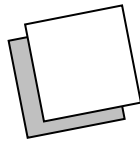


## CASE



## ESCRA

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**Keywords:** new client acquisition, buying center analysis, Brazilian Telecom-Market

**Abstract:** LUZ, a Brazilian energy supplier decides using their network for telecommunication. They found a subsidiary named LUZATEL for purchasing the required IT-equipment. Four IT-companies make it to the short list. One of them is ESCRA. ESCRA is a large Swedish producer of telecommunication equipment, who has recently started to additionally offer IT - Solutions. This case describes the acquisition-process from the perspective of the ESCRA sales manager, whose actions will be analyzed, evaluated and discussed in class.

Chris Jensen felt pleasantly excited. After a long flight, he had finally arrived at his hotel in Sao Paolo, had ordered a caipirinha from room service and thought about the events about to take place over the next three days. It was Monday evening, September 14, 1998. The final presentation for an acquisition project was scheduled for Thursday – his biggest project so far. And not only was the order in question one with a large revenue – \$9 mio., Chris Jensen was also convinced that he had the best chances of winning the order. “If everything keeps going as smoothly as it has so far, it should work out just fine,” he thought. Nevertheless, he vowed to not get too distracted by his euphoria, but focus all of his concentration during the following 72 hours on his sales success.

### A: The division „IT Telecom“ of ESCRA

ESCRA was a technology-oriented and diversified company with its main headquarters in Stockholm. It marketed components, products, and ready-made plants for fields such as medicine technology, traffic technology, energy or semiconductor technology, automation technology and telecommunication technology – generating a revenue of more than \$60 billion. In 1990, ESCRA established the independent business unit IT (IT = information technology), whose main task was to plan, distribute, install, and, on the customers’ request, run comprehensive IT systems for big companies. The business unit IT refrained from developing its own software but co-operated with a number of product partners such as SAP, Microsoft, Sybase etc. The unit also co-operated with nearly all significant hardware producers though ESCRA had its own business unit producing personal computers and servers. The business unit IT placed a lot of emphasis on being platform-independent and presented itself on the market as a service partner who selects and combines all elements of IT systems according to the individual requirements of each customer.

As the business unit IT had originally been set up out of many different IT departments within the corporation, there had been a high profit dependency at first. But very soon, IT was able to acquire external customers, particularly in the field of banking and insurance, and in the public sector. No deals had been concluded in the telecommunications industry within the first seven years, but this topic was on the agenda and was one of the purposes of the newly-founded division of IT Telecom. The division proved to be successful right from the start; nevertheless, the LUZATEL order would be the second largest project of the year.

### B: The market

In 1997, Brazil had the highest population of South America – 160 million – nearly half the population of the entire continent. Having been very unsteady during the early nineties, with inflation rates of over 1000%, the country’s economy and currency had now stabilized. This caused a GNP-growth of an annual rate of up to 5%, and an increase in investments.

The case is based on a true story. Developments and numbers are authentic. Names and locations were altered by the author for reasons of privacy.

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In 1995, the Brazilian government had developed an 8-year plan called PASTE for the telecommunications industry (PASTE = Program for the Recovery and Expansion of the Telecommunications and Postal System). Its purpose was to deregulate the market, up to that point monopolistically structured, step by step. It was assumed that more than \$ 80 billion would be invested in the expansion of the telecommunications network between 1995 and 2003. Brazil was already one of South America's most developed countries as far as telecommunications was concerned, with a country-wide telephone density of 11.56 %. Even growth rates in the mobile phone sector were the continent's highest.

As expected, the high market growth in telecommunications itself was even exceeded by the demand for the implementation of local IT systems. This was the result of increasing competition between well-established network operators and newcomers on the market, forcing each to be highly customer-oriented and cost-efficient. Therefore, a number of new services and very flexible offers were introduced (for example, special conditions for certain customers at a certain time) and the internal process had to be automated and rationalized. In order to do so, all up-to-date competitors made an increasing use of IT systems. The main components of an operator's IT solution were:

- providing systems enabling new customers and new services to be automatically installed for the necessary network elements
- surveillance systems which controlled the network's operations and, in the case of a malfunction, could direct data traffic to other lines automatically
- workflow management systems which were able to indicate all steps necessary for emergency maintenance within the network, while at the same time checking the availability of specific technicians, initiating the replacement parts' order, etc.
- billing systems which collected and added up all bills, automatically wrote letters and managed the money flow,
- mediation systems which transmitted the data collected from the network elements into a data format suitable for IT systems,
- enterprise resource-planning systems which were able to display, administer and direct financial and other processes,
- customer care systems which supported all activities necessary for comprehensive customer care and through which the staff could check the current order status and provide the customer with information on his orders at any given time. Apart from these central elements of an IT solution, some network operators implemented a number of other systems, for example "fraud systems" which detected fraudulent network usage, sales support systems for the sales force and many others. As there were overlaps between the functionality of individual software products, one had to define and configure the degree of application and of data exchange in a customer-specified way. This was a very complex undertaking, as the data formats of individual systems and their programming languages did not correspond to each other.

### ***C: The Customer***

LUZATEL was a new subsidiary of the energy company LUZ, one of two companies which, together, provided all 18 million inhabitants of Sao Paulo with energy. In addition, the company owned a pipeline system to a local energy supplier in Rio de Janeiro and Curitiba which was only to be used in the case of an undersupply of energy in these cities. In this market, LUZ faced no real competition and had been making excellent profits throughout the 70 years of its existence. Similar to many other energy companies in other countries where deregulation had already been implemented, LUZ planned to use the broad pipeline system to enter the telecommunications market towards the end of 1997. For this purpose, Mr. Alfonso, the company's dynamic chief executive since the beginning of 1997, founded LUZATEL in December 1997, in spite of the scepticism of some older board members.

LUZATEL had been founded as a 100% subsidiary of LUZ, but the idea of going public after having established the company in the market did exist. This is why it was decided to give a rather encompassing independence to its management. It was this independence which caused LUZ to "sacrifice" some of its most successful and experienced managers, appointing them LUZATEL executives.

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Mr. Basilva became Head of Financial Affairs and LUZATEL spokesman. The visibly cultivated man in his late forties was known for his leadership qualities and for being open to new ideas. Mr. Alfonso trusted him completely and the other executives at LUZATEL also respected his superior intellect and his well-proven integrity.

Mr. Charnissi held the position of Head of Technical Affairs at LUZATEL. During his 26 years at LUZ, he had held responsible positions in nearly all technical areas – he had been head of the maintenance team, had later supervised the construction of a nuclear plant and had eventually been made head of technical affairs for LUZ. He was said to be a technical genius and some referred to him as “señor Einstein”. He was not, however, always easy to deal with, being stubborn at times and easily frazzled.

Mr. Fernando was a member of his department. The graduated electric engineer was only 32. In the past he had been with Embratel, one of the biggest Brazilian telecommunications companies and had then moved to England for two years to do his MBA. For the past four years he had been working for LUZ. He was considered as being ambitious and having bright career prospects. Mr. Basilva had already mentioned the possibility of making him head of the technical division of LUZATEL once he had learned enough from Mr. Charnissi.

The third member of the LUZATEL executive board was Mr. Sherry, responsible for marketing and sales. Mr. Alfonso had thought it important to not only recruit internally but to also get some fresh blood from the outside when setting up LUZATEL. He found the internal marketing competence insufficient which was why he wanted to get an outsider for that area. After intense debates with the supervisory board, he finally had his way and called the North American into the position. Mr. Sherry had received an MBA at Harvard and worked in AT&T’s marketing division for the following 11 years, first on high level communications policy and market research and later taking charge of the entire private sector pricing policy.

The important job of LUZATEL’s procurement co-ordination, with approx. \$ 200 million in investment volume for the start, was given to Mr. Edmond who reported directly to Mr. Basilva. Mr. Edmond was in his mid forties and his size gave away his passion for good and rich meals. He had received a technical education at LUZ, later worked in marketing and sales, then moved into the procurement division three years ago.

The management of LUZATEL had to plan the business, procure equipment, and run the network profitably. By February 1998, people at LUZATEL were very satisfied with the first two months’ progress in setting up the new company. All bureaucratic hurdles to register the company, rent offices, sign up with head-hunter companies to get the necessary personnel and write a first marketing plan had been overcome. The latter gave an overview of market potential and competitive forces and it included first analyses of different customer segments’ price sensitivity and readiness to change suppliers. According to the marketing plan written by Mr. Sherry, pipelines would be let to other suppliers at first; half a year later LUZATEL would start delivering to corporate customers and, another six months later, supply to private customers within the city of Sao Paulo would begin.

### *D: The Competitors*

An RFI (request for information) sent out by LUZATEL in April was answered by nine companies. Four of them were considered suitable and put on the shortlist. Besides ESCRA, companies on the list were:

- **Aclutel** – the Belgian Aclutel was, just as ESCRA's telecom sector, one of the three big competitors in that industry. The three companies together covered nearly half the market and were established with most important companies. Similar to ESCRA, production and sales of switches were the main revenue generator at Aclutel but the company also sold other products for setting up and running a network. In doing so, the increasing service aspect of this line of business was the main focus. For this purpose, Aclutel had recently established a department to implement IT solutions for operators, the very one which had responded to LUZATEL’s RFI. Aclutel had a strong international business but only a weak presence in Brazil to date. Chris found another weak point in the fact that, according to Mr. Edmond, Aclutel-IT’s first interview with LUZATEL hadn’t been very successful. Unlike Chris, none of the two Aclutel-representatives could speak Portuguese and Mr. Charnissi was said to have left the meeting after only a few minutes.

*E: Acquisition  
Activities thus far*

- **Peterson Consulting** – Peterson Consulting was the world's third largest IT supplier, after IBM and EDS. For many years they had gathered experience with significant projects in the telecommunications industry, their customers being mainly the world's largest operator companies. Apart from implementing IT systems, Peterson Consulting worked primarily in management consulting. Here the company covered the entire product range in all important industries – projects of strategic planning, organizational development, process engineering etc. Peterson Consulting had more than 44,000 employees in 47 countries but no Brazilian branch so far. Its image was that of a professional but expensive company. Chris himself had experienced this on one occasion when he had co-operated with people from Peterson Consulting and found that their price per hour was nearly 30 % higher than his own.
- **Faro Group** – Faro Group was a consort founded in 1996 which included one financially extremely potent private person, and several smaller Brazilian IT companies. LUZATEL had not explicitly asked for a "local-content-share" but in Brazil they were very prominent. The significance of the content was especially important in this case, as the head of Faro Group was said to have close personal connections to business and politics and he was also assumed to know Mr. Alfonso personally. In the Brazilian telecommunications market, Faro Group had already won several IT projects, none of which, however, had been completed thus far. Faro therefore did not have any real references either. What they did have was a strong cost position, since both their employees as well as the SW products they used came from Brazil. This was not without effect on their prices; in another project they had been 20 percent cheaper than the foreign bidders. In order to sort through his thoughts, Chris summarized again for himself what had happened during the last several months.

**January 28<sup>th</sup> 1998**

André<sup>1</sup> called. Is working on a deal with LUZATEL at the moment. ESCRA telecommunications in Brazil is attempting to sell the switches and the cable network. As far as he knew, also an IT system was needed. Convinced him to take me to the first meeting with the customer on the 16<sup>th</sup> of February. Agreed to briefly introduce the ESCRA IT department after the network equipment presentation with the customer.

**February 16<sup>th</sup> 1998**

Meeting at LUZATEL went great. All executives were there, seemingly very pleased that ESCRA offers not only telecommunications systems, but also information technology systems. They were also impressed by the company's strong local presence. (ESCRA's telecommunication sector alone employs nearly 3,000 people in Brazil) Obviously, no one from LUZATEL realizes that ESCRA IT's telecom sector does not yet have employees in Brazil - they see us as one company.

Mr. Edmond introduced the main data of the further procurement process as follows: The idea is to have different tenders for the telecommunications and the IT systems. At the end of March, an RFI would be published asking all interested suppliers to present their company's potential and to draft the key elements of their solution and the respective price range. On the grounds of these documents to be submitted by the beginning of May, LUZATEL would write a shortlist of two or three companies. These companies would receive an RFP (request for proposal) at the beginning of June which would specify LUZATEL's IT system requirements. They would then be asked for a detailed statement as to whether or not they could meet the requirements and to make a fixed price offer. The bidders would have six weeks' time to answer the RFP and LUZATEL expected to need another six weeks to evaluate the documents. Two more weeks were then scheduled to co-ordinate detail problems, after which a final presentation was planned for mid September, whereupon the decision would be announced. The network was to be operational as of the beginning of 1999.

<sup>1</sup> André Luiz was a colleague from the ESCRA-Telecommunication department in Brazil whom Chris had met several years before in the head office, and with whom he kept in touch, seldom but on a regular basis

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Mr. Edmond pointed out the importance of keeping up with the schedule, as every lost month would also mean lost revenue and allow the competitors to establish themselves on the market. He is right about that!

After several hours of discussion, I asked all gentlemen present to dinner. Mr. Sherry and Mr. Basilva had other plans for the night, but Mr. Charnissi, Mr. Fernando and Mr. Edmond came along. Evening was very pleasant. André, Charnissi, and Fernando philosophized about technical visions for the new millennium; I spoke mainly with Edmond. Found out that ESCRA isn't unknown to LUZ. Only two years ago, LUZ successfully constructed a power plant in cooperation with the ESCRA energy sector. The plant had been finished just at the time when Mr. Alfonso became chief executive. Edmond described Mr. Alfonso's relieved sigh when he saw the successful and on-time start of the plant. At the end of that evening, I invited the LUZATEL guys to Sweden to get acquainted with our IT-business unit. Invitation was accepted, good-byes were cordial.

### **March 12<sup>th</sup>/13<sup>th</sup> 1998**

Charnissi visits our main office for one and a half days. Edmond, with whom I had talked on the phone a couple of times during the past few weeks, had already told me that he couldn't come himself and neither could Fernando. Also had invited Basilva and Sherry but both declined. But Edmond had assured me that, as the head of the technical department of LUZATEL, Charnissi would be just the right person to discuss the problems of IT-systems.

On the morning of the 12<sup>th</sup>, Charnissi received a detailed presentation about organization, product range and references of ESCRA's IT sector from Martini.<sup>2</sup> As always, Martini was eloquent and professional.

Even the lunch we shared afterwards was in a pleasant atmosphere. Martini told me I was doing great so far and that I should let him know anytime I needed help.

In the afternoon, different ESCRA specialists gave demonstrations of those software products that had been installed at past customers. Charnissi seemed very satisfied and mumbled something about wishing to see all that technical know-how "under the pretty curls of Brazilian suppliers."

By the way, Charnissi caught on to things really quickly. Asked astonishing questions about technical details, for instance about specific transmission standards; that got our people all excited.

A meeting at Swedish Telecom on the 13<sup>th</sup>. As expected, Charnissi showed a great deal of interest in obtaining insight into the headquarters of such a big network operator. Our division had only implemented a mediation system but the Swedish Telecom guys provided Charnissi with much broader insight and repeatedly spoke positively about our employees.

### **March 30<sup>th</sup> 1998**

RFI came. It outlines the market situation and expansion plans, all corresponding to the Sherry-marketing plans. Requirements for IT-systems are kept on a surprisingly general level. On the other hand, it does contain nearly the entire array of functions also included in the IT systems of big innovative operators.

### **May 4<sup>th</sup> 1998**

Completion of and response to the RFI. Decided to go by the two phase-plan, the usual for "start-up-telcos". In Phase One, only systems absolutely necessary for the network operation are installed. With the usual full-cost calculation, I figured costs of \$7.4 mio., (HW products 20 %, SW products 30 %, implementation and installment 45%, and

project management with 5%). Same calculation approach and same costs for Phase Two, to be started roughly one year after Phase One. Contains a full workflow management system, a comprehensive enterprise resource-planning system, a system for automatic network control and optimization of the usage intensity and a data

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<sup>2</sup> Mr. Martini was the head of sales for the IT Telecom division and therefore Chris Jensen's superior.

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warehouse system. Repeatedly went through each position because this would be the first time for us to implement a complete IT solution.

Before surcharging the profit margin of 12 %, I was told that I have to consider a “Brazil-risk-surcharge” of no less than 10 %. Based on this information, I gave LUZATEL a price range of \$ 8.87 mio. and \$ 9.49 mio. for the two phases.

**May 7<sup>th</sup> 1998**

Traveled to Sao Paulo to deepen contacts to the customers and to explain my RFI-response. First a short meeting with Basilva. Received me most warmly and apologized again for not having been able to come to the dinner or to come to Sweden. I outlined the main facts about the importance of IT systems for him and explained why it would make sense to buy telecommunication and information technology from the same company. Mentioned my two-phase implementation and got agreement in principle. He did not, however, want to talk in detail about the RFI and the response but I thought I should contact Mr. Edmond and Mr. Charnissi about that. At least gave him ESCRA’s new image brochure and mentioned that two new prominent references had been added since February. He said thanks and uttered laughing that he was sure about the success of one ESCRA department anyway. He then mentioned having met with Mr. Faccina recently, head of the Brazilian ESCRA telecommunication division, and found him pleasant. Serious again, he also mentioned that he had made it clear to Mr. Faccina that price would be a key factor in all decisions to be made.

Afterwards, several hours of meeting with Charnissi and Fernando. Explained explicitly ESCRA’s RFI-document. Charnissi had detailed questions regarding the scalability of the particular software products which I was able to answer to his satisfaction with regard to the HW- and SW products planned.

Mr. Fernando had several questions concerning process organization and coordination between the systems. He wanted to know, for instance, how a call center agent could arrange for reimbursement for an upset customer and how his actions would be linked with accounting. He also asked how much time it would take to identify and repair a network failure and how one could react if a customer refused to pay his bill. Explained to him that the ESCRA-solution would be able to make the adjustment, connection and interpretation of the systems entirely according the customer’s wishes.

In the late afternoon, meeting with Edmond, later dinner with him. A relatively formal conversation at first. Asked him if LUZATEL would be interested in a financing model since we could offer some interesting options in this matter. He didn’t respond to that but repeated Mr. Basilva’s statement that LUZATEL generally makes very price-oriented decisions. During dinner, the conversation turned more and more personal, up to the point of showing photos of the family. As we got back to the professional situation, Edmond told me that not everything goes smoothly at the LUZATEL and that there are some issues between Mr. Charnissi and Mr. Fernando at the moment. Also learned that Charnissi described his visit to Europe as a very interesting and promising one and Basilva is to have said, jokingly, that the ESCRA-guys deserve respect alone for causing Mr. Charnissi to give a compliment for once.

**May 22<sup>nd</sup> 1998**

During a phone call with Edmond today, I learned the names of our competitors on the shortlist. (They will be announced officially next week.) Edmond said that Peterson Consulting had been listed rather late and quite surprisingly for him as well. Mr. Charnissi had asked him to list them, practically at the last minute, and this although Peterson Consulting had not even previously given a presentation to LUZATEL. Edmond thought that this doesn’t have to mean bad news, as competition is fierce anyway, and that it isn’t the number of competitors that count but their strength. Apart from that, Charnissi did not intend to conceal his scepticism towards North American companies, previously referred to as “Coca Cola Colonialists”.

**June 5<sup>th</sup> 1998**

Got a more advanced version of Mr. Sherry’s marketing plan that accurately defines LUZATEL’s growth plans. Called Sherry immediately and briefly discussed the predicted numbers when entering the private customer market. This is very important,

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for instance, for the determination of licensing prices for the billing software. Sherry provided me with all the information without hesitation. His manner was very short but nevertheless friendly.

**June 22<sup>nd</sup> 1998**

Edmond called to tell me about LUZATEL's decision not to send out an RFP as announced. They had decided that the bidders on the shortlist would have sufficient insight into the situation and the plans of LUZATEL by now and that they should be able to concretize their offer on that basis. He pointed out that the binding offer of the listed companies should be explained in the final presentation, something which would increase the importance of the presentation. The original date for the final presentation remains and everything is going according to the schedule.

Asked Edmond whether and how he should enlarge or modify the RFI response. He said he did not see a great need to alter the initial ESCRA response. He advised me to be ready to answer detailed questions and mentioned that a lower price would be perceived very positively at LUZATEL.

**June 26<sup>th</sup> 1998**

Although no longer officially requested, I sent Charnissi the system descriptions of individual software products to be implemented at LUZATEL. These descriptions would otherwise have become part of the RFP response. Mr. Charnissi thanked me in a short e-mail.

**July 28<sup>th</sup>/29<sup>th</sup> 1998**

Charnissi called personally, thanked for the system descriptions and asked how many people would usually be employed for customer care in the case of corporate as well as private customers. Told him that this would depend on the aspired service level for the individual customer segments which had been outlined in Sherry-marketing plan. Charnissi responded that he did not know these plans all that well and that he would only need a very rough estimate. Told him I didn't have these numbers either but that I could ask one of the ESCRA customers about it. Next day, I had the information from two bigger companies and was able to pass them on to Charnissi. He thanked me and said that they corresponded to his numbers which he had only wanted confirmed.

**August 24<sup>th</sup> 1998**

After my well-deserved three weeks of vacation and back in my office again, I called Edmond to ask him about the latest developments. He told me that it has been very hectic at LUZATEL and especially at his office lately but that I had not really missed anything important. At the moment, they were discussing the optimal number of employees.

**September 9<sup>th</sup> 1998**

Got the documents for the final presentation ready. Got my way to have Mr. Klatt accompany me to Brazil for the "very detailed technical questions" signalized by Edmond. To cover the necessary net-know-how, André will come too; his own final presentation on the net-tender offer will be a day later. Have spoken with André a few times over the past weeks but we hardly ever discussed the acquisition efforts of LUZATEL since the procurement process for IT and the telecommunications net are being operated separately by the customer. However, he did talk of a certain atmospheric interference between Aclutel and the LUZATEL top; Charnissi even told him once that he can relate to the French jokes about the Belgian.

Gained a victory in negotiations about the ultimately lowest price limit. Could accomplish a reduction of the risk premium down to 5 % and of the margin down to 10 % but only with the promise that this negotiation scope would only be used in a case where it is absolutely necessary. On top of that, the head of the division decided to promote the sales efforts in Brazil should the LUZATEL order be won and to establish a service team on location.

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### September 13<sup>th</sup> 1998

Called Edmond one last time the day before my trip to Brazil. As expected, he seemed a little bit more reserved than usual, being only a few days before the decision. Only made an ironic remark about the lengthy discussion going on among “those at the top” regarding the size of the staff and said that he didn’t want to comment on the present state of procurement decisions. He did say, however, that Mr. Alfonso surprisingly announced that he would attend the final presentation. I see a quite positive development for us, if a chief executive who has already made good experiences with ESCRA doesn’t want to miss it.

Finished with his glass of caipirinha, Chris Jensen summed up his starting position for the final presentation: All important persons within the customer company thought positively about him. He had even built up a relatively close personal relationship to the responsible procurement manager and the executive in charge of technical affairs was convinced of ESCRA’s technical competence. He thought that at least no competitor was in a better position. Regarding the RFI response, there had been no major complaints and his phase concept had been fully accepted. He simply must not make any major mistakes now and give a convincing presentation. It was important to develop a clear structure, to collect and organize all arguments and to make the overhead slides look perfect. He would have enough time for last preparations during the next two days. “If the final presentation goes well, then we should get the job. And then”, he grinned, “I’m going to Rio this weekend and celebrate my own carnival – even if it’s mid September.”



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### ***Questions to ESCRA***

1. What is the probability for Chris to get the deal, in your opinion? How do you consider the competitors' chances?
2. Identify and evaluate the buying criteria of LUZATEL concerning the illustrated buying process?
3. Conduct a buying center analysis.
4. Can you discover any unusual issues in LUZATEL's decision process?
5. What has Chris done right in the acquisition process, what could have been done better?