Japan Rebooted

ASEAN, the next frontier: Tapping Southeast Asia's surging growth

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We wish to thank the many individuals and organisations who contributed their time and insights to this report.

All values are in AU dollars unless otherwise indicated.

Introduction

Jason Hayes

*There is now little doubt that Japan is finally on the tumultuous path to reform. As we have covered in previous issues of the **Japan Rebooted** series, the process of forging a new Japan has begun in earnest under Prime Minister Shinzo Abe and his Abenomics policies.*

The Bank of Japan's radical monetary easing policy continues to grow, and to boost the export earnings of Japanese companies that are – as we detailed earlier in the *Japan Rebooted* series – under pressure to internationalise and establish new foreign markets for their products and services.

This is not proving to be an easy process for Japanese firms, many of whom remain well behind most of their Western peers in establishing proper corporate and governance structures to become truly global players.

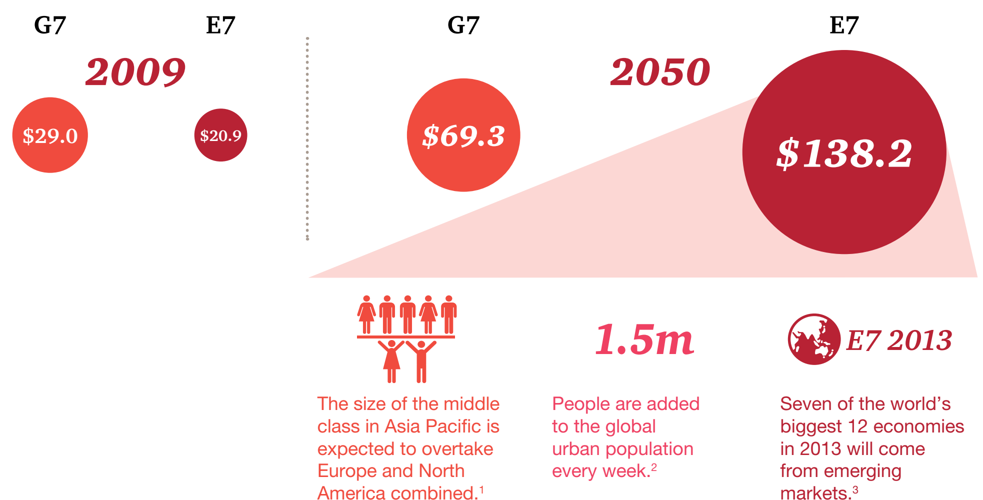
In this fourth *Japan Rebooted* publication, we aim to highlight the offshore opportunities on offer to Japanese firms if they can overcome the practical and psychological barriers that have been holding some back. We also aim to emphasise the opportunities for Australian companies to capitalise on the toehold Japan has in ASEAN in a way that could benefit both countries.

As can be seen in the accompanying graphic, GDP growth in the developing world is forecast to explode through to 2050 as emerging economies surpass the combined size of the developed world, creating a vast new middle class that will exceed the population of Europe and North America.

The need to act now to capitalise on the amazing opportunity offered by emerging markets has rarely been clearer as urbanisation and a growing consumer class in the developing world creates demand for products and services from the developed world.

Australian companies can learn a lot from the activities – both past and present – of the Japanese government, businesses and investors in Asia as it continues its journey towards this new frontier. In doing so, this may deliver new opportunities for Australian companies to develop strategic ties with Japan that are mutually beneficial for both countries in Asia.

Figure 1: GDP Growth of G7 versus E7 by 2050
Trillion GDP (GDP of G7 and E7 Countries at USD PPP)



Source: PwC Analysis, *The World in 2050: Will the shift in global economic power continue?* February 2015; **G7** – US, Japan, Germany, UK, France, Italy, Canada; **E7** – China, India, Brazil, Russia, Indonesia, Mexico, Turkey; 1. PwC World in 2000 Projection (2013); 2. UN Population Division, World Population prospects 2012; 3. United Nations, Department of Economic and Social Affairs, Population Division 2012

The next 40 years

*In this ASEAN issue of the **Japan Rebooted** series, we explore a large emerging region that is on Japan's doorstep and must be seen as a major consumer market rather than just an alternative manufacturing base to China.*

Now that Japan's foreign policy has elevated ASEAN to an unprecedented level of importance, Japanese firms have a great opportunity to secure offshore investment and earnings and underpin their futures.

The OECD estimates that ASEAN's growing middle class will account for 59 per cent of global middle-class consumption by 2030, up from just 23 per cent in 2009.

ASEAN's combined population is already larger than the European Union and the majority of its economies are surging while the developed world – with the notable exception of the US – largely sputters along.

Opportunities exist in providing consumer products, clothing, food, financial services, education and health care to increasingly discerning and demanding populations in South East Asia.

The steady tide of aid money from Japan into ASEAN countries has also opened the door to big opportunities in infrastructure provision for Japanese companies, whether it is in roads, ports and airports or electricity supply and other utilities.

The spectrum of sectors where Japanese firms could rapidly grow market share and insulate themselves against the demographics of the domestic market is huge, and includes: consumer finance, lending, retail, infrastructure, health care and even the arms industry.

But as we detail in this issue, time does not stand still. While no nation can rival Japan's aid contributions and active diplomacy in South East Asia, its corporations run the risk of being left behind by European and American rivals.

Japan's companies remain under pressure to develop corporate structures that will allow the devolution of responsibility and power to local subsidiaries to fully tap the energy, diversity, enthusiasm and potential of South East Asia.

In *ASEAN, As Best You Can*, we look at the achievements and deficiencies of corporate Japan's efforts in the region to date and pinpoint what needs to change for Japanese companies to more fully embrace the opportunities on offer.

We hope this publication serves as something of a wake-up call in terms of accelerating the internationalisation of Japanese companies and their ability to operate across all sectors of emerging markets and successfully integrate subsidiaries and create the kind of global enterprises that can dominate their sectors. At the same time, Australian companies should look to Japan as both a benchmark and strategic partner that ultimately supports their endeavours to gain closer access to new trade and investment opportunities in Asia.

ASEAN's growing middle class will account for 59% of global middle-class consumption by 2030.

The opportunity: ASEAN's phenomenal growth story

YOUNG, vibrant and rapidly growing, the ASEAN region is now central to the success of a host of global and Japanese companies. And it is not hard to see why. With GDP growth rates that are threatening to overtake China's, and a youthful, growing and increasingly educated population, the allure of the ASEAN markets is obvious.

The South East Asian bloc has come a long way since its formation in 1967 and now accounts for 8.8 per cent of the world's population. The combined GDP of the 10 ASEAN nations (Indonesia, Malaysia, Singapore, the Philippines, Thailand, Vietnam, Brunei, Cambodia, Laos and Myanmar), if taken as a single entity, would make it the sixth-largest economy in the world.

And when you consider that on OECD forecasts, growth in South East Asia between 2015 and 2019 is expected to average 5.6 per cent per annum, it makes this a part of the world in which multinational firms should have a strong presence.

While the region is comprised of countries at very different stages of development – consider Myanmar and Singapore for example – all are growing strongly (by the new global norms at least) and most are growing very quickly indeed.

Figure 2: GDP forecast, 2014-2019 CAGR
Calculated at current prices in USD

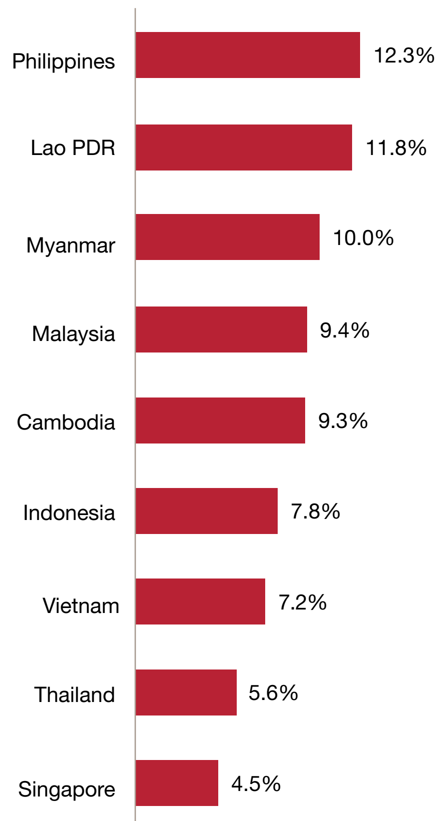
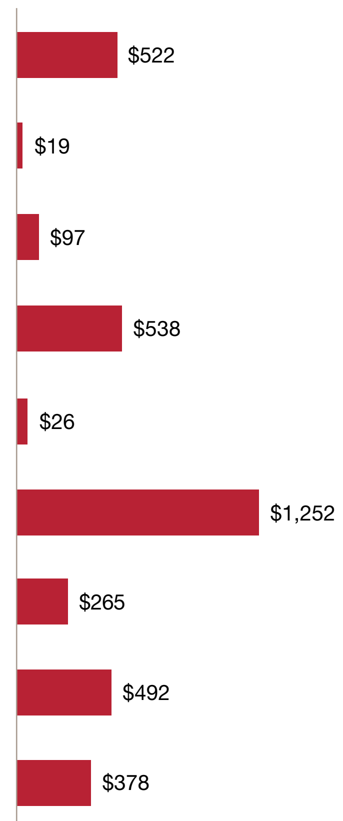


Figure 3: GDP estimate in 2019
Current prices in USD Billions



Source: IMF World Economic Outlook, US Census Bureau: International Programs

Figure 4: 2013-2020 real growth

Promising growth forecasts for 3 sectors of discretionary consumer spending in ASEAN through 2020

Communications ***+62%***

Education ***+59%***

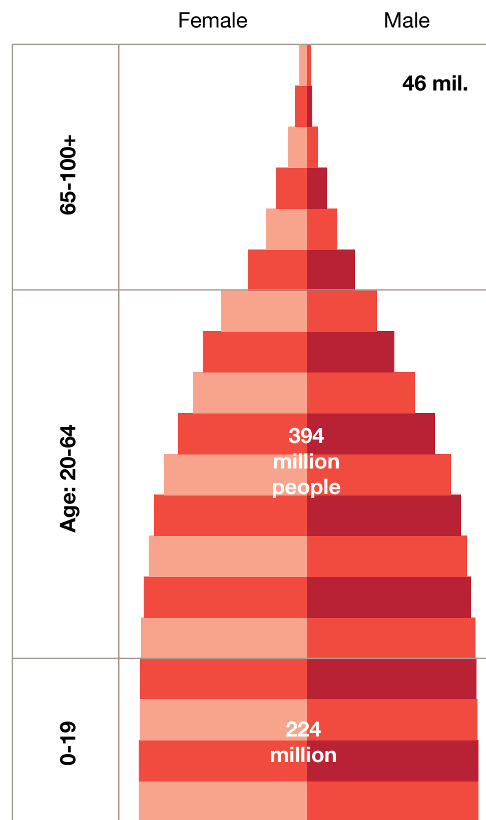
Hotels & Catering ***+51%***

Source: Euromonitor International

$2tn

ASEAN is forecast to reach $2 trillion in total consumer spending by 2020. $2 trillion represents a real growth of 45.7% over the 2013-20 period.

Figure 5: ASEAN population: 660 million forecasted by 2018
Breakdown by age group



Source: IMF World Economic Outlook, US Census Bureau International Programs

In ASEAN, consumer spending is expected to grow by 45 per cent between 2013 and 2020 with big gains in education, communications and hospitality, according to Euromonitor International forecasts. Put simply, the size of the consumer spending pie in the region is expected to hit $2 trillion by 2020.

As Asia's share of the global middle-class population grows from the current 30 per cent to an estimated 50 per cent or more by the end of this decade, global brands can sniff an enormous opportunity with some of the best gains likely to come in South East Asia.

While ASEAN's emerging nations have been seen in the past as great destinations for outsourcing of back office functions for global companies and, in some cases (particularly Thailand and Malaysia), as cost-effective manufacturing and assembly bases, the region is increasingly being seen as a consumer market in its own right.

Euromonitor International estimates that the number of households with an annual disposable income over $US10,000 (in constant terms) in the whole of ASEAN will reach 47.1 million in 2015, rising further to 63.9 million by 2020 and making it a consumer market that no global company can ignore.

The opportunities that come from feeding and educating this burgeoning middle class, and supplying a range of services from communications to leisure and health, will be immense. And as the wealth of these countries grows, so too will their populations' demand for dramatically upgraded infrastructure.

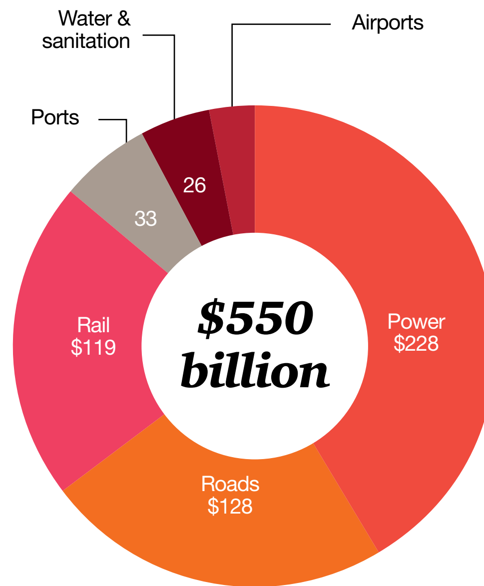
Goldman Sachs recently put the need for extra infrastructure investment in the region at $550 billion by 2020 in ASEAN's four largest economies – Indonesia, Malaysia, the Philippines and Thailand – with power, rail and road projects desperately needed throughout South East Asia.

Australian lawyer and infrastructure specialist Bob Seidler AM, the chairman of Hunter Phillip Japan, says that in ASEAN there is a vast infrastructure deficit that must be filled.

"Around the region the need for additional infrastructure, leave alone refurbished infrastructure, is enormous," he says. The Asian Development Bank estimates the unmet need for infrastructure investment in the decade 2010 to 2020 across Asia at $8 trillion.

"As many of the nations in the region move from an agrarian to industrialised economies, as the populations move from poor to middle class, they all want better services, better roads, better hospitals etcetera," Seidler says. "And if they are starting to trade goods, they need to have the ability to move people and goods so road, rail, airports and ports all become necessary. This is all about modernising these nations and improving the living standards of the people there so the need is enormous."

Figure 6: Projected need for infrastructure spending in ASEAN4, 2013-2020 $BN
Malaysia, Indonesia, Thailand, Philippines



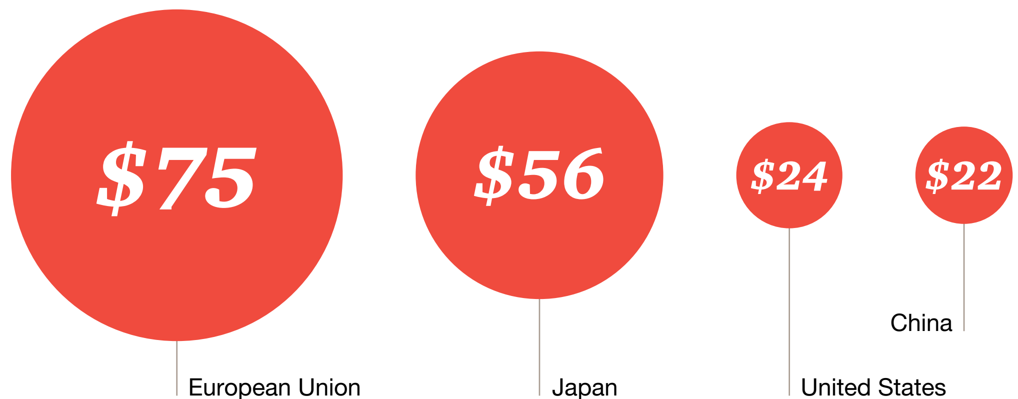
Source: Goldman Sachs

European companies have been the first movers in many of these ASEAN markets ploughing billions of dollars into the region in the past few years. But Japanese and US firms are now snapping at their heels as smart companies look to grab a share of the growth gripping a region that was, in the wake of the so-called Asian crisis of 1997, once avoided like the plague by corporate investors.

Singapore continues to see the bulk of the investment, accounting for half of the $120 billion investment in 2013, although this figure likely overstates the actual investment in Singapore as it is a transit point for capital that ultimately flows into other nations in the region.

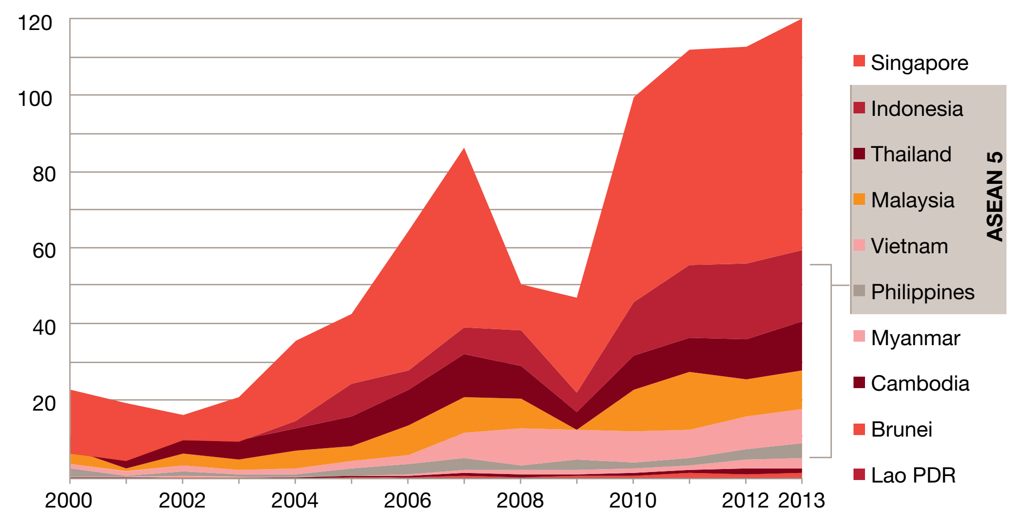
The ASEAN 5 nations make up most of the remaining half, with Myanmar, Cambodia, Laos and Brunei playing a very minor role as a destination for FDI. Although, it should be noted that for Myanmar, as discussed in a case study in this report, this situation is changing rapidly with foreign money, much of it from Japan, pouring into a country once touted as a potential food bowl of Asia.

Figure 7: Foreign direct investment, net inflows to ASEAN
2011-2013 in USD Billions



Source: Association of Southeast Asian Nations (asean.org)

Figure 8: Foreign direct investment, net inflows to ASEAN
USD Billions



Source: The World Bank

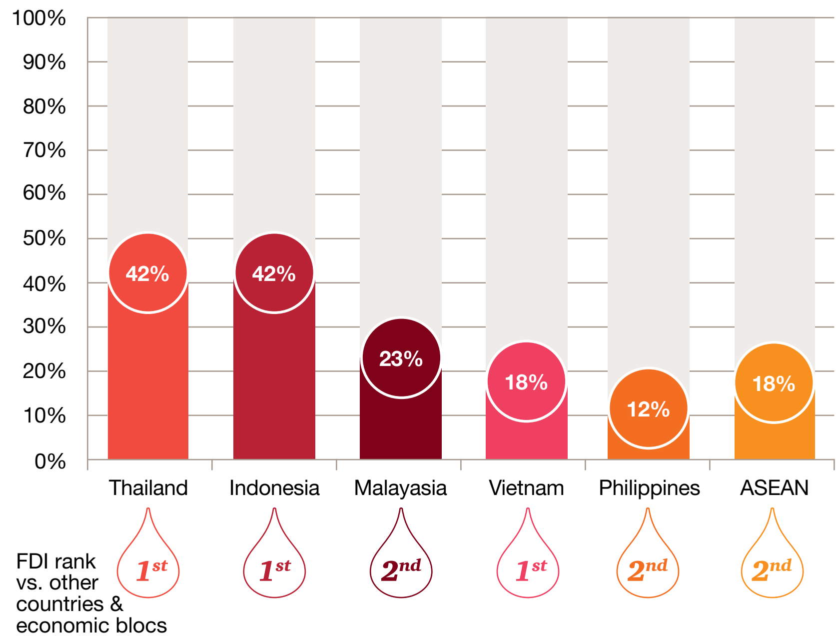
FDI from Japan into ASEAN nations jumped 120 per cent over the past year to $23.6 billion, according to the 2014 JETRO Global Trade and Investment Report. That's largely come at the expense of China, which saw Japanese foreign direct investment decrease by 33 per cent to $9.1 billion amid worsening ties between the two Asian powers and rising wages in Chinese factories. Overall, at least 58 per cent of Japan's FDI is now pouring into the four largest ASEAN economies, running at about twice what Japan is investing in China. Thanks to this surge of money, Japan is now the largest source of foreign capital for Thailand and Indonesia and the second largest in the Philippines and Malaysia.

Of course, this situation didn't happen overnight.

Japan has been conscious of the potential of ASEAN for years. Its development assistance in the region has been vast for decades and it is now clearly bearing fruit. Throughout the 1990s, Japan was the top foreign aid donor in the world, surpassing the United States in 1989. It has since lost the top spot but continues to be a massive donor in Asia, particularly in ASEAN.

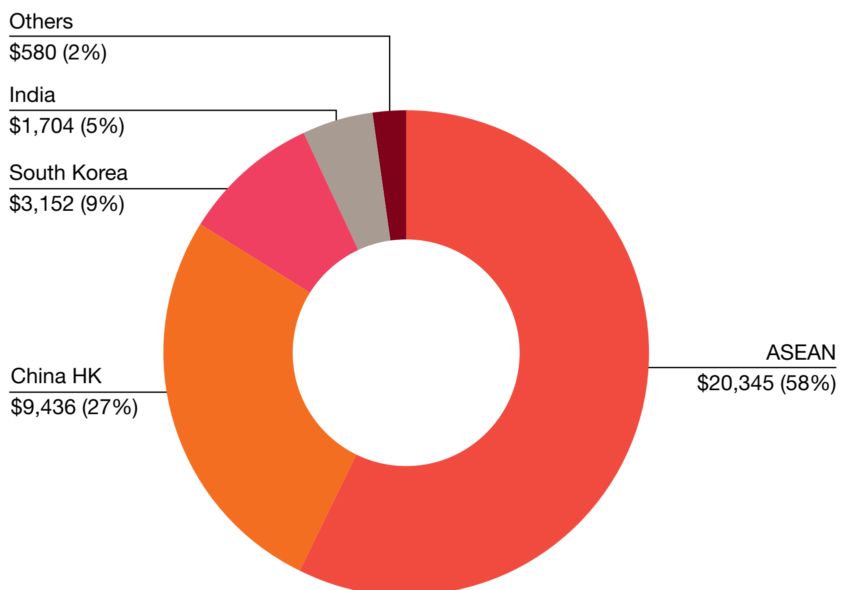
OECD data going back to 1960 shows Japan's cumulative development in aid in the Asia Pacific stood at more than $110 billion in 2012, more than double the next highest individual donor nation, the US. Two-thirds of its aid in Asia Pacific went to ASEAN nations.

Figure 9: Japanese FDI flow percentage of total FDI, 2005-2012



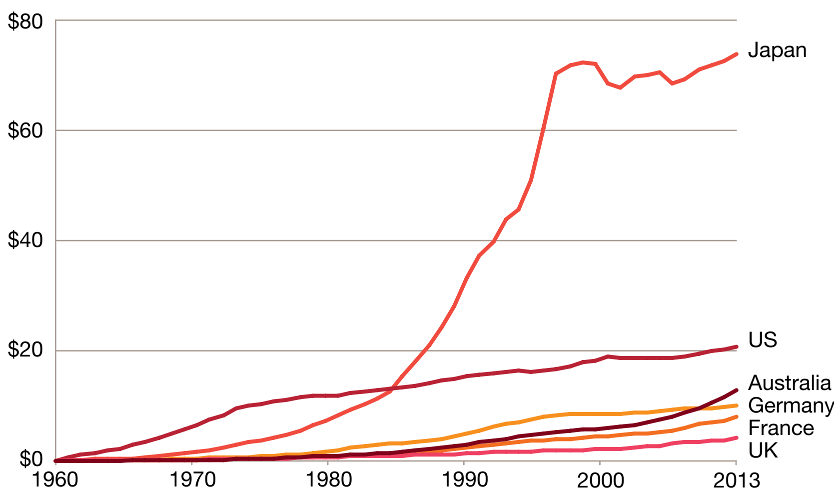
Source: ASEAN Statistical yearbook 2013, ASEAN total is for 2005-2013

Figure 10: Regional distribution of Japanese FDI to Asia, 2014
USD millions and as a percentage of regional total



Source: JETRO

Figure 11: Cumulative Net Official Development Assistance to ASEAN
USD Billions



Source: OECD

The election of Prime Minister Shinzo Abe in December 2012 gave Japan's diplomatic and economic efforts in ASEAN an immediate boost as he made clear his desire to establish a chain of friendly nations in the region, in part as a bulwark against China. Mr Abe visited all 10 members of ASEAN within his first year in office travelling to each of these countries before venturing to Australia, an important partner for Japan in terms of energy and food security and defence co-operation.

The legacy of the aid contributions, and the renewed interest in ASEAN in the Japanese government and corporate circles, has not gone unnoticed in the region.

A survey conducted in March last year for Japan's Ministry of Foreign Affairs that took in respondents in Indonesia, Malaysia, the Philippines, Singapore, Thailand, Vietnam, and Myanmar found that 96 per cent of those surveyed regarded it as important to have friendly relations with Japan.

More than 90 per cent regarded Japan as playing an active role in the development of Asia and making a proactive contribution to peace. Japan easily topped polls of which country was the most reliable, and which countries were regarded as important partners for ASEAN.

Surprisingly, China, the main rival to Japan and the US for influence in ASEAN, fared poorly in the survey and was rated by just 5 per cent of respondents as the most reliable country, compared to Japan (33 per cent) and the US (16 per cent). Similarly, Japan outstripped China in terms of who would be a more important partner for ASEAN both now and in the future. While the survey was funded by the Japanese government, it was conducted by a reputable pollster and the findings can be considered robust.

Japan: An important partner for ASEAN

The challenge for Japanese companies now is to convert this acceptance in ASEAN into business opportunities.

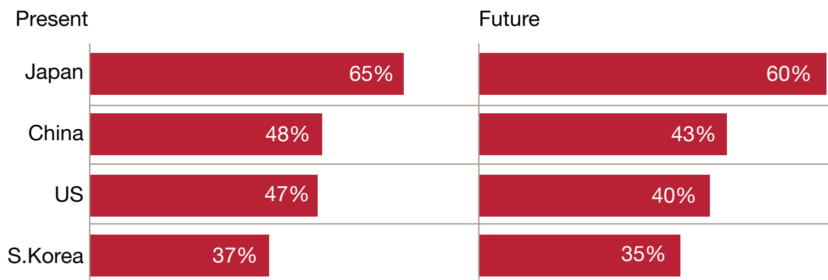
Japan development aid, as well as filling humanitarian needs, has also been a strategic investment and a form of economic diplomacy that Tokyo is now seeking to draw on to assist Japanese corporations abroad.

Whereas the vast rivers of aid from Tokyo may have initially come without strings attached, funding nowadays is contingent on projects having 50 per cent Japanese involvement.

This history of economic and political engagement in the region has created a bedrock of goodwill that companies are only just beginning to build on in ASEAN as more and more Japanese corporations grasp the imperative to invest overseas and build their offshore operations.

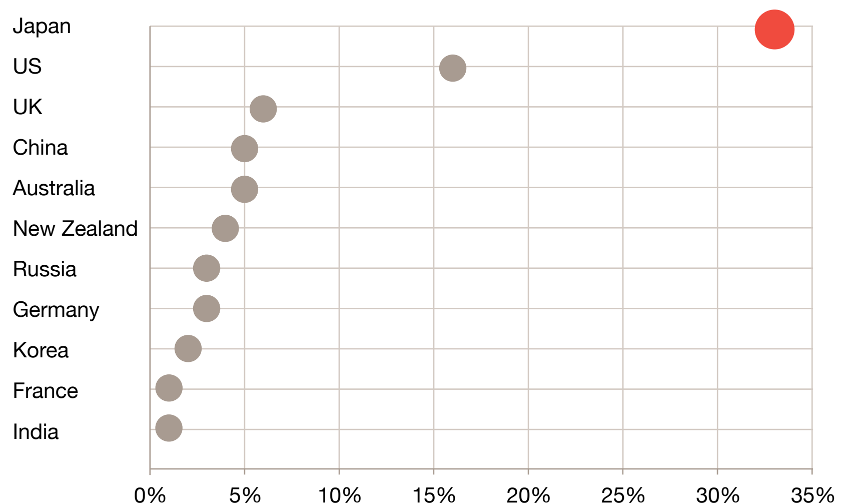
JETRO's annual survey of overseas orientated Japanese firms for FY2013 found strong enthusiasm for expansion in ASEAN. A poll of more than 1,000 respondents still had China listed as the main target for expansion (57 per cent) but almost 50 per cent of firms planned to expand in Thailand, 35 per cent in Indonesia and 30 per cent in Vietnam. Almost 20 per cent had plans to expand in Singapore.

Figure 12: Countries viewed as important partners for future ASEAN development



Source: JETRO

Figure 13: Countries considered to be most reliable for business



Source: JETRO

Countries and regions targeted for overseas expansion

76% of Japanese companies targeted ASEAN as a priority investment location in 2013.

Tracking the rise in sentiment towards ASEAN as a market, JETRO found that more than 50 per cent of Japanese firms surveyed saw Thailand and Indonesia as promising destinations for expansion and 44 per cent nominated Vietnam. More remarkable than the totals themselves, were the differences in these values from the 2008 survey where a far smaller fraction of firms (Indonesia 12 per cent, Thailand 21.8 per cent and Vietnam 16.3 per cent) identified the promise of ASEAN countries as markets.

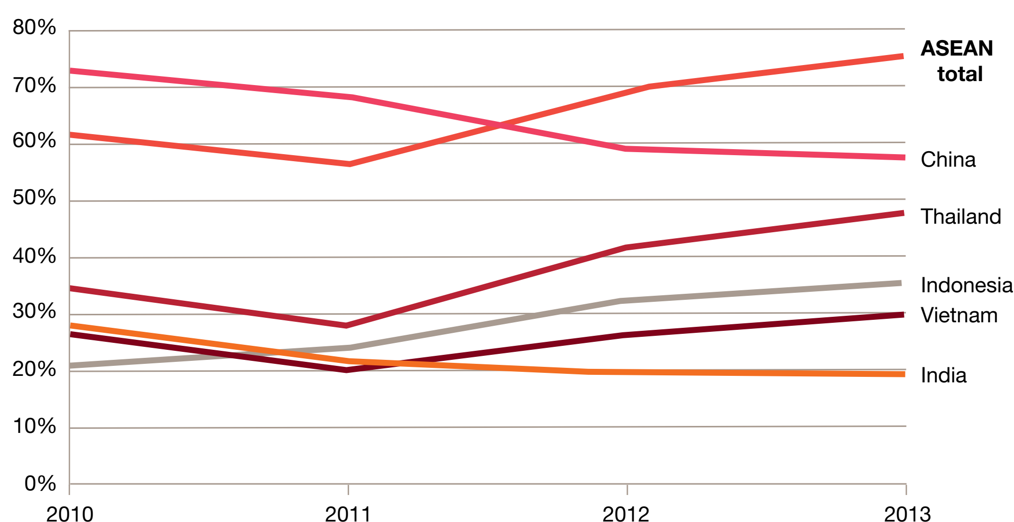
The other factor that may further increase the appeal of ASEAN to investors is the bloc's move towards economic unity by establishing an ASEAN Economic Community. The AEC aims to foster free trade between member nations and create harmonised standards and rules to make doing business in South East Asia easier. Few believe ASEAN will meet the end of 2015 deadline to achieve this goal, but most of the larger economies have already made many of the requisite changes. Tariffs on intra-regional trade have all but disappeared and product standards and regulations across the region are already quite consistent.

The AEC aims to emulate the successes of the European Union in terms of free trade and closer relationships, in a region that is already larger numerically in terms of population, without falling into the trap of a common currency.

PwC believes Japan needs to continue to push forward its plans and to seize this window of opportunity in ASEAN while it remains open. Just as US and European companies are already reaping dividends from their investment in South East Asia, the region's own large companies are becoming stronger and seeking to spread across – and dominate – the region.

Increasingly, FDI into ASEAN countries is coming from other ASEAN countries – led by Singapore and Malaysia based companies – as firms expand into neighbouring nations and the broader economic wellbeing of the region increases.

Figure 14: Countries of regions targeted by Japanese companies for overseas expansion



Source: JETRO (Feb. 2014) – FY 2013 Survey on the International Operations of Japanese Firms

Case study

The road to Mandalay: Myanmar rising

Myanmar is ASEAN's poorest nation, but it is rapidly becoming a vital target for Japanese investment. Japan Inc and the Japanese government view it as a long-term bet as the former dictatorship's reopening to the world pays dividends.

And in crafting its success in Myanmar, Japan has adroitly outpointed China, its principal rival in the region.

The list of blue chip names in Japanese corporate ranks keen to get involved in a nation once seen as the foodbowl of Asia – but crippled by decades of poverty and military rule – is impressive to say the least.

The Japan-Myanmar Association has grown since its inception in 2012 to include more than 130 corporate members including senior representatives from Marubeni, Mitsubishi, Sumitomo, Aeon, ANA, Hitachi, Kirin, Mitsui, Chiyoda, Lawson, Itochu, Bank of Tokyo-Mitsubishi UFJ, Sumitomo Mitsui Banking Corp and leading electronic, engineering, chemical and tourism companies.

Led by current and former politicans including ex prime minister Yasuhiro Nakasone, current deputy prime minister Taro Aso and former member of parliament Hideo Watanabe, the association is helping Japan's companies steal a march on their rivals.

A flurry of recent deals and announcements involving Japanese companies suggest it is working.

In late 2014, Japan's megabanks – Bank of Tokyo-Mitsubishi UFJ, Sumitomo Mitsui Banking Corp. and Mizuho Bank – were granted banking licences in Myanmar, along with Australia's ANZ and five other foreign banks.

PwC's Asia Pacific Financial Services leader Hugh Harley says that while these banking breakthroughs will help bolster Myanmar's global trade aspirations, Japanese firms are also helping revitalize Myanmar's run-down transport and energy infrastructure.

"Mandalay's airport is already run by a Mitsubishi Corporation and Jalux subsidiary and there are plans to turn it into a logistics hub," he says. "Mitsubishi is also heavily involved in the Thilawa Special Economic Zone. Marubeni recently announced its plans to build a high-tech coal fired powerplant in the south of Myanmar, which is rapidly finding it needs more generation capacity as its economy and living standards begin to grow."

Like its rivals, Japan has opened up a special economic zone. But experts say the Japan-backed Thilawa SEZ, a generous spread of land just 20 kilometres from Yangon (which features a port on the Indian Ocean) makes far more sense than the China-backed Kyaukphyu SEZ in remote Rakhine state and the Thai-based Dawei SEZ in the sparsely populated southeastern corner of the country.

PwC partner and infrastructure advisory specialist Mario D'Elia says the special economic zones, and the neat separation of investment that they have fostered, is a strategy that's working for Myanmar.

"The aid money has been split up. Japan's put money in, China has put money in and Thailand has put money in," he says.

"What Myanmar is saying is that Japanese money only goes to Japanese bidders, Chinese money to Chinese bidders and Thai money to Thai bidders. That process is running very well."

渋谷駅前

Every rose has its thorns: The challenges of ASEAN investment

It is easy, given the glittering allure of economic opportunities in ASEAN, for firms to underestimate the complexity, difficulty and challenges of buying or establishing a business in South East Asian markets.

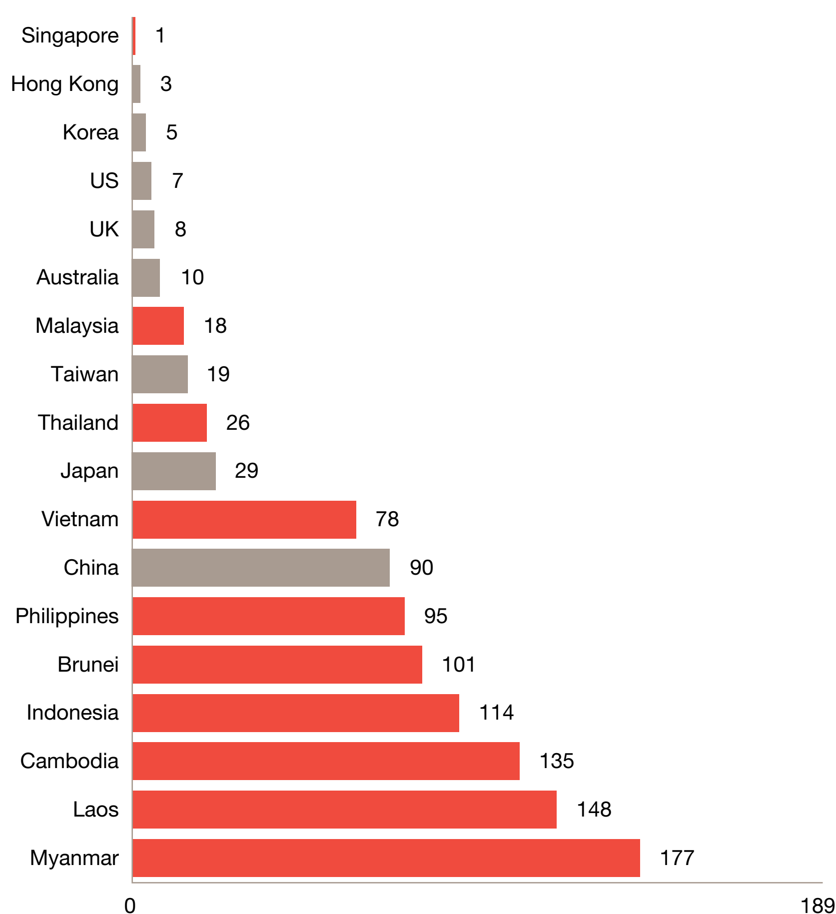
Yes, the region is booming, and its formidable growth and burgeoning middle-class population cannot be overlooked as sources of future growth.

But firms entering ASEAN should expect to encounter a completely different playing field when it comes to dealing with governments and regulators, as well as corporate rivals and the labour force.

Then there are the obvious infrastructure challenges in most ASEAN nations with clogged and dysfunctional roads and ports, and problems with the reliability of power supplies. As noted earlier, this presents opportunities for constructors and financiers, but for firms that have to operate in the region all the time, the pressure on overworked and dilapidated infrastructure can generate significant problems.

Figure 15: Ease of doing business

Ranking economies in 10 areas of business regulation with ASEAN highlighted in red



Source: World Bank Doing Business Guide 2015

While opening a subsidiary or regional headquarters in ultra-modern Singapore might pose few challenges, going further afield involves familiarising yourself with cultural differences, business practices, logistical issues and potential hiccups that can easily turn a good investment into one that struggles.

The World Bank's global rankings of the ease of doing business show that outside of world leaders Singapore (#1 ranking) and Malaysia (#18 ranking), the rest of ASEAN ranks towards the bottom of the table of 189 countries, with the honorable exception of Thailand, which ranks a more than respectable 26th.

It is also true that ASEAN suffers from more than its fair share of political instability. Thailand – the destination that has secured the lion's share of Japanese investment in recent years – has seen 15 coups in 33 years. The Philippines, Indonesia and even Malaysia have hardly been immune from political turmoil, although this has rarely had profound or lasting effects on those countries' economies.

70%

More than 70 per cent of Japanese companies in Asia and Oceania listed rising wages as a concern.

For Japan Inc, the appeal of ASEAN in the early years of investment was the low wages that allowed manufacturers to establish factories and export to the rest of the world. But now, wages – albeit off a low base – are increasing rapidly amid stiff competition in some markets for skilled employees.

Rising wages now ranks near the top of the list of concerns cited by Japanese executives in Asia responding to JETRO's annual survey of the international operations of Japanese firms.

More than 70 per cent of Japanese companies in Asia and Oceania listed rising wages as a concern, making it the dominant issue cited by corporate chiefs. Since then, wages have spiralled ever higher, comfortably outpacing growth in GDP.

Indonesia has topped the Asian wage growth table for two years running, posting a whopping 17 per cent increase in average wages for FY2013/14. Among other major ASEAN nations, Vietnam posted wage growth of 10.8 per cent while the Philippines and Thailand posted more modest increases of about 5 per cent, with Malaysia slightly behind at 4.8 per cent.

Growth in salaries across Asia and average labour costs

The other problem that has run in parallel with wage rises for Japanese firms in ASEAN is staff shortages with companies struggling to attract and retain key local hires. In some cases that may be due to cultural differences of working for a Japanese company, or the fact that many Japanese firms that are large and dominant entities in their home market don't have strong brand recognition abroad and thus may not be as appealing to staff as more well-known Western firms.

And in some countries, it is simply that there is a general shortage of staff to cope with the expansion of local and international businesses.

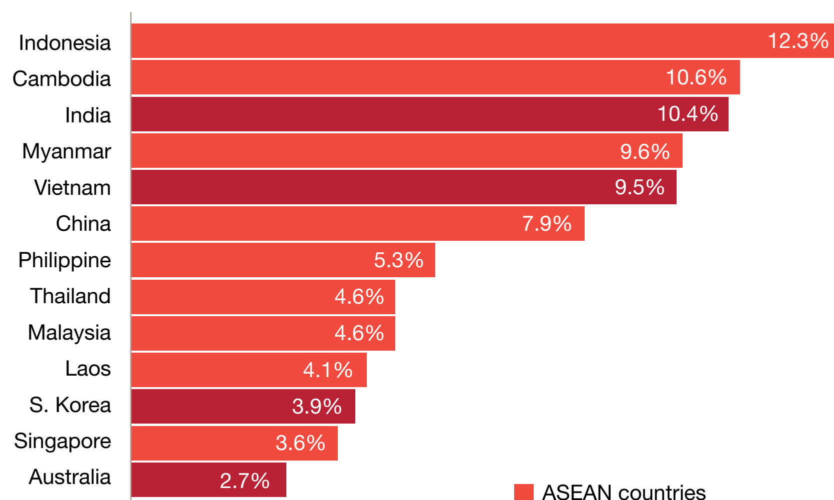
While corruption, wages and staff shortages – along with political and legal risks and poor infrastructure – are among the main problems cited by Japanese firms working in ASEAN, the situation differs markedly from country to country, reflecting the diversity of the region.

Not surprisingly, political risks are very much to the fore among firms in Thailand that have endured numerous rounds of civil tensions often culminating in coups and abrupt changes of government.

The 2011 floods in Thailand – which exposed the fragility of global and Japanese supply chains to environmental or disaster risks – remain prominent in companies' minds when it comes to the perils of investing there, along with rising wages. The typhoon prone Philippines also rates highly on natural disaster risks

Infrastructure problems dominate the complaints for Indonesia, Vietnam, the Philippines and Myanmar, while the legal system in Vietnam and Myanmar is cited as a concern.

Figure 16: Base salary growth rate y/y (%) 2014 to 2015



Source: JETRO Survey of Japanese – affiliated firms in Asia and Oceania (published December 2014)

Figure 17: Within ASEAN, Japan cites infrastructure, political risk and undeveloped legal systems as key business issues

Percentage of respondents

	ASEAN	Thailand	Malaysia	Indonesia	Philippines	Vietnam	Myanmar
Inadequate infrastructure	32.3	9.1	11.7	41.5	31.4	48.7	70.5
Political risks or problems in social conditions and law and order	25.2	46.4	5.7	22.6	23.2	8.20	32.7
Undeveloped legal system and problems in application of laws	19.6	7.1	7.1	24.5	12.2	31.9	42.5
High or rising labour costs	17.3	29.3	17.8	19.9	5.2	12.6	2.6
Natural disaster risks or environmental pollution problems	14.6	28.8	3.4	12.8	23.6	4.3	4.7
High level of exchange risk	14.9	13.1	11.8	21.8	11.6	15.7	12
Related industries not concentrated nor developed	10.9	2.1	7.1	9.4	11.6	17.9	28

Source: JETRO FY 2013 Survey on the International Operations of Japanese Firms (27 February 2014)

Striking sweet spots: Sector-specific opportunities in ASEAN

With conditions declining fast in the domestic market, investing heavily abroad is a case of do or die for many Japanese companies, even if they are yet to realise it. What's behind that imperative to invest abroad is the shrinking population at home. More than a quarter of the Japanese population is now aged over 65, and there are more than 50,000 people aged over 100 in Japan.

Over the next fifty years, Japan's population is forecast to drop from about 120 million to about 70 million people amid a decline in the birth-rate and a near-zero level of immigration.

As it strives to tackle the demographic issue, the Japanese government is actively encouraging Japanese firms to expand overseas into lucrative high-growth markets such as ASEAN, China and India.

As of 2011, Japanese FDI in ASEAN was dominated by manufacturing. Since then, that percentage has begun to slip as Japanese firms across a broader range of sectors – not just the electronic and auto giants – grasp the need to boost their presence in emerging markets before it's too late.

Deal activity has continued to reach new heights in recent years as Japanese firms make acquisitions and investments in a range of sectors from resources and infrastructure to finance and healthcare, but many opportunities are going unfulfilled.

To help firms better assess potentially lucrative niches, below we have assessed the performance of Japanese firms in a range of important sectors where ASEAN nations are likely to see ongoing development and investment from abroad.

Finance sector

Japan's megabanks had been conservative in terms of expanding into emerging markets, PwC-Japan's Financial Services industry leader Takeshi Shimizu says.

But Shimizu says now that several of the main players have made moves more acquisitions are likely. The deal that really set the ball rolling was the Bank of Tokyo – Mitsubishi UFJ's $5.6 billion takeover of Thailand's Thai Bank of Ayudhya – the Japanese giant's first foray into Asian retail banking outside its home country. Along with giving BTMU a growth platform in a fast-growing ASEAN economy, the deal provides the opportunity to supply financial services to firms in Vietnam, Laos, Cambodia and Myanmar and capture corporate and consumer driven demand in South East Asia.

The purchase diversifies BTMU's geographic mix and gives the bank a fully fledged commercial banking platform in Asia. Through acquiring the controlling stake in the Thai lender, BTMU has become the first Japanese company allowed to operate a local Thai bank as a foreigner. The Bank of Ayudhya's highly experienced management team was viewed as a strategic advantage of the purchase. The deal is also expected to be a boon for other Japanese companies operating in Thailand, many of whom have existing relationships with BTMU in their homeland.

For fellow megabank, Sumitomo Mitsui Financial Group, its $1.5 billion purchase of a 40 per cent stake in Indonesia lender PT Bank Tabungan Pensiunan Nasional (BTPN) in 2013 was the company's largest foreign purchase at the time. SMFG has since followed this up by buying a 12.25 per cent stake in Cambodia's largest lender by assets, ACLEDA Bank in August last year. That deal was one of the first major investments in Cambodia's financial sector by a large

The Japanese government is actively encouraging Japanese firms to expand into lucrative high-growth markets such as ASEAN, China and India.

$5.6bn

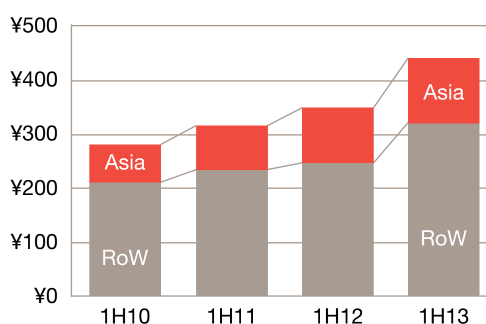
In late 2013, Mitsubishi UFJ Financial Group acquired a controlling stake (72%) in Thailand's Bank of Ayudhya (BAY) for 171 billion baht.

multinational, although Japanese financial services firm Orix also bought a stake in the Cambodian bank in 2013.

For Japanese lenders, this is not before time. Rivals in the region have certainly not been standing still.

Banks from Malaysia and Singapore, the most sophisticated and stable economies in ASEAN, have been expanding busily with the aim of becoming regional financial powerhouses. These include CIMB and MayBank in Malaysia, and DBS and OCBC in Singapore.

Figure 18: MUFG's overseas gross profit by region (¥BN)
1H FY2010 – 1H FY2013; Asia 10.2% CAGR

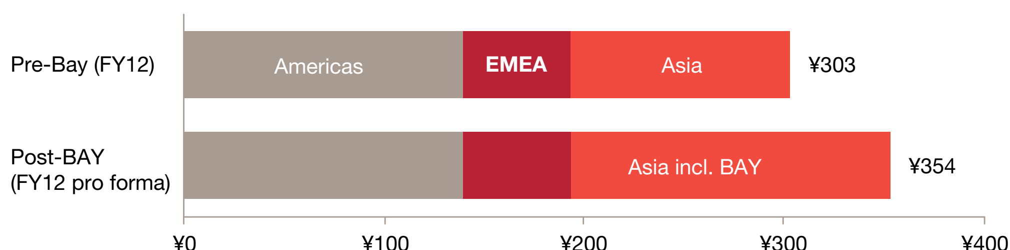


For Masaaki Amma, the executive managing officer of the Japanese government's international lender Japan Bank of International Cooperation (JBIC), Japan's megabanks have already established excellent servicing networks to take care of their Japanese clients' needs overseas, but they need to sprint quickly to keep up with their international rivals in tapping growth created by local companies and consumers in ASEAN, but also in India and China.

"Japanese megabanks should at least cover China, India and ASEAN, which are the fastest growing regions and the most important to their Japanese clients, and compete with non-Japanese banks as well" he says.

"They have finally embarked upon that point. BTMU have just acquired the Thai Bank of Ayudha and SMBC (Sumitomo Mitsui's wholly owned banking subsidiary) have just acquired 40 per cent of BTPN, which is a very unique microfinancing bank in Indonesia. The three megabanks in Japan have already acquired equity stakes in Vietnamese banks, but because they have started relatively late, it will take time to catch up."

Figure 19: MUFG overseas net operating profit comparision, post-Bank of Ayudhya (BAY) deal
¥BN



Source: Company Reports, PwC Analysis
Note: USD/JPY Rate is PwC FY14 exchange rate of 96

Infrastructure

PwC partner and Infrastructure advisory specialist Mario D'Elia says Japan's trading houses have historically been the most active players in terms of infrastructure investment abroad, partly because of the lack of international ambition of general construction firms.

A recent example of a trading house playing an innovative lead role in an ASEAN infrastructure project can be seen in the case study in this publication on Mitsui's Malaysian power plant deal.

Mitsui has also had a long history of involvement in power stations in Indonesia, constructing a major thermal power plant there in the mid to late 90s and following that up recently with the commissioning in 2012 of the Paiton III super-critical coal fired power station.

More recently, Marubeni appears to have clinched a deal to build a $3.2 billion supercritical coal-fired power plant in Myanmar to supply power to the former dictatorship, which is suffering crippling electricity shortages, and to Thailand too. The project is a joint venture with Thailand's state-owned oil company, PTT, along with the Electricity Generating Authority of Thailand and a construction company in Myanmar with the aim to break ground for the facility by 2016 and begin operations in 2020.

D'Elia says Japanese firms are also involved in gas-fired power plants in Vietnam, desalination plants in Singapore and telecommunications projects in Indonesia.

"While these projects are significant successes, they don't even scratch the surface in terms of the need for infrastructure in ASEAN with the need for new roads, rail, sewage, electricity and port and airport infrastructure," he says.

As the Abe government continues to pledge billions of dollars in aid for India and Bangladesh and in South East Asia, Japanese companies will be looking to win contracts, specifically in rail, ports and other infrastructure projects. Japan's national rail operators are battling with Chinese companies for new high-speed rail projects in India and across Southeast Asia, including an ambitious $12 billion project to connect Kuala Lumpur with Singapore.

While there is no doubting the demand for infrastructure, the problem for the time being, according Hunter Phillip Japan's Bob Seidler, is accessing the funding. Government's simply don't have the money in some cases and the public is often too impoverished to pay tolls or user charges.

"The other option, which is the more likely one around the region for some time, is aid money. It is simple – Indonesia, Philippines, Malaysia, India – all of them have a limited availability of money, so they simply can't meet their needs. They can do some of it, and the balance will have to come from aid money," he says.

D'Elia agrees affordability is an issue: "Someone has to pay for it. You can push out the payments and have user pays, but in these countries 10c is a lot of money for some people. It is a struggle to be able to build new infrastructure and to be able to afford to do it," he says.

"Then there is the question of how you can tie up with locals. It's often necessary to have strong local involvement to make the project meet political and societal expectations. Japan was successful in Malaysia by doing that," he says.

"But often when Japanese go into these joint ventures they tend to take a back seat.

"It is not just technical solutions, it is financial solutions, it's local solutions. I think they have struggled with that."

"I think they still have this mothership mentality because it is all co-ordinated from Japan. Asia is lots and lots of different countries and regions. If you are trying to control it out of head office without devolving responsibility you are going to struggle."

Marubeni appears to have clinched a deal to build a $3.2b supercritical coal-fired power plant in Myanmar.

“So there is no substantial reduction of cost in operation and maintenance. The current Japanese model per se cannot be exported to other Asian regions.”

Masaaki Amma, Japan Bank of International Cooperation (JBIC)

According to Masaaki Amma of JBIC, Japan needs to work hard to reduce the cost of delivering its style of infrastructure services and to explain the benefits of its approach to providing high quality maintenance and operational services.

“There is a huge demand for infrastructure, but the capital cost of Japanese infrastructure is too expensive,” he says. “However the good part of Japanese infrastructure is the very, very highly effective operation and maintenance… so for a life-cycle cost basis it is very (cost) effective.

“But we haven’t really pushed and made ourselves understood yet.”

Amma says Japan needs to get the model right at home first to strip back regulation and encourage private sector innovation.

“We have long privatised infrastructure in the railways, power and gas utilities, but we don’t see any private operators for water, airports and ports and highways. Japanese Private Finance Initiative (PFI) in the domestic market – it is really construction only. They didn’t really address the issue of operation and maintenance.

“So there is no substantial reduction of cost in operation and maintenance. The current Japanese PFI model per se cannot be exported to other Asian regions.

“What we need to see in the Asian region is a higher number of deals in private infrastructure – which should include the outsourcing of operation and maintenance works to the private sector.”

Amma says firms such as Hitachi are understanding the need to supply not just a piece of infrastructure, but rather an infrastructure solution that fulfils the customer’s needs as a whole and generates better returns for the provider.

Case study

Mitsui's Malaysian power plant deal

A deal involving Japan's Mitsui and the Malaysian government – put together with the help of PwC – to build a 2,000MW super-critical coal-fired power plant highlights how PPP projects can succeed with the right advice. The Energy Commission of Malaysia was keen to get foreign expertise in the project and to foster a competitive bidding process to help drive down the cost of the Jimah East Power project.

PwC's Mario D'Elia, a partner in the firm's Australian infrastructure advisory practice, worked extensively on the deal to help the Commission structure a bidding and selection process that garnered trust from bidders and highly competitive tenders.

"The first objective of the government was to get international capability involved and to internationalise the sector which has been dominated by domestic players," D'Elia says.

"We took a whole lot of information and needs and structured it into a request for proposal that a lot of bidders were interested in. It had finance cost certainty, construction cost certainty, intellectual property certainty and no leaks in the tender process.

"Having our brand name there was able to provide more prominence and reliability. Our experience in doing projects and asking for the right information and kept the project very tight."

Ultimately, a consortium involving Japan's Mitsui emerged the winner in the $3.6 billion tender process with a sophisticated bid that melded Japanese technology, a local partner (1MDB) and creative solutions on finance.

"They were able to bring Japanese technological capability to the table along with a debt package that included JBIC, Islamic finance and a corporate loan as well," D'Elia says.

"To me the key was the flexibility that Mitsui displayed dealing with so many different parties and cultures and the use of Islamic finance, which are all new things for them."

The tender to build the power plant, at Mukim Jimah in the state of Negeri Sembilan, succeeded – according to D'Elia – because the government decided to consult on setting up ground rules and processes that would ensure international interest and inspire trust

"A lot of times governments put out projects that haven't been thought out. They are just not viable and don't work," D'Elia says. "The type of work we have had in Malaysia is bringing that private sector experience into a public sector project.

"It has allowed people to put in a much more competitive bid than they otherwise could.

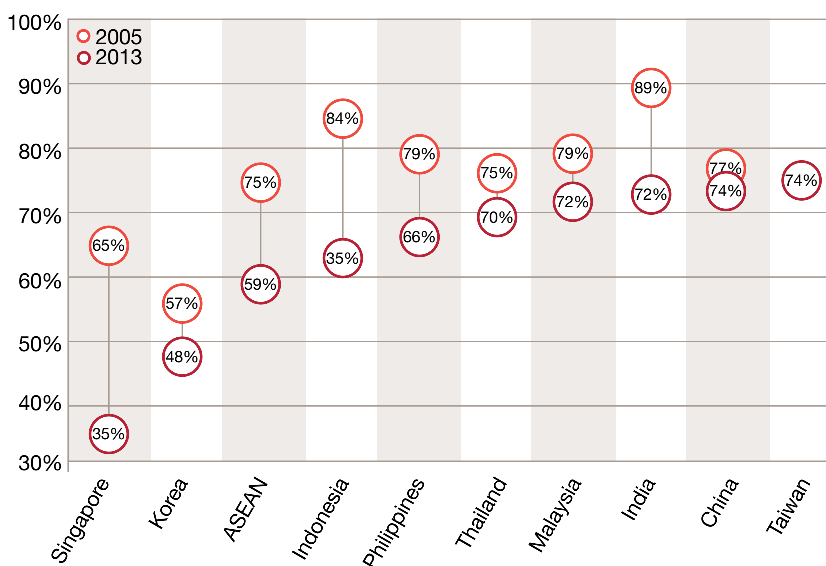
"If it is a questionable process, bidders put their B-team on it because they don't think it will get up. Our role was to make sure that people were comfortable to have their A-team bid and really go for it."

Manufacturing – a reality check

Manufacturing – particularly of high-tech electronic goods and automobiles – has been Japan's bread and butter for a generation. In the latest iteration of this business, Japanese firms have invested heavily in the ASEAN region to take advantage of opportunities for low-cost production.

The figures in the chart show the heavy concentration of FDI in this sector, but the trend is towards investments in consumer and services sectors. As ASEAN nations become increasingly seen as consumer markets, this investment will have the synergy of having production located close to the point of sales.

Figure 20: Japanese Manufacturing FDI stock as a percentage of Total FDI stock



Source: Bank of Japan

According to Amma, the logistics of the ASEAN-wide Japanese supply chain have created a clear competitive advantage with the network of suppliers and producers and distributors representing a key strength for Japanese industry, as it tackles potentially lucrative markets in China and India where it either lacks penetration or is being outpointed by products from South Korea or those produced locally in the case of China.

"In terms of manufacturing industry in Asia, the biggest and most valuable asset for Japan and South East Asia as a whole is the very unique de facto production and distribution networks, which is characterised by 'fragmentation and agglomeration'" he says.

"Actually Japan is the biggest beneficiary of this production network. Korea and Taiwan and Singapore too."

The challenge for Japan's manufacturers, Amma says, is to leverage the power of this network as a first step into establishing bigger presences in China and India.

"So far, even now, this production network is still not really connected yet to the domestic Chinese market or the Indian domestic market," he says.

"Our agenda as manufacturers is: how can we improve this asset, how can we can improve this network to capture future incremental growth in India and China.

"Japanese companies can still do a lot in establishing a more dominant presence in China because maybe in 20 or 30 years, the company that dominates the Chinese or Indian markets will dominate the world market.

"But Japanese electrical household products manufacturers are not doing well in China or India – they are relatively (being) left behind by LG and Samsung."

In automobile manufacturing, Amma says Japanese auto assemblers should be able to better their market share by approximately 10 per cent in China, where they are being left behind by Volkswagen.

"Japanese companies have very good technology and they are very competitive in the developed world (however) they are not fully committed yet to the Chinese and Indian markets – but they should try," he says.

"There are two options – either they should fully compete with Chinese and Indian manufacturers, low cost producers; or they should partner with them or utilise more local human resources.

"They need to come up with a very new production technique which should be cost effective in China, but my view is that Japanese manufacturing companies haven't really tackled this critical problem.

"They are still trying to stick to the old convention – highly value-added, highly functional products. Some of them are just waiting for the lower-income consumers to rise up to the middle class and buy their expensive products in future – but it is not so simple. In the Japanese market too, they have been growing together with Japanese consumers, who never bought non-Japanese electrical appliances. So they have to change a little, or sometimes drastically, the specifications, the utility and the pricing."

While issues remain with penetration into the two mega markets of the future, Japanese firms continue to gather momentum in the emerging markets of the ASEAN region.

Retail

Japan's leading retailers have been actively expanding in ASEAN countries and have ambitious plans to increase the pace of their push into some of the region's most promising consumer markets.

At the head of this retail expansion have been convenience store operators who have capitalised on their world-class performance in this category to roll out networks in parts of ASEAN, often partnering with local operators.

The major players (FamilyMart, Lawson and 7-Eleven) all have a significant presence in Thailand now and are expanding into Indonesia, the Philippines and other parts of ASEAN as South East Asia warms to the notion of the peerless Japanese-style convenience store. Lawson has announced it has a goal of opening 5,000 stores in ASEAN by 2018.

For the major players, the Philippines is now a key zone for expansion with Lawson announcing plans to build a network of 500 outlets by 2020 by combining with local retailer Puregold Price Club. According to Japan's Nikkei newspaper, 7-Eleven leads the pack with more than 1,000 stores in 2013, while FamilyMart operates 40 or so outlets and plans to open 100 new shops in fiscal 2014. Ministop, with about 410 stores, will add roughly 50 locations.

In the supermarket sector, Aeon, plans to double its sales in South East Asia over the next three years to ¥500 billion ($4.3 billion) by expanding from its regional base in Malaysia, while growing the number of outlets by 10 per cent to 144.

Japanese fast food companies, despite having strong and easily duplicated systems and attractive menus, have been slow in expanding beyond Korea and China and into ASEAN nations. Nonetheless, beef bowl giants Yoshinoya and Zensho Group (Sukiya) have some stores in the region, as does Mosburger, but the potential for further growth is obvious and untapped.

In the clothing retail segment, Uniqlo has been more proactive in terms of expanding into ASEAN with more than 80 stores in five of the 10 member countries. The president of Fast Retailing, the label's parent company, says ASEAN could become as big as China (with 330 stores) and South Korea (137 stores) for Uniqlo.

Tadashi Yanai's company has recently sought listing on the Hong Kong stock exchange as it continues with its expansion plans across Asia.

Japanese firms continue to gather momentum in the emerging markets of the ASEAN region.

Health care

Exporting healthcare services and technology remains a promising – and mostly untapped – niche for Japanese industry. Japan boasts a well regarded and innovative health care sector with leading global companies in pharmaceuticals and optical devices and other aspects of patient care.

These companies have made inroads in increasing the proportion of global sales in their revenue mix, but few Japanese companies have taken their skills in running hospitals into South East Asia, with the exception of Mitsui.

Through its 2011 acquisition of 30 per cent of Malaysia's Integrated Healthcare Holdings, the trading house is building a chain of clinics and hospitals across ASEAN to capitalise on increasing disposable income that leaves people able to pay for private hospital treatment in countries where the public alternative is often poor.

Seizing the opportunities

Looking at a snapshot of Japan's current presence in ASEAN it is difficult not to conclude that it is very much a job half done, or perhaps not even that.

Few firms can be said to have fully positioned themselves to reap the profits of ASEAN's projected growth and thus safeguard their firm's longevity against this backdrop of domestic decline.

So what is holding Japan back? And what more must companies do to seize the opportunities on offer.

According to JBIC's Masaaki Amma, Japan has already missed the boat in terms of organically growing business in ASEAN and must rapidly increase its efforts to acquire the right business in South East Asia and other emerging markets such as India and China.

"Acquisition is the only solution. At this stage it is too late – they cannot really start from scratch," he says. "They need to make a very quick decision so they (can) challenge difficult markets and countries."

PwC believes Amma is right in saying most Japanese firms that expand in ASEAN will do so via M&A. Building a business from scratch simply takes too long and is too difficult in most cases.

Yet even with a strong desire to expand in Asia, full board and management support, and cash to spend, finding and executing a deal in ASEAN is not always a simple task.

PwC partner Ken Kawamura says acquiring a business in South East Asia will usually pit a company against its Japanese and international peers, and local companies.

"This is true as corporations from the United States begin to invest heavily in South East Asia's more developed markets, such as Singapore, Thailand, Malaysia, and increasingly Indonesia," he says. "International private equity firms have likewise targeted the sub-region, raising funds and opening local offices to search out both minority stakes and buyout opportunities," he says.

"Another bottleneck to sourcing deals is the limited number of quality targets that are available. Singapore, Thailand, and Malaysia are populated with a rich mix of mature companies with higher governance standards than those in frontier markets, (but) potential deal targets are far fewer than in more developed jurisdictions."

The other challenge is in acquiring reliable and up-to-date information in the pre-deal process. Intelligence on targets can be gained from within their contact network, but often local advisors are needed to provide an accurate picture of the transaction and the target's market position and standing.

Potential acquisition targets in ASEAN will often be family-run businesses, which tends to pose a series of challenges to acquirers, particularly if the seller is to be involved in the business post sale.

On the other hand, family companies may readily see the merit in bringing on a large Japanese corporation as a means of addressing succession issues, bringing in new technology, conquering new markets or unlocking capital from the business.

"They need to make a very quick decision so they (can) challenge difficult markets and countries."

Masaaki Amma, JBIC

However, “the existing operating and organizational structures at many family companies can present challenges for an investor,” PwC partner Matt Wyborn warns.

“It is important to obtain an understanding of the controls in place over compliance and governance matters, while also ensuring that related parties and other key relationships or connections are identified. Diligence also needs to focus on gaining an understanding of the quality, timeliness and reliability of financial and regulatory reporting,” he says.

“The first-class European and American companies, they have already started PMI before the acquisition, maybe six months before.”

Masaaki Amma, JBIC

“With individual sellers, extra thought needs to be given to post-transaction remedies. It can be difficult to pursue individuals in the courts and they may not always have the financial resources to meet any claims brought against them.”

With the right advice, these issues can be managed and successful transactions achieved in ASEAN for Japanese companies.

Acquisition alone, though, is not always the silver bullet that Japanese firms hope it will be.

The problem is – as discussed in the third publication in the Japan Rebooted series – is that most firms have a poor track record in terms of integration of subsidiaries in the wake of acquisitions and lag well behind their American and European counterparts.

“Post-merger integration is a very big problem,” Amma says. “Some Japanese companies have basically no strategy at all with PMI, they just acquire and accept existing management, that’s all.

“They haven’t really even started with (exploiting) synergies, which is the first point of M&A.

“The first-class European and American companies, they have already started PMI before the acquisition, maybe six months before. When they acquire, they are really committed to changing the company within three months. (But) even in such a short period, the existing employees of the acquired company are usually satisfied with the new management structure. They are very happy and they don’t leave the new company.”

Although 70 per cent of Japanese companies surveyed by JETRO responded positively to delegating authority to local staff, three quarters of them said they had not set up any pathway for locally hired employees to become executives in the company’s head office.

More than 70 per cent of firms surveyed admitted there was no global standard across the group on how new executives should be chosen and which candidates deserved promotion.

Japanese firms also report difficulty hiring in ASEAN saying that sometimes their dominant brand power in Japan doesn’t translate to immediate recognition in South East Asia and there is higher turnover when they hire foreign staff.

Other difficulties include language problems (in Japanese and English) of new hires in ASEAN as well as the difficulty of reducing the number of expatriate Japanese staff to make way for locals.

Firms say they are working on ways to delegate authority and autonomy to regional operations to make them more flexible and appealing places to work, but there is still a reluctance to cede control and to reduce the overall headcount of employees in Japan.

The halfway house that most companies have adopted is to have a regional headquarters in Singapore, ASEAN's most stable, wealthy and advanced member. The RHQ then runs the ASEAN or Asia Pacific operations with some degree of autonomy. Along with stability and sophistication, Singapore offers good infrastructure, tax incentives, low trade barriers and quality staff, as well as the active engagement of the Economic Development Board in attracting and retaining investment. Singapore is a clear first choice for establishing a regional beachhead with the only downsides seen as the relatively high wage costs, rent and the intense competition for staff with other Japanese, local and multinational firms.

The rising popularity of a Singapore base can be seen in the 350 per cent rise in the number of inquiries between 2009 and 2011 to JETRO's branch office in the city state.

The EDB's assistant managing director, Lim Swee Nian, says Japanese companies are also choosing Singapore as a base for research and development due to the strong research talent available.

"Takasago, Bandai Namco, Shogakukan and Rakuten are examples of Japanese companies that have chosen to leverage Singapore as a product development hub for the region," he said.

Lim says the EDB is also aiming to make Singapore a hub for infrastructure expertise in ASEAN. "Multinational companies such as Hitachi have chosen to base their infrastructure regional headquarters in Singapore," he says. "Multinationals in Singapore are also leveraging our city to develop, test and commercialise smart sustainable city solutions to meet the needs of rapid urbanisation of Asia."

Singapore's network of free trade agreements (FTAs) with more than 32 different nations and its central position make it an obvious logistics hub. The other advantage of Singapore, according to Lim, is its livability. Great transport and housing, and dependable utilities and infrastructure, have helped it to win consistent plaudits in expatriate staff surveys on the quality of life in Asian cities.

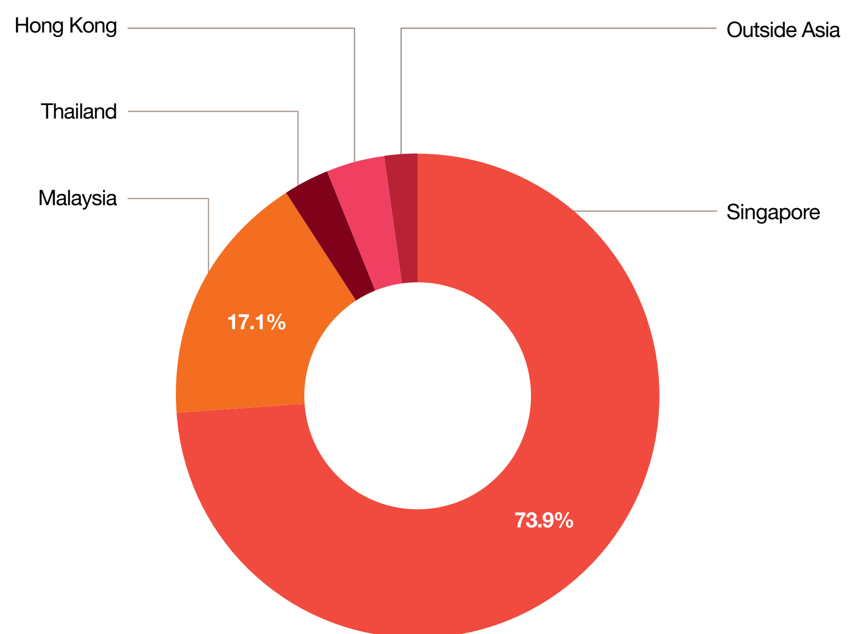
Despite the challenges and the inevitable tensions with head office, the system of having a regional headquarters, with a shared service centre in many cases, seems to be working for Japan with most firms (according to JETRO data) saying investing in ASEAN is what they expected or more.

While Singapore, and to a lesser extent Malaysia, dominate as the preferred location of RHQs for Japanese companies, the majority of firms still run their ASEAN operations out of Japan.

This is in contrast to international rivals who have been more proactive in establishing autonomous operations in ASEAN, particularly those who have been active in the region for a long time.

Figure 21: Location for managing ASEAN operations by Japanese companies (percentage of respondents)

Results are only for non-ASEAN Companies



Source: The Economist

Case study

Kirin's ASEAN experience

Brewing giant Kirin is typical of many Japanese firms in being acutely aware of the decline of its home market and is focused on capturing a growth opportunity in South East Asia.

Kirin's management has purchased large subsidiaries in Australia (Lion) and Brazil (Schincariol) to help bolster profitability over the medium term.

But it expects to find a major growth opportunity in the developing world, most likely in the ASEAN region.

Kirin Asia Pacific president Hiroshi Fujikawa says the company's Asian expansion plan is being run out of its regional headquarters in Singapore, the economic heart of ASEAN.

"The current focus is to maintain and improve position in Vietnam and Thailand, and may also consider opportunities to increase beer distribution across South East Asian markets," he says.

Kirin has a minor presence in Vietnam and Thailand for juice and tea products, but the hunt for bigger fish is on.

In the meantime, the company has amassed a body of knowledge about the risks and benefits, and practices that work and don't work, when operating in ASEAN.

"It takes time to become competitive in new markets, a long term view is essential," Fujikawa says. "Global competitors already have a good brand and system that provides them with a significant advantage.

"Local competitors on the other hand have a cost efficient business and local knowledge and are therefore in a stronger position than a new market entrant."

"So taking the time to understand how to 'win' in a new market is critical, especially for a company like Kirin, which sits in between the global majors and the local leaders.

Fujikawa says local partners are often the key to success, but companies need to understand these are often family owned companies that can be resistant to change.

Conducting due diligence on every aspect of the business prior to purchase is vital, as is establishing structures to run the operation properly.

"When you acquire a business in a developed market, like Lion Nathan, you can leave it to run, but finding the number one or number two operator and acquiring 100 per cent of that company in Asia is not easy," Fujikawa says.

"So one approach might be to acquire, or partner with, a relatively weaker business and implement your systems and processes."

When it comes to ASEAN and other developing markets, perhaps the biggest – and often neglected – challenge, according to Fujikawa, is the human and cultural side of the equation.

Like other Japanese companies bent on offshore expansion, Kirin is finding a dearth of executives and managers within its ranks who are able and willing to work in foreign markets.

Fujikawa says hiring locals is not always easy as rivals are on the hunt for good staff and it is hard to find employees with extensive experience in the fast-moving consumer goods sector.

Then there are the big cultural differences between Japanese and non-Japanese firms, and the need to operate the subsidiary according to local influences where possible.

"Kirin is still learning and has underestimated the task in Vietnam," Fujikawa says. "The group has learned a lot from the Lion and Schincariol transactions."

"Strong leadership and a clear sense of direction are important, as are proper systems and incentive processes."

"You need to invest in better understanding the local culture. Japanese management will often assume the local management think the same way as Japanese people – however, the reality is often locals are very different in terms of education, background and culture, and their attitude to company loyalty is also different."

For others contemplating expansion in ASEAN, Fujikawa has some sobering advice. Be prepared to encounter political volatility and some corruption, along with sudden regulatory changes. And above all, be clear in how you will define and achieve success.

"It is difficult to build a new business from scratch in ASEAN as it often requires a very, very long term point of view," he says. "Many times companies think their own way of business or business model will work in new markets, but that is often not the case."

"If you can't get control, you need a strong local partner. And you need to have a strong competitive advantage – such as brand, sales system or product quality – to succeed as a newcomer."

"Spend the time to define what constitutes success as this point is not considered well enough by boards."

"Strong leadership and a clear sense of direction are important, as are proper systems and incentive processes."

Two's company: How Australian and Japanese companies can work together to succeed in ASEAN and beyond

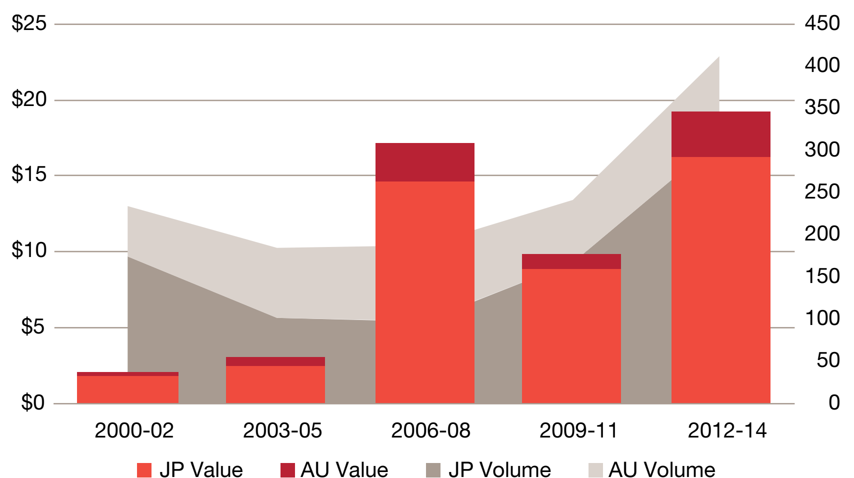
The deepening of economic and strategic ties between Australia and Japan was one of the big developments of 2014. But some astute observers of the region believe this could eventually be surpassed by what is an even bigger story – what Australia and Japan can do together in South East Asia and beyond.

We use the word "could" advisedly because for Australian and Japanese companies to team up successfully to conquer markets in this fast growing region will require far more courage than they have shown before.

Historically Australia has neglected investment opportunities in ASEAN and indeed in Asia as a while. Over 55 per cent of Australia's trade is with East Asia, yet only 4 per cent of Australian direct investment abroad goes into the region.

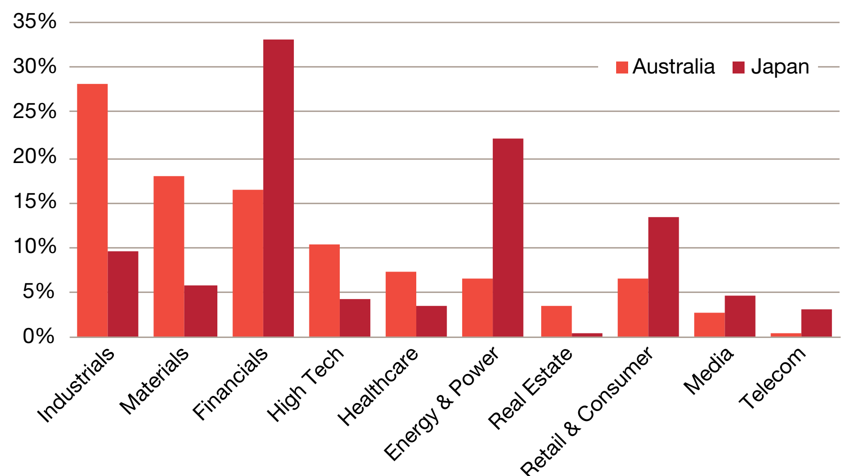
Despite having an emerging economic power in Indonesia on their doorstep, Australian companies have been reluctant to shoulder the risks involved in investing there and will thus miss out on the returns.

Figure 22: ASEAN M&A value and volume
$BN



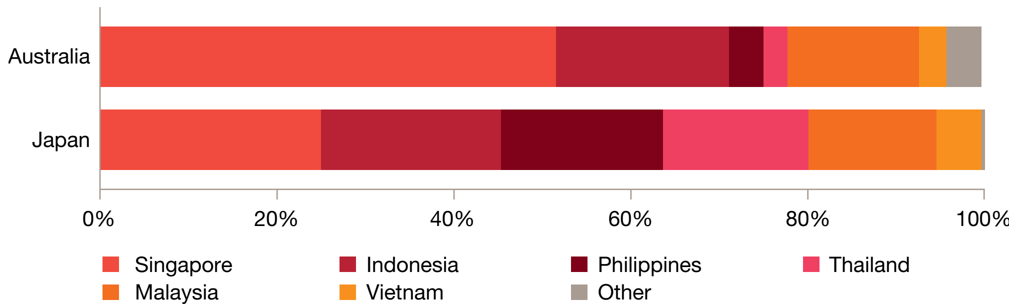
Source: Thomson Reuters

Figure 23: ASEAN M&A value by sector
Percentage of total M&A



Source: Thomson Reuters

Figure 24: ASEAN M&A value by country



Source: Thomson Reuters

Looking at Indonesia as an example, mining accounts for almost all of the miserly FDI total even though Australian infrastructure and services firms surely have a lot to offer in this market and others throughout the region.

Andrew Parker, the head of PwC-Australia's Asia Practice, warned in a recent report that Australian firms have failed to embrace Asia so far and, for many, this will be their last chance.

In a series of remarkable findings, PwC discovered that:

- Just 9 per cent of businesses are currently operating in Asia and only 12 per cent of Australian companies have any experience of doing business in Asia at all
- 65 per cent have no intention of changing their stance towards Asia in the next 2-3 years
- Of Australia's large companies, half are doing business in Asia but only 23 per cent have staff on the ground in-market.

"These results clearly show that Australian business is a long way from the level of engagement, investment and commitment needed to secure a long-term share of the region's growth," Parker says in the report.

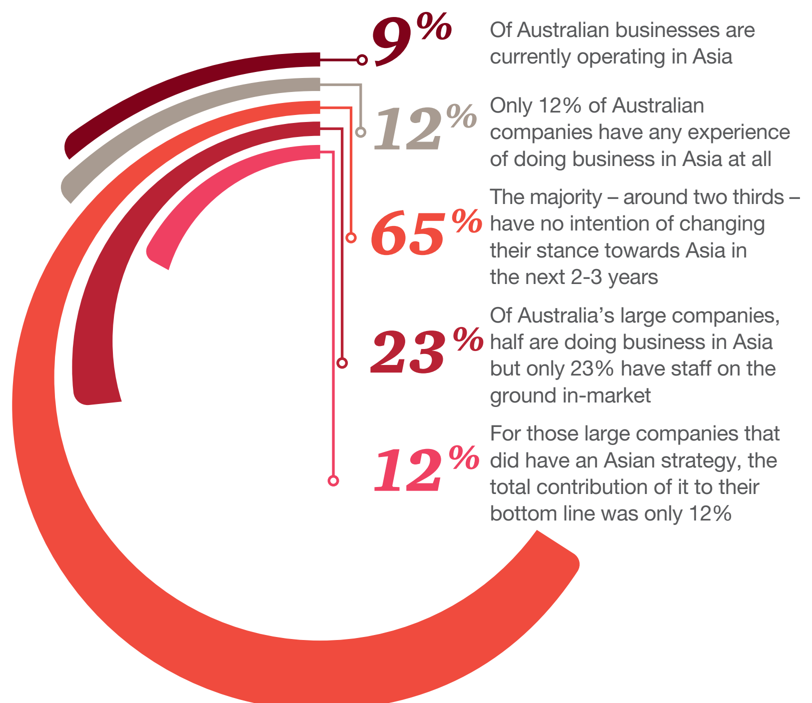
"Australian companies have struggled to execute in Asia. The biggest issues seem to have at their core, problems in relation to culture, our willingness to deal with change and our ability to manage and operate in an Asian environment. Putting it bluntly, Australian business has operated in a relatively sheltered, comfortable competitive environment. And we have become complacent."

"The opportunity for Australian businesses to get a substantial foothold in Asia is passing us by and we need to act now. This may well be our last chance."

$1.17bn

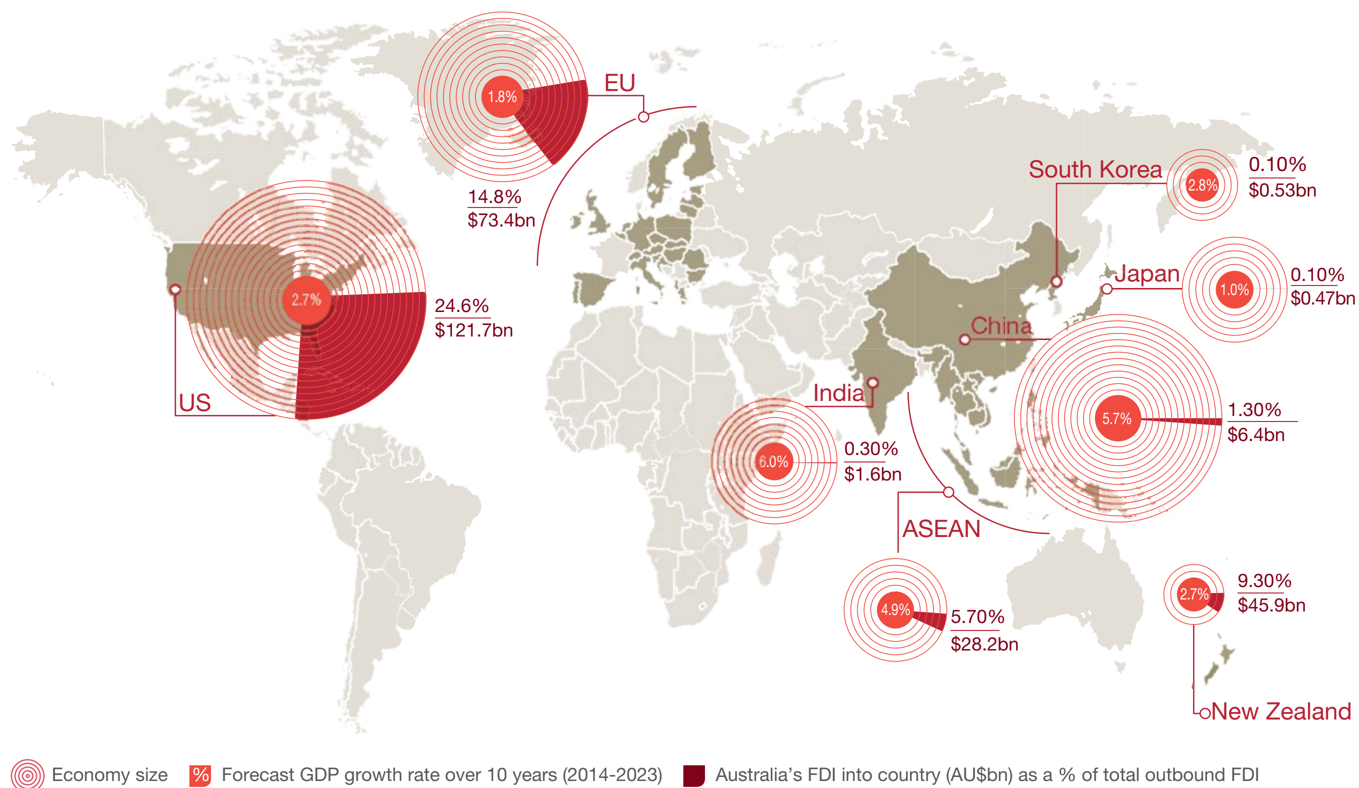
Oceania M&A in Indonesia has $1.17bn over 88 deals. Mining accounted for 68% of deal value and 63% of volume at $793 million in 54 deals.

Figure 25: Australian companies in Asia



Source: PwC's *Passing us by: Why Australian businesses are missing the Asian opportunity. And what they can do about it*, 2014.

Figure 26: Destinations for Australia's FDI relative to GDP growth and market size



Australia has invested more in New Zealand than in all ASEAN countries combined.

And the reticence of Australian companies to invest in Asia is even more acute when it comes to South East Asia with PwC's report revealing Australia has invested more in New Zealand than in all ASEAN countries combined.

Compared to Australian firms, Japanese companies have been far more active investors in ASEAN, although outside the leading manufacturers and trading houses, investment has been more modest.

Nevertheless, Japanese networks are active in many industry sectors in ASEAN and the amount of investment by Japan has doubled since 2007. From an Australian point of view, Japan has already done much of the heavy lifting by setting up strong trade and investment links in the region, aided by its ODA spending.

Many of the key players in Australia-Japan relations believe Australia could capitalise on the toehold Japan has in ASEAN in a way that would benefit both countries.

Australia's skills and experience in project management, engineering, PPPs and young, educated and more globally savvy workforce could complement Japan's deficiencies in this area, although leading Japanese firms with subsidiaries in Australia – such as Kirin – have found difficulty in persuading employees in Australia to latch on to opportunities in ASEAN and beyond.

Japanese companies also point to Australia's clean image and well developed financial services firms and retirement savings as things it could offer to any joint venture.

Japan, on the other hand, has world-class technology in many fields, proven expertise in product development, cheap debt for expansion and extensive government support to bring to the table. Procurement of subsidiaries of Japanese companies in Asia has risen from $265 billion in 2000 to $692 billion in 2013, which is a clear demonstration of the scale of Japan's presence in the Asian region.

This makes Japanese firms a compelling choice for risk-averse Australian firms in contemplating an ASEAN expansion.

Strategically, Australia would clearly benefit from attracting more Japanese companies looking to access Asian markets to use Australia as the location to support the development of their future business in Asia, with the recent acquisition of Toll Holdings by Japan Post as an example.

Perhaps one other shining example of this sort of collaboration is BlueScope Steel's joint venture with Nippon Steel Sumitomo Metals Corporation. The Japanese company, one of the world's largest steel producers, bought a stake in Bluescope's coated steel business to supply customers in South East Asia and beyond with materials for white goods in these rapidly expanding consumer markets.

The other area in which considerable work has been done in harnessing joint opportunities is in infrastructure.

PwC's Mario D'Elia says the Australian government has been active in trying to boost governments' grasp of the benefits of the PPP model in South East Asian nations.

"In Indonesia, there is a quite a bit of reform happening. They are setting up a centre of excellence with the support of the Australian government, which has a PPP unit. The government is also doing something similar in the Philippines," he says.

D'Elia says acceptance and utilization of the PPP model is low in Asia, despite some successes in Malaysia. Governments are slowly getting up to speed on how to structure projects to appeal to foreign investors and how to make them financially viable and to incorporate a user-pays element that does not make the cost to citizens prohibitive.

The other issue he has come across is a lack of refinement in the project pipeline citing the example of Indonesia, under the Yudhoyono government, producing a tally of 150 infrastructure projects that represented more of an impractical wish list than a realistic infrastructure game plan.

"If you say something you have to deliver it," he says. "Firms need to have a pipeline of projects rather than jumping around everywhere."

The Australia Japan Business Co-operation Commitee (AJBCC) has been active in trying to seize on the synergies of Australian and Japanese firms and encourage both sides to be more active in tackling third markets – together.

The AJBCC's infrastructure committee, led by Bob Seidler AM, has conducted missions to India and Indonesia to help corporate and public sector leaders understand the breadth of the opportunities and how they might be tackled.

D'Elia says Australia doesn't have all the answers, but can certainly bring considerable expertise to the commissioning, management, design and financing of large projects.

The infrastructure unit he leads within PwC Australia is playing a prominent role in PwC's work on infrastructure projects across Asia in recognition of the experience it has from both the client and government side on major projects.

"A lot of us have worked in investment banking and in government, so we have seen it from both sides."

Australia would clearly benefit from attracting more Japanese companies... to use Australia as the location to support the development of their future business in Asia.

When it comes to tackling ASEAN, pairing with Japanese firms may offer a lower risk path to success.

PwC believes that the FTAs struck with South Korea, Japan and China will eventually boost outbound investment into North Asia, but when it comes to tackling ASEAN pairing with Japanese firms may offer a lower risk path to success.

That might lie in supplying services and advice in infrastructure or a range of other sectors or even through supplying agricultural produce into Japanese food and beverage, supermarket and food production supply lines into ASEAN markets.

PwC believes the exact opportunity is less important than grasping that the time to act is now.

"Many Australian businesses fail to appreciate that the window of opportunity to get a foothold in Asia is fast closing," PwC's Passing Us By report says.

"Companies that are now successful in Asia arrived there approximately 15 years ago and they made their business plans and investments work. They, along with large local businesses, are now the competition – and they are world-class competitors."

Professor Peter Drysdale, Emeritus Professor of Econimics at Australian National University, urged "a paradigm shift in thinking about Australia's economic relationship with Japan" as far back as 2009.

The Japanese market is a market no longer confined to Japan itself. It is a huge international market generated by the activities of Japanese business and investors, especially via production networks in Asia," he says.

"To realise the new potential of the Japan relationship, Australia needs to develop its national and corporate commercial strategies through partnerships with Japan in Asia."

Infrastructure interview: Australia in ASEAN

Bob Seidler AM, AJBCC/Hunter Phillip Japan

Bob Seidler AM

Is Australia capitalising on this opportunity?

We are exporters of capital through our pension funds in terms of providing equity for projects. The big guys – Hastings, IFM and AMP – are all looking around the region and are all actively involved in Japan to raise money and they are all looking at India and Indonesia to invest in projects.

Banks like ANZ are very active and NAB are becoming more active in providing debt financing for infrastructure around the region. Generally you will find they will be going into places together with aid agencies so they have some confidence in getting the money back.

We don't have much technology to export. Engineering firms are quite active – GHD and the likes are very active in doing engineering work around the region. The advisory firms, accounting firms and legal firms are very active in providing consultancy, and then there is Leighton on the construction side.

In terms of doing capacity building we have got the expertise here. Australian advisory firms would be in strong demand.

In terms of construction, basically the Japanese construction firms are not very good at managing projects outside Japan. Part of it is cultural – they are not good at managing workforces outside Japan. If for example you go to a worksite of Leighton in Hong Kong, they have 30 different nationalities working on site. Thirty different languages, I don't know how many different religions. Japanese are just not very good at managing that. That's the other opportunity for companies like Leighton, who are good at managing workforces outside their home base.

How could collaboration work?

Ideally, it will be something like where Mitsubishi looks at a project and says they should bring in some Australians.

Let's say Mitsubishi wants to do a power plant in Malaysia. They say: 'What do we need to do to put this together?' We need to have equity. Are we happy to take the risk ourselves, or do we want to share it? Then if they want to share it they might say: 'Well in Australia we know AMP is involved in this because Mitsubishi Trust has 30 per cent of AMP Capital, so we will go to AMP and ask them to share the risk with us. Then they say: 'Well, we have to build this thing – who do we get to build it?' Ah, Leighton has got an operation in Malaysia and we know they are very good at managing workforces, so why don't we try to get Obayashi and Leighton together to do this. That is how it will come about.

If you do one project and it works, the next one that comes along, you can put a similar team together. Our strengths are Japan's weaknesses and vice versa. So we are complementary not competing.

What are some of the constraints and problems?

The problem with delivering infrastructure in the region is that the governments are still learning how to do it. If you think about building a road or bridge, the government has to understand how to design it, it's got to understand how to toll it, how to build it. In the end the actual work will have to be done by the private sector. The issue for governments around the region is capability: – How do I have the technical expertise to evaluate bids? How do I have the financial expertise to evaluate bids? So there is a lot of work being done by the aid agencies to lift the capacity of the governments to be able to do those things.

"Our strengths are Japan's weaknesses and vice versa."

“You have got issues of corruption… which is a significant issue that needs to be dealt with.”

What about PPPs?

You have to have a government that is relatively sophisticated to deal with the private sector. There is a lot of work being done by APEC, by us, and by others to upskill governments around PPPs, but it is a few years away. Then you have got the issues of corruption around as well, which is a significant issue that needs to be dealt with.

Are there sector or country-specific opportunities?

Every country has issues with upgrading its ports, every country in the region has a massive problem in terms of upgrading its roads, its airports, its water supply, its electricity supply, its hospital sector – they are all related to improving the quality of life for the growing middle class. Wherever you go in Asia the roads are clogged, there are too many cars, the hospitals are not (good) enough, the sanitation system doesn’t work, the water, the electricity. It’s the same issue everywhere, although there are greater needs in some countries and in some sectors than others.

Is corruption the main problem?

It is a very big one. Generally if it is an aid-agency funded project then there’s less likely to be corruption because they will supervise the bidding system. The problem then is you have got to implement the project. You have to get permits, you have got to get subcontractors, you have got to buy goods, equipment. The opportunity for corruption to occur through the supply chain and through the duration of the project is pretty big.

How can you mitigate it?

There are three basic solutions. One is you participate in an aid-funded project so you get some confidence that the bidding for the project is clean. Secondly you must have a zero-tolerance attitude towards corruption. The third is getting the right partner.

Governments are now more and more concerned about delivering infrastructure properly and what that means is you have to go with international companies. With simple infrastructure, the local companies may have the ability to deliver, but when you get to the more complicated engineering and technology – tolling systems and all that – local companies don’t have the expertise to do it. So they have to go overseas, and when you go overseas they have got to start thinking seriously about having a process that’s not corrupt.

Are there other problems?

The issue of capacity is also a problem. If governments don’t understand how the private sector works, it’s very hard for them to evaluate a project properly. Foreigners will look at it and say: ‘I am not interested.’ If I can’t add any value, I can’t compete with the local people what’s the point? The more sophisticated the government is in the region the more likely there will be opportunities for foreign companies to participate.

Are there efforts under way to educate governments on PPPs?

There is no point in doing a PPP in Indonesia if the market and projects are not attractive by international standards. Japan's capacity to deliver a PPP is quite limited.

We have been taking experts from Australia, predominantly government advisers, to Japan, to Indonesia, to India... and running private workshops for government by sharing our experience in delivering PPPS.

The experts coming up from Australia are sitting in front of a small group of a prefectural governments in Japan and saying: 'Let me tell you why we do a PPP, how we do it and what are the mistakes we have made and what we have learned – and then you can decide where you want to go from there.'

So we are knowledge sharing. Rather than us going up there and lecturing government on what they should be doing, we are taking government people up and sharing their experiences.

If you look at Australia 20 years ago. Each state had its own PPP system and documentation and each state simply went to the market with its own projects when it felt like it. We now have a uniform system, uniform documentation and Infrastructure Australia, which prioritises projects.

So Indonesia, the Philippines and India – with so many provinces – they have to get their act together. The governments around the region have got a lot of work to do to deal with foreign companies coming into their market.

There is a lot of work being done by APEC and other agencies to upskill the region but they are going to have to move pretty quickly because the population's requirement for improved infrastructure is running way ahead of their ability to deliver.

Are enough Australian firms are looking overseas?

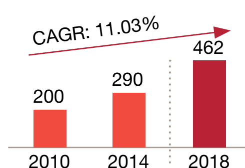
It is a very competitive market here. Competition is getting intense, so where does the growth come from? Asia.

"So we are knowledge sharing... we are taking government people up and sharing their experiences."

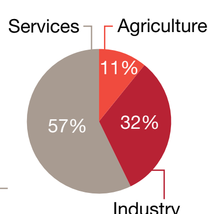
Appendix: ASEAN country profiles

Philippines

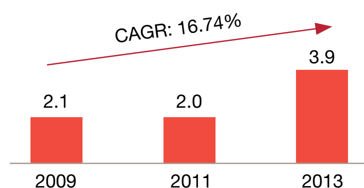
GDP
Current US$bn



By sector



FDI Inflow
US$bn



Business overview

- Strong GDP growth has been supported by significant infrastructure investment, a booming manufacturing sector and numerous PPPs.
- Preparation for the upcoming 2016 election has led to new political alliances and a renewed interest from the business community to implement economic reforms.
- IPO funding has been encouraging, as approximately US$100 million was raised in the first half of 2014.

Key economic indicators (2013)

1	GDP per capita	US$2,765
2	Unemployment rate	7.4%
3	Population % between 15-54 years	56.0%
4	S&P rating	BBB
5	Internet Penetration	37%
6	Consumer Price Index growth	2.8%
7	Ease of doing business ranking	95/189
8	Corruption Perception Index ranking	94/175

Tax and regulation (2014)

1	Corporate Income Tax(CIT)	30%
2	Personal Income Tax	20%-32%
3	Tax Incentives	Available
4	Total Tax Rate*	44.5%
5	Ease of paying taxes ranking	131/189

** Average world tax rate is 43.1%*

Sector attractiveness

Infrastructure (industry)

- The Philippines is witnessing a huge growth in PPP infrastructure projects – this is across airports, highways and trains.
- There are approximately 50 PPP projects in the pipeline currently.
- Key projects include the North-South commuter rail and the Mass Transit loop.

IT/BPO (Services)

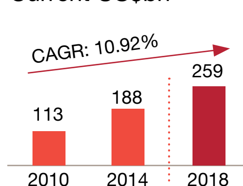
- The Philippines ranks seventh out of 51 of the popular countries for BPO services and investment.
- Key reasons for this are a young workforce, low operating costs, an educated and English-speaking population, and affordable real estate.
- The BPO industry is expecting an average yearly growth rate of 20 per cent, as investors are given numerous incentives.

Banking (Services)

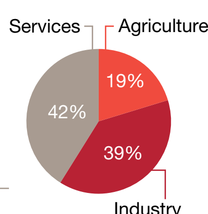
- In 2014, a new law was signed that allows full entry of foreign banks into the Philippines and grants locally-incorporated subsidiaries of foreign banks equal banking privileges as domestic banks.
- This, coupled with the availability of skilled talent and a well established banking framework has propelled the growth of the banking industry.

Sources: CIA factbook, Global-rates, World Bank, Oanda, IBGE, Trade Economics, IMF PwC Reports & Analysis

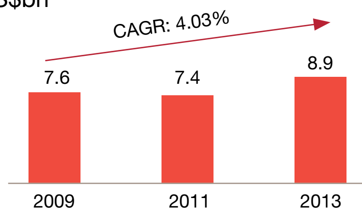
GDP
Current US$bn



By sector



FDI Inflow
US$bn



Business overview

- Vietnam has witnessed strong GDP growth since 2010, correlating with increased FDI inflows and a growth in overall household consumption.
- M&A deals have been on a decreasing trend – from US$4.9 billion in 2012 to approximately US$2 billion in 2014.
- Unclear and complex regulations, bureaucratic challenges and corruption are cited as the key challenges faced by foreign investors.

Key economic indicators (2013)

1	GDP per capita	US$1,911
2	Unemployment rate	1.3%
3	Population % between 15-54 years	62.6%
4	S&P rating	BB-
5	Internet penetration	43.9%
6	Consumer Price Index growth	6.8%
7	Ease of doing business ranking	78/189
8	Corruption Perception Index ranking	116/175

Tax and regulation (2014)

1	Corporate Income Tax (CIT)*	22%
2	Personal Income Tax	5%-35%
3	Tax Incentives	Available
4	Total Tax Rate**	35.2%
5	Ease of paying taxes ranking	149/189

** Expected reduction to 20% in 2016*
*** Average world tax rate is 43.1%*

Sector attractiveness

Energy and Utilities (Industry)

- The energy industry in Vietnam is evolving, as demand from businesses and households are driving a more sustainable model.
- Petroleum remains the main source of energy (approx. 25 per cent of total consumption); crude oil is one of the main Vietnamese exports (approx. 20 per cent of total).
- Hydropower is the main non-fossil fuel energy (approx. 10 per cent of consumption) – it is expected to grow steadily at a CAGR of 7 per cent over the next few years.

Pharmaceuticals and Healthcare (Industry)

- The Vietnamese pharmaceutical market was valued at US$3.3 billion in 2013, a 17 per cent increase from 2012.
- Key drivers include increased public and private healthcare expenditure, a growing middle class population and better health awareness.
- Complicated regulatory procedures is the key barrier for foreign companies looking to invest in the Vietnamese healthcare sector.

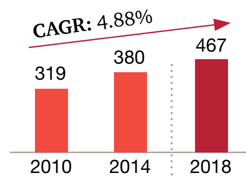
Retail and Consumer (Services)

- Double digit growth in the retail and consumer sector will be driven by rapid urbanisation, high disposable incomes and an improvement in consumer living standards.
- As a result of WTO efforts to encourage more investment, more foreign retailers have been entering the market.

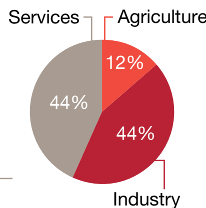
Sources: CIA Factbook, Global-rates, World Bank,Oanda, IBGE, Trade Economics, IMF, PwC Reports & Analysis

Thailand

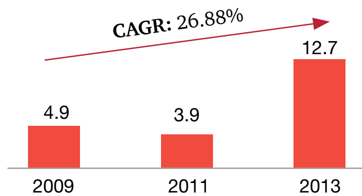
GDP
Current US$bn



By sector



FDI Inflow
US$bn



Business overview

- Thailand is ranked as the eighth most attractive country for investment in the region over the next three to five years.
- A 1H-2014 BOI survey of foreign investors indicated 98 per cent had continued confidence in Thailand due to adequate suppliers and raw materials, infrastructure, and funding.
- After a year of political instability, Thailand has re-positioned itself as a hub of medical tourism, agriculture and services.

Key economic indicators (2013)

1	GDP per capita	US$5,779
2	Unemployment rate	0.7%
3	Population % between 15-54 years	61.90%
4	S&P rating	BBB+
5	Internet penetration	28.9%
6	Consumer Price Index growth	2.2%
7	Ease of doing business ranking	26/189
8	Corruption Perception Index ranking	102/175

Tax and regulation (2014)

1	Corporate Income Tax (CIT)*	20%
2	Personal Income Tax	0-35%
3	Tax Incentives	Available
4	Total Tax Rate**	29.8%
5	Ease of paying taxes ranking	70/189

** Progressive tax rate of 0-20% applies to SMEs*
*** Average world tax rate is 43.1%*

Sector attractiveness

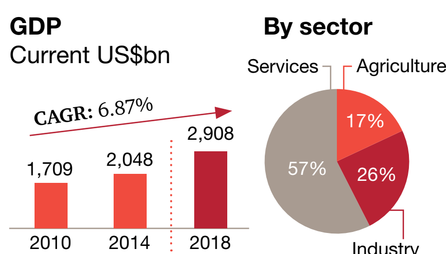
Food (Agriculture & Industry)

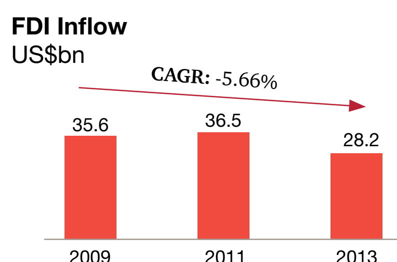
- Thailand's agricultural expertise and abundant natural resources have made the country one of the world's leading suppliers of commodities such as rice, sugar cassava, and rubber.
- The use of leading technologies combined with governmental support in food R&D have developed Thailand's reputation as the 'Kitchen of the World'.
- Increasing regulatory focus on implementing international standards of food safety and hygiene are increasing consumer trust and consumption.

Healthcare (Industry)

- Thailand is the world's largest medical tourism market due to its low-cost medical treatments and high quality of healthcare.
- The government continues to launch initiatives to strengthen its position as the medical hub of Asia such as internationally certified medical facilities and standards, tourist visa fee exemptions and discounts on parking and landing fees to entice both regular and medical tourists.
- The Thailand Board of Investment offers attractive incentives for a wide range of activities related to the medical sector such as manufacture of medical food and medical equipment.

Sources: CIA Factbook, Global-rates, World Bank, Oanda,IBGE, Trade Econimics, IMF, PwC Repoarts & Analysis, PwC APEC CEO Survey, Thailand Board of Investment Survey





Business overview

- Riding on the optimism of the recent election in India, the government has relaxed FDI regulations across several sectors to encourage investment.
- Rapid urbanisation is expected to increase the city population by 590 million by 2030 with the top 13 cities accounting for more than a third of this.
- In 2030, India will contribute to more than 28 per cent of the global workforce, benefiting from its rigorous tertiary education standards and availability of skilled labour.

Key economic indicators (2013)

1	GDP per capita	US$1,499
2	Unemployment rate	8.8%
3	Population % between 15-54 years	58.7%
4	S&P rating	BBB-
5	Internet penetration	15.1%
6	Consumer Price Index growth	9.6%
7	Ease of doing business ranking	142/189
8	Corruption Perception Index ranking	94/175

Tax and regulation (2014)

1	Corporate Income Tax (CIT)*	33.99%
2	Personal Income Tax	0-33%
3	Tax Incentives	Available
4	Total Tax Rate**	62.8%
5	Ease of paying taxes ranking	158/189

** On average, domestic companies pay 30% and foreign companies 40%*
*** Average world tax rate is 43.1%*

Sector attractiveness

IT (Services)

- The IT sector in India is fuelled by the availability of skilled low-cost labour that is largely English-speaking.
- Numerous global and regional technology companies have established a large presence in India, mostly providing back-end support.
- On the whole, the services sector accounts for almost 60 per cent of the total GDP.

Manufacturing (Industry)

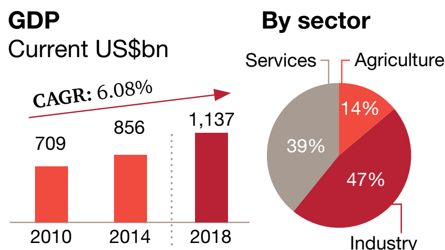
- The Indian manufacturing sector is expected to reach $1 trillion by 2025.
- Presently, it contributes to about 25 per cent of the GDP.
- According to the FICCI, 137 big ticket projects with an investment of $82 billion are under initial stages of implementation.

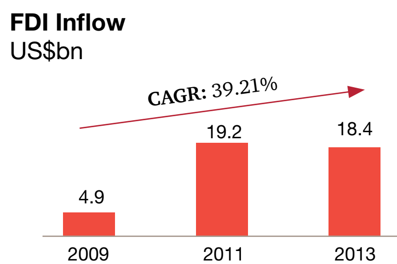
Retail & Consumer (Services)

- Total retail sales in India are expected to increase from $567 billion in 2013 to more than $1,048 billion in 2018.
- Per capita spend in retail has increased by 230 per cent in last eight years; from $200 in 2005 to $465 in 2013.
- The Indian middle class is expected to rise from 28.4 million households in 2009-10 to 113.8 million households by 2025 – indicating a massive opportunity for the retail industry.

Sources: CIA Factbook, canadean, Global-rates, World Bank, Oanda, IBGE, Trade Economics, IMF, PwC Reports & Analysis

Indonesia





Business overview

- Indonesia is an attractive market for investment; it has one of the biggest populations globally, an expanding middle class and high GDP growth.
- The newly elected government has begin to focus on infrastructure and the services sector, improving the regulatory framework to make it more conducive for foreign investment.
- Corruption, tax challenges and a lack of transparency are key barriers for growth.

Key economic indicators (2013)

1	GDP per capita	US$3,475
2	Unemployment rate	6.6%
3	Population % between 15-54 years	59.4%
4	S&P rating	BB+
5	Internet penetration	15.8%
6	Consumer Price Index growth	7.7%
7	Ease of doing business ranking	114/189
8	Corruption Perception Index ranking	114/175

Tax and regulation (2014)

1	Corporate Income Tax (CIT)	25%
2	Personal Income Tax	5%-30%
3	Tax Incentives*	Available
4	Total Tax Rate**	32.2%
5	Ease of paying taxes ranking	137/189

** Tax reductions, depending on the industry, can be between 5 – 50%*
*** Average world tax rate is 43.1%*

Sector attractiveness

Retail & Consumer (Services)

- The Indonesian retail sector is expected to reach US$13.4 billion in 2014 – largely driven by FMCG goods (particularly food and beverages).
- Strong local and foreign competition has led to development of multichannel strategies – leading to opportunities in e-commerce.
- The growth of the retail and consumer sector is expected to increase in proportion with the growth of the Indonesian middle class and their respective personal disposable income level.

Infrastructure (Industry)

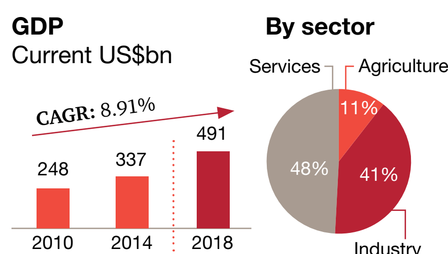
- The new government has renewed focus on infrastructure investment in Indonesia.
- Key areas of focus are roads, ports, power and water plants – most of these are done through a PPP process.
- Most recently the Ministry of Transport launched phase 1 of its PPP scheme to develop 10 airports.

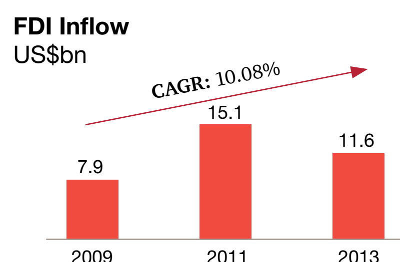
Energy (Industry)

- The energy industry is focused on alternative energy sources, whilst improving existing facilities to cope with increasing demand from businesses and consumers.
- Energy consumption is made up of: petroleum (36 per cent), coal (20 per cent), biomass and renewables (27 per cent) and others.

Sources: CIA Factbook, Global-rates, World Bank, Oanda, IBGE, Trade Economics, IMF, PwC Reports & Analysis

Malaysia





Business overview

- Malaysia is ranked highly as a favourable business location; it's competitiveness, connectivity and ease of doing business are attractive to foreign investors.
- The Government plays a proactive role in the economy, promoting significant public and private spending via its Economic Transformation Programme initiatives.
- Investors are provided with numerous concessions and tax breaks to boost FDI, driven by the government's plan for Malaysia to become a high income nation by 2020.

Key economic indicators (2013)

1	GDP per capita	US$10,514
2	Unemployment rate	3.1%
3	Population % between 15-54 years	58.1%
4	S&P rating	A-
5	Internet penetration	67%
6	Consumer Price Index growth	2.2%
7	Ease of doing business ranking	18/189
8	Corruption Perception Index ranking	53/175

Tax and regulation (2014)

1	Corporate Income Tax (CIT)* ^	26%
2	Personal Income Tax ^^	0-26%
3	Tax Incentives	Available
4	Total Tax Rate**	36.3%
5	Ease of paying taxes ranking	36/189

** 20% tax is imposed on the first MYR 500,000 of chargeable income*
*** Average world tax rate is 43.1%*
^ proposed tax rate of 25% in YA 2015 and 24% in YA 2016
^^ proposed max tax rate of 25% for YA2015

Sector attractiveness

Finance (Services)

- Malaysia strives to be a global hub for Islamic finance, with strong and comprehensive Islamic financial systems and a robust business driven regulatory regime and framework.
- Banking in Malaysia is adopting more technology and commercial banks are seeing consolidation within the sector.

Food (Industry)

- Malaysia strives to present itself as a global halal hub for halal food production, ingredients, cosmetics and personal care products, capitalising on its status as an Islamic country.
- It is expected that by 2020 – halal products will account for approximately 8.5 per cent of Malaysia's exports.
- The opportunity size of the halal market in Malaysia is estimated to be approximately US$500 billion.

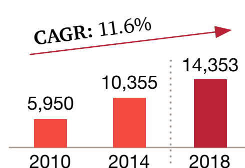
Palm Oil (Agriculture)

- Palm oil represents the king of commodities in Malaysia, accounting for over 80 per cent of total value of commodities.
- The country is the second largest producer of palm oil globally after Indonesia.

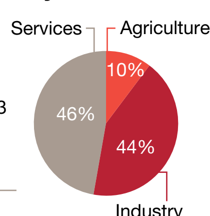
Sources: CIA Factbook, Global-rates, World Bank, Oanda, IBGE, Trade Economics, IMF, PwC Reports & Analysis

China

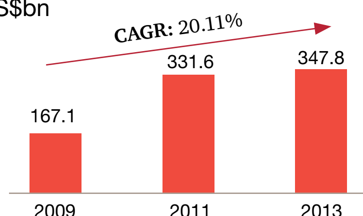
GDP
Current US$bn



By sector



FDI Inflow
US$bn



Business overview

- Economic growth in China has been slowing and was at 7.3 per cent in Q3 – 2014, its slowest growth in five years.
- The central bank initiated its first interest rate cut in over two years which is expected to bolster growth, improve GDP and foreign investor confidence.
- Global response to the Shanghai FTZ remains tepid and real economic benefits and reforms are still to be seen.

Key economic indicators (2013)

1	GDP per capita	US$6,807
2	Unemployment rate	4.1%
3	Population % between 15-54 years	61.9%
4	S&P rating	AA-
5	Internet penetration	45.8%
6	Consumer Price Index growth	2.6%
7	Ease of doing business ranking	90/189
8	Corruption Perception Index ranking	80/175

Tax and regulation (2014)

1	Corporate Income Tax (CIT)	25%
2	Personal Income Tax	5%-45%
3	Tax Incentives*	Available
4	Total Tax Rate**	63.7%
5	Ease of paying taxes ranking	120/189

** Companies that are eligible for incentives pay a CIT of 15%*
*** Average world tax rate is 43.1%*

Sector attractiveness

Healthcare (Industry)

- Growth of more than 14 per cent in the Chinese healthcare sector is being fuelled by public and private investment.
- Total healthcare expenditure doubled between 2008 and 2013 and is expected to reach more than US$1 trillion in 2020.
- The Government has initiated a privatisation pilot in certain cities which has led to increased interest from foreign healthcare providers.

Automotive (Industry)

- Automotive companies are evolving their business and operating models to capitalize on the opportunities in China.
- China outbound deal services for Chinese auto manufacturers remains attractive, particularly with Chinese OEM's expanding overseas for acquisition of technology, vertical integration and branding.

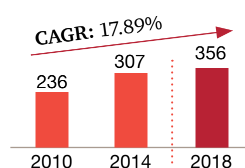
Retail and Consumer (Services)

- China is the second largest retail market globally – M&A within the industry continues to remain strong with buyers buying smaller companies catering to niche customer tastes such as sport and energy drinks.
- The R&C industry is undergoing a wave of digital and customer transformation and retail markets are shifting towards e-commerce channels with transaction values up by more than 150 per cent year on year in 2014.

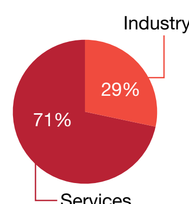
Sources: CIA Factbook, Global-rates, World Bank, Oanda, IBGE, Trade Economics, IMF, PwC Reports & Analysis

Singapore

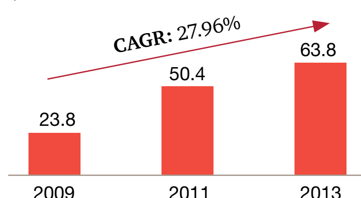
GDP
Current US$bn



By sector



FDI Inflow
US$bn



Business overview

- Singapore is one of the most attractive investment destinations in the region – FDI investment in 2013 was estimated at more than US$65 billion.
- As one of the most competitive and easiest countries in the world to do business, many MNCs continue to establish their regional headquarters in Singapore, spurring the economic growth of the country.
- The high cost of living and conducting business in Singapore is a concern that may impact the business environment in the long term.

Key economic indicators (2013)

1	GDP per capita	US$55,182
2	Unemployment rate	1.9%
3	Population % between 15-54 years	68.1%
4	S&P rating	AAA
5	Internet penetration	73%
6	Consumer Price Index growth	2.4%
7	Ease of doing business ranking	1/189
8	Corruption Perception Index ranking	5/175

Tax and regulation (2014)

1	Corporate Income Tax (CIT)	17%
2	Personal Income Tax	0-20%
3	Tax Incentives	Available
4	Total Tax Rate*	27.1%
5	Ease of paying taxes ranking	5/189

** Average world tax rate is 43.1%*

Sector attractiveness

Energy (Industry)

- Singapore is a regional leader in renewable energy – developing the clean technology sector to contribute US$2.7 billion to GDP by 2015.
- The government promotes use of natural gas (it fuels 80 per cent of Singapore's electricity generation). It is currently building a terminal to import liquefied natural gas and diversify its supply.

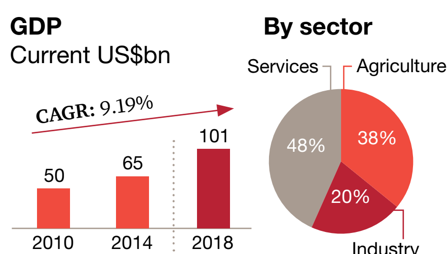
Healthcare (Industry)

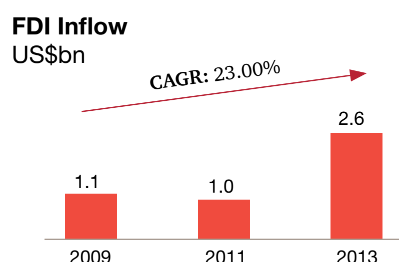
- Singapore has a mature healthcare market, ranked first in Bloomberg's annual healthcare efficiency ranking.
- Driven by an ageing population, increasing incidences of chronic diseases and medical tourism – healthcare expenditure is expected to grow at a CAGR of 12 per cent to reach US$22 billion in 2018.

Infrastructure (Industry)

- Singapore constantly ranks highly amongst attractive countries for infrastructure investment – key drivers include stable political and economic environment, transparency and ease of regulatory environment.
- Investors believe that challenges such as high cost of labour and real estate are outweighed by benefits.
- Investment in construction projects has amounted to between US$18-29 billion in the last 5 years.

Sources: CIA Factbook, Global-rates, World Bank, Oanda, IBGE, Trade Economics, IMF, PwC Reports & Analysis





Business overview

- There has been significant support from the ADB and the World Bank into channelling investment into Myanmar.
- Consequently, FDI growth has been phenomenal – 50 per cent increase from 2011 to 2013 to US$2 billion, with investment targeted into infrastructure projects, banking and telecoms and energy.
- Unclear regulations, unstable political environment, corruption and underdeveloped infrastructure are cited as the key challenges faced by foreign investors.

Key economic indicators (2013)

1	GDP per capita	US$1,126
2	Unemployment rate	5.2%
3	Population % between 15-54 years	61.4%
4	S&P rating	N/A
5	Internet penetration	1.2%
6	Consumer Price Index growth	5.7%
7	Ease of doing business ranking	177/189
8	Corruption Perception Index ranking	157/175

Tax and regulation (2014)

1	Corporate Income Tax (CIT)	25-35%
2	Personal Income Tax	1-35%
3	Tax Incentives	Available
4	Total Tax Rate**	48.9%
5	Ease of paying taxes ranking	107/189

*** Average world tax rate is 43.1%*

Sector attractiveness

Infrastructure (Industry)

- The World Bank recently announced a US$2 billion development program for Myanmar, including projects to improve access to energy and healthcare.
- The construction sector is expected to grow at approximately 14 per cent per annum until 2030 providing great opportunities.
- Myanmar is one of the top destinations for PPP investment. The most recent examples are Mandalay International Airport and Hanthawaddy International.

Energy (Industry)

- Since Myanmar instituted a change in its foreign direct investment law in 2012, there have been greater revenue incentives for international companies, especially those investing in energy.
- The government is keen to attract foreign investment and technical assistance to realize its oil and natural gas production potential as well as develop necessary energy infrastructure.
- The energy sector has being fuelled by numerous PPPs, as the government is actively seeking foreign investment to develop their renewable energy sector.

Financial and Telecom Services (Services)

- Both sectors are relatively nascent in Myanmar – growth is expected to be above 20 per cent per annum until 2020.
- Key drivers include urbanisation, expanding middle class and investment from regional companies.

Sources: CIA Factbook, Global-rates, World Bank, Oanda, IBGE, Trade Economics, IMF, PwC Reports & Analysis

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