HIGH GROWTH MARKETS

Insight and perspective on today's global economic hot spots

September 2014

Unleashing Africa's potential

A strong manufacturing sector is the key to sustainable growth

Telecommunications in Latin America
Sourcing the funds to deliver high-speed connectivity

India's budget
Can the new government translate bold words into action?

M&A in Indonesia
Open for business — but investors must do their homework

KPMG
cutting through complexity

A constantly changing global landscape

The fast pace of change in developing economies is throwing up new challenges and opportunities. As companies look to take advantage of opportunities in India, where the newly elected government is easing the restrictions for investors in hopes to regain its status among the world's leading economies, or in Africa, where countries such as Nigeria and Kenya are resizing their GDPs to show the true value of their markets, the doors are open for a variety of businesses to enter.

At KPMG, we understand the complexities of an international investment strategy and have built up on-the-ground expertise across high growth markets. We also recognize that innovation is not the exclusive domain of mature countries, and it creates some exciting openings for new business models — as opposed to simply exporting current ways of working.

In this issue

Africa's potential has long been a subject of speculation, with its billion, mainly young, citizens and rich natural resources. The article on page 11 discusses why the continent has yet to fulfil its promise, and it argues that only through manufacturing can economies build a sustainable base for long-term affluence. Fabric producer Vlisco can hardly claim to be new to Africa — the company is almost 170 years old — but through its clever brand repositioning, it is making and selling more of its products than ever before in the region, targeting the middle classes. Read more about this African success story on page 14.

India's recent economic record pales beside that of China, one of the factors behind the landslide victory of the Bharatiya Janata party. The new government's first budget comes under scrutiny on page 16, receiving a cautionary thumbs-up for its pledges to boost the industrial sector through economic zones and an easing of restrictions on foreign investment.

Consumers across Latin America are becoming increasingly frustrated at the poor broadband coverage that is restricting their use of smartphones and holding back business. An insightful feature on page 18 charts efforts to attract sufficient investment to create a comprehensive telecommunications infrastructure, with the likes of Colombia, Peru and Chile leading the way. Telecommunications deregulation in Mexico has largely replaced a state monopoly with a private version, and page 19 outlines government attempts to shake up the market through network sharing and new licenses.

Indonesia can no longer be described as a sleeping giant, with the world's fourth largest population and a GDP of US$900 billion. However, as the commentary on page 21 observes, deal makers are frustrated by a cumbersome regulatory climate and complex labor and insolvency laws, and need help navigating their way to successful M&As.

Finally, we return to the theme of innovation in an *Off-the-cuff* interview with consultant, author and Asia expert Ben Simpfendorfer. His recipe for success in the region is a heady cocktail mixing one part of e-commerce with two parts of local presence, shaken not stirred!

Mark Barnes
Global Lead Partner
KPMG High Growth Markets

Global briefs

Investment spotlight

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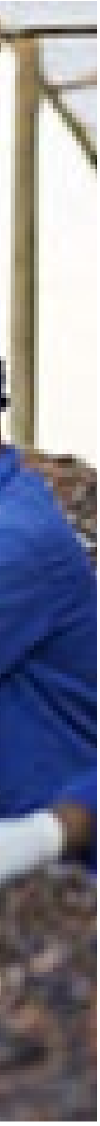

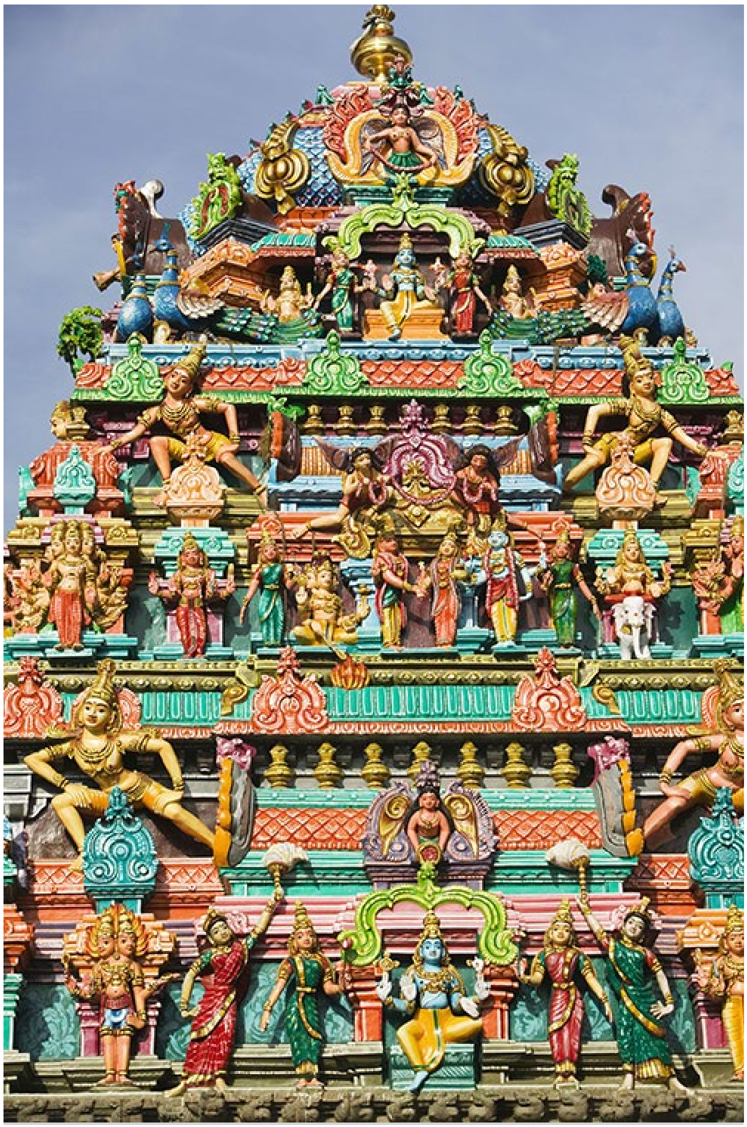

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GLOBAL BRIEFS

Observations, trends and indicators

Fast food, fast cars, fashion, fuel, financing and other trends happening across the world's emerging markets.

PHILIPPINES BANKING

Philippines opens its doors to **foreign ownership of banks**

A new act permits overseas banks to fully own existing Philippine banks or set up subsidiaries or branches in the country. Any applicant bank must be "established, reputable and financially sound", widely owned and publicly listed in its country of origin, except where owned and controlled by its government. Applications will also be influenced by the strategic trade and investment relationship between the Philippines and the bank's home country, as well as the reputation for innovation and willingness to fully share its technology. Minimum capital requirements will be the same as for Philippine banks.

INDONESIA INFRASTRUCTURE

Building for **success**

New president set to bet big on roads, rail and ports

Essential infrastructure improvements could revitalize Indonesia's flagging economy by lowering distribution costs and speeding up rural development. Newly elected president Joko Widodo has pledged to build 2,000 kilometers of roads and 10 seaports, to better connect consumers in the world's fourth most populous nation.

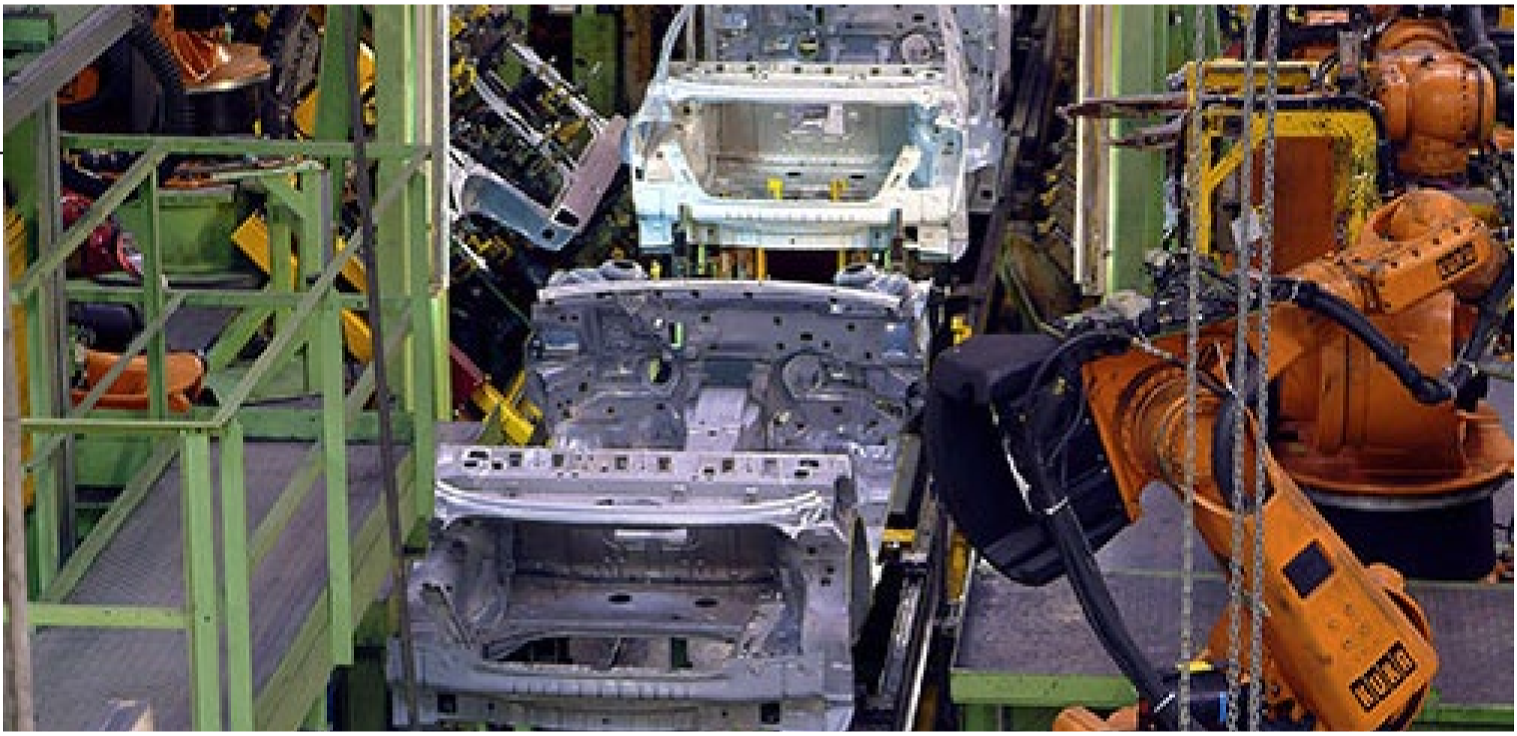
Poor transport links have swollen logistics expenditure to about 27 percent of gross domestic product (GDP), the highest in Southeast Asia. This holds back sales everywhere from the smallest shopkeepers to consumer giants such as Unilever. Those living in the 77,548 villages scattered throughout this vast archipelago are the hardest hit, with household consumption of staple products up to 60 percent lower than in towns and cities.

Indonesia's Food & Beverage Producers Association says sales could grow by as much as 50 percent with improved access to rural areas. This should mean good news for infrastructure companies poised to benefit from a slew of new projects.

VIETNAM PRIVATE EQUITY

Top of the radar

A survey of private equity firms suggests that Vietnam is a more attractive proposition than neighbors Myanmar and Indonesia. Half of those polled believe the economy will improve in 2014–15, with retail the single most appealing sector, followed by food and beverages and hospitality, leisure and property. The coming years should see considerable M&A activity, as foreign capital flows into the country in ever-increasing volumes. One of the priorities of any new investor will be to restructure businesses, bolster management and raise production efficiency.



CHINA AUTOMOTIVE

Driving **expansion**

New initiatives by GM and BMW reflect China's position as the world's number one auto markets.

China's insatiable hunger for cars has fueled significant developments by two major global players. In response to surging demand for larger, low-cost family vehicles, General Motors (GM) is redesigning its distribution network to speed up sales of its Baojun range. Sales in China of MPVs rocketed by 55 percent during the first half of 2014, as consumers in rural markets and lower-tier cities joined the clamor for mobility. GM has begun combining sales channels of its two largely-China-only brands with SAIC, China's biggest automaker, including plans for a limited number of 'dual-brand stores' where consumers could buy vehicles from both brands.

At the premium end of the market, BMW intends to double the number of models it produces in China and extend its successful alliance with local partner Brilliance China Automotive Holdings to 2028. This expansion includes a new, lower-price model designed specifically for local tastes — a growing trend amongst foreign manufacturers. With China surpassing the US as BMW's largest market, capacity in the German producer's two Chinese factories in Shenyang is due to rise from 300,000 to 400,000 vehicles per year.

BRICs FINANCE

New **BRIC development bank** launched

In an effort to accelerate economic growth, the BRIC group of emerging powers has introduced a US$50 billion development bank and a US$100 billion crisis contingency fund. These initiatives are seen as counterweights to the Western-dominated World Bank and International Monetary Fund. Based in Shanghai, the bank's first president will be from India, with a Brazilian chairing the board. The capital will be equally shared among Brazil, Russia, China, India and South Africa, and the emergency fund is designed to help avoid short-term liquidity pressures, promote further BRIC cooperation, strengthen the global financial safety net and complement existing international arrangements.

UAE HEALTHCARE

Cheaper flights for health tourists

Overseas patients traveling to any of India's Apollo Hospitals can now benefit from discounts on flights with Middle Eastern airline Emirates. Apollo is at the heart of the boom in health tourism, with customers from over 120 countries seeking high-quality, affordable healthcare. The agreement covers 19 countries across the Middle East and Africa, with discounts up to 10 percent. Apollo's Indian customers are also eligible for savings on flights with Emirates.

KENYA ECONOMY

Kenya's economy a fifth larger than previously estimated

A statistical revision has increased the size of the Kenyan economy by a fifth, spelling good news for foreign investors looking to buy into the country's debut sovereign bond. A change in calculation methods and better data collection has raised the country's GDP to US$50 billion, propelling it for the first time into the World Bank's definition of 'middle-income'.

Kenya's government is hoping to raise US$1.5 billion–$2 billion on the international market on the back of rising annual growth rates projected at 5.8 percent for 2014 and 6.4 percent in 2015. Early signs indicate a strong appetite for the bond, with analysts anticipating interest rates as low as 7 percent.

This resizing follows the announcement earlier in 2014 that Nigeria's GDP was 89 percent larger than estimated, making it Africa's biggest economy.

MYANMAR INVESTMENT

Universal attraction

Rolls-Royce and Vietnam's biggest pharma company to invest in Myanmar

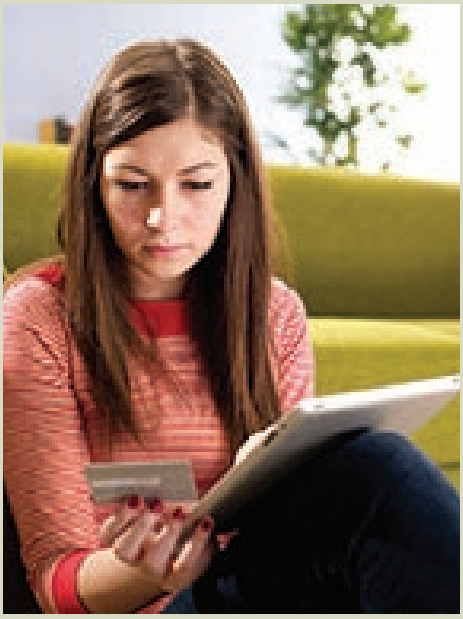
In another sign of Myanmar's resurgence, engineering giant Rolls-Royce is supplying engines, associated systems, and support and maintenance services for the Hlagwa Power Plant. The gas engine-based independent plant is owned by local operator RGK+Z&A Group and is a major step towards improving the country's electrification rate of just 26 percent.

Vietnamese pharma company VietNamNet Bridge — Hau Giang (DHG) is in talks over a joint venture project with a local firm to build a production facility. Myanmar offers a number of incentives for pharmaceutical producers, providing a sound base for DHG to increase its export revenue to offset predicted declines in its home antibiotics market. Several Vietnamese companies have invested in Myanmar, attracted by a population of 65 million and average annual economic growth rates of 8.7 percent over the past decade. DHG expects to put US$4.5 million into the deal, and construction of the plant could begin as early as 2015 if the two parties reach an agreement.

SOUTH AFRICA PAYMENTS

Shopping safely in cyber space

With the launch of a new digital wallet facility, MasterCard's South African customers can now make secure digital payments online. The MasterPass acceptance network allows user to store all their personal details in one place, enabling single-click checkouts from any device, without the need to enter card numbers, addresses and other information. Standard Bank is the first South African financial institution to offer MasterPass, with others soon to follow, and apps are available on iOS, Android and BlackBerry.



BRAZIL IT SECURITY

Online **freedom**

Brazil's new internet 'bill of rights' aims to safeguard freedom of expression, protect users' privacy and ensure equal access.

In a move that has far-reaching implications for online service providers (ISPs), retailers and publishers, Brazil has introduced a new Internet Law, with a strong focus on privacy. Collection and use of private information is now restricted, and such data cannot be shared without users' consent, which will impact the use of personal details for marketing purposes. Any company with servers located outside of Brazil is still subject to the law if they provide services to Brazilian users; this could conflict with their own national privacy or data protection laws.

Operators will no longer be able to charge higher rates for content that uses greater bandwidth, like video streaming or voice communication services. The law also clarifies that providers such as Facebook will not be liable for damages arising from hosting user-generated or uploaded content. Many Brazilians have no access to the internet, and the law obliges the government to improve services and connectivity.

INDIA E-COMMERCE

Jostling for position

Amazon's entry into India's e-commerce market has heightened competition and increased the pace of consolidation.

The arrival of global giant Amazon has shaken up the US$2.3 billion Indian e-retailing sector, triggering an upsurge in M&As. Deal value in the first half of 2014 had already exceeded the previous year's total, spearheaded by the US$330 million capture of online fashion retailer Myntra by rival Flipkart.

Investors are continuing to inject capital into a market that is forecast to account for 3 percent of all Indian retail sales by 2020 — totaling US$32 billion. With few large players, further consolidation can be expected as niche and specialty businesses are acquired by bigger firms.

LIBYA

Three years after the fall of Muammar Gaddafi, **is Libya on the cusp of a new era of growth?**

The low turnout in Libya's June 2014 general elections demonstrated the challenges gripping this fledgling democracy, as a combination of fear of violence and political apathy kept voters away in their hundreds of thousands. Such concerns should not overshadow the plentiful opportunities in a country still rebuilding after a brutal conflict and decades of corruption.

Infrastructure is arguably the single most pressing need, particularly for the oil and gas sector that forms the core of Libya's economy, accounting for around 70 percent of gross domestic product (GDP), 95 percent of state revenues and 98 percent of exports.[1] Poor links to ports means that the industry is operating well below full capacity, a situation exacerbated by industrial action that has closed oilfields and blockaded key ports. Consequently, a cash-strapped government has been forced to cut back on plans to replace and repair roads, universities and schools damaged during the 2011 uprising.

These challenges, however, can open the door further to private finance for a wide range of infrastructure projects. The government has ambitious plans to build a railway system stretching from Tunisia to Egypt, to expand the highway and road network, and develop seven major airports. Healthcare is lagging behind comparable nations, while the rapid urbanization has created a dire shortage of housing and associated services.

Strength through diversity

Libya is anxious to reduce dependence on hydrocarbons by diversifying its economy, with an emphasis upon agriculture, tourism, fisheries, mining and natural gas. The agricultural sector accounts for less than 2 percent of GDP but is becoming a top priority, with domestic food production currently meeting only 25 percent of demand.[2]

The government is extending a number of incentives designed to boost the tourism sector, with state-owned hotels being offered to private and foreign operators. In 2012, Tameer Holding (a United Arab Emirates property developer) announced a deal with the Libyan authorities to develop a US$20 billion residential and tourist project near Tripoli.[3] Several major hotel groups are launching new or revamped properties, including Sheraton, Marriott, Intercontinental and Radisson.

[1] *Hopes Pinned on Private Sector as Libya Economy Slumps,* Daily News Egypt, 16 February 2014.
[2] *Economic Developments 2013: Last Year Libyan Economy Experienced Major Rebound,* The Tripoli Post, 23 July 2013.
[3] Ibid.

Light manufacturing has growth potential both for domestic use and for export to Mediterranean and North Africa markets, with a number of former state-owned firms being privatized. Small businesses have been at the vanguard of progress, with shops and boutiques in Tripoli and other cities boasting the latest in luxury brands — often the results of partnerships with foreign investors.

Encouraging signs for private investors

Options for financing should broaden with the anticipated arrival of new laws regulating public-private partnerships (PPPs), along with pro-business reforms to encourage foreign direct investment and expansion of the private sector. The next bidding round for exploration licenses in 2014–2015 is set to include softer terms, to increase the attractiveness of the oil and gas sector. Telecommunications is also expanding, and tenders for a third mobile phone license are expected sometime between 2016 and 2018.

A number of sectors permit some form of foreign ownership, notably manufacturing. Participation is typically through joint ventures, and 100 percent fully owned operations are rare. A few Libyan banks have already been privatized, but foreign banks and insurance companies are currently prohibited — at least until 2015 when a new constitution is drafted, which is also likely to include a framework for Islamic finance.

With high unemployment and a young population, labor is in plentiful supply, although technical, professional and managerial skills are much harder to find. Investors into Libya would almost certainly have to import talent on a short-term basis to fulfil crucial roles and enable skills transfer, while increasing training across the workforce. One of the drivers for PPPs is to acquire essential project management and other competencies from more mature markets.

After 43 years in power, Gaddafi's shadow inevitably looms over Libya, and the current troubles in the east of the country indicate that the path to democracy may not always be smooth. A more permanent government should eventually restore stability, with Real GDP growth forecast to enter the black at 2.5 percent in 2015, rising to around 5 percent thereafter. This should lay the foundations for economic expansion, fuelled by infrastructure projects and healthy participation of foreign capital.

83rd

largest economy in the world and 105th largest GDP per capita

Population:

6.2 **million**

With a labor force of 1.35 million

Urban Population:

77.7%

Demographics: 0–14 years: 26.9%; 15–24 years: 68.3%; 65 years and over: 3.9%

Transitioned to a full democratic government as a result of the June 2014 election.

Major Cities: Tripoli 2.2 million; Benghazi 650,000; Misratah 385,000

Capital: Tripoli 2.2 million

Type of Government: Parliamentary Republic

Local Currency: Libyan Dinar (LYD)

Official Language: Arabic

Twenty-seventh-largest producer of crude oil in the world and 15th-largest exporter. Ninth-largest reserves of petroleum worldwide, contributing to more than 95 percent of total government revenue.

Libya's population is primarily Arab, Berber or a combination of the two.

Libya has a high literacy rate of around 90 percent.

The largest water development project ever devised, the Great Man-Made River Project, brings water from aquifers under the Sahara to Libya's coastal cities.

GROWTH MARKETS

African potential: unleashed or unfulfilled?

A strong manufacturing sector can help Africa's emerging economies escape the poverty trap and build sustainable growth.

With a billion people spread across 54 diverse nations, and rich natural and agricultural resources, Africa is often described as the last true frontier for economic development. Many of its governments are starting to address post-colonial inefficiencies by trying to establish stable democracies, effective legal and tax regimes and realistic economic strategies. These improvements, along with the obvious attraction of a young, growing consumer class, have attracted considerable interest from foreign investors.

Yet success in Africa is by no means assured, with progress held back by bureaucracy, inadequate infrastructure and a deep-rooted nepotism that obliges entrepreneurs to share their wealth and offer jobs to relatives and friends. Business people also have a bias towards trading over production, preferring a quick and easy mark-up on goods to the longer-term challenge of making things.

The contrasting fortunes of two other emerging economies — China and India — provide some useful lessons on how Africa can fulfil its latent potential. Through careful forward planning, China has become the workshop of the world, with a strong manufacturing industry that has brought employment to tens of millions in its plants and factories, and created further jobs in supply, maintenance, logistics, sales and marketing. This success has been founded on a robust supporting infrastructure, flexible working practices and an investor-friendly environment featuring special economic zones offering tax exemptions and incentives.

> Africa needs to emulate China, whose plants and factories have brought employment to tens of millions.

India, on the other hand, has seen its progress thwarted by red tape and political stalemate, with lack of investment in ports, airports, roads and energy, limited tax concessions, and major restrictions on foreign ownership of assets. Anyone wishing to start up a manufacturing facility has to cope with poor transport connections, an unskilled workforce, constant power cuts and restrictive labor laws, as well as painfully slow processes for resolving any commercial disputes. The thriving outsourcing sector — widely held up as a symbol of the new India — provides work for just a tiny proportion of the 1.1 billion population.

Consequently, China continues to enjoy higher employment levels and a stronger GDP growth rate, while India struggles with poverty and inequality.

Creating an industrial base

Across the African continent, countries face the same hurdles that have held back India. The riches of its resources and agriculture are under-exploited, as most materials and foods are exported in their raw forms, rather than adding value through refining and packaging locally. Meanwhile, government efforts to impose centralized strategies typically face opposition at federal and local levels.

Since 2009, special economic zones have been introduced in several African countries.

Africa is still not widely perceived as a welcoming place for overseas capital. Only three of its countries made it into the 2014 World Bank's Ease of Doing Business Index top 50 (Mauritius, Rwanda and South Africa in 20th, 32nd and 41st places, respectively), and African nations occupy most of the bottom rankings. Despite some advances, fiscal systems lack stability, corruption is still a major problem, while concerns remain over the fairness of judicial systems.

[1] *Angola Boosts Infrastructure Spend to Attract Investment,* Bloomberg, 3 October 2013.
[2] *GE Oil & Gas, GLS Form JV to Support Growth in Angolan Energy Sector,* Energy Business Review, 30 January 2013.
[3] *Nigeria Wins $1bn General Electric Manufacturing Investment,* Financial Times, 31 January 2013.
[4] *GE Plans to Establish an Assembly Plant in Ethiopia,* The Reporter, 25 January 2014.

In order to build modern economies, Africa's countries and regions must follow in China's footsteps and invest in manufacturing, which not only creates jobs, but boosts the balance of trade by reducing reliance on expensive imports. The Ivory Coast supplies a third of the world's cocoa, and until recently, exported raw beans at a low margin. Its government is now seeking ways to raise the proportion of cocoa processed domestically, through tax breaks and other fiscal tools, mandating that at least 30 percent of the annual harvest is transformed locally.

Africa's second biggest oil producer Angola is trying to diversify its industrial base, by investing in ports, airports, roads and hydropower. It expects to attract US$4 billion a year in non-oil investments from abroad by 2017, with recent projects such as bottling plants for drinks companies and a US$282 million hotel complex to pep up the country's tourist sector.[1] General Electric (GE) and Angola-based GLS Holding have formed a new joint venture, with a proposed initial investment of US$175 million to construct a new manufacturing facility.[2]

GE is also investing close to US$1 billion in factories for the energy industry in Nigeria, creating 2,300 jobs in the local economy — as direct hires or through suppliers — and positioning the country as a regional manufacturing hub.[3] And as confirmation of the US-based manufacturing giant's confidence in Africa, it is planning to establish a medical equipment assembly plant in Ethiopia.[4]

Chinese firm Huajian Shoes employs 600 workers at its factory near Addis Ababa in Ethiopia, but has much bigger ambitions, by investing over US$2 billion in a light manufacturing special economic zone that aims to create 30,000 jobs as part of a 'shoe city' producing footwear, handbags and accessories. Huajian is partnering with the China-Africa Development Fund (CADFund), a private equity facility promoting Chinese investment in the continent in agriculture, infrastructure, natural resources and industrial park projects. Other ventures include a power plant in Ghana, a port in Nigeria, cotton farms in Malawi and a US$100 million car plant in South Africa.[5]

Since 2009, special economic zones have been introduced in several African countries including Zambia, Mauritius, Ethiopia, Nigeria, South Africa, Egypt and Algeria, with more in the pipeline, offering exciting prospects for growth and job creation.

In it for the long-term

Having suffered the worst excesses of colonialism in previous centuries, African nations are understandably keen to avoid a repeat scenario and are wary of the motives of foreign companies. By investing in the physical and social infrastructure, and demonstrating a commitment to local communities, investors can be part of the continent's renaissance.

Effective social programs are an integral part of all multinational organizations' strategies, whether it is building roads, housing, schools and hospitals, improving sanitation and water supplies, providing vaccinations and health education, offering free broadband and laptops to schools and businesses, or training local workers.

One common barrier is a lack of certain essential skills such as engineering, IT and management. The more enlightened African governments permit foreign companies to bring in their own expatriate workers, on the understanding that these are temporary measures. In Ethiopia, the aforementioned Chinese shoemaker Huajian feels that the new business zone will act as a center of excellence to transfer skills to locals.[6]

Commentators often speak of Africa's growing population as a 'demographic dividend' promising some two billion consumers by 2050. However, without a strong industrial base, this could quickly turn into a demographic time-bomb of the discontented unemployed, fomenting civil disobedience, crime and terrorism. Manufacturing is the key to unlock the continent's massive potential, transforming countries from mere providers of resources to mature, broad-based economies.

[5] *Chinese Firm Steps Up Investment in Ethiopia with 'shoe city',* The Guardian, 30 April 2013.
[6] Ibid.

Material gains

The desirable fabrics of Dutch company Vlisco Group have been at the heart of West Africa's fashion trade since 1846. The customer-centric company is now using brand identity to accelerate its growth.

Hans Ouwendijk is the CEO of Vlisco Group. In 1982, he graduated in Business Economics at the Erasmus University Rotterdam. After his graduation, Hans Ouwendijk continued his career at Laura Ashley (1984–95) and at Mexx (1995–2006). In both companies, Change Management was his main focus.
Under the direction of Ouwendijk, among others, the Vlisco Group has grown into a company with over 2,700 employees. His strategic plan is paying off. For Hans Ouwendijk, bringing back the entrepreneurial spirit within the Vlisco Group is key. The transition from product-driven to brand-driven is the enormous success behind the tremendous growth.

"What surprised me most when I first started working for Vlisco," says CEO Hans Ouwendijk, "was that the African consumers really feel like they own our brand, not the other way around." It's something of a paradox that one of Africa's biggest cloth companies is based in a small town in the Netherlands. Founded in 1846 in the old textile town of Helmond in North Brabant, Vlisco originally sold hand-printed fabrics along the Dutch East India Company's trade routes. These fabrics, which used European industrial know-how to speed up labor-intensive Indonesian wax batik processes, were bartered during stopovers in western Africa and became highly sought after.

Over the years, Vlisco's compelling mix of Far Eastern inspiration, European adaptation to African demand for bolder colors and patterns, and high-quality 'Dutch wax' fabric helped it become a central part of commerce and culture in West and Central Africa. Designs acquired different names and symbolic meanings in different countries. In Togo, the market women who sold Dutch wax were known locally as 'Mama Benz' because they became wealthy enough to own the first Mercedes-Benz cars there — and became influential politically and socially.

Fast-forward to the present day, and the continued popularity of fabric that is turned into made-to-measure, bespoke garments by local tailors in Africa — where 95 percent of Vlisco Group's sales are generated — has helped the company flourish. In 2013, turnover reached a record US$378.4 million, a 61 percent increase on 2009's sales of US$234.2 million. Volumes are up too, from 52.4 million yards of fabric in 2009 to 65.7 million in 2012.

"We are growing fast in our markets because we are listening to consumers," says Ouwendijk, who has radically changed the company's strategy since arriving in 2010, when it was acquired by London-based private equity company Actis. "That is not a unique strategy, but we are one of the few companies doing this specifically for Africa."

> "African consumers really feel like they own our brand."

Ouwendijk joined Vlisco Group from Fashion Fund One BV, a private equity firm he founded in 2006. Under his leadership, Vlisco has repositioned itself as a brand-driven fashion company, helping it counter cheap counterfeits that threatened profits. "The company I inherited was very focused around design and manufacturing," he says. "Now we focus more on the consumer: on marketing, brand development, innovations and customer loyalty. Being close to our consumer is critical."

The company owns four distinct brands. Vlisco is the luxury, aspirational brand, still produced in the Netherlands. Uniwax and GTP, which are made in Ivory Coast and Ghana, respectively, target the growing middle class. Woodin, the firm's smallest and fastest-growing product, is made in Ghana and targeted at younger, pan-African consumers.

All four brands offer fabrics for consumers to create their own clothes, which accounts for most of the group's sales. Top-of-the-line Vlisco also produces scarves and luxury handbags, while Woodin's ready-to-wear range includes men's shirts and ladieswear.

The fact that one of the most successful fashion brands in Africa is a fabric maker is driven by cost — it's much cheaper to have the fabric tailored in Africa — and customer taste. Rather than signifying their allegiance

to a trend or community, the consumer wants to stand out with their own designs.

Sales channels play their part too. With traditional bricks and mortar retail still under-developed, most of the company's fabrics are sold via wholesalers and open air markets. Vlisco Group has 30 stores of its own and may double or triple that network in the next four or five years.

E-commerce is less developed than bricks and mortar. "Because of logistical limitations, African consumers are not ordering so much from the web yet," says Ouwendijk. "That is likely to change in the next few years. We believe there will be a massive opportunity for online sales in Africa when the logistical challenges are resolved."

Having a product for every price point is key to success. "Each brand serves a different consumer. This is an ideal position: multiple brands in different parts of this fast-growing consumer brand. For Uniwax and Woodin, we produce about 400 or 500 designs for each brand every year. We bring new designs to market in a few months," Ouwendijk says.

Customer tastes vary as widely in Africa as in Europe. Ghanaian consumers, for instance, like traditional green hues. Certain designs are popular in particular regions, often influenced by local sayings or landmark events. In Togo, the Love Bomb (or Wounded Heart) design symbolizes the mood of a woman heartbroken by her husband's adultery. Vlisco's customer focus helps it understand such nuances and react accordingly.

"We get a lot of feedback from our wholesale customers and our stores in West Africa," says Ouwendijk. "We also spend a lot of time and money on research: looking at trends in the market, what is happening to particular consumers — different cultural groups, for example — and the key decisionmaking points for individual consumers."

Vlisco Group is sourcing more of its raw materials in Africa: in 2010, all cotton was sourced in the Far East. Now, more than 30 percent is grown in the continent. "We are becoming more relevant in the societies where we operate," says Ouwendijk. "That really helps in a continent where governments are looking at the added value of businesses that enter the market, or who are looking to expand."

With seven of the world's 10 fastest-growing economies in Africa, Vlisco has cause to be confident about the future. "Consumer spending is moving more into products like fashion," says Ouwendijk. "The continent's economy is growing and our product offering is in the right spot to accelerate growth."

Vlisco's recent internal research indicates that the fabric segment will grow by 100 percent in the next five years. "I was expecting lower growth of sales and more focus on ready-to-wear," Ouwendijk admits. "In certain countries, consumers prefer to have ready-to-wear in African prints because they don't have time to go to the tailor or prefer the creativity of the company, but our growth will remain in our core products — our fabrics — for now."

Technology is bringing the brands closer to the people who wear them. "New forms of media are crucial for us," says Ouwendijk. "The number of Facebook subscribers to our brand pages are far beyond our expectations: we have more than a million 'fans'. This is building consumer loyalty."

For other brands and retailers contemplating Africa's market, Vlisco's story shows the need to be realistic about timescales — and that success starts with a lot of listening.

Backing strong words with deeds

India's first budget under a new regime includes some encouraging reforms to tax and foreign ownership, and could ignite the fires of an underperforming industrial sector.

The eyes of the world were on Finance Minister Arun Jaitley when he presented the new government's budget on 10 July 2014. Prime Minister Narendra Modi's Bharatiya Janata party had much to live up to, following pre-election pledges to kick-start India's flailing economy, tackle corruption and make the country a friendlier place for overseas investors.

GDP growth had dipped below the 5 percent mark for two consecutive years, while contracting investment in manufacturing had slowed industry growth to just 0.4 percent in the year ending 2013. Poor infrastructure was a major contributor to these worrying results, yet highly restrictive rules on foreign ownership, along with excessive bureaucracy and corrupt, had scared off many potential financiers, placing India 134th out of the 189 nations on the World Bank's Ease of Doing Business Index.

Fresh from its landslide electoral victory, the government had only 45 days to prepare the budget, and understandably, some of the plans lacked detail. Nevertheless, a number of bold initiatives have laid a foundation for policy reform and broadly won approval of the financial markets, with the Sensex — regarded as a good barometer of India's prospects — exceeding the 26,000 mark in July 2014, having fallen close to 19,000 12 months earlier.

Manufacturing received a welcome boost with the raising of foreign ownership limits from 26 percent to 49 percent in the insurance and defense sectors, although some would have wished for more. India also moved a small step towards its goal of developing 100 'smart' satellite cities by easing the conditions facing foreign construction investors. The minimum size of area to be developed was reduced from 50,000 square meters to 20,000 square meters, and minimum capitalization lowered from US$10 million to US$5 million. Manufacturers with partial foreign ownership are now allowed to sell their products through retail, including e-commerce platforms, without any additional approval.

> The budget vows to revive India's use of special economic zones, although more detailed plans are needed.

Special economic zones have played a big part in China's ascent to an industrial powerhouse. After years of neglect, the budget vows to revive India's strategic use of such zones, although offers little in the way of substance at this stage. Zones have been planned in the ports of Kandla in Gujarat and Jawaharlal Nehru, located south of Mumbai, and a further 16 new port projects have also been proposed, along with airports in tier I and II cities.

Public-private partnerships (PPPs) have attracted considerable controversy in India

and other countries, but the Finance Minister has spelt out his desire to increase their use, in order to channel funds into essential infrastructure and industrial projects. He even hinted that the much prized and publicly-owned national railway system could open up to private finance. As the Chief Minister of Gujarat, Narendra Modi presided over a radical improvement in that region's infrastructure, something which he hopes to repeat on a national scale.

Retrospective taxation has proved another deterrent to investors, with a number of high-profile cases involving demands for hundreds of millions and even billions of dollars, often relating to transfer pricing disputes with foreign multinationals. This year's budget speech outlined plans for a new, high-level committee to scrutinize such cases, and promised to bring India's transfer pricing regulations in line with leading practices from around the world. This includes more frequent use of 5-year advanced pricing agreements (APAs) that would also cover the previous 4 years.

Having previously channeled their funds through tax-friendly countries, foreign institutional investors holding shares in listed Indian companies will now be able to set up offices in India without experiencing an additional tax burden. This move should enable closer links with local projects and hopefully increase private investment in infrastructure. The introduction of India's most awaited tax reform — the uniform goods and service tax (GST) — is likely to happen by the end of 2014.

Subsidies for sectors such as food and petroleum have sucked money out of government coffers, and these are set for an overhaul, with significant reductions and finer targeting of beneficiaries.

India's previous government was criticized for the short-term nature of tax incentive schemes, making it hard for businesses to gain certainty over future revenue flows. In a bid to stimulate manufacturing, the period for claiming a 15 percent investment allowance on plant and machinery has been extended from 2015 to 2017, while the annual expenditure threshold for eligibility has been reduced from US$16.6 million to US$4.2 million. Energy providers have also received a boost, with the deadline for claiming tax holidays pushed back to 2017.

Overseas businesses do not want to fall foul of the Foreign Corrupt Practices Act and the UK Bribery Act, yet the endemic nature of corruption in certain areas of Indian commerce makes it hard to comply, driving many investors to avoid India altogether. Corruption was not explicitly mentioned in either the official budget or the speech, but is an issue near to the heart of the Prime Minister, so further activity should be anticipated.

Given its short time in power, the new government has presented what observers have described as a 'working budget'. If certain measures do not go as far as some would desire, they do form a statement of intent to overcome the obstacles that have slowed India's growth in recent years. With a clear mandate, the ruling Bharatiya Janata party has the best chance in decades to turn the country into a major global player. The coming months and years will tell us whether their strong words translate into firm actions.

The Finance Minister has tried to give a general direction in the budget, and I hope that policy reforms will continue beyond the budget. The objective of attracting investments, both foreign and domestic, is much appreciated. There is focus on infrastructure, development and financing, and an effort to stimulate and create a vibrant corporate bond market. Various tax incentives have been provided to the manufacturing and infrastructure sectors. These measures are bound to have a buoyant effect on investor sentiments, promoting greater stability and investments in India.

What is worth appreciating is a break from a consumption-led budget to an investment-led budget. The budget appears progressive and sets the tone for attaining a higher growth trajectory, supplementing job creation and attracting investments for an economy grappling with multiple challenges. Also, there is an intent to modernize India. More focus is being laid on the use of information technology. Given the political mandate and stability, I am hopeful that the government will stay close to its defined targets.

Richard Rekhy
CEO, KPMG in India

Ringing in the changes

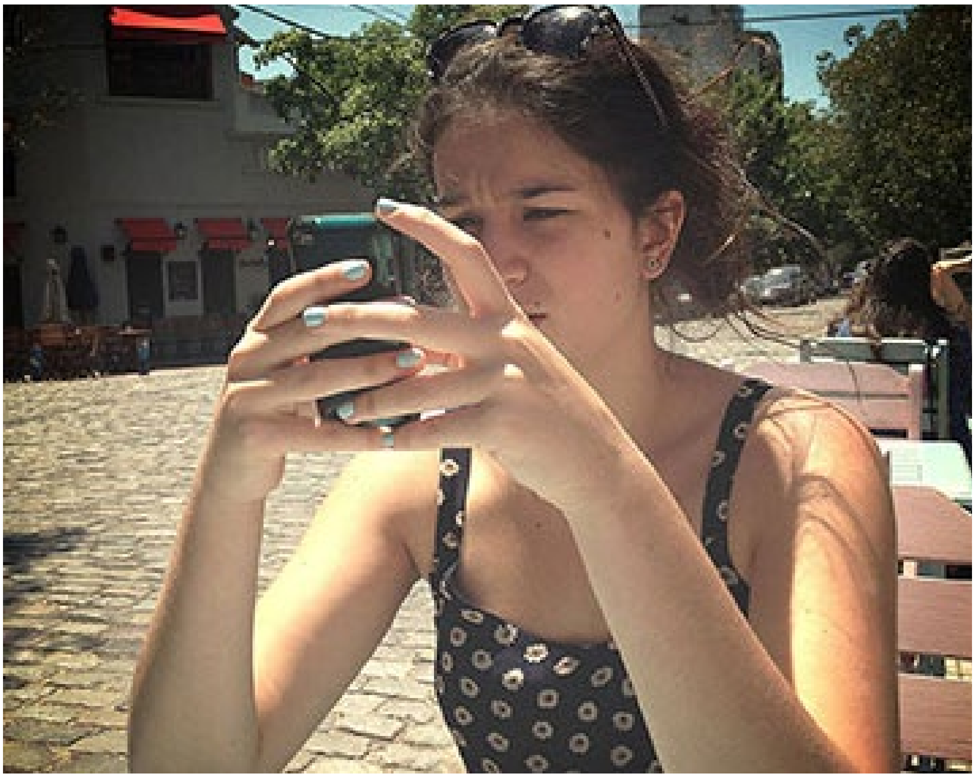
The future for Latin America appears to be mobile. Yet concerns still remain over the ability to finance the infrastructure to deliver high-speed connectivity.

Every time a TV camera panned to the crowd during the 2014 World Cup in Brazil, a sea of spectators could be seen taking photos, texting, calling or surfing on their mobile phones. If this was the tournament where mobile finally arrived, then Latin America was a fitting venue. With mobile penetration of well over 100 percent and a gradual easing of competition barriers, the continent is attracting the interest of both local and international operators eager for a share of telecommunications revenue that is forecast to reach an eye-watering US$167 billion by 2017.[1]

This boom had its roots in the deregulation of the 1990s and 2000s, when state-owned, monopoly providers were broken up, opening markets to new entrants. Two giants have emerged as the leading players across the continent: Mexico's América Móvil — which has become the region's largest wireless carrier — and Spanish firm Telefónica.

Not everyone feels that such dominance is good for the consumer, with particular concerns over high prices. In response, many countries are now in the midst of a fresh wave of regulatory reform, with Mexico and Brazil mandating network sharing, and a new media ownership law in Argentina that will force the country's largest media conglomerate, Clarín, to sell off dozens of operating licenses. Such moves will accelerate the convergence of fixed, mobile and broadcasting content.

As network sharing grows in popularity, a number of operators are bidding to become mobile virtual network operators (MVNOs), notably Virgin Mobile, which has signed an agreement with Telefónica to use the Vivo network in Brazil and the Movistar network in Mexico. Virgin already offers similar services in Chile and Colombia. The Brazilian Post Office, Algar Telecom, Tesa Telecom and Sisteer are also in the frame to become MVNOs in Brazil.



> A fresh wave of regulatory reforms is opening up networks to new operators.

Smartphones need smart networks

Latin America has largely skipped fixed line connections and moved straight to mobile, with the vast majority of customers choosing a prepaid option. Mobile internet usage is rising swiftly, fuelled by fast growth in smartphone ownership, which could reach almost 50 percent by 2017.[2]

However, fast broadband access is low compared to more mature economies, and governments and private providers are struggling to acquire the financing necessary to build next-generation fiber optic and 4G networks. Across Latin America, just 16 percent of people have direct use of broadband, two-thirds of which is through a fixed line [Teleco.com, 2014]. Insufficient bandwidth means that service tends to be slow, while an underdeveloped infrastructure often limits provision to the main cities.

Affordability is also holding back growth, with broadband prices as much as eight times greater than the OECD (Organisation for Economic Co-operation and Development) average. Consequently, less than half of Latin Americans living in areas served by fixed broadband choose to pay for the service.[3]

Continued on page 20

[1] *Latin America Telecoms Market: Trends and Forecasts 2012–2017*, Analysys Mason's, 20 February 2013.
[2] *Latin America – Telecoms, Mobile and Broadband Overview*, Budde.com, 2014.
[3] *IDB: LatAm Lagging Behind on Broadband Access*, Financial Times beyondbrics, 14 May 2014.

Better connections

Significant reforms to Mexico's telecommunications regulations could pave the way for greater competition, improved service and lower prices.

Mexico's América Móvil is a major force in global telecommunications, with a huge slice of the country's domestic fixed-line, mobile and internet market, and a leading position across Latin America, a strategy that has earned it over 270 million wireless customers.[1] Along with broadcasting giants Televisa and TV Azteca, it forms part of a triumvirate that emerged following deregulation in the late 1980s and early 1990s.

However, such dominance is also a source of frustration for the many potential competitors striving to make inroads into Mexico, with the likes of Vodafone, Telefónica and others all failing to gain a significant foothold.

An Organisation for Economic Co-operation and Development (OECD) study questioned this near-monopoly scenario, estimating that its inherent inefficiencies cost the Mexican economy as much as US$25 billion a year — equivalent to nearly 2 percent of gross domestic product (GDP). The study also ranks Mexico at the bottom of the OECD rankings for penetration for fixed, mobile and broadband, with severe under-investment in essential infrastructure and the highest prices of any emerging market.[2,3]

All this may be about to change, as the Federal Telecommunications Institute, known as Ifetel, attempts to level the playing field through a number of groundbreaking reforms, in a bid to reduce costs and improve service quality and coverage. One of the most noteworthy innovations is the requirement for the major players to share their networks, offering new entrants the opportunity to lease bandwidth for mobile voice, data and video. The government also intends to auction concessions for two new private television networks.

A new era of competition?

With the limit on foreign investment in telecommunications set to rise from 49 percent to 100 percent, and permitted foreign ownership of radio and television increasing from 0 percent to 49 percent, there is keen interest from private equity houses and other international investors from the US, Canada, Europe (particularly Spain) and China.

US broadcasters and content producers currently serving their nation's 38 million Spanish speakers see great potential in exporting to Mexico's 113 million inhabitants. This attraction is not just one-way, and Mexican media groups already have a presence in the US, while continuing to sell to Hispanic markets across Latin America and further afield in Spain, often using acquisitions and joint ventures to gain a stronger foothold.

Convergence of media and content for voice, data and video can only hasten the race for Mexico's consumers. Around half of broadcaster Televisa's revenues come from cable, telephone and wireless, while the country's low internet penetration creates ample space for multiple providers to grow concurrently.

Increased competition may eat into América Móvil's domestic business, but the ambitious group is expanding rapidly, with its recent acquisition of Telekom Austria creating a platform for expansion into central and eastern Europe,[4] where consumers favor the same prepaid model that has been so successful in Mexico.

Looking beyond telecommunications

Financial services could be another beneficiary of the communications boom. Less than a third of adults in Mexico possess credit cards, but virtually everyone has a cellphone, so telecommunications companies have the chance to stake a claim in the growing mobile payments and insurance markets. A more robust infrastructure should also boost the prospects for services such as call centers serving US businesses.

With a rising middle class and an average age of just 26, Mexico is undoubtedly becoming more attractive to external investors. Its ascension to the world stage has been further boosted by membership of the Pacific Alliance (a trade bloc that also includes Chile, Colombia, Peru and now Costa Rica) and the Trans Pacific Association Agreement, designed to enhance trade with the US and nine other Asia-Pacific member countries.

The pace of reform is unlikely to be rapid, due to a cumbersome legislative process and possible appeals from incumbent operators. Nevertheless, the next few years should see Mexico's telecommunications and media sector, so long a bastion against change, finally opening up.

[1] *New Rules to Reshape Telecom in Mexico*, The New York Times, 7 March 2013.
[2] OECD Review of Telecommunication Policy and Regulation in Mexico, 30 January 2012.
[3] *Mexican Leaders Propose a Telecom Overhaul*, The New York Times, 11 March 2013.
[4] *Slim eyes eastern Europe after Telekom Austria deal*, Reuters, 24 April 2014.

Nevertheless, several countries in the region are rolling out ultra-broadband and 4G networks. Colombia is enjoying the quickest growth and the highest broadband penetration rate of 16 percent, thanks to its National Fiber Optic Project, which will deploy 15,000km of cable at a cost of around US$600 million. An ambitious national broadband plan to build a fiber optic backbone for the more remote regions of Peru is expected to boost coverage to 9 percent by 2016.[4] Chile has an extensive and growing cable network able to transmit voice, internet and video, while Uruguay's state-owned Antel is pushing ahead with a nationwide fiber to the home (FttH) expansion plan, aiming to connect more than 720,000 households: almost a quarter of the population. In Brazil, Portuguese telecommunications giant Oi has a target of connecting 2 million homes with FttH by 2015.

Development is not restrained by national borders. The Union of South American Nations (UNASUR) has a bold vision of a 10,000km-long fiber optic broadband ring running through its member states, although this project is still at a nascent stage.

Expanding beyond traditional services

Given the low ownership of fixed-line broadband connections, mobile broadband may be the way forward for Latin America, with 4G seeing impressive growth, albeit from a small base. Brazil has been preparing itself technologically for the 2014 World Cup and 2016 Olympic Games, and the number of 4G lines was expected to quadruple from 2 million in 2013 to 8 million in 2014.[5]

Financing remains a big obstacle. Despite an estimated capital expenditure of US$50 billion in mobile networks in the past few years, there remains an urgent need for additional capacity. With profitability levels declining, operators are banking on new services such as applications, mobile banking and payments, machine-to-machine connectivity and mobile healthcare to generate additional revenue.[6]

The sheer demand for content should mean that, by the time you switch on to the opening ceremony of the Rio Olympic Games in 2016, many of the spectators will be enjoying super-fast broadband functionality via 4G. The sun may have set on an exciting World Cup tournament, but it is still rising on Latin America's telecommunications sector.

Across Latin America, just 16 percent of people have access to broadband.

[4] *Latin America – Telecoms, Mobile and Broadband Overview*, Budde.com, 2014.
[5] *2014 Predictions for Telecom in Latin America, Nearshore Americas*, Frost & Sullivan, 10 February 2014.
[6] *Mobile Economy Latin America 2013*, GSMA, 2013.

Just the deal

Indonesia's M&A market is very much open for business, but, as David East explains, investors have to do their homework.

"It's not that surprising that Indonesia is viewed as the 'go-to' destination in South East Asia" remarks KPMG's David East from his 35th-floor office that overlooks the impressive sights of downtown Jakarta. "Growth rates have been strong and the middle classes are eager to spend their newfound disposable wealth."

There is no disputing Indonesia's potential. Its 250 million population is only surpassed by China, India and the US, while a rising GDP (currently US$900 billion) is set to become the world's seventh largest by 2030. The economy also proved remarkably resilient to both the 1997 Asian economic crisis and the larger, global one that followed a decade later.

There are signs that economic expansion has stalled somewhat, as demand for key commodity exports and inflows of much-needed foreign capital softened. According to David, this coincided with a series of domestic events that have had a 'domino' effect upon the economy: "First of all, the government took the controversial decision to lift fuel subsidies and electricity tariffs. On top of this, inflation has risen, along with interest rates and unemployment, while a weakened rupiah has pushed up the price of imports."

Fortunately, such a slowdown is regarded as no more than a temporary correction at a time when other emerging economies are experiencing similar challenges.

Needle in a haystack

When you take away foreign direct investment into greenfield or existing businesses, the amount going into mergers and acquisitions (M&As) is actually quite modest. David feels that this is not due to any lack of interest: "We see an abundance of foreign capital lining up, but investors are frustrated by a difficult legal and regulatory environment, and opaque company ownership data that makes it hard to identify targets."

"A degree of nationalistic sentiment has crept into policy making, with regulations heavily skewed in favor of local businesses. Many laws are unclear or apparently conflicting, and reform of the judicial system is long overdue, making it hard for foreign owners to enforce contracts and agreements in Indonesian courts. Institutional corruption is also endemic, although this is being tackled by the government's Corruption Eradication Commission."

Business owners are further restricted by an undeveloped insolvency framework and uncompetitive labor laws that reduce flexibility in hiring and firing. But, as David points out, arguably the biggest challenge is locating a suitable target: "It's a bit like finding a needle in a haystack. Market information is poor, with no obvious facility for searching for private companies, not all of whom will have even filed their details. Many companies exist within large, diversified, family-owned groups that share functions and resources, so it's almost impossible to know where one ends and another begins. Corporate websites — where they exist — are thin on information, and nominees are commonly used in shareholding structures, hiding the identities of the real owners."

David East is Head of Transactions & Restructuring at KPMG Siddharta Advisory in Indonesia.

When an owner does decide to sell, the deal process can be frustrating, as the vendor is often a reclusive patriarch with limited or no prior transaction experience. A high proportion of deals abort during the cycle, due to overcooked pricing (Indonesia is still a seller's market), transaction structuring complications and deficiencies in due diligence.

Despite these obstacles, David feels there is cause for optimism: "Subsidiaries of these family groups are coming onto the market, and many have been performing well despite limited management attention, leaving plenty of room for new owners to add value. My biggest tip is to be patient. Indonesia is a very large country, so building up relationships with intermediaries and advisors inevitably takes time. Those that persevere will find that it is well worth the wait."

Reading between the lines

Uncovering the hidden truths about countries' **resilience to change**

In a cautionary tale, a microfinance business was puzzled at its inability to make headway in an African market that appeared to have excellent potential. Management had done its homework, checking out economic and demographic trends and evaluating banking and insurance penetration levels. It had even sized up cellphone ownership and network coverage, given the importance of mobile finance apps. Yet sales had still failed to take off.

A detailed study of the latest Change Readiness Index (CRI) would have revealed that this particular country scores extremely low on 'gender', indicating that women's rights are limited, for a number of social and religious reasons. Females are traditionally a main driver behind microfinance, yet in this case lacked the decision-making power to buy products.

The CRI, launched in 2012 and new country rankings released in 2013, is designed to consider and understand the many risks facing foreign and domestic investors, governments and communities as they strive to create sustainable economic growth. It also gauges countries' resilience to environmental hazards such as earthquakes and floods, civil unrest and wars, famine and financial meltdown. And it evaluates the physical infrastructure, the legal and regulatory framework, and the cultural conditions necessary to improve living standards.

Looking beyond the numbers

Most country analyses and indices tend to focus on issues such as political climate, GDP, imports and exports, key industries and tax regimes. The CRI goes much, much deeper, taking 70 secondary data variables, enhanced by responses to 21 survey questions from country experts, to arrive at three main dimensions that together measure a nation's capacity to manage change: enterprise capability; government capability; and people and civil society capability.

Enterprise capability considers, among many factors, the flexibility of the labor market, diversity of the economy, openness to overseas investment, innovation and R&D base, physical infrastructure, and quality of financial systems. Government capability encompasses state involvement with business, macroeconomic and fiscal policies, regulations and laws, and food and energy security. Finally, people and civil society capability includes the skills and education of the workforce, entrepreneurship culture, health, civil stability, and gender equality.

To ensure that it collects the right data, KPMG seeks advice from a wide range of experts including policy makers, development agencies, private organizations, and world-renowned research group Oxford Economics. The latest index includes 90 countries, the majority of which are high growth markets. The 2015 index will expand to 120 countries.

Although the overall rankings and capability scores are insightful, they are not an end in themselves, but a starting point for more detailed discussions with country and regional specialists, to gain a more intimate understanding of what it is like to do business in these countries.

Spotting the warning signs

A low country ranking on regulation and/or public administration may raise alarm bells, with further investigations uncovering a host of frustrating bureaucratic restrictions that hold back commerce. This may well extend to property ownership, stretching out the time it takes to buy and take ownership of real estate. A poor score for human capital could signify an inadequate education and training system that leaves companies short of skilled workers.

Readers should not view scores in isolation, as the different variables can impact each other. For instance, a sound economic base and good financial systems do not necessarily guarantee stability. Events such as the Arab Spring or the Ukrainian uprising took many investors by surprise, while resource nationalism can occur in emerging nations (such as Argentina) as well as developed ones (like Australia).

CRI findings show that per capita income level and resilience are strongly correlated, due to richer nations having greater financial resources and private sector capacity, more stable and effective governments, better trained workforces and stronger civil societies. Conversely, countries most impacted by conflict and political instability, or with weak governments and civil society, are generally those least capable of withstanding sudden shocks.

However, the index also includes a few surprises. Chile is higher placed than wealthier, more developed nations such as the US, France and South Korea, while the Philippines outperformed Spain, Portugal, Italy and Greece, four countries that suffered particularly from the Eurozone crisis. Of course, these findings do not mean that there is greater economic potential in Chile than in the US, or that Italy and Spain should be avoided at all costs. But the scores should open investors' eyes to opportunities and risks.

Haiti's devastating 2010 earthquake hit a country unable to cope with such a disaster, with limited healthcare and rescue resources, and virtually no funds to rebuild. Chile and Japan, however, both responded impressively to earthquakes.

Sri Lanka's ranking of 47th has been achieved despite only recently emerging from a protracted civil war, proving that, with the right conditions in place, countries can quickly recover from severe shocks. Other governments can learn from these examples, to develop their own ability to manage change. The index findings can also be a spur to overcome critical weaknesses. South Africa may benefit from more relaxed labor laws and greater inclusiveness, while Mongolia could diversify its economic base to avoid becoming over-reliant upon resources. The Democratic Republic of Congo needs a more business-friendly environment, and Sierra Leone should raise its skills base.

Lower income groups also struggle to adapt to changes, especially in societies where inequality is rife, which perpetuates a weak labor market and increases the chance of civil strife. Private companies can play their part in resolving such failings, through targeted social investment in education, infrastructure and healthcare, to ensure that they are funding activities that bring the greatest benefit to local communities, resulting in greater corporate responsibility and citizenship.

To view a copy of the latest **Change Readiness Index**, go to *kpmg.com/changereadiness*

The dimensions of capacity to manage change

CHANGE READINESS			
Enterprise capability	Relates to broad capability of private and state-owned enterprises	**– labor markets** **– economic diversification** **– economic openness** **– innovation and r&d** **– business environment**	**– financial sector** **– infrastructure** **– informal sector** **– trade policy and economic openness**
Government capability	Relates to capability of governmental and public regulatory institutions	**– macroeconomic framework** **– public administration and state/business relations** **– regulation** **– fiscal and budgeting**	**– rule of law** **– government strategic planning and horizon scanning** **– environment** **– food and energy security**
People & civil society capability	Relates to individual, societal and cultural determinants of capability	**– human capital** **– entrepreneurship** **– civil society** **– safety nets** **– technology**	**– gender** **– inclusiveness of growth** **– demographics** **– access to information** **– health**

OFF THE CUFF

With Ben Simpfendorfer

Eastern promise

From Chinese e-retail to Indonesian punk rock, consultant and author Ben Simpfendorfer takes us on an exhilarating ride across the East.

Your latest book *Rise of the New East* is a fascinating guide to doing business across a huge geographical area. What compelled you to write at this time?

Multinational and mid-market companies in more mature markets see enormous opportunities in a region of 50 countries from Beijing to Istanbul containing over half the world's population. But it is also getting vastly more complex to do business in the East, with converging consumer tastes and ever more intense competition from local businesses. Where once the 'Asia strategy' used to mean a couple of offices in Hong Kong and Singapore and a factory in China, it now entails sites in every country and increasingly in second- and third-tier cities as well. That's a lot to cope with, on top of which you have the impact of megatrends such as urbanization and water shortages.

As someone that works extensively across the East, you have often spoken about the need to balance a global versus a local strategy.

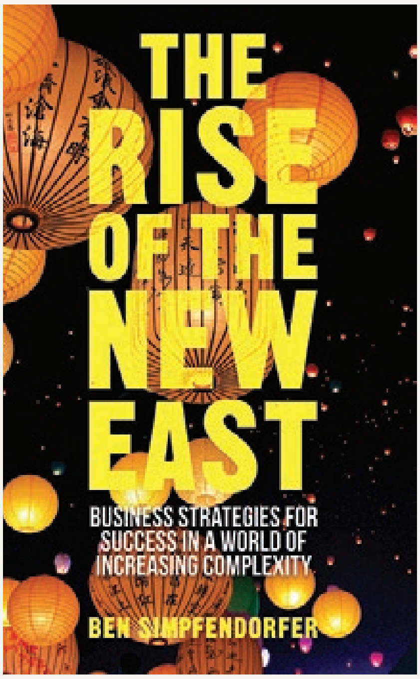
Across the East, there are 270 cities with populations of over 750,000, each with a growing, affluent middle class eager for premium brands. Any company with serious ambitions therefore needs more locations and greater decentralization. With scale, however, comes complexity, and global businesses must relinquish a degree of control to give local management greater freedom, especially as these personnel better understand the tastes and preferences of their compatriots. But are national or regional managers the right people to make wider strategic decisions — such as whether to open new stores in China's Anhui province or on Indonesia's Sumatra? And although demand for established brands remains high, competition from emerging local products is also intensifying. Even a seemingly all-powerful force such as Hollywood has had to adapt its strategy. US films enjoy only a single-digit share of the film market in India, so American studios are linking up with Indian partners to produce movies in Hindi, Tamil and Bengali, featuring local screenwriters and actors. UK retailer Tesco has followed a similar path, entering into a joint venture with China's second-largest retailer Vanguard to accelerate its expansion.

The digital revolution knows no boundaries, and Eastern consumers have shown a voracious appetite for both devices and content. How has this impacted business strategies?

In countries with relatively little history of cars and shopping malls, e-commerce presents a tremendous opportunity to reach tech-savvy consumers across multiple cities. Chinese fashion e-retailer Glamour Sales has rapidly built an entire web business from its Shanghai base, with over half of its sales coming from customers in mid-tier cities purchasing on handhelds from the comfort of their homes. In Indonesia, UK retailer Mothercare has expanded beyond the capital Jakarta by establishing a strong web presence for its brand, without the expense and risks associated with opening up new stores in unfamiliar places. Social media also offers a new way to attract customers. One unconventional example is Indonesian punk rock band Superman is Dead, which has spent the past decade or more acquiring a loyal following via Facebook, Twitter and other sites, enabling it to compete with the major music labels in a way that was previously not possible.

The vast majority of the world's Muslims live in the East. What kind of approaches are proving effective in penetrating this market?

Muslims represent possibly the last great untapped opportunity, although they are of course spread across a vast range of countries. Most of us immediately think of Islamic finance and halal meat, but other products also have considerable potential. Nicorette — which produces aids to quitting smoking — noticed a spike in sales around the religious month of Ramadan, so, consequently, focused much



of its marketing efforts around this period. In another example, McDonald's in Indonesia took to wrapping the company's traditional golden arches by day and then unwrapping them at night to signify the end of the fast. Meanwhile HijUp.com is an up-and-coming online retailer selling fashion items for Muslim women, notably hijabs that cover the head and neck.

Given the size of countries such as China, India, Indonesia, Pakistan and Bangladesh, how do you see environmental megatrends affecting business growth?

Water shortages are arguably the biggest concern in a region that is already short of this vital commodity. As people move in the millions to cities, they instantly consume far more water, and with fast-rising demand from factories and farms, the kind of urbanization seen in 20th-century US, Europe and Japan is simply unsustainable. Technologies for filtering water from rivers should prove invaluable, while organizations that can develop water-efficient supply chains could gain a major cost advantage and reduce the chance of interruptions to production.

With consumers converging, mid-tier cities booming and local competitors growing in strength, what kind of a window exists for companies wishing to invest in the new East?

It is certainly getting pretty crowded, but there is always space for those that can identify specific tastes and tailor appropriate products. Businesses should not underestimate the value of trust associated with established global brands. Recent food scares in China and other nations have caused a surge in demand for well-known names that are believed to be safe and reliable. Sales of organic beef from New Zealand and organic fruit and vegetables from the US are booming in Hong Kong and Singapore, while wealthier Chinese consumers are regularly making the trek to Hong Kong to purchase milk powder and luxury goods, in the belief that these are more likely to be genuine. Ultimately, the one constant in this vast region is the unpredictability. The meteoric change in fortunes of Myanmar, from closed military dictatorship to an attractive base for manufacturing and a growing consumer market, demonstrates the importance of keeping a finger constantly on the corporate pulse of the new East.

In countries with relatively little history of cars and shopping malls, e-commerce presents a tremendous opportunity to reach tech-savy consumers across multiple cities.

Ben Simpfendorfer

Ben Simpfendorfer is Managing Director and Founder of Silk Road Associates, a strategy consultancy based in Hong Kong with offices in Beijing and Melbourne. Ben works with a range of multinationals and mid-sized firms on their expansion strategies in China, Southeast Asia and the Middle East. Ben was the former chief China Economist for RBS and senior China Economist for JPMorgan where he advised some of the world's largest financial institutions and multinationals. His forthcoming book, *The Rise of the New East*, looks at managing growth and complexities in the Asia market and will be published by Palgrave Macmillan in mid-2014. His previous book, *The New Silk Road*, examined commercial ties between China and the Middle East. Ben speaks Arabic, Cantonese and Mandarin. He has lived in Hong Kong for over a decade, but started his career in the Middle East, living in Beirut and Damascus. He writes a regular column for FT.com's *beyondbrics* and features regularly on the BBC World Service's *Business Matters*. Ben also partners with New York-based Global Strategic Associates and Dubai-based RHT Partners to identify cross-border investment opportunities between Asia and the Middle East.

BACKSTORIES

Global bites

TRAVEL ADVISORY

Chennai, India

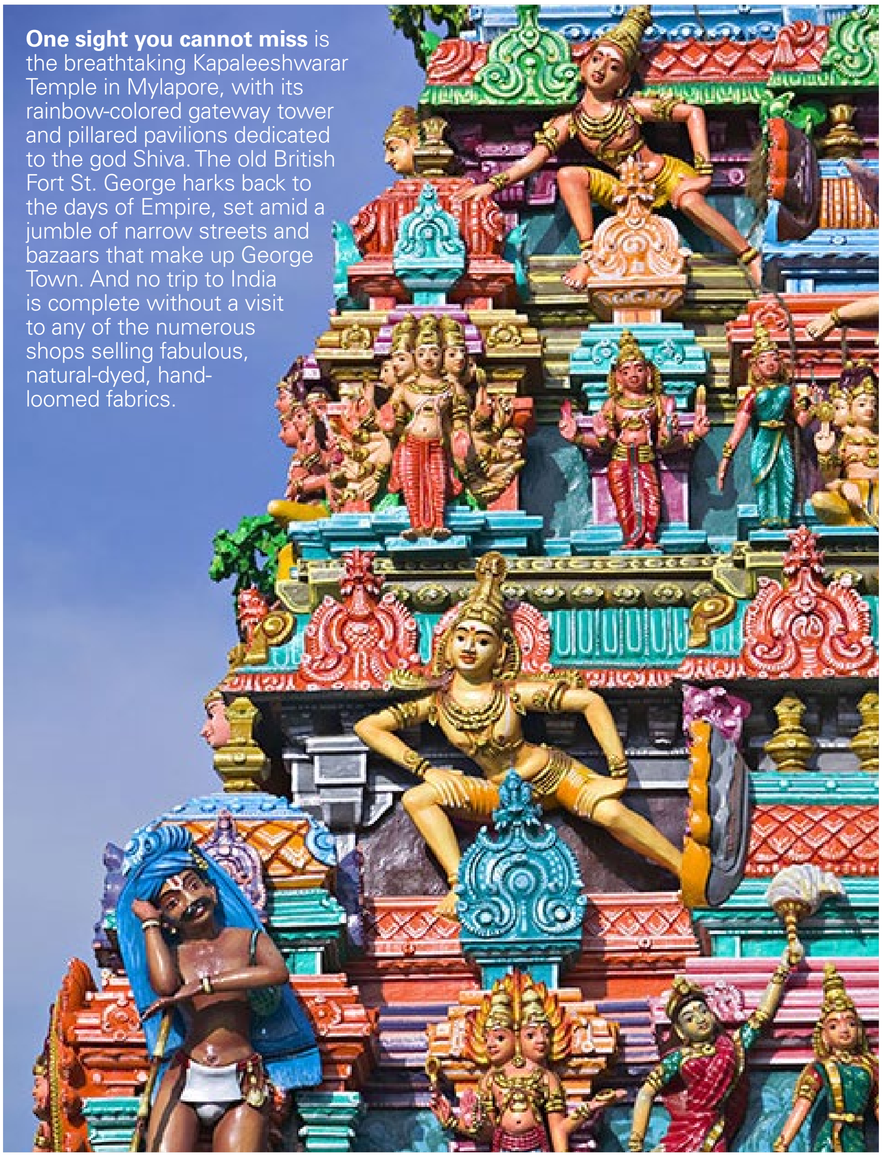
The 'capital of the south' has a distinct Tamil culture unlike any other Indian city

Still commonly referred to by its former British name, Madras, Chennai is India's sixth largest city, with a population of over 4.5 million. It is the capital of Tamilnadu, the keeper of South Indian artistic and religious traditions, and the center of the Tamil movie industry.

A major transportation hub and one of the country's major ports, Chennai's economic boom has been based on thriving automotive, software services, medical tourism, hardware manufacturing and financial services sectors. As the home of the Madras Stock Exchange, the city is India's second biggest financial base after Mumbai.

Hot, congested and noisy, Chennai boasts fine examples of Raj architecture, Christian pilgrimage sites and a flourishing arts scene reflected in highly distinctive dance, sculpture and clothing. Recent years have added a new layer of cosmopolitan glamour in the shape of luxury hotels, shiny boutiques and contemporary restaurants.

Like many fast-growing metropolises, the city's infrastructure has struggled to keep pace with rapid growth, but ambitious new projects such as the soon-to-be-completed metro should see Chennai striding confidently into the future.



One sight you cannot miss is the breathtaking Kapaleeshwarar Temple in Mylapore, with its rainbow-colored gateway tower and pillared pavilions dedicated to the god Shiva. The old British Fort St. George harks back to the days of Empire, set amid a jumble of narrow streets and bazaars that make up George Town. And no trip to India is complete without a visit to any of the numerous shops selling fabulous, natural-dyed, hand-loomed fabrics.

BUSINESS ETIQUETTE

INDIA HAS MORE SOCIAL RULES than most countries, so be sure to prime up before your visit. First meetings are invariably formal, with a strict observation of seniority. The pace of negotiations or discussions can be slow, and high-pressure tactics should be avoided. Due to the heat, suits are rare, while women are advised to stick to long dresses or trousers.

MOBILE

INDIAN CITIES have extensive mobile coverage, with Wi-Fi available in most hotels as well as a host of restaurants and cafés. With some of the world's cheapest cellphone rates, you could even buy a local SIM card.

CLIMATE

CHENNAI'S TROPICAL CLIMATE is characterized by intense humidity throughout the year. There are three major seasons — winter, monsoons and summer — with the hottest months coming between April and June, where temperatures can average as much as 40 degrees celcius. The north-east monsoon brings the heaviest rainfall from October through to December, so winter is the best time to visit, with pleasant sunshine, balmy evenings and moderate rainfall.

MONEY

TRAVELERS CAN GET around 60 Indian rupees (INR) to the US dollar (US$). Although ATMs are everywhere, maximum withdrawal limits can be low. Credit cards are accepted in all major hotels, shops and restaurants, but keep plenty of cash for those must-have purchases from markets, smaller shops and stalls.

GETTING AROUND

CONGESTION REMAINS CHRONIC and has been exacerbated by construction work on the new metro. When ordering a taxi, make sure you request an air-conditioned vehicle and call shortly before your trip to confirm, as service can sometimes be unreliable. A taxi from the airport to the city center costs approximately INR450 (US$8) and takes around 25–30 minutes.

FURTHER INFO

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Designed by Evalueserve.
Publication name: High growth markets: Unleashing Africa's potential
Publication number: 131548; Publication date: September 2014

IN OUR NEXT ISSUE

ASEAN is open for business

Covering a land area of 4.46 million km, ASEAN hosts almost 9 percent of the world's population with a combined nominal GDP of more than US$2.3 trillion. Our next issue examines the global importance of this region and where the most lucrative opportunities exist.