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Growth in new markets: It's all about how

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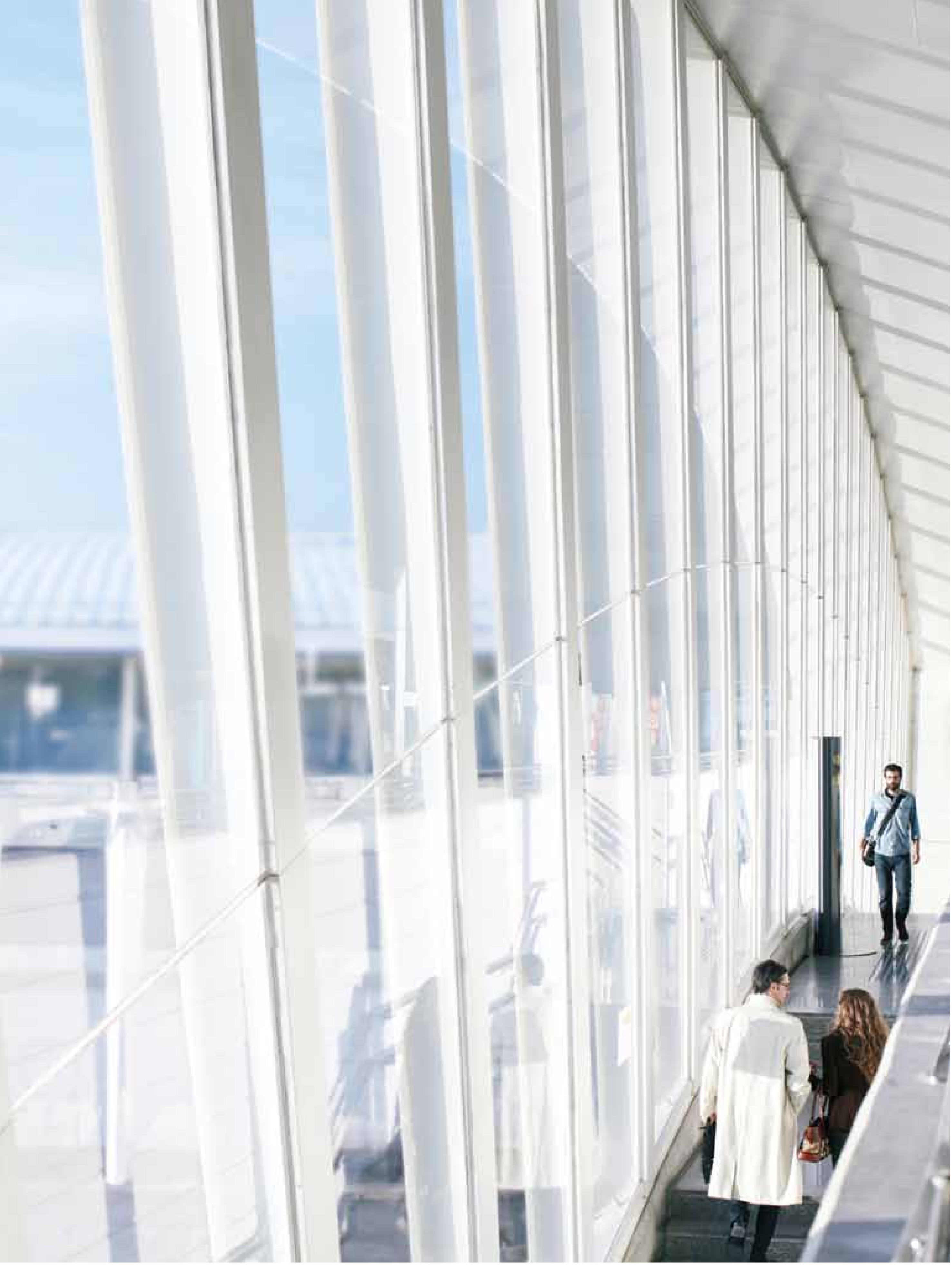


Globalisation is a risky business. Here is one leader's pithy summary in his journal: "If we are to win the game, the pieces must be moved properly; a false move and everything could be lost."

In this case the writer was Roald Amundsen in 1911, en route to the South Pole. Amundsen was intensely competitive. He was in a race against the British Antarctic Expedition, led by Captain Scott. After some early setbacks, Amundsen began his epic journey on 20 October 1911. Nearly eight weeks later, he and his team arrived at the Pole, the first men ever to reach 90° 0´ South. They were 34 days ahead of the British. As is well known, the Norwegians then all made a safe return; Scott and his men, cold, sick, hungry and exhausted, all died[1].

The contrast is striking because Scott and Amundsen had the same goal, the same ambition and courage. They knew what they wanted to do and why. Both were veterans of Polar expeditions and understood the harsh environment they were heading into. But the approaches they adopted to win the game – the 'how' – were very different, as were the results.

Framing the globalisation challenge

When it comes to globalisation, and delivering growth in new markets, the strategy – the 'what, where and why' – is rarely in doubt. You and your main competitors are usually heading for the same places. You have the same insights and will compete with an array of domestic and multinational players in the same markets for the same scarce resources, whether that's technology or talent. ***Success in globalisation is all about the 'how'***.

In 2010, we published a new framework to provide a way for senior executives to think through issues of globalisation (Figure 1, ***The Globalisation Maturity Model***). Two eventful years on, we've integrated the latest data and insights from PwC's annual global survey of some 1,250 CEOs[22]. We show through case studies how clients have used the framework to address specific problems. These and other examples suggest how boards can minimise the risks from globalisation and maximise their chances of long term success.

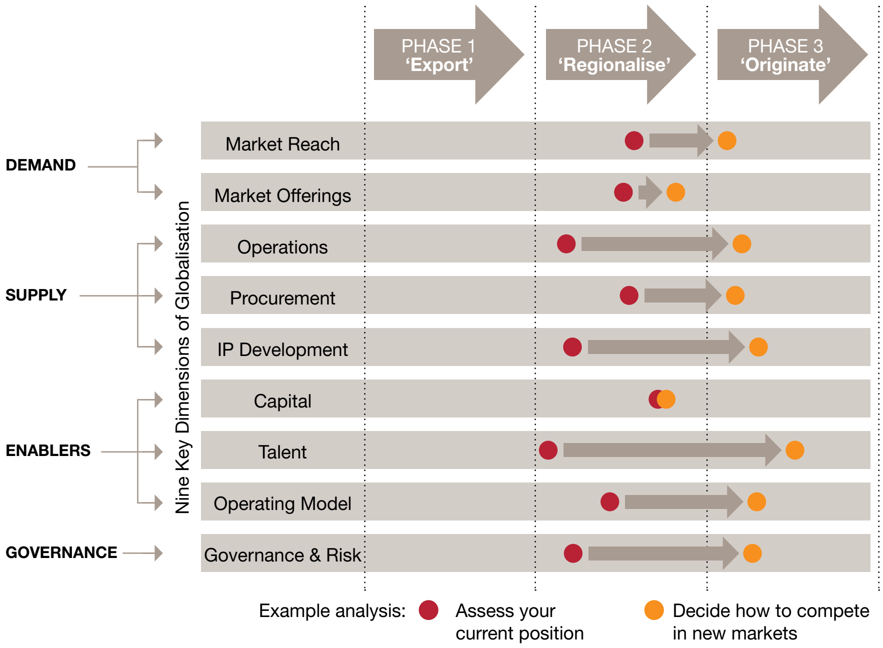
The Globalisation Maturity Model

Our research in 2010[2] showed that the globalisation journey occurs in three distinct phases.

- **In the 'Export' phase, a firm sells its domestic market offerings to similar customers in selected overseas markets.**
- **In the 'Regionalise' phase, it focuses on adapting to local market needs.**
- **In the 'Originate' phase, it's fully global.**

The Globalisation Maturity Model integrates these elements. It provides a framework firms can use to define where they are today and what they need to do to realise their strategic goals.

Figure 1: The globalisation maturity model



The game is getting harder

What are some of the practical challenges that global businesses face when it comes to executing their chosen strategies?

"In a globalised world, even localised crises end up having an impact on all economies. The 2008 crisis taught us that." Brazilian retail entrepreneur Luiza Helena Trajano[2] has grown her business from a single store in 1957 to 728 stores and USD 3.2 billion in annual sales today.

Her company, Magazine Luiza, is firmly focused on serving the emerging middle class in Brazil's huge domestic market. Growth has been impressive, averaging 26% a year for the past decade[3].

Such growth opportunities have attracted the attention of major overseas players, as well as home grown competitors. Domestic and global markets have become ever more intertwined.

This means, the challenges of "moving the pieces properly" get ever more complicated and the implications of getting it wrong ever more costly. The recent forced re-nationalisation of Spanish oil firm Repsol's holdings in Argentina's YPF[4] is a cautionary tale in this respect.

Picking the right approach for each market is critical. Nancy McKinstry, CEO and Chair of Wolters Kluwer, the global information services and publishing business, puts it thus: "We've not been able to take one strategy that will work in India, that will work in China, that will work in Brazil. So you have to adapt the strategy very much to the local market."

Local adaptation and the interconnected nature of markets are two of many which make the game harder. Large numbers of people across an organisation, not just the top few dozen executives, need to grasp how the game has changed in order to execute well and grow in new markets.

Many organisations struggle to do this consistently, if at all. They often stick with familiar methods that worked well in the 'old' world, or adopt narrowly functional approaches to solve complex challenges. We see three issues in particular where joined up thinking and a fresh approach are 'easy to say, hard to do':

- Be wary of precise plans
- Balance objective and entrepreneurial instincts
- Get ready for deeper collaboration

Be wary of precise plans

The choices a company makes about how to build a global business have very long term consequences. There are public policy, economic, social and environmental factors to consider – each chock-full of disruptive "known unknowns"[5]. History tells us that a 15-year time horizon will include two or three governmental cycles, at least one recession, one or more major spikes/slumps in key commodity prices and several natural catastrophes, plus human disasters of conflict, want and disease.

On the positive side, there will also be new patterns of prosperity and dramatic innovations. 15 years ago, for example, there were some 200 million mobile phone subscriptions worldwide; today, there are 5.3 billion, an annual growth rate of 28%[6]. Likewise, if Facebook – launched just eight years ago – were a country, it would now be the third most populous nation on earth[7].

Within a firm, decisions about innovation across regions, extended value chains, capital allocation, tax optimisation or talent management pose very specific, structural questions with deep implications for the long term. The problem is, no one's found the perfect crystal ball yet.

The issue is complicated by the intense short term pressure on those who have to decide. Their tenure is getting shorter; research in the USA shows that in the last decade the average time in office for a CEO has fallen below five years[8]. Economic turbulence, annual budgeting, aggressive sales targets and industry league tables all encourage a focus on this year and the next, not a decade hence.

Markets are impatient, too. In a landmark speech made in 2011, Andrew Haldane and Richard Davies of the Bank of England concluded: "There is statistically significant evidence of short termism in the pricing of companies' equities. This is true across all industrial sectors. Moreover, there is evidence of short termism having increased over the recent past. Myopia is mounting[9]."

The net result: many companies find developing the one to three year view relatively easy but the five to 15 year view extraordinarily hard. In the near term, personal objectives can be tied to targets; issues can be analysed and action plans agreed. There is a degree of comfort with the clarity and precision. But the broader, longer term view is often regarded as too difficult and is avoided.

Take the example of a leading pharmaceutical business with a strong position in the mature markets of North America and Western Europe.

Recently, the firm's growth in these regions has flat lined or turned negative. By contrast, its sales in emerging markets in Latin America, Asia and Africa have been booming, with annual growth rates of 10-14%. A disciplined commercial focus has underpinned this success.

So far so good. But the top line growth concealed deep tension within the business, causing problems when it came to delivery. The company's operating models – its supply chain in particular – were tuned for the mature markets of Europe and North America. These are well known markets with stable demand and high volumes. At the same time, there was a strong emphasis on the short term planning cycle and 'hitting the numbers'.

The tension arose because the business case for restructuring the company's delivery models to capture the new waves of growth needed to take account of the uncertainties inherent in markets like Africa.

In this environment the spreadsheet driven precision the business had come to expect was illusory and unhelpful. But the status quo persisted: operational fulfilment and customer satisfaction were suffering.

The first step was to recognise the true nature of the problem. So the company used our globalisation framework to help stakeholders think through the long term implications of emerging market growth and how its approach needed to change.

Using a seven year time horizon, it developed a comprehensive view of the trends in key regions and territories. It set about collating the supply chain requirements for each country: these differed a lot and it was important to understand the differences. Such information gathering had previously been wholly decentralised, but the quality was patchy, and it was hard to 'read across' different markets. The firm therefore added a small central team to improve the quality of its market intelligence and risk analysis. Then it built a range of scenarios (not forecasts) to work through the strategic options.

The result was a redesigned, more modular supply chain which could accommodate the uncertainty in demand planning while minimising stock outs. The firm also learned two key lessons. First, tackling the challenge of globalisation means putting aside old mind sets and behaviour, even when these have historically been very successful. Second, it's possible – and profitable – to design an organisation to respond to uncertainty. As the head of the business reflected, "In emerging countries, how well we execute locally is fundamental to our philosophy and to business success."

Balance objective and entrepreneurial instincts

Decisions on globalisation can be powerfully influenced by the advocacy of a single person, especially if that person is the boss.

The entrepreneur's instincts are vital for growth. Advocacy – the championing of a vision or opportunity – can make all the difference, particularly in the early stages of a strategy. It helps raise and commit money, build teams and generally get things going. But advocacy alone isn't sufficient.

Take, for example, Cisco Chairman and CEO John Chambers' decision to champion India. Cisco opened its first Indian sales office in 1995, the year he became CEO. By 2001, the company's sales in the country were still modest – only 0.33% of its global revenues[10].

But Chambers noted India's huge growth potential and its talent pool, saying: "Unlike China, India has a strong education system for software engineers[11]." He made a bold forecast: within the decade India could be generating 5-10% of the firm's revenues.

Over the next four years Cisco invested $200 million in building its local capabilities, including R&D. In 2005 Chambers raised the stakes five-fold, committing senior executives and a further $1.1 billion to create Cisco's Globalisation Centre East in Bangalore.

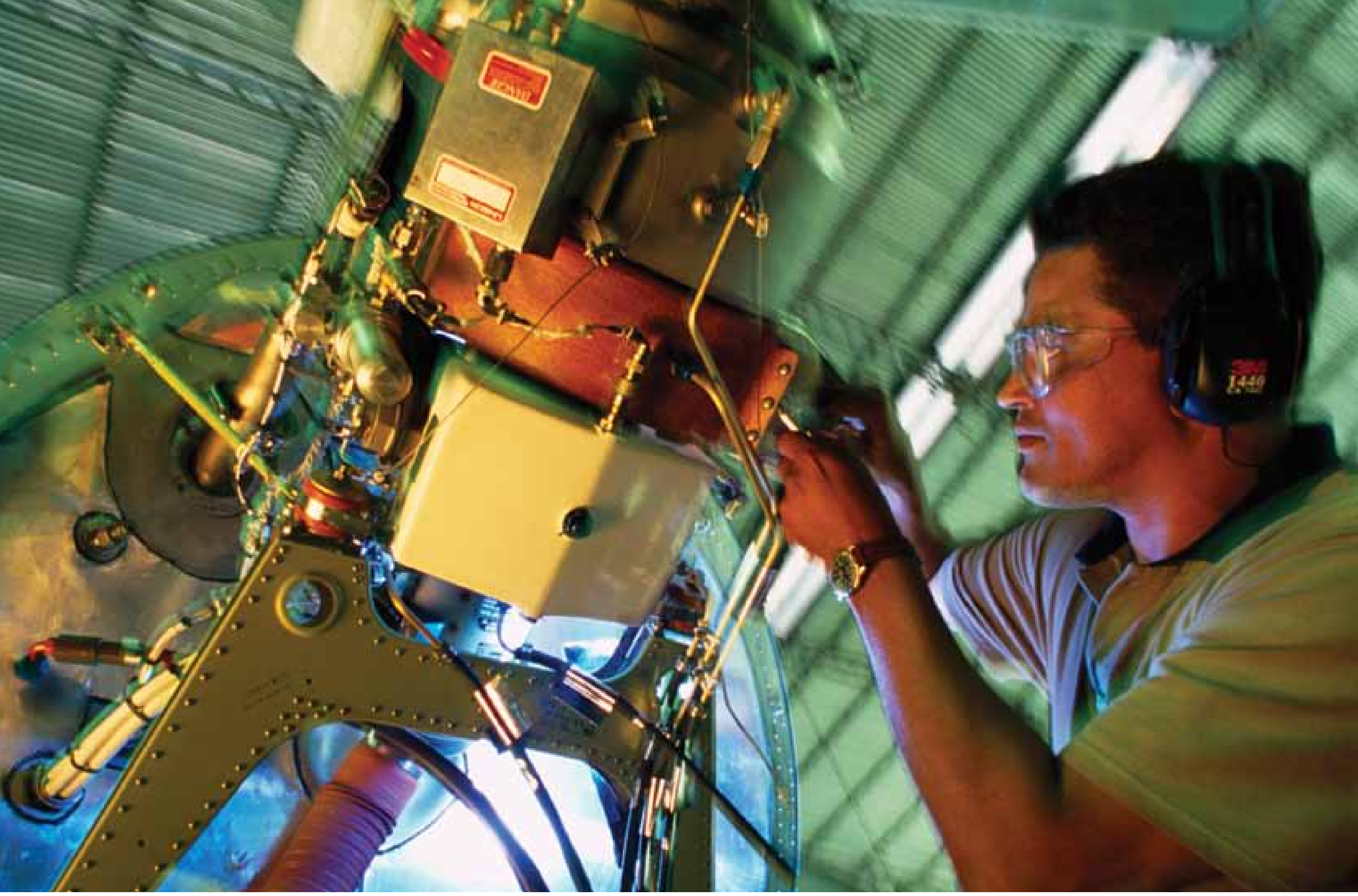
By 2011, Cisco's revenues in India were more than $1 billion (Rs 4,600 crore) or 2.5% of its $40 billion total sales – a long way short of the earlier forecast[12]. Did Chambers and Cisco make the right call on India? The jury's still out. But the scale of investment and the sales undershoot shows how big – and how risky – these globalisation decisions are.

So how to strike the right balance? The broader your exposure across different markets, the more important it is not to spread yourself too thinly. The top two or three priority markets are usually obvious enough. But businesses often have more opportunities than they can sensibly pursue. So how should they arbitrate on the middle pack? These will each have their advocates, forcefully arguing the case.

The problem is: like must be compared to unlike. How do you compare the merits of a new distribution centre in Malaysia with a proposed new office for government relations in Brazil or the worldwide harmonisation of legacy IT systems? The very different risks involved mean that 'gut feel' based on experience is an unreliable basis for decision making. And a simple Net Present Value (NPV) calculation isn't enough. There are many other non-financial factors that must also be considered – for example, the potential for disruption to supply chains from natural disasters like the floods in Thailand and the tsunami in Japan.

We helped an electronics business work through such complications. The company had a charismatic founder, an engineer entrepreneur who registered his first patent from a farm shed in Northern Europe. The business grew steadily by manufacturing energy efficient, highly reliable, precision engineered components for industrial customers in Europe. Then, in the mid 2000s, it set itself a bold new goal – to expand from its middle ranking market position and become one of the top three global players.

Eyeing the booming markets in Asia, it made an initial foray by acquiring a factory in China to make low cost versions of its products. At this point the leadership team recognised that strategic ambition wasn't enough; it also needed to put its globalisation plans on a proper footing.



So it commissioned a deep review of every aspect of its business. The brief was to look at every aspect of its business and operational model and identify what might need to change. The next step was to highlight the capabilities the business would need to have in place to deliver the changes and thereby the strategy. The review involved local managers from all the main regions, as well as the top executives, and two aspects proved particularly useful.

First, the team made sure it 'got numbers into the argument'. It gathered wide ranging data on many different aspects of its target markets, such as the challenges of recruiting talent and trends in 'green' thinking which would influence long term demand for its energy efficient products. It also benchmarked its operational practices and performance against its customers' requirements and the practices and performance of its global and domestic competitors.

Second, the team worked out where it wanted to be on each dimension of the globalisation framework. It discovered that some of its plans, such as the plan to open some new Research & Development (R&D) centres, were out of sync with its manufacturing capabilities in the regions. And, given the level of global volatility, it also decided to take a cautious approach with its capital.

The result? The leadership team stayed true to its strategic intent, but adjusted growth targets to reflect the time required to develop a more mature global capability in terms of its people, processes and tools. It kept R&D close to home until the Asian centres were ready to support regional innovation. This approach proved its worth during the financial upheavals of 2008. Since the crisis, global sales have grown by 20% and operating profits by nearly 30%.

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Get ready for deeper collaboration

There's an uncomplicated view of globalisation. You have a product or service that's successful in your home market. You believe customers in other countries will like it just as much. You get on a plane, negotiate the first sale, and before long there's a local team and a new subsidiary in place. Or you send commodity managers abroad to secure low cost sourcing or contract manufacturing agreements, so that your business remains competitive in its prices.

Such approaches are characteristic of the 'export' phase in our framework. They're long established, successful and transactional. A centrally controlled, hub and spoke management model underpins the buying and selling. But intensifying competition soon forces a firm to rethink this basic model.

Even Jeff Immelt, CEO of General Electric, one of the strongest and most experienced global players, admits as much: "Globalisation makes companies like ours much more competitive. There's nothing more humbling than when you have to sing for your supper in every corner of the world … it's harder to win at Emirates than it is with an American airline … it's an away game!"[13]

To win that game, companies increasingly need to think beyond the traditional export model. Achieving sustainable market leadership calls for something more. The starting point for businesses looking afresh at their global footprint should be what we term 'Needs and Offers'.

'Needs' have an 'outside-in' dynamic. Thinking about what a country needs doesn't mean simply asking how many customers there might be for what you sell. It means asking 'what are the deeper needs of the country that a smart strategy should address?' For example, what are the core aspirations of the four billion people who earn between $1,000-4,000 a year?[14] The answers will vary enormously. And companies that address that agenda directly and precisely can gain a long-term, structural advantage in the country concerned.

The world's third largest brewer, Heineken, provides a striking example of a needs-driven market approach. According to the *Financial Times*, "Food and drink makers as well as soft commodity traders have been at the forefront of efforts to train farmers and improve social infrastructure, […] fostering relations with governments and improving the lot of future consumers"[15]. So in earthquake-stricken Haiti the company's planning to build hospitals and schools, as well as to sell more beer.

Heineken's president for the Americas, John Nicolson, says the days of investing simply for financial reward are coming to an end. "Fifty years from now, if that's your modus operandi, I think you will be out of business."

'Offers' represent the flip side of the coin. They focus on what capabilities a given country can contribute to the competitiveness of your company at large, whether that's a deep talent pool, patient capital, risk sharing partnerships, or geo strategic resources such as ports or minerals.

This strategic perspective can be applied to mature economies as well as growth markets. When India's Tata Motors bought the UK's Jaguar Land Rover (JLR) for $2.3 billion in 2008 it acquired much more than a local manufacturing base and order book[16]. It recognised that JLR offered a unique set of premium brands. Like other English luxury goods such as Burberry or Mulberry, these brands were ripe for globalisation. They offered Tata a way to showcase its technology and move up the automotive value chain.

Within four years Tata had built on that brand offer and turned JLR around. New production centres were established in China and India, and JLR announced plans to build a top of the range supercar. This strategy has been a stunning success. In 2011, JLR generated post-tax profits of £1.04 billion (US$1.7 billion) – 80% of parent Tata Motor Group's net profits [17].

The concept of 'Needs and Offers' also pushes businesses to think harder about the way they engage with a country, in particular a country's government. Success today needs to go well beyond licences, offset arrangements or tax planning, vitally important though these are[18].

Governments make – or break – the local rules. In many countries, the government is simultaneously rule setter, referee and a player on the field, either through state controlled firms or entities like sovereign wealth funds. But the ambitions, motivations and operating methods of a government are substantially different from those of most businesses.

For businesses, working across the divide is both a necessity and a real challenge. Yet relatively few companies spend enough time and money working out long-term 'Group to Government' strategies for their key markets.

By such strategies, we mean that sustained relationships and effective governance arrangements all need to be in place to realise the desired outcomes. Otherwise businesses and governments risk retrenching to distrust and parochialism and investing sub-optimally in the assets they both seek to build – human, physical, social and other types of capital – all of which are necessary to promote growth[19].

Instead, it's more common to see intense lobbying around specific sales campaigns, with the 'home' government often co-opted in pursuit of the deal.

A recent illustration: in 2010-11, when the Indian government was deciding on a big defence procurement contract for fighter aircraft, the country was graced by official visits in rapid succession by the Presidents of the United States and France, the Chancellor of Germany and the Prime Ministers of Russia and the United Kingdom. Coincidence? Unlikely. Short term advocacy? Very likely.

We helped one leading engineering systems and services company evolve its approach to globalisation at the country level. The company had a clearly stated goal: to double its revenues over the next decade.

The business was performing well: its various divisions held solid and long established positions in many markets. That said, the leadership team knew that realising its revenue goal would require a step change in both strategy and execution. Its divisions had traditionally operated with a high degree of autonomy and a sales driven culture. This was becoming duplicative and inefficient: the firm also knew that securing the best opportunities in key markets increasingly called for a more joined up approach. The firm's reputation was a major asset when dealing with governments – but it needed to act more like a group, and less like a diversified conglomerate.

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Despite wars, recessions and natural disasters, the pace of globalisation is still increasing. It remains – and will remain for the foreseeable future – a hot topic and management priority for leadership teams in every region of the world.

So the company took a fresh look at its country strategies. It tasked its divisions and functions with developing a consistent, scenario based view of the 10-year demand potential in its top five growth markets. It used the same timeframe to explore whether each country offered a comparative advantage for global or regional supply. This turned out to be difficult, even controversial.

Next, the company used the concept of 'Needs and Offers' to sharpen and deepen its strategy for specific countries. For example, in one oil rich state the head of the ruling family was strongly committed to fostering education and employment. Identifying these 'Needs' helped the company identify several ways in which it could support that agenda, thereby positioning it favourably as a trusted partner of the whole nation. The same exercise also revealed a 'talent risk'; many of the most important local relationships centred on a single employee who was nearing retirement.

Similarly on the 'Offers' side, the state was thinking long term and preparing for its post petroleum future by trying to diversify its power generation mix away from hydrocarbons. Our client had launched a new business unit in the same segment. There was clearly an opportunity for collaboration and co-investment, which could also front load the order book. The global market position of this start-up unit would benefit enormously. The company strengthened the unit's strategic ventures team accordingly.

Finally, by using a common framework, the company was able to 'read across' multiple markets. This helped compare the very different opportunities each presented. It also helped integrate the geographic dimension of its businesses more effectively into the group's annual strategy round and business planning cycle.

The great scientist Louis Pasteur famously said: "Chance favours the prepared mind"[20]. The global environment will always be complex and prone to unexpected events. This client has found that clear country strategies have made it more sure footed in its quest for growth.

Racing to the south pole

If we return to the heroic race of 1911-12, we can also see vividly the importance of strategic maturity and 'joining the dots' between the different dimensions of the enterprise.

Scott had the advocate's characteristic confidence in his plan. He wrote in August 1911: "I feel sure we are as near perfection as experience can direct." He made some crucial choices about his modes of transport in the race for the South Pole. He committed to a bold innovation – motorised sledges. He also used horses and dogs. His main fall back was the 'classic' mode of man hauled sledges. It was a complex mix.

You cannot maintain your relevance by just staying put.

Unfortunately, none of these modes was fit for purpose. Half of his ponies died before the expedition set out. This meant the food stores for the return journey were placed short of where they needed to be. The motorised sledges were an immature innovation and broke down. Everything travelled at different rates. Man-hauling the sledges was very slow and, as the disappointed expedition returned to base, placed a fatal strain on hungry, exhausted men.

Compare Amundsen's joined-up approach. He had learnt first hand the value of adapting to the extreme climate. He used Inuit-style furs for clothing and seal meat for food. He paid meticulous attention to his supply chain, refining his methods as he laid stores along the route. Above all, the members of his team were expert in the use of skis and in handling sled dog teams – modes of transport that were fully proven and brilliantly effective.

As Amundsen himself wrote, "This is the greatest factor [for success] – the way in which every difficulty is foreseen, and precautions taken for meeting or avoiding it."

What next?

To recap. In our experience global organisations need to adopt three key practices to support their growth strategy: they need to think through the "known unknowns", balance ambition with fact driven realism, and understand a country's Needs and Offers in both strategic and practical terms.

Our globalisation framework provides a way for businesses to do this. Thinking through the three phases helps determine the right overall positioning and thus establish a coherent basis for action.

Next steps? Here are three suggestions for CEOs.

1. Be wary of a precise seven to ten year plan. Challenge your team to think through tougher scenarios, bolder innovations and a broader range of outcomes – consider new fiscal crises, Facebooks and Fukushimas.
2. Balance objective and entrepreneurial instincts. Find ways to measure and compare your firm's capabilities across different global markets. How will you execute your strategy and plans? Then cross check – are your various capabilities joined up and locally appropriate? If not, your competitors will have the upper hand.
3. Get ready for deeper collaboration in your priority markets. Trade-offs will be complex and the payoff uncertain. Focus on the broader needs of the country as well as your commercial objectives. Use the framework to get them in perspective, with your team aligned and ready to act when the right opportunities arise.

Despite wars, recessions and natural disasters, the pace of globalisation is still increasing. It will remain a hot topic and management priority for leadership teams in every region of the world.

Minister Mentor of Singapore Lee Kuan Yew puts it like this: "Globalisation cannot be reversed because the technologies that made globalisation inevitable cannot be uninvented.

In fact, better and cheaper transportation and communications will further advance the forces of globalisation.

The world changes. There are shifts in the geopolitics and the economics of the world. The perennial challenge is to remain competitive."[21]

Given the clarity of that challenge, globalisation and growth in new markets have become all about the how.

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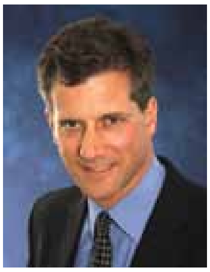

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Methodology

Completed in early 2010, our global research study was designed to determine how top executives perceive and respond to the challenges of globalisation. We developed a series of questions based on a proprietary model of globalisation maturity. We then identified 30 leading companies that described themselves as "global," and summarised their current practices relative to this maturity model. Each company was given a scaled score on the maturity index across all nine distinct dimensions. The companies we studied represented three major sectors of the economy: health care, industrial, and telecommunications. Findings were validated via in-depth interviews with executives at selected companies.

The Design Group 21141 (11/12)