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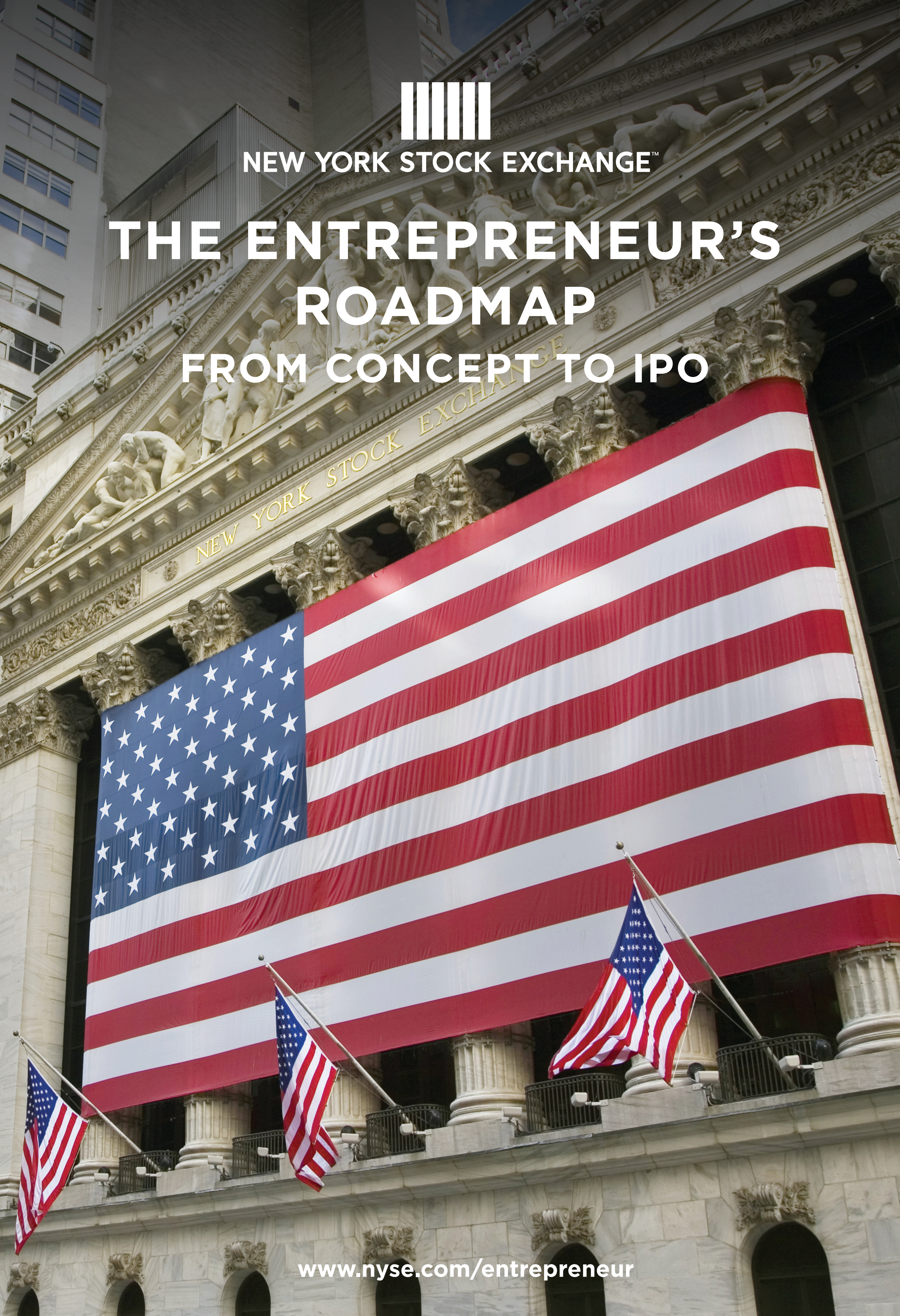

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GOING GLOBAL IN HIGH GROWTH MARKETS

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Businesses, including startups, are always looking for opportunities to grow. In many cases, that means expanding abroad. If your firm is considering this international option, you have some choices. Some firms may prefer establishing operations in one of the developed foreign countries (e.g., France, Germany, Ireland, Italy, Japan, the Nordic countries, United Kingdom, and Spain). These countries typically have stable governments, well-developed infrastructures, and an established business culture. Or they can look to one of the many developing countries located in Africa, Asia, South and Central America, and parts of Europe with rapidly growing economies and potential high growth markets (HGMs). This article focuses on business opportunities in these HGM countries, the challenges you may encounter, and some examples of companies that have faced and overcome these challenges.

$600 BILLION IN INVESTMENTS

A recent KPMG LLP survey of 200 senior executives in the United States found that 86 percent view developing overseas HGMs as important to their company's strategy and growth. In fact, U.S. businesses invest over $600 billion annually in these markets. Yet more than half of this amount goes to just five countries: Mexico, Brazil, Chile, India, and South Korea. That's because, despite their enormous potential, U.S. companies consider many of these developing countries to be too risky, too unstable, and/or too corrupt. So they are skittish about investing in them.

We believe that this perception can get in the way of real opportunity. Unquestionably, many developing countries present challenges for multinational companies (MNCs) and startups alike. But there are ways to minimize these risks. This article takes a look at several developing HGM countries that the KPMG survey identified as having particular promise. {For more detailed information about these and other promising overseas markets that have been overlooked by U.S. companies, read KPMG's white paper, *Don't miss out: Recognizing opportunity in high growth markets.)*

CHINA

China is trying to shift from a high-growth, manufacturing-based economy to one powered by consumer spending. That means MNCs should focus on what the government needs to meet domestic demand: quality and affordable healthcare and housing, improved transportation, and environmental cleanup. Many U.S. technology startups have the know-how to help China achieve its ambitious goals, but they face significant competition from Chinese domestic companies, which have been quick to embrace e-commerce and are increasingly globalizing. Currently, partnering with domestic companies may be the only way in, depending on the industry, but the results can be very lucrative.

Case in point: While Ford Motor Company isn't a startup, its success in the highly restricted automotive industry provides a blueprint on how both large and mid-market companies can succeed.

The Chinese government requires foreign automakers to operate through 50-50 joint ventures with domestic partners. Large, state-controlled companies typically provide the labor and government connections for the joint ventures, while MNCs provide most of the designs, engineering, and marketing. Ford entered a 50-50 joint venture in 2001 with China's largest domestic automaker. Between 2003 and the first quarter of 2015, Ford increased market share among both domestic and joint venture automakers by more than 563 percent, and it continues to grow.

INDIA

India offers extremes of opportunity and challenge. On one hand, it's the fastest-growing major economy, with strong forex reserves, a rising middle class, and a young, educated English-speaking workforce. On the other hand, India ranks low for ease of doing business because of its bureaucratic regulatory environment.

However, over the past few years, a new pro-business government has taken steps to transform the business landscape, including increasing transparency, liberalizing industry sectors, and launching manufacturing initiatives. All of this has helped make India the # 1 U.S. foreign direct investment destination in the world.

Still, before a business makes a direct investment in India, it should understand ground-level impediments—such as red tape, lack of infrastructure, and changing tax and regulatory rules—and formulate a long-term strategy for dealing with them.

Case in point: One foreign online retail company recognized that it would need to radically revise its strategy to accommodate the wild-west chaos of India. Management realized that its methodical and precise playbook wouldn't work in a country with inadequate infrastructure, opaque rules, and a primitive retailing structure.

Leadership understood that it didn't need computer scientists as much as personnel who weren't afraid to take risks. So they built smaller warehouses near customers, established informal drop-off locations, navigated clogged motorways with motorcycles, and perfected backpacks for delivery personnel. They also figured out how to deliver packages to addresses that were only vaguely defined. These improvisations allowed the company to succeed in the growing online retail market.

INDONESIA

This historically protectionist country recently removed 45 business lines from the Negative Investment List and began allowing foreign companies to operate in those areas without restriction. Indonesia also launched a massive infrastructure program to speed up commerce among the country's 13,500 islands. While Indonesia can be one of the most rewarding and profitable countries in which to operate in Southeast Asia, there still can be regulatory hurdles that need to be overcome and a risk that local businesses could demand the government reinstate some restrictions.

Case in point: A North American manufacturer of infrastructure had a significant business relationship with a large U.S. natural resources company located in Indonesia. But because of Indonesian regulations, the manufacturer needed to have its product manufactured in Indonesia (rather than in North America). This requirement could have been a roadblock to the manufacturer's ability to do business in Indonesia. But by working with its U.S. customer and drawing on the many business relationships that the customer had developed during its years of operating in Indonesia, the North American manufacturer was able to quickly identify and secure a local partner. As result, it was able to begin manufacturing product in Indonesia, meeting the regulatory requirements, satisfying the needs of its customer, and keeping the government happy by generating local job and tax revenues.

The lesson here is that you sometimes need to think outside the box, and work with people or companies that have already developed contacts in the developing country to comply with government requirements.

NIGERIA

Nigeria has the largest economy in Africa and is the key driver of international trade in West Africa. In 2014–2015, it was the third fastest growing economy in the world. But with oil representing 70 percent of government revenue and 90 percent of export revenue, the fall in crude oil prices resulted in the projected growth rate dropping to 2.3 percent in 2016, the lowest rate in 15 years.[6] Still, the government is committed to going ahead with plans to increase capital spending by 30 percent this year to build up its infrastructure. It's also cracking down on corruption and moving ahead with plans to make the country less dependent on oil. Foreign companies planning on investing in Nigeria stand to benefit from these moves.

Case in point: In 2014, the Coca-Cola Company faced sluggish sales due, in part, to concerns that its sugary drinks were contributing to obesity and diabetes. It felt the need to expand beyond its core soda bands. At the same time, Coke was increasingly targeting Africa for growth, announcing that it would invest $17 billion between 2010 and 2020 and singled out Nigeria as a country with great growth potential. Despite a history of political and government instability, Nigeria is one of the most culturally diverse societies in the world. So in 2016, Coke bought a 40 percent stake in Nigeria's largest juice maker, Chi Ltd., which also sells evaporated milk, drinkable yogurt, and snacks. (It plans to buy the remaining 60 percent within three years.) Coke is now well positioned for a post-oil-boom market. And partnering with Chi Ltd. also means that Coke can broaden its portfolio and introduce new products to market. By doing its due diligence and weighing the pros and cons of investing in Nigeria, Coke found that risks of political and government instability were outweighed by the potential rewards.

SAUDI ARABIA

The fall in oil prices has forced Saudi Arabia to confront two big issues: the country's over-dependence on oil and its massive public spending. The government is encouraging foreign investment in nearly all economic sectors, with priority given to transportation, education, health, information and communications technology, life sciences, and energy.[7] Still, the kingdom's fundamentalist Islamic culture and Sharia-based judicial system present obstacles to even modest reforms. On the other hand, the country has an ample local talent pipeline that foreign companies can train and employ to staff their operations.

Case in point: Honeywell has been delivering technology solutions to Saudi Arabian industries and consumers since the 1970s. One challenge has been recruiting workers with the necessary advanced technical skills to staff its systems, electrical, computer, and chemical engineering areas. This is due, in part, to Saudi restrictions on the number of "foreign" workers a company can employ. The other factor is the lack of properly trained Saudi workers. Only about 20 percent of college graduates major in technical and scientific fields; the vast majority major in humanities and social sciences.[8] In 2009, Honeywell began offering enhanced technical support, regional training services, and research and development collaboration with Saudi universities. As a result, by the end of 2015, Honeywell was able to employ more than 600 Saudi workers. And it's continuing to recruit and develop Saudi talent in engineering and technical roles. Honeywell found that the investment in education for the native Saudi workforce has paid off in multiple ways. It's allowed Honeywell to (1) meet the government's employment restrictions, (2) acquire qualified and loyal talent, and (3) engender good will with the government.

SOUTH AFRICA

South Africa has plenty of challenges: political uncertainty, electricity shortages, skills gaps, labor unrest, and economic and social disparities. Yet the county also provides lucrative opportunities for foreign companies. Despite the global commodity price crunch, the country still has a wealth of natural resources. And the struggling economy makes the government more receptive to granting favorable investment conditions to foreign companies. Still, South Africa has a host of complex laws and regulatory measures that must be accounted for.

Case in point: In 2011, Walmart acquired Massmart, one of the largest wholesalers and retailers on the African continent. The acquisition needed to be approved by South Africa's antitrust authorities, which Walmart anticipated. But it didn't anticipate the onerous tax compliance requirements that impacted the non-South African workers it brought into the country on a temporary basis to help manage the transition. Under South Africa's tax rules, temporary workers who spent even a few days in the country were required to file complete tax returns. But with the help of KPMG's High Growth Markets practice, Walmart was able to arrange things so that only a dozen or so employees out of the hundreds of assignees each year were required to file full South African tax returns. According to Walmart, these efforts, while costly, were important and necessary ones. As the Walmart example illustrates, there are times it makes sense to bring in a third party to help advise you on how to comply with complex tax and regulatory requirements in the most cost-effective and time-efficient manner.

VIETNAM

With Vietnam's participation in recent trade agreements, the country is tilting decisively toward the United States. Vietnam is eager to welcome U.S. investors, but companies have been slow to take advantage of the opportunities. As China's economy slows and labor becomes more expensive, Vietnam is becoming the go-to place for manufacturing, particularly in textiles and electronics. However, there's a need to educate and develop skills among its labor force, particularly skills for modern industry and innovation.[9] This can be a challenge to potential U.S investors that are considering opening operations in Vietnam.

Case in point: Intel, headquartered in Santa Clara, California, was one of the first high-tech companies to build a factory in Vietnam. Intel understood from the outset that it needed to help develop a workforce with appropriate technology skills. To date, it has invested over $22 million for education, notably in the Higher-Engineering Education Alliance Program (HEEAP), the first-ever public-private partnership in education and in the Intel Vietnam Study Abroad Program. As with Honeywell in Saudi Arabia, Intel found that the investment in education and training of the native workforce has resulted in multiple benefits. It's helped Vietnamese students achieve higher education degrees and employment opportunities. What's more, in 2014, Intel announced the first ever "made-in-Vietnam" central processing unit (CPU), and the company is on track to produce 80 percent of its CPUs for the world market in Vietnam.

12 TIPS FOR INVESTMENT SUCCESS

Before a company makes an investment in a potentially high growth market, there are a number of factors to consider and steps to take that can increase the likelihood of success.

The following are 12 guidelines for spotting—and overcoming—challenges that companies may encounter along the way. Keep in mind that these guidelines apply regardless of whether the HGM is a developed or developing country. However, they are particularly critical with respect to expanding into developing countries.

See the local country through HGM eyes: The lack of cultural understanding is a top reason for failure in HGMs. This is especially relevant now as executives are looking to a broader range of emerging and frontier markets than ever before. Consider establishing a long-term local community presence and have local talent help guide important initiatives.

Blend local and U.S. leadership: Ensure that you have strong local HGM leaders. Also, leverage local managers and market experience while still maintaining U.S. leadership. Develop strong communication between local country employees and host countries, and develop strong mentor-mentee relationships. Train local talent in core business operations so they can take higher positions as soon as possible.

Be patient: Take a long-term view when considering the profitability of your investment. This includes taking the time to understand potential partners and the overall business environment.

Build a flexible business model: Make sure your business model can respond quickly to emerging competitive threats and the unique needs of individual HGMs. Observe how local HGM companies adapt to changes so you'll know how to react appropriately when the time comes.

Develop a strong employee retention program: Provide competitive compensation and benefits, opportunities for advancement, training, and programs that create optimism and a desire to stay at the company. This applies both to workers native to the HGM as well as to "foreign" workers you need to bring in. If available, hire employees who are already comfortable working in a U.S. company and pay them a premium.

Raise capital for the long term: Assemble enough capital to support your long-term view. Adequate capital can also help you develop an adaptable business model as well as attract and retain the right talent.

Understand the business environment: Audit the business environment prior to risking technology and capital. Make sure that management and the board have the proper experience to provide international oversight.

Retain a local trusted adviser: A local trusted adviser can offer invaluable knowledge on a variety of issues. This includes regulatory and tax advice as well as help in dealing with local government officials. Work closely with your adviser to develop a thorough understanding of the political, cultural, legal, and business environments.

Learn how to deal with government: It's essential to learn and understand what a specific HGM government needs. Build relationships through the help of a local adviser. Retain local or market experts to help manage the different government relationships and the bureaucracy.

Establish a robust anticorruption policy: Maintain a non-negotiable set of global ethical standards and provide compliance training throughout all levels of your organization. Partner with a local adviser who has longtime operations in the HGM and who shares your company's values. Clearly communicate to local operations that there is to be no compromise on these rules, and reinforce this message with periodic follow ups.

Spend time observing foreign operations: Take the time to visit foreign operations. Experience the culture, meet the people, study the operations, and understand what management is struggling with. This can provide you and your executives with invaluable insight into your HGM operations and what you need to do.

Establish an exit strategy up front: Develop an exit strategy to leave a country if a certain level of net profits is not achieved by a certain time. It is sometimes more difficult to exit a country once you've "broken ground" than it is to establish operations there in the first place. Companies must be clear eyed about market entry or foreign acquisitions and know when and how to walk away.

CONCLUSION

Expanding your business into high-growth markets has its risks but also can hold great potential for growth and profit. What's more, as we've explored in this section, there are great opportunities for success in some lesser known and less developed countries considered to be HGMs. While some of these countries may, at first glance, appear too risky, too unstable, and/or too corrupt, there are steps you can take that minimize these potential hazards. We've included examples illustrating challenges that multinational firms have encountered while expanding into HGMs, and how they've successfully addressed these issues.

Granted, the companies in our examples are international giants. However, the challenges they face typically are the same or similar to the ones that large and mid-market entrepreneurial firms would encounter. So before you expand into a HGM, consider partnering with one of the established companies with experience in that space, or at least consult with them to get a better idea of what to expect. Doing so can greatly increase your chances of success in both the short and long term.

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Mark Barnes leads KPMG's initiative focused on International Corridors and High Growth Markets (HGM). He has many years of experience working across a diverse range of sectors with companies investing to and from growth markets such as China, India, Korea, Brazil, Russia, and ASEAN. The HGM practice is made up of dedicated teams helping FORTUNE 1000 enterprises better understand opportunities in rapidly developing markets and work across Global Corridors in areas that include market entry or expansion strategy, buying and selling businesses, risk frameworks, protecting intellectual property, Tax, and regulatory to name just a few.

During Mark's tenure, the High Growth Markets practice has grown significantly to provide a broad range of practical services helping businesses achieve their growth ambitions across the investment lifecycle, from initial strategy and market entry to expansion or consolidation.

Mark is a frequent public speaker, contributor to news publications, and regularly hosts webcasts on topics such as cross border investments; updates on business and regulatory climate in growth markets, risk, and regulatory framework models; and managing culture.

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