RED HERRING THE BUSINESS OF TECHNOLOGY

Rio Riches

Brazil is the new darling of high-tech and cleantech investors.

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After years of sending greenbacks halfway around the globe to feed technology-related investments in Asian countries, U.S. investors are turning an eye due south. Brazil, they are coming to realize, is not just the land of samba, gorgeous beaches, and annual ritualized mass parties.

Venture capitalists and other investors are beginning to view South America's largest and most populous country as an ideal location for research and production of cleaner fuels, outsourcing of customer service and software development centers, and, to a lesser extent, manufacturing high-tech products for sale to emerging markets. In all of Latin America, $609 million in private equity and venture capital funds were invested in 2004, but that skyrocketed to $4.26 billion last year, much of it in Brazil, according to data compiled by research firm Venture Equity Latin America.

"It's a very fruitful market that has not been looked at because everyone's running to India and China, while a country which is closer in many different ways could bring just as strong a return at the end of the day," says Mark Heesen, president of the National Venture Capital Association.

One telling sign of expanding investor interest was the recent announcement by influential VC firm Draper Fisher Jurvetson of its $40-million early-stage fund financed by Brazilian investors and a soon-to-be-created $100-million fund composed of U.S., Brazilian, and other investors.

"We see it as a large economy with talented people, smart people, some world-class universities," says Don Wood, DFJ's managing director. "It's been essentially starved of the venture capital ecosystem that fuels innovation." Brazil's economy, he notes, is slightly larger than Russia's and on par with India's.

What made the announcement even more significant was DFJ's decision to team with Brazil-based FIR Capital Partners, which will provide local knowledge of people, customs, and rules. Mr. Wood says his is the first U.S. venture capital firm to form such an association.

The list of big names making a splash in Brazil goes on. AOL co-founder Steve Case, Sun Microsystems co-founder Vinod Khosla, and supermarket magnate Ron Burkle announced in March that they would invest $200 million in Brazil-based ethanol producer Brenco. And billionaire George Soros is investing $900 million in another ethanol company.

Observers say that U.S. investors are attracted by a thriving software developer community, low labor costs, and a stable government and currency, despite periodic economic upheavals in recent years. They also are drawn by the fact that the United States is much closer to Brazil in terms of time zones than it is to India.

Intel, Hewlett-Packard, and other well-known U.S. tech companies are experiencing solid results there. Google, which bought Brazilian search company Akwan in 2005, is expecting revenue growth there of up to 200 percent this year. Investments in ethanol, soy-based biodiesel, and other segments of cleantech also are growing. That is likely to continue unless oil prices take a precipitous fall, says Laurence Alexander, an analyst at Jefferies & Co.

Like many developing countries, Brazil is a fan of open-source systems. Partly for that reason, IBM is expanding its Linux Technology Center there, says Claudia Fan Munce, managing director of the IBM Venture Capital Group. To counter the rise of Linux, Microsoft announced plans last month to offer scaled-down versions of its primary desktop software products for $3.

Of course, not everyone is on the next plane to Rio. Some U.S. business leaders are unhappy about Brazil's recent decision to break patent rules and permit government purchases of a generic form of a Merck HIV drug. "High-tech investment really depends on the protection of intellectual property," says Mark Smith, executive vice president of the Brazil-U.S. Business Council. "Unfortunately, Brazil has had a relatively mixed record."

—Herbert A. Sample