Global Trends

GT BRIEFING: September 2011

It's a Multipolar World: What's Changing?









September 2011: Economic power is shifting to BRIC plus a next tier of rapidly developing economies, due to a combination of increasing financial power, resources, knowledge base, population, and consumer affluence – leading to a multipolar market landscape. Markets are also moving beyond national borders or clear demographic groups – urbanization and the rise of megacities are leading to new forms of "city-states" which can be considered markets in their own right. And "pure" demographic segmentation is giving way to segmentation by communities of choice, which are fluid and often driven by social media. Values and beliefs as well as behaviours are also becoming more diverse – and mobile across borders.

Mutipolarity is asserting itself in more than markets – the world has a huge range of economic systems from centrally driven economies to free markets with many shades in between. Political and geopolitical systems are becoming more diverse, reflecting global economic and power shifts, for example the move from the G8 to the G20 forum. And don't forget competition. Those companies which are among the largest economic entities in the world will shape this multipolar landscape, but may require a broader portfolio of products, services, business models, knowledge and organizations to succeed. They will also be facing new, formidable competitors – new global challengers are emerging, often building on domestic strength in rapidly developing economies.

The bottom line: The world is becoming more diverse and less predictable. To operate in this shifting environment, in multiple systems at the same time, organizations are going to need to be more flexible and agile, managing several business models at the same time. In this briefing we look at some of the dynamics of multipolarity in terms of markets, competition, and economic/political systems. The question is how you and your organization can navigate this world successfully.

Multipolar Markets

As America developed in the 1800s and 1900s, the call was to *"go west, young man"* (attributed variously to John Babsone Soule, Aaron Burr and Horace Greeley). Today they would say keep right on going or, from a European vantage point, head east and south. Economic power is shifting to the rapidly developing economies (RDEs) of BRIC (Brazil, Russia, India and China) plus a next tier of countries whose economic power and market attractiveness is increasing. Already some of these, including Saudi Arabia, South Africa and Turkey are members of the G20. Others may not be part of global governance (yet) but will have a significant impact on the way the economies and markets of the world develop, due to factors including financial power, resources, knowledge base, population size, market attractiveness or some combination thereof. The result will be an increasingly multipolar market landscape in the next ten to twenty years – one that is already starting to develop. Now that the global recession has dispelled the myth of decoupled economies and markets, a key question in this multipolar world will be how these economies work together and independently to create and share value, through international trade and in their domestic markets. And what does this mean for businesses seeking both to create and capture value across a diverse portfolio of markets?

In Action!

The emerging middle class in BRIC and beyond: In 2010 China became the second largest economy in the world, overtaking Japan, with estimates suggesting that by 2025 it may become the largest economy in the world, while India will potentially rank among the top 3 or 4 economies. Also in 2010, Brazil became the fifth largest economy in the world. As BRIC and other rapidly developing economies grow, the wealth of their citizens is also increasing, contributing to the rapid rise of a global middle class in the decades ahead, with enormous potential spending power. Estimates of the size of the middle class vary depending on the income bands used, but in all cases the numbers are in the billions in terms of people and trillions in terms of spending power. A recent OECD study suggests the emerging global middle class is set to grow by some 3 billion people worldwide in the next two decades to number 4.9 billon people. These are people with incomes of between US$10 and US$ 100 per day (2005 PPP) who combined could have spending power of some US$56 billion by 2030 –income to spend on goods and services from consumer electronics and cars to education and health. They represent a significant opportunity to drive economic growth and future revenues for business.

Urban economic power: More than 20 of the world's top 50 cities ranked by GDP will be located in Asia by the year 2025, up from 8 in 2007. More than half of Europe's top 50 cities will drop off the list, as will 3 in North America. In this new landscape of urban economic power, Shanghai and Beijing will outrank Los Angeles and London, while Mumbai and Doha will surpass Munich and Denver. (Source: McKinsey Quarterly) And don't forget that already more than half the world's population lives in urban areas – by 2050, this will be around 70% of the global population or 6.3 billion people.

The Triad – consumers but not growth drivers: The triad markets of the 1980s (US, Europe, Japan) have already ceded their place as the main drivers of global wealth creation. However, these markets still dominate global consumption and will do for decades to come. However forced austerity is translating into frugality in these markets with consumer confidence at historical lows, thanks to the sovereign debt crisis, government spending cuts and stubbornly high unemployment rates in the US and the Eurozone. Growth trends in US personal consumption expenditures are still positive but waning, while private consumption has picked in Japan but that in the Eurozone is fragile. Consumption growth is expected to return with economic growth but this will take some years and an aging population and depleted household savings mean that consumption is likely to expand less rapidly than it did pre-crisis. (Source: BEA, Deutsche Boerse)

China – one country, many markets: Only few companies would apply same strategies in Germany as they would in France, which should also be the case in China considering the vast size of the Chinese market and significant differences in the environment and growth across regions. Prioritization is a must. For example, two southern cities, the size of small European nation, ranking among the 4 wealthiest in China and only separated by a 3-hours drive, would appear to have a lot in common. But Shenzhen is home mainly to migrant workers who communicate in Mandarin with a local dialect, and prefer to drink in bars, while in nearby Guangzhou just over a quarter of inhabitants are migrants, more people are older, communication is mainly in Cantonese, and citizens enjoy going to restaurants to drink with family members. Given too the huge disparities in income, education and opportunities between rural and urban areas, a one-size-fits- all strategy in China is a no go. (Source: McKinsey Insight China)

Look Out For...

Africa rising: Ignoring Africa as a powerful economy is no longer an option and Western companies will have to tackle this huge market – or rather collection of markets, since the differences between countries are substantial. Overall, growth for the continent in the coming year is expected to be nearly 6%, with the

Republic of Congo, Ethiopia, Ghana, Mozambique, Nigeria, Tanzania and Zambia all expected to be among the world's ten fastest-growing economies. (Source: The Economist). A worldwide rise in demand for commodities in which Africa is rich – natural resources like oil, timber, coal, copper, bauxite, gold, diamonds, uranium, gas and more – is driving this growth, together with a rising domestic consumption. Investments from wealthier nations including China, India and Brazil have helped boost African development but often in exchange for these resources. For example by 2007, Chinese FDI in Africa had reached US$13.5 billion, or 14% of all Chinese FDI. (Source: Reuters) Looking further ahead, Goldman Sachs suggests that by 2050, individual African countries will remain small relative to BRIC, but as a group they have the potential to become larger than either Brazil or Russia, but not China, India and the US.

Hot zones: BRIC will continue to be the most important global growth markets in the next decades – but everyone knows that, so these markets are increasingly crowded with domestic and international companies vying for a share. The question is where are the next "hot zones"? The regions, countries, even cities which will deliver the next wave of growth markets as BRIC matures? To get a strong foothold in these markets as they start to take off, the time to act is now – and BRIC companies are certainly turning their attention to this in earnest. Based on our analysis, the next tier of future markets in terms of size, growth potential, natural resource positions and global focus/influence over the next 30 to 40 years is likely to include: Indonesia, Mexico, Turkey, Iran, South Korea, Egypt, South Africa, Nigeria, Thailand, Vietnam, Pakistan, Bangladesh, the Philippines and Argentina. This includes the *Next 11* list proposed in 2005 by Goldman Sachs based on similar analysis (except resource positions). The additions on our list are South Africa, Thailand and Argentina, which have relatively large populations, plus higher GDP per capita and stronger natural resource positions than some other countries on this list. Argentina and South Africa are members of the G20, with the latter also well positioned as a gateway for the broader African region.

City states: In 1950, there were 2 megacities in the world with 10 million or more inhabitants. Today's 21 megacities account for 9% of the world's urban population (324million) and are expected to rise to 29 in 2025 accounting for 10% of the urban population. Asia has the largest number of megacities with 11 in 2010, followed by Latin America with four and then by Africa, Europe and Northern America, with two each. By 2025, the number of megacities is expected to reach 29, with an additional five in Asia (Shenzhen, Chongqing, Guangzhou, Jakarta and Lahore), two in Latin America (Bogotá and Lima), and one in Africa (Kinshasa) (Source: UN). The rise in urbanization will help drive economic growth and open up new consumer markets in developing economies with some megacities becoming markets comparable in size to small (or even not so small) nations. The question is will cities become more important than states?

Multipolar Competition

The competitive landscape is changing: It is no longer "traditional" players (aka Western multinationals) competing in "traditional" industries with "traditional" business models. If you don't change to meet consumer/customer needs then someone else will – maybe someone outside your industry. Boundaries are blurring between industries, between organizations, between geographies and regions. Future market spaces will be defined not by industry labels but by the needs of different communities and consumer/customer groups. Will you be where your consumers/customers are? The diversity of competitors is also increasing in terms of geographic origin as large firms from rapidly developing economies build from their growing local markets to expand across the globe – and they are focused and hungry! It is also increasing as new types of organizations with purposes and business models that are not purely commercial enter the battle to meet emerging consumer needs and demands. For example firms that have a mix of commercial and social objectives which are increasingly termed "social businesses" – and don't ignore the pure non-profits, which are in some cases competing with commercial businesses to serve markets. Then of course, there are the increasing numbers of partnerships, collaborations and alliances between all the different types of players, underscoring the growing interdependence between them.

In Action!

The new global challengers: According to Boston Consulting Group the 2011 global challengers (emerging economy multinationals) come from 16 countries, with China, India, Brazil, Mexico and Russia dominating the list, although less so than recent years. Africa, which is a continent with new-found ambitions, has placed 4 companies on the list. In the coming years these global challengers will potentially successfully take on established multinationals because of their innovative business models and understanding of emerging markets. Some of the new additions to the challenger list include: Anshan Iron and Steel Group (China) with a revenue of US$15+ billion; Bharti Airtel (India) ranking as one of the largest telecom operators in the world; Bidvest Group (South Africa) which is the largest food-distribution company outside the U.S.; and Indorama Ventures (Thailand), one of the largest global producers of polyethylene terephthalate (PET).(Source: BCG -2011 Global Challengers)

Social business: Described by Nobel Peace Prize laureate Prof. Muhammad Yunus as a cause-driven business, in a social business the investors/owners can gradually recoup the money invested, but cannot take any dividend beyond that point. The purpose of the investment is purely to achieve one or more social objectives through the operation of the company, no personal gain is desired by the investors. Such companies are intended to cover all costs and make a profit, at the same time as achieving the social objective, such as providing healthcare, housing and financial services for the poor, nutrition for malnourished children, safe drinking water or introducing renewable energy. (Source: Yunus Centre) Grameen Danone which is a joint venture addressing malnutrition in Bangladesh is Yunus' prototype social business. In addition Grameen Bank, owned by the poor women it serves, is using a social business model.

Non-profits: NGOs spent the second half of the 20th century as outsiders challenging the system instead of being a part of it. Now many of the bigger NGOs have turned themselves into international super brands, some of them only focusing on a single issues like the environment, while others diversify their focus to cover areas such as health, education, social issues and climate changes etc. But one thing is alike for all of them. The influence of the NGOS on the national and international scene is rising and people trust the voice of NGO representatives. Today the trend is now far more towards informed dialog, with NGOs increasingly willing to move towards partnership with businesses and governments to realize mutual objectives, e.g. UN Global Compact; CI working with McDonald's or The Gates Foundation.

Look Out For...

Beyond ownership: Peer-to-peer sharing and renting solutions are emerging in more and more sectors such as transportation, homes, fashion and car parking. The consumer is pursuing the "owner-less" economy to avoid the greater costs and commitments of traditional ownership versus a fractional ownership or leasing lifestyle. Car sharing is no longer a new concept but what about renting vehicles from neighbors? A number of startups, including RelayRides, Spride, and Getaround, are trying to make it work in the city (California recently passed a bill that allows people to participate in peer-to-peer carsharing without violating their insurance policies). Getaround, which just launched this year, is also growing rapidly. (Fast Company)

Co-creation: With more consumers globally with more wealth, choice and desire to get involved in co-creation, the fight is on to own the new consumer – a consumer that wants more involvement and personalization, that wants it all anywhere, anytime, and wants it to be cheap and chic as the climate of frugality bites. Businesses at all points in the value chain are trying to connect with the consumer to build reputations, trust, loyalty, returns, market position and ultimately the license to compete. As consumers increasingly demand experiences and solutions, this fight may evolve into new, creative forms of cooperation between firms and others. More companies are taking up the idea of co-creation, e.g. LEGO Factory; Redesignme ; Spreadshirt and Jovoto.

Crowdsourcing plus: Crowdsourcing has changed the way we work, think and innovate. It continues to forge new routes to market and provide us with new solutions to old problems. An increasingly diverse range of platforms is evolving: *Crowdsource Design (*e.g. Crowdspring and 99Designs) can be used if you are looking for a design. *Crowdfunding (*e.g. ArtistShare and BuyaCredit) is about asking a crowd of people to donate money to your project. *Microtasks* (Microtask) involves breaking work up into tiny tasks and sending the work to a crowd of people. It typically cost .01¢ – .10¢ (10 cents) per completed task. *Open innovation* (e.g Open Innovation Sara Lee, Innovation Exchange, Innocentive and Eureke medical) is for ideas whether product design, marketing or something else. (The Daily Crowdsource). For a list of crowdsourcing platforms please visit Open Innovators.

Multipolar Economic/Political Systems

Even as markets and competition are becoming multipolar, so too are the systems which govern our societies and economies. Trust in national governments is low globally, as voters push back against parties and individuals tainted by scandals, voting irregularities and undelivered election promises. With less than half of the world's population living in countries which Freedom House defines as free in terms of political rights and civil liberties and a trend towards reduced democratic freedoms globally, increasingly people are turning to communities of choice to get their voices heard – or taking direct action as in the Middle East and North Africa. The level of central control in key rapidly developing economies remains high and will have greater impact as their global influence increases.

Economically, the Western system of free market capitalism is being challenged by the consequences of the financial system crisis and economic recession beginning in 2007 which are still playing out. The current crises fuelled by sovereign debt in Europe and the US are clear examples of failures of interconnected politics and economics. However, they have also highlighted challenges in centralized systems as the crises have spilled over to create pressures in China (see below). Politics and economics are interconnected, nationally and globally. There is an increasing need to find hybrid models of governance reflecting a balance between states, individuals and communities of choice – within and across national borders – which may signal increased political volatility in future. A key question for businesses will be how to find the right balances in terms of operating frameworks, business models and values to be successful operating across these very different economic and political environments in future. Likely a portfolio of approaches will be required – one size does not fit all – and it will be critical to anticipate shifts in the environment. But this also focuses attention on core values and principles which cannot be compromised – where are the lines in the sand that cannot be crossed?

In Action!

Google in China: In March 2009 China blocked access to YouTube, with speculation of an attempt to filter videos from Tibetan exiles. In June that year a Chinese official accused Google of spreading obscene content, a day after Google services became inaccessible to many users. In December 2009 Google.cn and other large companies experienced cyber attacks with the primary goal suggested to be accessing Gmail accounts of Chinese human rights activists – Google made this information public. In March 2010 Google stopped co-operating with China's censors and Google shut Google.cn, moving its service to Hong Kong to avoid mainland censorship laws. Since then, Google has found it much harder to do business in mainland China. The chief beneficiary is Baidu, China's leading search engine. Its share of internet searches, already vast, has grown to a dominant 75%. (Source: BBC News)

Free market capitalism under pressure: The financial crash and economic recession has called into question fundamental beliefs underpinning Western free market capitalism. Among 20 countries polled in both 2009 and 2010, an average of 54 % in 2010 rated the free market economy as the best economic system, unchanged from 2009. But Americans have lost faith with only 59% in 2010 seeing free market capitalism as the best system for the future, a fall of 15% versus 2009. The results mean that a number of the world's major emerging economies have now matched or overtaken the USA in their enthusiasm for the free market. 67% of the Chinese and Brazilians now regard the free market system as the best on offer and enthusiasm in India now equals that in the US. (Source: Globescan)

Eurozone/EU under pressure: Europe continues to be submerged by the continuing economic crisis and more countries are feeling the pressure. Merkel and Sarkozy are proposing a euro-zone "government" to tackle the debt-crisis. But the Europeans will have to agree on more than just budget-deficit thresholds as the foundation for closer integration, and control over budgets goes to the very heart of sovereignty. European nations will not give up control unless their neighboring countries take their security and political interests seriously. Some commentators see Europe is evolving into a set of regionalized groupings, with differing ideas about security and economic matters. One country may belong to more than one grouping, but for the most part membership will largely be based on location (Source: Stratfor). These economic, political and security tensions are likely to put the Eurozone/EU under more pressure.

Look Out For...

Russian privatization: Russia has privatized twice before. First, right after the fall of the Soviet Union but this was seen as a threat by Vladimir Putin as he became president in 2000, so he purged foreign entities from the country, its economy, its businesses and strategic sectors. The second time was in 2006, when the Kremlin privatized stakes in 1,500 companies, but with little success. Third time lucky? The Russian government is now launching a dual-objective program intended to leapfrog Russia into a more modern economy while bringing in cash. The privatization program alone is aimed at privatizing 5,000 companies as well as strategic stakes within 10 to 12 of some of Russia's most important firms, with the expanded plan increasing the number of strategic stakes on offer to 20 to 22 firms. (Source: Stratfor)

China's social pressures: Western crises have reduced demand for China's exports. To sustain the economy, the Chinese government has increased credit to avoid defaults by affected firms. This has also driven increased inflation, leading to the need to increase wages, which in turn has raised the cost of exports – presenting ongoing challenges for China as well as the West. To stabilize the situation (and their own positions) the political elite in China has increased control over the financial system and corporations. The result is that the political elite is no longer dealing with a financial crisis but with a far more dangerous political crisis that possibly could lead China into fragmentation and conflict, which in turn would exacerbate economic problems not only in China but worldwide. (Source: Stratfor)

Hybrid models: In just twenty years Vietnam has gone from being one of the poorest places on earth to one of South-East Asia's success stories. It started the transformation to a market economy in 1987 but its political system remains a mix of Marxism and capitalism, one that has brought enormous economic progress. The Vietnamese economy is weathering the global economic crisis well due to consumer spending, exports and a vast flow of foreign direct investment (US$10billion to US$11.5billion a year). Yet, demonstrations by farmers who have been thrown off their land, or workers angry about their tiny wages, happen. Complainys about corruption, bureaucracy and the incompetence of petty potentates surface. But overall, Vietnam is under control and there is little real political opposition. Looking ahead, the question is: "How long will it manage to reconcile the communist system with a capitalist economy?" (Source: Guardian)

Impact of elections/political changes in Russia, China, France and the US in 2012: China will be the first of these four powerful nations to hold its presidential election on January 14, 2012. Up next is Russia which will follow parliamentary elections on December 4, 2011 with presidential elections in March 2012. The two rounds of the 2012 French presidential election will be held on 22 April and 5 May, 2012. Last comes the United States presidential election, which is to be held on November 6, 2012. It is the first time in history these leading economic powers are likely to announce new political leaders in the same year. In fact, 24 countries worldwide including Spain, India and Mexico will appoint new political leaders in 2012. Under normal circumstances this should not be of major concern but according to Roland Berger Strategy Consultants "…we are living in a time of great economic and political turbulence, the political changes in 2012 will in some cases lead to changes in government that will affect the whole global economy. This may cause some instability, but could also open up new opportunities for development." (Sources: Project 2012 - Roland Berger Strategy Consultants, The Yale World Fellows Program, Haute Ecole de Commerce (HEC))

In October: Look out for trends in action on our changing world in 2011 (and the year's not even over yet!).