

Riding the ASEAN elephant

How business is responding to an unusual animal





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Preface

Riding the ASEAN elephant: How business is responding to an unusual animal is an Economist Corporate Network (ECN) report, sponsored by Baker & McKenzie. ECN performed the research, conducted the interviews and wrote the report independently. The findings and views expressed in this report are those of the ECN alone and do not necessarily reflect the views of the sponsor.

Justin Wood was the author of the report. Gaddi Tam was responsible for design and layout. The cover image is by iStockphoto.

We would like to thank all interviewees for their time and insights.

February 2013

Interviewees, in alphabetical order:

Manu Bhaskaran, CEO, **Centennial Asia Advisors**

Stuart Dean, CEO of ASEAN operations, **GE**

Grant Powell, head of Singapore Management Consulting Innovation Centre, **Accenture**

Nazir Razak, chairman, **CIMB**

Pushpanathan Sundram, managing director for Asia, **EAS Strategic Advice**

Peter Ter Kulve, CEO of South-east Asia, **Unilever**

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Executive summary

The Association of South-east Asian Nations (ASEAN) is enjoying a golden period, with high-growth and resilient economies. Foreign investment is pouring in, keen to capture the opportunity.

Much of the investment is directed at specific opportunities in individual markets. But some is also being made in the belief that South-east Asia is becoming more integrated. The ASEAN organisation aims to create an ASEAN Economic Community by the end of 2015—a single market and production base that stitches together the bloc's 10 economies into a coherent whole.

This report is based on a survey of 147 large multinationals operating in South-east Asia, asking them about their strategies in the region against a backdrop of deepening integration. The report also incorporates interviews with a handful of business leaders working in the region.

Among the report's key findings:

- The reasons for investing in South-east Asia vary by sector, but high on the list are impressive rates of economic growth, and a powerful consumer spending story. South-east Asia also has a strong manufacturing story, given that China is becoming expensive, and it has a growing investment story in fixed assets such as infrastructure. Alongside these factors, companies are also being attracted by the possibilities for greater integration in ASEAN—the stitching together of 10 smallish markets into one large one of 617m people.
- The ASEAN region faces many hurdles in its aims to achieve economic integration. Nationalism and protectionism continue to run high. Rivalries between ASEAN nations, and lack of trust are perennial issues. And staggering levels of diversity, on income levels, politics, culture, language, religion, and in economic systems continue to cause difficulties.
- But, despite the barriers, 95% of companies in our survey express confidence that ASEAN will achieve its vision of creating an economic community. What's more, companies say ASEAN's integration policies are starting to be meaningful for them. One quarter describe ASEAN's policies as "extremely important" in driving their strategy in ASEAN, while a further 60% describe them as "somewhat important". Regional agreements, such as the ASEAN Trade in Goods Agreement and the ASEAN Single Window, are helping to create a more harmonised market across the 10 ASEAN countries.
- Top-down policies from the ASEAN Secretariat are only part of the integration story. Just as important are the bottom-up integration dynamics. Local companies are pushing into their neighbouring markets. Investment flows across ASEAN borders are picking up. And people are



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moving across the region in ever greater numbers. In banking, for example, even though the ASEAN Banking Integration Framework is yet to be ratified, some banks in Singapore and Malaysia are already building a pan-ASEAN presence. Companies know they will benefit from ASEAN integration agreements, but they aren't waiting for them to arrive before they act.

- What sort of presence do companies have in the region? Stripping out local companies from the survey, the results show that Singapore has attracted the greatest level of foreign interest. Some 84% of global companies in the survey have set up their own operations in the city state. Malaysia comes a close second, with 76% of companies opening their own operations there.
- The survey shows a clear picture of two sub-groups of markets in South-east Asia. Six economies—Singapore, Malaysia, Thailand, Indonesia, Philippines and Vietnam—have attracted high levels of foreign investment. The remaining four—Cambodia, Myanmar, Brunei and Laos—have attracted much lower levels of interest. In the years to come, it is quite likely that Myanmar will join the ranks of the larger six nations.
- Where do global multinationals put their ASEAN management teams? Some 74% of firms choose Singapore, followed by Malaysia with 17%. Only 5.4% of respondents run the ASEAN region from a base outside ASEAN.
- Because ASEAN is diverse, many companies are forced to adopt a “multi-local” strategy across the region. Sales and go-to-market strategies are highly localised and tailored to individual markets. This prevents companies from clustering markets into meaningful groups.
- ASEAN diversity thus acts as a strong barrier to achieving scale. While 28% of companies see “big potential” for achieving scale across ASEAN markets, a further 56% see only “modest potential”. But companies believe this picture will improve.
- One area where firms are more successful in achieving scale is in their back office and support functions. In our survey, 44% of companies run “highly centralised” support services in ASEAN, and 30% run “somewhat centralised” operations.
- Can ASEAN diversity be turned into a positive? Can companies use varying levels of income and economic sophistication to split up their operations and run them in appropriate places across the region? Some 56% of companies regard ASEAN diversity as positive for their business, whereas only 14% regard it as negative.
- It's important to remember that ASEAN also carries large challenges. The biggest headache, say companies, is an uncertain legal environment. And while companies remain confident of ongoing integration, many say that some markets in South-east Asia remain protected. Companies in the survey consider Indonesia and Myanmar to be the most closed markets.



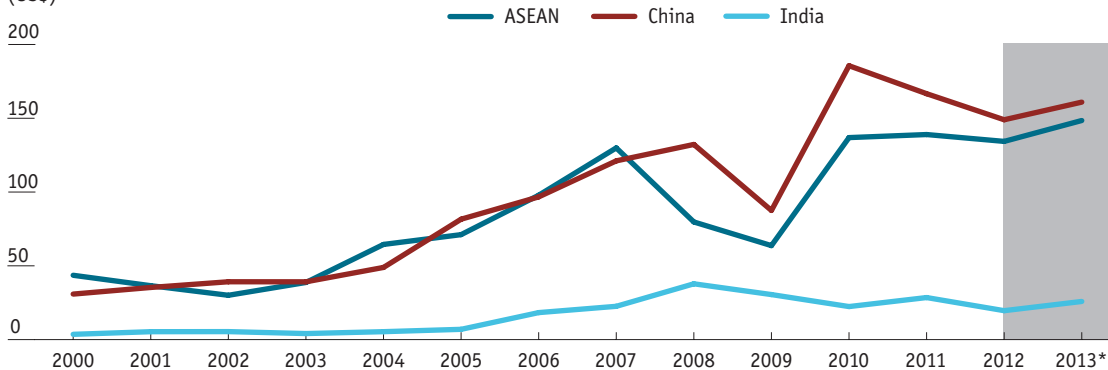
1. Introduction

With record levels of foreign direct investment reaching its shores, the ASEAN bloc is firmly in the spotlight. We survey 147 companies about their strategy in the region.

The global map of economic opportunity is never static. Markets constantly rise and fall in terms of their perceived attractiveness. One place that is seeing a dramatic surge in interest is the Association of South-east Asian Nations, or ASEAN bloc.

The 10 nations that make up ASEAN are attracting record levels of foreign direct investment. On a per capita basis, ASEAN is pulling in seven times more FDI than India, and almost the same amount as China. (See chart 1.)

Chart 1
Foreign direct investment per capita
(US\$)



* Forecast
Source: Economist Intelligence Unit

Naturally, much of this investment is directed at specific opportunities in individual markets. But much is also being made in the belief that South-east Asia is becoming more integrated.

The ASEAN organisation aims to create an ASEAN Economic Community by the end of 2015. The vision is of a single market and production base that stitches together the bloc's 10 economies into a coherent whole. Such a dream is still far off, but more and more companies are buying into the ASEAN vision. As such, the Economist Corporate Network has written this report in order to:

- understand how multinational firms are thinking about ASEAN;
- understand how they view the potential for ASEAN integration;
- explore what all this means for crafting corporate strategy in the region.



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In researching this report, we conducted a survey of 147 big companies from a wide variety of sectors operating in the ASEAN region. Roughly a third had global revenues of less than US\$1bn, another third had revenues of between US\$1bn and US\$10bn, and the final third had revenues of more than US\$10bn. The respondents were all senior executives with regional responsibility. The majority worked at Western firms, with 40% working for European companies, and 35% for North American multinationals. The remaining 25% of respondents worked for Asian companies.



2. Why ASEAN? Why now?

Rapid economic growth, and the rise of a vibrant middle class are fuelling opportunities in ASEAN. But deepening integration is also important.

The reasons for investing in South-east Asia vary by sector. But underpinning everything are impressive rates of economic growth. Respondents to our survey highlighted this as the most attractive feature of the region. (See chart 2.) For the period between 1999 and 2012, the ASEAN region grew in real terms by an annual average rate of 5.5%, so doubling in size in just 13 years. At the Economist Corporate Network, we expect South-east Asia to grow at a similar pace for the foreseeable future.

Chart 2
How attractive are the following criteria for your business in ASEAN?*
(%)



*(1 is highly unattractive, and 5 is highly attractive)
Source: Economist Corporate Network

Super consumers

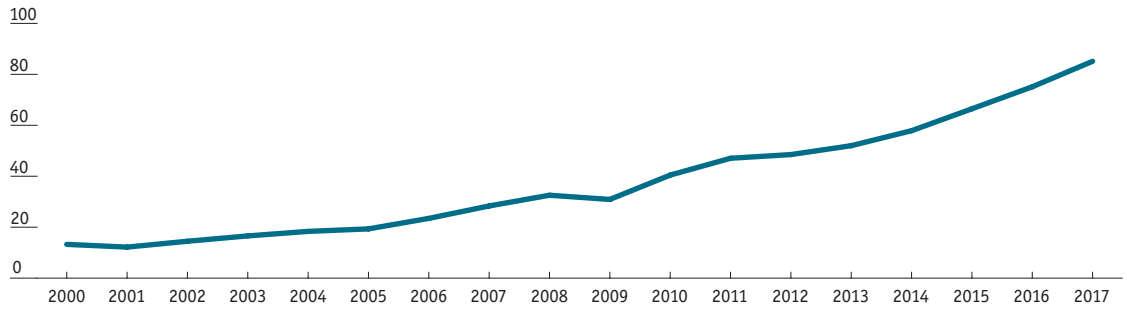
This rising economic wealth, coupled with a population of 617m people, creates a powerful consumer spending story. Indeed, our survey shows this to be the second most attractive feature of South-east Asia. Huge swathes of ASEAN's population stand on the threshold of middle class status, which we define as a household income of US\$5,000 or more. At this point, consumers no longer buy only necessary items such as food, but start to buy discretionary items such as smart phones. We forecast the number of middle class households in ASEAN will rise from 40m in 2010 to 85m by the end of 2017. (See chart 3.)



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Chart 3
Number of households in ASEAN* earning more than US\$5,000 per annum
 (millions)



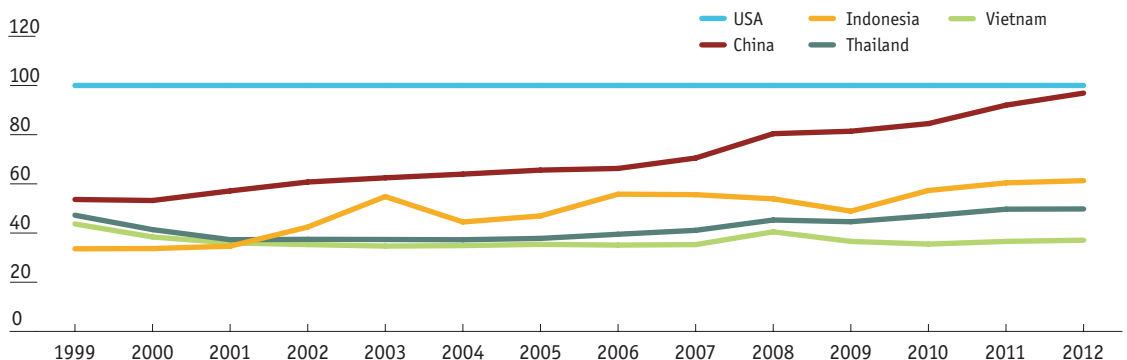
* Indonesia, Thailand, Malaysia, Singapore, Philippines, Vietnam
 Source: Economist Intelligence Unit

This burgeoning market is highly attractive for consumer goods firms. “We are extremely bullish on South-east Asia,” says Peter Ter Kulve, CEO of Unilever in the ASEAN region. “The populations are young and growing. Incomes are rising rapidly. The cities are doing very well, but the rural story is just as strong. Given increasing demand for food globally, agricultural wages on the plantations across the region are rising.”

Factory firepower

Alongside agriculture, industry is also doing well, and starting to compete with China. While China remains the manufacturing capital of the world, the country is becoming increasingly expensive. Unit labour costs in China are now almost the same as in America (even though hourly wages remain much lower). By contrast, unit labour costs in Vietnam are only 37% of US levels, causing many firms to put manufacturing in South-east Asia. (See chart 4.)

Chart 4
Unit labour costs
 (the labour cost of producing one unit of economic output, or GDP, indexed to USA = 100)



Source: Economist Intelligence Unit



Our survey shows that companies are just as excited about B2B opportunities in the region as they are about B2C. GE, a diversified US conglomerate, has grown its business in ASEAN by 20% every year for the past two years. “About 80% of our business is in infrastructure,” explains Stuart Dean, CEO of GE’s ASEAN operations. “The demand for new infrastructure is strong across the board, in aviation, power, oil and gas, healthcare, railway locomotives.”

Investment fuels the furnace

Indeed, it seems likely that ASEAN stands on the brink of a multi-year investment boom. Many ASEAN nations have significantly under-invested in infrastructure and other fixed assets in recent years thanks to the fallout from the Asia Financial Crisis of 1997 and 1998. During the years after the crisis, many companies and governments in the region concentrated on paying off debts and repairing balance sheets rather than investing in new projects.

The resulting investment deficit has created huge pent-up demand for infrastructure, for housing, and for factories. This pent-up demand will drive high levels of investment activity for many years, fuelling economic growth in the short-term through construction activity, as well as in the long-term by raising the region’s future productive capacity.

Integration nations

Companies in our survey also say they consider the prospect of greater economic integration in ASEAN to be attractive. However, as chart 2 shows, integration is currently considered a less important factor than many other aspects of the picture in South-east Asia.

The views of Nazir Razak, chairman of CIMB, one of Malaysia’s largest banks, are similar to those of many companies. “The domestic story in ASEAN markets is the primary attraction. We’ve always been excited by that,” he explains. “But the cross-border story is getting much more interesting these days, and it will grow exponentially more interesting as the barriers to integration are brought down under the various ASEAN initiatives.”

Pushpanathan Sundram, managing director for Asia at EAS Strategic Advice, a trade consultancy for the food business, and a former deputy secretary general of the ASEAN Secretariat, is of a similar mind. “Twenty years ago, companies were only interested in ASEAN markets on an individual basis. At the time there were no implementable agreements to stitch the region together,” he notes. “Today that has changed. These days we have common agreements on trade, on investment, and many others are in the works. We have numerous connectivity projects around physical infrastructure and telecoms and IT, and around soft issues like culture too, and what it means to be an ASEAN citizen.”



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3. ASEAN integration: A work in progress

ASEAN's top-down integration projects move slowly, but the direction of change is positive. Companies expect them to keep moving forward.

Most observers agree that cross-border integration of ASEAN's 10 economies is essential if the region is to continue to thrive. Only by joining together to create real scale can ASEAN markets and companies become truly competitive and efficient.

But trying to integrate 10 economies that are as diverse as those in the ASEAN organisation is a giant challenge. Indeed, ASEAN is arguably the most diverse regional grouping in the world. On a per capita basis, the richest country, Singapore, is 56 times wealthier than Myanmar, the poorest. In terms of people, Indonesia's population of 248m is 593 times larger than Brunei's 420,000 citizens. Political systems range from quasi-dictatorships to vibrant democracies. Economic systems range from communist to capitalist. Religions and languages are equally varied.

ASEAN's expanding ambition

Against this huge diversity, efforts to integrate the ASEAN region have grown ever more ambitious. When the ASEAN idea was first forged in 1967, the goal was merely to create a security union among neighbouring countries to promote peace.

Over time, the bloc's aspirations grew. In 1992 it signed the ASEAN Free Trade Area Agreement with the goal of reducing tariff barriers between member states. Today, almost all products can move across ASEAN without tariffs being applied, although non-tariff barriers remain deeply entrenched in many cases, thereby undermining the benefits of tariff reductions.

The most far-reaching step came in 2007, when ASEAN's 10 members agreed to create an ASEAN Economic Community by 2015. The vision is of a single market in which products and services can flow across borders free of tariff and non-tariff barriers, in which investments can be made without stumbling into foreign ownership rules, and in which skilled labour can move to wherever it is in demand.

Daring but demanding

The vision is bold, but fraught with challenges, not least because the process of integration requires sacrificing sovereignty, which ASEAN countries have historically been reluctant to do. Many observers point to a lack of trust between ASEAN neighbours as a major impediment to integration.

Issues of nationalism and protectionism also hold back progress. Indonesia is notable in this regard. As the biggest economy in ASEAN, some in the country feel that regional integration is a low priority. Instead, they push for measures that raise the barriers to integration. In the past year, policies have



been proposed to lower foreign ownership limits in banks and mining companies, and to put controls in place on certain types of imports and exports.

At CIMB, Mr Nazir notes a certain local rivalry between ASEAN nations that also throws up barriers. “Some countries in ASEAN would rather see a European bank do well in their country than a Malaysian bank,” he notes. Observers in other sectors agree with him. For foreign multinationals, such local rivalries can also be a headache, such as when citizens of one nation are reluctant to report to citizens of an ASEAN neighbour, but are more open to having a boss who comes from outside ASEAN.

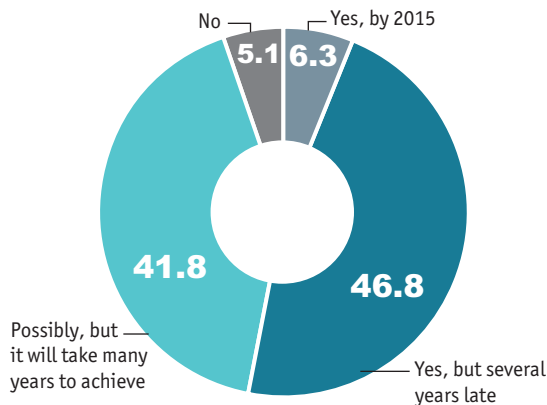
Thus, while countries make bold public statements in support of a regional community, some ASEAN members remain half-hearted in their commitment to the idea. This lack of commitment means that the ASEAN Secretariat is woefully under-funded and under-manned. While the European Union civil service has a staff of 30,000 crafting and implementing integration policies, the ASEAN Secretariat has just 200. And it lacks any powers to push member states to implement their ASEAN agreements or to punish those who break the rules.

Slow progress, but moving forward

And yet, despite the slow pace of progress, and occasional reverses, most observers feel the ASEAN Economic Community will eventually be achieved. Our survey shows that, while only 6% of respondents expect it to be achieved by the 2015 deadline, another 89% expect it to be completed eventually. (See chart 5.)

“The pace of change is slow, sometimes frustratingly slow, but what’s important is the direction of change,” says Mr Pushpanathan at EAS. “And remember that the goals for the ASEAN Economic Community are very bold. Even if they only achieve 70% of their targets by 2015, that will still be a huge achievement.”

Chart 5
Will ASEAN succeed in building an ASEAN Economic Community by 2015?
(% of respondents)



Source: Economist Corporate Network



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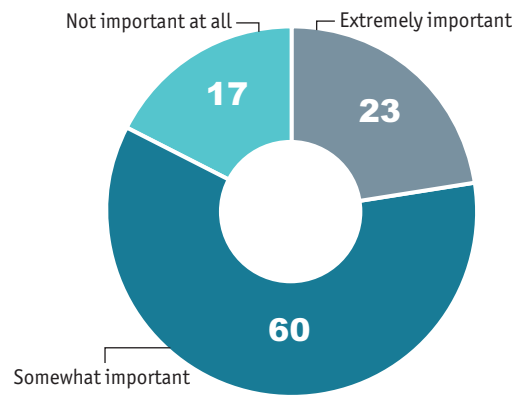
4. ASEAN integration becomes meaningful

Companies say that ASEAN integration efforts are starting to have an impact on their business and their strategy in South-east Asia.

The previous section showed that companies believe ASEAN integration will continue, and that an ASEAN Economic Community will emerge. But are such developments feeding into corporate strategy? Our survey shows that they are. Some 23% of respondents described ASEAN integration policies as being extremely important in driving their strategy, while a further 60% believed them to be somewhat important. (See chart 6.)

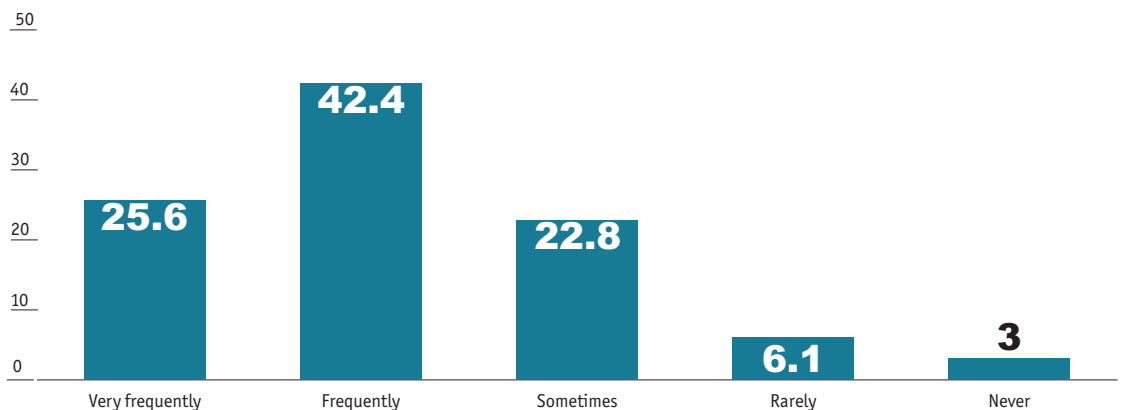
Our survey also shows that companies are benefitting from the agreements that ASEAN is managing to implement. For example, among the manufacturing companies in our survey, 26% say they make use of the ASEAN Trade in Goods Agreement (ATIGA) “very frequently”, while a further 42% use it “frequently”. (See chart 7.) Increasingly, companies are able to manufacture goods from one location and ship those goods across the region without bumping into barriers and constraints.

Chart 6
How important are the integration policies of the ASEAN organisation in driving your ASEAN strategy? (%)



Source: Economist Corporate Network

Chart 7
Do you use the ASEAN Trade in Goods Agreement (ATIGA) or other free trade agreements between ASEAN and her trading partners to minimise customs duties in your supply chain?*



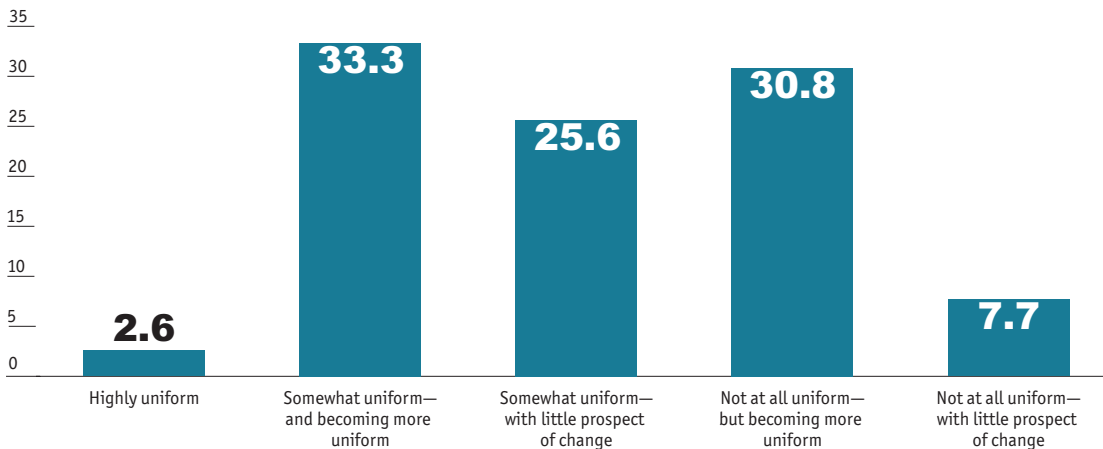
* Responses include only companies whose primary activity is manufacturing
Source: Economist Corporate Network



“Many of ASEAN’s integration efforts are starting to become meaningful,” notes Mr Dean at GE. He points to efforts to integrate the region’s capital markets. By pooling capital and liquidity, it helps the formation of cross-border infrastructure funds, which in turn provide finance to build the infrastructure that GE supplies. And, he notes, “Customs harmonisation and the ASEAN Single Window are very important.”

Indeed, since 2005 ASEAN has been working on creating a “Single Window” for customs and cross-border trade. The idea is that companies involved in trade and transport will only need to submit one

Chart 8
How uniform are customs procedures for your industry across ASEAN?*
(%)

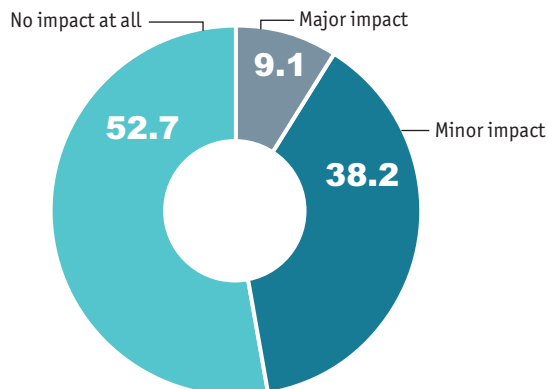


*Responses include only companies whose primary activity is manufacturing
Source: Economist Corporate Network

set of standardised documents in order to move goods across ASEAN borders, instead of doing so with every individual customs organisation. Our survey shows that 67% of respondents believe customs procedures are either already highly uniform across the region, or have good prospects for becoming more uniform. (See chart 8.)

Of course, the impact of ASEAN’s integration initiatives varies by sector. For services companies, the benefits have arguably been less extensive. In our survey, 53% of respondents felt that the ASEAN Framework Agreement on Services has had no impact at all on harmonising their industry across borders. (See chart 9.)

Chart 9
What impact has the ASEAN Framework Agreement on Services (AFAS) had in harmonising your industry across ASEAN?
(%)



Source: Economist Corporate Network



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5. Companies are doing it for themselves

While top-down integration by the ASEAN organisation continues, bottom-up integration is already happening. Companies are pursuing regional strategies without waiting for ASEAN to create a perfect market.

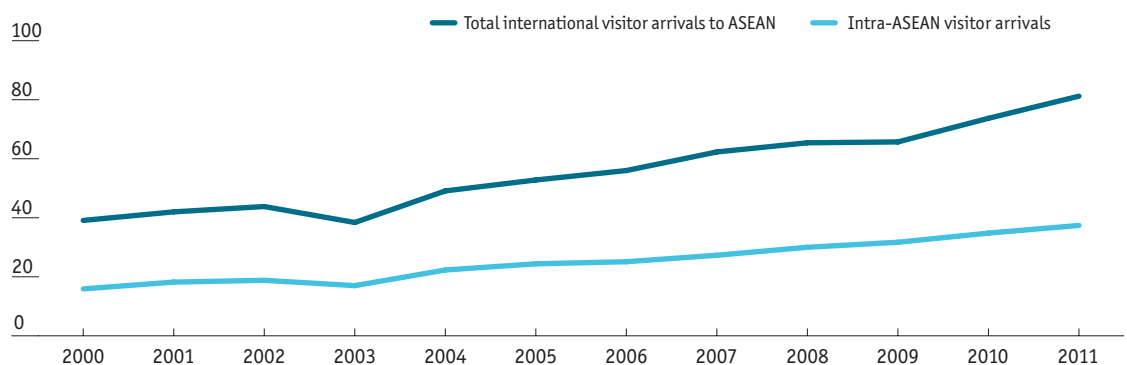
Importantly, top-down policies from the ASEAN Secretariat are only part of the integration story. “Just as important are the bottom-up integration dynamics,” argues Manu Bhaskaran, CEO of Centennial Asia Advisors, a consulting group in Singapore.

He points to sub-regional integration efforts, such as those underway in the Greater Mekong Sub-Region, a project driven by the Asia Development Bank to stitch together the economies of Thailand, Myanmar, Laos, Vietnam, Cambodia and the Yunnan province of China. Even more localised are projects such as the integration underway between Singapore and the Iskandar Development Region in Malaysia. Companies that find Singapore to be increasingly expensive are shifting investments into more affordable Malaysia as the two countries grow ever closer.

At the most micro level of all, individual companies and people are also driving integration. Local companies are not waiting for ASEAN to create a perfect playing field before they do business in their neighbouring markets. Investment flows across ASEAN borders are picking up.

And people are moving across the region in ever greater numbers. The volume of intra-ASEAN international travelers—tourists, investors, and migrant workers—has more than doubled from 16m in 2000 to 37m in 2011. (See chart 10.)

Chart 10
International visitor arrivals into ASEAN countries
(millions)



Source: ASEAN Secretariat



At CIMB, the regional expansion strategy is partly about finding new markets overseas. But just as importantly, it is about serving clients from existing markets as they increasingly invest and travel across the region. In other words, the bank is growing by supporting the bottom-up integration of ASEAN markets.

For example, tourists require ATM services—Mr Nazir claims CIMB was the first bank to build out a pan-ASEAN network of free ATMs. And corporate clients need their local bank to support them overseas. “ASEAN companies are really starting to build a regional presence,” he says.

Today, CIMB has a presence in every ASEAN market except Laos. And yet the ASEAN Banking Integration Framework is still to be ratified by the region’s central banks. The lesson, stresses Mr Nazir, is that, even though companies will benefit from ASEAN integration agreements, they shouldn’t wait for them to arrive. Rather, they should push ahead and create a regional strategy today, because bottom-up integration across ASEAN is already happening.

Global MNCs, but local MNCs too

Many of the firms crafting regional strategies in ASEAN are foreign multinationals. But an increasing number of local companies are buying into the idea too. Those from Singapore, Malaysia and Thailand are especially keen, because many of these firms have reached the limits of growth in their domestic markets and are looking for new pastures.

In banking, CIMB and Maybank in Malaysia, and DBS from Singapore are all building a pan-regional presence. In fast-moving consumer goods, Thailand’s ThaiBev is involved in a bid to buy Fraser & Neave, a large drinks business in Singapore.

In transport, Malaysia’s AirAsia is rapidly turning into a pan-ASEAN airline by setting up a network of local operations in markets like Thailand and Indonesia where local partners own a big chunk of the business. In healthcare, ParkwayPantai, is the result of a union between two hospital and healthcare providers, one Singaporean and one Malaysian. The group now has 17 hospitals, including operations in Vietnam and Brunei.



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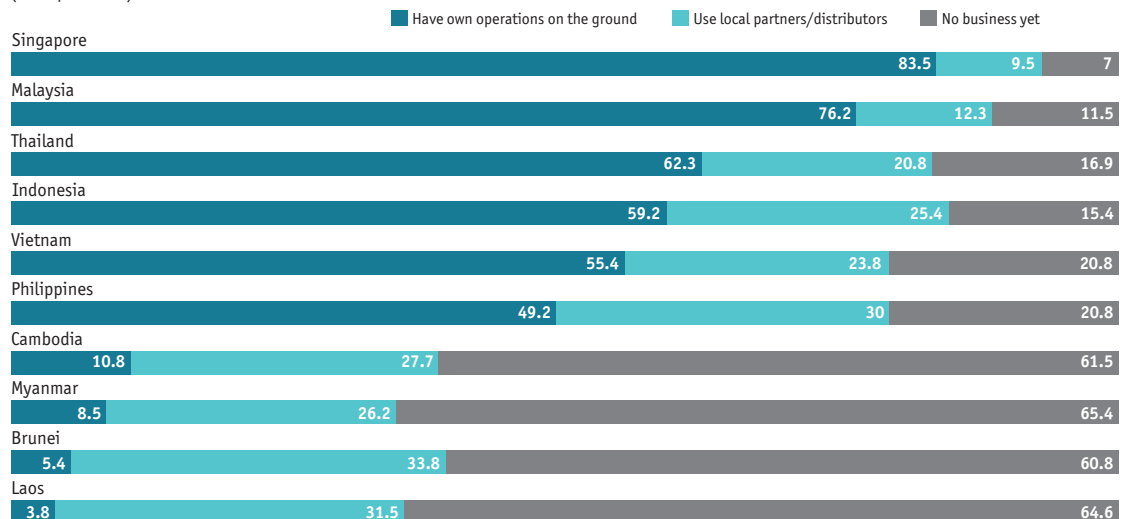
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6. ASEAN strategy: what and where?

With 10 different markets to choose from, where are companies setting up operations?

Given that south-east Asia is full of opportunity, what sort of presence do companies have in the region? Stripping out local companies from our survey, so as to eliminate home bias, our results show that Singapore has clearly attracted the greatest level of foreign interest. Some 84% of global companies in our survey have set up their own operations on the ground in the city state. Malaysia comes a close second, with 76% of companies having opened their own operations there.

Chart 11
Do you do business in these ASEAN markets?*
 (% respondents)



* Results are only for non-ASEAN companies
 Source: Economist Corporate Network

The results also reveal a clear picture of two sub-groups of markets in South-east Asia. Six economies—Singapore, Malaysia, Thailand, Indonesia, Philippines and Vietnam—have attracted high levels of foreign investment. The remaining four—Cambodia, Myanmar, Brunei and Laos—have attracted much lower levels of interest. In Laos, for example, only 4% of companies have set up their own presence on the ground.

The two different groups are clearly a reflection of the different size of the markets. (See table 12 and chart 13.) In the years to come, it is quite likely that Myanmar will join the ranks of the larger six nations, and attract many more companies to invest there. GE, for example, is opening its first office in Myanmar in March 2013.

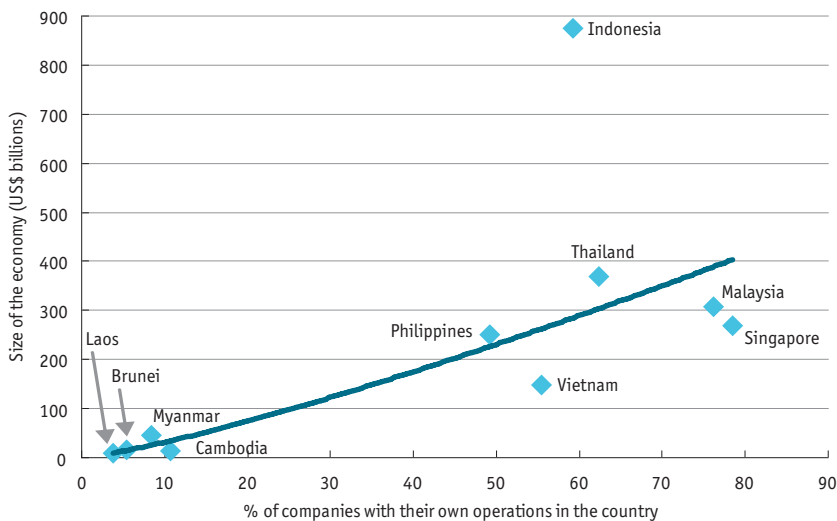


Table 12
Incomes, population, and economic size across ASEAN

| | GDP per capita (US\$) | Population (m) | Size of the economy (US\$m) |
|-------------|-----------------------|----------------|-----------------------------|
| ASEAN | 3,700 | 617.4 | 2,284.4 |
| Indonesia | 3,520 | 248.2 | 873.7 |
| Thailand | 5,370 | 68.8 | 369.5 |
| Malaysia | 10,490 | 29.3 | 307.7 |
| Singapore | 49,790 | 5.4 | 267.9 |
| Philippines | 2,420 | 103.8 | 251.2 |
| Vietnam | 1,650 | 89.5 | 147.7 |
| Myanmar | 896 | 51.4 | 46.1 |
| Brunei | 39,600 | 0.4 | 16.6 |
| Cambodia | 978 | 14.6 | 14.2 |
| Laos | 1,470 | 6.4 | 9.4 |

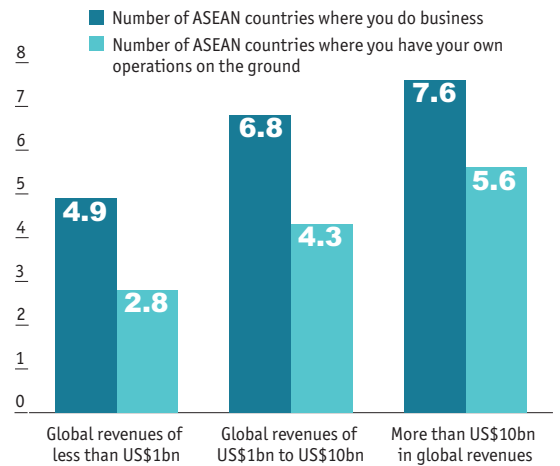
Source: Economist Intelligence Unit

Chart 13
Number of companies with their own on-ground presence (%) plotted against size of each economy (US\$ billions)*



* Results are only for non-ASEAN companies
Source: Economist Corporate Network

Chart 14
Number of ASEAN markets where companies are active, broken down by company size (% of respondents)



Source: Economist Corporate Network



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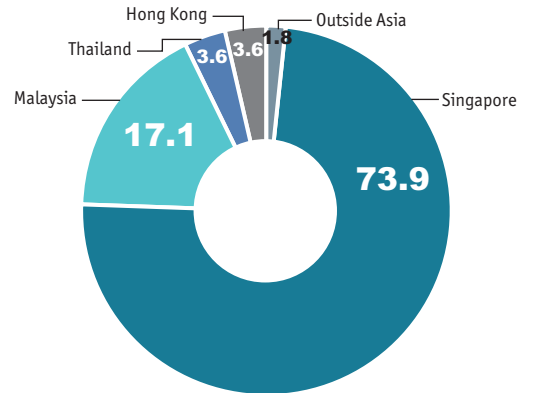
Our survey results also show a clear correlation between company size and the number of ASEAN markets where they do business. (See chart 14.)

Running regional hubs

Given this pan-regional presence, we asked the global multinationals in our survey about the location of their ASEAN management team. The clear leader is Singapore, with 74% of firms running their regional head office there. (See Chart 15.) Interestingly, 5.4% of respondents said they run the ASEAN region from a base outside ASEAN—3.6% doing so from Hong Kong, and 1.8% doing it from a country outside Asia.

Chart 15

From where do you manage your ASEAN operations?
(% of respondents)*



* Results are only for non-ASEAN companies
Source: Economist Corporate Network



7. ASEAN strategy: markets and operations

Diversity in ASEAN presents both challenges and opportunities for corporate strategy.

Several important features of the ASEAN business landscape stand out. Firstly, despite deepening integration, the region remains highly fragmented. Secondly, these individual fragments—the 10 ASEAN nations—are highly diverse.

The result is that, for now at least, many companies are somewhat limited in the degree to which they can pursue unified, pan-regional policies. Instead, many firms are forced to adopt a “multi-local” approach to their markets in South-east Asia.

Going multi-local

At Unilever, Mr Ter-Kulve notes that his company considers some regions of the world to be highly homogenous, but not ASEAN. For example, in Latin America, Unilever is able to bunch together the region’s 30-odd countries into two broad clusters of markets. Within each of these two clusters, the approach to marketing, branding and customer insight is broadly similar. Unilever has a similar approach in Western Europe, where uniformity across markets enables the firm to have just three broad clusters of markets.

In ASEAN, however, Unilever has no market clusters at all. The approach taken in each market is specific to the local culture and consumer character. Of course, for some international brands, such as Unilever’s Belgian chocolate products, the company has a consistent approach to marketing and product positioning. But for most brands, the treatment is much more localised.

It might seem intuitive that consumer product companies would adopt a highly differentiated approach to their business across ASEAN’s culturally-diverse landscape. But B2B companies also need to adopt a similar approach. At GE, Mr Dean notes, “From a marketing and selling point of view, you need to be in each individual market. You can’t have a single ASEAN sales force based in one central hub like Singapore. You need local teams in the ground who understand the local language and culture.”

At CIMB, Mr Nazir runs a similar approach. “Our business model is very dispersed,” he says. “Our teams in each country are highly localised, and our product operations are highly differentiated by market. You have to give sufficient latitude to the local teams to adjust the products and the marketing to suit local preferences.”

Scale and efficiency

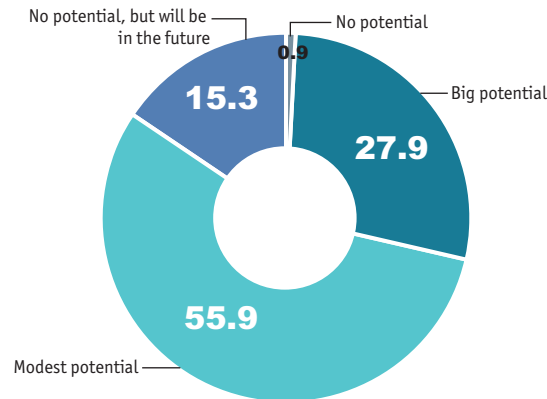
Naturally, this need to be local across many markets means that some companies struggle to achieve meaningful scale. Our survey shows that 28% of companies feel the potential for achieving scale across ASEAN is large, while a further 56% see only modest potential for achieving scale. (See chart 16.)



Riding the ASEAN elephant

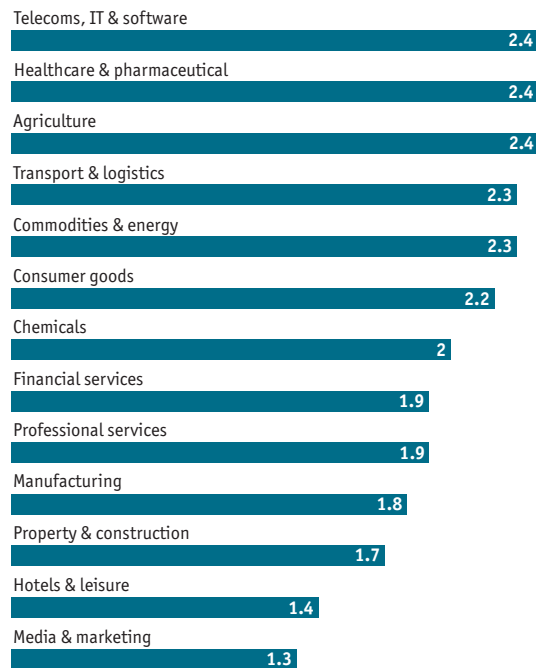
How business is responding to an unusual animal

Chart 16
In your industry, what potential is there to achieve scale across ASEAN markets?
 (% of respondents)



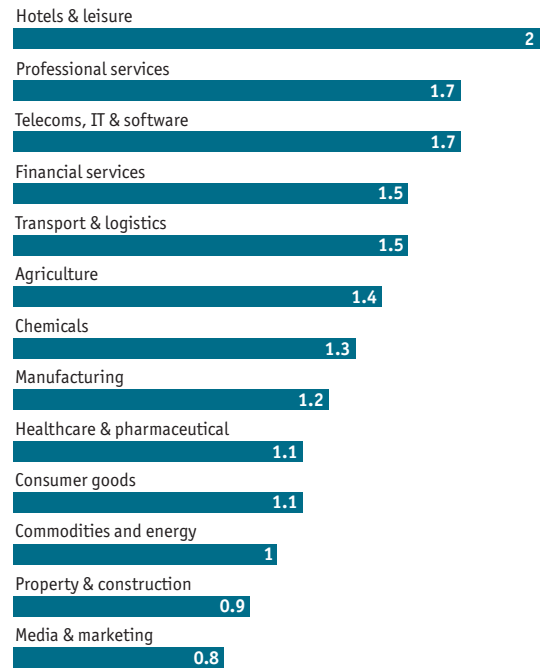
Source: Economist Corporate Network

Chart 17
How consistent and standardised are the products and services you offer in ASEAN markets?*



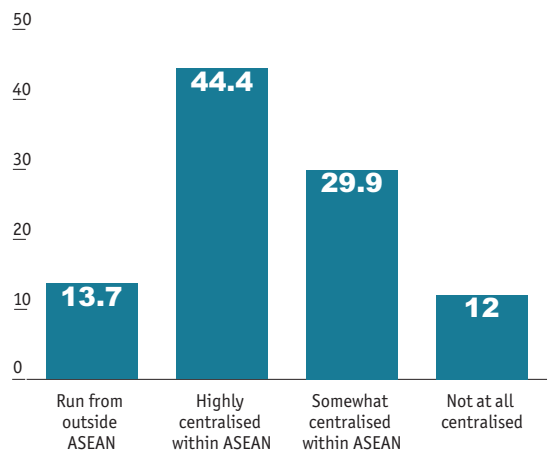
* (0 = not at all standardised, and 3 = highly standardised)
 Source: Economist Corporate Network

Chart 18
How consistent and standardised are the rules and regulations governing your industry across ASEAN markets?*



* (0 = not at all standardised, and 3 = highly standardised)
 Source: Economist Corporate Network

Chart 19
How centralised are your business support services (eg finance and HR) for your operations in ASEAN? (% of respondents)



Source: Economist Corporate Network



However, as the integration efforts of the ASEAN organisation progress, so the opportunities for achieving regional scale should grow. As Mr Bhaskaran at Centennial notes, “This is the real test of success. If companies can’t achieve economies of scale then integration will have failed. Right now, a lot of companies aren’t able to generate real scale, but it will come.”

For that scale to arrive, companies must feel that they are able to offer a consistent set of products and services across the region. Our survey shows that, at present, many industries have some confidence in this regard. Companies in sectors such as pharmaceuticals, software and commodities say their products across ASEAN are fairly consistent, although other sectors are less positive. (See chart 17.)

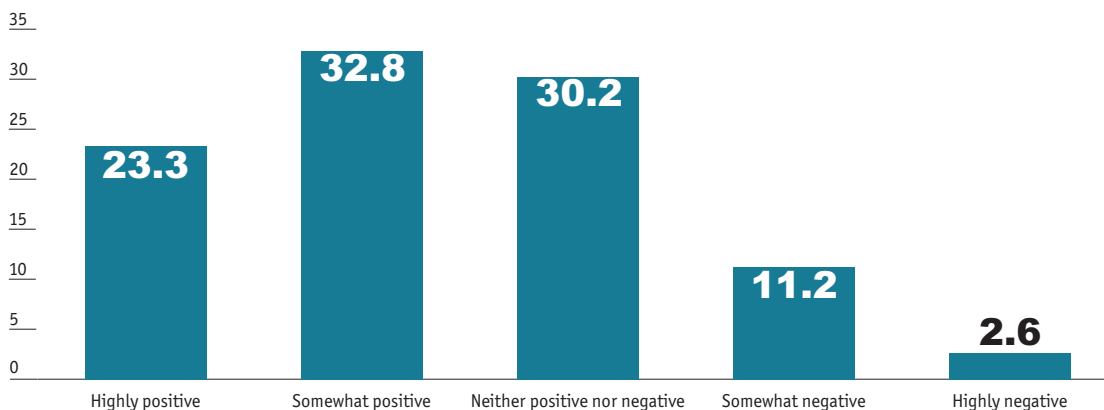
Just as important for achieving scale, companies must feel that ASEAN economies operate with a consistent set of standards that govern their products and services. Here, the results are much less positive. (See chart 18.) Take the pharmaceutical industry. While its products are largely consistent across ASEAN markets, the local regulations in each market are highly varied.

But while front office functions like sales and marketing might struggle to achieve scale, companies do seem to be recording greater success with their back office roles such as finance and HR. Our survey shows that 44% of companies have support services across the region that are “highly centralised”. Another 30% say such services are “somewhat centralised”. (See chart 19.)

Diversity equals complementarity?

Interestingly, the centralisation of back office operations in ASEAN has been driven in part by the region’s high diversity—the very same diversity that has impeded economies of scale in the front office. Because wages and skills vary across the region, it creates opportunities for complementarity. Companies can take the full spectrum of their operations, from manufacturing to accounting, break them into chunks, and put these chunks in places where they can be done best. At least that’s the theory.

Chart 20
Is ASEAN diversity positive or negative for your business?
(% of respondents)



Source: Economist Corporate Network



Riding the ASEAN elephant

How business is responding to an unusual animal

Are companies actually doing this? Grant Powell, head of Accenture's Management Consulting Innovation Centre in Singapore, believes that some are. "At the moment I would say the companies using ASEAN's complementarities are much more likely to be global MNCs," he says. "Many of them already run global supply chains from within the region, they already have call centres in Manila, and IT services in Kuala Lumpur or financial operations in Singapore. Local ASEAN companies are a bit more reluctant to do this type of thing."

Mr Powell sees other advantages to ASEAN diversity too. "Diversity helps to nurture creativity and innovation," he says. "It brings different perspectives and ways of thinking."

Respondents to our survey tend to agree with views such as these. Some 56% of companies say they think ASEAN diversity is positive. Only 14% consider it to be negative for business in the region. (See chart 20.)



8. Conclusion

While companies are right to be excited about South-east Asia, the region also presents serious challenges.

The title of this report is “Riding the ASEAN elephant: How business is responding to an unusual animal”. The analogy of an elephant is apt, because as ASEAN comes together and deepens its ties across the region, so it becomes a formidable size, accounting for 10% of the global population and 3.5% of the world economy. Given ASEAN’s strong growth rates, that share of the global economic pie will rise to 4.5% by 2017, and keep rising thereafter.

Equally, just as an elephant is an unusual deign, so too is ASEAN an unlikely combination. Given the diversity of its 10 member economies, there is little that ties them together naturally. And yet, the coming together of these economies is creating a powerful combination.

For companies the challenge is learning to harness this unusual beast to their own ends, which requires a distinct approach to managing strategy. In particular, it means recognising how to combine a highly differentiated front office, with the possibilities for efficiencies in the back office. Equally, it calls for recognition that the possibilities for achieving scale and uniformity are likely to keep rising as the region’s economic integration deepens.

The dangers of being thrown

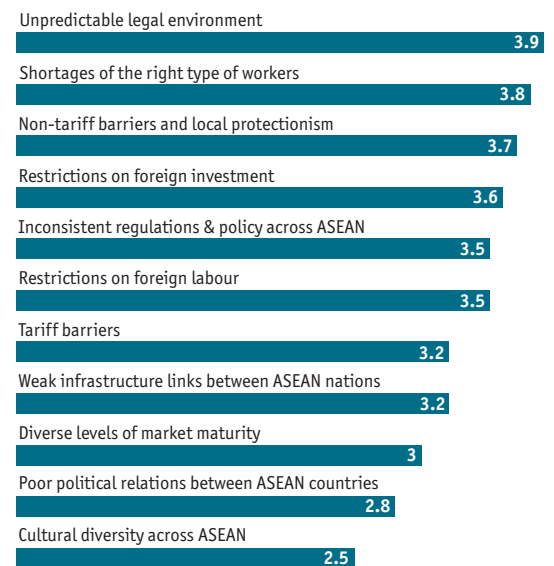
Learning how to handle this unusual animal also means recognising that its behaviour can at times be erratic. Bull elephants occasionally go into a period known as musth, when their behaviour becomes highly uncertain and aggressive. In the same way, major challenges can break out in ASEAN.

Some markets are prone to economic uncertainty. In Indonesia, the rupiah can be volatile. In Vietnam, inflation rates have been uncomfortably high for a number of years, and the country is experiencing a small-scale banking crisis. In Thailand, politics can be febrile. In Myanmar, the opening up of the country is by no means certain to stick to its current positive path.

According to our survey, executives acknowledge these concerns. In terms of operational challenges, they highlight legal uncertainty as a major concern in doing business in ASEAN. Governments change their minds about important legislation with little warning. And even when laws remain unchanged, court decisions and interpretations of the laws can be highly arbitrary. (See chart 21.)

Another issue that companies have to contend with is protectionism. Despite ongoing efforts at integration and opening up of ASEAN’s internal

Chart 21
How serious are these challenges to growing a regional business in ASEAN?*



* On a scale of 1 (not serious) to 5 (extremely serious)
Source: Economist Corporate Network



Riding the ASEAN elephant

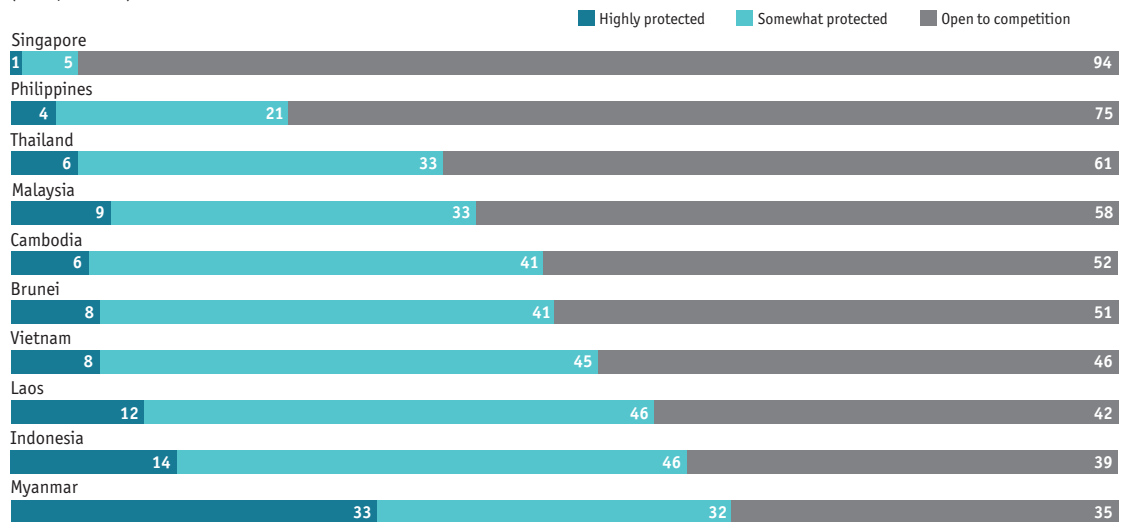
How business is responding to an unusual animal

market, resistance remains strong from local players in many markets. In our survey, executives say Myanmar and Indonesia are the two most protected markets. (See chart 22.)

Chart 22

How open are the following countries to foreign competition in your industry?

(% respondents)



Source: Economist Corporate Network

But for all its challenges and undoubted risks, the ASEAN region is undeniably one of the bright spots in today's global economic landscape. The region is growing rapidly. Its economies are integrating at many different levels. And companies that persist with an image from yesteryear of an ineffective ASEAN bloc are likely to miss important opportunities.

About Economist Corporate Network Asia

Economist Corporate Network (ECN) is The Economist Group's advisory, briefing and networking service for Asia-based senior executives seeking insight into economic and business trends in key growth markets. Through a tailored blend of interactive meetings, high-calibre research, and private client briefings, ECN Asia delivers country-by-country, regional, global and industry-focused analysis.

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