AGILE GROWTH IN UNCERTAIN TIMES

By Mark Spelman

Like death and taxes in the good old days, it seems now that the only thing certain in the economy is uncertainty. In the face of this, it is important for organisations to be agile and responsive - although, there is a propensity for organisations to dig in their heels in the face of ambiguity. Following on from his latest article with Criticaleye, The Power of Three, **Mark Spelman**, *Global Head of Strategy at Accenture, looks at how economies are growing at different speeds, the uncertainty this creates and the implications on organisations.*

We have three sets of growth rates in a 'multi-speed' recovery. The Western world - including the US, eurozone and Japan - is heading for 0 to 2.5 per cent growth in 2011. In the eurozone, we see different growth rates, depending on the country's structural position.

The country to watch in this area is Germany. It has strong exports and is ahead of other EU governments in terms of trying to rebalance its budget. It is running a trade surplus and is looking to take € 80 billion out of spending by 2014 to balance its budget, at a time when the rest of Europe is struggling with high deficits and relatively weak exports. Germany has good labour productivity, and will balance government spending significantly ahead of any of the other European countries. This puts them in a very strong long-term position.

The fundamental challenge in Europe is that the North has been supporting the South, and now the Germans have said that enough is enough... it is time to adhere to the rules, to have more transparency and more balanced government budgets. This structural change will play out over the next 10 years.

Japan is hindered by high debt levels and, as most of that debt is held by Japanese banks, the domestic drag will result in an ongoing low growth outlook.

The US economy will continue to be hindered by a weak housing sector, difficulties in reducing unemployment and the deficit. Despite more stimulus, the US outlook for 2011 looks likely to be below the recent annual trend growth rates of 3 per cent plus.

In the rest of the world, there are essentially three groups. First, there are countries such as Mexico and South Korea, which are going to be at the low end of the 3 to 6 per cent GDP per annum growth range. There are a group of countries in the middle (eg, Brazil, South Africa and Russia) that will be growing in the 4 per cent per annum range. Then there are one or two countries, like Vietnam, which will grow at 6 per cent plus.

At the top end are the two stars - China and India - that will be growing at about 8 per cent in 2011. There are different growth rates, but the headline message is that there are very few countries anticipating a GDP growth rate in 2011 higher than that of 2010. Vietnam is one of these exceptions. Everybody else recognises that structural weaknesses will produce lower growth rates.

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CHALLENGES TO GROWTH

As with all outlooks, it is important to monitor the risks and the game changers. In the US, the two factors to watch are government spending and the ongoing uncertainty regarding housing prices.

In Europe, the challenges are around reform and innovation and to what extent the EU and member states can drive reform to the structures and create the environment to get the innovation engines going.

In Asia, the risks are around asset bubbles, as capital flows into the higher growth Asian markets, and increases the prospects for inflation. The question is, can the Asian economies manage the growth in capital inflows without inflation?

LONG-TERM OUTLOOK

The outlook will be a rollercoaster, but there are also important longer-term economic, political, social and technological forces at work. Economically, the long-term problem of trade imbalances is not going away. China, Japan and Germany still have large trade surpluses, which must be addressed over the medium- to long-

COMMUNITY COMMENT

Dan Londero, MD – International Sales Group, Reed Exhibitions

Internationally we observe a general degree of optimism, although several sectors remain troubled. The key question right now is how permanent are the global changes that we have recently experienced and what is the right balance of business to have in the different continents in order to capitalise upon those shifts? Our strategic planning exercise when dealing with the immediate as opposed to the medium- to long-term is now, more than ever before, reliant on leading indicators of business performance. The development of more reliable leading indicators is also of priority. Given the uncertainty in global markets, our planning exercise has become more granular and frequent.

Too many boardrooms are stuck in old paradigm thinking of Western domination and are not anticipating changes being driven by a multi-speed global economy

THE NETWORK OF LEADERS

CRITICALEYE

term. Two-thirds of all the world's foreign reserves now sit in Asia and, over time, these funds will be recycled through asset purchases in different parts of the world.

The US government's deficit position is different to other countries. Comparing the US and Greece, nobody wants Greek bonds but, as the US economy is 25 per cent of the world's GDP and there is structural interdependence on it, it is easier for the US to run a large deficit.

However, there's a sting in the tail. The US can run a deficit as long as Asia, and particularly China, is willing to buy treasury bonds to fund it. China will continue to buy those bonds owing to interdependency in the global economy. It needs the West as an export market until its domestic economy is sufficiently strong that it is no longer dependent on exports and the US consumer for export-led growth. The moment that happens, the pressure will be on the US to make sure their government spending is in balance. This trend will not happen quickly, but the failure to address trade imbalances will create longer-term tensions.

A second big long-term trend is demographics. This is both an opportunity and a challenge. The focus is on ageing in the West, and the emerging middle class in many parts of Asia and Latin America. Ageing populations and mass urbanisation will challenge government spending, but will create many new opportunities from healthcare to new city infrastructure.

There are major global governance issues concerning banking, energy and the environment. Although the technicalities of those subjects are different, the governance principles and the problems are very much the same, which are about how to create a global framework to oversee rules, decision making, cost and benefit allocation.

Many have assumed, rather hopefully, that issues such as climate change would be addressed by a global agreement – but, with Copenhagen, this looks less likely. A more realistic assumption is that there will be a patchwork of solutions, different types of regulations and gradual convergence over time. This will require corporations to be more flexible as they learn to operate under different regulatory frameworks around the world.

THE PERFECT STORM

The other long-term challenge that will increasingly play out this decade is 'the perfect storm': the shortage of food, water and energy. The global population will grow from 6.8 to 9.2 billion over the next 40 years. Agriculture productivity needs to gear up by 2 per cent per annum in order to be able to feed those people.

Demand will be driven as people come out of poverty, or as the new middle classes aspire to eat more meat and vegetables. The problem is that 70 per cent of all water goes into agriculture production. In many developed countries, we are not conscious of what is happening with water stress, but many companies that enter emerging markets will find much more sensitivity around water usage.

After water, there is energy access, security and reducing carbon intensity. In many emerging markets, the gap in terms of raw

COMMUNITY COMMENT

Tim Eggar,
Associate, Criticaleye
& Chairman, Nitol Solar Ltd

I am struck by the number of low-debt larger Western companies, which appear to be waiting for ever more economic data points. European and Asian Governments have gone a long way to clarifying their policies; the performance of the US is perhaps less clear, but I think we have reached the point where shareholders in many sectors expect investments to be made. The contrast with the decision-making process in larger Asian companies is stark.

COMMUNITY COMMENT

Mike Turner, Chairman, Babcock International plc

Uncertainty, cyclicality and the timing of business cycles are not new phenomena. What should remain as a constant is the pursuit of the company's strategy. Whilst the strategy has to be regularly reviewed by the board, executives should always remain focused on executing the strategy and the pursuit of growth, both organically and by acquisition.

energy demand is being covered by the introduction of new nuclear and renewable energy. The challenge is that the demand for fossil fuels is not decreasing. The trend is still increasing as we struggle to bring electricity to the 1.4 billion people who lack it.

More people means more food, water and energy. The other complementary factor is biodiversity - the losses of species around the world. If there is an increased loss of species, food productivity is hindered. This is a subject that we will hear a lot more about over the course of the next 12 to 18 months as the rate of loss of species continues to accelerate.

Technology will also be a major business disruptor in the longer-term as new mobile applications and cloud computing change industry boundaries and solutions. Customers become more powerful as they have more 24/7 information on products and services.

These long-term economic, political, social and technological trends will impact the global economic outlook. Some will help, others will hinder. The issue for businesses is about monitoring the potential impact they will have on operations.

BUSINESS IMPLICATIONS

In a world of uncertainty, many businesses still have much of their thinking driven by a flat line, incremental approach. The forces at work mean that businesses must understand the global context and what it means to be agile and flexible in the face of uncertainty.

The start is 'what happens if' and the need for a more disciplined approach to risk and downside scenarios. This requires a careful look at the assumptions in the boardroom. The danger is that too many boardrooms, particularly in the West, are stuck in old paradigm thinking of Western domination and are not anticipating the changes being driven by a multi-speed global economy and new competition.

The world is going to be about the dynamics of economics and politics playing out in a true multi-polar world where the West no longer sets all the rules. 2003 to 2007 was all about economics; it was all about global growth at 5 per cent per annum where everyone won. Now, post 2008/9, the shift in economic power and the need to address global governance mean that the global business landscape is also shifting. More attention needs to be paid to new growth markets, new competitors and different regulatory structures.

The boardroom agenda today is driven by four items: growth, innovation, cost and complexity. This is a source of rich discussions as everyone wants to grow, reduce cost and innovate but no one wants more complexity. This is a critical discussion in any boardroom, and links back 'fair and square' to what is going on in terms of the macro-economic context.

In conclusion, a view of the global economy needs to be cast in an understanding of short-term realities, of longer-term challenges and opportunities, and boardroom implications. Many are focused on the realities of the next quarter. It is necessary to have a short-term view, but wise leaders are able to understand the implications of longer-term context.

The key message is the world will be more uncertain, more 'multi-speed', more diverse and experience even more rapid change as new technologies create new business models. The assumptions of the past need to be challenged – uncertainty requires an even greater premium on organisational agility. Efficient growth through an agile organisation will be key to future success.

Mark Spelman
Global Head of Strategy
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Mark leads Accenture's Global Strategy practice and runs Accenture's global macro economic and political think-tank and the Institute for High Performance. He is responsible for the firm's strategic relationship with the World Economic Forum (WEF) and is a regular participant and session leader at Davos and the WEF regional summits. Mark has almost two decades of experience working at board level in senior management and business strategy positions. His client work over the past decade has centred on energy, utilities, natural resources and chemicals companies globally.

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