Growth Markets Centre – Developing profitable distribution partnerships in the growth markets

Presence to profitability

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Contents

Introduction

The diversity of growth markets* leads to most companies investing considerable time in establishing their strategic direction in order to prioritise which markets to enter and expand in, and identify which consumer segments to focus on with particular elements of their product/service mix.

Although this is key to success, the execution of this strategy is often more difficult in growth markets than in developed markets, due to the complex and fragmented routes to market that companies often have to navigate to reach their target consumers. The inability or reluctance, in the first instance, to develop direct routes to market leads companies to rely more on local third parties than is normal in their home markets and to become comfortable with reduced control and visibility as to how their products/services are being delivered to consumers.

As we will see, companies can take a number of steps to ensure that this lack of control and visibility does not impact their journey from ‘Presence to profitability’ in a growth market. These begin with the selection criteria, which should assess more than mere reach, and extend to growth market specific partner management policies which must be embraced by both the company and the local partner to develop trust - a vital ingredient for success. Appreciating and enhancing the qualities that made a partner attractive to go into business with in the first place has been seen to be more effective than making wide-reaching changes on day one.

However, as we learn every day, these growth markets are constantly evolving, with consumers becoming more aspirational and demanding, infrastructure maturing and regulations changing how foreign organisations can operate, for better or for worse. Companies therefore need to employ a flexible approach to react to these circumstances. What worked to enter a new growth market might not be appropriate for later expansion, and with this in mind, the relationships with those initial channel partners might have to change or even end to enable a foreign company to react to new opportunities.

One thing is clear, it is more complex to manage partners in growth markets than in developed markets. However, with the right approach and flexible mindset, companies can build profitable and, most importantly, trusting partnering relationships for long-term profitability.

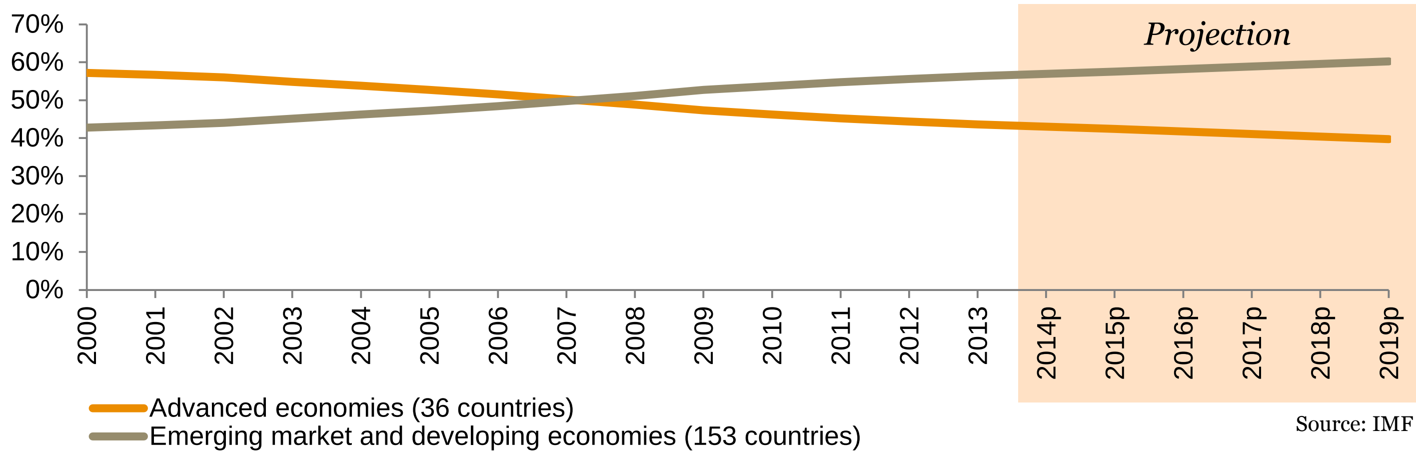
**The growth markets referred to throughout this publication range from the more established growth markets such as Brazil, Russia, India and China, to other emerging and high-growth economies like Indonesia, Nigeria, Mexico and Turkey and new markets such as Myanmar.*

Understanding the need to partner

New opportunities

Most multinationals across sectors have long recognised the importance of major growth markets such as China, India and Brazil; not just as sources of cheaper manual labour, but increasingly as the fastest-growing new customer segments for their products. Despite the well-known difficulties of doing business in growth markets, many multinationals have been successful there.

The IMF has emphasised this point by stating that the emerging market and developing economies will contribute to over 60% of global GDP by 2019[1].



Source: IMF

Figure 1

Contribution to global GDP (In PPP terms) - advanced versus emerging market & developing economies

Key challenges

Many multinationals sell more of their products and services in growth markets than in developed. For example, German automaker Volkswagen derives up to 40% of its profits from China alone[2].

However, few have been able to develop a distribution network that gives them the same level of confidence and, more importantly profits, as they enjoy in their home markets. In fact, most see distribution as perhaps the most difficult aspect of entering into a new growth market.

The challenges companies have to navigate are varied and complex. In addition to the sheer size of some of these markets, there is a need for local knowledge and strong relationships. Basic infrastructure is also often lacking.

[1] IMF World Economic Outlook October 2014, GDP is in PPP terms

[2] Volkswagen Group records robust business performance in the first nine months, Oct 30, 2014, http://www.volkswagenag.com/content/vwcorp/info_center/en/news/2014/10/Q3_2014.html

A complex distribution landscape

In India, the need for effective strategic distribution partnerships is critical to success across many sectors. This is largely due to the lack of adequate infrastructure (roads and storage facilities) and the unique nature and complexity of the existing distribution landscape. Whilst modern trade is growing, there is still a large dependency on small local distributors (kiranas – mom and pop stores), which makes it more complex to manage how goods and services reach consumers.

Shashank Tripathi, Executive Director – Advisory, PwC India

"Most see distribution as perhaps the most difficult aspect of entering into a new growth market"

Infrastructure and scale

Roads and storage facilities in the growth markets often deteriorate rapidly, particularly in the major cities, which increases the reliance on a local distribution partner's own infrastructure and access. However, few local companies are able to meet the expected technological and logistical standards on their own, and even fewer are able to achieve full geographic coverage within a country. As a result, distribution can often only be achieved through an extensive network of small, local, independently owned distributors, each with their own capabilities, processes and support needs. Even major third-party logistics providers such as UPS and FedEx can be obliged to sub-contract local providers to ensure coverage in remote locations.

Local regulations

In addition to these physical challenges, multinationals are increasingly obliged to consider their home territory legislation in relation to their local activities, particularly with respect to financial compliance and governance. Where these provisions differ from local regulations, a further layer of complexity may be applied to local relationships.

These challenges have led many multinationals to minimise investment risk by entering new growth markets mostly through arms-length agreements with one or more local third-party distributors to meet their primary goal of achieving market 'presence' - *"How can I get my product/service out there as quickly as possible?"*.

Diverse and demanding consumers

Such 'indirect distribution' approaches became the default Go-To-Market (GTM) strategies for many multinationals, and were, in fact, initially quite successful, in part because most growth markets were still relatively small, which meant that only a few of the larger cities needed to be covered. However, this traditional approach is rapidly becoming obsolete as the growth

Dealing with scale

The sheer size of distribution areas poses a major challenge in many growth markets, not least in Brazil, and with this comes a number of associated complexities. One is how to segment and manage a region in order to best capitalise on the operational and administrative capabilities of each different distribution partner, whilst also minimising the risk of channel conflict.

Wholesalers tend to market a wider array of goods (less specialisation) and offer your product at lower prices than local distributors. They have a more extended reach; however, they can also be less committed to your product.

In contrast, a local distributor can act as a sales representative and market your proposition as a higher value-added product, but has limited reach and needs more management.

If these two channels market in the same regions, it can generate friction, with both the manufacturer and the end consumer losing out. Hence, managing the portfolio mix of types of distributors across a large area needs careful planning and management.

Leandro Spadini, Partner - Advisory, PwC Brazil

markets themselves continue to mature, giving rise to new and more affluent consumer segments, not just in a few major cities, but increasingly also in smaller rural cities. In addition, consumers in growth markets are becoming increasingly diverse and demanding a far greater range of products - from value to premium - than before, while competition from local and other foreign players is intensifying.

As a result, many multinationals are being forced to fundamentally rethink their GTM strategies to meet future demand and remain competitive in the major growth markets.

Presence to profitability

In order to meet these new challenges and evolve from mere 'presence' to 'profitability', many multinationals will have to acquire a new, more advanced, set of GTM capabilities. For starters, they will need to gather much more granular information about these new consumer segments from credible points-of-sale (POS), and achieve far greater levels of transparency and control over how their own products and services are actually reaching these consumers. Doing so will require higher investment levels and involvement with distribution partners, leaving many multinationals with no choice but to restructure their local partnerships and joint ventures around future growth potential and varying levels of support, based on each partner's specific organisational capabilities, performance level and strategic significance. In addition, multinationals need to ensure that these partnership agreements leave them with enough freedom to vary the distribution mix and reduce their reliance on 'indirect' only approaches, as opposed to more heterogeneous GTM solutions that achieve a better balance of power with their distributors.

Achieving greater insight, control and profitability requires a higher degree of effort to identify the right set of select partners and develop an effective operating model. This will enable the company to expand and grow profitably with the opportunities and challenges of the market.

Identifying the right channel partner

It is more than just distribution reach

While businesses in developed markets can generally choose from a wide range of capable potential distribution partners, selecting a partner in growth markets involves a much broader range of considerations.

These are often specific to a local market and can be difficult to articulate to a remote headquarters or management board without experience in the location, but can be critical to the success of a new market venture.

1 Reach

2 Knowledge gaps

3 Power balance

4 Regulatory considerations

5 Risk and sustainability

6 Exit strategy

Figure 2

Key partner identification criteria

Reach

It is not surprising that the extent of a potential partner's coverage is a standard starting point when evaluating the suitability of a distribution partner. However, it is rare that one partner has the size and scale to distribute and maintain the relevant product and service experience, particularly where complex after-sales service is required. The relevant local skills may not be available, or may be difficult to retain, which leads companies to invest in training and recruitment programs to enhance local skills in these areas.

Knowledge gaps

In addition to the coverage of a local partner, the quality of the information gathered and analysed is another key consideration which is often hard to identify, let alone evaluate. Those who have a decent distribution coverage may not have the capacity or desire to invest in systems and structures which can provide customer information and feedback, supporting the development of the market. Point-of-sale information can be difficult to obtain, and restricts the ability of the business to manage and adjust the supply chain. In this case, foreign companies may need to invest in other channels, including local champions such as village elders or local business associations, to improve this visibility.

Power balance

These reach and capability challenges are hard to navigate, but they are often accentuated by the fact that many local distributors also play a much broader role in their communities. This further increases their influence and the balance of power in the foreign company-local partner relationship.

In the agricultural sector in the Philippines, for example, the local entrepreneur will supply seed to small farmers and finance their crops in return for first rights to the harvest. This full cycle involvement creates significant barriers of entry for new providers, and allows the distributor to control product selection and promotion.

In addition to this, local distributors will often have a monopoly in their region, allowing them to be selective in choosing products to promote and invest in. They are less reliant on exclusive relationships, and can play suppliers off against each other to optimise their own returns. As a result they may have no desire nor need to scale up in line with the expansion plans of the business. This places them in a strong position in negotiation, forcing the international business to choose between power in the relationship and presence in the market. Addressing this balance of power is critical in moving from mere presence to profitability.

Establishing the right operating model

A leading global Fast-Moving Consumer Goods (FMCG) company in China had been using a wholesale distribution approach for several years to reach consumers across the country. However, it became more and more difficult to profitably address an increasingly heterogeneous and demanding customer base across a growing number of price points and retail formats.

This was compounded by a suspicion that discounts were not being driven down through the distribution chain, or were sometimes simply pocketed by the wholesaler. All these issues prevented the company from realising 15-20% more in profits.

To combat these issues the company worked with Strategy& to develop a distribution strategy that was nimbler and provided better control. This was based upon five key principles:

1. *Map products to certain consumer segments*
2. *Calculate the profit to serve (sales uplift – cost to serve)**
3. *Establish a channel mix/mosaic to distribute products*
4. *Build the right capabilities (e.g. customer insight, account planning, partner relationship management)*
5. *Develop good local talent*

Although it was challenging to address these topics, the company has begun to reap the benefits and has established greater control through its distribution channels, leading to enhanced profitability.

John Jullens, Partner, Strategy&, China

**Cost to serve:* *This includes direct costs (the costs of distribution from plant to wholesaler or plant to retailer and sales force budgets) and external costs (promotions and discounts).*

Sales uplift: *This involves estimating potential revenue and sales gains or losses of different distribution model scenarios, focusing specifically on the impact of varied point-of-sale approaches, increased number of stock keeping units (SKUs) and out-of-stock reductions.*

Knowing what to look for

A global food company considering market entry opportunities in the FMCG industry in Saudi Arabia asked PwC to support in identifying a suitable local distribution partner. Beyond just the ability to distribute high volumes of produce to a large number of retailers and cover multiple regions, PwC looked for the following in a potential partner:

- *A long track record of operations in Saudi Arabia*
- *Deep sector expertise relevant to the company's product portfolio*
- *Strong local business connections*
- *A good reputation and sense of integrity*
- *Commitment to marketing and promoting their products effectively*
- *Clear and open communication processes*
- *Understanding of/willingness to follow western commercial business practices*

Philip Shepherd, Partner - Advisory, PwC Middle East

Regulatory considerations

Understanding the business environment is a key component to selecting the right partner; often local laws and regulations will narrow the partner shortlist depending on the sector you are operating in. Thus, gaining a good understanding as to what you can and cannot do will save time and expense.

Similarly, rules on secondary manufacturing and packaging can influence the capabilities required of the partner, while in some sectors, such as pharmaceuticals in Indonesia, local manufacturing of products for local distribution may be mandated, narrowing the options further.

For example*, local content rules in the automotive industry in the Association of South East Asian Nations (ASEAN) typically run at 30-40%, with different levels for the ASEAN region compared to local country auto incentive schemes, and different formulae for calculation. As local content can include the cost of domestic transport, storage and warehousing, selection of a distribution partner can impact this calculation.*

Regulatory compliance

A US multinational was evaluating a potential joint venture in Yangon to partner on infrastructure development projects across Myanmar. The projects were to be awarded through a government tender process, which raised the possibility of corruption due to the potential for illicit payments being made to government officials.

As the US company was subject to the Foreign Corrupt Practices Act (FCPA) prohibiting corrupt payments to foreign government officials to obtain or retain business, the company took the precaution of engaging PwC to conduct reputational due diligence using a variety of sources:

Public domain research including local press, online materials and open source information in both English and the Myanmar language

Opposition party information and records on the country's prominent business figures

In-country corporate public records to identify principals of the subject companies

Proprietary industry-leading risk and compliance databases and international media archives

Satisfied that the joint venture was at an acceptable level of risk to proceed, the company then worked with PwC to provide anti-bribery and corruption training to the management and employees.

Mark Brown, Director, Forensic Services, PwC Singapore

Risk and sustainability

As well as understanding what the local regulations will permit a company to do, it is also vital to evaluate the business risk and sustainability of a potential new relationship. A fragmented and broad distribution network inevitably increases the risk of losses and theft, as well as the potential for breach of intellectual property. To protect against these financial risks, thorough due diligence is needed. However, it is rare for sufficient information to be readily available to make a sound decision. This necessitates on-the-ground assessments of reputation and associations. Standards and consistency in ways of working may also vary from those considered usual in more developed markets.

Managing brand risk

PwC was engaged by a leading motor vehicle Original Equipment Manufacturer (OEM) to explore how best to restructure its distribution activities to increase profits in line with growth in the Indonesian market. The company had been in partnership with a local distributor in Indonesia for eight years.

An initial review revealed that the local distributor had most likely been declaring inaccurate purchase prices when the motor vehicles were imported into Indonesia. This had resulted in huge cost savings to the distributor but was clearly a violation of Indonesian customs law.

As a result, the OEM's profitability assumptions on the Indonesian market were based on a non-compliant and ultimately unsustainable business model. If the OEM or a new distributor paid the correct amount of import tax on the vehicles, the profitability of the market would be much lower than expected.

The OEM was faced with the difficult decision of whether or not to immediately prevent the current distributor from continuing to underpay import tax. Failure to do so would put the brand at risk, but doing so would destroy the distributor's profitability and put it at huge risk of a Customs investigation into past imports.

Frank Debets, Managing Partner, Customs and International Trade, PwC Worldtrade Management Services (WMS) Singapore

A key learning:

It is worthwhile taking the time to conduct regulatory compliance checks to ensure local distributors are complying with applicable regulations to avoid a brand-damaging situation.

In Indonesia the mis-declaration of imported vehicles to avoid tax is common and local companies may have successfully employed this strategy for many years. However, the environment is changing and anti-corruption and transparency drives within the Indonesian government are closing these loopholes.

When the local distributor is caught, it will be the name of the famous OEM which appears in the newspaper rather than that of the local distributor.

Risk to the organisation's reputation must also be considered, as the dominant partner in a location may operate under particular political or military patronage. The impact of association with such links may be detrimental to the organisation, either within the local market or in the external environment. In many cases the long-standing relationships that distributors often enjoy with regulatory authorities can ease daily business operations. They may, however, also result in practices that are not compliant with regulation. When circumstances change – for instance a new political party comes to power or an anti-corruption drive occurs – such practices may result in supply chain risk, additional costs and brand exposure. A brand owner that wishes to take over distribution in a maturing market may also find that the regulatory requirements it faces are quite different and more costly than those formerly encountered by its local distributor(s).

Free Trade Agreements (FTA) - Vietnam/Indonesia

For years a major consumer goods company had been saving millions of USD in import duties by using the ASEAN FTA, whilst manufacturing materials in Indonesia for sale to its related manufacturing companies across Asia.

A change in the regular shipping schedule to Vietnam meant that different customs officials reviewed the ASEAN FTA documentation. They noticed that some of the information on the form was unlikely to be accurate and submitted a formal government-to-government request to Indonesia for verification.

Pending the Indonesian government's response, the company asked PwC to investigate whether or not the product shipped from Indonesia did in fact qualify as 'Made in Indonesia' under the terms of the ASEAN FTA.

Vietnam

It appeared that the Indonesian manufacturing company had been engaging a third party logistics company (3PL) to complete the ASEAN FTA documentation on its behalf; that company had used the same information on all the FTA forms regardless of the product or manufacturing. In fact, 22 separate product types had been declared as of Indonesian origin and had incorrectly enjoyed ASEAN duty preference for years.

The potential exposure to the client was over US$6M, and its financial model, which was based on assumptions of preferential duty rates on these products, had to be completely reworked.

Indonesia

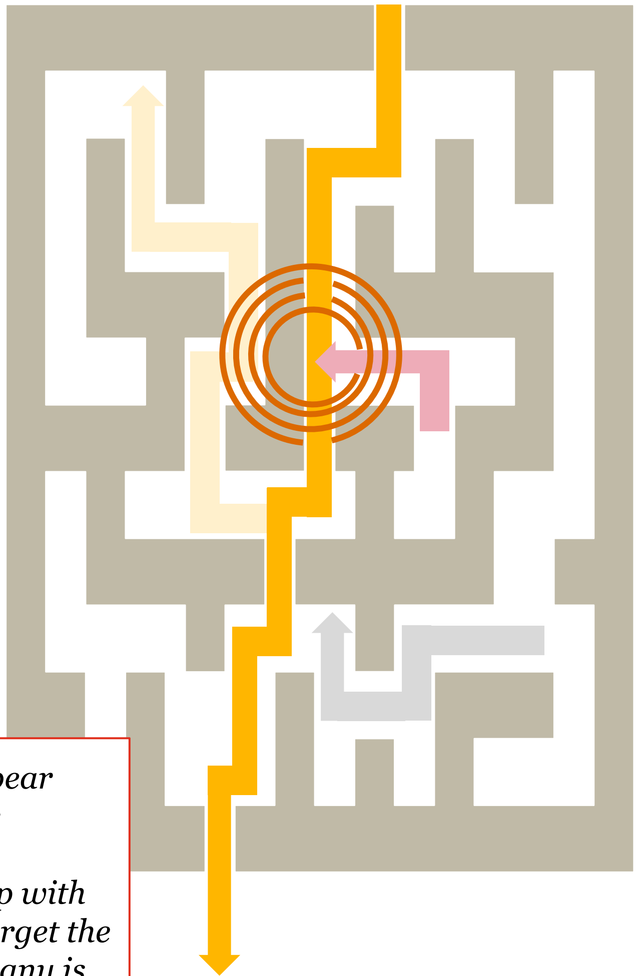
Frank Debets, Managing Partner, Customs and International Trade, PwC Worldtrade Management Services (WMS) Singapore

Exit strategy

If, having evaluated all the aforementioned considerations, a foreign company is lucky enough to identify a potential partner to facilitate its entry into a new market, it must acknowledge that things change rapidly in growth markets.

A distribution strategy that works for entering a new market might not be the most suitable for wider expansion. Customers' needs evolve quickly and new consumer segments may arise which are not within the reach of an initial distribution plan. As such, foreign players need to be prepared to adapt their initial distribution plan. This may involve enabling an existing partner to expand their capabilities to meet the demands of these new consumers.

However, in some cases tougher decisions might need to be made, such as finding new partners to add to a partnering mix, or even dissolving a partnership and developing one's own distribution capabilities. Planning for tomorrow's growth when entering a new market will make it easier to execute expansion plans at the right time.



Whilst long-standing relationships may appear fruitful and effective, sometimes they can be restrictive. One Japanese consumer goods company has enjoyed a 30-year relationship with a local distributor which has helped them target the mass consumer market. However, the company is now unable to execute plans to expand into the more profitable premium segment as its local partner is unwilling to adjust its own local focus.

In summary, the selection of a partner to enter a growth market must extend beyond distribution reach and facilities. It must consider the compatibility and relative control and influence of the two parties, synergies in ways of working, local and international compliance and brand, product and reputational risk. Many of these aspects will be defined at a local level, and may be beyond the experience of global or even regional management, so a structured approach to assessment is essential for both practical evaluation and senior management buy-in. The assessment must also include an exit strategy, with the recognition that this may include full withdrawal from a particular market if no viable alternative is available.

Making a partnership work

The complex nature of distribution in a growth market means that partnerships cannot be based solely upon transactional targets and sales Key Performance Indicators. Whilst these are of course important, the chances of achieving or exceeding country targets are enhanced if softer relationship-based targets are also considered.

Sales targets and contractual terms may be the building blocks of a partnership, but it is the relationship-enhancing measures that are the glue to building a successful and profitable partnership.

Although many foreign companies have been present in China for decades, managing partners effectively and operating profitably is still not an easy task. The following core principles are worth noting from a China context:

Figure 3

Eight core partnership principles in the China context

Focus on filling capability gaps

- In unfamiliar circumstances it is easy to favour comfortable partnerships; however, capability-led approaches tend to be more profitable.

Don't be fooled by guanxi

- Developing relationships is an important part of doing business in China; however 'guanxi' is often overrated and misunderstood, and is rapidly becoming less important.*

Remain flexible

- Customers, partners and markets change quickly in China, so companies need a flexible partnering strategy, often with a portfolio of several partners.

Keep on triangulating

- Quality data does not always exist and so effective relationships can help access current information and provide a more balanced and reliable view.

Conduct a thorough stakeholder analysis

- Identify key decision makers and understand their own objectives.
- Often these may not align to yours and frequently the government is involved.

Clarify decision rights up front

- Even in a relationship-based environment it is crucial to have decision-making processes, roles and responsibilities defined at the outset. This avoids unpleasant surprises later.

Go easy on the integration

- Although some Chinese companies might be less sophisticated, avoid imposing immediate changes that may destroy the value which made the company initially so attractive.
- Be deliberate about what to change and what to keep 'local'.

Find ways to earn trust

- Establishing a commitment to combined goals, empowering the deal-team and ensuring that senior executives on all sides are actively involved in decisions are key steps to a trusting relationship.

Source: Jullens, J., "*Solving China's M&A Maze*", Strategy + Business, April 1st 2013

*The Chinese concept of *guanxi* is based on mutually reinforcing cycles of reciprocity and influence, often involving gifts and favours.

A locally defined partnering agreement will give you early presence....

Contractual terms are important; however, the areas of emphasis and metrics applied may differ significantly, as ability to enforce the contract will be directly affected by factors such as the number of alternative providers, the ease and cost of transition, local regulations and business practices. While basic contract structures may be similar to those in developed markets, they may require variation to deal with the particular nuances of growth markets.

Organisational structure

Building the most suitable organisational structure with the requisite authority, governance and control measures is an obvious contractual consideration. However, this may include changes to the normal business structures employed in developed markets. Decision-making may need to be empowered much closer to the local market, and may require greater flexibility than usually allowed. Conversely, headquarters and central boards of management must be satisfied that appropriate controls are in place to manage business and reputational risk at the local level.

Locally defined goals and responsibilities

With this hybrid organisational structure, a clear definition of achievable goals and responsibilities is needed. Local business practice may influence the interpretation of these definitions. For example:

- State-linked companies or joint ventures in China will typically include a Party committee. While not directly responsible for the operation of the business, this committee oversees the social and political obligations of the organisation, and can exert significant influence over process and decision-making.
- Under Indonesian company law, limited liability, or "PT" companies must have both a Board of Directors responsible for day to day management, and a Board of Commissioners which acts as a supervisory body over the Board of Directors. This can add complexity to relationships and negotiations.

Recognising that the parties will have different business priorities and that (as noted previously) power in the relationship may lie with the local partner, a clear definition and agreement as to what is expected from each contracting party at the point of contracting is crucial to the success of the market entry.

Implementation of systems and processes

A common problem for businesses in all industries entering growth markets is the ability to view demand information beyond the local distributor. Therefore it is usually necessary to agree on the level of systems and process capability needed to provide visibility on distributors' activities and customer behaviour. A further complication is that distribution networks are likely to be more fragmented with multiple local providers involved. Hence organisational structures may require additional administrative and technological support to address overlaps and higher levels of transactional activity. As a result, typical benchmarks used in setting up the structures may not be relevant and must recognise the sophistication of the distribution partner as well as the partner's willingness to provide this transaction data.

Performance measures

Even with these systems and processes in place, the data which is captured may not be to the level of detail or accuracy commonly achieved in developed markets. Therefore, performance indicators and metrics included in the contract must be relevant to the environment.

Timelines

In addition to metrics, clear and realistic timelines must be built into the contract. Local conditions, business practices and local regulations can add significant time to the establishment of a new network, or even to relatively minor changes. In Indonesia, changes to a label for a nutrition product require regulatory approval and typically take six weeks, compared to just days in other parts of Asia, while time to approve a new business licence in China varies significantly by city or province, and can take more than six months.

Plan for tomorrow

Given that these contracts are typically developed at the entry point to a new market, it is appropriate to include some provision to address a path for future development of the relationship or, in the worst case, a mechanism to exit the market. This 'pre-nuptial agreement' can include provision for a review of the partnership after a set period of time, options to increase or divest a share of the partnership, or caps on the range and scope of the relationship.

... but the establishment of an effective relationship will lead to profitability.

An effective relationship is of paramount importance if a partnership is to achieve profitability rather than simply a presence. Whether a company's presence in the market is through a majority share acquisition or a partnership agreement, it is important to move from a relationship based on authority or commercial benefit to one that is based on trust as soon as possible, and ideally from the outset.

A solid, trusting relationship is what will motivate a local sales person on the ground to push one foreign company's product more than any other, drive sales and gain market share and intelligence - ultimately yielding the results headquarter boards understand and strive for.

Building a successful business in a new growth market has a price, and establishing effective relationships is the most important element. Developing these relationships may not be something which can be attributed to a line item on a Profit & Loss statement, as the principal investment is time. Therefore, it is important to communicate to headquarter boards that time is required to establish profitable relationships so that there is no undue pressure to rush things on the ground. After all, having carried out the due diligence to find the right partner, it is worthwhile investing the effort to ensure it becomes a profitable relationship in the long term.

A Japanese conglomerate was evaluating a Thai lubricant manufacturer as part of a potential acquisition and one aspect that they valued most was the local company's long-standing relationships with their sole distributors. It was hard to put a price on them but these local relationships were the catalyst for driving sales.

Philippines

Training / up-skilling

A western European transportation company needed to transform the way its Global Finance team functioned - from being a reactive scorekeeper to a proactive business partner. A key aspect was the interaction between the Accounting & Reporting function located in the Philippines and controllers operating in their own territories across Europe, North America and China.

The company worked with PwC to deliver a global training programme targeted at improving the communication between the Philippines team and the global controllers. The programme included providing insights on preferred behavioural and communication styles and role-playing each other's interaction styles as well as developing roadmaps with 'golden rules' to improve each team member's overall communication and interaction. These roadmaps and golden rules were then shared globally.

Almost all the Finance professionals in the company across the globe participated in this exercise. Ultimately, the programme introduced a common language across the global Finance function and created a better understanding of how best to build interpersonal strategies to work more effectively, whether with someone from your own country, or a partner that is at the other end of the world.

Martijn Schouten, Director,
PwC South East Asia Consulting, Singapore

Figure 4

Five key relationship dynamics in every partnership

Listener vs Imposer

Performance measures

Building trust is a challenge within an organisation; building it across two separate ones with different cultures is a huge task indeed. A good starting point is to simply listen to your local partner. Assess the skill of the sales team, the efficiency of the process and the reason behind incentives before implementing a new set of rules. For your company to have chosen them as partners, they obviously must be doing something right. Respect that and ensure their key strengths – be it their people or processes – are preserved.

Systematic vs Mercurial

Locally defined goals and responsibilities

Very few people appreciate a change in their style of working, especially if their current style has seemed to work for them for a long time. A strategy like 'increasing market share by selling high value products' requires a change in the selling tactics of a team that has been selling mass products for years. This requires time from the management, not just in training, upskilling and coaching, but also to ensure change is systematic rather than based on rash and quick reactions. It is sensible to start with must-haves like accounting standards and then move to nice-to-haves like gift policies.

Integrator vs Operator

Implementation of systems and processes

Foreign firms often fail to put themselves into a local partner's shoes. A key task here is to ensure that a local partner's interaction with the person responsible for driving change and integration is smooth and positive. This is a role for an integrator, not a firm's number one operator. An operator might focus more on sales targets than on getting the right people to achieve them. It is important to identify the right person who understands headquarter functions, appreciates the local conditions and can dedicate a significant amount of time to building the right local relationships. One of the best ways to gain trust is to have an intermediary that both parties trust.

Sharing vs Instructing

Organisational structure

In most growth markets, getting people to sell is about more than just asking them to do it – it is about persuading them into 'wanting' to do it. This happens when the local team feels like they are part of your company. Involving the partners in strategic discussions and asking for their insights helps gain their trust. Training sessions and secondments can act as platforms for sharing. This includes inviting some key people from the local teams to spend time in the foreign company's headquarters, as opposed to only sending people from HQ to the local countries – which is the norm.

Making a partnership work

A leading international packaging company and one of their customers in Africa had been in partnership for several years. However, there was dissatisfaction on both sides about the relationship. The packaging company felt that they were not creating value or growth and their partner did not feel the packaging company was prioritising their business to enable them to be more profitable in the face of increased competition. The relationship was not progressing.

The packaging company worked with PwC to address their Customer Satisfaction process with a specific focus on identifying the following:

- *Factors that were hindering the effectiveness of their partnerships*
- *How to develop trust and credibility*
- *An agreed plan to work towards a strategy for growth on both sides.*

Having established management goals and a commitment to change, PwC supported the packaging company in carrying out a series of interviews across their partner's business. Customer data was also analysed to identify the key issues and risks to their business relationship.

Africa

The results were discussed and brought to life candidly by management on both sides. Having then understood the priorities, preferences, opportunities and risks, a long-term strategic plan was jointly developed.

Sustaining meaningful partnerships takes courage, commitment and time. In this case, it took seven years to get to a true partnership status. By confronting the issues together openly, the packaging company's performance rating improved from 3/5 to 4/5.

Peter A. Hoijtink,
Associate Director - Advisory,
PwC Africa (South Africa)

Communicating - Sender vs Receiver

Timelines

"I will send an e-mail on the process change and it will be done in a day" – ever wondered why it is 'still not done' after months? How we communicate is important in getting a corporate message across. In most growth markets communication is more personal. Selling is often done in a more informal manner or event (over a meal or several!). At times, communicating system changes and corporate goals via email is considered impersonal. Developing an open and transparent communication style makes your partner keen to accept your culture and way of doing things. Once they are on board, resistance towards change starts to melt away; the move towards more corporate ways of communicating can begin once trust and understanding have been developed.

Growing to the next level

Once an initial go-to-market presence has been established, companies must shift their attention to growing their fledgling distribution networks to the next level. This is relevant not only in terms of geographic and channel coverage, but also with respect to the capabilities required to profitably serve markets which are likely still to be rapidly evolving, with new customer segments, competitors and technologies emerging on a frequent basis.

It must be acknowledged that all this is taking place whilst underlying customer wants, infrastructure and, of course, the regulatory environment are simultaneously evolving in often unpredictable ways.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Geographic expansion

Most obviously, companies will want to expand their initial distribution footprint into new geographies. This would typically include markets in smaller cities and more rural areas with far less sophisticated buyers and infrastructure. This often requires a rethink of the initial go-to-market strategy, as even the company's existing local partners may not be able to profitably serve these new markets themselves.

For example, several western consumer electronics and white goods manufacturers initially entered China successfully through partnerships with local retailers, such as Suning, which offer commercial real estate and other support services to create store-in-store marketplaces that have been highly successful in major cities such as Beijing and Shanghai.

However, China's smaller cities and more rural markets typically don't offer the customer density required to operate such stores profitably. Morever, in a related development, Chinese consumers have highly embraced shopping via the internet. In fact, China already has the largest number of internet consumers in the world today. As a result, even Suning has been struggling to reinvent its own business model to expand its product categories and better integrate online and offline sales.

Maturing customers

At the same time, companies will often have to re-evaluate their existing distribution networks in the larger cities as well, but for very different reasons. Here the challenge is typically that their growth market consumers are learning and evolving rapidly themselves. They are becoming far more sophisticated shoppers who are not only less willing to pay above-market prices for luxury goods but also increasingly aware of price-value trade-offs for mainstream products. In addition, they will likely start to demand much higher levels of customer service.

For example, Chinese consumers have lately taken notice that they appear to pay far more for their cars and aftersales service parts than consumers in, for example, the US and Europe. This has prompted the central government in Beijing to take action under its previously largely dormant anti-monopoly regulations and levy hefty fines on several foreign automakers and parts suppliers.

How Coca-Cola has grown effectively in India with a hybrid channel mix of partners and its own distributors

Our vast production and distribution network, which we refer to as the 'Coca-Cola system', is the core of our business in India, as it is in all 207 countries we operate in. Our beverages reach our ultimate consumers through our customers: the grocers, small retailers, hypermarkets, restaurants, convenience stores and millions of other businesses that are the final points of distribution for our products.

The aim is for the relationship with our customers, which includes merchandising, selling in and the order-taking process, to be managed by the Coca-Cola system, and we are working towards increasing this coverage and capability. The delivery is made through a mix of Direct Store Delivery (DSD), distributor model and a hub-and-spoke distribution model for rural India.

Our key focus for future growth is to expand our outlet penetration from the current 30%+ of all FMCG outlets by expanding our existing distribution system, serving existing opportunities like the vast railways channel and building our presence in emerging channels such as online as well as organised retail.

Sanjeev Kumar, Chief Financial Officer, Coca-Cola India

Increased flexibility, more control

In response, many multinationals are forced to take much greater control of their existing distribution networks to improve transparency and in-store capabilities, instead of relying primarily on their partnerships with local distributors. They also have to experiment simultaneously with alternative approaches, partners and business models for new segments and markets.

The key is to adopt a very local and granular approach with, for example, different strategies for larger cities that offer greater customer density and sophistication versus smaller cities with alternative customer and profitability profiles. In addition, there must be enough flexibility to tailor each overarching approach to the unique needs of each specific segment or market.

The result is typically a 'mosaic' of tailored go-to-market strategies, based on differences in each segment or geographic market's optimal sales and distribution model (e.g. online versus offline), the role and profile of the sales force (e.g. account openers, business advisors, in-store merchandisers), and, of course, whether the company should own the channel itself or partner with a third party.

Not surprisingly, such mosaics present most companies with formidable management, organisational and even measurement challenges.

In other words, if one-size-fits-all distribution networks are suboptimal and the business and regulatory environments are also changing rapidly, it is crucial to invest in local capabilities, devolve real decision-making authority to the local organisation and invest heavily in local capabilities. Many companies struggle with this, as it implies not only duplication and a resulting loss of efficiency, but also a partial loss of managerial control over what may very well be the company's most important growth market(s).

However, most companies have little choice in the matter, as it is simply impossible to manage the complexity and speed required in most growth markets from the comforts of a developed market home. At best, headquarter decisions are simply too slow. More likely, they are also suboptimal and, not infrequently, even counter-productive, especially in the face of increasingly formidable and much more nimble competitors from these growth markets themselves. As a result, most companies will have to move away from their global organisational structures to something much more flexible. In some cases, it is enough to merely redefine a few key decision rights, while in others a complete organisational redesign is required.

Conclusion

Although many companies have now established a presence across several growth markets, reaching the levels of profitability acceptable to shareholders remains complex. Navigating this complexity involves a different strategy from what delivered profitability in the developed markets. However, this approach needs to be nimble in order to react to the rapidly evolving business environment and consumer expectations in these growth markets.

As we have seen, key to success is finding the right partner. Therefore, it is worth noting that in addition to the familiar capability-focused selection criteria, such as pure reach, and the ensuing performance-based measures, companies growing in these markets need to be cognisant of some wider considerations which, if neglected, may cause serious damage to profitability and the brand.

Thoroughly vetting a potential partner and fully comprehending and adhering to both the local and domestic regulations and trade treaties may seem cumbersome at the time, but could make the difference between realising a new set of profits and retreating from a new market having experienced a costly loss to brand and profitability.

Not only is the selection of the right partners different in these markets from those back home, so too is effective management. Working at building an effective and mutually beneficial relationship is crucial to success, but so is staying true to the initial rationale for the partnership. Rapid change towards more traditional processes might not be as effective in a growth market as in a developed one and in many cases will counter the advantages of the partnership.

Having established an effective and profitable partnership is no guarantee to future growth, and in many cases the road to further growth and profitability may be with an extended partnering mix or someone else entirely. Profitability is not an automatic outcome of presence in the growth markets, so being aware and prepared that certain partnerships have a lifespan will enable companies to adjust a channel strategy to meet their growth potential and the constantly evolving market circumstances.

About the Growth Markets Centre (GMC)

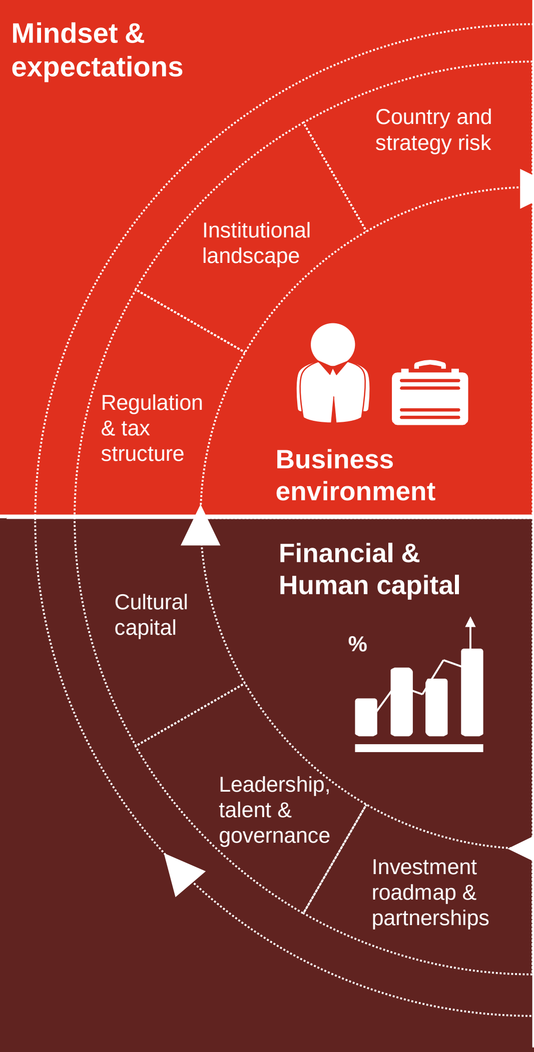
PwC's Growth Markets Centre brings together the best of PwC and Strategy& growth markets expertise

Our growth markets methodology supports companies in addressing their market entry and expansion

Growth markets methodology

Business environment:

Acknowledging the complexities associated with a territory's laws and regulations, including its political and economic stability



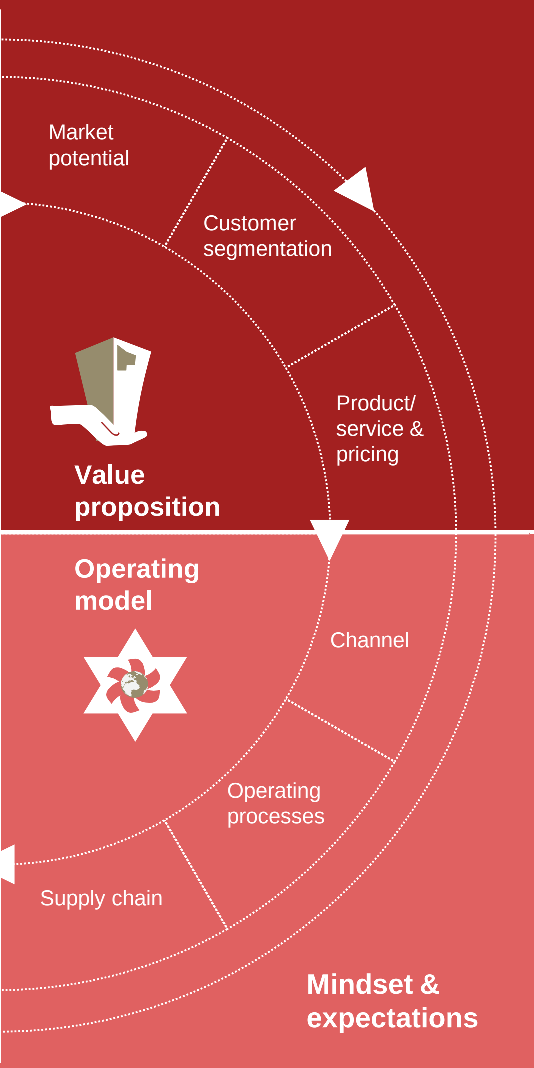
Financial and human capital:

Addressing the 'softer' challenges of acquiring talent, developing partnerships, securing financial support and appreciating cultural differences

Mindset & expectations:

Linking all of these elements is the understand what it takes to succeed

from across the globe to help companies navigate these complex new markets profitably.
needs.



Value proposition:
Assessing the attractiveness of new markets or regions, identifying the right customers and evaluating which products and services to take to market and at what price

Operating model:
Establishing the necessary balance of global and local expertise to be able to source, manufacture, and distribute effectively in a market

change in mind-set needed to in a growth market.

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PwC's insights and research

Through the Looking Glass: What successful businesses find in India

Multichannel strategy

Profitable growth strategies for the Global Emerging Middle: Learning from the 'Next 4 Billion' markets

Growth in new markets: It's all about how

Customer-centricity and selective capillarity: A multichannel strategy for telecom operators