integrAsian
How Asia’s economic ties are changing the business landscape
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At first glance, Asia may seem perfect for itself. It is the factory floor of the world, producing nearly half of the world’s manufactured goods. End markets are increasingly no longer half a world away. By 2030, Asia will be home to 66% of the global middle-class population and 59% of middle-class consumption, compared to 28% and 23%, respectively in 2009, according to the OECD. Some of these new middle-class consumers may want, perhaps, a new car. Conveniently, motor vehicles produced in Asia as a share of global production has doubled in the past decade from 21% to 42% in 2014, figures from the International Organization of Motor Vehicle Manufacturers show.

However, statistics such as these do not always provide a clear view of conditions on the ground. There are realities that make economic integration in Asia challenging. Despite some progress at the sub-regional level with initiatives such as the Association of South-east Asian Nations (ASEAN), broader multilateral trade and investment arrangements have faced obstacles such as nationalism and disparate regulatory standards. As growth slows in China but picks up elsewhere in the region, the question remains how can Asia unlock additional value through regional economic integration?

This Economist Intelligence Unit (EIU) study, sponsored by ANZ Banking Group, looks at how trade and investment ties between Asian economies are evolving, and the opportunities as well as risks this process is creating for the private sector. This report is based on a survey of senior executives at 525 companies in Australia, China, Hong Kong, India, Indonesia, Singapore and Taiwan, as well as interviews with business leaders and experts. It also examines how growing integration affects the business strategies of firms in the region through profiles of companies in three industries: information technology, consumer electronics and energy.
Respondents, by function (%)

- CEO/President/Managing Director
- Head of department
- Head of business unit
- SVP/VP/Director
- Other C-level executive
- CIO/Technology Director
- Board member
- CFO/Treasurer/Comptroller
- CMO

Respondents, by annual revenues (%)

- Less than $50m
- $50m to less than $1bn
- $1bn to less than $5bn
- $50m to less than $150m
- $150m to less than $500m
- $5bn to less than $10bn
- More than $10bn
The key findings of this study include:

- **New trade and investment corridors** between markets such as North Asia and South-east Asia, and China and India are likely to strengthen. Many manufacturers will shift production from China to lower cost markets in South-east Asia and India. Services companies will focus on regional expansion efforts in South-east Asia.

- In the next decade, Myanmar, Vietnam and Thailand will become top intra-Asian investment destinations. Myanmar registered the strongest interest, with 42% of respondents saying in the next five to ten years they will open a new factory or office in the country.

- China will become an even more important link for regional trade and investment in Asia. Despite slowing growth, China is a vital part of Asia’s economic activity, through policy and diplomacy-driven initiatives and increased international use of the renminbi as a trade and fundraising currency.

- Many Chinese companies are taking an Asia-wide approach to their sales strategies, another sign of the country’s increasingly regional role. However, many of Asia’s corporate chiefs will struggle to follow suit. The region’s varied consumer preferences, regulatory structures and development gaps will continue to make a one-size-fits-all approach challenging.

The EIU would like to thank all those who participated in the survey for their time and insights and to the following people, who contributed their expert views through in-depth interviews:

- Ajoy Misra, chief executive and managing director, Tata Global Beverages
- Awie Wang, founder and marketing director, BNV
- Brian Tang, managing director, Asia Capital Markets Institute
- Daniel Weinberg, senior partner, Optiver
- Geoff Weir, director, Financial Sector Services
- Maarten Wetselaar, executive vice-president, Shell Integrated Gas
- Michael Dean, executive director, Myanmar Investments
- Rick Scurfield, regional president, NetApp
- Yoshiaki Ito, chief executive, Haier Asia
- Zennon Kapron, founder, KapronAsia
Companies in Asia will finance their regional growth plans primarily through bank loans and equity markets rather than bonds, and US dollar- and euro-denominated funding will remain dominant.

Asia’s business leaders are generally optimistic about the resilience of the region’s capital markets and their ability to provide sufficient funding to support ambitions to expand. Many companies are also hopeful that the region’s integration will have a positive effect on capital market transparency.
SHIFTING SANDS

Production will shift from China to South-east Asia. In ten years, Myanmar is seen as a top destination to develop operations.

From efforts to liberalise trade such as the ASEAN Economic Community (AEC) to the emergence of the China-led Asian Infrastructure Investment Bank (AIIB), recent signs point to an increased focus on cooperation and integration among the region’s policymakers. Businesses in Asia, too, have been keen on exploiting opportunities in the region, with intra-Asia trade flows expected to surpass those in Europe as the world’s largest by region next year, according to consultancy McKinsey and the International Monetary Fund.

However, on-the-ground progress with integration remains limited in some respects. Intra-regional trade as a share of Asia’s total trade has barely budged over around 55% in the past decade, according to the Asian Development Bank. Goods or services moving from one Asian market to another must still often contend with varying standards and regulations or cumbersome customs procedures.

Large domestic markets take precedence for China and India

Among many of the region’s firms, a “home bias” remains. The focus on domestic markets seems greatest among firms in the region’s largest – India and China. Eighty-nine percent of firms surveyed in China named it as a target country for expansion over the next five years, making it by far their top pick, while 83% of Indian firms said the same about their home base. Many Chinese and Indian companies continue to see significant growth opportunities at home as consumer preferences develop. “Our focus so far has primarily been on India,” says Ajoy Misra, CEO and managing director at Kolkata-based Tata Global Beverages. “Enhanced water is an emerging segment in India and we think it has huge potential … green tea is another segment that has been seeing rapid growth.”

Regional expansion will benefit China, Indonesia and South Korea in particular

The survey also indicated many firms in Asia plan to extend their regional operations. South Korea is seen as increasingly important, with 54% of firms in China, 49% of companies in Indonesia and 35% of companies in Hong Kong identifying it as a top market for expansion in the next five years. Forty-one percent of companies from the manufacturing sector targeted South Korea, the second-highest choice after China. The trade corridor between China and India will be busy as well: 52% of
firms in India chose China as a top expansion market, while 35% of respondents in China chose India.

A very significant share of manufacturers surveyed (82%) chose China as a top destination for expansion in the next five years. The survey results suggest that, at least in the next five years, manufacturing in China will remain robust despite a well-publicised increase in labour costs throughout the country. In 2014 manufacturing labour costs in Shanghai, Jiangsu province and Guangdong province – important production areas in China – were actually lower than in South Korea, Brazil, Taiwan and Mexico.¹

Perhaps encouraged by the emergence of the AEC, scheduled to formally come into being by the end of 2015, intra-ASEAN trade and investment is poised to grow. Just under half of the companies in Singapore (48%) identified Indonesia as a top market for expansion in five years, and 39% of Indonesian firms said the same about Malaysia.

“I’m very keen on (the AEC) because I have factories in Vietnam, Thailand and Indonesia,” says Yoshiaki Ito, chief executive of the Asia operation of Chinese home appliance maker Haier Group. “If I can utilise the tax benefits to move products within this territory, that definitely helps me because I have a very ambitious goal to double the size of business in ASEAN countries in the next five years.”

Regional expansion will be driven primarily by emerging-market enterprises. Firms in China and Indonesia have the most capital-intensive expansion plans, with 60% or more of respondents planning to invest in new infrastructure over the next five years. Companies in China, India and Indonesia are the most likely to be hiring, with at least 50% of respondents in these countries saying they will add to their existing labour force.

¹ For further research on this topic, see Still making it: An analysis of manufacturing labour costs in China, Economist Intelligence Unit, December 2014.
Case study: Haier Asia looks to expand in China’s backyard

Chinese consumer electronics and home appliances maker Haier Group is aiming to expand deeply into Asia, but will do so without adopting a region-wide strategy. The company will take a nuanced approach to each market it targets because of the region’s wide range of consumer preferences and business environments.

Haier, which had annual revenues of 201bn renminbi last year (US$32bn), has spent a lot of time digesting its 2012 acquisition of Sanyo Electric’s white goods business from Japanese electronics giant Panasonic. With that process nearly complete, it is embarking on a major sales push, aiming to double its ASEAN business in the next five years, according to Yoshiaki Ito, chief executive of Haier Asia.

Mr Ito, whose areas of responsibility include South-east Asia and Japan, says when it comes to Haier’s business, even markets that are at relatively similar stages of development – Vietnam and Indonesia, for example – are viewed very differently. This is partially a result of inheriting the Sanyo brand, which in Vietnam occupies a leading position and is perceived as relatively high-end and aspirational. Haier continues to use the Sanyo brand in Vietnam, a strategy that has been reinforced by the political tensions between Vietnam and China, which culminated in attacks on Chinese factories in Vietnam last year. “We don’t want to get caught in the political situation at all; we’d rather continue to use the DNA or heritage of the Japanese brand (in Vietnam),” Mr Ito explains.

In Indonesia, however, Haier has found more success with lower-priced, entry-level products, and the company uses an approach that features both Haier and Sanyo names. A similar approach is taken with the Philippines and Malaysia, but not Thailand, where Haier is relatively well-established and uses its own brand almost exclusively. The next few years, however, may see more regional convergence; Haier is introducing the ‘Aqua’ brand to replace Sanyo in most markets. “We will gradually move away from the Sanyo brand because it doesn’t make sense for us to use somebody else’s name and keep paying the royalties,” Mr Ito notes.

Thailand, Indonesia in focus

Mr Ito plans to concentrate sales efforts on markets with significant growth potential. These include Indonesia, which has a large, relatively young population, and Thailand, which Mr Ito says, is poised to become a regional nexus as the ASEAN Economic Community comes into being. “It’s the centre of ASEAN,” he says, referring to Thailand. “All the cross-border trade within the ASEAN countries will be tax free, so location-wise alone it makes sense to make Thailand a high focus country. We also have a factory there.” Due to its high connectivity and social media usage rates, Thailand, along with Japan, is also seen as a potential test bed for new business areas that incorporate elements of electronic content and commerce.
Haier divides the remainder of the region into “moderate” maturity markets such as Vietnam and Japan, which are already in a fairly developed phase, and “growth” areas like the Philippines and Malaysia, where Haier has historically struggled with profitability but sees significant potential.

Emerging priorities for the firm are Laos, Cambodia and Myanmar. While Haier has no formal presence in these countries, its products have already crept over their borders from neighbouring Thailand, and Mr Ito is making contact with officials with the aim of building relationships for the long term.

This sometimes involves Haier stretching beyond its comfort zone. It recently inked a memorandum of understanding with the Ministry of Science and Technology in Laos to jointly develop everything from educational devices to electronic bikes – despite not making electronic bikes currently. In a place where the visibility of its products is limited, Mr Ito sees this as the best way to eventually target the country’s consumers. “I’m not trying to take the regular marketing approach; we don’t have the brand awareness yet,” Mr Ito says. “I’d rather focus on the B2G or B2B (business to government, or business to business) strategy.”

**Currency conundrum**

Manufacturers in South-east Asia often point to tariffs and non-tariff barriers as the biggest obstacles to doing business in the region. Such is not the case with Haier. A more significant challenge currently is Japan’s easy monetary policy, which has helped push the yen to multi-year lows. Many of the products Haier sells in Japan are imported from its South-east Asian factories. “Because we have only one small factory in Japan, the forex impact is just too big,” Mr Ito says. The company has already started to hedge by using multiple currencies and currency futures.

Besides exchange rates, the company also struggles with logistics costs. Regional integration is expected to improve cross-border transport routes but domestic infrastructure needs are also high. Indonesia, with its thousands of islands, represents one of Haier’s biggest logistics hurdles. “Sending a refrigerator from one island to another costs much more than sending the same refrigerator from Thailand to Japan,” Mr Ito says. And in many markets, the shipping and transport industries remain heavily government-influenced or controlled, “making it very difficult to lower prices”.

The company ultimately hopes to become a model of Asian economic integration. Having absorbed Sanyo, Mr Ito is now aiming “to convert what used to be a typical Japanese domestic company into a truly global company, based in Asia, owned by a Chinese company. All our marketing strategies are based on that”.

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Investment in Myanmar will accelerate on a ten-year horizon

Over the longer term, intra-regional investment will shift sharply away from China. Seven-in-ten respondents (71%) say they are planning on adding factories and/or offices in China in five years, while only 22% say the same of Myanmar, which has seen foreign investment rise since a series of reforms in 2011-2012 opened up the economy after five decades of isolationist policies. The picture changes on a ten-year horizon. Forty-two percent of respondents say they will open a new factory or office in Myanmar in a decade, while only 23% will be looking at doing the same in China in that timeframe.

“Our investor base is ASEAN, the Middle East and India. Because they’re not that far away, they can see the opportunities,” says Michael Dean, executive director of Yangon-based Myanmar Investments, which helps channel foreign funds into infrastructure and other opportunities in the country.

However, the road to investment in Myanmar is not without its obstacles. Respondents planning on opening a few factory or office in Myanmar were more likely than others to find different consumer preferences and political corruption to be barriers to achieving a consistent sales strategy. “Asian companies are coming in (to Myanmar), they want to invest, but it’s still a bit ‘wild west’,” says Myanmar Investments’ Mr Dean.

What is striking is the focus on the services sector. Almost half the respondents (48%) from both the financial services and professional
services sectors say in ten years they will open offices in Myanmar. Vietnam and Thailand will also see intra-Asian investment pick up within the next decade, also led by the professional services sector. Between five and ten years, interest among Asian companies to open a factory or office in Vietnam and Thailand will rise to 38% and 36% from 30% and 31% respectively.
ALL ROADS LEAD TO (OR FROM) CHINA

The Middle Kingdom will be an increasingly important link for regional companies, and the yuan will be critical for facilitating regional business.

China is a major driver of regional integration, whether through initiatives like the AIIB or its backing of the Regional Comprehensive Economic Partnership (RCEP), a proposed free-trade bloc that would encompass ASEAN and other major Asia-Pacific economies like China, Japan, South Korea, India and Australia. In the business world as well, China is a powerful force promoting closer ties between Asian markets. The survey data indicate that despite placing a high priority on expansion in their substantial domestic market, 41% of Chinese companies say they have a single sales strategy for the entire Asian region. That is significantly higher than the 25% for all respondents.
How do companies in China intend on executing their regional strategies? Liberal policies will help. Nine-in-ten firms in China (89%) believe new free trade or investment agreements would have a very significant or significant impact on generating more cross-border business in the region, versus only 53% of Australian companies. Furthermore, 61% say they would view having a dedicated presence in more Asian markets as a major indicator of success, versus a survey average of 51%.

Renminbi usage will support China’s importance in Asia

One of China’s main contributions to regional economic integration may have less to do with diplomatic or business developments than market forces. The survey shows China’s currency, the renminbi, is gaining ground as a de facto regional trade currency, and that non-Chinese companies in Asia, though still heavily dependent on the US dollar, are increasingly using the renminbi. The US dollar was the top choice of respondents, with 37% saying they would use it to settle 20%-50% of their payments and invoicing over the next five years, while 18% say they would use the renminbi, the second-highest choice.

Increased use of the renminbi is a function of China’s trade importance, says Geoff Weir, a director at consultancy Financial Sector Services, who authored a paper on the currency’s internationalisation for Australia’s Centre for International Finance and Regulation. “Particularly in the aftermath
of the global financial crisis, there’s a desire to see a wider range of safe-haven currencies develop. That requires reasonable confidence in the economy of the issuing country and in the way the economy is run. You need confidence in the currency, you need size and you need a globally connected economy, and China increasingly has all three.”

“We think there’s going to be more internationalisation of the renminbi and a lot more renminbi-denominated products coming through into Hong Kong, so we will definitely increase our participation in renminbi assets,” says Daniel Weinberg, senior partner at Australia-based proprietary trading firm Optiver.

China’s increasing economic and diplomatic heft will help fuel regional integration and the growth opportunities that come with it—but will also create risks. As other Asian economies are increasingly connected to China, they are also more dependent on Chinese demand, and more likely to be buffeted by its problems. The IMF has noted that due to China’s crucial role in the region’s vertical trade integration, “spillover” effects from growth shocks in China are almost twice as large for Asian markets as those outside the region. This makes Asia more vulnerable to any sharp deterioration in economic conditions in China, and means China is likely to lead regional economic cycles -- just as signs emerge that the country’s era of red-hot growth is drawing to a close.

Renminbi regionalisation will slowly spread beyond Greater China

Outside of mainland China, firms in Hong Kong and Taiwan were the main renminbi adopters. Indeed, nearly half of respondents in Taiwan say they expect 20% or more of their invoicing or payments to be conducted in the currency in the next five years. However usage also seems to be picking up outside of Greater China; 15% of Indian respondents anticipate conducting at least 10% of their transactions in renminbi over the next five years. By contrast 84% of Australian respondents expected not to use the renminbi at all.

Asian companies from the construction, financial services and manufacturing sectors will likely continue to drive renminbi use. Thirty-two percent of manufacturers and 19% of both construction and financial services companies expect to use the renminbi for 20%-50% of their payments and invoices in the next five years. The retail and technology sectors were more likely to use the renminbi for 1%-20% of their payments and invoices.
GROWTH STRATEGIES IN ASIA

Asia’s immense diversity will make it challenging for many firms to maintain a consistent sales strategy across the region.

From a business perspective, approaching Asia as a single region or even a group of sub-regions can be challenging because of its sheer size and diversity. Only a quarter of firms surveyed said they adopt a single sales strategy for all of Asia, 34% of respondents say they have strategies for sub-regions and 41% apply country-specific strategies. Sub-regional strategies are the most popular in Singapore, with 54% of companies in the city state using the approach. This likely reflects Singapore’s role as a hub for ASEAN. Three-in-five Indian firms (60%) say they focus mainly on individual markets in Asia rather than the region. Professional services and manufacturing firms were the most likely to adopt a regional marketing approach at 36% and 28%, respectively, versus only 20% of retail firms.

Cross-border business in Asia is heavily exposed to economic cycles

Whether companies in Asia use a regional, sub-regional or market-specific strategy, many are highly dependent on cyclical factors to drive cross-border business. When considering what factors would help them generate more international business in Asia, firms polled clearly placed the most weight on macroeconomic conditions, with 90% saying an improving economic backdrop would have a somewhat significant or very significant impact on their international sales. This suggests that regional integration in Asia could accelerate when economic activity picks up, or conversely, may be negatively affected by a sharp slowdown.

Haier Group’s international expansion has focused more on identifying niche markets in specific geographies, rather than prioritising regions. “Each country has a different structure, different dynamism and different background, even though revenue-wise they might be similar,” says Haier’s Mr Ito.
Case study: Shell Integrated Gas shows the heart of its Asia growth strategy

The integrated gas business – which includes liquid natural gas (LNG) marketing and trading, as well as gas-to-liquids projects – is increasingly important to global energy giant Shell, especially in a low oil price environment. Integrated gas revenues jumped 400% between 2009 and 2013 to US$9bn, representing 60% of total upstream – or oil and gas production – earnings. Asia is at the heart of this lucrative operation. In 2012 the company moved its integrated gas headquarters from Europe to Singapore in response to shifting demand patterns.

Though the firm produces LNG at sites around the world, most of it is consumed in Asia. “Our customers are mostly in this time zone,” says Maarten Wetselaar, executive vice president at Shell Integrated Gas, from his office in Singapore.

While the company sees all of Asia as an opportunity for growth, it has offices in nearly every country in the region mainly because of their different regulatory structures and market dynamics. “If you would compare the degree to which we are able to regionalise our presence in let’s say Western Europe, it would be higher than in Asia because there’s simply more commonality, more market integration than here.”

A rising energy source

While demand from Japan, South Korea and Taiwan has stabilised, worries over pollution and the drive to diversify energy sources is contributing to the appeal of LNG in emerging markets. As in many other industries, China’s demand for LNG is significant, but Shell also sees a lot of latent demand in a cluster of ASEAN countries including Thailand, Vietnam and Indonesia, which was historically an exporter of energy but will have to turn to imports to meet the needs of a swelling middle class.

Shell is also relatively bullish on India’s formerly stagnant energy market. Mr Wetselaar expects concerns on air quality to inevitably lead India to reduce its use of coal and increase its use of other energy sources. In addition, he believes that poor infrastructure in India is contributing to energy demand not being met. The implication is that as the infrastructure is built, energy demand will increase.

Poor energy infrastructure is not only an issue in India, but also in other parts of Asia, and contributes to limited regional integration.

This is despite some two decades of discussions on a planned Trans-ASEAN Gas Pipeline, which would allow gas from production sites in countries like Myanmar, Indonesia and Malaysia to be transported across borders to
consumers throughout South-east Asia. These initiatives “are well articulated and researched, but they hardly get executed”, says Mr Wetselaar. “There’s certainly at the abstract level the political will to do so, but the practicalities of deregulating markets, de-monopolising markets and eventually going to a more regional market-based pricing system, all of those challenges together have still been too big to overcome in the short term.”

**Tariffs not the issue**

Shell welcomes tariff reductions and freer trade in Asia which it sees as broadly positive for business. However, in the energy sector, the full benefits of liberalised trade can only be reaped with the right equipment in place. “Import tariffs might be the next issue, but as always if there’s no physical infrastructure you don’t need to worry about that because you can’t move (product) across borders.”

Tariffs also matter less because in many countries in the region energy prices are heavily controlled by regulators or monopolies. “There are very few countries that have a market-based energy price or gas price. It tends to be regulated by the government, often subsidised. As a result cross regional trade is even discouraged, because people worry that their subsidies are exported,” Mr Wetselaar explains.

However there are factors emerging that are seen driving the adoption of LNG, and perhaps also the removal of some of the bottlenecks in the regional gas trade. With the US poised to start exporting LNG this year, an abundant and cheap new source of energy has appeared in the market.

Infrastructure is also improving slowly in several Asian countries before gas pipelines are completed. Asia has had a serious shortage of the receiving terminals needed to accept exported LNG, adding to the lack of trade links between countries. However China has been on a terminal building spree and “capacity is actually starting to get ahead of the amount imported”. There are plans for new terminals in other markets as well, including Vietnam and India. Technological improvements in areas like offshore floating storage and re-gasification, the process in which liquefied gas is turned back into natural gas, can also give markets access to imported LNG without full-scale LNG terminal development. These developments suggest potential for greater two-way trade in Asia, particularly in the ASEAN area.

Overall, Mr Wetselaar says despite the barriers Shell’s gas business faces, he is optimistic about the prospects for further regional integration – and mindful of the steps taken in that direction thus far.

“A move to regionalise the market, that could carry quite substantial synergies for the region and give another level of security of supply,” he says.
Reductions in tariffs, FTAs can boost intra-regional trade

In addition to macroeconomic factors, tariff reductions are seen as having either a significant or very significant impact on cross-border business by 77% of companies regionally. 85% of companies in the manufacturing sector, which are among the most likely to see taxes or duties applied to products they ship internationally, say lower tariffs would have a significant impact on overseas business in Asia.

“The main obstacle (to business expansion in Asia) is the cost, because many export-import regulations are not yet clear,” says Awie Wang, founder of Indonesian shoe designer BNV, which is concentrating on nearby markets like Malaysia, Singapore and Thailand. “With the ASEAN Economic Community, barriers from export-import related costs will decline significantly.”

Creating a lower-cost and more transparent trading and investment environment with the use of free-trade agreements is also a key driver for companies in Asia. Around three quarters of respondents (77%) cited new free trade and investment agreements as either significant or very significant for international sales. Indeed, the results of India’s efforts to conclude more FTAs “will be tangible since we are a global beverages player,” says Tata Global Beverages’ Mr Misra. “(They) are likely to help facilitate investment proposals and eliminate duties on several key products, thus impacting the business positively.”

Key drivers of cross-border business

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<td>Improving economic conditions</td>
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Having to personalise goods and services for Asian consumers is a challenge

Asia’s growing middle-class populations is a tremendous source of opportunity for many businesses. However, catering to the region’s profound diversity of cultures and levels of development is a formidable undertaking. That Singapore (GDP per capita of US$52,000) is in the same sub-region as Myanmar (GDP per capita of US$1,100) is only one example. “Where parties that come from offshore tend to make the mistake is looking at the region similarly to Europe and the US,” says Optiver’s Mr Weinberg. “What you soon find out is that each jurisdiction has its own … rules, regulations, different tax regimes, different ways that the market structure is set up. That is the burden of trading in Asia, (and) you really have to have people within the business who have expertise in each market.”

Differing stages of development was a commonly cited barrier to achieving a consistent sales strategy across Asia, with 42% of respondents citing it as a very significant factor and 43% as significant. Different consumer preferences were also seen as a big barrier, and as a factor it was cited by 45% of respondents as very significant and 39% as significant. More than half of companies in China (56%), India (53%), Indonesia (69%) and Taiwan (60%) say this is a very significant barrier to maintaining a consistent sales approach.

“Overall the appeal of Asia as an investment destination is still dominated by the growth that the different countries are promising … the integration potential is probably seen as something that promises more for later rather than something that is driving growth at the moment,” says Maarten Wetselaar, Singapore-based executive vice president for Shell Integrated Gas.

### Biggest barriers to business expansion

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<td>Difficulty sourcing talent in some Asian economies</td>
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<td>Poor physical infrastructure in some Asian economies</td>
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<td>Political corruption and instability in Asian economies</td>
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<td>Different legal standards or regulations</td>
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<td>Different consumer preferences</td>
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<td>Differing stages of development among Asian economies</td>
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Case study: NetApp shifts its focus in Asia from countries to customers

When it came to Asia, US-based data management vendor NetApp initially customised its marketing approach for individual countries, especially core markets such as Japan and Australia. However, this is quickly changing, as the use of cloud computer services and big data analysis becomes much more common in the region.

Improving data infrastructure and communications networks have meant that emerging markets in Asia now need—and can support—the kind of data storage capabilities previously only available in developed markets.

“In terms of the broader technology demands of each market, we are now seeing much greater alignment. For example, the value propositions for storage virtualisation and storage efficiency that were a key differentiator for mature markets a few years ago, now resonate extremely well in broader markets across (Asia Pacific),” says Rick Scurfield, regional president for NetApp.

That means that rather than differentiating customers according to country, NetApp is increasingly targeting corporate clients according to their size, regardless of where they are based. When it comes to data management needs, a small enterprise based in Thailand, for example, is likely to have more in common with a small business in Malaysia than a conglomerate in its home market.

“We take an approach that optimises our investments for the different segments of the overall (Asia Pacific) market,” Mr Scurfield says. This has involved an extensive effort to identify large, mid-sized and small to medium-sized businesses, and “to make investment choices based on the consumption patterns of each of these customer groups”.

Throughout the region, NetApp sees large businesses continuing to focus mainly on “on premise” storage, using cloud storage for secondary or backup needs. Mid and small-sized enterprises, meanwhile, are migrating more quickly to cloud-based storage architecture, which is generally more scalable and involves lower maintenance costs.

In March 2015, an Economist Intelligence Unit survey of 525 executives in Asia showed that most companies take a country-by-country approach to sales and marketing in the region. Forty one percent of respondents said they only have sales strategies for individual markets in Asia, 34% said they strategies for sub-regions and 25% said they have a single strategy for all of Asia.
The financial sector and government have driven regional business

NetApp has manufacturing, logistics and customer support centres throughout China, India and South-east Asia, sales offices in virtually every Asian market and a customer base that spans the region, from Indian rural bank cooperatives to Australian business advisory firms. Demand for its storage solutions has grown as more financial and public sector activity has moved online, particularly in South-east Asia.

“The financial services industry is equally important across ASEAN and the public sector is most relevant in Singapore, Indonesia and Thailand. This is because the governments in these markets have an emphasis on e-citizen services, and smart-city solutions around infrastructure and healthcare.”

“Within ASEAN specifically, Singapore is our main focus,” Mr Scurfield adds. “We will continue to focus on Thailand, Indonesia and Malaysia, and emerging areas such as Philippines, Vietnam, Myanmar and Cambodia.”

Going local

The company’s regional expansion hasn’t been without its challenges. As NetApp uses a dollar-based pricing model across most of Asia, the recent strengthening of the US dollar against the currencies of ASEAN, Japan and Australia has affected its bottom line.

“We are seeing significant incremental adoption of NetApp technology from a unit perspective; however, the translation of that success can be muted due to the impact of exchange rates,” Mr Scurfield says.

The company is considering using more local currencies in, for example, Japan, China and potentially India, though it is yet to take concrete steps in this regard.

The company believes regional integration, particularly among South-east Asian countries through the ASEAN Economic Community scheduled to formally come into being by the end of 2015, could translate directly into increased sales. NetApp is staking its business on the view that greater two-way trade between countries in South-east Asia will generate stronger demand for applications to help businesses operate more efficiently.
“The ASEAN region … is expected to contribute significantly to our growth. Trade liberalisation in the region will lead to more investment to promote innovation, economic growth and development,” Mr Scurfield says.

NetApp expects that closer trade and investment ties between countries in South-east Asia will raise issues that have not been fully explored yet and may prove challenging to tackle. For example, virtually unlimited, dispersed, cloud-based storage is difficult to offer consistently across markets where the network infrastructure is vastly different or that adopt disparate data protection standards. In other words, the same cloud-based applications in very large markets may not necessarily work in smaller markets in the same region. In addition, different countries may have different cyber-security requirements, affecting approaches to data management. Mr Scurfield also cautioned that economic integration may progress in unexpected ways that affect intellectual property rights and government procurement policies. These shifts could have an impact on the way NetApp conducts business in Asia.

Though these potential changes due to economic integration in Asia would suggest a country-based business approach may become necessary, NetApp for now is focused on using customer demographics.
Companies in Asia are generally confident about their ability to access liquidity in local capital markets. Yet companies in emerging markets have a much rosier view of Asia’s markets.

To what extent will Asia’s capital markets have a role to play in intra-regional corporate investment plans? A decade ago the answer would have been probably not a large one, as memories of the 1997-1998 Asian financial crisis and its devastating effect on liquidity and private sector activity lingered. However, today, Asia’s economic growth, significant accumulation of foreign exchange reserves and relative political stability have contributed to confidence in the region’s capital markets, which will likely be an important source of funding for corporate Asia.

In South-east Asia, regulators have set a foundation for closer market integration. In equity markets, stock exchanges and regulators in Malaysia, Thailand and Singapore in 2012 launched the ASEAN trading link to offer easy access to each other’s stock markets, and in debt markets common disclosure standards have been implemented that would allow issuers to issue debt securities across various ASEAN markets with a single prospectus. Some analysts believe that the Shanghai-Hong Kong stock connect facility, which allows mainland Chinese investors to buy stocks in Hong Kong and has fueled a surge in Hong Kong-listed Chinese shares, could be replicated in other parts of Asia.

Divergence in perceptions of Asian capital markets

Almost two-thirds of respondents (64%) say they are generally confident about accessing sufficient liquidity through the region’s markets to support their Asian operations. Sixty-three percent of respondents regionally either agreed or strongly agreed that China’s capital markets are generally resilient, just behind Hong Kong (68%) and slightly ahead of Singapore (62%). In addition to the Shanghai-Hong Kong stock connect facility, other efforts by Beijing to improve market access in the past several years, such as the Renminbi Qualified Foreign Institutional Investor scheme, which allows foreign institutions to invest in mainland bonds and stocks, appear to be paying off despite capital restrictions still in place. Nearly a quarter of the respondents (24%) disagreed with the statement that Asia’s capital markets are less efficient than those in Western Europe and the US.

A closer look at the results shows that respondents in emerging markets were much more likely to have stronger confidence in markets in developing economies compared with respondents in developed markets. For example, 46% of respondents in China, India, Indonesia
and Taiwan strongly agreed that capital markets in China are generally resilient compared with 24% of respondents in Australia, Hong Kong and Singapore. There was also a strong divergence in views when it came to India. Almost a third of respondents (30%) in the survey’s emerging markets strongly agreed that India’s capital markets have sufficient levels of liquidity, while only 8% of developed market respondents had the same view.

This difference in perceptions may be rooted in many different factors, including lack of experience among companies in developed economies when it comes to capital markets in developing economies, and lack of access to financial market information. Intra-regional expansion plans of companies in Asia suggest that divergent perceptions of local capital markets will slowly ease as treasurers and finance chiefs explore efficient forms of funding.

**A dependence on bank loans and equity markets for funding**

In the next five years, survey results suggested that companies in Asia will depend on a variety of local currency markets for financing. Bank loans (58%), equity issuance (56%) and internal funding from other parts of the company (52%) were the top three ways that companies would raise capital in local currency markets. Less than half of respondents (45%) were planning on tapping local currency bond markets, despite significant growth in the asset class in the past several years. Taiwanese, Singaporean and Indian firms were most likely to seek local currency funding.

The most popular source of funding is the most traditional. More than two-thirds (70%) say US dollar- and euro-denominated bank loans will be a source funding in the next five years. Indonesian, Chinese, Australian companies are more inclined to obtain funding in dollars or euros instead of local currency markets.

The preference for traditional funding sources is understandable in a relatively easy policy environment, says Brian Tang, managing director at the Hong Kong-based Asia Capital Markets Institute. “If I’m a decent-sized corporate, I can tap my local markets, and my banks are lining up to fund me,” Mr Tang says. However, cross-border corporate bond issuances can be constrained by the credit rating of their respective sovereigns, meaning even that the best companies can’t borrow offshore at a better rate than their governments. “That cost is an impediment for national champions.”

**Accessing funding from more than one market in Asia**

The tendency to seek funding from established connections and close to home is a barrier to the development of a genuinely regional capital market. However many firms do seem to be planning financing on a regional basis, particularly in developing markets. Among companies in Indonesia, 81% agreed they would need to access funding from more than one Asian market to expand their operations; 79% of Indian firms and 70% of Chinese companies held the same view. That compared to just 26%
Sources of US dollar/euro-denominated and local currency denominated financing expected in the next five years

Funding denominated in US dollars and/or euro, (%)

- Bank loans
- Sales of equity stake(s)
- Private placement
- Equity raising
- Funding from head office/other divisions or group companies
- Bond issuance

Funding denominated in local Asian currencies, (%)

- Bank loans
- Equity raising
- Funding from head office/other divisions or group companies
- Sales of equity stake(s)
- Private placement
- Bond issuance
of Australian firms and 42% of Hong Kong firms. Markets where companies are most likely to seek financing regionally are also those where they are generally most confident about being able to access enough funding, and where there optimism surrounding the impact of integration on capital markets is greatest. Four-in-five Indonesian companies (79%) and three-quarters of Indian and Chinese firms agreed regional capital markets would become more transparent as integration progressed, versus just 44% of Australian firms.
CONCLUSION: A MORE INTERCONNECTED FUTURE

Prospects for sub-regional schemes such as the AEC and grander efforts like the US-backed Trans Pacific Partnership (TPP) suggest government-led trade and initiatives will help strengthen economic integration in Asia in the years ahead. That may be the case, but companies in Asia are not waiting around. This study has shown that firms in the region have ambitious expansion plans in the next five years to build new infrastructure, hire more staff and open new offices, primarily in China, India and South Korea.

In the next five to ten years, intra-regional investment flows, particularly from the services sector, will shift to focus on South-east Asia. Myanmar, Thailand and Vietnam will become much more important destinations of direct investment, not just because of their low-cost environments but also their fast-growing, relatively young populations.

China will remain a powerful force shaping business in Asia, and the institutions advancing regionalism may increasingly have more Chinese characteristics. “It already appears that the newly established (AIIB) will dwarf the Asian Development Bank in terms of its potential lending portfolio and is the clearest example yet of China’s outsized and ambitious agenda to create a more cohesive Asia-centric economic bloc,” says Zennon Kapron, founder at financial market research firm KapronAsia.

Increased use of the renminbi as a trade currency and funding source will contribute to this process, though financing plans of companies, which favour bank loans and equity markets, suggest that the US dollar will remain a dominant choice of funding currency in Asia for the foreseeable future.

Regional integration will not be a steady process. The international business strategies of most companies in Asia take a country-by-country approach rather than a regional or even sub-regional one. Asia’s wide range of consumer preferences and levels of economic development will make maintaining a consistent sales strategy challenging, particularly when many industries are pursuing greater customisation and personalisation of goods and services.

Unlike Europe, regional integration in Asia will be entirely economic, driven by trade and investment relationships. That is why private sector plans are so critical to understanding how the process of integration will develop. Despite the challenges of diversity and other thorny issues such as lack of harmony in national trade policies, businesses in the region are intent on pursuing opportunities in their own backyard, expanding beyond their own borders and ensuring that in the years to come Asia is more than the sum of its parts.
For more insights and perspectives about intra-Asian trade and investment ties, go to integrasian.economist.com
APPENDIX: SURVEY RESULTS

1. What is the location of your office or primary place of work?

2. Which of the following best describes your title?

3. Do you have knowledge of and responsibility for sales and marketing strategy?
4. What are your organisation’s annual revenues in US dollars?

<table>
<thead>
<tr>
<th>Revenue Range</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than $50m</td>
<td>10%</td>
</tr>
<tr>
<td>$50m to less than $150m</td>
<td>15%</td>
</tr>
<tr>
<td>$150m to less than $500m</td>
<td>20%</td>
</tr>
<tr>
<td>$500m to less than $1bn</td>
<td>25%</td>
</tr>
<tr>
<td>$1bn to less than $5bn</td>
<td>30%</td>
</tr>
<tr>
<td>$5bn to less than $10bn</td>
<td>35%</td>
</tr>
<tr>
<td>More than $10bn</td>
<td>40%</td>
</tr>
</tbody>
</table>

5. What is your company’s primary industry?

- Aerospace/defense
- Agriculture and agribusiness
- Automotive
- Chemicals
- Construction
- Real estate
- Consumer goods
- Education
- Energy and natural resources
- Entertainment, media and publishing
- Financial services
- Government/public sector
- Healthcare, pharmaceuticals and biotechnology
- IT and technology
- Logistics and distribution
- Manufacturing
- Professional services
- Retail
- Telecoms
- Travel and tourism
- Transport

6. Please select the option that best describes your presence in the following Asian markets:

- China
- India
- Indonesia
- Malaysia
- Myanmar
- South Korea
- Taiwan
- Thailand
- Vietnam
- Other, please specify

- We have an on-the-ground sales team
- We use an offshore sales team
- We have local partners or distributors
- No presence
7. Please select the statement that best describes your company’s primary sales and marketing strategy.

- We only have sales strategies for individual markets in Asia
- We have sales strategies for regions within Asia (e.g., ASEAN)
- We have a single sales strategy for the entire Asia region

8. Thinking of what would generate more cross-border business for your company in Asia, please rate the following factors according to the significance of their impact:

- Improving economic conditions (i.e., higher growth rates, rising employment)
- Harmonisation of regulations and/or product standards affecting my industry
- Easing of regulations that hamper cross-border investment
- Tariff reductions
- New free trade or investment agreements
- More consistent cross-border legal enforcement (e.g., of intellectual property rights)
- Reduced capital controls
- Greater political stability
- New tax incentives
- Infrastructure improvements

9. Please rate the following factors according to their significance as barriers to achieving a consistent sales strategy across Asia:

- Differing stages of development among Asian economies
- Differing cultures, languages and business practices among Asian economies
- Differing consumer preferences among Asian economies
- Differing legal standards or regulations among Asian economies
- Tariff and non-tariff barriers (i.e., varying customs procedures or product standards) between different Asian economies
- Political corruption and instability in Asian economies
- Poor physical infrastructure in some Asian economies
- Lack of distribution networks in some Asian economies
- Difficulty sourcing talent in some Asian economies
10. Please select the top three countries targeted for business expansion over the next five years.

- China
- India
- Indonesia
- Malaysia
- Myanmar
- South Korea
- Taiwan
- Thailand
- Vietnam
- Other, please specify

11. Please indicate your specific plans for the countries that you selected in the previous question.

- Make an investment to build new infrastructure
- Make an investment to improve existing infrastructure
- Add to my existing labour force
- Open dedicated offices in these locations
- Hire a local agent or distributor
- Form a JV or strategic alliance with a local partner
- Conduct market-entry research and due diligence

12. Thinking about currencies your company would use to settle payments and invoice customers and suppliers, how much would your business use the following in the next five years?

- US dollar (USD)
- Euro (EUR)
- Hong Kong dollar (HKD)
- China renminbi (CNY)
- Offshore China renminbi (CNH)
- India rupee (INR)
- Australia dollar (AUD)
- Indonesia rupiah (IDR)
- Singapore dollar (SGD)
13. Please indicate the extent to which you agree or disagree with the following statements about capital markets in developing Asian economies.

14. Please indicate the extent to which you agree or disagree with the following statements about capital markets in developing countries.

15. Please indicate the extent to which you agree or disagree with the following statements about capital markets in developing Asian economies.
16. Please check all the sources of financing that your business is likely to use over the next five years - Denominated in US dollars or euros

- Bank loans
- Equity raising
- Sales of equity stake(s)
- Bond issuance
- Private placement
- Funding from head office/other divisions or group companies

17. Please check all the sources of financing that your business is likely to use over the next five years - Denominated in local Asian Currencies

- Bank loans
- Equity raising
- Sales of equity stake(s)
- Bond issuance
- Private placement
- Funding from head office/other divisions or group companies

18. Thinking of events and issues that may have an impact on your business, please rank the following risks.

- Cyclical slowdown in one or more key markets
- Political instability and/or corruption
- Rising labour or logistics costs
- Increased competition
- Lack of progress in regional trade liberalisation
- Increased scrutiny from regulators and/or policymakers
- Theft of intellectual property
- Varying standards for professional qualifications
- Lack of visibility on demand
- Financial market volatility
### 19. Please select all overseas markets where you expect to establish a new factory or service centre in five years:

<table>
<thead>
<tr>
<th>Market</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>China</td>
<td>80%</td>
</tr>
<tr>
<td>India</td>
<td>60%</td>
</tr>
<tr>
<td>Indonesia</td>
<td>40%</td>
</tr>
<tr>
<td>Malaysia</td>
<td>20%</td>
</tr>
<tr>
<td>Myanmar</td>
<td>20%</td>
</tr>
<tr>
<td>South Korea</td>
<td>20%</td>
</tr>
<tr>
<td>Taiwan</td>
<td>20%</td>
</tr>
<tr>
<td>Thailand</td>
<td>20%</td>
</tr>
<tr>
<td>Vietnam</td>
<td>20%</td>
</tr>
<tr>
<td>Other, please specify</td>
<td>0%</td>
</tr>
</tbody>
</table>

### 20. Please select all overseas markets where you expect to establish a new factory or service centre in ten years:

<table>
<thead>
<tr>
<th>Market</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>China</td>
<td>80%</td>
</tr>
<tr>
<td>India</td>
<td>60%</td>
</tr>
<tr>
<td>Indonesia</td>
<td>40%</td>
</tr>
<tr>
<td>Malaysia</td>
<td>20%</td>
</tr>
<tr>
<td>Myanmar</td>
<td>20%</td>
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<tr>
<td>South Korea</td>
<td>20%</td>
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<tr>
<td>Taiwan</td>
<td>20%</td>
</tr>
<tr>
<td>Thailand</td>
<td>20%</td>
</tr>
<tr>
<td>Vietnam</td>
<td>20%</td>
</tr>
<tr>
<td>Other, please specify</td>
<td>0%</td>
</tr>
</tbody>
</table>

### 21. Which of the following would you consider major indicators of success for your business in Asia over the next five years?

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>A dedicated presence in more Asian markets</td>
<td>80%</td>
</tr>
<tr>
<td>Increasing sales/market share</td>
<td>60%</td>
</tr>
<tr>
<td>Larger/more diverse customer base</td>
<td>40%</td>
</tr>
<tr>
<td>Establishment of more local alliances or partnerships</td>
<td>20%</td>
</tr>
<tr>
<td>Maintaining current presence and market position</td>
<td>20%</td>
</tr>
<tr>
<td>Improved brand or company visibility</td>
<td>20%</td>
</tr>
<tr>
<td>More demonstrated interest in our company from regional investors</td>
<td>0%</td>
</tr>
</tbody>
</table>