The Economist Intelligence Unit

Re-drawing the ASEAN map

How companies are crafting new strategies in South-east Asia

A management brief sponsored by Baker & McKenzie CIMB

Preface

Re-drawing the ASEAN map: How companies are crafting new strategies in South-east Asia is an Economist Intelligence Unit (EIU) report, sponsored by Baker & McKenzie and CIMB. The research was conducted by the Economist Corporate Network (ECN), a division of the EIU. The findings and views expressed in this report are those of the ECN alone and do not necessarily reflect the views of the sponsors.

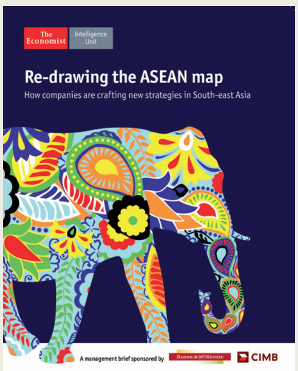
Justin Wood was the author of the report. The cover image is by Shutterstock.com.

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

November 2014

Interviewees, in alphabetical order:

Dilip Kumar Agarwal, CEO, **Indorama Ventures**
Matt Bradley, president, ASEAN, **Ford**
Scott Cassin, chief technologist and strategist, **Asia Pacific, Hewlett Packard**
Chris Fossick, managing director, South-east Asia, **Jones Lang LaSalle**
Anuj Lal, managing director, ASEAN, **Kimberly-Clark**
Munir Abdul Majid, chairman, **Bank Muamalat**
Satish Shankar, managing partner, South-east Asia, **Bain & Co**
VR Srivatsan, managing director, ASEAN, **Autodesk**
Vaidyanath Swamy, CEO, **N-Vision Consulting**
Peter Ter Kulve, president, ASEAN, Australia and New Zealand, **Unilever**
Mike Van Breugel, CEO, South-east Asia, **Siegwerk**



The picture of an elephant on the cover of this report serves as a metaphor for the unfolding character of the ASEAN region. The elephant, which is native to much of the region, is an unusual beast, constructed from a bizarre assembly of parts: trunk, tusks, giant ears, barrel-like body, whimsical tail. In the same way, ASEAN is a collection of unusual and diverse countries. At first glance, the parts don't appear to fit together with any sense of cohesion or design. And yet, when the different parts of ASEAN are combined, they do indeed form a powerful entity, just as in the case of the elephant. For companies, the trick is learning how to ride this powerful, colourful, yet unusual beast.

Contents

1. Introduction

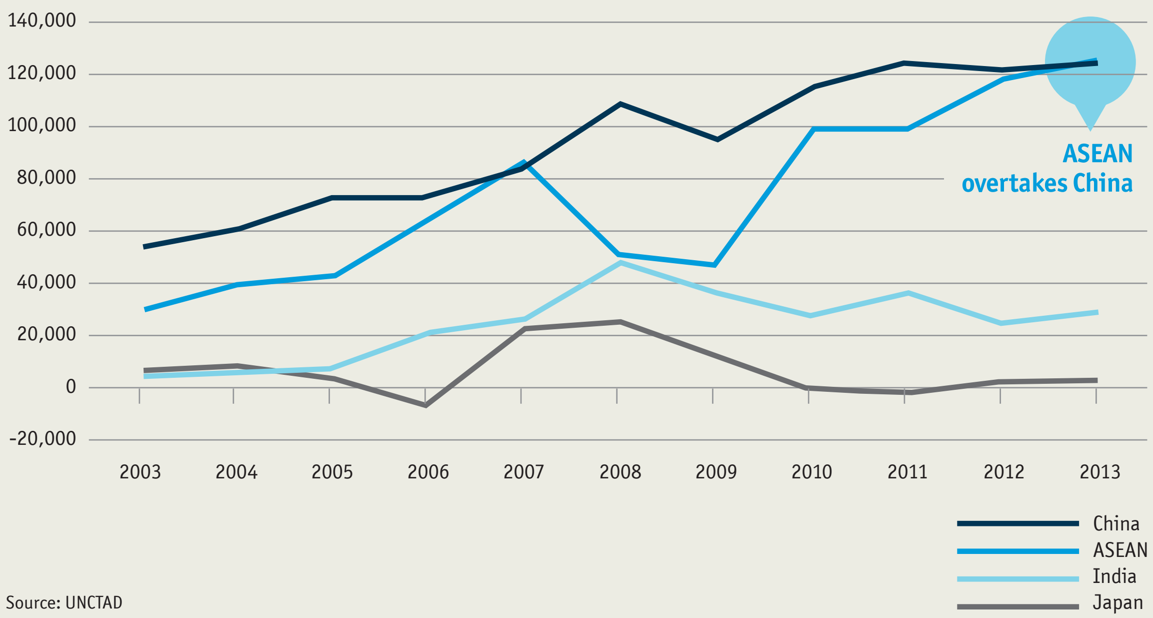
The profile of the ASEAN bloc is soaring. We survey 171 large companies to understand their strategy in the region

The 10 economies that make up the Association of South-east Asian Nations (ASEAN) stand out as being one of the most exciting parts of the world. For evidence, consider flows of foreign direct investment (FDI). Not only have they reached record levels in ASEAN, but in 2013 they overtook China. (See chart 1.) The profile of South-east Asia, and the ASEAN bloc that connects the region, is clearly rising around the world.

Companies investing in the region—both local and foreign—face a landscape of tremendous opportunity. But to capture it, they naturally face many strategic challenges and decisions. One of the biggest considerations is the degree to which businesses can treat ASEAN as one integrated bloc. Should businesses think of ASEAN as one economic unit and address it with a single, region-wide strategy? Or should they instead attach importance to the differences between countries and treat each of them individually?

Undoubtedly, the region is becoming more deeply integrated in many ways. One of the most prominent forces for integration comes from the ASEAN Secretariat and its efforts to create an ASEAN Economic Community by the end of 2015. The goal is to forge a single market and production base that stitches together 10 countries—most of which are relatively small on their own—into a coherent, integrated whole, with meaningful size and scale.

Chart 1
Value of annual foreign direct investment inflows (US$ millions)



Source: UNCTAD

In many ways, ASEAN nations are trying to re-draw the regional map by de-emphasising national boundaries. But to what degree do companies think this is possible? Is it useful? And how is it impacting their strategy? As such, the Economist Corporate Network has written this report in order to:

- Discover whether companies are thinking of ASEAN as one integrated economic unit or as 10 separate economies;
- Understand the trends that support a regional approach to strategy in ASEAN and the issues that stand in the way;
- Describe the different strategies that different types of company are pursuing in the region.

In researching this report, we surveyed 171 business leaders running operations in the ASEAN region. They came from a broad mix of industries, and worked at large companies: 78% had global revenue of more than US$1bn.

Respondents mostly worked for non-ASEAN companies (only 14% had their global head office in the ASEAN region). Nearly half of the sample (47%) had manufacturing plants in ASEAN. Some 60% of respondents worked at companies that were primarily business-to-business (B2B), while 40% were primarily focused on consumers (B2C). (See Appendix on page 40 for further details.)

We also conducted 11 in-depth interviews with a range of business heads running ASEAN operations in order to gain deeper insight.

In many ways, ASEAN nations are trying to re-draw the regional map by de-emphasising national boundaries. But to what degree do companies think this is possible? Is it useful?

2. ASEAN: Overcoming diversity?

Despite significant diversity and big hurdles, the 10 nations of ASEAN are becoming more integrated. Companies are confident that an ASEAN Economic Community is emerging

It would be hard to imagine 10 countries that are less similar than the member states of ASEAN. From an income perspective, Singapore, the richest country, has a per capita GDP that is 76 times bigger than in Myanmar, the poorest country in ASEAN. Indonesia's population of 251m is 600 times bigger than Brunei's 420,000 citizens. Political systems range from autocracy to democracy. Economic systems range from socialist to capitalist. Religions and languages are even more varied. (See table 1.)

Indeed, one of the only things that ASEAN countries appear to have in common is geographic proximity. And yet, despite this diversity, the region is rapidly integrating.

Bottom-up integration

Take regional trade. Between 2000 and 2013, the value of intra-ASEAN trade more than tripled to US$607bn. Or look at regional investment flows. Back in 2000, annual intra-ASEAN FDI stood at just US$0.9bn. By 2013, the figure had grown to US$21.3bn. Deepening regional integration is just as evident in the number of intra-ASEAN visitors. Back in 2000, ASEAN citizens visited another ASEAN country a total of 15.9m times. By 2012, that number had more than tripled to 39.9m visits.

The bulk of this deepening regional integration is a bottom-up process, and can be attributed to the efforts

Table 1
Key economic data for ASEAN and its 10 member economies

	Size of the economy (US$ billions)	Population (millions)	GDP per capita (US$)	Trend rate of annual economic growth (real GDP) 2013 to 2018 (%)
ASEAN	2,397.54	625.31	3,770	5.64
Brunei	16.18	0.42	38,760	3.10
Cambodia	16.20	15.14	1,070	7.44
Indonesia	868.35	250.80	3,460	6.18
Laos	11.00	6.78	1,620	7.35
Malaysia	313.16	29.72	10,538	5.64
Myanmar	44.85	61.95	724	7.06
Philippines	272.07	98.39	2,770	5.94
Singapore	297.94	5.40	55,183	4.76
Thailand	387.25	67.01	5,780	4.49
Vietnam	170.55	89.71	1,901	6.38

Source: Economist Intelligence Unit; data for 2013 of individual companies and citizens. It's only natural that when companies grow, the first place they look for opportunity is in the countries closest to them. Similarly, as ASEAN citizens get wealthier and more educated, and as they start to travel in search of jobs and holidays, the first countries they visit are their neighbours.

Top-down integration

However, top-down policies from the ASEAN Secretariat also deserve some credit. When the ASEAN organisation began life in 1967, territorial disputes in the region were commonplace, the spread of communism was perceived as a major threat, and political instability was widespread. As such, the goal of ASEAN initially was to create a security union among neighbouring countries in order to promote regional harmony. That ambition has been achieved, creating a long era of peace during which South-east Asia has seen its economies grow and living standards rise dramatically.

In the years since 1967, the ASEAN bloc's aspirations have grown. In 1992, it signed the ASEAN Free Trade Area Agreement with the goal of reducing tariff barriers between member states. Today, almost all products can move across ASEAN without tariffs, although non-tariff barriers remain deeply entrenched.

Community spirit

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

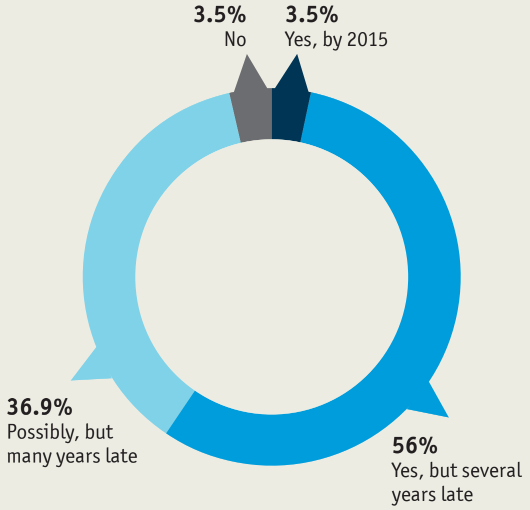
The idea for the AEC was born partly from recognition that deeper integration would support economic growth. Equally, it was forged against the rise of China and India. National leaders in South-east Asia hoped that, by joining together, ASEAN could become a formidable third economic engine in emerging Asia.

The vision behind the AEC is bold, but fraught with difficulty, not least because the process of integration requires sacrificing sovereignty, which ASEAN states have been reluctant to do. Some observers point to a lack of trust between ASEAN neighbours as a major hurdle to integration. Some raise concerns about protectionist sentiment in certain ASEAN countries, where powerful local industries are reluctant to open up to competition. Others highlight a lack of investment in the ASEAN Secretariat. Today it has a staff of less than 300, compared to more than 30,000 employed by the European Union civil service.

Buying into the AEC

Nonetheless, despite the difficulties, the formation of the AEC is pushing ahead. When measured against its own timetable for completion—for example the deadlines for implementing common industry regulations—the AEC is behind schedule. But, while the roll-out may be slow, business leaders remain convinced that the direction of change is positive. In our survey, nearly 60% of respondents expressed confidence that the vision of the AEC will be achieved. Only 3.5% said they thought it would fail. (See chart 2.)

Chart 2
Will ASEAN succeed in creating an economic community by the end of 2015? (% of respondents)



Source: Economist Corporate Network

3. ASEAN as one country

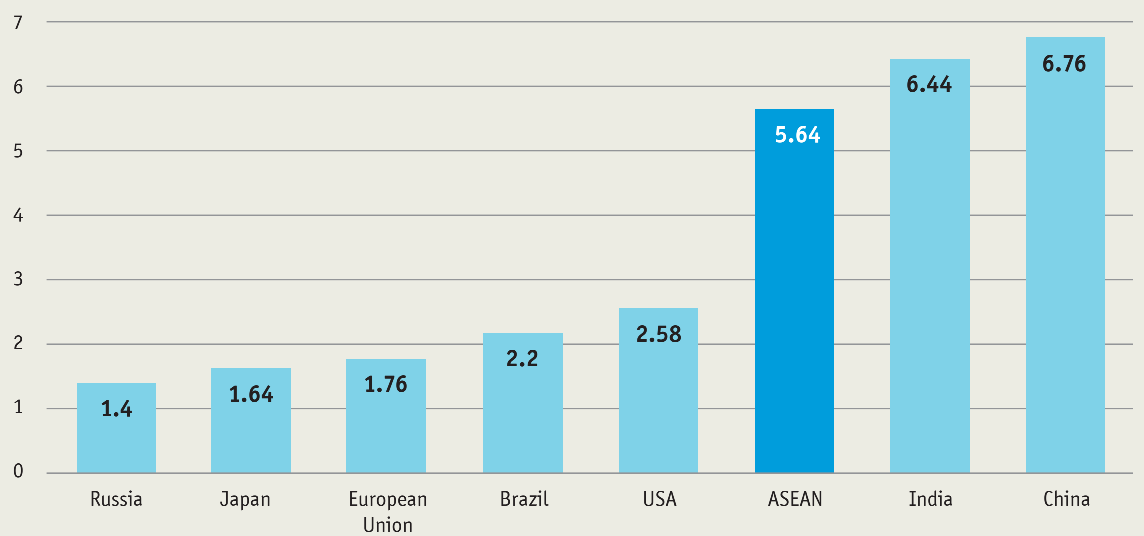
With integration pushing ever onwards, what would ASEAN look like as a single economic area?

If, as seems likely, the nations of South-east Asia succeed in creating an ASEAN Economic Community, what will it look like? If ASEAN is thought of as one integrated economic unit, what characteristics will it have? One simple exercise is to aggregate the region's data and think of ASEAN not as 10 countries but as one nation. On this basis, ASEAN is both big and interesting. (See table 2 on page 10.)

It is home to nearly 10% of the world's population, and ranks as the seventh largest economy. By 2018, it will be the world's fifth biggest economy, thanks to strong economic growth. Taken as a whole, the Economist Intelligence Unit expects ASEAN to grow by an annual average of 5.6% for the next five years. Indeed, ASEAN's growth rate will be only marginally behind India and China, and well ahead of other emerging markets such as Brazil and Russia. (See chart 3.)

14 of the top 100 BPO cities globally are found in ASEAN, more than any other "country"

Chart 3
Trend rate of annual economic growth (real GDP) 2013 to 2018 (%)



Source: Economist Intelligence Unit

People power

Many things will drive ASEAN's growth. Demographics are generally positive, with a young, growing population. Between 2013 and 2018, the region's labour force will expand by 1.7% a year, adding 28m new workers. Many of these workers will still have relatively low wages, and so will attract significant manufacturing investment, especially as China becomes more expensive. ASEAN is already the world's fourth biggest exporter, and will be the third biggest by 2018.

The population will become ever more urban. In 2013, the region had 317m urban dwellers. By 2018, that number will rise to 345m. That's around 5.5m new urban dwellers in ASEAN every year—the equivalent of adding a new city with a population the size of Singapore every year. (For more on urbanisation, see "ASEAN from an urban perspective" on page 23.)

This urbanisation, together with industrialisation, will drive investment into fixed assets such as infrastructure and housing. In 2013, ASEAN saw US$650bn invested into fixed assets, or 3.8% of the global total. By 2018, annual investment will rise to US$1.2trn, or 4.8% of global capital formation.

Productivity is rising across the region, especially in less developed countries, which is driving up incomes and creating a giant middle class. Indeed, the ASEAN consumer story is one of the world's most impressive. In 2013, the region had 36.3m households with a combined income of US$10,000 or more. By 2018 that will more than double to 79.7m households. The region is already the fifth biggest car market in the world, and the third biggest market for mobile phones.

Building mines and mining data

ASEAN is a big producer of commodities. It grows 90% of the world's crude palm oil, 70% of all natural rubber, and a quarter of the world's rice. It produces 6.4% of the world's natural gas, and 7.4% of its coal.

Internationally competitive service industries are also growing. Take business process outsourcing (BPO). Tholons, an outsourcing consultancy, recently listed the top 100 BPO cities globally, and found that 14 of them were in ASEAN, more than any other "country". Financial services are deepening, especially wealth management in Singapore, and Islamic finance in Kuala Lumpur—ASEAN was home to 74% of all Sukuk (Islamic bond) issuance in 2013. The region's stock exchanges are home to more than 6% of the world's listed companies, and plans are underway to link the ASEAN exchanges together in order to pool the region's trading activity.

Not everything is exciting. While some parts of ASEAN are highly developed and modern, many parts remain deeply poor. As such, research and development activity is thin. The number of patents registered by domestic ASEAN organisations is equal to only 0.3% of the global total. However, as education improves, as infrastructure is built, and as local companies grow, this will surely improve in the years ahead.

ASEAN is the third biggest market for mobile phones in the world

Table 2
What if ASEAN were one country...
What would ASEAN look like if it were one economy instead of 10?

	ASEAN figure	Share of global total	Rank in the world	Date
Economic				
GDP	US$2,398bn	3.23%	7th	2013
GDP in 2018	US$3,875bn	3.97%	5th	2018
Private consumption	US$1,333bn	3.12%	8th	2013
Private consumption in 2018	US$2,308bn	4.10%	5th	2018
Fixed asset investment	US$650bn	3.83%	4th	2013
Fixed asset investment in 2018	US$1,153bn	4.77%	5th	2018
Exports	US$1,568bn	6.84%	4th	2013
Exports in 2018	US$2,670bn	8.19%	3rd	2018
Financial				
Annual gross national savings	US$737bn	4.11%	4th	2013
Annual gross national savings in 2018	US$1,293bn	5.20%	3rd	2018
Foreign exchange reserves	US$782bn	6.59%	3rd	Q1 2014
Foreign direct investment inflows	US$125.4bn	8.64%	2nd	2013
Equity market capitalisation	US$2,203bn	3.44%	8th	2013
Number of listed companies	2,933	6.17%	8th	2012
Sukuk (Islamic bond) issuance	US$88.6bn	74.00%	1st	2013
Demographic and income				
Population	625m	9.54%	3rd	2013
GDP per capita in 2013	US$3,770	-	122nd	2013
GDP per capita in 2018	US$6,110	-	103rd	2018
Number of households with HH income of US$10,000 or more	36.3m	4.50%	7th	2013
Number of households with HH income of US$10,000 or more in 2018	79.7m	7.60%	3rd	2018
Muslims	234m	14.40%	1st	2011
Buddhists	191m	22.60%	2nd	2011
Christians	123m	5.16%	3rd	2011
Land and agriculture				
Land area	4.46m km^2	3.00%	7th	2013
Coastline	105,070km	29.51%	2nd	2013
Rice production (metric tons)	117.05m	24.35%	2nd	2013
Crude palm oil production (metric tons)	56.24m	90.20%	1st	2013
Natural rubber production (metric tons)	8.73m	76.31%	1st	2012
Poultry production (metric tons)	6.76m	6.83%	4th	2011
Business and technology				
Mobile phone subscriptions	702.45m	10.60%	3rd	2013
Facebook monthly users	162.9m	13.00%	2nd	Dec-13
Patents filed by local companies/organisations	4,078	0.30%	14th	2011
Number of cities in top 100 BPO locations worldwide	14	14.00%	1st	2014
Local companies in the Forbes Global 2000	72	3.60%	4th	2014
Flights (both domestic and international)	2.08m	7.00%	3rd	2013
Vehicle production (annual output of cars, trucks and buses)	4.36m	4.99%	7th	2013
Vehicle sales (annual sale of cars, trucks and buses)	3.58m	4.19%	5th	2013
Number of ports in the world's 100 biggest	7	7.00%	3rd	2012
Cargo volume (in metric tons passing through the world's 100 biggest ports)	1.07bn	8.79%	3rd	2012
Energy				
Production of natural gas (cubic metres a year)	216.bn	6.40%	3rd	2013
Consumption of natural gas (cubic metres a year)	148.6bn	4.40%	5th	2013
Proven reserves of natural gas (cubic metres)	5.5trn	2.96%	8th	2013
Production of coal (tonnes of oil equivalent annually)	287m	7.39%	3rd	2013
Consumption of coal (tonnes of oil equivalent annually)	113.8m	2.97%	5th	2013
Proven reserves of coal (tonnes)	29.4bn	3.30%	10th	2013
Production of oil (barrels a day)	2.45m	2.86%	12th	2013
Consumption of oil (barrels a day)	5.49m	6.02%	3rd	2013
Proven reserves of oil (barrels)	13.3bn	0.80%	16th	2013

Sources: Economist Intelligence Unit; IMF; UNCTAD; IATA; BP Statistical Review of Energy 2014; OICA; AAPA World Port Rankings; Pew Research Centre; World Bank; ASEAN Secretariat; CIA World Fact Book; FAO; ITU; Facebook; WIPO; Tholons; Forbes; US Department of Agriculture; MIFC; World Federation of Exchanges

If ASEAN were a single country, where would it rank compared to other countries?

1

- Crude palm oil production
- Natural rubber production
- No. of cities in top 100 BPO locations worldwide
- Size of Muslim population
- Issuance of Sukuk (Islamic bonds)

2

- Value of foreign direct investment inflows
- Length of coastline
- Rice production
- No. of monthly Facebook users
- Size of Buddhist population

3

- Size of overall population
- Size of Christian population
- Mobile phone subscriptions
- No. of flights (both domestic and international)
- Foreign exchange reserves
- No. of ports in the world's 100 biggest
- Sea-borne cargo volume
- Production of natural gas
- Production of coal
- Consumption of oil
- 2018 Value of exports in 2018
- 2018 Annual gross national savings in 2018
- No. of households with HH income of US$10,000 or more in 2018

4

- Value of investment into fixed assets (like infrastructure)
- 2013 Value of exports in 2013
- Annual gross national savings
- Poultry production
- Local companies in the Forbes Global 2000

5

- Vehicle sales (annual sale of cars, trucks and buses)
- Consumption of natural gas
- Consumption of coal
- 2018 GDP in 2018

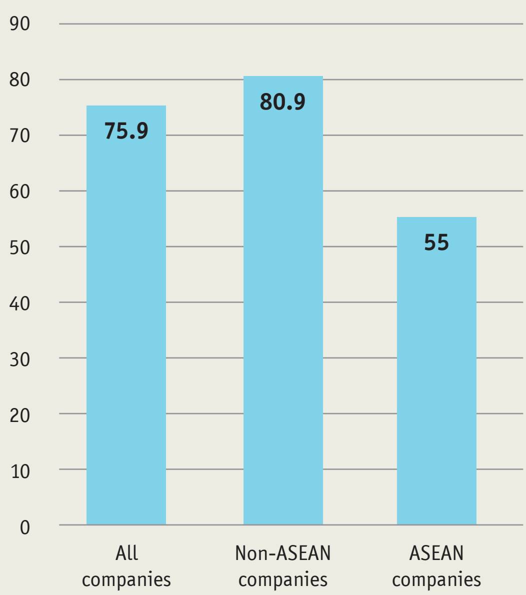
4. A pan-regional ASEAN strategy

Companies are increasingly managing the ASEAN region as an integrated economic area, with a pan-regional strategy

In order to capture the unfolding opportunity in ASEAN, companies are increasingly running their operations in the region with a single strategy oriented around the ASEAN area. Indeed, 76% of the companies in our survey say they have a strategy that is focused on the ASEAN bloc. They already think of ASEAN as an identifiable entity that demands its own strategy. (See chart 4.)

Interestingly, non-ASEAN companies are more likely to have a regional strategy (81%) than local firms (55%). Many theories exist to explain this difference, but the fact that local companies are generally smaller than global multinationals is likely to be a major factor. (See "Local catch-up?" on page 14.)

Chart 4
Share of companies that have a strategy oriented around the ASEAN region (% of respondents)



Source: Economist Corporate Network

Why strategise around ASEAN?

So why are companies choosing to craft strategies around ASEAN? What is the rationale? One major reason lies with the integration policies of the ASEAN organisation itself. When asked how important these policies were to their business, almost one third said "extremely important", while another 57% said "somewhat important". The Economist Corporate Network asked the same question of 147 companies in a previous survey in December 2012, and the results show that rising importance is being attached to these ASEAN policies. (See chart 5.)

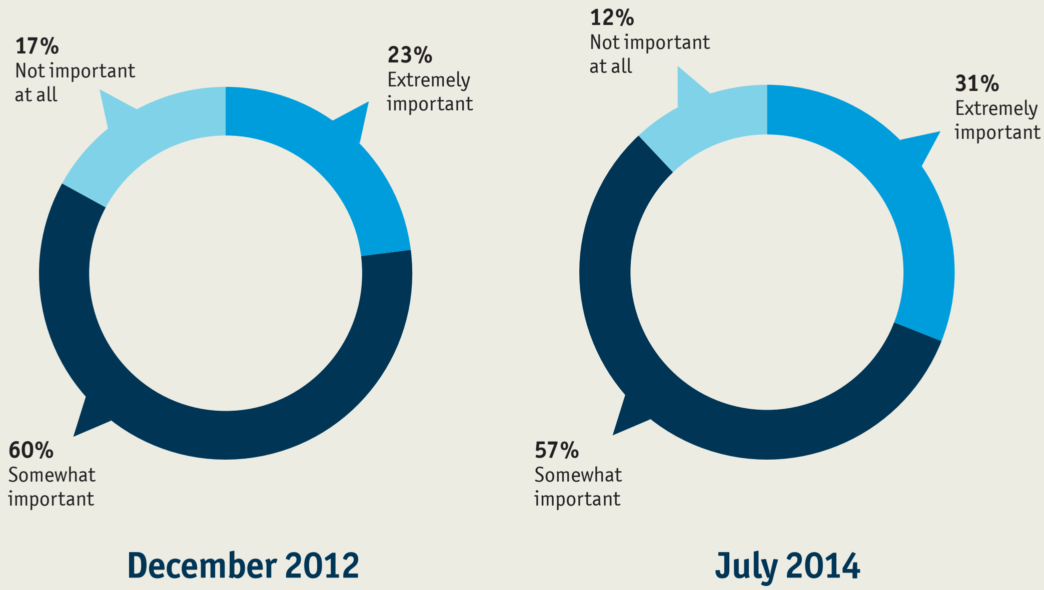
While the ASEAN Economic Community has a long way to go until it can be considered a true single market, it holds the promise of major benefits for companies operating in the region. For a start, companies will reap greater economies of scale and improve efficiency by harmonising their operations across a wider area. Having a single market will also help to reduce complexity, as companies will be able to standardise products, services, business models and marketing plans.

As capital markets become more joined-up, companies will be able to access deeper pools of liquidity for raising money. And as labour markets become more integrated, companies will find it easier to recruit, retain and manage their workforce on a regional basis.

Talking to companies in face-to-face interviews reveals a wide range of reasons behind building a strategy that is oriented around ASEAN:

1. The policies of the ASEAN Secretariat and its AEC project are helping to forge a more integrated regional market (see above). This enables companies to reap economies of scale across the whole region, reducing costs and complexity and raising efficiency.
2. Given falling trade barriers and deepening harmonisation of industry standards across ASEAN

Chart 5
How important are the integration policies of the ASEAN organisation in driving your ASEAN strategy? (% of respondents)



Source: Economist Corporate Network survey of 171 companies in July 2014 and of 147 companies in December 2012

(albeit slowly for many industries), companies are increasingly able to consolidate and centralise their manufacturing in ASEAN. Again, this opens up the benefits of greater scale, as well as reducing complexity. For some firms, falling trade barriers are opening up possibilities for greater fragmentation of their supply chains. Increasingly they can break up their activities into distinct parts and put them into places with the most appropriate costs and skills. (See chapter 11 on page 31.)

3. Companies feel that, despite the huge diversity across ASEAN, their customers are becoming more similar and can be served with a more unified approach. (See chapter 6 on page 19.)
4. In some cases, companies feel that the opportunities to harmonise and standardise their front office client-facing activities in ASEAN remain limited. However, they feel that back-office and sales support functions (such as finance, HR and planning) can be run on a regional basis. (See "Corporate insight", on page 15.)

> **"There is a lot of last-minute swatting. Companies are realising that the AEC will expose them both to more competition and more opportunity, so they're trying to catch up quickly."**
>
> **Munir Abdul Majid, chairman of Bank Muamalat**

5. Many companies recognise that, individually, ASEAN economies are small. This makes it hard to attract the right managerial talent needed to run them. But by combining the ASEAN 10 into a bigger cluster, companies are able to attract a higher calibre of managerial talent. (See "Corporate insight", on page 15.)
6. While ASEAN's economies are still highly diverse, they do share one important characteristic: high growth. As such, companies feel that it makes sense to have a regional management team co-ordinating and overseeing a strategy that is appropriate to a high-growth environment. (See "Corporate insight", on page 15.)
7. In the case of B2B companies, many recognise that their clients are increasingly adopting a pan-ASEAN strategy. This in turn means that it makes sense for them to do so too in order to serve their clients more effectively. (See "Corporate insight", on page 15.)

Local catch-up?

Many theories exist as to why ASEAN companies are less likely to have a regional strategy than their global peers. However, much of the difference is likely to be caused by company size.

While ASEAN does have giant corporate champions, many local firms are still small by the standards of global multinationals. As such, they may still operate solely in their home market, or they may operate only in ASEAN, and therefore have no need to differentiate their local strategy from other parts of the world. Being small may also make them opportunistic, expanding into new ASEAN countries without having a highly-formed regional plan. Equally, their smaller size makes them less likely to have the in-house legal, regulatory and management expertise to make full use of the opportunities that ASEAN integration policies have to offer.

Nonetheless, observers express confidence that the situation is changing swiftly. Munir Abdul Majid, chairman of Bank Muamalat, a Malaysia-based bank, says awareness of ASEAN's regional potential has only just taken hold. "Many of the small and medium-sized enterprises in ASEAN have been very happy with the growth rates in their home country and didn't see a need to go out into the region. Sure, their costs were rising, but growth was good and they were comfortable. So they've tended to be a bit absent-minded about the regional picture," he notes.

"But with the arrival of the AEC in 2015, that complacency is changing, perhaps more in countries like Malaysia, Singapore and Thailand than the others. Companies are now behaving as if they have an exam coming up. There is a lot of last-minute swatting. Companies are realising that the AEC will expose them both to more competition and more opportunity, so they're trying to catch up quickly."

Corporate insight: Reasons for an ASEAN strategy

To attract management talent

"One of the main reasons for having a pan-ASEAN focus is to attract management talent. Individually, one country in ASEAN might only be worth US$50m to US$100m, and it's hard to attract top talent for a business of that size. But if you put all the economies together then the region becomes much more interesting."
-Satish Shankar, managing partner, South-east Asia, at Bain & Co, a strategy consultancy

To match the needs of clients

"The AEC is making progress. It's slow, but it's not going backwards, and it opens opportunities for us to take a more regional approach. Importantly, our clients, like the big FMCG companies, are also taking a regional approach, and that feeds down into our own organisational structure."
-Mike Van Breugel, CEO, South-east Asia, at Siegwerk, an ink manufacturer for the packaging industry

To co-ordinate a high-growth approach

"We re-organised our activities into an ASEAN-focused unit, with a regional management team back in 2006. In part it was about recognising that these are all high-growth economies and we wanted to have a co-ordinated approach to capturing the growth. Equally, many of the markets were still quite small, so it made sense to cluster them together. More recently, we've found that our clients are also organising on an ASEAN basis, and they want us to do the same. If we're managing a portfolio of property for them across the region, we need to be consistent."
-Chris Fossick, managing director, South-east Asia, at Jones Lang LaSalle, a real estate services firm

To reap back-office and sales support efficiencies

"Our approach to sales in ASEAN is still very local and in-country. One or two of our channel partners are becoming more regional, but they are still the exception. However, all the functions that support our sales are organised on a regional basis, the finance team, HR and marketing. There's a lot of scope for integrating that side of the business across ASEAN… Another important trend that supports a regional strategy is the ASEAN Economic Community. This will increase competition, which is an important story for a business like ours that helps companies to be more competitive."
-VR Srivatsan, managing director, ASEAN, at Autodesk, a design and engineering software company

5. Towards a full ASEAN footprint?

Truly regional sales platforms are emerging as companies expand their footprint across ASEAN. Big companies now sell into almost every ASEAN economy, and small companies are close behind

Where in ASEAN are companies focusing their sales efforts? Stripping out local companies from the results, in order to remove home bias, our survey reveals two groups of markets.

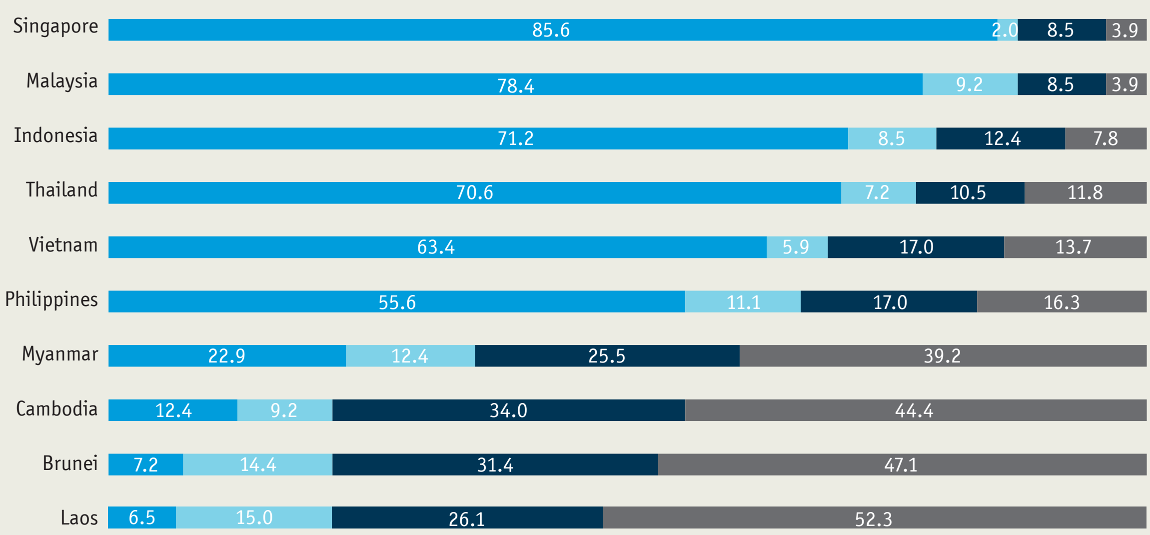
The six biggest economies in South-east Asia—Indonesia, Thailand, Malaysia, Singapore, the Philippines and Vietnam—all have a high degree of penetration by companies. The majority of the international firms in our survey have their own sales team on the ground in all of these countries. The four smaller economies of Myanmar, Cambodia, Brunei and Laos have a notably lower penetration. Sales in these four are much more likely to be via local distributors and partners. (See chart 6.)

Building a pan-ASEAN sales platform

When the results are analysed by company size, it's clear that bigger companies operate in more countries than small ones. (See chart 7.) Companies with global revenue of US$10bn or more, now sell into an average of 8.4 countries in ASEAN. But even small companies, those with global revenue of less than US$1bn, still sell into an average of 6 countries.

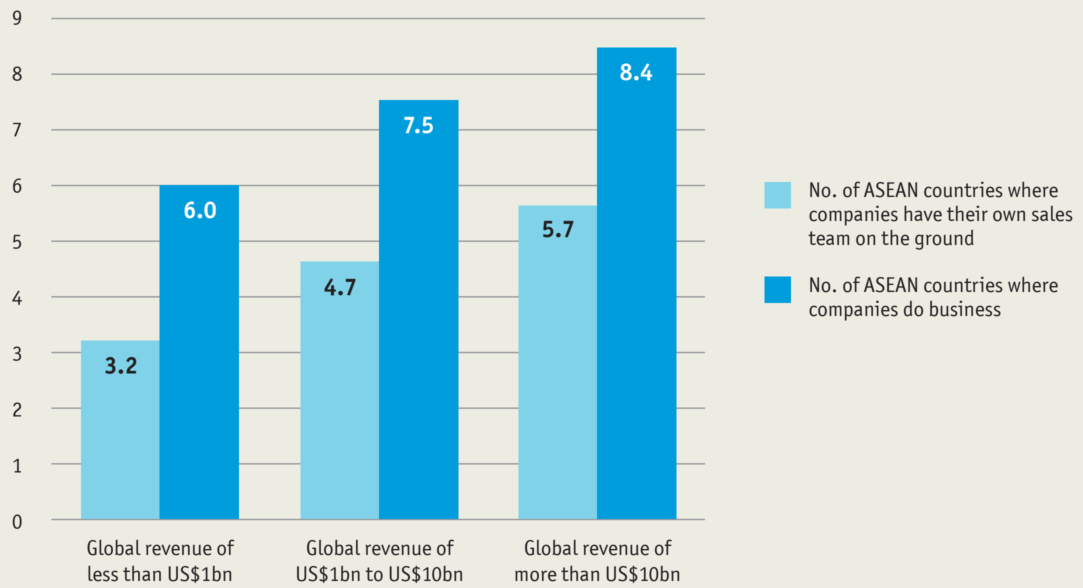
This suggests that companies are building a pan-ASEAN sales platform that serves the entire region. Even the smallest of ASEAN's markets are attracting interest. Laos is a tiny economy, but it is still a viable market for almost half the companies in our survey.

Chart 6
Do you do business in these ASEAN markets? (% of respondents)*



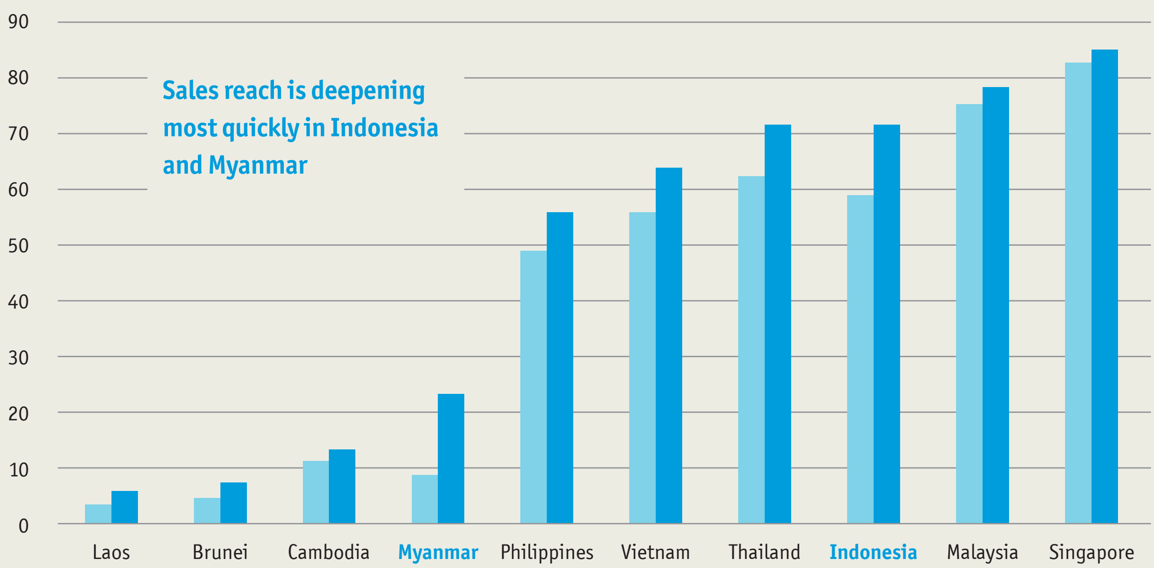
Source: Economist Corporate Network
* Results are only for non-ASEAN companies

Chart 7
Average number of ASEAN economies where companies are active, broken down by company size*



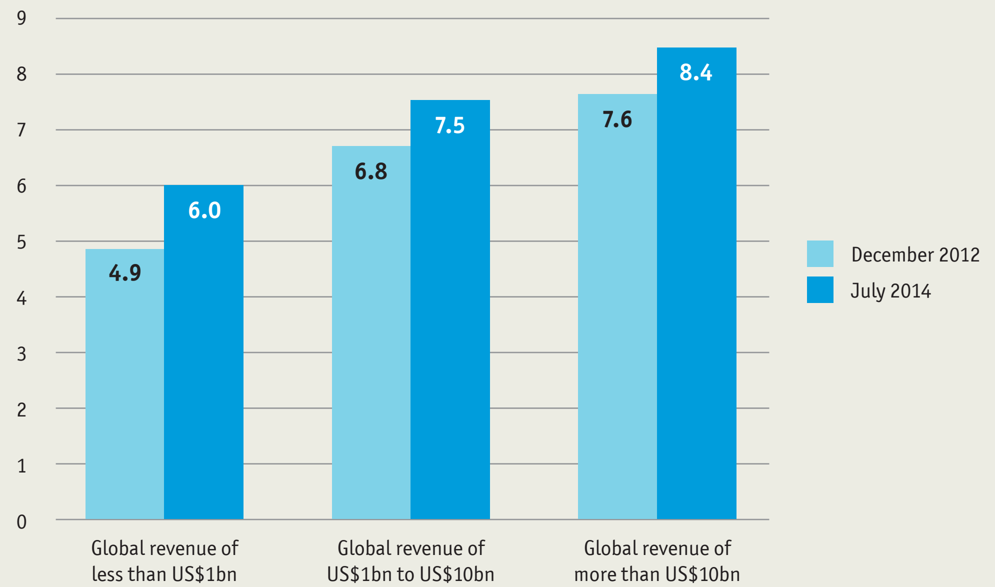
Source: Economist Corporate Network
* Results are only for non-ASEAN companies

Chart 8
Do you have your own sales team on the ground in these ASEAN markets? (% of respondents)*



Source: Economist Corporate Network survey of 171 companies in July 2014 and of 147 companies in December 2012
* Results are only for non-ASEAN companies

Chart 9
Average number of ASEAN economies where companies are active, broken down by company size*



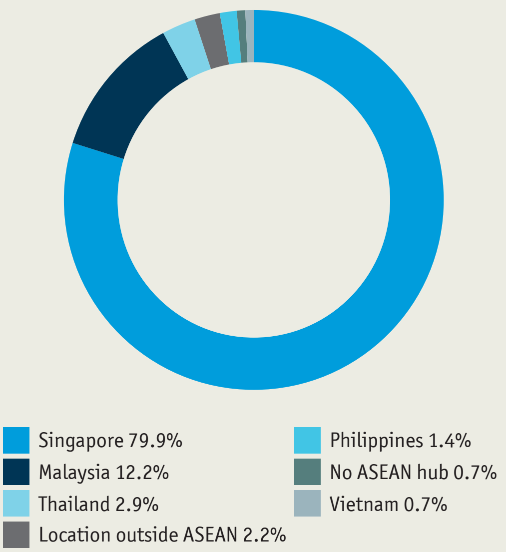
Source: Economist Corporate Network survey of 171 companies in July 2014 and of 147 companies in December 2012
* Results are only for non-ASEAN companies

And this regional sales platform is growing. Comparing these results to a similar survey conducted in December 2012 shows that international companies are deepening their presence in every single ASEAN country. The places with the most rapid deepening of sales reach are Indonesia and Myanmar. (See charts 8 and 9.)

Running regional hubs

Given this deepening pan-regional presence, we asked the global multinationals in our survey about the location of their ASEAN management team. The clear leader is Singapore, with 80% of firms running their regional head office there, followed by Malaysia with 12.2% of firms. Less than 1% of companies say they do not have an ASEAN head office. (See chart 10.)

Chart 10
From where do you manage your ASEAN operations? (% of respondents)*



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

6. Towards a common customer?

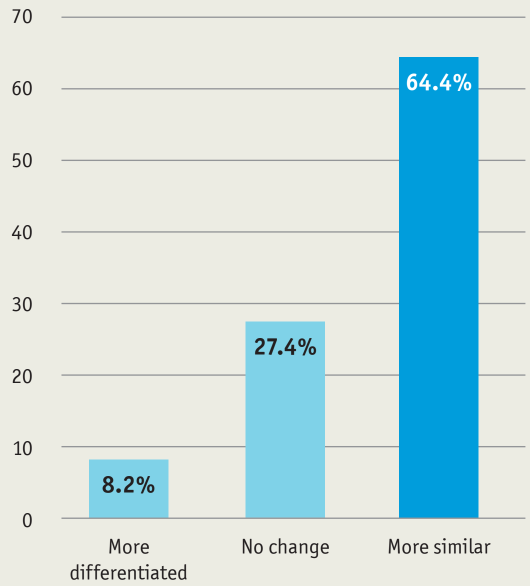
ASEAN markets remain highly diverse, but companies say that their customers across the region are becoming more uniform. This is helping to standardise products and services

If companies are to treat ASEAN as a single market, then there must be uniformity across the 10 economies. This uniformity can take many forms. For a start, companies need harmonisation of the operating landscape, such as standardised laws and business regulations, and uniform product and service standards. In many cases, these issues remain far from harmonised, and stand as barriers to a single market. (See chapter 9 on page 27.)

But even more important is the uniformity of customers:

- How diverse is their purchasing power?
- How varied are their tastes and preferences?
- Can customers across ASEAN be served with the same set of products, services, brands and business models?
- Or is ASEAN better addressed as a patchwork of highly individual markets?

Chart 11
Are your customers across ASEAN becoming more similar or more differentiated? (% of respondents)



Source: Economist Corporate Network

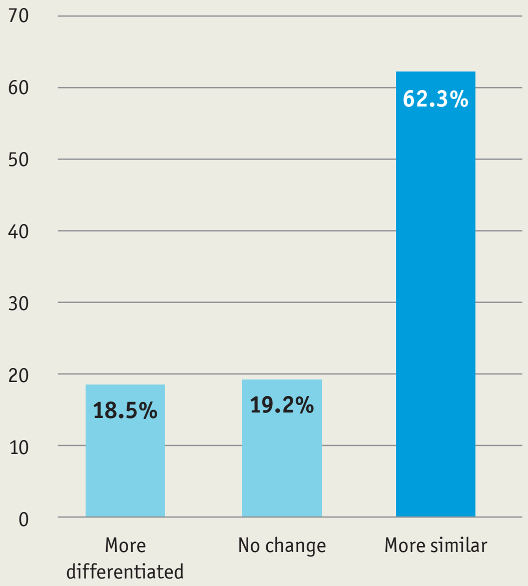
Diminishing diversity

Interestingly, companies in our survey report that their customers are indeed becoming more similar to each other. ASEAN continues to have all kinds of diversity, both between countries and within countries. But despite this diversity, almost two thirds of business leaders in ASEAN say their customers are growing more alike. Only 8% say they are becoming less similar. Diversity appears to be diminishing. (See chart 11.)

This trend towards a more homogenous customer base often emerges within specific segments of purchasing power. Countries as a whole may still differ greatly from one another, but certain categories of customer within each country may be growing more similar. This is especially true at the premium end, where customers are more exposed to global business practices and cultural trends.

This increasing uniformity of customers is feeding through into uniformity of offering. Respondents to our survey say that the products and services they provide across ASEAN are becoming more similar. Indeed, 62.3% of companies say they are standardising their offering across ASEAN, while only 18.5% say they are doing the opposite. (See chart 12.)

Chart 12
Are your products and services across ASEAN becoming more similar or more differentiated?
(% of respondents)



Source: Economist Corporate Network

Of course, the degree to which products and services are harmonised across ASEAN depends on many things. Some of the considerations include:

- **B2B or B2C**
  Companies selling to business customers are generally much more able to offer a standard set of products and services than those that cater to consumers. The way that businesses buy computers or financial services or industrial goods is much more standard than the way that consumers buy shampoo or watch TV.

- **Purchasing power**
  Both B2B and B2C companies need to tailor their offering to match the purchasing power of their customers. Across ASEAN, incomes and spending ability do vary greatly, and companies continue to adjust both their product mix and their prices by market across the region. However, this variability doesn't necessarily prevent a pan-regional approach.

  Indeed, every market across ASEAN has within it both wealthy and less affluent customers. Some companies are adopting common regional strategies for different income segments. For example, the top income segment in all 10 ASEAN economies might be targeted with a uniform product set and marketing plan, with a different pan-regional plan for each income group beneath that.

- **Categories**
  Certain categories of goods are much more sensitive to local tastes. For example, food is notably hard to standardise across different ASEAN markets because local tastes vary sharply. Such products often have to be highly localised, for example by adding local flavours. In contrast, cars tend to be far more standard across markets. In general, high-value/premium goods are more standardised than low-value/affordable goods. In part this is because premium customers tend to be more alike. Equally it is because the development costs for premium goods are often too great to offer much flexibility. A maker of aircraft engines is unlikely to tailor its product to different markets, whereas a maker of washing powder can easily add a lemongrass variant.

- **Brands**
  Some brands are intentionally fixed and unchanging around the world, while others are highly tailored to local conditions. French perfume and Swiss watches, for example, rely on their country of origin for their identity and cannot change their character in each market. However, tea and coffee and noodle brands can be localised to a much greater degree.

7. Towards a regional sales and marketing strategy?

Many companies still organise their sales and marketing activities in ASEAN on a country-by-country basis, but many are also moving to a pan-regional approach based around customer segments or industry sectors

So far, this report has identified a number of important trends in ASEAN, namely:

- More and more companies are setting up pan-regional management teams with an ASEAN-focused strategy
- Companies are rapidly building a pan-regional sales platform that reaches into every corner of ASEAN
- The ASEAN bloc remains deeply diverse
- But the region's 10 economies are increasingly integrating with each other
- Customers across the region are becoming more similar
- And the products and services that companies offer across ASEAN are becoming more standardised

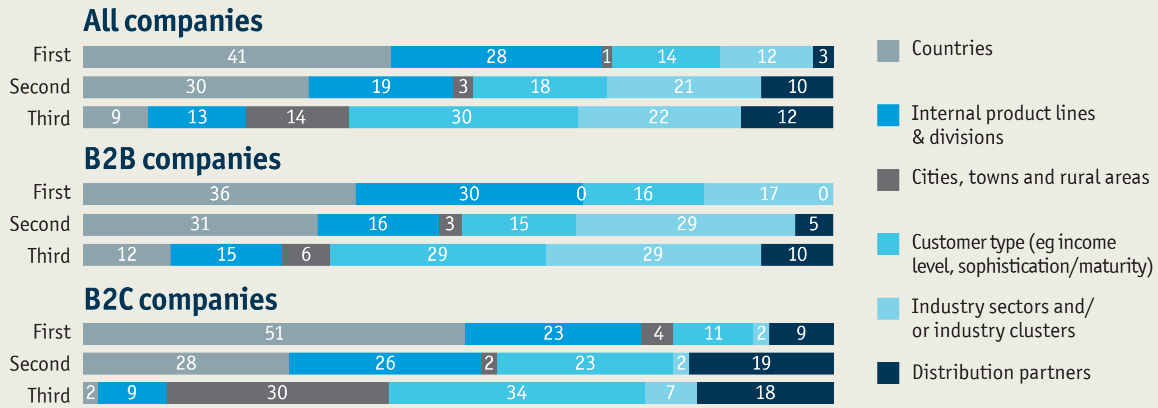
Given these trends, how are companies changing their sales and marketing in the region? How are they changing the way they position their brands and the way they go to market? Is it possible to adopt a pan-regional approach rather than a county-by-country approach?

Customers not countries?

To answer these questions, we asked companies to share the top four criteria they use for organising sales and marketing activities in ASEAN. The results suggest that, yes, companies are indeed taking a more regional approach to sales and marketing.

For example, only 41% of companies say that "countries" or national borders are the first criteria they use to organise sales and marketing in ASEAN. (See chart 13.) The figure is lower for B2B companies, where only 36% of companies use "countries" as their first organising principle. For consumer companies, the number is higher, with 51% organising their activities in the first place by national borders. This may well be because national diversity (in terms of language, religion and culture) is more significant for B2C than it is for B2B.

Chart 13
The top three criteria that companies use to organise their sales and marketing activities in ASEAN (% of respondents)



Source: Economist Corporate Network

In place of countries, many companies instead are organising their sales and marketing activities by other criteria. "Internal product lines and divisions" naturally feature strongly as one of the dimensions. "Industry sectors and clusters" is another organising criterion that is widely used, especially by B2B companies. So too is "customer type", ie the level of income or the sophistication/maturity of customers.

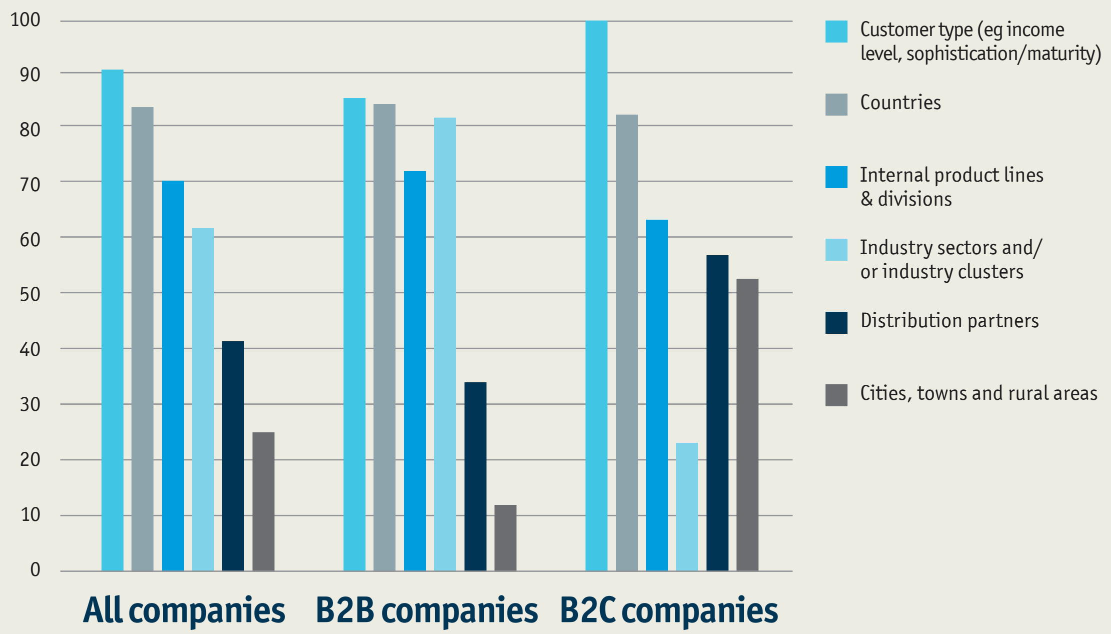
In many cases, companies operate with a matrix structure that combines both countries and customer types. Take Autodesk, a US computer-aided design software group. In ASEAN, the company organises its go-to-market strategy around four industry groups: architecture, engineering and construction; energy, natural resources and infrastructure; manufacturing; and media and entertainment. These industry groups overlay six in-country teams that manage local sales and channel partners.

Importantly, by organising around principles such as "industry sector" or "customer type", companies are able to adopt a pan-regional approach, and apply a uniform strategy to these market segments across all ASEAN countries. As such, ASEAN starts to become one market rather than 10.

By adding up the number of times that companies list different sales criteria among their top four, we get a further sense of how companies are organising themselves. For example, only 84% of companies list "countries" as being among their top four organising principles. Conversely, 91% of companies say that "customer type" is among their top four criteria. In the case of B2C companies, 100% of companies use "customer type" (See chart 14.)

One interesting way of dividing up ASEAN on a pan-regional basis is to segment it by type of settlement. The idea is that companies segment their markets by distinguishing between large cities, small towns and rural areas. In our survey, this is popular with consumer-focused companies, with 53% of companies using this classification. (See "ASEAN from an urban perspective".)

Chart 14
Share of companies (%) that name these factors as being among the top four criteria they use to organise their sales and marketing in ASEAN (% of respondents)



Source: Economist Corporate Network

ASEAN from an urban perspective

The ASEAN region crossed the threshold of having more than 50% of its citizens in urban areas in 2012. Almost half of the population still lives in rural areas that are often hard to reach, with weak transport infrastructure, and deeply informal and unorganised retail networks.

However, ASEAN is rapidly becoming more urban. Some 13% of ASEAN citizens live in the region's 28 cities that have more than 1m in population. Another 14.3% live in 367 settlements of between 100,000 and 1m people. (See chart 15.)

Many companies today are thinking of ASEAN not from a country perspective, but through the lens of cities, towns and rural areas, with common product, pricing, branding and distribution strategies for different types of settlement.

Chart 15
ASEAN population through the lens of settlement size

Many of ASEAN's rapidly growing cities are not yet familiar to those outside the region, but they will become increasingly well-known given their rapid growth and rising wealth. Consider Samarinda, an Indonesian city of 780,000 people. Between 2010 and 2025, McKinsey & Co, a management consultancy, estimates its population will grow by 2.9% every year, and its GDP by 8.9% a year. Or look at Tangerang, a city of 1.8m people in West Java. Between 2010 and 2025, McKinsey estimates the population in the city will grow by 2.1% a year, and its GDP by 8.1% every year.

8. Corporate insight: ASEAN and the FMCG sector

Attitudes in the fast-moving consumer goods (FMCG) sector about how to approach ASEAN vary widely, as these three perspectives show

Perspective 1: Taking a pan-regional approach

Since April 2014, Vaidyanath Swamy has worked for N-Vision Consulting in Singapore, helping FMCG companies to run their operations in Asia. But for 25 years before that he worked in the sector itself, first at Procter & Gamble, a US FMCG giant, where he ran various businesses in ASEAN (including leading the integration with Gillette in 2005), and most recently as head of Asia for the snacks division at Kellogg's, a US food group.

At all these companies, the approach was to treat ASEAN very much as one market rather than 10. Mr Swamy believes that ASEAN is seeing rapidly deepening homogeneity among its consumers. This growing similarity is most prominent at the premium end of the market, but is emerging at lower tiers too. He believes that companies should approach the ASEAN region by crafting pan-regional sales and marketing strategies that target these income segments in the same way, regardless of which country they live in.

"We realised that, if you look at the top cities across ASEAN, such as Kuala Lumpur, Singapore, Jakarta, Manila, Ho Chi Minh, Bangkok, there is a great degree of similarity. The shopping malls that premium consumers visit are increasingly alike, the media they consume is getting ever more aligned, and their consumption habits are very similar. Many can afford an iPhone 5S, a premium TV and a car. A Taylor Swift concert is just as popular in this segment in Singapore as it is in Bangkok. Korean popstars are universally followed," he explains.

Mr Swamy believes that ASEAN has around 25m citizens that qualify for this super-premium end of the market and the numbers are growing swiftly. He calls this segment ASEAN I. At P&G, he focused the firm's top-end products, such as Fusion razors or Pantene Premium shampoo treatments, on these consumers.

"We realised that, if you look at the top cities across ASEAN, such as Kuala Lumpur, Singapore, Jakarta, Manila, Ho Chi Minh, Bangkok, there is a great degree of similarity."

Vaidyanath Swamy, CEO, N-Vision Consulting

Beneath ASEAN I, Mr Swamy identifies a group he calls ASEAN II, which comprises citizens with lower incomes, and are found mostly in small and medium-sized cities. Today, he reckons there are around 90m people in the ASEAN II segment. Again, he sees growing similarity among these consumers across the region.

For example, he explains, "A young woman who has just moved to the city, she wants to find a job, she wants to help her parents, she wants to move up in life. The aspirations across the region are very similar. So the marketing messages can be very similar too." In selling into this segment, Mr Swamy says mid-market brands, such as P&G's Rejoice shampoo or Mach III razors are most appropriate.

The third segment, ASEAN III, contains all of the rest of ASEAN's consumers, most of whom are found in rural areas. Here he pitches the most affordable brands, and the most appropriate packaging. At P&G, that means disposable razors and shampoo sold in sachets.

Adopting a strategy such as this requires companies to set up pan-regional organisational structures. Brands, consumer marketing, and trade marketing are managed centrally. Of course, local country teams are still essential, but their role is really about sales activation and deployment. "The local marketing teams don't create new advertising copy. Instead, their role is about deciding how to maximise the ASEAN plan within their market. They're very sales-focused. For example, how do they position a brand and its messaging around local festivals?" he explains. "The role of the local country head also changes. It's mostly about driving distribution, and developing strong relationships with external stakeholders in the country, including retailers and the government."

Perspective 2: The importance of local insight

Peter Ter Kulve has been the ASEAN president of Unilever, an Anglo-Dutch consumer goods giant, since mid-2011. He believes that ASEAN has a long way to go until it can be considered as a single market.

In particular, he feels that ASEAN consumers differ from one another not only by country, but even by province within a country. "Of course, there are broad similarities across markets," he concedes. "Everyone in ASEAN loves children, they all value the importance of family. But if you look closely, the markets are very different. The way that consumers think is different, the character of local competition is different, the structure of formal and informal trade is different."

At the premium end of the market, Unilever does manage brands on a regional basis. A shampoo like TRESemmé is positioned in a very similar way across all of ASEAN. "If you're selling an idea of international beauty, like TRESemmé, then the positioning is the same," notes Mr Ter Kulve, "but if you're selling local beauty, then you need to make the local connection. The way an Indonesian thinks about beauty is different to the way a Vietnamese thinks about beauty. A brand like Sunsilk shampoo is about local beauty, and to make the connection you need deep, deep local insight."

He agrees that the ASEAN organisation is pushing deeper integration across the region. "But," he stresses, "ASEAN is a political idea, a political entity, not a consumer entity. I believe that ASEAN is not yet a meaningful consumer aggregation. It is a political aggregation, and in time an economic one too, but not yet a customer aggregation. Consumers in ASEAN don't think of themselves as ASEAN. A person in Vietnam may not even think of themselves as Vietnamese, but rather as a citizen of Hanoi or Ho Chi Minh."

For these reasons, Unilever adopts a mostly country-by-country approach to its business. "Is the ASEAN integration project important for our business? Yes, undoubtedly so. When we plan our business out over the next 10 years, we absolutely take the ASEAN project into consideration," says Mr Ter Kulve. "But to do well in these markets, you need to understand the local consumer and the local competitor better than other companies."

Perspective 3: Empowering an entrepreneurial mindset

At Kimberly-Clark, an American personal care products group, ASEAN is run as a management cluster under the oversight of Anuj Lal, the firm's managing director in South-east Asia. Within this ASEAN cluster, individual country markets run their own portfolios of brands and products that are tailored to local consumer insight. Sitting behind these local operations, the ASEAN-wide structure adds value by harnessing the firm's global R&D base and marketing expertise.

> **"ASEAN is a political aggregation, and in time an economic one too, but not yet a customer aggregation."**
>
> **Peter Ter Kulve, president, ASEAN, Unilever**

"We have a country-for-country focus. Our country general managers are empowered to operate like entrepreneurs," explains Mr Lal. "If a country leader wants to launch a new product or commercial idea, it is up to them, so long as it fits our marketing framework. At some other FMCG companies a new product launch is often more of a regional initiative. They have to see demand from lots of markets."

Kimberly-Clark does manage some of its brands on a regional basis, but they tend to be at the premium level. "Premium diapers are positioned and managed in a similar manner across most of the markets. They are targeted at a distinct cohort of mothers who are exposed to travel and education and have similar needs," says Mr Lal. "But if you look at other segments, such as the more affordable ranges, then decisions about what is appropriate for each market lie with the country management teams, based on their local consumer insight."

The reason, he adds, is that usage patterns vary widely. For example, female sanitary products are designed differently for a market like Malaysia compared to a market like Vietnam or the Philippines. The products are used differently, and so the product range and the marketing have to be different too.

Similarly, product packaging can vary. "In Vietnam, women buy diapers in 10- or 20-packs. In Indonesia they prefer to buy singles. In Vietnam a lot of baby products are sold in general [informal] trade outlets. A woman might arrive at a stall on her motorbike and buy the product without ever dismounting. So the role of packaging in these two markets is quite different," he says.

As such, Kimberly-Clark pursues a strategy that is about trying to be as "fit for purpose" in each market as possible, be it product range, pricing, packaging, marketing, or distribution strategies. "Our approach is specific to each country, and it's largely led by the local country head," says Mr Lal.

9. Barriers to a regional sales strategy

Companies say that the biggest barriers to implementing a regional sales approach across ASEAN are institutional. Cultural and economic considerations are far less of an obstacle

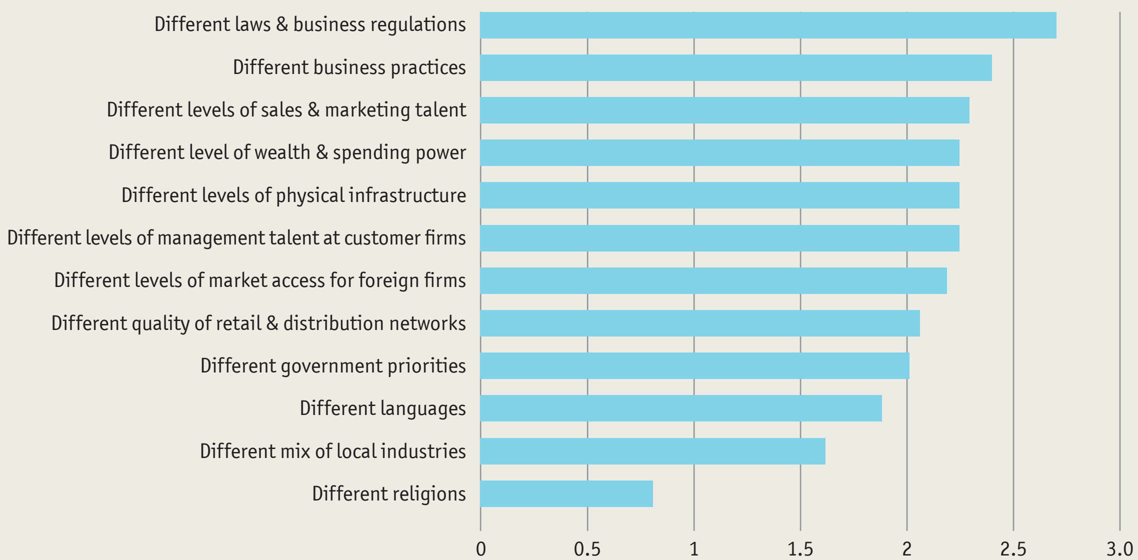
This report has already touched on many barriers that stand in the way of companies applying a uniform approach to sales and marketing across ASEAN markets. To get a sense of which barriers are greatest, we asked companies to rate the different issues on a scale from 0 (no barrier at all) to 4 (a significant barrier).

The results show that the number one issue is "different laws and business regulations". The fact that industry standards are not yet harmonised, and that companies must conduct business in different ways in different ASEAN countries is clearly the biggest challenge that companies face. (See chart 16.)

Interestingly, companies say that different customer characteristics are less of an issue. True, ASEAN's different stages of economic development are regarded as an obstacle to implementing a region-wide strategy. In our survey, companies ranked differing levels of wealth and spending power as the fourth biggest barrier. However, cultural considerations, such as different religions and different languages, are generally considered to be the smallest barriers.

For the ASEAN organisation this must be encouraging news. The results suggest that the greatest barriers preventing companies from treating ASEAN as a single market are institutional. They are

Chart 16
How important are these barriers to adopting a consistent approach to sales and marketing across different ASEAN countries? (Scale of 0 = no barrier to 4 = significant barrier)



Source: Economist Corporate Network

barriers that can be addressed. Language, religion and culture cannot be changed. But disjointed regulations and unharmonised standards are more easily fixed.

Not that anybody is suggesting the process of integration at this level will be simple. Certainly many companies express concern at the slow pace of change. Take the food sector.

"I'm on the board of the food committee in ASEAN and we're trying to harmonise things like food labels and ingredients, but it's very hard," says Mr Ter Kulve at Unilever. "There are so many people that work in food in almost every ASEAN country. Many governments are understandably nervous about opening up their food sectors to regional competition."

Nonetheless, as these results show, if governments really want to link ASEAN markets into one, and thereby reap the benefits of creating regional scale, then addressing these institutional barriers will go a long way towards achieving their goal.

10. Deepening the manufacturing footprint across ASEAN

Manufacturing companies have big plans to increase investment in ASEAN. Indonesia and Myanmar will see the most investment, but Vietnam and the Philippines will also do well

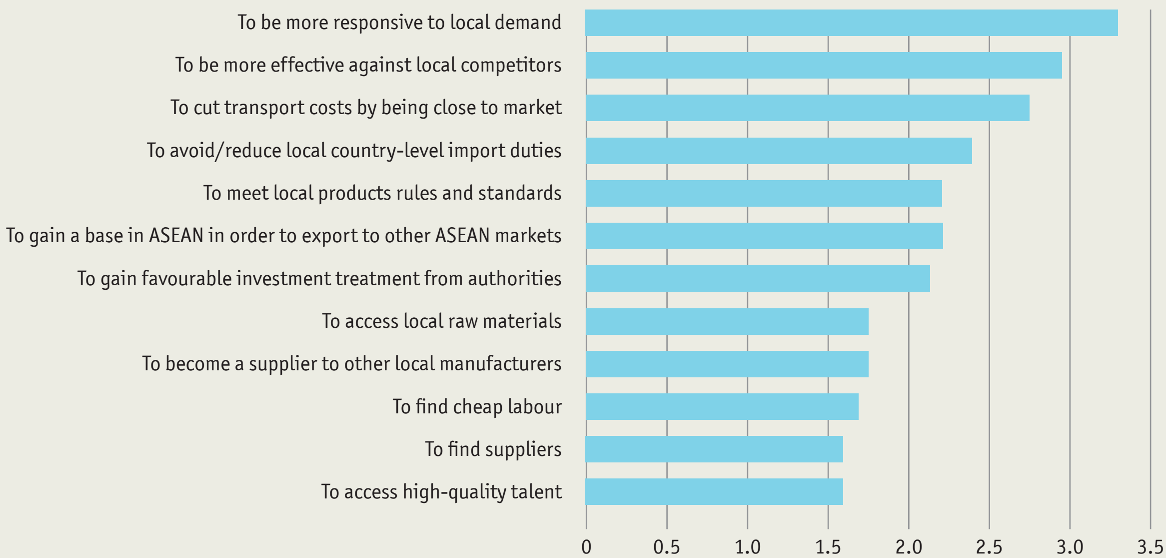
ASEAN is already a big manufacturing centre. While the region's economy makes up 3.2% of global GDP, it accounts for 4.3% of global manufacturing output. As these figures show, ASEAN's factories have historically had a heavy export-orientation, with the region's relatively cheap costs attracting significant export-focused investment.

Market seeking or efficiency seeking?

Looking ahead, however, our survey suggests that future manufacturing investment is likely to become more focused on serving local demand within the region rather than global demand elsewhere. That's not to say that ASEAN's export story will falter. Indeed, a lot of export-oriented manufacturing that used to be done in China is now moving to ASEAN, where wages are cheaper. Electronics assembly in Vietnam and textiles in Cambodia are two notable examples. However, as ASEAN gets wealthier and its economies grow, much of the region's manufacturing will focus on serving blossoming local demand.

Among our survey respondents, 75 companies conduct manufacturing in the region, and we asked them why they chose ASEAN as the location for their factories. The replies show a clear focus on serving local customers. Indeed, "being more responsive to local demand" was cited as the number one reason for putting production in ASEAN. By contrast, finding cheap labour was considered a much less important reason. (See chart 17.)

Chart 17
How important are the following criteria in your decision to manufacture within ASEAN (rather than manufacture elsewhere)? (Scale of 0 = not important to 4 = extremely important)



Source: Economist Corporate Network
Responses from 75 companies with manufacturing operations in ASEAN

Companies make manufacturing investment decisions both to seek markets as well as to seek efficiencies. In the past, ASEAN was very much a destination for efficiency seeking. Today, however, it seems that market-seeking is becoming more important.

Matt Bradley, president for ASEAN at Ford, a US automotive group, sees big potential to increase his manufacturing investment in the region. He runs three plants at present, two in Thailand and one in Vietnam. Some of the output from these plants does get exported out of ASEAN. However, the main focus is on supplying the local region.

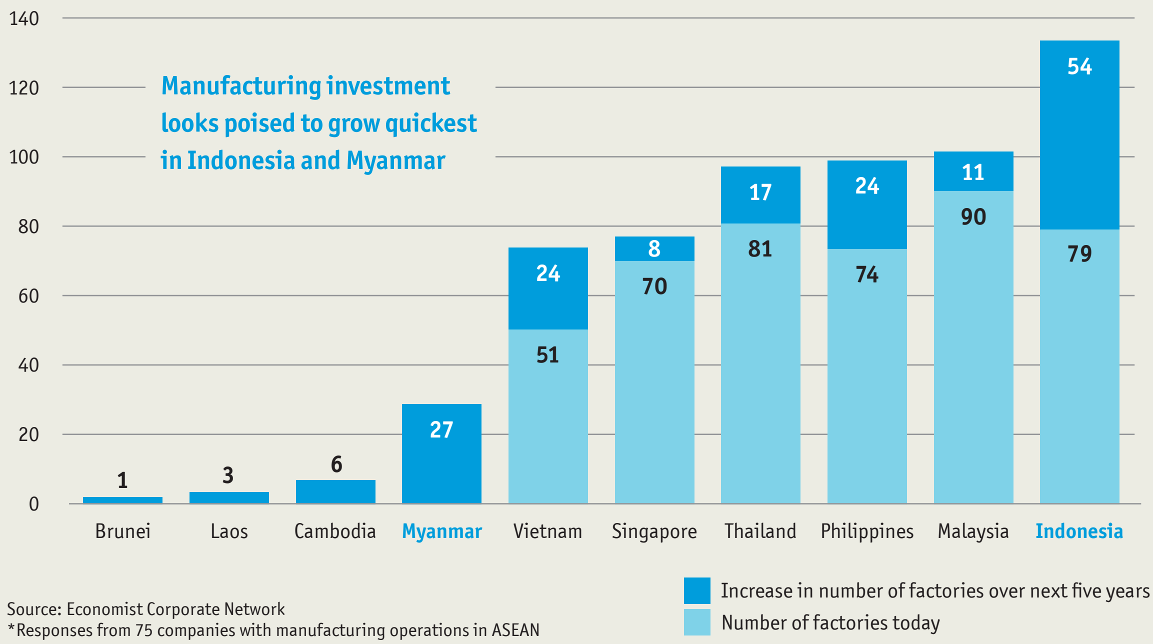
"Our manufacturing in ASEAN is set up primarily as a production hub for ASEAN itself. More than 90% of the cars we sell in the region are produced here," he says. "We do see opportunity to expand production. Given the population base in ASEAN, and the rise of the middle class, there's going to be a lot more consumers who can afford to buy our products."

Indonesia and Myanmar: future stars?

Our survey also shows clearly how patterns of manufacturing investment in ASEAN will change. We asked the 75 firms in our survey that produce goods in ASEAN to list the number of factories they operate in the region today, and to say how that will change over the next five years. Based on the responses, it's clear that every country in ASEAN will see its manufacturing footprint grow and deepen. However, some countries will see manufacturing grow more quickly.

Indonesia and Myanmar stand out as being places where manufacturing investment will grow quickest. Our 75 manufacturing firms currently have no factories in Myanmar. By 2018, they expect to have 27. In Indonesia, the number of factories will rise by 68% over the next five years, from 79 today to 133 by 2018. Vietnam and the Philippines are also poised for considerable manufacturing investment. (See chart 18.)

Chart 18
How many factories do you operate in ASEAN today, and how many factories will you operate in five years' time?*



Source: Economist Corporate Network
*Responses from 75 companies with manufacturing operations in ASEAN

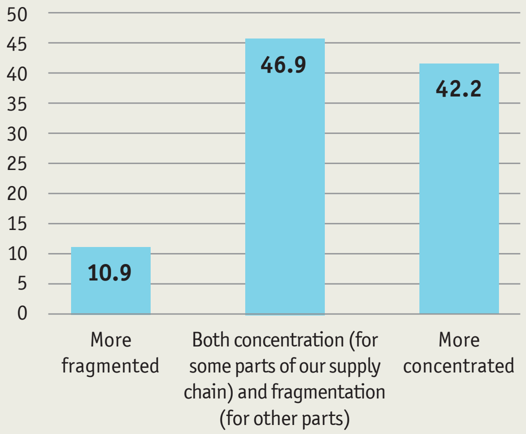
11. Re-drawing the map of manufacturing in ASEAN?

As the AEC presses forward, and barriers to regional trade come down, companies are adjusting their manufacturing strategy, seeking both economies of scale and greater specialisation

As the ASEAN region inches closer to creating an AEC, it offers interesting opportunities for manufacturing companies. On the one hand, it holds out the promise of allowing greater consolidation. Rather than produce goods in lots of places, companies can instead produce in one place and serve the whole region from that site, thereby reaping economies of scale.

Equally, however, the AEC offers possibilities for fragmentation of supply chains. Companies can take their manufacturing activities and break them down into component parts in order to put different bits in different places. For example, labour-intensive processes can be moved to cheaper labour locations. The wide diversity of both labour costs and industrial sophistication across ASEAN suggests that the region may offer attractive complementarities and opportunities for fragmentation.

Chart 19
Is your manufacturing strategy in ASEAN becoming more concentrated (eg to achieve economies of scale) or more fragmented (eg to break up your value chain and put different parts in different places)? (% of respondents)



Source: Economist Corporate Network

Consolidation or fragmentation?

Our survey reveals that companies are in fact pursuing both strategies. While 42% of companies say that consolidation is their priority in ASEAN, a further 47% say they are both consolidating and fragmenting. (See chart 19.)

Satish Shankar, managing partner in South-east Asia at Bain & Co, a strategy consultancy, sees a strong trend towards consolidation at the firms he works with. “The barriers to manufacturing on a regional basis are coming down,” he confirms.

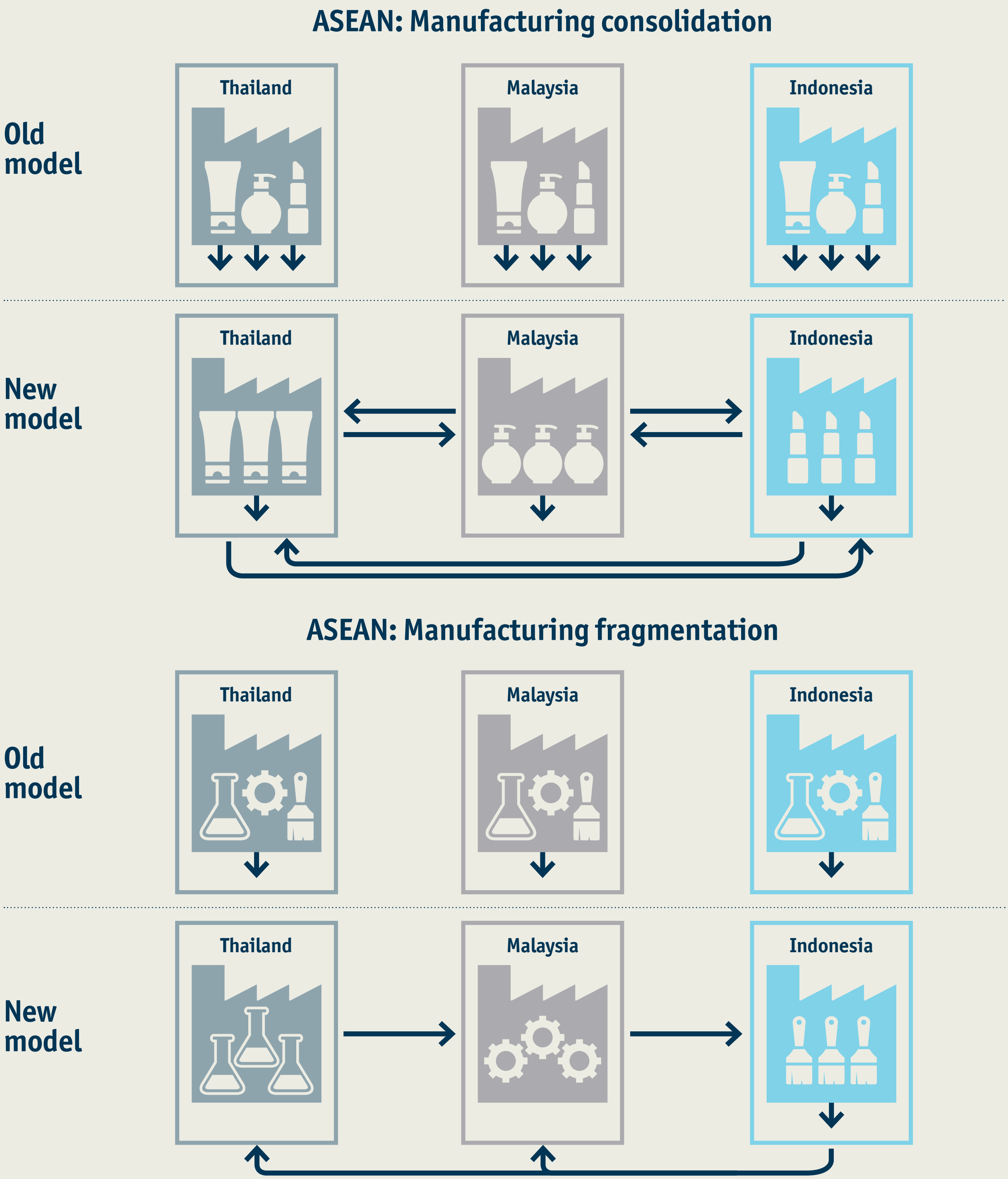
In particular, he notes, companies are re-organising existing manufacturing to achieve regional scale, as well as to reduce complexity. For example, previously a company might have had six factories in ASEAN, with each one producing a full range of products for the local market. Today, says Mr Shankar, companies are choosing to have each factory specialise in just a few goods and then supply the region. The number of factories may stay the same, but all of them become more specialised and, as such, each one achieves greater scale.

“Choosing to consolidate is a delicate trade-off between achieving scale and exposing yourself to concentration risk,” he notes. “The region does have political risk, and is exposed to natural disasters, so companies have to balance those risks.”

Naturally, not all manufacturing can be consolidated. Some products can only be produced locally. Indorama Ventures, a Thai plastic manufacturer, has a big business making bottles for drinks companies. “You have to make bottles locally because they are too bulky to transport, you can’t make them regionally,” says Dilip Agarwal, the firm’s CEO. As such, his manufacturing footprint is widening. “We’re planning to invest in Myanmar. Companies like Coca-Cola are investing a lot there right now.”

New manufacturing strategies in ASEAN

As ASEAN integrates and becomes more of a single market and production base, companies are adjusting their manufacturing strategy. Firms are both consolidating their operations, to reap economies of scale, but also fragmenting their value chains, in order to put different parts of the manufacturing process in places with the most appropriate skills, costs, resources and connectivity. In both cases, the volume of cross-border trade within ASEAN is rising sharply.



12. Corporate insight: ASEAN and the manufacturing sector

The coming together of ASEAN as a more integrated region offers scope for new manufacturing strategies, as these two perspectives show

Perspective 1: Pan-ASEAN consolidation

Siegwerk is a German ink manufacturer that serves the packaging and printing industries. Across ASEAN, the company has seven factories in five countries. In five years' time, it will have nine factories in six countries. But, as well as growing in the region, Siegwerk is also changing its manufacturing strategy. Consolidation is a big part of the plan.

The ink business has two main stages. The first is to produce the basic building blocks that go into an ink, such as resins, solvents and colour ingredients. Siegwerk produces around 300 such components. The second stage is to mix these building blocks to create specific types and colours of ink.

Today, Siegwerk's factories across ASEAN each carry out both stages, from producing basic ingredients to blending them into final inks. But this is soon to change. Siegwerk is about to open a new factory in Indonesia that will do the bulk of the manufacturing for the first stage. These core ingredients will then be shipped across the region to local blending plants in the countries where the inks are needed.

"The idea is to make our production more efficient," explains Mike Van Breugel, CEO of South-east Asia at Siegwerk. "Goods flow across borders in ASEAN relatively freely now. There's still a bit of local protectionism in some places, and cross-border regulations could certainly be a bit easier, but it's manageable. So putting our upstream manufacturing in one place makes sense."

As for the downstream part, Mr Breugel says it's possible to consolidate there too, but that his clients like to have the blending plants close by. And having a network of downstream factories also provides a measure of risk management, because they can also be called on to manufacture some of the upstream ingredients too, should a supply chain disruption occur.

Perspective 2: Pan-ASEAN fragmentation

Indorama Ventures, headquartered in Bangkok, is the world's largest producer of polyester, an ingredient that is used to produce plastic. With US$7.5bn in revenues, it has operations all over the world.

But producing polyester is a commodity business. As such, being the biggest company in the sector offers only limited protection from price competition. And so Indorama is moving downstream into higher value-added products such as making plastic bottles for the drinks business and plastic fibres that are used in clothing and healthcare products. "High value-added products are a new area for us, but will help us to maintain healthy margins," explains Dilip Agarwal, the firm's CEO.

In ASEAN, Indorama has traditionally manufactured its polyester in its home country of Thailand. But, as Mr Agarwal explains, "Thailand today has a high cost structure." For that reason, the firm is moving the

> **"Goods flow across borders in ASEAN relatively freely now... so putting our upstream manufacturing in one place makes sense."**
>
> **Mike Van Breugel, CEO, South-east Asia, Siegwerk**

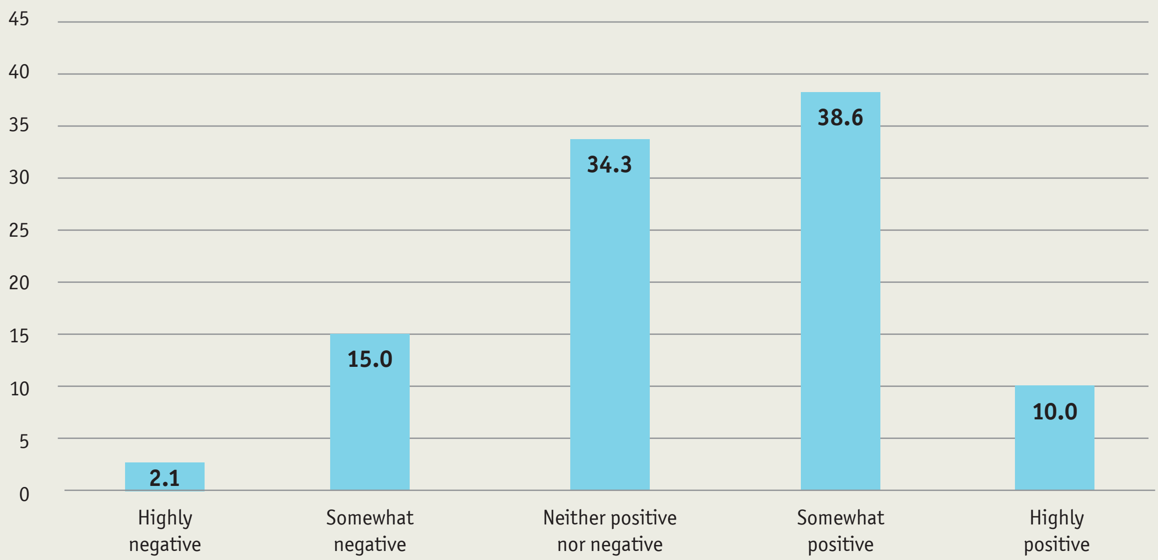
commodity side of its business to Indonesia where it opened a giant facility this year at a cost of US$200m. "Labour is cheaper in Indonesia, and energy is cheap. Indonesia has abundant coal, and we've built our own captive coal-fired power station to serve the plant."

Meanwhile, the company is re-purposing its production facilities in Thailand to focus on the downstream, higher-margin products, with a special focus on hygiene fibres. The plant in Indonesia will supply the basic polyester that the Thai factories need. It will also supply Indorama's expanding network of plastic bottle factories in Thailand, the Philippines, and other parts of ASEAN.

The strategy is a clear example of a company breaking up its value chain in order to put different parts in places where local cost structures and skills are most appropriate. Indonesia is cheap and more appropriate for low-value work. Thailand is expensive and more appropriate for high-value work.

Many observers argue that ASEAN has large potential for doing this sort of fragmentation. Indeed, in our survey, companies said that they believe the diversity across ASEAN to be generally a positive thing because of the complementarity it creates. (See chart 20.)

Chart 20
Is ASEAN's diversity positive for your company (eg offering differing skills and costs that are complementary) or negative (eg leading to varied markets and inconsistent rules)? (% of respondents)



Source: Economist Corporate Network

13. Re-drawing the ASEAN map for services?

Many businesses in the services sector find it difficult to operate in ASEAN on a pan-regional basis. Nonetheless, the potential for achieving regional scale may get greater as the AEC is launched

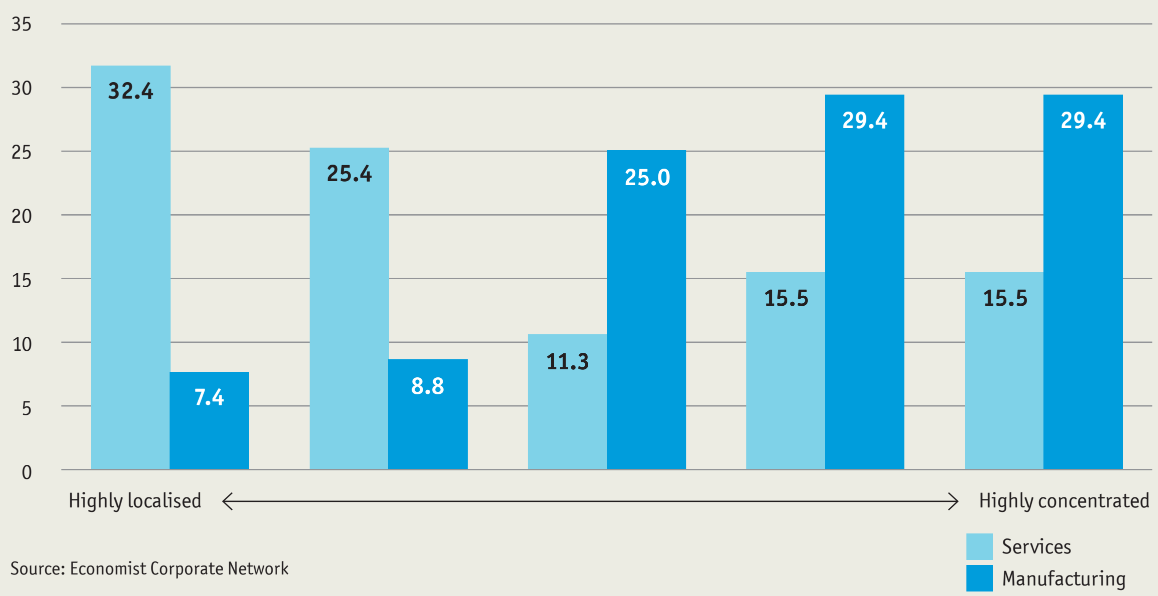
As the AEC continues its progress, and the region becomes more integrated, opportunities will unfold for service industries to build a scale business across ASEAN. In air transport, for example, efforts are ongoing at creating an Open Skies Agreement in time for the launch of AEC in 2015. In banking, the ASEAN Banking Integration Framework is similarly a work in progress.

The potential is there. However, in our survey, services firms say that their ability to take a regional approach to their business is much harder than in the manufacturing sector. (See chart 21.) Undoubtedly much of this is due to the nature of a service business, whereby human contact is an important part of the delivery. Doctors and restaurants and financial advisors have to be physically present to deliver their service, whereas a car manufacturer can serve many countries from just one factory.

Local vs regional approaches

In some cases, the highly local nature of a services company is down to market maturity. Consider the case of real estate. At Jones Lang LaSalle (JLL), an American real estate services firm, the company has two broad parts to its business. One is managing property on behalf of large clients. Here, the business is indeed becoming

Chart 21
How localised or concentrated is your production of goods or delivery of services? (% of respondents)



Source: Economist Corporate Network

more regional as clients themselves take a regional approach to managing ASEAN. For example, an oil group might ask JLL to find and manage a network of offices on its behalf across the region.

However, the other side of the business is helping property developers to sell real estate, and investors to buy it. Here the business remains extremely local. "We're starting to see a bit of cross-border activity. Some of the investors in Singapore, for example, might look at Jakarta, but it's at a very early stage. Most of the real estate investment side of things is still very local," notes Chris Fossick, managing director in South-east Asia for JLL. "It's not at all a market like Europe, where real estate investment is a much more cross-border business."

Regulatory tangles

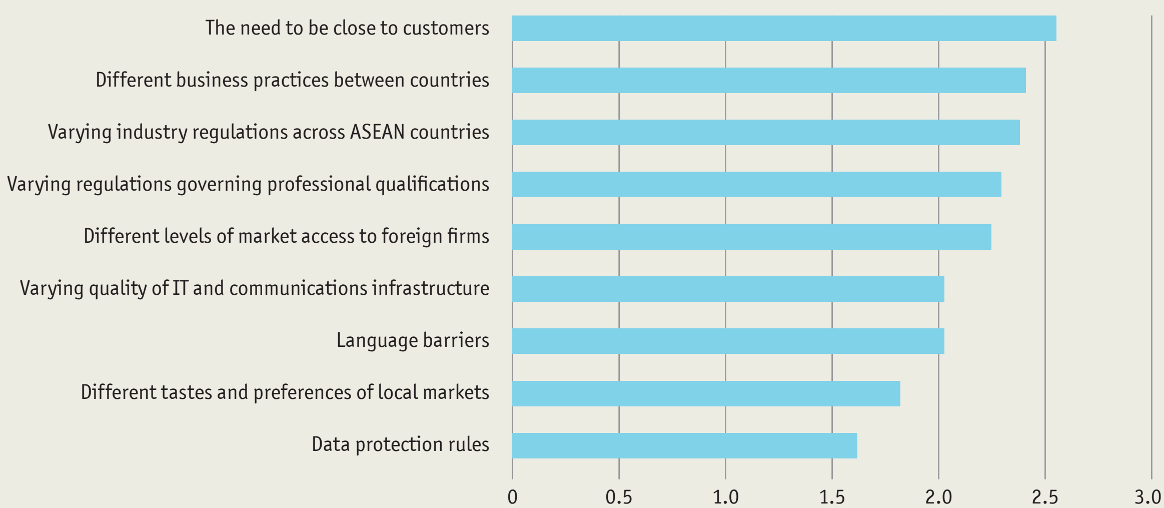
Another impediment to running a regional business is a lack of joined-up regulations. In banking for example, the credit card business is best run at scale. The more customers that a bank has, the more efficient the business becomes, not only by having centralised back office processing, but also through better data analytics around a bigger pool of customers, which in turn improves risk management. Yet, in ASEAN, banks are largely prevented from running their credit card businesses across borders. Customer data is required to be kept in-country rather than processed in neighbouring places.

When asked about the greatest impediments to going regional, respondents to our survey listed "the need to be close to customers" as the greatest barrier. (See chart 22.) But companies also ranked issues such as unharmonised industry regulations and inconsistent rules around professional services qualifications as being equally troublesome. (See Chapter 14 on page 38.)

For the ASEAN Secretariat, many of these issues are ones that can be addressed. The issues that cannot be changed, such as different languages, and different market tastes and preferences were not considered to be big barriers to taking a regional approach.

If ASEAN countries can tackle these different rules then the opportunities for the services sector to achieve scale will rise. But other factors could be equally important. Technology has huge potential to help services firms implement a more regional approach. (See "Tech to the rescue for services consolidation?")

Chart 22
How important are these barriers to adopting a regional approach to providing services across ASEAN?
(Scale of 0 = no barrier to 4 = significant barrier)



Source: Economist Corporate Network

Tech to the rescue for services consolidation?

One important trend in ASEAN is the deepening penetration of technology. Many countries, such as Indonesia, Vietnam, Singapore and Malaysia now have mobile phone penetration rates well in excess of 100% of the population. Internet access is deepening rapidly, much of it via mobile devices. The Economist Intelligence Unit expects the number of internet users in ASEAN to grow from 186m in 2013 to 353m in 2018. And social media is rising at staggering speed: across ASEAN, 36% of all adults have a Facebook account—in many countries, Facebook penetration is significantly higher than the penetration of bank accounts.

"The demographic profile in ASEAN is very young, and younger populations tend to be more open to new technologies," says Scott Cassin, chief technologist and strategist in Asia Pacific at Hewlett-Packard, a US IT services giant. As such, he says, the ASEAN region has huge potential, not only to leapfrog old technologies, but to harness new ones for exciting new business models.

For service industries, technology adoption across the region may help to achieve greater consolidation, more efficiency and greater regional reach. Consider retailing. With the rise of online commerce, retailers no longer need to build a physical network of stores, but instead can serve the region from a set of virtual storefronts, supported by centralised warehouse operations. In education, companies no longer need to have physical schools or training centres, but can serve ASEAN via virtual classrooms. Again, these can be run from one country, yet serve the entire region.

Healthcare offers another example. By using videos and telepresence, doctors can treat patients virtually or online. The emergence—and now ubiquitous use—of personal, wearable devices as well as smartphone apps that can monitor heart rate and provide a great wealth of personal health information allows for all sorts of illnesses to be diagnosed on the internet. "Many smartphones today can help detect problems and diseases faster and more cheaply, by using high-definition built-in cameras and the connectivity of the device to send feedback to professionals for diagnosis," notes Mr Cassin.

What's more, he adds, technology will play a significant role in accelerating the implementation and integration of regulatory, commercial, and operating models across ASEAN. Defining and implementing data and business process integration standards, such as XBRL (eXtensible Business Reporting Language) will be essential in enabling consistent and efficient cross-border trade and commerce.

14. Re-drawing the ASEAN map for professionals?

Businesses want to have a more regional approach to recruiting and managing their workforce, but progress is slow

One of the stated aims of the AEC blueprint is to have a "freer" flow of skilled labour across borders in South-east Asia. The region can hardly call itself a single market unless citizens of one ASEAN country are able to work in another.

This is important for the services industry. The ability to move people across borders and to recruit talent from across the region is all part of having a regional approach.

However, given the wide diversity of education, training, skills and wages across ASEAN, it is unrealistic to expect countries to fling open their borders to free labour migration. Nonetheless, things look set to improve, albeit slowly. In future, companies can expect to see greater mobility for certain professions.

To achieve this, the ASEAN organisation is working on a set of mutual recognition agreements (MRAs) for professional qualifications. The frameworks for negotiating MRAs have been agreed for seven priority professions: engineering, architecture, nursing, accountancy, surveying services, medical practitioners, and the dental profession. MRAs are also in the works for other sectors, such as tourism. The idea is for professional qualifications such as licenses and certificates that are granted in one ASEAN country to be recognised as acceptable in all the others.

The status of these MRAs is mixed. For example, progress is much more advanced for architecture and engineering than for the other five priority sectors. What's more, while the MRAs help to provide a more level playing field across the region for skilled labour, many local regulations still stand in the way. For example, nurses in Thailand are required to speak Thai in order to work there. In Malaysia, foreign engineers can only practice in the country if they have a minimum of 10 years of experience, are sponsored by a local Malaysian company, and it can be proven that no local engineers can perform the role.

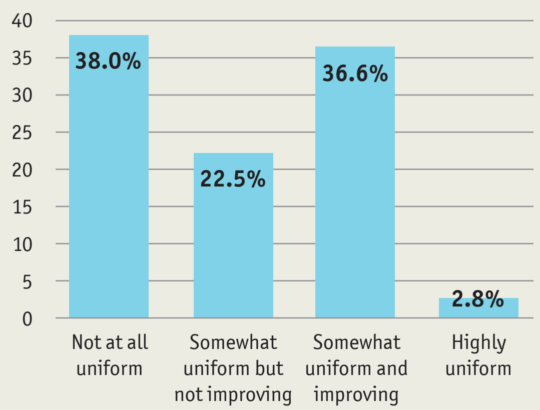
Labour still needs work

Respondents to our survey say that a lack of harmonisation for professional qualifications is still a major impediment to their business. Only 2.8% say that the rules governing qualifications in their industry across ASEAN are highly uniform, while 38% describe them as not at all uniform. More hearteningly, just over a third of companies state that the situation is improving. (See chart 23.)

"One of the biggest impacts of the AEC for us will be greater mobility of people," notes Mr Agarwal at Indorama Ventures. "We have excellent technical managers in Thailand, but struggle to find similar talent in Indonesia. It would be highly beneficial if it gets easier to move people around the region."

However, he adds, improving labour mobility won't necessarily solve all his challenges. "There are cultural issues too. A Thai engineer might not want to go and work in Indonesia."

Chart 23
How uniform across ASEAN are standards and regulations governing professional qualifications for staff in your industry? (% of respondents)



Source: Economist Corporate Network

15. Conclusion

The map of ASEAN is indeed being re-drawn, with the region becoming more of a single economy instead of 10. Companies need to sketch a new mental map of what that means, not only for their business in ASEAN, but for their strategy in Asia as a whole

What emerges from our survey and from the interviews we conducted is a strong sense that ASEAN as a region is taking on a much more distinct identity. The region is by no means a natural agglomeration. Myanmar and Indonesia have little in common. Thailand and the Philippines are deeply different.

And yet, despite ASEAN's diversity and differences, the region is indeed becoming a recognised bloc. A majority of international companies recognise the region as a distinct entity that needs its own management team and its own strategy.

And the strategies that are being deployed are highly regional in character. Be it the consolidation happening in manufacturing, the harmonisation of product and service offerings, the belief that customers are becoming more homogenous, the adoption of regional sales plans focused on customer types or industry sectors rather than countries—time and again, companies are applying a more regional approach to their business.

Naturally there is a long way to go before ASEAN can be considered a true economic union. For example, the region is arguably decades behind where the European Union stands today. But the fact that ASEAN is committed to rolling out the AEC by the end of 2015 is a clear statement of intent of where the region is going.

Some commentators worry that, as the AEC draws closer, nationalist and protectionist sentiment will grow stronger and undermine the integration process. But the companies in our survey do not share that sentiment. Only 3.5% of firms think the AEC will fail. The majority are positive it will succeed.

So, in conclusion, it does indeed seem that the map of ASEAN is being re-drawn. At a policy, top-down level, the ASEAN Secretariat continues to push towards achieving its goals of creating a single market and a single production base across the region. And at a bottom-up level, companies themselves are increasingly treating ASEAN as one economy, and not as 10 separate economies.

National borders will, of course, stay in place. And national identities will remain important considerations. But if companies are to recognise the true potential of ASEAN, then they will need to sketch out a new mental map of Asia—one that recognises not only the size and scale of China and India, but also the size and scale of ASEAN alongside them.

16. Appendix

Data on the 171 companies that took part in our survey

A total of 171 companies took part in the survey. They came from a broad mix of industries, with no sector accounting for more than 12% of respondents. Respondents generally worked at large companies: 41% came from firms with revenue of more than US$10bn, and 37% from firms with revenue of between US$1bn and US$10bn. Respondents mostly came from non-ASEAN companies (86% of the total). Around 60% of the companies were primarily B2B, and 40% primarily B2C. Nearly half the companies (47%) did manufacturing in ASEAN.

In which sector do you operate?

	(% of respondents)
Financial services	11.7
IT & software	11.1
Professional services	9.3
Chemicals	8.6
Transport	6.8
FMCG	6.2
Healthcare & pharma	6.2
Manufacturing	6.2
Agriculture & food processing	4.9
Automotive	4.9
Media & marketing	4.3
Real estate & construction	3.7
Engineering	3.1
Hotels & leisure	3.1
Oil & gas	3.1
Electronics	2.5
Energy & power generation	1.9
Mining & metals	1.9
Retail	0.6

What is your global revenue?

	(% of respondents)
US$10bn or more	41.0
US$1bn to US$10bn	36.6
US$100m to US$1bn	16.8
Less than US$100m	5.6

Where is your company's global HQ?

	(% of respondents)
Non-ASEAN	85.8
ASEAN	14.2

What is your primary customer group?

	(% of respondents)
B2B companies	61.8
B2C companies	38.2

Does your company do manufacturing in ASEAN?

	(% of respondents)
No	53.1
Yes	46.8

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