Grant Thornton
An instinct for growth™

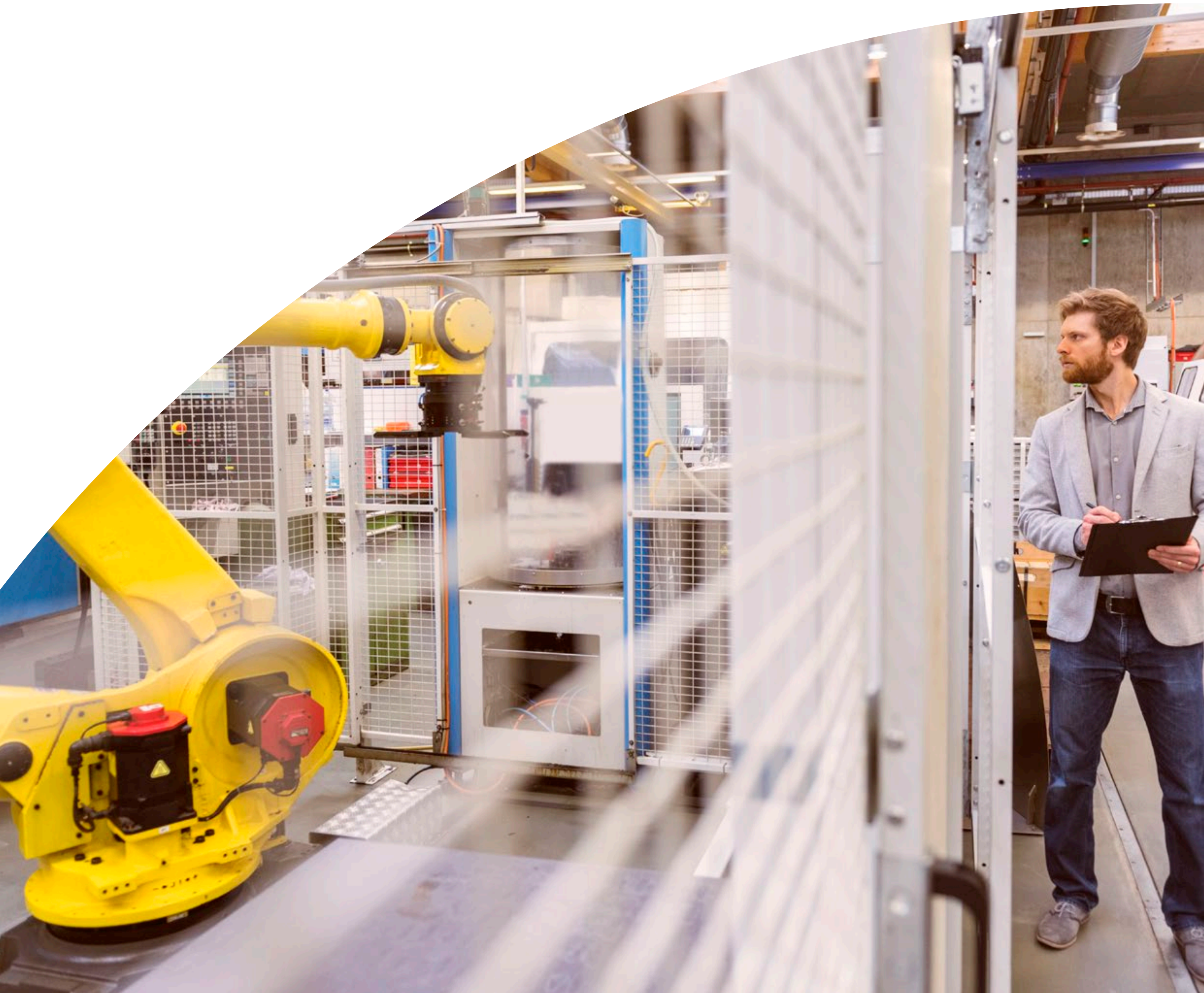
Global

Economy

Growth

Thriving in 2020: Capitalising on resilience

February 2020



Making sense of complexity

Our latest International Business Report (IBR) reveals a complex, volatile picture across the mid-market business landscape.

In 2019 we saw how businesses prepared themselves for uncertainty and potential shocks such as higher tariffs, escalating trade tensions, and an unpredictable Brexit. This year may prove even more challenging.

The coronavirus has already caused major disruptions to global supply chains and markets around the world as the knock-on effect of the virus and resulting quarantine measures seep into the world economy. And later this year, there will also be the uncertainty of the US presidential elections.

Business leaders in the mid-market tell us that they are concerned about the state of the global economy, with IBR data showing another rise in economic uncertainty over the past half-year and heightened concerns about falling demand

However, for all these concerns, there are underlying drivers supporting growth. Before the emergence of the coronavirus export expectations for the next 12 months leapt to the highest level since 2011, in the second half of 2019. Most strikingly, over half of businesses reported revenue growth above 5% in the past 12 months. These figures reveal the hardy nature of the mid-market and its ability to grow against the odds.

Looking to 2020, our IBR data and industry experts have identified three ways in which mid-market businesses can bolster themselves against the prevailing headwinds and be ready to take advantage of opportunities as they arise.

First, business leaders should take a more international outlook across their operations to diversify customer bases, reduce risks in supply chains and find savings from outsourcing in different territories.

Second, we see business leaders keen to invest in their future, but accessing finance is challenging. There is a need to think creatively about how projects are funded, looking at collaboration with other companies while presenting comprehensive plans to attract funding.

Third, with unemployment at record lows and skills in short supply, it is essential for businesses to review their employee skills strategy, boost staff efficiency with technology and ensure that they create a compelling employer brand.

Volatility does not need to be an obstacle to growth; in fact, it has proved an opportunity for many businesses that are agile and forward-thinking. Mid-market businesses will benefit from planning for the inevitable changes.

Francesca Lagerberg
Global leader – network capabilities
Grant Thornton International Ltd

Fragile optimism

Businesses around the world faced numerous economic headwinds in 2019, but optimism among business leaders held up in H2 at 59% – a 3 percentage point (pp) increase on H1 2019 – although still below the 2017–2018 average. Expectations for revenues and profitability have also improved, albeit modestly, up 1pp and 3pp respectively.

Indeed, as 2019 drew to a close, other mainstream forecasters expected the worst of the clouds to have lifted in 2020 with the IMF predicting global growth of 3.3% and 'tentative stability'. One reason that businesses were somewhat more positive could be the announcement of a phase one trade deal between China and the US, alleviating the worst fears of a full-blown trade war.

The last year demonstrates that growth is achievable even in challenging circumstances and that mid-market businesses are doing well and remain well placed to succeed. The latest data indicates that business leaders have factored in uncertainty into their operations. They want, and expect, to increase investment to safeguard and build on their advantages in a fast-changing world.

59%
Business leaders are more positive about the economy, with optimism up 3pp

1/4
One quarter of business leaders are very optimistic about the economic outlook

36%
Business leaders expecting exports to increase over the next 12 months have jumped to an IBR series high of 36%

Investment intentions

33%	42%	55%	52%	47%
New buildings	**Plant and machinery**	**Technology**	**Staff**	**R&D**
up 3pp	up 3pp	up 3pp	up 4 pp	up 2 pp

Global investment intensions have risen across all categories for the past three surveys.

49%
Economic uncertainty
The proportion of business leaders citing economic uncertainty as a constraint on growth rose from 46% in H1 2019 to 49%, just 1pp down from the series high recorded in H2 2018.

All source data Grant Thornton IBR, H2 2019.

Growth amid persisting uncertainty

Sentiment among business leaders brightened at the end of 2019, but global and regional concerns still weigh on their outlook.

Economic uncertainty remains stubbornly high. It climbed again in the last six months of 2019, despite small improvements in the first half of 2019. Much of this was driven by speculation over the health of the bellwether US economy, with specific concerns about losses in the US manufacturing sector earlier in the year. Meanwhile, the presidential impeachment inquiry also clouded leaders' outlook as they speculated over its impact on policy.

Indeed, in North America, 48% of business leaders expect economic uncertainty to constrain business activity, which was up 11pp from the first half of 2019, the highest level since IBR records began. However, notwithstanding the impact of the coronavirus, some of the more immediate US-centric concerns have now lifted.

Multiple trade relations are frayed

The trade tensions between the US and China have not vanished despite recent thawing. Meanwhile, other trade spats such as those between Japan and Korea, the US and EU also loom on the minds of business as they speculate on what impact potential tariffs might have on their export margins and supply chains.

Business optimism across Europe defied the global average, and slipped 5pp to 45% – the lowest level since 2013 – while economic uncertainty rose to 45% in the region. Some of this can be attributed to ongoing concerns about the future trading relationship between the EU and the UK.

Optimism among businesses in developed Asia Pacific also fell, with declines now 8pp down from the second half of 2018. Export intentions also remained subdued, as economic uncertainty from trade wars took their toll.

Some of the worst impacts of that uncertainty are localised around individual cities, says Rodger Flynn, regional head of Asia Pacific at Grant Thornton International Ltd. "Two of the cities hit hardest are Shanghai and Hong Kong. The latter is the only Asian market in recession, with social unrest compounding weak business optimism there." However, China more broadly saw economic optimism improve by 11pp in the second half of 2019. This could be sharply undermined by the coronavirus outbreak in past months, exacerbating the impact of tight lending conditions following China's deleveraging campaign. Businesses elsewhere will look closely at how China performs over coming months and how that will impact the global economy.

Concerns over reduced demand for goods and services also inched higher globally, with 41% of businesses expecting a shortage of orders to constrain growth in the next 12 months. Meanwhile, in the US, a potential shortage of orders has risen again to 35%, having tripled from 10% to 30% in H2 2018. In Europe, worries over demand rose 6 pp to 38%, while in Asia Pacific those concerns retreated by 4pp but, at 46%, remains higher than the global average.

Global lessons from South America

Latin America's economy, which has been traditionally difficult to characterise, with huge volatility and variation between strong, successful countries such as Brazil on the one hand and very challenged economies like Venezuela's on the other, saw optimism improve by 14pp after falling in the first half of 2019.

However, Latin America's historical and persistent volatility reflects the new reality for mid-market businesses across the global economy. Roy Buddle, regional head of Americas at Grant Thornton International Ltd says Argentina – which has been dealing with ongoing uncertainty for the past 20 years – represents an example from which lessons can be learned. "Effectively, businesses have developed resilience and an ability to plan for the worst, to work through what can be very unpredictable conditions, and sometimes these happen very quickly," he says.

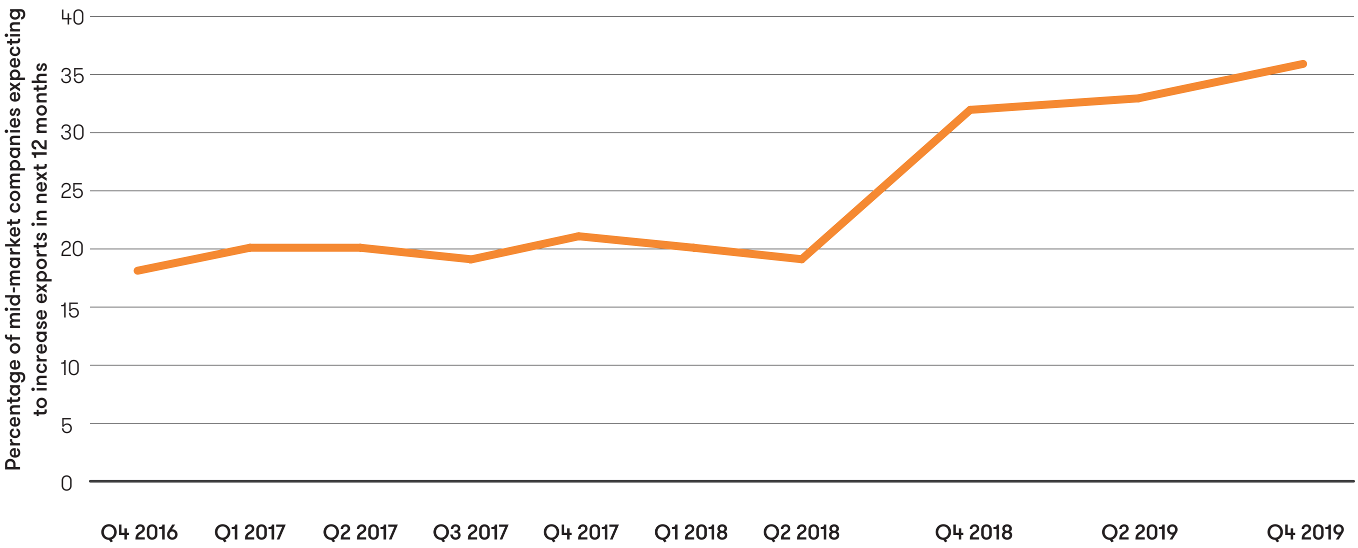
"It is about having contingency plans, about managing crisis on an almost ongoing basis. With devaluation of greater than 100% since 2018 and almost 60% inflation last year, how do you price your goods and services? How do you manage the challenge of facing higher wage bills and the costs of running a business? But in fact, they have managed. Argentina is a great example because last year it grew 62% in dollar terms."

While this scenario may be an extreme one, it does show that businesses can prosper through sustained volatility. Leaders of successful businesses know they can't stand still and wait for stability to return while their competitors are putting in contingencies and taking managed risks.

Look internationally for new markets and cost optimisation

Build resilience

Global exports expectations for over the past five years



All source data Grant Thornton IBR, H2 2019.

Often when optimism declines, mid-market businesses find smart ways to succeed. Last year's report, Thriving in 2019's global economy, encouraged business leaders to focus on building skills, low-cost digital technology and internationalisation to build resilience against uncertainty and a softening global economy. That appears to have paid off.

Larissa Keijzer, region head Europe, at Grant Thornton International Ltd says: "If you look at exports, they are growing again because that is what the mid-market does when optimism falls: these companies start looking for international trade flows and new ways of doing business." While domestic growth has been challenging at times, businesses have worked to grow and expand their export markets. Prior to the coronavirus outbreak, trade expectations for the next 12 months were trending higher with notable gains in Spain (12pp) as it continues its economic recovery from the 2009 financial crisis, and in Ireland (9pp) which is benefitting from some service businesses in the UK relocating due to Brexit.

Meanwhile, the falling cost of digital technologies, ecommerce, increasing access to software as a service and cloud products continue to provide new revenue streams and extend international reach for the mid-market. Indeed, technology investment expectations are accelerating, led by North America up 6pp from H1 2019.

The mid-market should continue to seek out new trade routes and international markets to diversify and protect their customer base. In broadening their international outlook, businesses should also build more contingency into their international supply chains to minimise risks, while reducing costs through outsourcing operations in different territories.

Adapt products and services to new markets

Businesses are investing in R&D to develop new products and adapt old products to reach new markets. In H2 2019, global R&D investment expectations continued their rise to 47% from lows of 23% in H1 2018, with Asia Pacific countries leading the way (see article: Driving growth through R&D investment).

One example is Australian winemaker Cassegrain[1], which is looking to increase its exports from 30% to 70% over the next five years. It invested in R&D to adapt its product to reach the growing Chinese market. The vintners changed everything from the size and shape of bottles, labelling and packaging to a product that would appeal to Chinese buyers.

1. https://www.exportfinance.gov.au/wine/cassegrain-wines/

Reduce risks and costs through outsourced shared services and new supply chains

The increasingly international outlook of business leaders goes beyond direct exports. In Asia Pacific, where the US-China trade dispute has had the most impact, many businesses have altered their operations and supply chains with some production shifting from China to benefit manufacturers in Indonesia and Vietnam.

Rodger Flynn says: "Some businesses have invested heavily in shared services to build various efficiencies in their businesses. Some of them have been investing in technology, such as AI. Once again, there has been some focus on offshoring certain operations to maintain margins."

Similarly, businesses in Western Europe have looked eastwards to optimise costs, Keijzer says. "I see a lot of companies growing their factories in Poland and the Czech Republic, looking for labour and shared services in those countries when they would normally perhaps look to Asia but [haven't]. They are spreading the risks and looking for alternatives, due to political and other developments involving China."

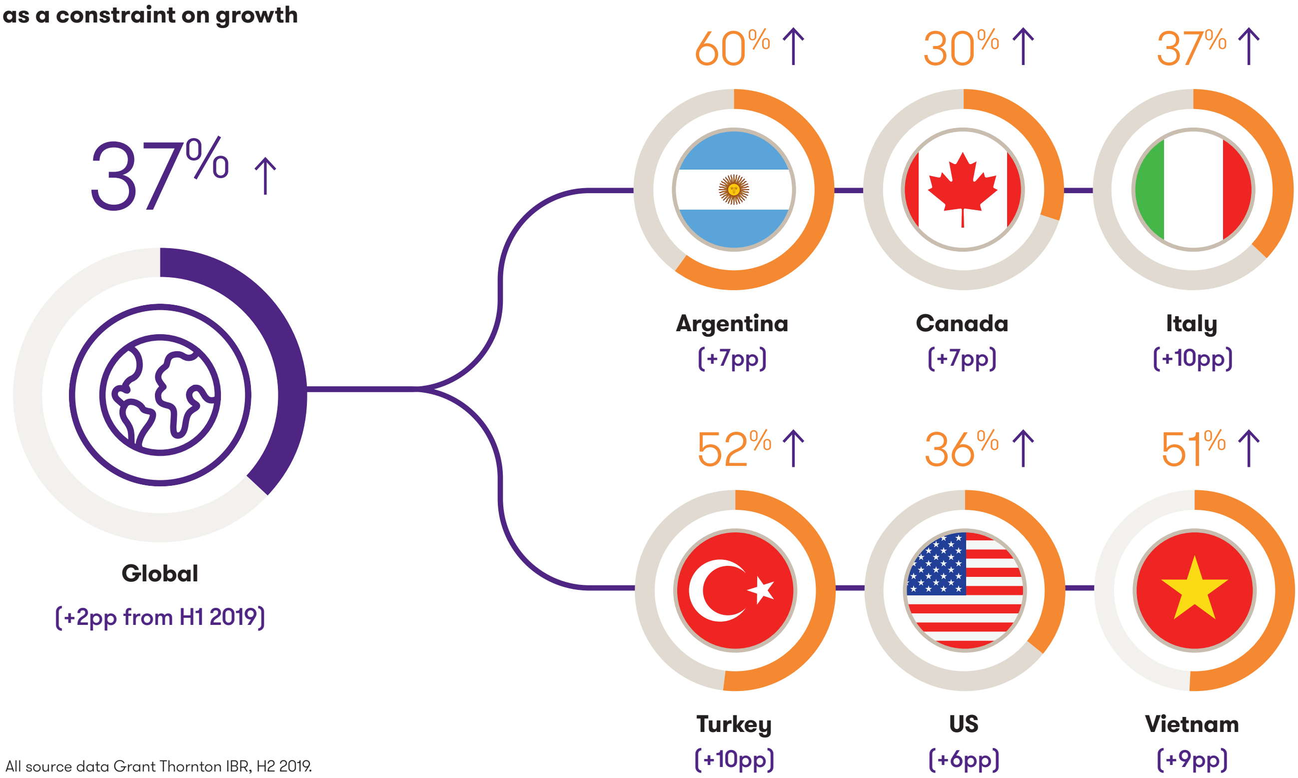
"Some businesses have invested heavily in shared services to build various efficiencies in their businesses. Some of them have been investing in technology, such as AI. Once again, there has been some focus on offshoring certain operations to maintain margins."

Rodger Flynn, Regional head of Asia Pacific, Grant Thornton International Ltd

Focus on the future economic environment and the needs of your business

Access to finance

Business leaders citing shortage of finance as a constraint on growth



All source data Grant Thornton IBR, H2 2019.

Businesses have a healthy appetite for investment right now, but 37% of business leaders cite a shortage of finance as a constraint – a near series high. Businesses in developing markets such as eastern Europe, emerging Asia Pacific and Latin America were most concerned by access to finance.

For example, in Latin America, the majority of commodity-driven economies have not solved their government budget issues. After a decade of high government spending readily available from low-interest rate levels and boosted with record-high commodity prices, budget deficits keep pushing debt levels higher.

Meanwhile, concerns over the shortage of finance increased by 7pp and 6pp in Canada and the US respectively.

Although interest rates are low, debt piles have mounted and as investment activity and transaction prices increase, investments become riskier, and financing becomes increasingly complicated. Some sectors struggle more than others, with TMT and construction and real estate particularly challenged.

Francesca Lagerberg, global leader of network capabilities at Grant Thornton International Ltd, says: “How to get the funding to invest is always an issue for growing businesses. You can often get funding for a narrow range of investments but not always for the more exploratory things that businesses want to do. Sometimes investments don’t fit into a neat model suited to more traditional ways of finance.”

Develop compelling and future-fit investment plans

When the economy is speeding up, accessing finance tends not to be an issue, but when shocks occur, whether it is in politics or something else, then making a good business case to attract investment becomes more critical.

Businesses seeking finance need to look ahead and convince lenders and finance partners that their investment has a viable future. Ignacio Munyo, a business consultant at Grant Thornton Uruguay, says: "Sustainable finance has become one of the key topics as the global uncertainty debate grows. To successfully access finance, Latin American companies need to develop strong data-driven business models consistent with a changing landscape. They need to assess if their business model will have value in 10 years' time, this will include a range of factors such as the level of demand they expect and what they need from their future workforce."

Look to investment collaboration and smart financing alternatives

Business leaders could benefit from looking at alternatives to traditional lenders. Private equity, which currently has plenty of liquidity, is one option. Although not right for all businesses, some are increasingly seeing the catalytic potential for growth. Rodger Flynn says: "A large number of ASEAN businesses have been successful because of inbound investors, mainly from Japan. There has been a significant boom of the Japanese corporations, investing in infrastructure projects in the Philippines, Thailand and Vietnam."

Lagerberg says: "A lot of organisations are getting smarter and asking, can we partner with people? Can we form alliances? Can we join together with other organisations that want to do similar things? We see a range of different approaches because businesses also want to make sure that if they're investing in something like technology, it's going to be future proof; you're not going to spend a massive investment on something that's outdated very quickly."

> "How to get the funding to invest is always an issue for growing businesses. You can often get funding for a narrow range of investments but not always for the more exploratory things that businesses want to do. Sometimes investments don't fit into a neat model suited to more traditional ways of finance."
>
> **Francesca Lagerberg, global leader of network capabilities, Grant Thornton International Ltd**

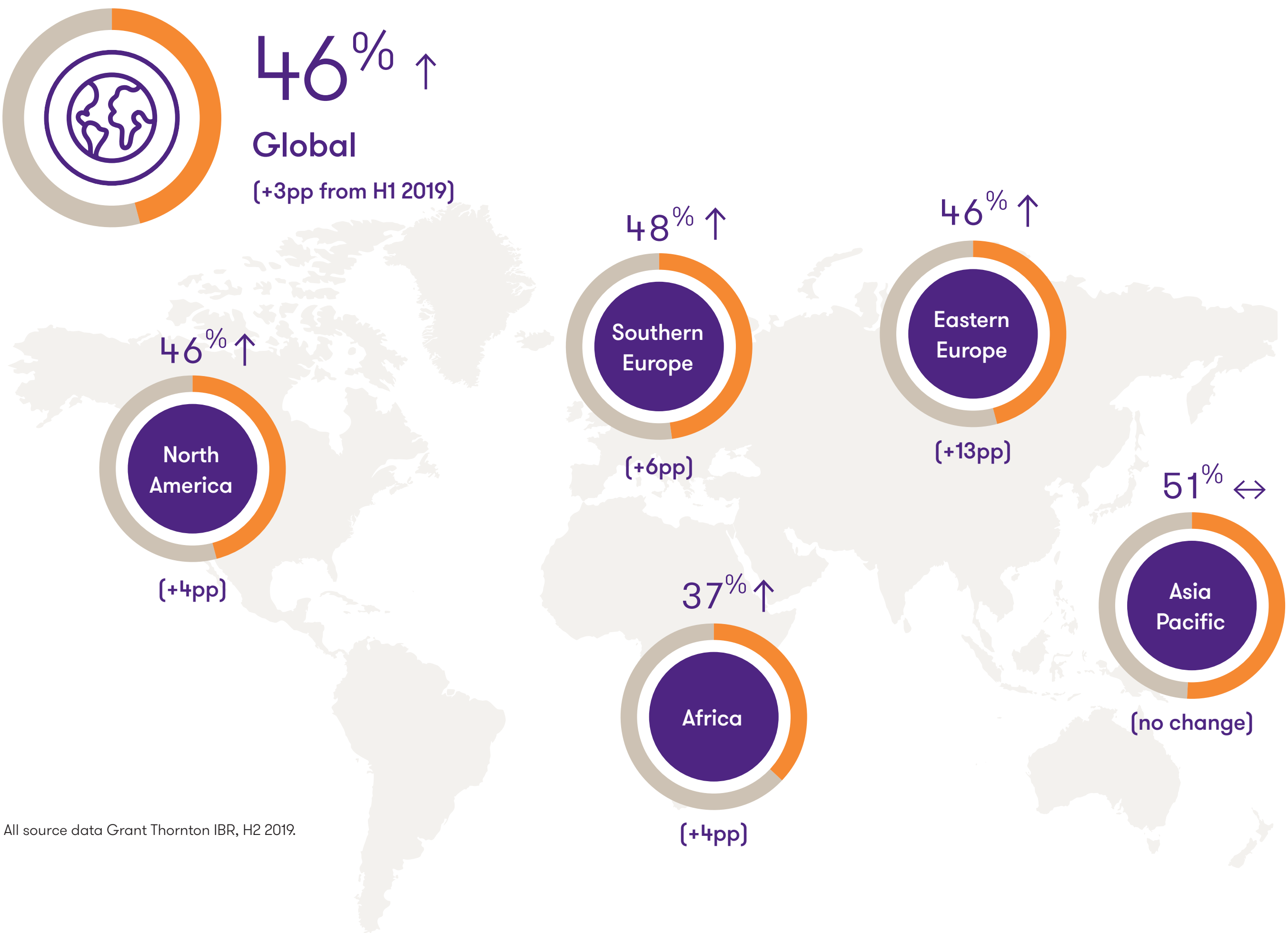
Open innovation, for example, has been a common practice among software developers for a while. Some businesses could link up and share the investment pain as well as the benefits, building a foundation block to take them forward. For example, T-Mobile and the University of Washington and the City of Bellevue recently established the 5G Open Innovation Lab, which is also backed by private and public organisations such as Intel and NASA. It aims to attract a broad range of technology skills and help explore and develop new applications for 5G while also providing collective vision for 5G's potential.[2]

2. https://thenextweb.com/podium/2019/11/27/the-secret-sauce-of-collaboration/

Look beyond your borders and develop an attractive employer brand

Availability of skills

Business leaders citing labour costs as constraint on growth



All source data Grant Thornton IBR, H2 2019.

With increased intentions to invest, the demand for skills is growing. However, as unemployment levels hit historic lows, business leaders are concerned about the cost and availability of skilled workers. Despite some signs that the labour market is cooling across developed economies such as North America and Europe where employment growth is static, 46% of business leaders feel the impact of labour costs on their growth, with Asia Pacific and Southern Europe most concerned. Meanwhile, 45% of leaders expect employment to continue to grow over the next 12 months, with ASEAN, Latin American and African countries expecting the most significant increases.

Africa has the youngest educated labour population in the world, yet skills availability is exceptionally tight. And in South Africa, the number of business leaders citing labour costs as a constraint jumped 6pp to 42%. John Lourenco, IBC NCT director for EMEA at Grant Thornton International Ltd, says: "roughly 80% of the population is below the age of 25, educated and available to join the workforce but in South Africa and Nigeria particularly, they're not the people businesses are reluctant to take these people without experience because the need is immediate and the opportunity cost of investing in training programmes prohibitively high. Additionally, unfriendly labour laws that make it difficult to exit non-performing employees exacerbate the situation."

"Often it's not just a shortage of people but a lack of people with specific skills," Lagerberg says. "The market is changing quickly. The skill needs are so different and if you have an organisation where you tend to take people at a certain age and develop them through the business, the pool from which you bring them in might be based on a model no longer reflective of your business today."

Take managed risk on future skills

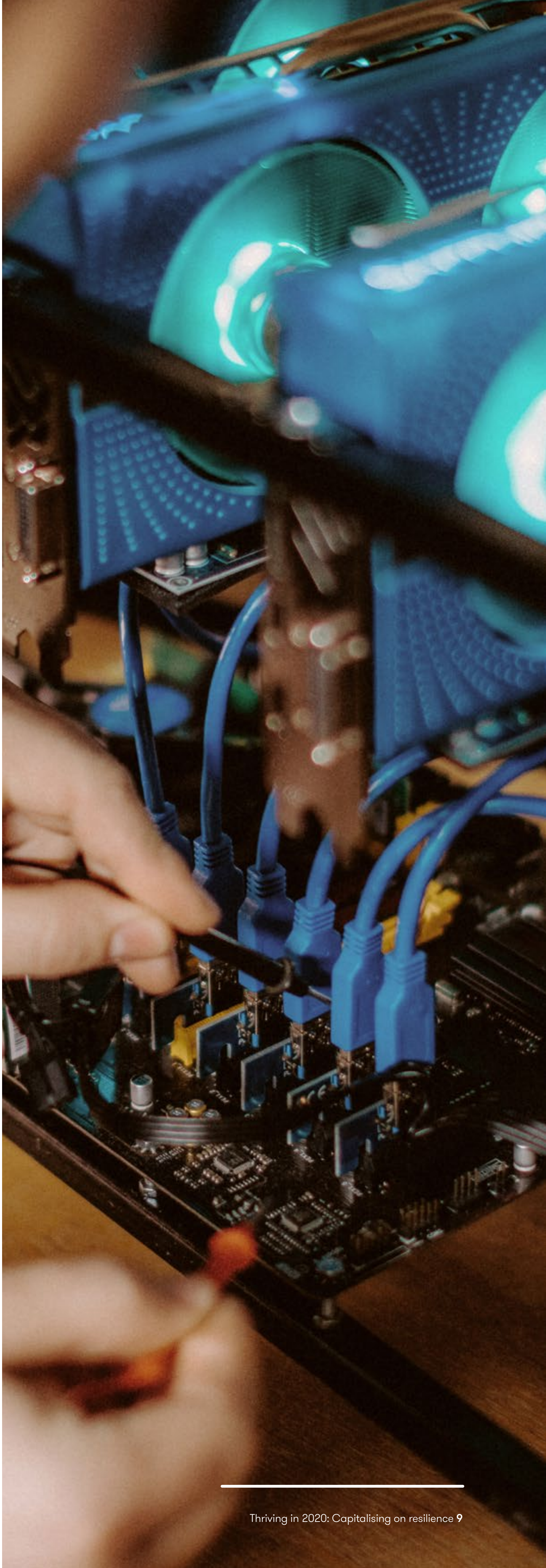
Investment in technology is one way businesses could fill skills shortages. In the healthcare sector, for example, where demand from ageing populations will put continued pressure on healthcare providers, technology is helping to make the skills available more efficient as well as create better care programmes. Keijzer says: "Providers are heavily investing in ehealth and logistics to bring more people to one place and to work on apps to service the demand that we don't have the labour for."

An international outlook can also help acquire critical skills. Some businesses are setting up offices specifically to mine prized technology skills. An example of this is Dutch interactive mapping platform Spotzi, which visualises the world's demographic composition to help marketers target consumers. It recently developed operations in Canada, capitalising on the specialist talent and knowledge in big data located in Toronto[3].

More generally, businesses that attract the right skills tend to have established positive employer brands: people want to make a difference in what they do and where they do it, says Lagerberg. Leaders need to think about the environment they are asking new employees to join. What makes their employees proud of what they're doing and what makes them want to stay there? Diversity of thinking, flexibility and purpose are three qualities employers need to incorporate in their skills strategies.

Leaders need to be looking to the future and thinking about what sort of skills and workforce they need. Says Lagerberg: "For businesses it's about looking ahead and making some bets, knowing that not all of them will come true. And that is the same for every business: you take some managed risks about what you need your workforce to be. What type of people do you need? That's where attributes can sometimes be more compelling than pure qualifications. Someone who has flexible ability who could do many things could be of more value than somebody coming in to do one specific thing."

3. https://ec.europa.eu/trade/trade-policy-and-you/in-focus/exporters-stories/dutch-mapping-spotzi/



Getting comfortable with the speed of change

Growth won't be easy to grasp in 2020, uncertainty and risks are present across all regions. Businesses will continue to scan the horizon for potential shocks and disruptions as a matter of course and adapt where necessary.

Those businesses that are most resilient are proactively exploring international pathways to reach new markets for their goods and services, and investing in the technology that will help them achieve that. However, the availability of finance is a constraining factor on investments, and leaders need to examine their business plans and ensure they are robust enough to convince lenders of their growth potential in this rapidly changing global market. At the same time, businesses may look to collaborate more with each other to achieve their investment goals when finance is challenging.

Meanwhile, acquiring the right skills for the future is critical but difficult when available talent is in short supply. Harnessing technology and accessing new pools of talent locally or internationally will help. However, employers also need to review the way in which they operate to attract and retain the next generation of talent.

Lagergberg says: "It is also about appreciating that business models that were great 10 years ago might not be right now. Success will come in getting comfortable with the speed of change and not perceiving it as purely a threat but as opportunity as well."

Speak to a local Grant Thornton adviser via grantthornton.global to find out how your business can build resilience and adapt to change.

IBR 2019 methodology

The Grant Thornton International Business Report (IBR) is the world's leading mid-market business survey, interviewing approximately 5,000 senior executives biannually in listed and privately held companies all over the world. Launched in 1992 in nine European countries, the report now surveys around 10,000 businesses leaders in 32 countries on an annual basis, providing insights on the economic and commercial issues affecting the growth prospects of companies globally.

The findings in this report are drawn from 4,900 interviews conducted in October and November 2019, before the outbreak of the coronavirus. These interviews were with chief executive officers, managing directors, chairs, and other senior decision-makers from all industry sectors in mid-market businesses in 32 countries. The definition of midmarket varies across the world: in mainland China, we interview businesses with USD 5 million to USD 500 million in revenue; in the United States, those with USD 100 million to USD 4 billion in annual revenues; in Europe, it is commonly those with 50 to 499 employees.

For more information:
grantthornton.global/About-IBR/
E gtimarketing@gti.gt.com

About Grant Thornton

Grant Thornton is an award-winning, globally recognised professional services network and is one of the world's leading organisations of independent assurance, tax and advisory firms. Grant Thornton is a leading business adviser that helps dynamic organisations to unlock their potential for growth.

Our brand is respected globally, as one of the major global accounting organisations recognised by capital markets, regulators and international standards-setting bodies. Our global scale across more than 140 countries with over 53,000 people means we can meet your changing needs and provide you with the insight and agility to help you stay one step ahead.

Privately owned, publicly listed and public sector clients come to Grant Thornton because of our technical skills and our industry capabilities, but also for our different way of working. Our member firm partners and teams invest the time to truly understand your business, provide you with real insight and a fresh perspective to keep you moving. Whether a business has domestic or international aspirations, Grant Thornton can help you to unlock your potential for growth.

Visit **grantthornton.global** today to find out how we can help you.

Grant Thornton

grantthornton.global

EPI.371