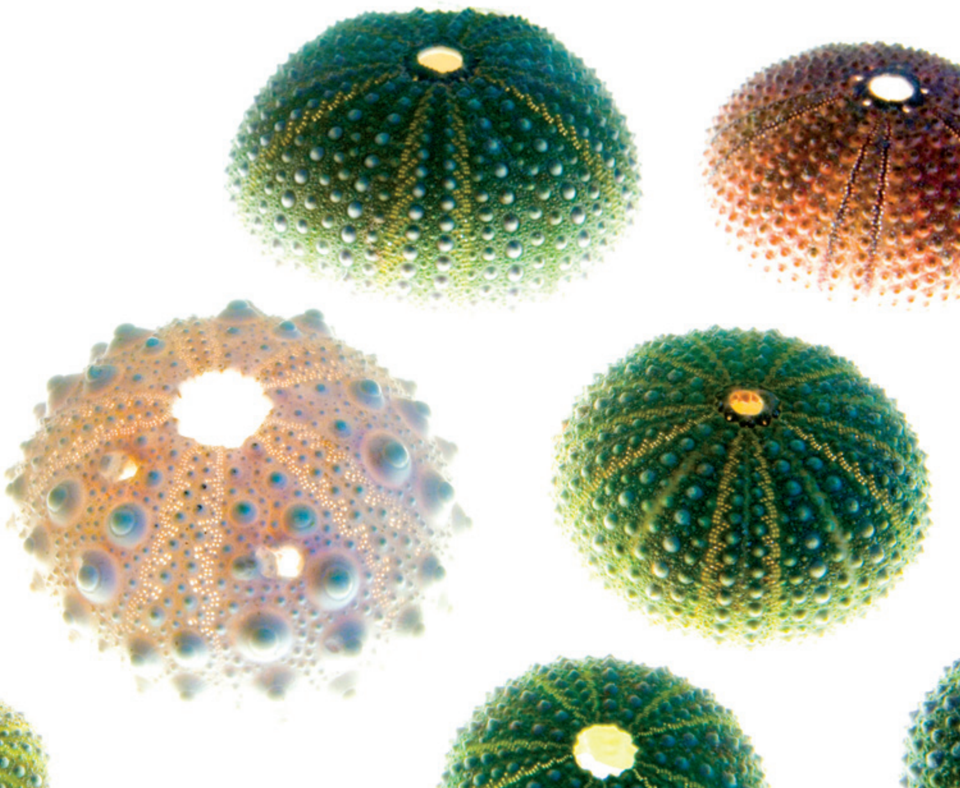
Winning in growth markets
Developing collaborative ecosystems for success

The growth of the global middle class across India, China and other fast growing economies is arguably the most important trend in the coming decades. So how should firms organise themselves for success in these markets? Deloitte believes that, to build advantage, firms need to adopt an ecosystem approach to better realise strategic opportunities, particularly those that require significant knowledge and technology capabilities.



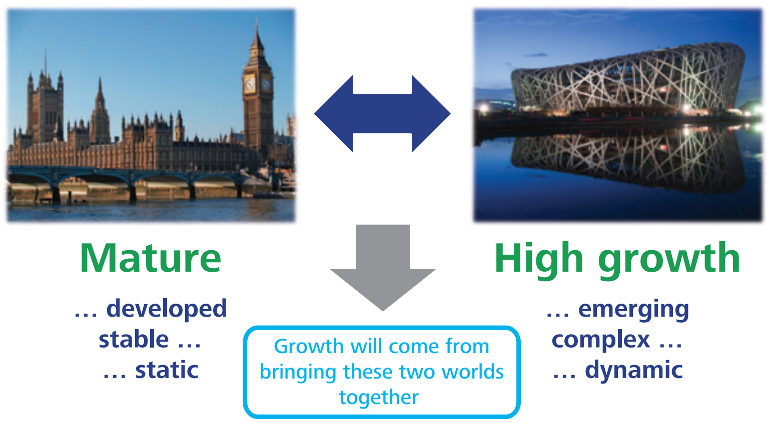
Deloitte point of view

The unprecedented growth of the new middle class outside the western economies will arguably be the most powerful economic trend in the coming decades. As the economic expansion of India, China, as well as others, accelerates, and the spending power of the middle class surges, their demand for world class infrastructure, better healthcare, sophisticated goods and services will also expand exponentially. It is important that firms in mature markets recognize the need to better connect with the rising aspirations of this new middle class to unearth strategic growth opportunities.

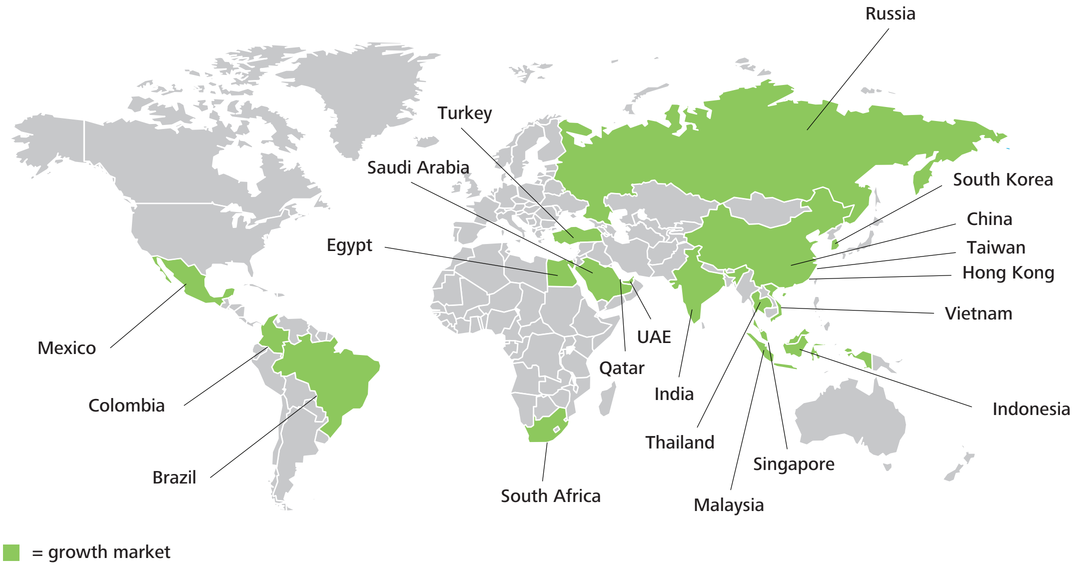
Much of the developing world's growth is centred on rapid urbanisation. At current trends, the growth markets will have over 300 cities of more than 1 million inhabitants by the end of the decade, up from 232 in 2010[1]. Furthermore, there will be 2 billion middle-class households in Asia – over 1 billion in China and India alone – representing over 25 times the entire UK population[2].Consumption in these cities is increasing fast, and the middle classes living there want to leapfrog to the latest technology.

The rising aspirations of the new middle class and the dynamic nature of these markets, is creating a need for complex solutions. Consider the rapid urbanization that is occurring across these growth markets, urbanization is not just about constructing new buildings and roads, it involves a very complex multi-disciplinary set of capabilities around sustainable urban planning, waste management, security & governance, healthcare systems, digital infrastructure amongst others. Further, the growth markets have the added complexity around scale, speed, sophistication and constraints around resources. Therefore we believe there is a significant requirement of knowledge intensive capabilities across the growth markets to address their respective growth bottlenecks.

The growth imperative



Growth markets[3]



Paradoxically, the mature economies' knowledge intensive companies are ideally placed to provide many of the sophisticated goods and services that are in demand; but they have not been particularly successful at capitalising on their opportunity. While companies based in the growth economies are building their own knowledge intensive capabilities, a number of these sectors remain the areas where mature economies retain greatest comparative advantage. Yet we believe that companies can do a lot more to target this demand – although they will need to raise their ambitions and rise to the challenges of expanding into foreign countries with different business practices and immature governance standards.

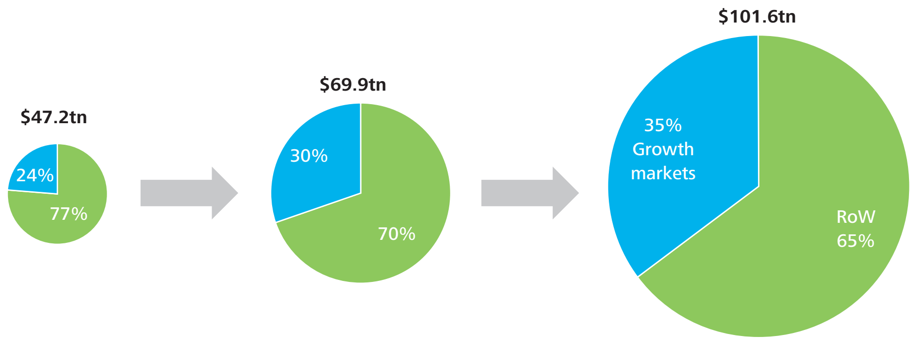
The UK illustrates the failure of mature economies to take advantage of their competitive edge in this field. Recognised as a leading knowledge economy, its knowledge intensive companies have particularly strong positions in sectors such as business services and professional services, education, health services, medical equipment and pharmaceuticals. Within the UK economy, the value-added by the knowledge intensive industries as a proportion of GDP was nearly 40% in 2010[4]. This figure is the fourth highest proportion amongst OECD countries and compares very favourably to a growth markets average of c.21%.

Yet the UK continues to punch below its weight in these growth markets, as its companies stick to old trading relationships rather than venturing further afield into growth markets. Its major trading partners remain the US and Europe, while exports to the fast-growing markets represent c.16% of the total[5]. Similarly, in 2011, 67% of the country's foreign direct investment was directed towards the US and EU27. As a result, the largest 100 companies headquartered in the UK still earn more than 70% of their revenues in the US or Europe[6].

While this mismatch between growth market demand and mature economy supply is already in evidence, the growth market's continuing superior growth will amplify the discrepancy. In the next decade, the GDP of these markets and their imports will expand exponentially. According to our analysis, the 20 high-growth countries identified by UK Trade & Industry as growth markets will increase their share of global GDP from approximately 30% in 2011 to more than 35% by 2020. At the same time, their imports will swell from £12.6 trillion to £25.0 trillion.

Global GDP, 2000-2020[7]

$tn(real 2011 prices), %



	2000	2011	2020
Growth markets share of global imports	21%	33%	41%

Rest of the world · Growth markets

Based on our studies of individual cases, and extensive UK client interaction, we believe there are several reasons for knowledge intensive companies' failure to take advantage of the opportunity offered to them by growth markets. Lack of ambition is partly to blame, as companies simply seek to continue trading nearer to home and lack the foresight to eye opportunities in growth markets. Another explanation is the tendency to project successful formats developed within headquarters into new markets without understanding local nuances. Finally, knowledge intensive companies often simply do not have the contacts or understanding of what it takes to do business in some of these countries.

That said, there are outstanding examples of success. Our analysis has shown that the companies that have been successful in growth markets tend to share a common characteristic – a purposeful approach to building and maintaining local ecosystems. Local ecosystems have helped some of the UK's most successful companies to overcome the difficulties of expanding into these markets, mitigating risk while bridging cultural differences, and managing geographical and political complexities.

What do we mean by ecosystems? An ecosystem is a network of organizations and individuals that co-evolve their capabilities and roles, and align their investments, so as to create additional value and/or to improve efficiency[8]. Ecosystems are by no means a radically new idea. Studies of the woollen textile cluster in 14th Century Prato, Italy, show how specific companies both contributed to and leveraged upon the mutual strength of a network[9]. Today the technology industry gives ample evidence of ecosystems at work. Companies such as ARM Holdings, Google and even Apple (which has traditionally preferred a tightly integrated business model) have gained success by powerfully shaping the formation of business ecosystems around them that have helped to fuel growth and to enhance returns.

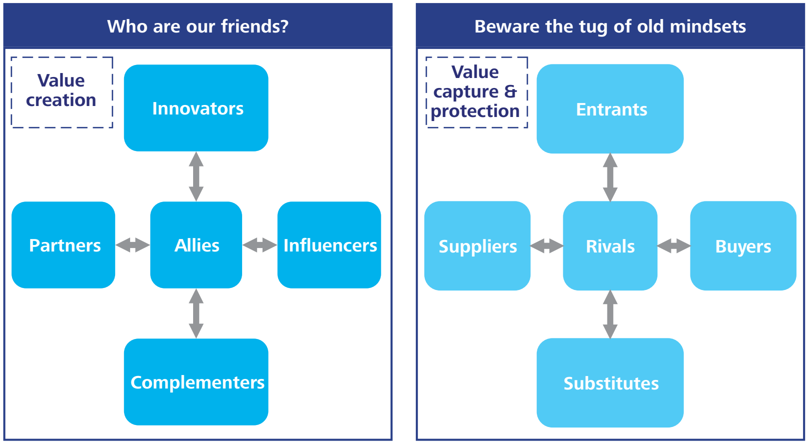
Clearly, not every strategic opportunity needs to be addressed by an ecosystem approach. Our analysis of UK champions shows that ecosystems work best where knowledge is a key resource that tends to be dispersed among different organisations around the globe, and where there is considerable uncertainty – which in turn means companies have to be flexible about how they create value. Such is the complexity of high-end knowledge intensive sectors that individual companies rarely possess the capabilities to construct the end goods and services all by themselves. They need to engage a diverse group of stakeholders, which bring different assets and capabilities to develop the required solution. Furthermore, ecosystems have particular advantages for mature-economy companies operating in fast-growing markets, which have inherent intricacies and uncertainties.

On the other hand, for standardised services where economies of scale and operational efficiency are critical, the ecosystem system approach is less useful and can even be detrimental given the inherent transaction costs involved in coordinating ecosystem players. So, for example, while an ecosystem approach might be invaluable for complex business or urban management service providers, it would not be useful for a bottle-cap contract manufacturer.

The ecosystem model allows businesses to focus on their core operations, to cope with rising investment demands, and to adjust to changing situations. While typically facilitating a global delivery model, it also allows companies to manage economies of both scale and scope. But in order to make the ecosystem model work, companies need to change their mindsets – promoting a behaviour and culture of collaboration throughout their organisations, and casting off old competitive attitudes.

A business ecosystem typically consists of a dynamic combination of innovators, allies, partners, influencers and complementors. Critically, successful participants in ecosystems have a collaborative mindset when creating value – they have moved away from a defensive approach, looking for quick payoffs and constantly protecting themselves, to a more collaborative mindset that co-creates value.

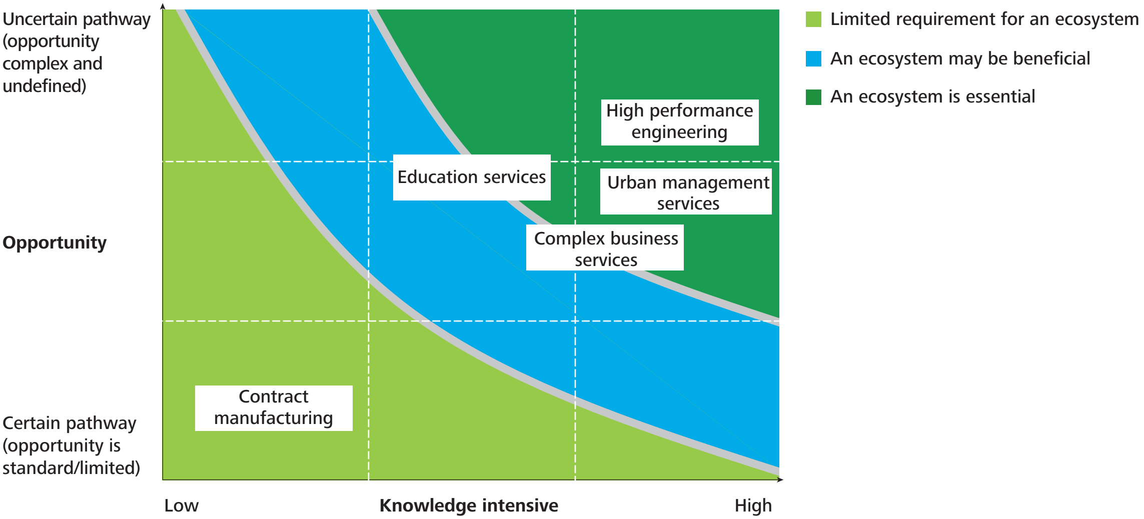
Typical players in an ecosystem[10]



Generally speaking, successful ecosystems benefit all parties – not only mature economy companies seeking to expand but also growth-market collaborators seeking greater understanding of the knowledge champions' capabilities.

In the strategy framework below, we have selected examples that, we believe, show where ecosystems are most effective. In the brief case studies that follow, we have then taken some UK knowledge champions that are examples of the framework and have shown how they are using ecosystems to navigate complex paths to market.

An ecosystem view – select examples[11]



> Arup: Building the 21st Century mega-cities

When Arup designed the iconic ‘bird’s nest’ Beijing stadium for the 2008 Olympic Games, it demonstrated its role in shaping China’s modern landscape, and its position as one of the few global firms of designers, planners, engineers and consultants. Founded in 1946 with an initial focus on structural engineering, London-headquartered Arup has invested a lot of time in building a business ecosystem that helps it to adapt its world-class expertise to a local context.

The partnership’s leaders are dedicated to finding the right ecosystem collaborators to work with – those that share its values and ambitions. For example, Arup is the primary technical adviser to C40, a network of the world’s mega-cities acting to reduce greenhouse gas emissions. Arup has run several workshops with leaders of fast-growing mega-cities such as São Paulo and Ho Chi Minh City to identify strategic pathways to tackling climate change, helping them to design and manage current and future mega-cities in a sustainable way. In turn, stakeholders perceive Arup as a global thought leader in sustainable urban management, and invite it to participate in critical projects

More than 60 years after inception as a UK firm, Arup has almost 11,000 employees in more than 90 offices around the world. Almost a quarter of its staff works in China, where the firm’s innovative and sustainable designs have significantly influenced urban development. Arup regards developing the optimal ecosystem as critical to its success.

“The best way to win work in China today is to go back 20 years and start building relationships,” says Arup chairman Philip Dilley.

> McLaren Automotive: Delivering the F1 performance experience to road cars

Launched in 1989, McLaren Automotive is a relatively young company that is using its dealer ecosystem to expand swiftly in growth markets. The company sits at the intersection of high performance, high-end luxury and high priced product segment. The luxury sports car company has high ambitions for expansion in the next few years, and expects at least a third of its growth to come from fast-growing markets such as Brazil, China, Malaysia and the Middle East.

McLaren Automotive's ecosystem includes both its F1 racing sister company and its dealer network. In 2012, the growth markets hosted approximately 40% of F1 races, up from just two in 2000, and McLaren Automotive leverages these Grand Prix events to enhance the appeal of its cars. McLaren also invests a lot in its dealer network in these markets, regarding the network as critical partners. After a rigorous selection process, McLaren actively trains and supports them, enabling them to offer world-class service. The dealer network in growth markets (e.g. Chengdu China) provides the team at McLaren's headquarters with valuable insights into the local mindset of consumers to help customize its offering for the growth markets.

In the next five years, McLaren Automotive intends to expand its range of cars and to grow its sales significantly, while competing against some of motorsport's greatest brands. Its ecosystem in growth markets will play an essential role.

"We consider the local dealers to be a critical player in our growth markets ecosystem. To ensure the right fit, we ensure a stringent selection criterion; arguably it is easier to get into Harvard than getting selected as a McLaren dealer," says Anthony Sheriff, CEO, McLaren Automotive.

> Markit: Springboard for regional players to integrate with global financial community

Just 10 years after its inception, Markit has grown to over £500 million in revenues with over 2,800 staff in 20 offices globally. The company provides information, financial transaction processing and business solutions customers in over 70 countries. In creating this thriving business, Markit has built a complex ecosystem in the developed markets of the US and Europe, which it is extending into the growth markets.

Markit's primary opportunities remain in the mature economies, where it partners with some of its competitors in an ecosystem and distributes their data to its customers, making sure they receive the information they need through their channel of choice. But Markit increasingly sees a role for itself as a key partner to the growth markets' regional financial institutions. As the emergent financial institutions increasingly look to expand and become global players, they can leverage organizations like Markit to access best-in-class financial services and to learn from their expertise to compete effectively against global leaders.

This reverse view of the business ecosystem allows Markit to deliver value to the next generation of financial services leaders across these growth markets. For example, a bank in China that has traditionally focused on its local market could gain access to other global financial institutions through the Markit trade-processing network. By partnering with Markit, it would be able to access liquidity and international growth opportunities.

"Although traditionally we have used our ecosystem model to build a robust and sustainable business in the developed world, we now see ourselves acting as a key player to emergent companies in the growth economies as they seek to build out their financial services ecosystems across the developed world in order to succeed," said Lance Uggla, CEO of Markit.

Concluding thoughts

Building an ecosystem in order to thrive in a fast-growing market often takes more than a willingness to embrace open innovation or to build a "hub-and-spoke" structure of multiple alliances. An ecosystem has many complexities, like a jigsaw puzzle that needs to decoded and assembled carefully.

As part of a strategic initiative to help stimulate growth in the UK economy, Deloitte UK has created 'UK Futures', a multi-year programme to assess and facilitate how business can drive UK growth. Under this broader charter, Deloitte has identified a few critical topics such as international ecosystems. To this end, Deloitte's 'Ecosystem-in-a-box' programme will help decode the core elements of the ecosystem puzzle, to enable our global clients to mitigate risks as they shape and develop international ecosystems, especially in growth markets.

As a key step in this exercise, we hosted a discussion at Davos in January 2013, alongside the World Economic Forum, with representatives from the organisations used as case examples, to hear and debate their views. Following this, we have now begun the next stage of our research in which we are investigating the relevant efficacy of ecosystems against other collaboration models, and how firms should structure their ecosystem initiatives to simultaneously create and capture value. In the later part of the year, we will be communicating the key findings, describing what constitutes best practice in shaping and managing ecosystems.

Further, Deloitte has also launched a growth escalator program for CEOs from high potential mid-market UK companies to help them bridge the gap between ambition and outcome.

For more information please visit our website: www.deloitte.co.uk/ukfutures

UK Futures

Deloitte UK has created "UK Futures", a multi-year programme to assess and facilitate how business can drive UK growth. The aim of this strategic initiative is to identify the key opportunities and challenges facing British businesses and articulate the key interventions that would enable these businesses to both create and capture value in the changing global landscape.

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Endnotes & sources

Endnotes

(a) The 20 countries identified by UKTI are Brazil, China, Colombia, Egypt, Hong Kong, India, Indonesia, Malaysia, Mexico, Qatar, Russia, Saudi Arabia, Singapore, South Africa, South Korea, Taiwan, Thailand, Turkey, UAE and Vietnam

(b) The import figures for 2011 and 2020 are nominal

(c) The global middle class is defined as those households with daily expenditures between $10 and $100 per person in purchasing power parity (PPP) terms

(d) The knowledge intensive sectors identified by the OECD 2010 research are transport, storage and communications; financial services; real estate, renting and business activities; education; health and social work. The high-technology manufacturing sectors are pharmaceuticals; computers and office machinery; semi-conductors and communications equipment; scientific instruments; aircraft and spacecraft

(e) In 2011, exports to the 20 UKTI growth markets represented 16.7% of total UK exports

Sources

1. United Nations, Deloitte LLP

2. Brookings Institution, International Monetary Fund (IMF)

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6. OECD, IMF, Mint UK, Company annual reports, Deloitte LLP

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8. J.H. Moore, “Predators and Prey: A New Ecology of Competition,” Harvard Business Review, 71/3 (May/June 1993): 75-86

9. M. Lansiti and R. Levin, The Keystone Advantage: What the New Dynamics of Business Ecosystems Mean for Strategy, Innovation, and Sustainability (Boston, MA: Harvard Business School Press, 2004), p. 124

10. Building resources for competitive success, Prof. Dominic Houlder, London Business School

11. Deloitte LLP research

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