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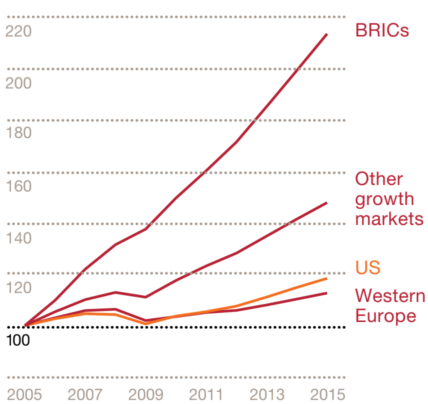
Emerging markets calling
Growth beyond the comfort zone

pwc

Emerging markets calling: Growth beyond the comfort zone

Businesses are going where demand is growing. That means venturing into new markets abroad —a move that doesn't come naturally to all private companies yet may be more manageable than they think.

Where the growth is



2005 = 100 GDP
Source: Oxford Economics

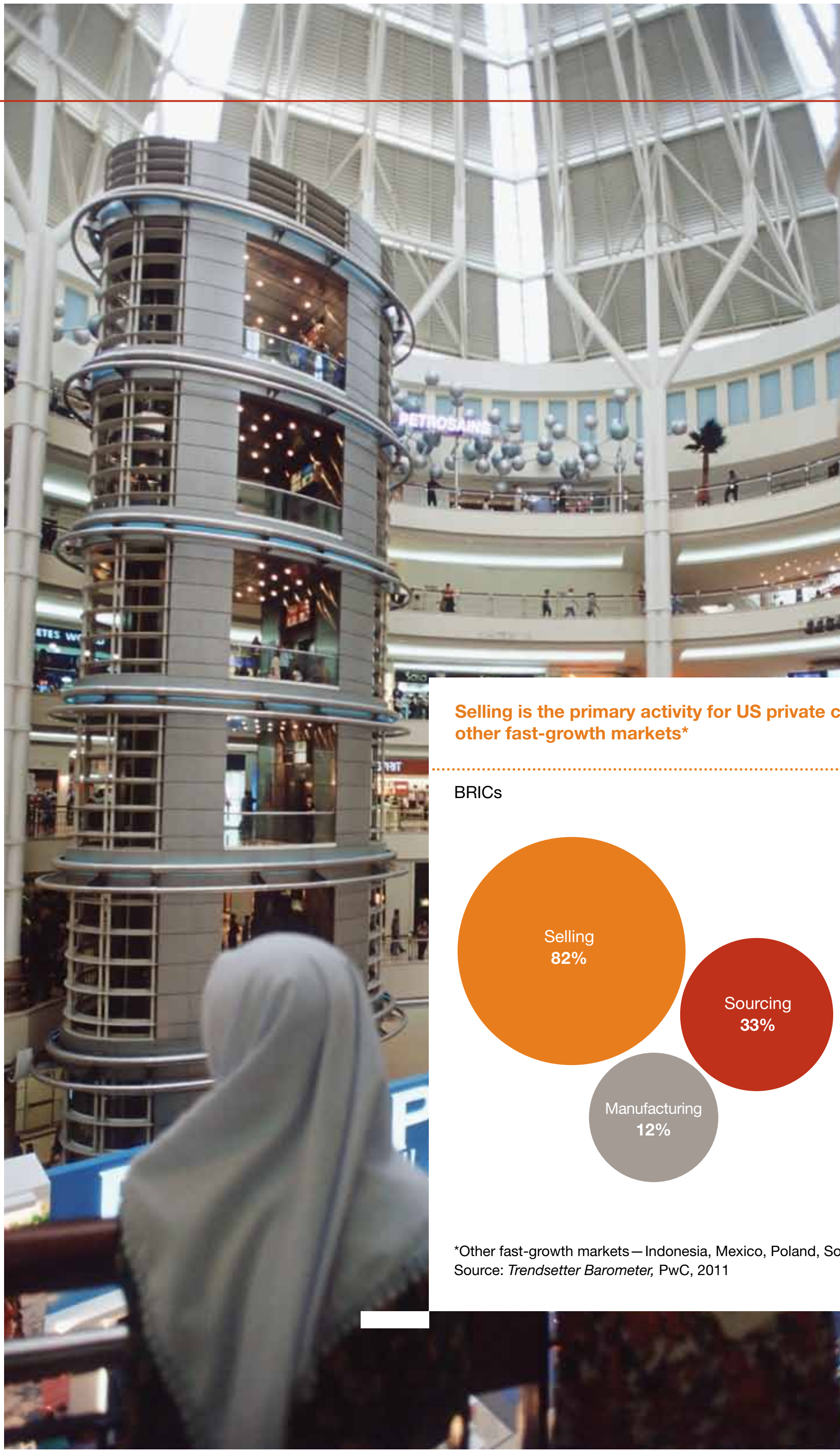
These are tumultuous times for the world economy. The United States continues to face massive debt, faltering growth, and stubbornly high unemployment. Europe, meanwhile, is contending with rising anxiety over whether the sovereign debt crisis will spread beyond the Eurozone periphery and ignite another banking crisis. The economic outlook for the Eurozone has dimmed accordingly, with US economic prospects brightening only slightly.[1]

These developments are more than just short-term gyrations; they underscore a fundamental change on the world playing field. While advanced economies in the West face an era of heightened uncertainty, escalating debt, and aging populations, emerging and fast-growth markets seem to be following a virtuous circle upward—despite their own sets of challenges—as they invest their newfound gains in education, technology, and infrastructure.

This global divide is evident in PwC's *Trendsetter Barometer* survey: Leaders of private companies operating in emerging markets foresee 18% sales growth in BRIC countries over the next one to two years, compared with 9.7% growth for sales here in the United States. For these companies, going global is essential for driving revenue. Foreign markets—particularly larger emerging countries with strong growth, vibrant populations, and sound credit ratings—are fast becoming targets for future sales.

"International expansion has gone well beyond trying to manufacture goods in low-cost markets," says Ken Esch, a partner in PwC's Private Company Services practice. "At this stage, it's really about increasing sales, growing the top line, delivering returns to investors, and making companies more profitable."

1 Oxford Economics, for one, puts the probability of recession at 15% for the United States, and puts at 80% the probability that the Eurozone economy is already in recession.

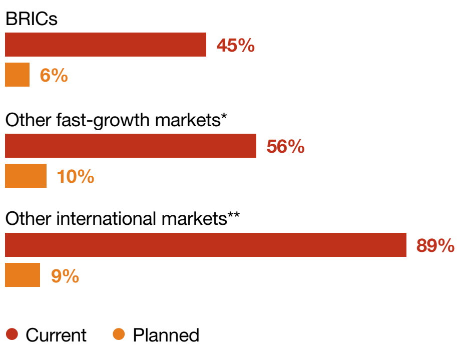


Selling is the primary activity for US private companies in the BRICs and other fast-growth markets*

*Other fast-growth markets — Indonesia, Mexico, Poland, South Africa, South Korea, and Turkey
Source: *Trendsetter Barometer,* PwC, 2011

Top international destinations for US private companies

Current and planned investment over the next one to two years



*Indonesia, Mexico, Poland, South Africa, South Korea, Turkey
**Canada; Central America; South America (other than Brazil); Western Europe; Central/Eastern Europe (other than Poland); Japan; Southeast Asia (other than Indonesia); other Asia (other than Japan, South Korea, China, India); Australia; Africa (other than South Africa); Middle East (other than Turkey)

Source: *Trendsetter Barometer,* PwC, 2011

That said, expanding into new territory can be challenging—particularly for private companies that traditionally have focused on markets geographically close or culturally similar to the United States (e.g., Canada, Mexico, and Western Europe). Impressive progress notwithstanding, emerging markets still have deficits in legal, commercial, and governmental infrastructure, to say nothing of corruption, financial issues, and language barriers.

But executives who are up to the challenge will reap the benefits: SVP Worldwide—owner of the Singer sewing machine brand—draws 61% of its revenue from international sales. “The trend for us has been higher growth in international markets, driven by a weak dollar and strong brand penetration,” says the company’s CFO, Marty Moore. At Cargill, the largest private company in the United States,[2] CEO Gregory Page attributed his firm’s resilience in 2010 ($107.9 billion in revenues) to its focus on overseas markets, including frontier economies: “The diversity in our business allowed us to deal effectively with uncertainty in the global economy.”[3, 4]

Seizing the moment

Fewer barriers, more opportunities

Companies looking to expand abroad are finding fewer barriers to entry than in the past. Looser trade restrictions and more effective financial systems encourage doing business in a global marketplace.

International shipping and logistics providers have made delivery of goods far more cost-effective and reliable. And technological advances, particularly in the areas of mobility and Internet access, have made it far easier to service and acquire customers. Ascendant technologies like cloud computing may be among those that are especially promising for private companies seeking expansion abroad, enabling them to do more with less.

Given all this, it’s little wonder that Hal Varian, chief economist at Google, claims that the future is all about *micromultinationals*—small companies that operate globally. “Even the smallest company can now afford a communications and computational infrastructure that would have been the envy of a large corporation 15 years ago,” he recently stated.[5]

Meanwhile, swelling numbers of middleclass consumers in emerging and other fast-growing markets have developed healthy appetites for Western products and, increasingly, have money to spend. There is also the burgeoning need for such products and services among rapidly expanding firms in those markets and the modernizing governments there. And of course, private companies often benefit from following their current multinational clients abroad.

Findings from PwC’s recent *Trendsetter Barometer* survey on private-company activity abroad confirm that many executives see global markets as a key opportunity for growth. When asked about the most important reasons for doing business abroad, *Trendsetter* executives cited expanding their customer base (80%) as the primary motive, followed by serving global clients better (43%) and compensating for slowed growth in their home market (33%).

Gateway markets—to the BRICs and beyond

Geographic and cultural proximity understandably make Canada, Mexico, and Western Europe cozy markets away from home. However, those well-charted regions have also begun to assume a vital new role as gateways to robust markets farther afield. Canada and Mexico often are the first stops on trade routes that lead to Asia and Latin America. Likewise, Western Europe is frequently a launch pad to Eastern Europe and the Middle East. Companies eyeing established markets in this new light recognize that if growth is a priority, they must venture beyond their comfort zones.

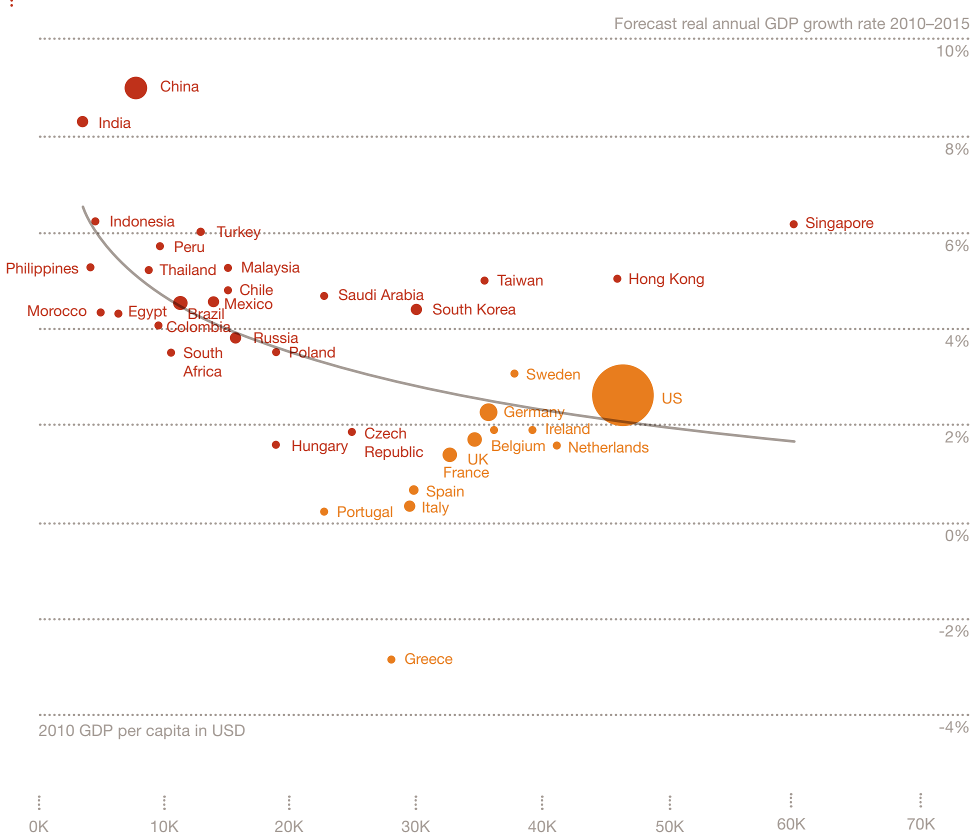
2 http://www.forbes.com/lists/2011/21/private-companies-11_land.html
3 http://www.cargill.com/news/releases/2010/NA3032488.jsp
4 http://www.cargill.com/news/releases/2010/NA3023517.jsp
5 http://www.foreignpolicy.com/articles/2011/08/15/micromultinationals_will_run_the_world?page=0,0

Among private companies that are doing just that, roughly half (51%) have a current or planned presence in the BRIC countries (Brazil, Russia, India, and China), while two-thirds (66%) are venturing into a second group of large, fast-growth markets comprising Indonesia, Poland, South Africa, South Korea, and Mexico, according to PwC's *Trendsetter Barometer*. "Each of these countries has a substantial population and growing consumer class," says Ashley Scott, a partner in PwC's Private Company Services practice. "While there are certainly risks to bear in mind, many globally expanding companies consider them proportionate to the opportunities, especially when weighed against the risk of continued stagnation in home markets."

Reluctance to leave familiar shores

Adaptation eases the way

Despite clear opportunities, many US private businesses remain unconvinced that going global is the right path for them. In fact, about half of all private companies in the *Trendsetter Barometer* survey have no international operations nor intend to pursue any.[6] Among *Trendsetter* companies that do operate internationally or plan to in the next couple of years (51%), the primary focus is on Canada, Western Europe, and Mexico; considerably fewer operate or intend to enter markets in the Middle East, China, Brazil, and India.



Growth trajectory

Emerging markets outpace mature economies

Size of bubble denotes nominal GDP in 2010. The horizontal axis is GDP per capita in 2010. The vertical axis is forecast growth rate in real GDP through 2015.

● Emerging/fast-growth ● Mature

Source: Oxford Economics

6 In contrast, all of the Western private companies that were canvassed in a separate survey (35% of them US companies; 47% Western European businesses) said they either have or plan to establish a presence abroad. Over 60% of those survey participants included middle-market companies with revenue ranging from $100 million to $1 billion: *Building a Presence in Today's Growth Markets: The Experience of Privately Held Companies,* PwC, 2011


Просто обратитесь к нам.
Услуги по установке?
Таймер
окончания стирки
1600 оборотов
Ремонтные услуги?
SAMSUNG

What's holding these US private companies back? By far, the leading response among *Trendsetter* companies selling solely in the United States is that their products and services are tailored specifically for the US market (42%). While that may be the case, it doesn't mean US companies must reinvent the wheel when they venture abroad. There is, however, generally a need to modify products and services to suit the requirements and budgets of customers in particular regions. Known as *glocalization*, this tweaking sometimes happens after a company is already in a foreign market. "It's not uncommon to see a private company's sales office in a foreign market evolve into an R&D center of sorts as they begin to better gauge the preferences of their local customers," says Esch.

The tweaking needn't be extensive. Although SVP Worldwide will develop a new, tailored product for a particular market if there's a strong business case for doing so—such as a Singer sewing machine that SVP designed specifically for the mass merchant sales channels in Germany and the United States—it isn't practical to do this in every market. "We don't have a lot of inventory that's highly customized," says Moore. "You can't do mass customization if you're trying to go international. You need a handful of basic models that you can tweak and sell across all markets." SVP recently took the model it designed for US and German big box stores and adapted it for the company's Argentine market.

Some companies have gone so far as to engage in "reverse innovation." Pioneered by large multinational firms, reverse innovation is a process whereby a company initially creates products and services for customers in emerging markets and then later rolls them out to mature markets. This approach not only can help firms penetrate global markets, but can also lead to innovative product ideas that help drive sales in home markets.

"You can't do mass customization if you're trying to go international. You need a handful of basic models that you can tweak and sell across all markets."

Marty Moore,
CFO, SVP Worldwide

Challenges in going abroad
As cited by private companies with international experience

	Total	BRICs	Other fast-growth markets	All other international markets
Finding the right business partner	68%	85%	76%	42%
Cross-cultural management	63%	79%	68%	42%
Finding adequate local talent	56%	69%	65%	36%
Security risks	49%	59%	53%	29%
Local regulatory requirements	48%	54%	49%	45%
Corruption	46%	54%	54%	19%
Local tax policy	42%	49%	44%	36%
Poor infrastructure	39%	49%	43%	23%
Distribution / supply chain	38%	48%	48%	16%
Contract disputes	36%	41%	35%	26%
Protecting intellectual property	32%	41%	37%	16%

Source: *Trendsetter Barometer, PwC,* 2011

What's the best strategy?
A flexible one

There is no single business development model for going abroad. Different markets vary as much as individual companies; a blanket approach won't work. Nor will a static one. A company should routinely update its strategy in international markets to keep pace with competition, customer preferences, and economic shifts.

Take SVP Worldwide, which has a global presence in 190 countries. Its best-known brand, Singer, has been sold abroad since the 1860s. As markets have evolved, so too has SVP's approach.

One such market is Turkey. Although SVP has been selling Singer sewing machines there for decades, the company has only recently begun doing so through mass merchants, with differentiated products. While commonplace in the United States, big box stores are still a relatively new phenomenon in Europe, but they're quickly taking off. SVP has switched gears accordingly.

In a market like Malaysia, on the other hand, SVP continues to rely on mom-and-pop stores to sell its machines. The same is true in India and China, where the company uses distributors to access dealer channels. Despite the immensity of those two markets, they are not big revenue generators for SVP: Sewing machines are outside the range of the average Chinese and Indian consumer, for now. "That may change in the next five years," notes SVP's chief financial officer, Marty Moore, "which is why we're establishing a toehold there."

The key is to be adaptable and poised to move when opportunity arises. "New channels continue to develop," says Moore. "By taking advantage of them quickly enough you can beat the competition to new customers."

Fortune favors the brave

Navigating risk

Private companies that have successfully adapted their products/services to international markets still face a host of other challenges when going abroad. These include finding the right business partners (68%), establishing good cross-cultural management (63%), and tapping adequate local talent (56%), according to PwC's *Trendsetter Barometer*. There are plenty of other issues, too: security risks, local regulatory requirements, and corruption rank high among private companies' concerns as they eye foreign markets. In emerging and fast-growth markets specifically, poor infrastructure, distribution and supply chain issues, and inadequate protection of intellectual property remain worrisome to executives.

As in any market, risk mitigation starts with due diligence. Before venturing into new territories, it helps to seek advice from peers, customers, and partners who have already come up the learning curve. That was the approach taken by Koch Enterprises, a manufacturer of aluminum die-casting parts, which sought recommendations from its automotive customers before moving into Brazil. Says CEO Robert Koch of the expansion, "Probably the longest part was our preliminary investigations, learning more about the country, the culture, the geography, where our customers would be, where competition might be, the quality of competition." [7] If there is one absolute rule, it's *go in with eyes wide open*.

To avoid substantial upfront investment or major risk exposure, private companies generally prefer entering emerging markets in stages. Many manufacturing and product-focused companies start with a sales office (often comprising just a handful of representatives, if that) to test the waters. Later, as commitments deepen, such companies graduate to strategic alliances with local suppliers and distributors.

"We've seen private companies that have significant distribution capabilities and an appetite for expansion but no inclination to build warehouses or deploy a fleet of trucks in a remote market," says PwC's Esch. "Rather than make a large greenfield investment, they've formed an alliance with a local company that has trucks and storage capacity, in exchange for which they've contributed mostly logistics expertise in lieu of capital. These have been profitable ventures, but without the need for companies to make a substantial investment in their own infrastructure."

Using the distributor model as an initial form of entry is also a way to test-drive a new market. At SVP Worldwide, success in emerging markets often depends on that model: "We'll learn the market from the distributor and then, after a few years, if we're successful in that country, we may go our own way and set up a direct-sales organization there, although oftentimes we'll continue with the distributor arrangement—we have flexibility," says SVP's Moore.

Of course, alliances can be risky, too. To mitigate credit risk, SVP requires distributors to pay up front in US dollars (or with letters of credit denominated in US dollars), a policy that puts less strain on accounting and eases currency risk. Most arrangements go smoothly, but Moore says that the agreements must be flexible. "Distributors are given a specific contract," he says. "They have to adhere to the terms and conditions. We will change them out for another distributor if they don't."

7 *Building a Presence in Today's Growth Markets: The Experience of Privately Held Companies,* PwC, 2011

Navigating risks is part of the initial investment you make. The more adept you become at dealing with them in one country, the less daunting they appear in the next market.

Service companies, meanwhile, take a different tack. Because success depends on delivering intangible goods, they often opt for wholly owned greenfield investments. While this requires more investment and commitment, *Trendsetter Barometer* findings show that taking such an approach may lead to higher rates of growth for private companies. For example, privately held service firms that do business abroad estimate returns of 17.9% annually over the next two years, compared with 12.3% for privately held product firms.

For many companies, the biggest hurdle is taking the first plunge into a foreign market. That experience gives executives the insight and confidence they need for further expansion into frontier markets, says PwC's Scott: "Navigating these risks is part of the initial investment you make. The more adept you become at dealing with them in one country, the less daunting they appear in the next market."

Conclusion

As mature economies continue to stagnate and competition heats up, the biggest risk for many US private companies may be an overreliance on domestic markets. Businesses seeking growth will increasingly need to look abroad—particularly to emerging markets, where a rising middle class promises a long-term consumer base. Getting there won't be easy for all companies, but those that proceed methodically can position themselves for sustained growth, keeping the following imperatives in mind:

— Go where your customers are going. Multinational corporations are following a shift in global wealth from west to east, and to emerging markets in particular. If your current customers are moving into foreign markets, it's an opportunity to expand your business with them while testing out new territories.

— Use near-shore markets as a springboard. Historically, private firms that sell outside the United States have focused their efforts on Canada, Mexico, and Western Europe. Now, however, these well-charted regions are also assuming a vital new role as a gateway to dynamic offshore markets.

— Reconsider your approach to product development. In the "new normal" economy, companies that turn their backs on emerging markets risk succumbing to an outdated notion that consumers there are outliers. "Glocalization" is an important first step in a process that can eventually lead to reverse innovation, potentially resulting in product/service improvements that boost sales in a company's domestic market.

— Leverage local partners. In emerging markets, ascendant companies are not married to dated ideas about organization and management, which can impede progress in the new digital climate. Instead, they are wide open to new thinking and ways to implement it. Partnering with such companies can give US businesses a distinct competitive advantage.

— Do your due diligence. Not all emerging markets are equal, in opportunity or risk. To make sure all your bases are covered, talk to your customers, partners, and peer companies that have experience operating in emerging markets. It's also a good idea to keep an eye on where the largest public multinational firms are expanding—and how they're going about it. Their movements may provide critical insight into the next frontier markets.

— Establish a method for managing emerging market risks. While emerging markets are now on a relatively sound economic footing, their fast growth puts them at risk of overheating. They also tend to carry a host of other substantial risks, such as geopolitical, infrastructure, and corruption risk. To succeed in these volatile markets, companies will need to continually identify, track, and mitigate the various risks there.

As the world's economic center of gravity moves to the south and east, these actions are what growth-oriented companies are increasingly setting their compass by. Private companies are no exception.

More information

Want to learn more about expanding into emerging markets? Please contact someone on the PwC team, including:

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1 2011 Forbes America's Largest Private Companies List