Large global transitions are affecting economies and the way businesses and governments cooperate. These transitions, or megatrends, include demographic shifts, economic power transitions, accelerating urbanization, climate change, and technological breakthroughs. A business’s approach to domestic and global incentives must evolve to meet the changing landscape reflected in these megatrends. Companies that anticipate and react to these transitions will gain significant strategic advantages, which could lead to greater market share and profitability.

Economic power balance shifting to developing countries will impact a business’s domestic and global incentives function

In this article, we explore how the shift in economic power from developed to developing countries may impact a business’s domestic and global incentives function. The shift in global economic power from developed to developing countries will demand a more in-depth understanding of tax and business incentives available to organizations from jurisdictions around the world. Undoubtedly, how such incentives are used to offset initial startup costs and ongoing expenses will be critical to an organization’s ability to improve margins and increase profits.

Companies may overlook the opportunity to negotiate valuable incentives for funding because they simply do not know what is available in various regions of the world. Companies need to stay informed about the types of programs offered outside the United States by nations with a strong desire to be key players in the global economy. Understanding the opportunities available requires a coordinated approach built on a global perspective that allows for the identification and evaluation of potential tax benefits and economic incentives.
The shift from developed to developing countries

The global balance of economic power is shifting from developed to developing countries. This trend will have a significant impact on where growth opportunities arise and will trigger a dramatic realignment of global business activity and spending power.

For example, we will see this long-term economic rebalancing reach a tipping point as emerging markets expand their global influence. In 2009, the total gross domestic product of the E7 (China, India, Brazil, Russia, Indonesia, Mexico, and Turkey, the world’s seven leading emerging nations) was about two-thirds that of the G7 \(^1\) (US, Japan, Germany, UK, France, Italy, and Canada). According to a PwC analysis, by 2050, these positions will be reversed, with the E7’s aggregate GDP rising to almost double that of the G7. As developing nations become more prosperous, their citizens will demand more high-quality goods and services. To meet this demand, companies will have to expand or relocate facilities and distribution channels.

Shifting the global economic balance from developed to developing countries will require businesses—large and small—to increase their focus on global market share, new customers, and new markets. The trend impacts multinational companies seeking new opportunities for growth, as well as middle-market and private companies as they consider their supply chains or overseas competitors. We already see increasing demand from companies requesting ‘Location Selection Studies’ not only for the purpose of locating low-cost production facilities, but also to be ready to supply their goods and services in countries whose citizens are becoming more affluent.

Attracting and retaining businesses

The global economic power shift megatrend comes as global incentives are increasingly fueling efficient growth for international businesses. For years, countries, as well as state and local governments, have offered a number of inducements to companies willing to invest capital and create jobs in their jurisdictions as companies relocate or expand. For example, developing countries often support foreign direct investment (FDI) within their borders. FDI brings to a country an influx of capital, facilitates the transfer of technology, and boosts its citizens’ social mobility. Countries already offer tax incentives to drive FDI, and we expect the power-shifting megatrend to drive further reliance on non-tax incentives to attract and grow businesses that form the foundation of a country’s economy.

In addition to tax benefits, inducements often include loan enhancements, various cash grants, reduced utility rates, reduced social program costs, site selection and site preparation assistance, employee training and relocation support, and other financial incentives. Some of the benefits are provided via specific statutory provisions while others are discretionary and negotiated with government agencies. In many cases, both foreign and domestic governments are willing to work with companies to find ways to increase the probability of success for a new or expanding business.

Other factors—though not financial incentives in the strict sense—that can have a significant impact on the bottom line, and definitely drive business decisions on where to locate, include: politically and financially stable governments, effective trade agreements, business regulatory reform, an improved business climate, an educated workforce, sophisticated technology and telecommunication infrastructures, effective transportation networks and infrastructures, a stable and supportive economy, and protections from copyright and patent infringement. A number of jurisdictions also tout their cultural and lifestyle benefits including art and music centers, parks and recreation facilities, and other benefits.

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**Incentives promote capital investment**

As emerging countries grow and their workforces become more skilled, the competition among countries to attract and retain both industry and labor will intensify. Countries and regions will need to compete based upon the incentives they offer or risk job loss and investment locating elsewhere. Rising wages across the globe make simple cross-border labor arbitrage a losing proposition. Incentives become even more important as wage costs level out and stabilize.

PwC’s 2013/2014 Worldwide Tax Summaries Online\(^2\) provides a current summary of basic information about corporate taxes in over 150 countries, including tax credit and incentive information. These country summaries provide insight into the broad variety of tax credits and incentives offered by the E7 countries to incentivize business growth.

For example, Brazil offers investment project incentives that may provide for (1) total or partial tax exemptions, (2) accelerated depreciation, (3) low-cost financing, (4) sales tax exemptions, and (5) incentives for projects focusing on technological innovation. Additionally, regional tax exemptions or reductions may be available for the purpose of accelerating the development of certain less-developed regions and industries considered important to the economy.

India offers tax incentives primarily for new industrial undertakings in designated states and districts. Incentives may include: full or partial tax exemptions for up to 20 years, immediate expensing of certain qualifying capital expenditures, free or below-market land, and infrastructure improvements.

China provides industry-oriented, limited geography-based tax incentives. Emphasis is placed on ‘industry-oriented’ incentives aimed at directing investments into those industry sectors and projects encouraged and supported by the state. Incentives may include industry-specific tax reductions, tax holidays and exemptions, investment and foreign tax credits, and the potential expensing of research and development costs.

It is worth keeping in mind that certain countries, including China and India, no longer look to become major global providers of low-cost goods and services. These countries look to ‘up-skill’ their citizens and increase their technological resources to better compete in this global economy.

**Incentives develop a skilled workforce**

The world’s growing economies will make the transformation from centers of unskilled labor and production to those fostering talent and innovation. This transformation will necessitate a more sophisticated workforce. As these emerging markets grow, their success will hinge on businesses’ ability to attract and develop skilled talent. Governments have the opportunity to use incentives to encourage companies to provide increased training and development.

There is already evidence of a global skills shortage in the developing world. Manpower’s 2013 Talent Shortage Survey\(^3\) found that, against a global average of 35%, Brazil has one of the most severe talent shortages with 68% of employers reporting difficulty filling positions as a result of a lack of suitable candidates. India (61%), Hong Kong (57%), and New Zealand (51%) reflect similar talent shortages. When compared to 2012 figures, talent shortages are a growing issue within three Asian economies—China, Japan, and India.

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2 http://taxsummaries.pwc.com/uk/taxsummaries/wwts.nsf/ID/PPAA-85RDKF

3 http://www.manpowergroup.us/campaigns/talent-shortage-2013/
Survey results suggest that in both 2012 and 2013 the most difficult vacancies to fill were workers in skilled trades. Employers noted that the reasons for such talent shortages include a lack of technical competencies, a general lack of applicants, and a lack of experience.

This skills shortage will put additional stress on businesses to make talent planning a strategic priority. One solution to this problem is increased company training and development. However, businesses initially may not want to increase workforce training due to its cost, the loss of production, and skepticism on the return on investment. Government incentives may ease such financial concerns and help promote an educated and skilled workforce.

For example, Singapore has a Skills Development Fund to subsidize training, and it has operated a skills and technology transfer program with foreign governments and foreign direct investors to improve training. Similar country programs include Brazil’s SENAI, National Service for Industrial Apprentice, program; South Africa’s National Skills Fund; Chile’s FONCAP program; and Malaysia’s Human Resource Development Fund, dedicated to fulfilling the nation’s aspiration to attain the status of developed country by 2020.

As developing countries evolve, competition among countries to attract the best talent will only intensify. Countries will need to provide training incentives to remain competitive, and businesses will need to maximize these incentives to contain costs and remain competitive.

What this means for US domestic activity

Mature markets like the United States could see a loss of influence and become less attractive to businesses that seek to expand into emerging markets. One way to remain competitive is for federal, state, and local governments to increase efforts to attract businesses through tax and other government incentives. Whether referred to as in-sourcing, reshoring, or otherwise, businesses could experience a renewed effort by US policymakers to encourage them to increase activity in the United States. The US will remain competitive if it focuses on its strengths as a stable economy. By focusing on security, rule of law, as well as productivity and technology, the United States can retain its position as the world’s largest and strongest economy.

Increased domestic expansion may be desirable for many business reasons. For example, because China’s government has not historically enforced intellectual property protection laws, many companies that rely heavily on technology have decided to bring operations back to the US, rather than risk losing their investments in intellectual property. In addition, changing dynamics such as increased oil production and investments in alternative energy may reduce costs in the US, making domestic business expansion more attractive. New technology may decrease domestic production costs. Finally, the cost of doing business outside the US is escalating due to increases in wages, production costs, and shipping costs.

While economic power may shift to the East, that doesn’t mean the West will remain dormant. We expect US federal and state governments will increase efforts to encourage capital investment and job creation through the use of tax and other types of incentives.

Success flows from global understanding

As technology brings the world closer together and the focus of growth migrates overseas, a successful global enterprise must have a strong appreciation for the unique benefits many competing countries offer. The costs of doing business in these countries are often mitigated by the quality of tax and business incentives offered. In addition, businesses must be well attuned to the goals of governments and other resource

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7 http://www.sence.cl/sence/
8 http://www.hrdf.com.my/wps/portal/PSMB/MainEN/Corporate-Profile/About-HRDF
providers that wish to attract, train, and retain a talented and educated workforce. With this knowledge, businesses can reduce investment, hiring, and employment costs in order to remain competitive, both domestically and globally.

Companies must also consider how credits and incentive programs operate around the world. Just as in the United States, some programs are subject to statutory restrictions that establish clear guidelines for qualification. However, there are often discretionary programs that require negotiation with designated representatives of a tax or economic development agency. Without a clear understanding of statutory requirements and discretionary program guidelines, companies may miss important opportunities. In addition, they may unintentionally limit future expansion.

**Conclusion**

What used to be a competition among states, local jurisdictions, and regions for jobs and capital investment has now become a global contest for economic development opportunities. Knowledge of incentives as part of a robust ‘Location Selection Process’ is critical to economically manage and expand an international business. Businesses that recognize the power-shifting megatrend and adopt a global view of potential incentives will be well poised to compete and succeed in the ever-changing economic landscape.

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**Let’s talk**

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