Growing Beyond

Beyond Asia:
Strategies to support the quest for growth

Thailand highlights

Ernst & Young
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About this report

Rapid-growth markets have largely been viewed and studied from the perspective of inbound investment by companies based in the West. *Thailand highlights* and the larger report of which it is a part, *Beyond Asia: strategies to support the quest for growth*, offer rare insights about the strategies of outbound investment from companies based in Asia and provide in-depth perspectives on decision-making for companies from both mature and rapid-growth markets.

Thailand highlights is based on a survey of 617 business executives based in East and Southeast Asia, conducted by the Economist Intelligence Unit in March and April 2012. Companies were headquartered in mainland China, South Korea, Hong Kong, Indonesia, Malaysia, Singapore, Taiwan, Thailand and Vietnam. The sample included 50 interviews from Thailand. The complete report, *Beyond Asia: strategies to support the quest for growth*, includes the full results from the survey in addition to qualitative interviews with several Ernst & Young sector and country leaders and the viewpoints of senior executives from companies across the region. Oxford Economics provided analysis of current and predicted trade flows among individual Asian markets and between Asia and the rest of the world.

All of the companies surveyed are Asian multinationals that obtain substantial revenues and profits from international markets. Companies with operations limited to East and Southeast Asia were classified as regional; those with operations in two or more markets in the Americas, Europe, the Middle East, Africa, India, Australia, New Zealand or Japan were classified as global. Both groups contained companies from all nine countries surveyed; large and small companies by revenue, a mix of public and private ownership, and a spread of industry sectors.

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Introduction

In the face of a slow global economic recovery, Asia continues to grow at a rapid pace. Over the next decade, the region's GDP will grow more than 6% a year, according to forecasts by Oxford Economics. In the last 10 years, the region has been the world's fastest-growing source of foreign direct investment (FDI). In 2010, FDI outflows from South, East and Southeast Asia totaled US$230 billion. Although overall outflow has not yet reached the level of inflow, clearly the gap is fast narrowing. Regional companies are looking beyond Asia and targeting other regions of the world, whereas Asian companies that are already global are consolidating their investments and competing on a level platform with traditional Western multinationals.

Based on in-depth research conducted for Ernst & Young, featured in our report, *Beyond Asia: strategies to support the quest for growth*, we examine the practical issues that both regional and global Asian companies will need to consider to succeed in the next few years. We look at how, why and where companies are expanding and examine the challenges they are likely to face, and how they might overcome them. A key component of our analysis compares companies that currently operate only within Asia (regionally focused) and those that have significant operations or investments outside Asia (globally focused). As a result of this analysis, we have developed practical strategies to help businesses focus on the right rationales for investment, modes of entry and capabilities, as well as forecasts to improve decision-making and planning for future global expansion.

With its businesses already highly internationalized, Thailand is already a major investor within Asia. This report compares our overall findings for Asia with those for Thailand and highlights the unique characteristics of Thai companies that are regionally and globally focused. It contains challenging and thought-provoking insights for Asian companies as they develop their strategies for expansion within and outside the region.

Ruth Chaowanagawi
Thailand Country Managing Partner
Ernst & Young

The Thailand country report and Beyond Asia: strategies to support the quest for growth are part of ***Growing Beyond****, our flagship program that explores how companies can grow faster by expanding into new markets, finding new ways to innovate and implementing new approaches to talent management.*

Lessons from Asia:

What Thai companies can learn

As Asian companies grow in stature, the pattern of their overseas investment is changing. Over the next three years, many players that are predominantly regional now will seek to become global players. Our survey found that Asian companies are expanding overseas for six key reasons: growth; diversification; routes to market; access to resources; access to skills; and access to technology. Regional companies emphasize building the capabilities and resources needed to further their ambitions, whereas global companies see expansion first as a means of securing new customers and sales growth.

The Asian business model is also changing. Where once they were renowned for low-cost manufacturing, Asian companies can now rightly boast of the quality of their products and services, and the strength of their technology. When asked about their key strengths and advantages, Asian executives are most likely to point to those factors as key advantages when targeting overseas markets. Furthermore, Asian companies are becoming more conscious of — and more flexible about — the deal structures they will consider. Regional companies in particular say partnerships and alliances will become more important to them, whereas mergers and acquisitions are a much more viable option for the globally focused companies.

Autonomy, profitability pose challenges

Still, several challenges remain. The farther from home they travel, the more likely Asian companies are to encounter difficulties with understanding the nuances of the local market abroad. Our regionally focused respondents consider themselves more effective than do their global peers at dealing with the challenges of running an international business, but they should not underestimate the complexity ahead. Control is also an issue, as globalization brings with it a need for greater autonomy. Many Asian companies remain tightly controlled from the center, but this raises questions about the effectiveness and agility of their decision-making, particularly in markets that are distant and unfamiliar. In general, companies in the survey tend to become more decentralized as they expand into developed markets.

Another hurdle is that profitability tends to lag investment. Growth may come relatively quickly, but making sure that investments are profitable is much more challenging. Increasing profitability requires companies to focus on efficiency and execution.

The need for an international mindset

Asian companies with a more diverse geographical footprint readily admit that their management teams need a better understanding of global markets and a more international outlook. Senior managers must have experience of different markets, the ability to understand and reconcile different cultural norms, and the ability to combine local and global talent into one seamless whole.

A step change is also required in talent management. Companies must create the right blend of local and global management and ensure that the right talent is in the right place to achieve key performance objectives. This becomes more difficult as companies broaden their footprint: global companies are less likely than are their regional peers to think that they are effective at many of these key aspects of talent management.

Fast facts: Asia

- Rapid-growth markets from Asia represent the fastest-growing economic region in the world, with annual growth forecast at more than 6% a year.
- The IMF expects advanced economies to grow by just 1.4% in 2012 and 2% in 2013. The corresponding figure for East and Southeast Asia in 2013 is 7.9%.
- Since 2000, Asia has been the fastest-growing source of foreign direct investment (FDI). Its businesses currently produce a quarter of the world's exports (US$3.77 trillion in 2010) and form 87 of the Fortune Global 500 largest firms.
- FDI outflows from East and Southeast Asia recorded a compound annual growth rate of 22.9% in 2005–2011, jumping from US$70 billion to US$242 billion.
- Investors from East and Southeast Asia are major drivers of growth in global foreign direct investment (FDI) outflows, making up 16% of the world's total FDI (up from just 7% in 2005) and driven by increased outflows from mainland China, Hong Kong (SAR), Malaysia, South Korea, Singapore and Taiwan.
- Intra-regional trade is expanding rapidly, reflecting the shift towards higher consumption in Asia. China leads the way in terms of outflows and destination, with growth for Indonesia, South Korea, Thailand and Vietnam close behind.
- Trade flows from Asia to the US and Canada, the Middle East, Latin America and Africa are expected to increase by over 10% a year up to 2020.
- Cross-border M&A purchases are consuming an ever-larger slice of FDI flows, with purchases from Asia reaching a record US$94 billion in 2010.
- The China - US trade route is forecast to see the biggest increase in the world, predicted to rise by almost US$700 billion by 2020.

Sources: UNCTAD, IMF, Oxford Economics

Fast facts: Thailand

- Thailand continues to make a steady transition toward a middle-income economy. By 2013, the Economist Intelligence Unit forecasts that GDP per capita, in purchasing power parity terms, will surpass US$10,000 for the first time.
- Following widespread flooding in 2011, Thailand's economy narrowly avoided recession that year, but has bounced back sharply since, with growth of 6% in 2012 expected. Looking ahead, the country is expected[1] to continue expanding by an average of 4.7% during 2013-16. Its GDP in 2011 was US$346 billion, in real terms.[2] In purchasing power parity terms, it is the 25th largest economy in the world.[3]
- Thailand's FDI outflow has increased sharply in recent years; it is expected to reach more than US$18 billion in 2020, up from about US$12 billion in 2012, according to Oxford Economics (see Figure 1).
- Exports are also forecast to continue growing strongly, increasing in value at an average of just over 10% per year between 2010 and 2020 (see Figures 2, 3 and 4).[4]
- Machinery and transport, along with other manufactured goods, account for nearly half of Thailand's exports today. This should remain the case over the coming decade. From a regional perspective, the strongest growth is expected within Asia, especially India (growing by an average of 15.6% per year), China (by 15.3%) and Korea (by 13.9%). However, growth is expected to be strong across all major export markets (see Figures 4 and 5).
- As of 2010, Thai companies exported similar volumes to both China (US$21 billion) and the US (US$20 billion). By 2020, China's nearly US$89 billion will far surpass expected US demand of about US$54 billion.[5]

Footnotes

1. Economist Intelligence Unit
2. Ibid.
3. *CIA World Factbook*
4. Oxford Economics
5. Ibid.

Outward bound:

The agenda for Thai companies

The growth of Thai FDI outflow has been rapid, even by emerging Asia standards. Between 1996 and 2004, outflow averaged just over US$400 million per year. By 2010, however, that figure had jumped to US$5.5 billion and in the last two years more than doubled again to US$12 billion, helped in part by high liquidity in the banking sector. This expansion is expected to continue in the decade ahead, expanding by about 50% to reach US$18 billion by 2020. This growth is reflected in the responses of Thai executives, who are far more likely to hold financial investments in international markets than their regional peers (60%, as opposed to 49% from the rest of the survey sample).

A strong desire to move up the value chain

The aims of Thailand's outward investments vary sharply between developed countries farther abroad and high-growth markets closer to home. For developed markets, Thai companies are firmly focussed on gaining access to intellectual property (48%) and skilled workers (44%). In both cases, these figures are well ahead of the rest of Asia. By contrast, they are looking to rapid growth markets for access to raw materials or natural resources and access to new distribution channels (both 38%). In general, Thai companies are less interested than their regional peers in finding new customers or sales growth, suggesting that for them internationalization is much more about improved access to supplies and moving up the value chain (see Figure 6).

> "Southeast Asian companies are getting smarter and realize that they can't continue playing this low-cost game because of competition. In order to maintain margins, they need to move up the value chain and they need to acquire the know-how and the technology as part of that strategy."

Seng-Leong Teh, Transaction Advisory Services, Ernst & Young

This is consistent with another key finding from this survey, which is that Thai executives see their ability to innovate as their biggest advantage in operating abroad. This is cited by 40% of respondents, compared with just 29% for the overall survey (see Figure 7). The local electronics industry, for example, produces 35% to 40% of all hard drives in the world. In the INSEAD 2011 Global Innovation Index, Thailand is ranked 33rd out of 125 countries in terms of its market sophistication and 25th in terms of business sophistication. However, further progress is still needed. In the same Index, it ranks relatively poorly on research and development in particular, coming in 83rd overall.

> "Asian firms face a lot of issues around the fact that they don't have international management that's experienced. On the other hand, the advantage Asian firms have is that they don't have baggage. Therefore they're very flexible and they don't have the same kind of heritage to protect in terms of brand and the expectations of shareholders."

Peter Williamson, Professor, International Business,
Judge Business School, University of Cambridge

This survey also reveals some concerns that are particularly relevant for local companies seeking to move up the value chain. Sixty percent of respondents cite a poor understanding of global supply chain issues as a leading area where management needs more knowledge or insight in order to succeed internationally (combined with 41% overall), suggesting that many companies will experience a steep learning curve as they seek to tap into sources of raw materials in developing countries (see Figure 8).

Despite greater market entry flexibility, Thai companies still prefer tighter control of regional operations.

Thai companies are more flexible about the modes of entry they employ for forays into the rest of Asia, as compared with their regional peers. They are almost equally likely to use their own local sales, distribution or sourcing desks (42%), partnerships or alliances (40%) or joint ventures (38%). More than one-third (34%) are ready to use outsourcing in the region, well ahead of the survey average (24%). This is less the case for developed markets and non-Asian rapid growth markets, though. Thai respondents are more wedded to local desks or direct export than are their Asian peers and less willing to contemplate other arrangements.

Thai executives are also more likely to try to maintain far more direct control of foreign operations than their Asian counterparts. Six in 10 Thai companies tightly control developed market activities from their head office; 52 percent do the same for operations in the region. In both instances, they are well ahead of the survey average (see Figure 9). As a result, only 10% say they are very effective at empowering local decision-makers.

Greater efforts to internationalize management will likely be needed.

Thai executives are more likely than average to believe that their corporate leaders have a good understanding of international markets. Forty percent of executives say their corporate leadership needs more such knowledge, with 46% strongly agreeing that top management has sufficient work experience outside Thailand. Both results are much better than the survey average. However, many show concern that this knowledge is not being applied effectively. Only 32% strongly agree that top management has an international outlook on decision-making and over half (52%) believe that understanding of local cultures and practices is limited for their senior management.

Similarly, Thai companies do not appear to be using their international expansion as a way to internationalize managerial talent—an effective way to make corporate culture more global. Only 10% expect to emphasize international recruitment for the management team, less than half of the figure for the survey as a whole (23%), and far fewer than the 60% who will rely on internal development (see Figure 10).

International expansion:

Business implications for Thai companies

Venturing into international markets brings both significant opportunities and significant challenges. As our survey of Asian outbound investment shows, the business implications of growth — and the strategies to manage them — are quite different for global and regional players and need to be explored carefully. The following are some key tactics we have identified:

For regional companies

Consider the implications of greater competition. As companies from both inside and outside Asia continue to target the region, this will increase competition — for assets, talent, resources and customers. Regional companies need to consider the impact of this trend on their prospects.

Build capabilities for international expansion. Regional companies seeking to build a global footprint must ensure that they get the basic capabilities in place before making bold moves. They need managers who have an understanding of international markets, and core functions, like finance, HR and IT, that can support multiple markets.

Leverage global resources. Regional companies will be under greater pressure to ramp up their innovation, product and service mix and talent pipelines. By building partnerships with companies outside Asia, or acquiring companies with the right resources and expertise, regional companies can leverage global resources to ensure that they remain globally competitive.

Enable greater local autonomy. Greater geographic scale makes it more difficult to control from the center. Companies should therefore consider devolving greater autonomy to regions, but do so within a set of parameters and risk frameworks.

For global companies

Put in place robust risk management. Enable entrepreneurship and autonomy at a local level but do so within a set of parameters and rules that give business leaders at headquarters comfort that the company's values are being upheld. A robust risk system will also provide early warning of problems on the periphery of the organization.

Improve profitability. For many globally focused Asian companies, the priority remains investment and growth. But profits have not kept pace with revenue, as our survey consistently shows. As Asian companies' investments mature, they will need to do more to introduce efficiency and increase productivity.

Focus on different modes of investment. There has been a new wave of mergers and acquisitions in developed markets as Asian companies seek brands, know-how, technology and intellectual property. Globally focused companies are bolder than their regional counterparts in conducting mergers and acquisitions or greenfield investments to drive growth, but will still need to identify the right partners and to maximize value.

Make the corporate culture more international. By recruiting managers with experience of different markets, reducing reliance on expatriate workers, and putting in place global talent management programs that enable the flow of key talent around the world, companies can disseminate best practice and create a more international workforce.

Choose where functions should be global or local. Companies need to think about where they can derive economies of scale without compromising local relevance. Functions such as finance, HR and IT are often good candidates for centralization. It is also possible to create platforms for services that are delivered locally.

What do these trends mean for Thai companies?

The trends outlined within our research hold a number of implications for Thai businesses seeking to expand abroad. Some of the most important of these include:

Increased competition from abroad will not be restricted to price. Thais will not be the only ones looking for resources abroad. There will be growing competition for assets as regional rivals also seek new growth. The nature of competition is also changing as Asian companies move away from low costs to focus on product and service quality. Improving all aspects of innovation will be crucial to success.

New patterns of investment and trade flows will emerge. Rising wages and input costs will force companies to think differently about how and where they choose to compete. The expansion of supply chains globally will require new skills and capabilities inside companies. New partnerships and strategic alliances will also need to be sought out to further expansion plans, making partner selection crucial to success.

Companies will need to rethink their organizational design and operating models in response. Executives need to consider how to combine local relevance with global scale. Greater autonomy at a local level may require a rethink of how companies are structured. Managing talent internationally may mean reconsidering HR and executive search policies.

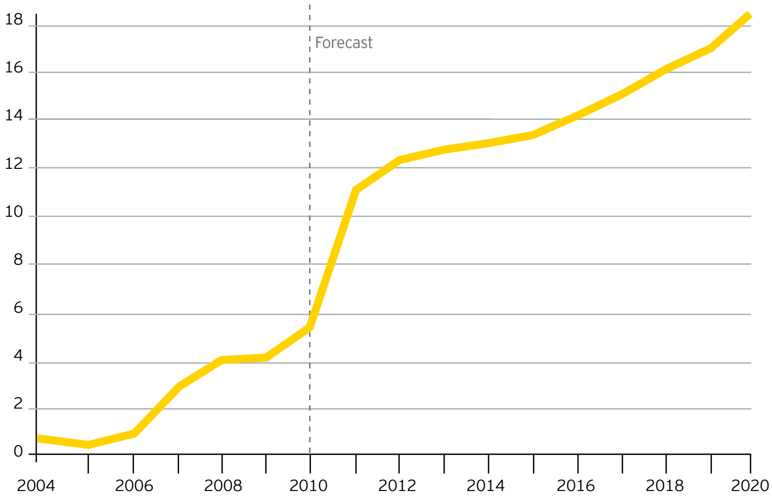
> "The transition from a local or regional company to a global company relies heavily upon appropriate logistics planning. Oftentimes, Asian companies expanding into global markets will be competing against other companies that have been operating globally for a number of years. To be successful, Asian companies will need to make this transition seamlessly such that their costs and therefore pricing can remain competitive on a global scale."

Channing Flynn, Global Technology Tax Leader, Ernst & Young

Careful consideration will be needed about how to move from investment to profitability. Companies will need to be clear about how and when they will achieve a return on investment, as overseas expansion can bring complexity and higher costs. Rigorous performance management will be essential to ensuring that managers are clear about what they need to achieve and by when.

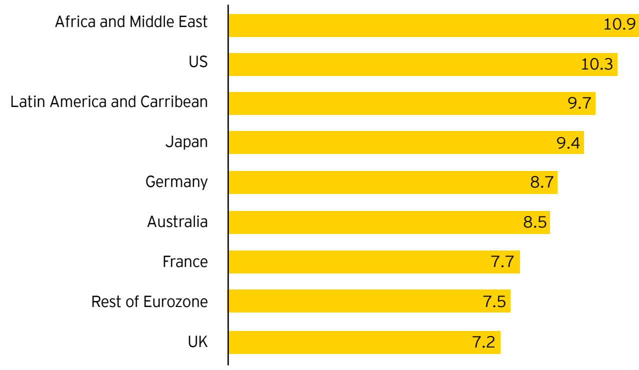
Figures

Figure 1: Outward FDI is expected to rise rapidly for Thai companies



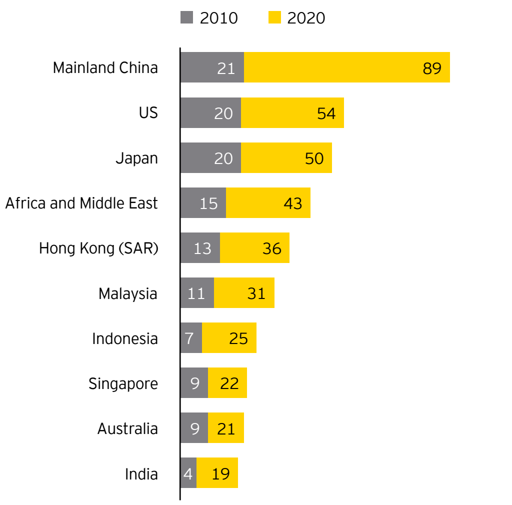
Source: *Oxford Economics.*
Shown: Outward FDI, US$b.

Figure 2: Annual growth in Thai merchandise exports outside of Asia, 2010-2020



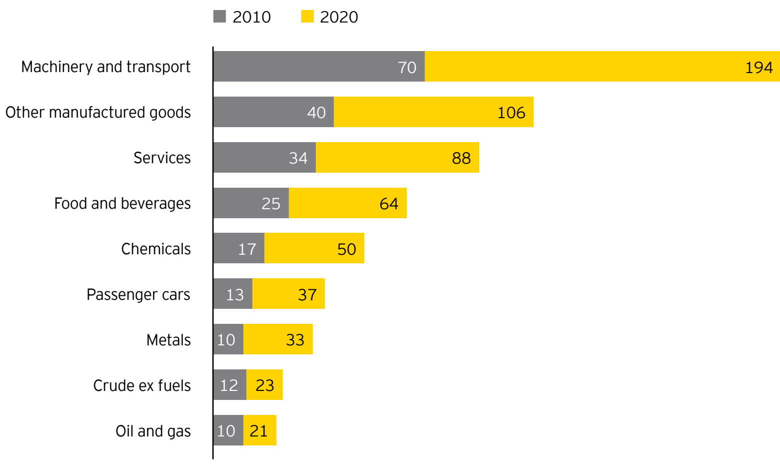
Source: *Oxford Economics/IMF*.
Shown: Per annum percentage growth in exports.

Figure 3: Thai merchandise exports, 2010-2020



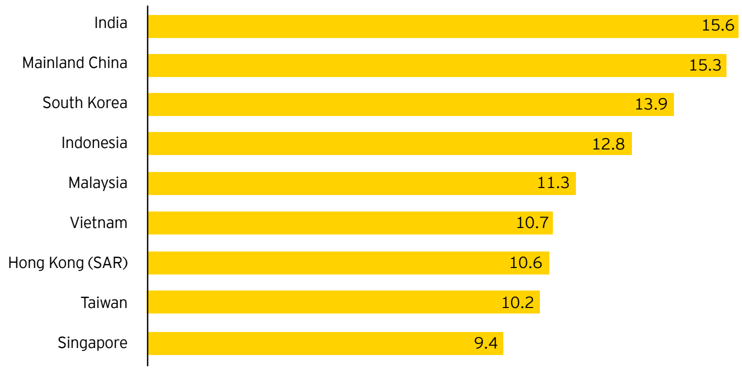
Source: *Oxford Economics.*
Note: Export value by destination market, US$b.

Figure 4: Thai exports by sector, 2010-2020



Source: *Oxford Economics/UNCOMTRADE.*
Note: Export value by sector, US$b.

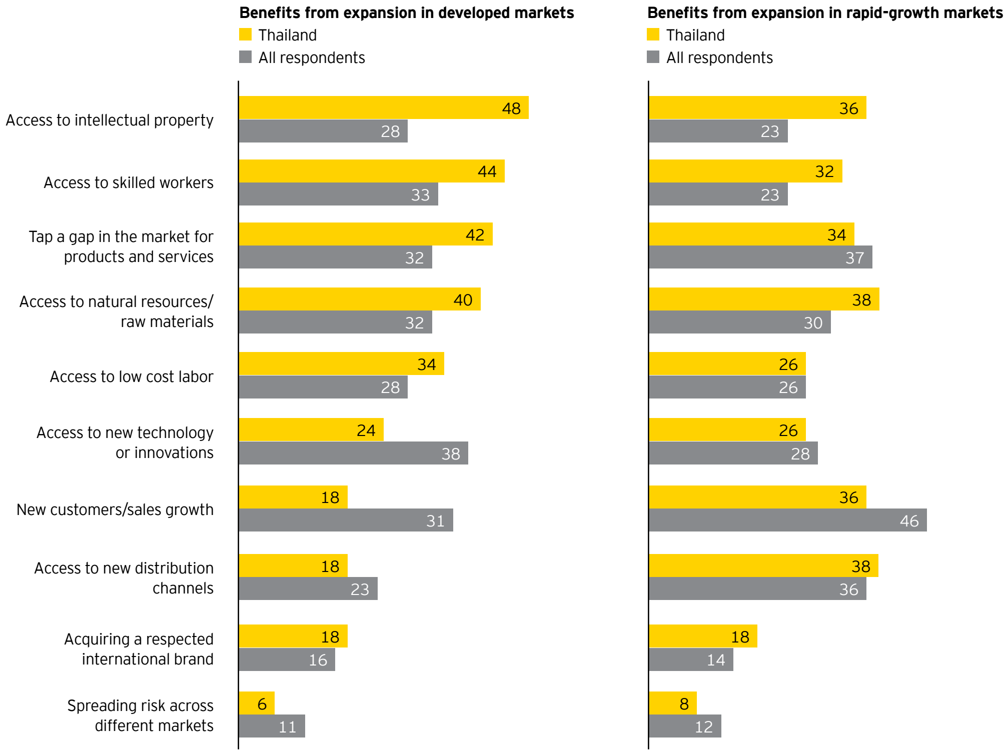
Figure 5: Annual growth in Thai merchandise exports within Asia, 2010-2020



Source: *Oxford Economics/IMF*.
Shown: Per annum percentage growth in exports.

Figure 6: The benefits of international expansion go beyond sales growth alone

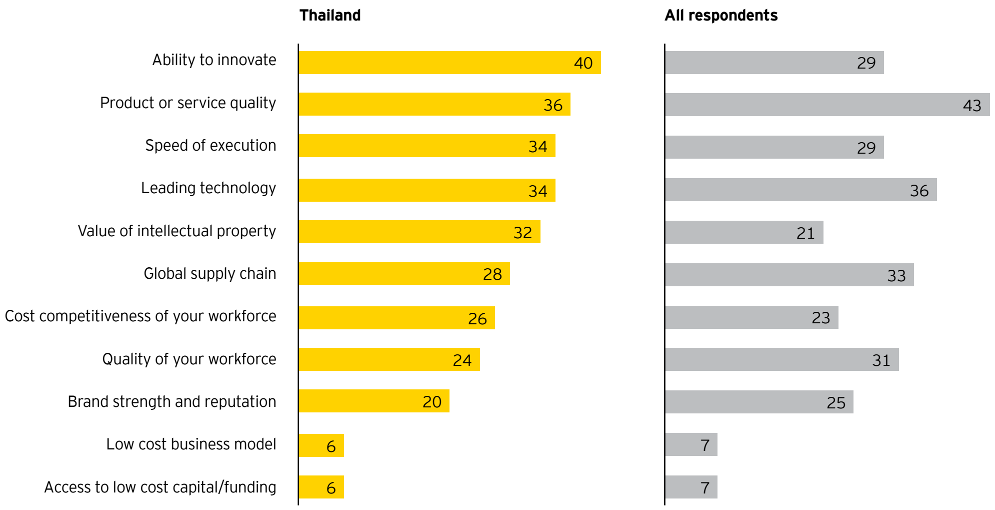
What are the most important benefits you would be looking to achieve through international expansion in developed markets and rapid growth markets?



Source: Ernst & Young *Beyond Asia* survey.
Shown: Percentage of respondents. Thailand (50), all respondents (617).

Figure 7: Thais see innovation as their leading asset

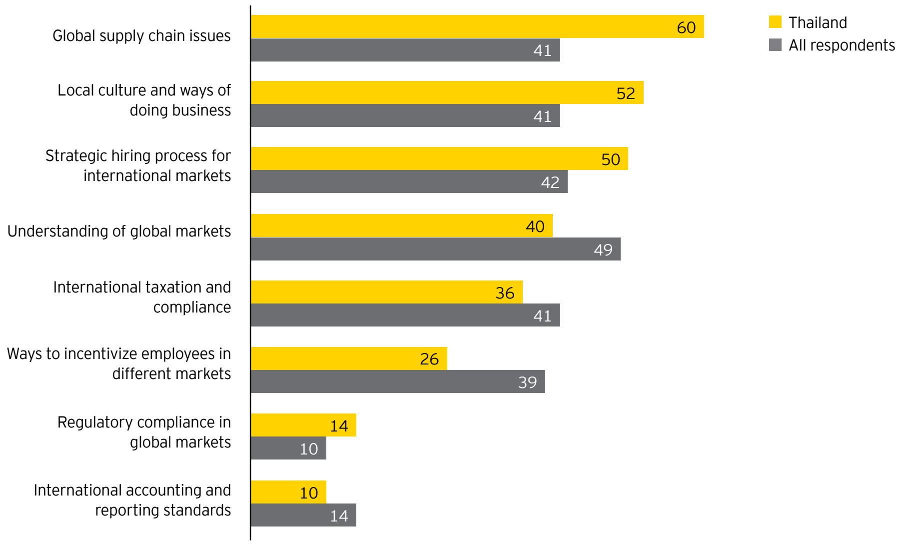
What are your companies most relevant strengths and advantages as it targets international markets for sales and investment?



Source: Ernst & Young *Beyond Asia* survey.
Shown: Percentage of respondents. Base: Thailand (50), all respondents (617).

Figure 8: Supply chain issues and strategic hiring are important areas where Thai corporate leaders need to develop expertise

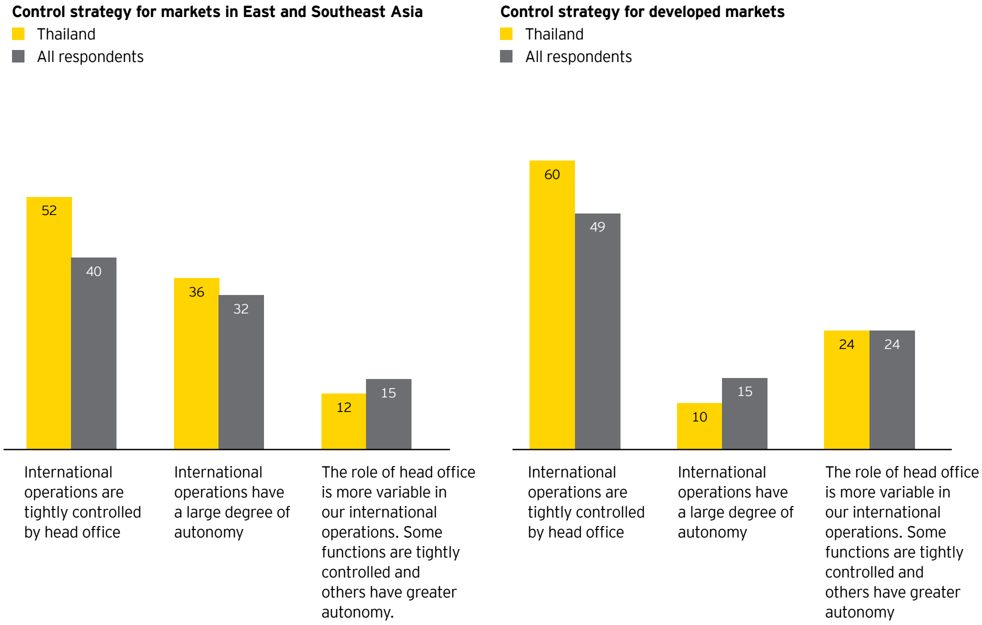
Where does your organization's top management team need more knowledge or insight to be successful in today's global marketplace?



Source: Ernst & Young *Beyond Asia* survey.
Shown: Percentage of respondents. Base: Thailand (50), all respondents (617).

Figure 9: Thai companies are more likely to control international operations from head office, as compared with their regional peers

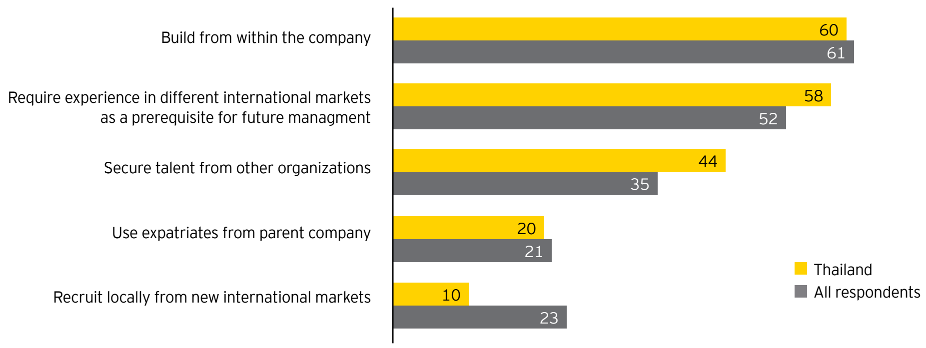
Which description best fits your company's international strategy in East or Southeast Asia? And in developed markets?



Source: Ernst & Young *Beyond Asia* survey.
Shown: Percentage of respondents. Base: Thailand (50), all respondents (617).

Figure 10: Thai companies are far more averse to recruiting managerial talent from new international markets

Where does your organization's top management team need more knowledge or insight to be successful in today's global marketplace?



Source: Ernst & Young *Beyond Asia* survey.
Shown: Percentage of respondents. Base: Thailand (50), all respondents (617).

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In these challenging economic times, opportunities still exist for growth. In *Growing Beyond,* we're exploring how companies can best exploit these opportunities – by expanding into new markets, finding new ways to innovate and taking new approaches to talent. You'll gain practical insights into what you need to do to grow. Join the debate at www.ey.com/growingbeyond.

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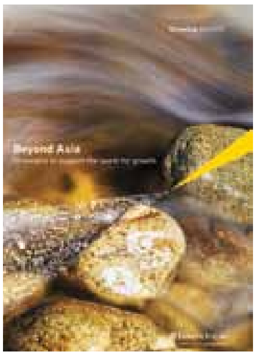

Asian companies face major challenges as they expand globally. This report explores these challenges and their business implications.