are at a point where Brazil needs to take corrective actions that the government did not take in the period of abundance. Even as the economy contracted over the past two years, we have been preparing and we feel positive signs that the economy's engines are warming up to a new virtuous growth cycle.

Which sectors show signs of recovery?

We are seeing parts of the services sector starting to move a little more, especially small businesses and startups. Small manufacturers, who are more agile than large ones, have also recorded some growth. In summary, we see that the movement is coming from services and from the bottom of the economy up.

How has the economic crisis affected Totvs demand given that 40% of its revenues come from industry and retail?

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somehow because this crisis was not only economic but also institutional, with the investigations of major corruption in the state oil company. And the world economy is not thriving either. This resulted in less demand for IT solutions. Meanwhile, the digital transformation in recent years has swept every sector of the economy. First it was the music industry, followed by photography, and now information technology. Software development itself is also going through a digitalization process: instead of selling licenses to use software, we now market subscriptions (which reduces the supply chain and lengthens the period of financial return). ... To Totvs, this change in its business model has deepened—in the first quarter of this year, for the first time subscription revenue surpassed licensing.

How has the recession impacted this change in business model?

Being Brazilian is actually doing whatever it takes. When you look at society as a whole, after

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people connected to the Internet, they began to change the concept of owning something or rent, subscribe, use it. For example, having a car or taking an Uber. So what is happening with software meets the expectations of this new Internet-connected generation. ... We still have customers who prefer use licenses for certain software, but have a new generation of clients that prefer to have variable cost (use-signature contract) to an upfront fixed cost. The current crisis in Brazil has helped to move demand for software to the use-signature model. When you have to make choices to improve investment, and you look at lower revenues and earnings and at cost increases, a use subscription may allow you to do more with your money than buying something. This is a positive aspect of the crisis: it causes companies and people to think hard about what they really need to have.

The recent period of economic growth was marked by a strong increase in wages above productivity. Has this negatively impacted the operation of Totvs, which has 12,000 employees?

No, but it is logical that the heated labor market in recent years caused wages to rise more than average productivity. With the

crisis since 2014, however, the labor market ended up correcting itself. A positive side to all this is that after dealing with higher costs due to the general lack of infrastructure, Brazil will end up adapting, and I think this new growth cycle will be much smarter.

The issue of labor productivity also involves better training of workers. To what extent does education weigh in the IT sector?

When we talk about innovation, growth, putting the country on another level, the first step is education. And not only education, but a culture of doing things well, having regard to schedules, and the quality of what you are delivering. When we hire someone in Brazil, she usually begins to be productive after 90, 120 days—only after this period of training does she start to pay off for the company.

What would be the ideal period for a new hire to start to pay off?

We have labs in Mountain View, California, and Brazil. There you have someone actually working productively in less than 30 days. Here, it takes twice as long. In California it is also much faster to hire someone already well-trained, knowledgeable; you simply specify what you want. Basically, comparing a newly graduated engineer in the northern hemisphere and the southern, depending on the university, you have a gap that requires effort to bring people to the same work level.

We have to invest big in education, so that we can make the country more competitive. And it is important not only to invest in increasing the number of people enrolled in universities, but also to have a plan that indicates which sectors need professionals with what training and knowledge—to cover Brazil's educational gaps. I am vice president

of Brasscom (Brazilian Association of Information Technology and Communication Companies) and we have mapped what the IT sector needs, what kind of engineers, which educational gaps we have.

What negative aspects of the Brazilian business environment most affect your activity?

Today with the Internet of things we have begun to get things connected to generate information, competitiveness, generating consumption knowledge that can be distributed at any time anywhere in the globe. So to actually make Brazil prosper, all ideas have to be somehow applied within an international environment. It will be hard, but we can do it. The close proximity of both consumption and distribution, access to other markets, knowing other regulations will accelerate Brazilian understanding of the processes that we cannot do differently from what others are doing.

For this reason, we need to address three issues. The first is the lack of flexibility in labor rules. Today, 70% of costs for the IT industry are concentrated in people. Our main asset is people. We work with innovation, creativity, and the moment you say that employee has to work eight hours, she cannot do more than two extra hours, it has a negative impact on productivity. For low-wage, low added-value activities, where the employee may be at a disadvantage, these labor rules seem fine. But when you look at the IT sector, the employee knows what she wants and knows how to produce. If she has tools that allow her to work in the car, at home, or anywhere, these labor rules hinder her productivity. Changing Brazil's labor laws is not a simple thing. But we could evolve, setting a ceiling, for example: that labor laws would apply only

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to jobs paying up to R\$10,000. Above that, free negotiation would apply.

In California, the situation is simple: we propose a challenging task, we define a remuneration, and our employees there work any time they want and whenever they want. For the IT industry, this is fantastic. When it comes to creating disruptive models, digital ideas, turning these ideas into models, it is important that the environment supports the growth of companies in line with how society lives today. Labor relations need to be much more open, frank, transparent, with simpler rules regulating the worker's relationship with the labor market.

What are the other two issues?

The second issue is taxes. When we develop something, it can be in Brazil, but the developer may also be an Indian, a Chinese, an Israeli, a Uruguayan, who works in his country and sends the new code by Internet. It has no border. So for Brazilian companies to compete, the tax issue is important. The issue is not just the tax environment, but the diffi-

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culty of calculating what is owed; it depends on the state and the city. There are simpler taxation models around the world.

The last issue is a sustainable business environment. If there are not very clear rules that allow for businesses to be the sustainable, we will see Brazil repeat the poor growth associated with ups and downs every 15 years. We have no time for this. ... IT industry investments to deliver a disruptive technology in three, four, five years, take time. We must have clear rules that support investment.

In your opinion, would you say the service sector is still not considered when it comes to industrial policy?

In talking about policies to incentivize production, we cannot think only of agribusiness, manufacturing, or services. A large country like Brazil has a very well developed agribusiness sector and could have such a manufacturing industry if an enabling environment for it is created. ... We need a national plan that defines what we want to be

in 5, 10, 20, 30 years. Where we want to be in agriculture, industry, and services. And if this works, we will have income and consumption. The policy in recent years to make consumption the driver of growth worked as long as households had little debt. But when people lose income, consumption loses relevance ... Consumption has to be the result of a well-grounded economic structure.

Some argue that services are still taxed little. What is your view?

The services sector may have a lower tax burden, but it has no compensation at all. We first have to talk about reducing the size of government. Until we face the fact that the government is too big, we will not be able to do tax reform. The government must have a budget and stick to it, because we can no longer think of covering budget deficits with tax increases. If we have a deficit at home, we cut spending because we cannot increase our own salary. Companies do the same: if you do not reach a certain level of profitability, you need to decrease the size of the company. But government does the opposite—and this is exactly the discussion now on the government agenda. I see difficulties in both the Senate and the House in getting the constitutional amendment passed to cap primary spending. But we must confront head-on the need to limit state funding for current spending and gradually focus the government on what really matters: education, health, public safety and legislation. The rest should be up to the private sector. The government does not have to own an airport; it does not need anything other than the core activity of a government. If we can limit public spending, we will be able to determine the tax burden to support the government's size. ▣