



GLOBALSUCCESSADVISORS

Global business and economic trends and impact on EMEA

By Nenad Pacek

President

Global Success Advisors Ltd.

Author of „Emerging Markets: Lessons for business success and outlooks for different markets“

September 2009

Nenad.Pacek@GlobalSuccessAdvisors.eu

Tel. +43 676 64 60 607



GLOBALSUCCESSADVISORS

To understand the future, we must first understand the past and the present

We are currently living through the largest crisis ever during peace time

This crisis is 4 times larger than the Great Depression as a % of global GDP

The big business boom of 2006 and 2007 will be repeated but only when we all die



GLOBALSUCCESSADVISORS

How did the world end up in such a mess?

Crime, corruption, fraud, bad regulations, greed and stupidity temporarily destroyed two big engines of capitalism: trust and confidence

Economics is primitive, like medical science 100 years ago

We had more economic crises in the last 35 years than in the 350 years before that



GLOBALSUCCESSADVISORS

The deadly crisis sequence

1. Unsustainable super-cycle – built on easy money and easy liquidity
2. Build up of global imbalances
3. Unregulated and fraudulent financial institutions – hiding and selling well packaged debt – illusion of healthy balance sheets
4. Buyers of such debt use it as a collateral enabling them to borrow and lend more, but also fraudulently hide and sell debt themselves

Role of credit rating agencies – 12 companies with Triple A rating vs. 64,000 instruments with Triple A rating



GLOBALSUCCESSADVISORS

How was the Depression avoided?

Opposite policy response vs. 1929-1932 when mantra was „no need to do anything, market are self-correcting“

Despite good policies authorities have been too slow to catch up with unprecedented complexity of the crisis

Slowness of policies pushed the world into a crisis of confidence (recessions are very psychological) and the Great Recession



GLOBALSUCCESSADVISORS

The Great Recession coming to an end

Restoring confidence never occurs over night and this time it will take longer than usual -- this is not a typical cyclical recession

This crisis has been cyclical and financial at the same time, and more global than any other in economic history

There is no easy way out of recession – it will be slow, with false starts and volatility



GLOBALSUCCESSADVISORS

History tells us we are probably at the bottom

During past banking-induced crises averages* were:

1. GDP falls for 2 years, down 9%
2. Unemployment goes up for 4 years, increases 7%
3. Equities fall for 2.5 years, decline 35%
4. House prices fall for 6 years, decline 55%
5. Government debt almost doubles in less than 4 years

*research by Rogoff and Reinhart

Copyright GSA Global Success
Advisors GmbH 2009



GLOBALSUCCESSADVISORS

Short and medium-terms risks for recovery

- Fiscal stimulus evaporates without private confidence fully in motion
- Banks still not cleared of toxic debt instruments and bad loans are rising
- Unemployment is still rising in most countries
- Bank recapitalisation delays
- No great clarity yet about desperately needed new financial regulations, little global co-ordination
- Protectionism – visible and hidden
- Past banking-induced crisis were national or regional – massive globality carries uncertainties
- Derivatives market and counterparty risk



GLOBALSUCCESSADVISORS

Why slower post-crisis era?

- Super-cycle peak built on massive leverage cannot be repeated again to the same extent
- Deleveraging process takes a long time
- Banks will need more capital injections, reducing lending – they don't like to lend during slow times anyway
- Squeeze of the „shadow banks“ with new regulations
- Huge restoration of balance sheets needed at government, corporate, private and banking level
- „Living within our means“ decision making – memories of this crisis will not evaporate soon
- Need to reduce public debt in many countries



GLOBALSUCCESSADVISORS

Impact on emerging markets

- Decoupling theory in today's world is largely flawed
- USA, EU and Japan are still 70% of the global GDP (at market exchange rates)
- No sustainable and strong recovery in emerging markets is possible without proper recovery in the developed world
- History tells us that banking-induced crises affect some emerging markets more than the developed world
- I coined this phenomenon „temporary negative decoupling“



GLOBALSUCCESSADVISORS

Impact on emerging markets

- Negative decoupling: If an emerging market has bad fundamentals (like USA), it suffers more than the USA; or if an emerging market has better fundamentals than the USA, it can still suffer as much as USA
- The main reasons for negative decoupling are: perceptions, high dependence on credit, lack of accumulated wealth, IMF dictat, lack of countercyclical policies



GLOBALSUCCESSADVISORS

Sufferers in emerging markets

- Emerging markets that suffer more are those with: high annual debt repayments, high external and public debt, low savings, inadequate reserves relative to obligations, high budget deficit, high current account deficit, low competitiveness
- Large chunks of the CEE region are in this category and their recovery will take time
- This includes Lithuania



GLOBALSUCCESSADVISORS

Emerging markets – tectonic shift

- By 2011/2012 emerging markets will produce half of world's GDP (at purchasing power parity) for the first time in over 150 years
- They consume half of world's oil, buy half of world's exports, hold 70% of global foreign exchange reserves
- Population growth of 6m people every month, vs 300,000 in developed world (mostly US)
- Account for over 80% of world population
- In the post-crisis era, GDP growth will outperform developed world by a 3 to 1 margin



GLOBALSUCCESSADVISORS

Economic world you will inherit

- Massive age of leverage that would fuelled unsustainable growth unlikely to return for decades (unless regulators fail again)
- Economic growth will return but at lower levels
- Growth rates should be more predictable and more sustainable
- Commodity, currency and other speculation will continue but it will be less leveraged – producing fewer and smaller speculative peaks
- Inflation rates should therefore be easier to forecast
- Access to finance for your distributors will be tougher and more expensive



GLOBALSUCCESSADVISORS

Economic world you will inherit (II)

- Over the next 5-10 years, many emerging markets will become less dependent on developed world and will reduce their large debts – sudden growth spikes
- USA's role as an engine of demand will be lower in the years ahead – debt overhang problem. No obvious replacement in the short-term
- China and India cannot be engines of private consumption in the short-term. They together consume less than 20% of USA households.
- Economic power will gradually shift and in the next decades we will live in a multi-polar world. This will require rethinking of business strategies



GLOBALSUCCESSADVISORS

2009 global economic performance

- Globally worst economic performance since World War II
- USA down between 2.5 and 3%
- Western Europe down between 4 and 5%
- Japan down between 6 and 7%
- Emerging Asia up 2 to 3% largely thanks to China and India
- CEE down 6 to 6.5%
- Latin America down 3.5 to 4%
- Sub Sahara down 2 to 2.5%
- MENA up 0.5 to 1.5% but how reliable?



GLOBALSUCCESSADVISORS

2010 global economic performance

- All regions should be in a small plus
- USA and Japan are likely to grow between 1.2 and 1.7%, Western Europe between zero and 1%
- Best performance will be in MENA and Emerging Asia (over 3%)
- CEE will need longer to start proper growth path – in 2010 will grow 1 to 1.5%
- Latin America and Sub Saharan Africa should be around 2 to 2.5% up but final outcome heavily dependent on commodity prices
- Little upside potential but still substantial short-term downside risks (double dip recession risk)



GLOBALSUCCESSADVISORS

Western Europe and its Mediterranean belt

- Deepest recession since World War II
- Less competitive EU countries and those with housing bubbles will take longer to bounce back and their growth will be more subdued
- Many of those are in the Mediterranean belt
- Strong euro, weak lending, weak export markets
- Public debt to zoom to over 80% next year and over 100% of GDP by 2015
- Industrial production is at the same level as in 1997



GLOBALSUCCESSADVISORS

CEE region and its Mediterranean belt

- Worst hit region due to large debts at government, corporate and private level as well as lack of proper stimulus packages
- P, Cz, Slk, Slo and Rus have a stronger bounce back potential
- Most others including those in the Mediterranean belt either need external assistance or new loans to survive – bounce back potential weak and extended as structural reforms and debt reductions take place
- No full recovery possible without proper recovery in Western Europe
- But medium to long-term potential strong



GLOBALSUCCESSADVISORS

MENA region and its Mediterranean belt

- Algeria and Lybia enjoy strong reserves and can mitigate recessionary pressures
- Israel, Egypt, Morocco, Tunisia – stronger growth depends on global recovery, but economic fundamentals are quite good
- Weaker fundamentals in Turkey, Lebanon and Syria although Turkey has a strong bounce back potential and a major strategic importance for business
- In 3-5 years Turkey will be one of the most important emerging markets and its fundamentals will improve allowing it to fulfil stronger growth potential



GLOBALSUCCESSADVISORS

Which companies have a better chance for future success?

- Privately held companies that are not managing quarterly bottom line under stock exchange pressure
- Those with senior management that thinks long-term
- Those that are alert to new competitive trends and adjust internal innovation and product development
- Those that take emerging markets as seriously as they take developed world
- Those with cash reserves
- Those that use this crisis as an opportunity to increase market share



GLOBALSUCCESSADVISORS

Competitive world you will inherit

- Keep in mind how economic powers are shifting
- No big leveraged boom expected
- In a world of less robust growth two big competitive forces shaping up:
 - 1. Multinationals getting more systematic and serious about emerging markets and downward innovation
 - 2. Emerging market multinationals (currently 10% of Fortune 500 companies and rising every year) are more regional and global in their ambitions and keen to move from lower market segments to higher



GLOBALSUCCESSADVISORS

Competitive world you will inherit (II)

- These forces are making international business more competitive and tricky than it has ever been
- Competition can come from unexpected corners and close technology, capital and talent gap – leapfrog also possible
- Emerging market multinationals particularly from Asia are not easy to compete against: different margin objectives, loose compliance, lower prices, often acceptable quality, poaching best staff, copycat product and campaigns
- Companies should keep an eye even on no-names



GLOBALSUCCESSADVISORS

Corporation of the future is a „two headed monster“

- One head focuses on big volume, slower growth developed markets
- Other head focuses on lower volume, higher growth emerging markets
- Separate corporate structure to allow focus, attention and investment on emerging markets



GLOBALSUCCESSADVISORS

Best practice during the crisis

- Once in a life time opportunity to improve market position, weaken competitors and take more control over business
- Companies with cash reserves and senior mgt that think long-term are in the best position to take advantage of the crisis
- In past recessions/slowdowns such companies did things that helped them come out of the crisis stronger than the competition



GLOBALSUCCESSADVISORS

What to do to come out stronger in the post-crisis era?

- Focus on building market share. Change reward systems to that while times are tough.
- Each point gained during the crisis increases long-term profitability
- Cutting back severely during the crisis often means lost market share that might never be regained or it will be very expensive to do so
- Keep promotional spend going as others retreat
- Even closer to customers – they do not forget those who stay close during tough times



GLOBALSUCCESSADVISORS

What to do to come out stronger in the post-crisis era? (II)

- Do not let the crisis move you away from long-term strategy against multinational and local competitors
- Avoid knee-jerk reactions
- Consider acquiring distributors, land and competitors who might be trading at the discount or a privately overleveraged (desperate to sell)
- Be proactive and fast about acquisitions – internal dedicated teams to handle
- Time to gather teams to think out of box – internal creativity more important than ever



GLOBALSUCCESSADVISORS

What to do to come out stronger in the post-crisis era? (III)

- Indiscriminate cost-cutting tends to be counter-productive
- Rather look at accumulated fat which is hidden during good times (look at processes, structures, back-office, weak performers) – trimming really unnecessary fat
- Maintain heavy focus on innovation and product development
- Understand that once consumer goes to „good enough“ products he is hard to move up again
- Support distributors financially if need be and if you can afford it



GLOBALSUCCESSADVISORS

Thank you!

- **Global Success Advisors** is focused on assisting companies outperform competition and succeed in international markets. The company works with senior executives at global and regional level. It helps them make right assumptions about economic developments as well as understand and implement best business practices for international success.
- **Nenad Pacek**, founder and president, is the best selling author of „*Emerging Markets: Lessons for business success and outlook for different markets*“ which is now in its second edition. As a former Vice President of the Economist Group he spent almost two decades in Group’s economic intelligence and business advisory division working as a consultant to regional and global directors of some 300 multinational companies. He chaired more than 100 Government Roundtables with Prime Ministers on all continents. He managed a large business unit globally and several in the EMEA region.