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COVER STORY

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## Extreme Investing: Inside Colombia

An improbable journey from crime capital to investment hot spot. Can this boom last?



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"You going there to get some kilos?" asks the driver as he drops me off at Newark's international airport for my six-hour flight to Bogotá. He grins at me in the rear-view mirror as if he has cracked the most original one-liner in history. "Like Scarface," he continues, shifting to his Pakistani/Latino gangster accent: "Say hello to my little friend! Pow! Pow!" He hands me my bags and reminds me to call my mom and make peace with the Almighty before I embark for certain death. "You are crazy, my friend."



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Traveling to Colombia to chronicle the investment miracle unfolding there seemed perfectly reasonable a few weeks earlier. The stats all scream "Go! Go! Go!": Colombia's stock market has soared fourteenfold since October, 2001. Foreign direct investment and capital inflows have more than doubled, while real estate prices have tripled in many areas. Citigroup ([C](#)) CEO Chuck Prince even kicked off his February "world tour" in Bogotá, where the bank is building branches and a Latin American call center. But when most Americans hear the name Colombia they think about the late Medellín drug lord, Pablo Escobar. And roving paramilitary death squads. And speedboat-loads of cocaine headed for Miami.



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I've been assured by bankers that things are getting much better in this nation of 42 million. But it isn't until I step onto the packed 737 to Bogotá that I get my first real sense of the intense interest in Colombian investments. I spy at least 20 business suits, including the laptop-toting Swede sitting next to me who's building a boutique hotel in the beautiful 16th century city of Cartagena on the north coast.

Investors like these have visited many exotic ports in recent years. Colombia's surprising rise has been

fueled by two larger trends: the enormous amount of money sluicing through global markets and investors' increasing risk tolerance. First, cash poured into the so-called BRIC countries—Brazil, Russia, India, and China. Next it flooded riskier secondary destinations such as Turkey and Poland, and last year, with ferocity, Vietnam. Now money is gushing into third-tier hinterlands fraught with political and economic problems, where even the rule of law isn't a given.

### THE *CONFIANZA* INDEX

Call them extreme emerging markets. The Standard & Poor's/IFCG Frontier Index of 22 such destinations, which includes investing curiosities like Lebanon, Côte d'Ivoire, and Bangladesh, has gained nearly 400% in the past five years. The question is whether these nascent markets have what it takes to parlay the fickle enthusiasm of hedge-fund traders and other investors into long-term economic development.

Yet Colombia is so extreme that it hasn't even made the Frontier Index. Its stock market has an aggregate capitalization of just \$59 billion. In this parallel investing universe, price-earnings ratios take a backseat to fuzzy measures such as *confianza*, which translates into confidence and trust but is more accurately described as the general sense that people can safely transact business and get through everyday life unharmed. The handful of Wall Street analysts who cover Colombia supply their clients with charts of murder rates and kidnappings.

President Alvaro Uribe, who took office in 2002, nearly five decades into a civil war that has pitted Marxist guerrillas against right-wing death squads, has made *confianza* his overarching goal. Killings and abductions are down sharply in the big cities, and that has been a boon for all manner of investments, from stocks to real estate. "I guarantee that if you graph the decline in kidnappings to investment gains, the correlation would be one-to-one," says Ben M. Laidler, head of Andean research for UBS Pactual.

On a continent whose economic history is the stuff of a blooper reel, Colombia's strong fundamentals stand out. Its \$130 billion economy, a world leader in the production of coffee, petroleum, textiles, and flowers, is growing at 6.8% a year, two full points faster than the Latin American average. In the past 10 years, Colombia has slashed its inflation rate from 18% to 5%, and since Uribe was elected, unemployment has dipped from 16% to 13%. The nation has never defaulted on its debt or experienced hyperinflation. And entrepreneurial thinking is spreading. Run a Google ([GOOG](#)) geographical-hit query, and you'll see that, per capita, nowhere in the world are there more searches for the words "Peter Drucker," the late management guru, than in Bogotá. No. 2? Medellín.

Yes, Medellín. Once the murder capital of the world, this city of 2.4 million is regaining its status as a commercial hub, hosting regional offices for a growing roster of multinationals including Philip Morris ([MO](#)), Toyota ([TM](#)), and Renault, as well as globally minded Colombian companies that make up 70% of the country's stock market value. More high-rises are under construction here than in Manhattan and Los Angeles combined.

But all of it—the stock market gains, the development, the rising living standards—rests on *confianza*. Foreigners' view of Colombia as a lawless, violent, riven land won't change quickly. As Commerce Minister Luis Guillermo Plata acknowledges, "Why would I invest in a country if I can't go there?"

As I get into the cramped cab that's taking me to my hotel, I can't help thinking about the fabled "millionaire's tour of Bogotá," a stretch of road where colluding cabbies and thieves once drove passengers from ATM to ATM to drain their bank accounts. And then there's the drugs. Colombia still produces the majority of the world's cocaine, an ongoing crisis that draws a steady supply of U.S. military and financial aid. Even corporate crime here takes on deadly overtones: Cincinnati-based banana giant Chiquita Brands International ([CQB](#)) was in the news recently for admitting to having paid \$1.7 million in protection money to a Colombian paramilitary group on Washington's list of foreign terrorist organizations.

I'm here to find out whether Colombia's fledgling stock market can keep surging, whether its financial and physical infrastructures can accommodate the flood of investment, and whether an equity culture can take hold.

At the center of everything is President Uribe. "We need to rescue international confidence in our country," he tells me in his heavily guarded compound in Bogotá's historic center full of Spanish colonial architecture. Access to Uribe is preceded by an hour of security checks and chilling looks from guards holding bayonet-tipped machine guns.

The 54-year-old Uribe is a rarity in increasingly leftist Latin America. A center-right ruler with an approval

rating of more than 60%, he won a landslide second term in 2006 after having amended the constitution to allow him to run again. Uribe knows Colombia's history of violence firsthand: A decade ago he was governor of Medellín's province, and in 1983 his father was murdered by kidnappers. The sometimes dour leader has driven most of the drug traffickers and leftist guerrillas out of urban centers, though they still reign in remote regions.

But allegations have surfaced in Colombia that the President himself has links to right-wing paramilitaries who murdered hundreds, including labor-union activists. On May 14, 20 Colombian lawmakers and businessmen were arrested on charges in connection with the scandal. Colombia's police chief and head of police intelligence, meanwhile, were ousted amid allegations of illegal wiretapping of opposition politicians and journalists. Uribe vehemently denies any personal connection to the affair. (See [Alvaro Uribe: The Change Agent](#)).

Despite his obsession with law and order, the economy is never far from his mind. "The state is the most important private enterprise," he says, "and the public is like a universe of shareholders." Javier Vargas, a Colombian banker with Credit Suisse ([CS](#)), has heard Uribe sound that theme many times. "He talks like a person who is selling and marketing his country," he says. "Investor confidence is key for him." In May, Uribe visited Washington to meet with supporters in the Bush Administration and lobby congressional Democrats on a free-trade pact between the two countries. Democrats have been uneasy with Uribe since the recent allegations surfaced. But Colombia is a vital strategic ally in an increasingly hostile continent, bordered by Hugo Chávez' Venezuela and left-leaning Ecuador. Washington has sent Colombia \$5 billion in aid since 2000, including \$650 million last year; only Iraq, Egypt, Afghanistan, and Israel receive more.

For Uribe, a deal is crucial both for the tangible economic benefits and the perceptual ones. He has invested much political capital already, visiting the U.S. at least 25 times since taking office. Winning full free-trade benefits with the U.S. would do much to bolster the fragile investor confidence he has been nurturing, while a loss would damage his prestige. Uribe's challenge is one that everyone, from business leaders to taxi drivers, acknowledges. "Investing here is rooted in improving physical safety and lowering the risk of doing business," says Alexander P. Kazan, a Latin American strategist at Bear Stearns & Co. ([BSC](#)). "You really cannot overstate the importance."

### **SLEEPY EXCHANGE**

On a cool April morning, I make my way to Bogotá's bustling financial district. Amid the roar of motorcycle engines and a haze of bus exhaust, the district brims with young professionals sipping *tintos*—tiny cups of dark coffee—while chatting on newfangled cell phones. At every crosswalk and on street medians, the less fortunate hawk snacks, cigarettes, and telephone calling cards from salvaged baby carriages, stark reminders of the gaping disparities in this poor nation.

Halfway up a glassy office building is an ultramodern floor containing Colombia's stock exchange, the Bolsa de Valores. It's high-tech, but no one would confuse it with the NASDAQ. Just 12 people sit around a circular table staring at their flat-panel displays in a space no bigger than a conference room at a Best Western hotel. It's so quiet you might think you showed up to take the GMAT. I jokingly ask if we're at the right place. Our photographer wonders aloud if he should bother unpacking his equipment.

"This is it," says Jaime Sarmiento, the exchange's 34-year-old communications director, sensing the anticlimax of the moment. He points up at the ticker, a circular LCD sign. "Does anyone know how to turn this thing on?" The specialists on the floor arrange a photo op, choosing a mustachioed elder to sit on the elevated chair in the center of the ring and motion as if he is directing order flow. Truth be told, everyone is just waiting for 1 p.m., when the market closes and the power lunch scene takes hold. When I ask if the early close is a vestige of the Spanish siesta, I'm curtly told that it's purely a result of how little business there is to transact. Sarmiento takes us downstairs to tour the *café*, a swank lounge that was conceived as a high-energy, high-buzz meeting place for stock junkies. On this day, two or three guys sit around reading the paper, blissfully unaware of the handful of digits flickering on the wall-mounted display above.

Such sleepiness belies the market's breathtaking volatility. This is the central paradox of extreme emerging markets: With so few buyers and sellers, small upticks can quickly turn into major surges, while the faintest of downticks can lead to painful routs. After posting a 128% gain for 2005, second best in the world, the Bolsa nosedived 45% in two months during last year's late-spring emerging-markets swoon, the second-worst showing on the globe. It has since jumped 75%; on June 15, 2006, alone, the index gained 16%. It's down 5% in 2007.

All the choppiness merely confirms the suspicions of most of the locals, who eschew stocks for government

bonds, even though they yield just 6% now, a third of what they did eight years ago. "The general public just isn't all that accustomed to stocks," says Rodrigo Jaramillo, CEO of Interbolsa, the country's largest brokerage, and former chairman of the stock exchange. He notes that fewer than 70,000 Colombians bought local shares in 2006.

Even people who invest for a living are reluctant to buy Colombian stocks with their own money. "I like to invest in young cows," admits a 26-year-old private investment adviser in a British-spread collar and Hermès tie between bites of an empanada in a breakfast joint near the exchange. His eyes light up as he explains that his uncle has given him dibs on investing in heifers, an inside opportunity that has lately scored him 20% to 30% annual returns. Why dabble in risky stocks, he asks, when he can collect steady returns on the family ranch? "I sponsor the cows until—how do you say?—graduation," he says, grinning diabolically, of the day when they're auctioned off and he reaps his windfall.

But in fits and starts local investors are coming around. I'm struck by how many twenty- and thirtysomethings in Bogotá are at the leading edge of business and civic life: chief executives, money managers, restaurateurs, even cabinet ministers. Young and educated, Colombia's new elite could ply their trade anywhere in the hemisphere. A decade ago there would have been no question that they would end up abroad. Just four years ago, Bogotá's Club El Nogal, a hot night spot, was car-bombed by a leftist rebel group, resulting in 36 deaths. But El Nogal has come back stronger than ever. Even with all the bomb-sniffing dogs, the place is nearly impossible to get into on a weeknight. Bogotáns consider it a metaphor of their resilience.

I meet some young professionals for dinner at Balzac, a restaurant modeled after Manhattan's trendy Balthazar. José María de Valenzuela, a recently minted MBA at INSEAD in France, lights a cigarette and reflects on his accomplishments. "There was just a small possibility I'd end up back here," he says. All of 32, Valenzuela, who did his undergraduate work at Brown University a decade ago, used to specialize in what you might call distressed investing. "People were afraid to leave the city," he recalls of the siege mentality of seven or eight years back, when terrified families sought escapism at his miniature golf course in Bogotá. "You could buy real estate just for the cost of the taxes." Which is what Valenzuela did, before selling into a property boom and plowing his winnings into what he and a former finance professor correctly thought would be the start of a roaring bull market for stocks. Last summer, Valenzuela rolled those profits into a partnership with HenCorp Futures, a U.S.-based trading firm, to offer currency strategies to foreign investors—a critical building block to outside participation in the Colombian market. The only way to buy Bolsa-listed stocks directly is in pesos, and there are no pure-play Colombian mutual funds available to foreigners.

The next afternoon, on Valenzuela's recommendation, I head to Harry's Bar, in a tony Bogotá neighborhood that resembles San Francisco's Russian Hill. Amid the din of clinking wine glasses, blond-streaked women and sharply dressed men pick at plates of seared tuna and Argentinian steak. In the evenings the place is often overrun by actors, soccer stars, and diplomats. The owner, spotting my reporter's notebook, stops by. "Please tell America we're not a bunch of drug dealers shooting at each other from trees," he says.

## **COFFEE BUZZ**

In walks my lunch guest, Felipe Gaviria, the boyish money manager whose name is on the lips of everyone in the smart-money set. In 1997, at 23, Gaviria was promoted to head of currency trading at a small bank in Cali. Two years later he left for business school in Barcelona. He returned to Colombia when Uribe was elected in 2002, sensing the moment was right to buy Colombian property and bet that the peso would strengthen against the dollar. Now he oversees \$3 billion in pension assets for Spain's Grupo Santander. It's common knowledge that Gaviria is being wooed by bulge-bracket investment banks and hedge funds. "I receive everybody," he says coyly.

With more money pouring in as the economy grows, Gaviria says he's impatient for more local investment options. Fortunately for him, some big ones are just around the corner. In an audacious move, Procafecol, of the fast-growing Juan Valdez coffee shop fame, is floating its shares on the Bolsa. The unlikely beneficiaries: thousands of rural *caficultores*, or coffee growers, who make up Colombia's national coffee alliance. They've recently been swarmed by an army of financial advisers dispatched to the countryside. "Your preferred shares give you dividend priority over ordinary investors," reads the glossy offering letter, as if to poke fun at the more cosmopolitan Class B shareholders.

The real game changer could be the \$4 billion initial public offering of state oil concern Ecopetrol, one of South America's four largest. In short order, it could become the most widely held stock on the exchange. And with U.S. bankers circling, a New York Stock Exchange ([NYSE](#)) listing could be in the offing. The only

other Colombian stock listed in the U.S. is Medellín-based Bancolombia ([CIB](#)), whose shares have jumped twentyfold in the past five years.

Indeed, Wall Street is doing its best to ride the Colombia wave. In 2005, SABMiller ([SAB.L](#)) PLC took over Colombia's biggest brewery, Bavaria, for a record \$7.8 billion, with Merrill Lynch ([MER](#)), JPMorgan Chase ([JPM](#)), Lehman Brothers ([LEH](#)), Morgan Stanley ([MS](#)), and Citigroup ([C](#)) advising on the acquisition. Last year ABN Amro advised on the sale of a controlling \$657 million stake in a key oil refinery to Switzerland's Glencore International. "You're having more and more investment banks going into Colombia," says Eric Newman, a Bogotá native who was recently poached from Lehman Brothers by Morgan Stanley to cover the country for its Miami-based Latin American private banking arm. He shuttles to Colombia 20 times a year.

Not only are Colombia's top companies doing better at home, they're also branching out to the rest of Latin America and beyond. A company called Chocolates, essentially Colombia's Kraft Foods ([KFT](#)), now ships to Los Angeles and the Southwest, while Argos, the country's foremost cement producer, has been buying operations in Arkansas, Georgia, North Carolina, and Texas. Bancolombia recently acquired El Salvador's largest bank.

One sign of the rising fortunes in Colombia is the sudden misfortune of the self-proclaimed Bulletproof Tailor. Miguel Caballero makes suits and other apparel tough enough to withstand gunshots. His garment factory, located in a seedy neighborhood of Bogotá, features a picture gallery of famous customers, including action film star Steven Seagal and President Uribe, as well as glossies of Caballero discharging his handgun into the bulletproofed torsos of employees. Ten years ago, he says, his company sold 70% of its wares in Colombia. Now, thanks to the ebbing violence, that figure is just 20%. Caballero is dispatching salesmen to Russia, Venezuela, even Iraq. "The idea is to save the business," he says. "You can say we're globalizing."

The growing confidence in Colombia brings a new set of challenges. The streets are safer, and citizens are road tripping again. Export-import activity is steadily growing. Tourism has nearly tripled in five years, and beach-lined, historic Cartagena is among South America's most expensive real estate markets. But with all of that happening, Colombia's highways, roads, ports, and other industrial backbones are becoming increasingly overburdened. "We're really behind on infrastructure," says Juliana Ocampo, a recent MBA from Massachusetts Institute of Technology who returned to Bogotá to work for Mexican cement giant Cemex. "If you ask everyone here, that's where the investment needs to flow next." Says Gaviria, the young money manager: "Our north port is terrible. If we had a world-class port project, I would invest right then and there." Bear Stearns warned in a recent report that growth could halt if tens of billions worth of infrastructure isn't soon built, noting that Colombian pension funds are clamoring to invest. If the buildout stalls, it will undermine Uribe's reforms.

## **STOCK OPTION**

I take up the issue with Vice-President Francisco Santos. Schooled in Texas and Kansas and formerly the editor of Colombia's largest daily newspaper, Santos was once kidnapped by Pablo Escobar's men and surely draws satisfaction from the fact that the cartel's late-'80s vehicles sit rusting in a pound adjacent to his office. "The roads are getting so clogged," he concedes. "But who will pay for all the infrastructure?"

Financiers argue that the money is there for the taking, if only the government would change its thinking. Historically, Bogotá has issued bonds to fund such projects, but investors were hungrier for them when they yielded 20%. It also takes time to rouse all the layers of bureaucracy in the way. Bankers want the government to sell equity in the projects instead, following the privatization trend sweeping Europe and the U.S. "We can build roads without a penny of government money," insists Pedro Nel Ospina, the head of Corficolombiana, one of the country's top investment and merchant banks. "Let us do it already. Give us equity."

The government isn't ready to make that leap just yet. But the fact that a vigorous debate about how best to become an ownership society is heating up—complete with business page editorials and regional free-trade zones—shows how far this rugged stretch of the Andes Mountains has come.

Medellín, in particular, is undergoing one of the most extraordinary urban makeovers in modern times. "Our trucks, drivers, and distributors were attacked at least once a day," recalls Carlos Enrique Piedrahita, president of Chocolates, of the scene seven years ago. "Now it just doesn't happen."

The 45-minute ride to town from Medellín's main airport winds through lush forests and fragrant flower farms. The city is shaped like a bowl, with commerce and wealth concentrated at the center as poverty

stares down from the rim. It all descended into chaos with the decline of Medellín's textile industry in the 1970s and the simultaneous rise of the drug trade. In 1991, two years before Escobar met his end in a rooftop gunfight with police, he was recruiting cocaine-addicted teens in the hillside slums, paying them \$750 for every police officer they murdered. Gang shootouts continued into emergency rooms. "One can have the impression that Medellín is about to drown in its own blood," *The New Yorker* magazine's Alma Guillermoprieto wrote in 1991, when the city's homicide rate was 381 per 100,000, the highest in the world.

But exploding revenue from Medellín's resurgent corporate tax base is funding a rapid metamorphosis. Now those very same shanties are connected to the city center by a sky-lift gondola of the sort you might find at EPCOT Center. New libraries and schools court students from other parts of Colombia. "Imagination Park" stands where murdered bodies were once dumped. The business assistance office in the heart of the slum is helping tiny food stores and Internet cafés flourish where there used to be only crumbling cinder block and exposed sewer pipes. Today, Medellín's murder rate is 28 per 100,000, lower than those of Baltimore and Washington, D.C.

Statistics alone don't capture the sense of rebirth here. Atop the slum, in the shadow of ascending gondolas and a new computer lab, the city's poorest children think they're kings of the hill. They chase after me, tugging at my jacket, 30 or 40 at once. It's not my money that they want, it's pictures of themselves and their friends. As I sit down to catch my breath, a runty seven-year-old boy with a precocious understanding of digital photography suddenly climbs out from under the bench. "I don't have e-mail yet," he says. "So print it for me for when you come back, O.K.?"