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Global

Economy

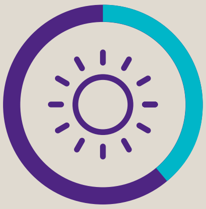
Growth

Thriving in 2019's global economy

Use agility to manage uncertainty

February 2019

Outlook for 2019



39%

Global economic optimism fell to net 39% in Q4 2018, a drop of 15pp since Q2 2018

21%

Global export expectations have risen to net 21% as business leaders look to other markets for growth opportunities

50%

Economic uncertainty has spiked at net 50%, rising 22pp since Q2 2018

31%

Investment in research and development (R&D) has risen dramatically to net 31% in Q4 2018 from net 22% in Q2 2018

60%

Despite uncertainty in the global economy, 60% of business leaders are either optimistic or very optimistic about their country's economy over the next 12 months

86%

Technology remains a priority for business leaders. 86% expect their technology investments to either increase or stay the same in 2019

Foreword

Business leaders are markedly less optimistic than they were a year ago. Momentum in global economic growth has softened as political uncertainty continues to undermine business confidence. However, growth remains achievable. It requires a calm assessment of the economic fundamentals combined with a strategic analysis of which markets and technologies offer the best prospects for growth.

The change in business sentiment may seem startling; Grant Thornton's latest International Business Report (IBR) reveals that business leaders believe economic uncertainty is now the biggest constraint facing their business, having spiked 22 percentage points from Q2 2018 to net 50%. This uncertainty is a key driver behind a 15pp fall in global optimism to net 39%, down from a record high of net 54% in Q2 2018. While the headlines appear daunting, there are good reasons for business leaders to hold their nerve. And for nimble businesses, there are still opportunities to seize and sustain growth.

First, business leaders in 2019 need to focus on economic fundamentals and the health of their own businesses. The global economy may be slowing, but it is still growing – at 3.5% in 2019, according to the latest IMF estimates[1]. There are opportunities for business leaders to drive growth by transforming their businesses to be future fit in a changing economic landscape.

Second, businesses must think creatively and differently about where growth will come from. Just as supply chains continue to expand into new markets around the world, so do export opportunities. Our IBR data indicates that emerging markets in Asia Pacific and Latin America show particular promise, with robust business optimism and healthy revenue and profit expectations.

Third, turn to technology, which can enable businesses to access these new markets faster and with less risk when implemented correctly. More broadly, digital tools are enabling new business models, whether through cheaper access to cloud computing solutions and 'software as a service' models, or social media's dismantling of traditional mass media marketing channels. Leaders should pursue appropriate technology strategies to make the most of opportunities for growth.

The good news is that, despite rising uncertainty, today's growing businesses are more agile and better able to adapt to changing market conditions. Small and mid-sized businesses were once at a distinct disadvantage compared to larger competitors – often lacking resources, new product development capacity, political influence and access to international markets. Today, technology levels the playing field, meaning smaller or more nimble businesses can compete and change faster.

There is no doubt the market is changing. Change has always been a risk as well as an opportunity. Those businesses able to combine a sustainable long-term strategy with an ability to adapt to changing market dynamics will be in the best position to thrive, whatever lies ahead.

Peter Bodin
Global CEO
Grant Thornton International Ltd

1. IMF World Economic Outlook (WEO): Jan 2019

Economic uncertainty is the keynote for 2019

The global economic cycle has peaked and businesses face a more downbeat global economy in 2019. Among the 5,000 mid-market business leaders Grant Thornton interviewed as part of the IBR's global economic outlook, global optimism sits at net 39%, a fall of 15 percentage points (pp) from net 54% in Q2 2018. This is the weakest optimism score seen since Q4 2016.

While the drop in optimism is marked, it is worth highlighting that 60% of respondents remain either optimistic or very optimistic about the future. In addition, while uncertainty is making business leaders more circumspect about the outlook, a slim majority still expect revenue (53%) and profits (52%) to increase this year, with only a small number (12% and 13% respectively) expecting these to decrease.

Political volatility undermines business confidence

A raft of geopolitical events underpins the battered business outlook for 2019. European sentiment dropped 18pp to net 28% in Q4 2018, possibly connected to the rise of political populism in Italy, Poland and Hungary clouding business leaders' ability to plan with certainty. Meanwhile, protests in France have shocked the political establishment and ongoing tensions between Russia and Ukraine (and other European states) remain on Europe's border.

In the UK in particular, optimism has plummeted from net 17% in Q2 2018 to net 9% – most likely linked to protracted uncertainty over Brexit. There has also been a sharp increase in skills constraints (up 22pp to net 54%), which may also be related to slower inbound migration.

On the other hand, though falling from net 78% in Q2, confidence in the US remains relatively robust at net 60%. However, North America still has its fair share of uncertainty with the new NAFTA agreement yet to be ratified, and interest rates are rising. Meanwhile, US policymaking remains unpredictable, and the US and China trade dispute rumbles on.

In Asia Pacific, China is a concern after the economy grew at its slowest rate since 1990[2]. Business confidence in APAC more broadly stands at net 34%, down from net 55%, while optimism across ASEAN dropped 22pp to net 42%. This could be down to concerns that Asian economies will be the hardest hit by China's declining growth rate, given the region's emphasis on domestic trade.

Slowing investment intentions

The rise in uncertainty, coupled with falling optimism, is having a knock-on effect on business leaders' investment intentions. According to the IBR, global investment intentions in plant and machinery currently stand at net 26%, down from net 38% in Q2 2018. In Germany, investment in plant and machinery has notably dropped from net 56% in Q2 to net 11%. Meanwhile, investment in new buildings globally fell to net 17% from net 25% in Q2, the lowest level since Q1 2016.

But this is only part of the story. On the whole, a larger number of business leaders see their investment intentions increasing or remaining the same rather than decreasing in 2019. As we will explain, it is where businesses are putting their money that tells us how business leaders think they can achieve a real advantage in a disrupted and changing market.

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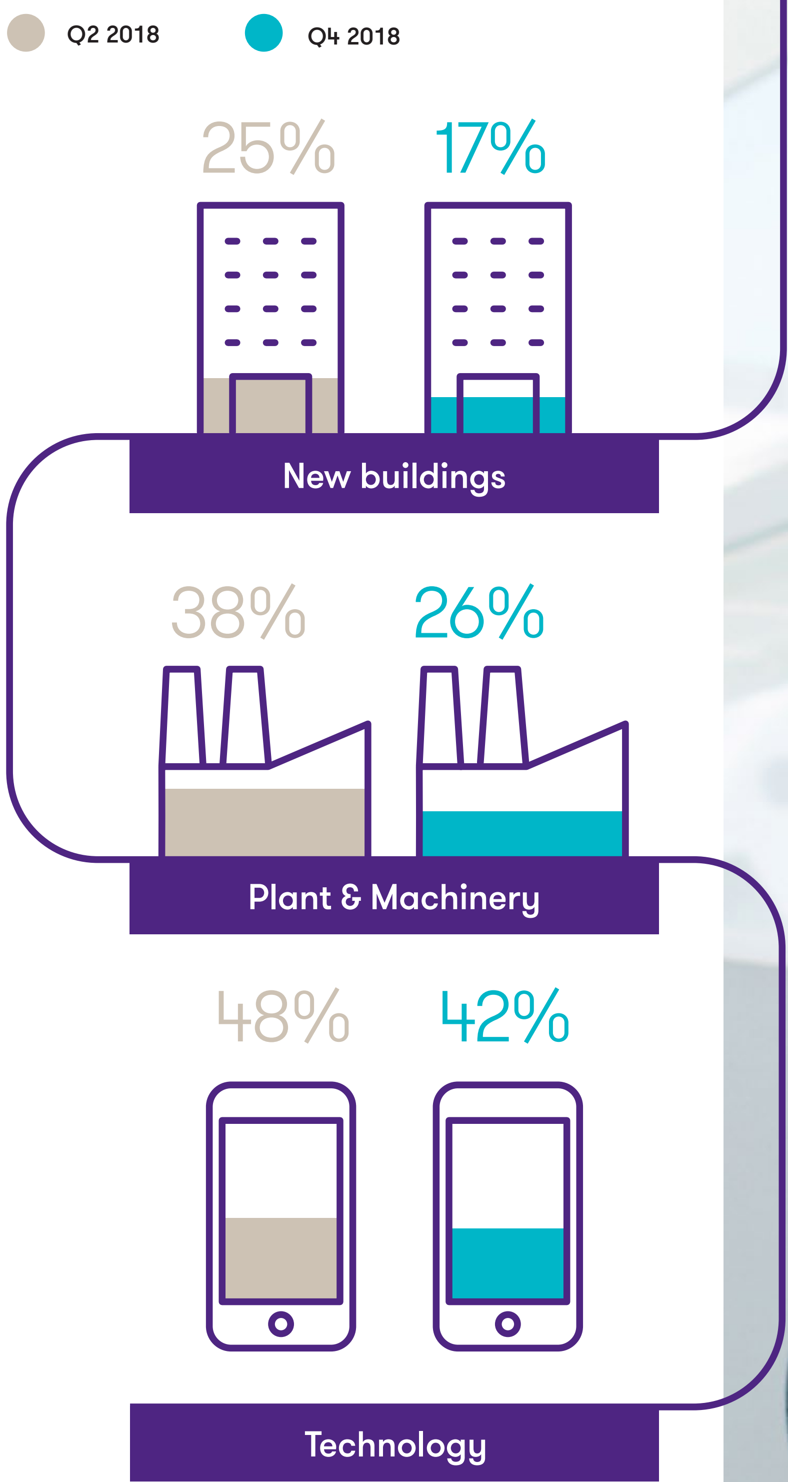
The big question: Amid the less clear outlook, with risks increasing, how can you achieve growth and continue to thrive in 2019?

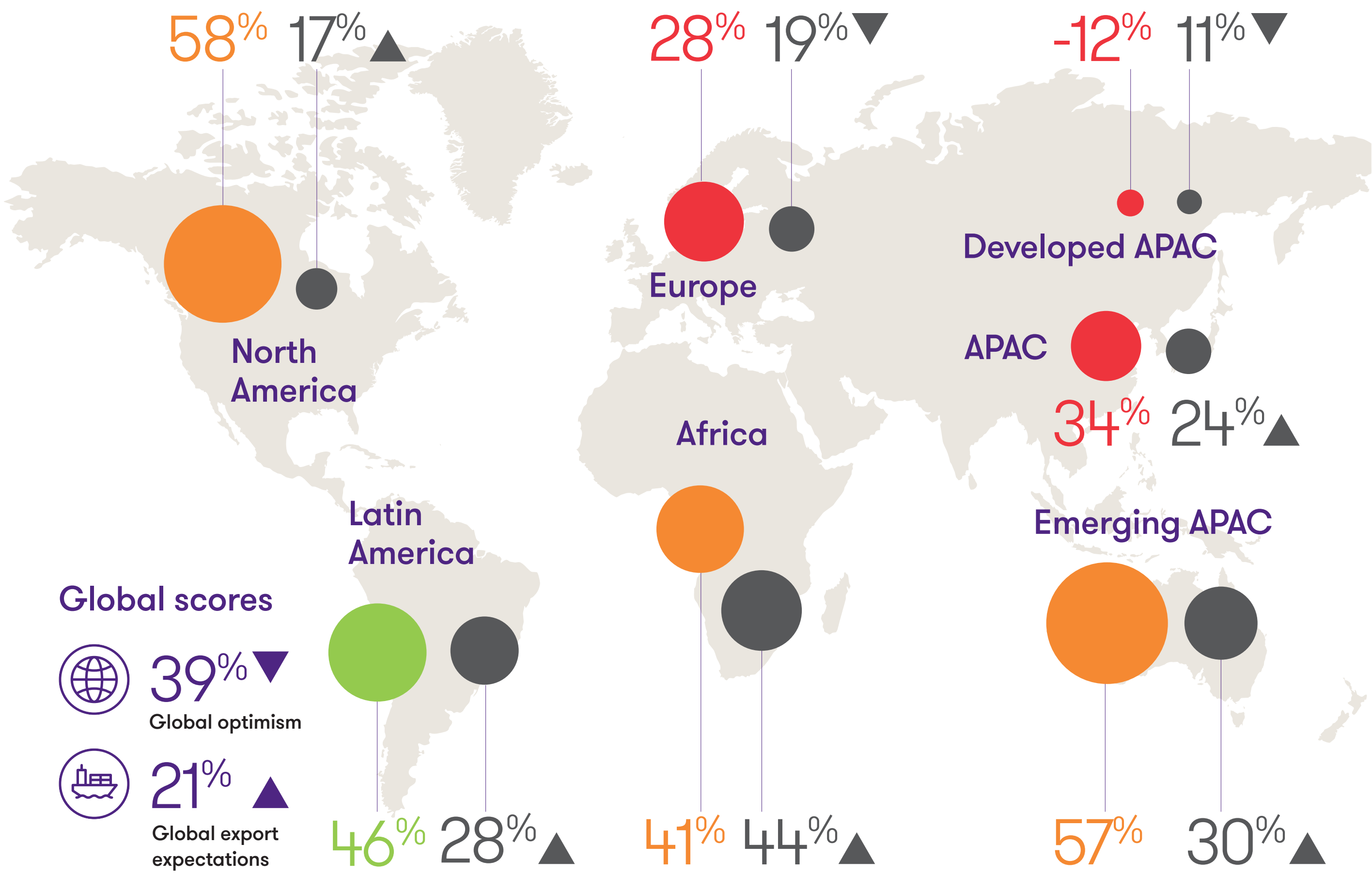
2. National Bureau of Statistics of China, Jan 2019

Investment intentions decrease



Opportunities remain in the global economy

Despite a more downbeat global outlook for 2019, there are opportunities for global expansion. Business leaders are feeling positive about exports, with only 11% globally expecting a decrease. Expanding internationally can accelerate growth when domestic markets look uncertain.



Business optimism (net %)*

- Optimism increased in Q4 2018
- Optimism decreased in Q4 2018 but is above the global optimism score
- Optimism decreased in Q4 2018 and is below the global optimism score

Export expectations over the next 12 months (net%)

- Export expectations for the next 12 months (net %)
- ▲ Increase in export expectations since Q2 2018
- ▼ Decrease in export expectations since Q2 2018

*Net optimism is calculated as optimistic business leaders minus pessimistic respondents.

1. Focus where it matters

The gloomy picture may deter some business leaders from expanding or investing in new opportunities. But others are taking advantage of continuing growth and are transforming their business models by investing in the markets and technology that will continue to drive returns.

Francesca Lagerberg, global leader – network capabilities at Grant Thornton International says: “While global financial markets are increasingly volatile, business leaders in the real economy remain optimistic because global GDP is forecast to continue growing and they know their businesses will grow with it. Despite increasing downside risk, economic fundamentals remain strong, and opportunities exist.”

Indeed, the IMF projects global GDP to grow by 3.5% in 2019 and by 3.6% in 2020, with advanced economies expected to grow 2.0% in 2019 and developing economies by 4.5%[3]. Global unemployment has also dropped to its lowest level since 1980[4]. In theory, this should translate to higher wages and greater consumer spending.

More significantly, the lack of skilled labour is driving investment decisions to help transform businesses in the absence of the people necessary to do the work. While investment in new buildings and plants and machinery have decreased, R&D and innovation are at the forefront of business leaders’ minds as they grapple with how to deliver their growth plans.

Global investment in research and development (R&D) is up 9pp to net 31% in Q4 2018 from 22% in Q2. In the US R&D investment sits at net 34%, more than doubling since Q2 2018, although this is likely due to US tax cuts in 2018. Meanwhile, India’s R&D investment leapt from net 21% in Q2 to net 51%, and in the Philippines, investment jumped from net 48% in Q2 to net 60% in Q4. Investment in technology also remains a priority for businesses at net 42%.

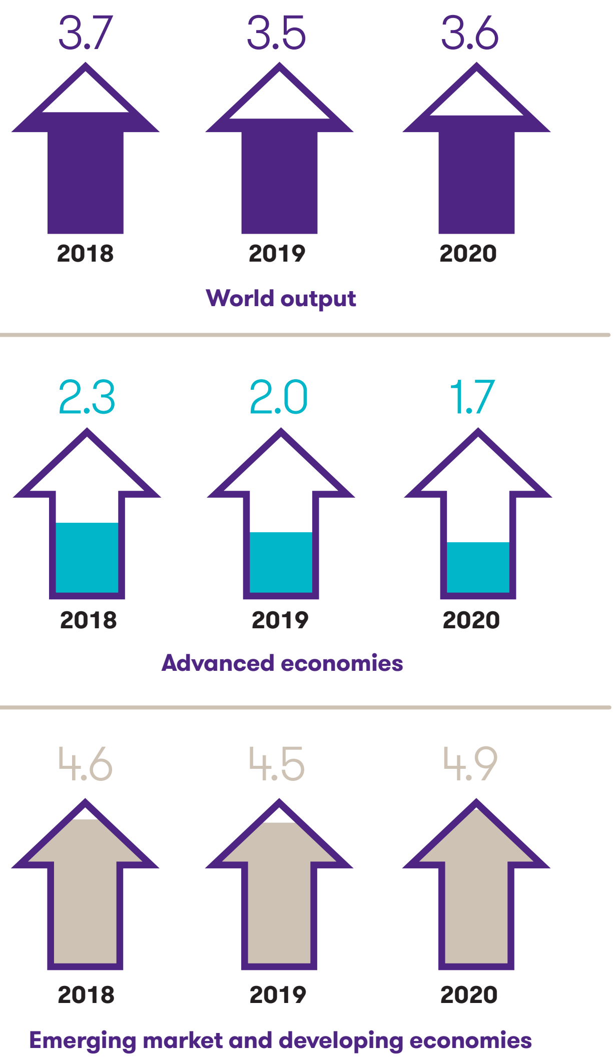
Paul McCann, Global Head of Advisory and partner at Grant Thornton Ireland says: “More and more businesses are focusing on building resilience into their business models as they assess increasing risks across their supply chains and geographic markets. Investment intentions seem to indicate business are seeing the opportunity to bank the strong returns from the past few years and transform their businesses through strategic investments.

Where and how to invest that money will surely be the difference between the winners and losers of the next cycle.

3. IMF World Economic Outlook (WEO), Jan 2019
4. Financial Times, Dec 2018

Moving into a period of uncertainty from one of relative, measurable risk may require a shift in strategy and a greater focus on scenario planning.”

Growth softens but remains steady in 2019



Source: IMF World Economic Outlook (WEO), Jan 2019

2. Be ambitious: think creatively about international markets

The one sentiment that seems to undermine the more negative views of the global economy is business leaders' export expectations. While they may be less optimistic overall, the number of decision makers who expect their exports to increase has actually risen by 3pp to net 21% from Q2 2018.

Regionally, aside from the European Union and developed APAC, export expectations have risen across the board, with the highest numbers seen in Latin America (net 28%) and emerging APAC (net 30%).

Francesca Lagerberg, global leader – network capabilities at Grant Thornton International says: "Balancing domestic trade with international markets is important to businesses at times of uncertainty because it helps to diversify risk. This can help a company better withstand changes in domestic markets if it can generate growth elsewhere."

New export markets can expose businesses to a larger pool of customers than they may have at home, and technology is playing a critical role in helping business gain access to the world (see next section).

Businesses' strategies for entering a market can be as varied as the markets they choose to target. Joint ventures and partnerships can be effective tactics to gain a foothold in unfamiliar markets. Smaller companies with valuable intellectual property, for example, can find larger global partners hungry for their innovation.

Where to seek growth

There are some bright spots around the world. Emerging APAC and Latin American countries could prove a popular choice for exporters.

Optimism in emerging APAC stood at net 57% while revenue expectations, although down from net 61% to net 52%, are holding up well in contrast to other, more advanced economies such as Europe. Resilient domestic demand in Asia is balancing the negative impact of slowing exports to China.

Wardah – Indonesia's first pure-play Halal cosmetics brand – recorded double-digit annual growth in 2018 having found success in emerging APAC. Offering skincare and make-up products for young Muslim women, the business is rapidly emerging as a prominent player in the Indonesian cosmetics and toiletries market[5].

Meanwhile, China's One Belt One Road (OBOR) initiative and increasing urbanisation across the region are driving physical infrastructure projects, providing opportunities for related suppliers, consultancies and engineering contractors. Ceres Power, a small UK fuel cell company, leveraged its intellectual property to gain access to the Chinese market by entering into a joint venture with Chinese bus manufacturing company Weichai Power[6].

Developing a stronger international network can take time and energy, but it can be done. It is an area that should be prioritised to leverage overseas markets.

India is set to grow by 7.5% in 2019 according to IMF projections, and its growing middle-income families expected to help boost growth. Elsewhere, smaller countries such as Vietnam, which are considered an alternative to China as a manufacturing location, may benefit from a continuing China-US trade war.

In Latin America optimism rose to net 46% in Q4 2018 from net 23% in Q2 2018 with hopes that burgeoning private consumption will support regional growth. Confidence in Brazil leapt from net 28% to net 66% in Q2 of 2018; possibly a positive reaction to populist, Jair Bolsonaro's presidential win in Brazil in November 2018 on hopes of fiscal reform and a new anti-corruption stance.

5. GlobalData, Sep 2018
6. The Economist, Jan 2019

3. Embrace digital tools and embed technology into your strategy

When it comes to technology, business leaders know they cannot sit back and wait, regardless of the outlook. While the net position has fallen from 48% to 42%, in total 86% of business expect their investment in technology to either increase or stay the same this year.

Successful businesses increasingly turn to new technology as a pathway to rapid growth. Digital tools extend the reach and enhance the agility of businesses while improving back-office productivity. Both of these are critical to executing quick strategic pivots when new technology disrupts or economies turn.

Many businesses today are 'born global'; agile but small in size, they have a big appetite for growth and use an array of technologies to reach customers, process data, utilise knowledge resources and perform back-office functions. Spotify and Skype, for example, represent some of the original 'born globals' due to their ability to use cloud-based systems that remove barriers to entry into new markets and rapidly connect with customers all over the world.

By drawing on the natural advantages of size – unencumbered by legacy systems and protracted decision-making processes – dynamic businesses can turn the traditional, competitive advantage of scale on its head. And technology is amplifying that effect in many and ever-increasing ways.

Growing businesses have an ever-increasing suite of digital tools helping them to reshape their business models very quickly.

Cloud-based systems and on-demand ICT platforms allow smaller businesses to use services at a fraction of historical costs. A small biotech business in Amsterdam, for example, could access supercomputer-level processing and storage in a pay-as-you-go model, where previously it would have needed to find time on a university supercomputer.

Enterprise resource planning systems provide enhanced insight into the ebb and flow of goods and services and manage complex supply chains, increasing efficiency, reducing waste and supporting greater flexibility.

Then there is e-commerce that facilitates a closer relationship between brands and their customers, while the use of AI and chatbots enhances customer experience, increasing productivity by reducing customer inquiries.

Businesses are using new technology such as customer relationship management systems and marketing automation to enable enhanced business development. Meanwhile, social media tools provide insight into buyer behaviour in addition to client engagement, and smaller companies are well placed to react to changing buyer preferences. These are tools that are ultimately helping businesses to adapt almost as quickly as their customers do.

Luckin Coffee, which launched in China at the start of 2018 and offers consumers the choice of sit-down, pickup, or delivered coffee demonstrates how putting technology at the heart of any business is becoming ever more important. The company has adopted an internet business philosophy by implementing an aggressive expansion strategy, seamlessly integrating online and offline experiences and placing a high value on customer data[7].

Australian footwear manufacturing company Redback Boots is also deploying technology to improve customer experience. It has just invested in new enterprise resource planning systems, along with a new customer relationship management system and better diagnostics. As Mark Cloros, co-founder and director, explains: "We were finding the cost of servicing customers quite high, so being able to communicate with customers on things like delivery dates is really important. It is getting more affordable with cloud-based systems making a huge difference[8]."

7. CNN Business, Jan 2019
8. Conversations for Growth, Grant Thornton Australia, Sep 2018

Technology as a strategic priority

All these technology tools require a comprehensive strategy woven into the business's structure, operations, processes and assets.

Paul McCann, Global Head of Advisory and partner at Grant Thornton Ireland, says: "While businesses have been using digital technology for years, there has been a recent shift to pursuing durable transformations rather than tactical upgrades, remaking individual functions. Companies are now more strategic than they were, they are more committed to investing in digital transformation for long-term growth, not short-term improvements."

Therefore, successful organisations continue to invest in technology. Incrementally, every year new technology is coming on stream; leaders need to continually understand what will add value, whether that's automation, data analysis or understanding customers better.

Even amid uncertainty, new technologies and digital tools can speed growth by lowering barriers to entry and creating economies of scale. For ambitious, technologically committed businesses the ability to take advantage of new opportunities quickly is in their power.

Ambition to thrive in 2019 will breed success

Uncertainties are rife in 2019, but that does not make growth impossible for dynamic organisations. Despite a slowdown in the global economy, economic fundamentals remain strong. The message to businesses is to understand where they need to refocus their priorities to realise growth.

Businesses can not only survive but become even more competitive during this period of global uncertainty by investing in technological capabilities to make sense of any changes in their operating environment and enhance their natural agility.

By expanding into new geographical markets, they can smooth and limit the regional disruptions in demand caused by geopolitical events, as well as create profitable new revenue streams.

Speak to a local Grant Thornton adviser via **grantthornton.global** to find out how your business can adapt to thrive in disruption.

IBR 2018 methodology

The Grant Thornton International Business Report (IBR) is the world's leading mid-market business survey. Launched in 1992 in nine European countries, the report now surveys more than 10,000 senior executives in 35 economies on an annual basis, providing insight into the economic and commercial issues affecting both listed and privately-held businesses. Fieldwork is undertaken on a biannual basis, through both online and telephone interviews.

IBR is a survey of mid-market listed and privately held businesses. The definition of the mid-market varies by country; in the EU, we interview businesses with 50-499 employees; in the United States, we interview those with annual revenues of USD20m to USD2bn; in China, those with 100-1000 employees. Respondents are chief executive officers, managing directors, chairpersons or other senior decision-makers.

For more information:
grantthornton.global/About-IBR/
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About Grant Thornton

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