

Industry Response to New Protectionism

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Thierry de Montbrial

Is Total a French company? Is L'Oréal a French or Swiss company? In this session, we would like to see how two large international companies are affected by what geopoliticians or geoeconomists perceive as the major uncertainties for the future. Their operations are indeed geopolitical by nature.

Total's and L'Oréal's market capitalization as at April 3, 2019 is very close; L'Oréal prevails with 134.6 billion euros, ahead of Total at 132.1. When we look at turnover, it is 177 billion for Total and 27 billion for L'Oréal. As for operating profit, it is 13.6 billion euros for Total and 4.9 for L'Oréal; the net result is 11.5 for Total and 3.9 billion for L'Oréal. Cash flow is 10.3 for Total and 3.9 for L'Oréal, and investments are 10.5% for Total and 1.4% for L'Oréal. In terms of staff, Total has 104,000 and L'Oréal 86,000. How is it that the market capitalization is the same, with such different figures? How is it that Total's market capitalization is not markedly higher than L'Oréal's? Could there not be explanations related to geopolitical uncertainties behind this?

Oil and gas: specific geopolitics

Patrick Pouyanné

All of this raises the question of the future of large oil and gas companies. We are in a world where energy transition is gaining a foothold. This is why Total is implementing not only an oil and gas strategy, but also an electricity one. The question is, really: what will the future of our companies be? Of course, the framework of our thinking is geopolitical. Our largest competitors are "Anglo-Saxon", the major global shareholders are American and British, and as always, they prefer to invest in companies in their country rather than those in a Europe, whose geopolitical future seems uncertain. Many US oil companies are just about 1.5 times larger than mine.

I would like to recall some characteristics specific to the world of energy.

It is a very capital-intensive industry. Companies like ours must develop resources in many countries that lack the financial means to do so themselves. It is a long-term industry (we invest in projects over 20 or 30 years); an industry that implements a lot of technical skills (engineering) – we have to provide a strong innovative capacity: you do not improvise as a geologist or driller... Finally, this industry affects states' national sovereignty. Our profession is to develop the natural resources of the countries we work in, and these natural resources generate significant tax revenue. Therefore, we are a key partner of the states involved.

What kind of protectionism are we facing? Historically, oil and gas resources were discovered by private companies. Total was founded in the Middle East in 1924. Over the years, there has been a strong tendency for countries to take back control of their natural resources. This goes back to the issue of local skills training. Countries now use regulations putting some forms of protectionism in place in order to train their local content. For five years, south-eastern Asian countries have been taking back control of their natural resources, while for decades they had trusted large private companies. It is renationalizing resources, rather than protectionism. In Africa, this is not happening yet; for the time being, leaders of these countries know that they need our companies' skills and financial resources.

We are scarcely affected in our profession by tariff and customs barriers. Oil crosses many borders and everybody needs it. When we talk about protectionism, we think about US secondary sanctions. The United States and China use such weapons to skew international competition to their benefit. Washington uses all the strength of its capital (besides, 40% of Total's shareholders and bondholders are mainly in the United States) to impose extraterritorial laws. For example, we had no choice with regard to Iran. If we had stayed in Iran, the American president could have decided to deny Total access to the entire US financial system. Yet we cannot manage Total and reinsure it without the US's financial system.

Similarly, in China, forms of protectionism are obvious as part of a state economy. China accounts for nearly 40% to 50% of the global renewable energy market. If we want to develop in this market as a foreign company, we do not have access to the same state subsidies as our Chinese competitors. Total has also just signed an agreement with a Chinese company to set up a joint venture in the battery field – the electric bicycle market is Chinese, and for a year all of Beijing has been traveling by electric bicycle.

Access to the Chinese market is therefore possible but restricted, and protectionist measures are taken. If Total goes to court against a Chinese company for an intellectual property matter, the chances of Total winning are low... And this restricts my development.

These developments are a challenge for Europe. To adapt, we have our skills, our size (having a considerable balance sheet is very important: it helps to absorb geopolitical risks; for example, even in the event of a crisis with Russia, Total could survive). We prefer to engage with these countries rather than to fight them. We work with many national companies in countries that want to nationalize their resources. Total has agreed to set up joint ventures with skills transfer, which helps us to win contracts, for example in the Middle East. Total's biggest global partner nowadays is PetroChina. We decided about ten years ago not to fight them, but to engage with them.

In our world, the fact of being French is far from being neutral. In the market we're talking about, Total is the only non-"Anglo-Saxon" company. As France is a member of the Security Council and one of the few countries able to project its troops into various theaters of operation, some agree to entrust a part of their natural resources to Total, which they consider as an alternative to the "Anglo-Saxon" or Chinese world. We can play the nationality card – and some people abroad think that Total's shareholder is the French state. In reality, the French state holds no Total shares ; our shareholders are about 20% French and the rest are mainly British and American.

I would like to add that our reality is multilocal. People often ask me: "How are you at this point in time the biggest oil company both in Abu Dhabi and Qatar, and working in Saudi Arabia?" The response is that we are multilocal: we provide our best expertise worldwide in the interest of each country.

Thierry de Montbrial

But today, how do you do it, go from Doha to Abu Dhabi?

Patrick Pouyanné

You can't do it by plane. When you go to a country, you commit yourself to that country. You can't explain, "I'm coming, but I must leave early to go and see your neighbor" – if that's the case, your contact partner's attention drops by two notches. This is diplomacy: the order in which I choose to go to Doha or Abu Dhabi may be interpreted by them as a

sign, when it may be a simple matter of schedule. Everything is interpreted and it is best to avoid going to both places in a short period of time. I was in Doha ten days ago. And I'll be going to Abu Dhabi soon.

Specific geoeconomics

Thierry de Montbrial

Jean-Paul Agon, it seems that geopolitics/geoeconomics hardly affects you.

Jean-Paul Agon

Geoeconomics affects us, but in very different ways. You cannot find two more different companies than L'Oréal and Total. L'Oréal makes consumer products, is targeted at 1.5 billion women and some 100 million men worldwide. Our products are not political – which is an advantage because we are in a non-strategic sector. For example, in China, they told me that cosmetics would not be part of the strategic sectors that could ultimately be regulated, which is reassuring. We are established in the world without really having contact with governments and politicians. The only thing that matters is that the women in these countries appreciate us. From this perspective, we are much freer.

However, we are not totally immune: some countries can close to us for different reasons; non-tariff barriers can be erected, like indirect regulations hampering operations. We try to compensate for this by a number of choices. First, we are very capital-light. We set up our factories worldwide, wherever we sell. We can also move our factories easily, move our supply chains, with a “light footprint” concept that provides us with a lot of agility. This is one of L'Oréal's characteristics, and has become crucial in recent years, since the world has become volatile, complex, uncertain and ambiguous. As we are everywhere – France only represents 7% of our turnover – we have to be constantly agile to anticipate movements.

From this perspective, I think that companies, and L'Oréal in particular, should be great partners (or clients) of think tanks. The world is becoming so unpredictable that it is very important to be able to be helped in the development of various scenarios, and to think about strategies of flexibility and agility in the coming years.

Thierry de Montbrial

You mentioned the JCPOA and the unilateral American termination of this nuclear agreement with Iran, which is a scandal, since, beyond the companies affected, it is confidence in the United States and even the

dollar that is affected. Although the Americans are short-term winners, they will be losers in the long term, because all the rest of the world, starting with the Chinese and even perhaps the European Union, will seek to get around the obstacle. Beyond this one-off problem, is there not ever-increasing greater politicization of the economy and law? How do you perceive it? Patrick Pouyanné, do you think that in some countries, you could be arrested getting off the plane?

Stability and legal certainty

Patrick Pouyanné

We companies are probably one of the sources of this insularity. The globalization movement has clearly dominated the global economic and political arena for 30 years, and has had obvious beneficial effects for some countries in terms of lifting them from poverty. Globalization has created actors like ours, who are perceived by some governments as supranational. We pay taxes in countries where we manufacture; hence the debate over whether we should not pay tax in the countries where the products are used. The trend is to want to create counterweights against the economic powers that the large groups have become. The GDP of Belgium is 150 billion...

I would be tempted to classify countries in two large categories: those where I can have confidence in the proper functioning of the legal system, and others. In the latter, the peace of mind that we must have to invest is of a different nature, and we take more risks there. This is a real issue, especially when we are investing significant amounts of capital in another country.

Can I be arrested on leaving an airplane? Probably not: when you lead a global group, the first rule is to respect the laws of the countries where we operate.

Thierry de Montbrial

Admittedly, but even in a state governed by rule of law, legal instability can occur. Jean-Paul, you are extremely active in China. Political authorities are obviously very present in these countries, but it must be said that they try to please you...

Jean-Paul Agon

L'Oréal is probably an exception. We sell beauty products that are scarcely taken seriously by politicians. The Chinese like L'Oréal. This works very

well, we pay them a lot of taxes, we comply with the ethical rules, environmental requirements, and we pay good salaries. I have respect for the Chinese, since they have understood that beauty products contribute to quality of life, whereas other countries think that it is a secondary issue. A Chinese minister asked me to make sure we serve all Chinese consumers: not just the middle classes, but also the working classes. He understood that we could contribute to developing the standard of living and the quality of life. It is the only country in the world where, once a month, the city authorities come and ask what they can do to help us develop our business better.

To return to the original question: are we French? Yes, L'Oréal is a French company. We were founded in France, our headquarters is in France, research is conducted in France, although only 7% of our turnover is made in France. Beauty, like the luxury sector, is part of the "French genius" and it is a field where we can take pride in being the best in the world, although we are no longer the only ones. At the same time as GAFA, we can talk about KHOL (Kering, Hermès, L'Oréal and LVMH), which have quite comparable growth to that of GAFA.

L'Oréal feels French and is fundamentally European. Our major competitors are American, Japanese, Korean, and in the future Chinese and Indian. We don't use European companies' soft power enough to fight against the rivalry of the US and Chinese empires. We have companies in Europe that are present all over the world and that, along with their economic power, have a real impact, which is not used enough in the global geostrategic great game.

What is the future for China?

Thierry de Montbrial

Doubtlessly, Europe is going through discomfort; if we manage to come out of it, we will probably be able to better exploit our advantages.

We are struck by the increase in political authoritarianism in China. Many intellectuals no longer dare to talk to us, without mentioning the use of modern technology to monitor the population 24 hours a day, as will no doubt be the case in the smart cities of the future. What perception do you have of the country's development, apart from the helpfulness that L'Oréal can benefit from locally?

Patrick Pouyanné

China is managed like a super company of a billion people. The organization is remarkable, including in terms of human resources management,

and the quality of our contacts is striking. A top business executive explained to me that in China there is a human resources organization, dedicated to finding high performers, directly attached to the prime minister's office, and that it manages appointments to large companies.

The Chinese have entered a second wave of their entrepreneurial development. The first wave started with the state-owned companies, the monopolies. The second phase will be based on private companies, which will move the system forward, and result in more openness. The contracts that I was able to discuss lately in Shanghai are much more "Western" than those I have known previously. We must learn to put ourselves in the place of the Chinese in China. Chinese digital technologies are incomparably greater than those we make in Europe. We are ten years behind. I am not defending China. Yes, the system is organized and very controlled; but it is rapidly changing and I think the gains and benefits are greater than the remaining restrictions. Despite everything, some freedoms are opening up in the country.

Jean-Paul Agon

The Chinese Communist Party has changed in the last five years into an incredible technostucture. It has 50 million members; it therefore has a very programmed human resources organization, with a meritocratic system. People who come up through the ranks rise up through loyalty to the Party and through performance – performance indicators are also very accurate. The Chinese probably have the only mayors in the world with binding performance indicators in all areas (pollution, security, standard of living). Nowadays, in China, we are already in the 22nd century.

I follow China's development, since I go there about two times a year. China was behind for a long time, but now it is ahead of us, and ahead of Silicon Valley in many areas. It's a different system, with its risks and opportunities, which is part of the game.

Thierry de Montbrial

I am not sure that the terms "democracy" and "liberal" apply to China, but it's clear to me that, if the so-called liberal democracies are in danger, it is because they are no longer effective. The problem with liberal societies is they are increasingly worse in their state and sovereign roles, as well as in their executive roles.

