Crystal Ball Gazing: Asia-Pacific in 2005 and beyond

In this inaugural, January 2005 edition of the E-quarterly, we interview Spire’s Group Managing Director Leon Perera for his views on trends making an impact in the Asia Pacific’s sales and marketing landscape in 2005 and beyond.

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Spire E-quarterly: 2004 ended tragically with the tsunami disaster affecting much of South and Southeast Asia. What impact will this have?

Leon: The tsunami tragedy has taken a terrible toll in human life. Despite this, the experience of past natural disasters suggests that the economic impact on the affected countries should be fairly limited. This is provided that relief efforts contain the risk of epidemics of disease spreading in the wake of the disaster. Ports and shipping have not been seriously affected. Clearly the tourism industry in places like Thailand, Sri Lanka and the Maldives will suffer short-term damage and this might affect their economies in 2005. Estimates of the size of Thailand’s tourist industry range from six to 12 percent of GDP. However recovery is certainly possible if the right systems and assurances are put in place. There is talk that regional governments will establish a tsunami early warning system similar to what exists in the Pacific. Hopefully this materializes quickly.

Spire E-quarterly: What is the outlook for the region in 2005? Which countries will provide the best opportunities to regional marketers?

Leon: The regional outlook in 2005 is fairly positive. Economic growth will be robust, if not as high as in 2004. Most countries in the Asia Pacific region will be growing GDP in the band of four to five percent. Without a doubt, China will remain the biggest market growth story for the region in 2005 and for quite some after, which is why we have devoted an article in this E-quarterly to the China consumer market. China’s fundamentals remain incredibly strong. There is still enormous upside for export-oriented manufacturing, inbound FDI and productivity growth from the application of technology and more efficient allocation of capital by the financial services sector. All this will keep consumer demand very healthy indeed. However companies face stiff competition, falling prices and over-supply in some domestic China markets. Marketers should not ignore exciting growth opportunities in India, Thailand, Malaysia and, for consumer products, Indonesia. All four countries have confident consumers. Australia will remain an attractive high-income market. We believe the downturn in Asia’s third largest economy, Korea, will soon bottom out, moving into recovery around 2006. Japan is something of a question mark, but moderate growth is the likeliest outcome for 2005. In the mid to long-term we believe the outlook for Japan is positive, as its exporters take advantage of China, banking reforms take effect and consumer confidence creeps back.

Spire: Why Japan? Isn’t Japan perpetually tomorrow’s growth’s story and one which never seems to live up to this promise?

Leon: First of all Japan is by far the largest economy in Asia in hard currency terms, with a GDP roughly equivalent to all the other major Asian economies added together. So a small amount of growth in Japan represents enormous growth in absolute terms. Japan’s problems since the collapse of the bubble economy in 1990 have been balance sheet problems – the ever-greening of non-performing loans by the banks and such like. All this obstructed credit, stoked deflation and made consumers save rather than spend out of fear of future tax rises and unemployment. Although the pace has been slow and progress sometimes stalls, we can see that Japan is steadily eliminating these balance sheet problems through banking sector reform and corporate consolidation. At the same time, Post Office reform and other measures hold out the hope of Japanese consumers realizing higher rates of return on their savings. All this is laying the groundwork for a gradual resurgence of consumer confidence in about three to five years time. Japan may not return to the growth rates of the late 1980s but it may attain rates mid-way between those of the European Union and the United States. This
will throw up vast opportunities for marketers, though ones that will be hard to tap given the distribution and cultural barriers associated with the Japanese market.

**Spire E-quarterly: What will be the key changes in doing business that regional marketers should be aware of?**

**Leon:** The most important change, and one that is already well underway, will be the increasing emphasis on services even on the part of manufacturers. Companies are using the internet and increasingly mobile services to deliver loyalty programs to existing customers. The template has been established by airline frequent flyer programs. Apart from cross-sell and up-sell to existing customers, such programs stimulate new sales through referrals. The “Sonystyle” internet club is a good example of such a program. Another is “myphilips.com”, a portal which Philips product owners can use to access internet services, buy products and more. Many digital imaging vendors have created websites where their camera owners can store and share images, print on demand and even communicate with one another. We see this trend going beyond the consumer electronics space to affect markets like automotives, financial services, office automation products and high-involvement FMCG products like skincare and cosmetics, where the trend is not yet as well developed. Connected to this is a trend towards branded vendors wanting to establish more direct relationships with their customers. Of course vendors like Dell define their business model by going direct. But even firms that have traditionally relied on channels are exploring ways to get closer to customers. Look at the growth of branded retail stores by the likes of Hewlett-Packard, Sony and Samsung. In the US, Coca-Cola is directly selling music downloads to its soft drink customers via its website. Photocopier vendors like Fuji-Xerox, Ricoh and Canon who have traditionally relied on dealers for a big chunk of their business are starting to push direct sales tied to services like consultancy, software customization and document management solutions.

**Spire E-quarterly: Won’t this alienate channel partners and undermine channel sales?**

**Leon:** It has the potential to do so if mismanaged. Which is why only the very strongest brands will lead this charge, those which are market share, brand or technology leaders and hence have a bit more bargaining power with channels. At the same time, some vendors are giving their channel partners a role in this equation. Many automotive manufactures are revamping their websites to offer a range of services and functionalities without usurping the role of the dealer as the point of contact with sales leads. Their sites would schedule sales appointments and test drives only at individual dealerships. BMW works with its Australian dealers to help each one develop their own site, though all the sites sport the same BMW brand values and have a similar look and feel.

**Spire E-quarterly: What consumer industries will see the most exciting developments in 2005 and beyond?**

**Leon:** The industries that will see the most explosive and broad-based growth across the region will be consumer electronics, automotives (both cars and motorcycles), non-essential healthcare and travel and tourism. In the consumer electronics space the watch-words will be digital content, connectedness and portability. Digital camera and phone camera sales will continue to surge, as will the business of digital imaging websites, digital photo kiosks and home photo-printers. Consumers are upgrading to flatter and larger televisions that can display high definition feed - this trend is still at an early stage in most countries and has much room to grow, especially as digital TV broadcasting takes off. Terrestrial digital TV has already been launched in Australia, Japan and Korea. China plans to migrate its entire terrestrial TV
broadcasting to digital between 2005 and 2010, to make the best of the 2008 Olympics. Increasingly home devices like the TV, computer and set-top box will converge to create an integrated point of access to the internet and TV – Korea and Japan will lead the way here. Spire’s next E-quarterly will look at this interesting trend. Strong growth in digital content-related devices will continue – portable storage devices like micro-drives and digital video recorders for example. However consumers still want to print hard copies of some types of content - multi-function home printers in Asia will surge towards the high penetration levels seen in the US, benefiting vendors like Hewlett-Packard.

In the automotive space, demand has been lifted along by economic growth, particularly in the case of the passenger car market in China and Thailand and the motorcycle market in some ASEAN countries like Indonesia and Vietnam. In the medium term, the market for consumer-electronics within cars holds tremendous potential. The cars of the future will have internet and television access, GPS capabilities, GIS software, digital audio broadcasting (DAB) equipment and other bells and whistles. Such devices have already made inroads in the more mature economies like Japan and Singapore, with its mobile TV systems being sold to car owners. However we won’t see an explosion in this space in 2005, as it will take a few years for more manufacturers to build these features into cars and for prices to come down.

Non-essential healthcare is another hot area. By this I mean products and services that are sought for preventive, aesthetic or experiential benefits, rather than to cure illnesses. Cosmetic surgery is seeing a boom in countries like Korea and China - this trend will probably take root in more Asian countries. The health supplements field will remain healthy due to growing interest in self-medication and this will benefit manufacturers as well as pharmacy chains. The health supplements industry in China is one of the largest spenders on advertising, for example. There has been a backlash against supplements which make wild claims but this still leaves the field open for more traditional micro-nutrient and herbal-based health supplements.

In travel and tourism, the big development is the arrival of budget travel in Asia. This has opened up a huge new mass market for the industry. Thanks to Air Asia, for example, the Malaysian media reported the case of a janitor who is considered to be a frequent flier, something which would have been unimaginable say two years ago. In China, the budget hotel industry is taking off. However profitability in this game is challenging and the budget airline industry will see consolidation in about two years time as happened in Europe, so it will not be a totally smooth ride.

Spire E-quarterly: What about the business to business space?

Leon: A few themes stand out. As the economy slows down a little in 2005, we expect that most companies will focus more on cost-cutting, especially the larger companies. Shipping industry growth will continue. The whole field of security and disaster back-up will see good growth as well. We see more investment going into supply chain management as manufacturers and their logistics partners work harder to reduce inventory and transport costs. This is a pressing concern given the rising sea freight rates we have seen in 2004. We’ll see the application of new processes (eg better software) and new technologies (eg Radio Frequency Identification Devices to tag items in warehouses and on retail shelves). Companies will also look to outsource so-called non-core functions like certain IT, finance, accounting and human resources functions. Not all of these functions will be outsourced by any means, but only the more labour-intensive aspects, like supplier invoice processing and
payroll. Companies offering such services will grow across the region, though most of the back-end operations will wind up in Asia’s export of services powerhouse, India. Another interesting area of cost-cutting will be in office automation. Companies will seek to reduce the cost of ownership for their printers, copiers, scanners and so on. Office automation vendors like Hewlett-Packard, Fuji-Xerox, Ricoh and Canon are offering services like consulting, document management and monitoring software to enable customers to reduce spending on equipment and track costs.

Unfortunately 2005 will see greater concern over the dangers of terrorism, owing to the rise in terrorist incidents worldwide over the last few years, and in particular the gruesome terrorist attack on a school in Beslan, southern Russia in 2004. This has already led to growing demand for (increasingly digital) surveillance systems, metal detection and bomb detection equipment, access control systems and such like - a trend which will, sadly, continue into 2005. The tsunami tragedy will probably fuel demand in the whole risk management arena. This will drive interest in things like remote data back-up, diesel generators to back-up the electricity supply to key facilities as well as disaster recovery solutions.

**Spire E-quarterly: Will there be any business spaces whose growth will not match the media hype?**

**Leon:** 2.5G and 3G services are being rolled out across more Asian countries but we believe the take-up will be slow, as some of these services, like MMS and mobile streaming video, are probably not attractive enough to consumers to justify the initially high prices. There is massive growth potential in Asia for consumer banking products like credit cards, credit lines and mutual funds if one looks at the low penetration of such products in some Asian countries with a large middle-class like China and India. But in Korea a credit-card bubble burst in 2002, dragging down consumer confidence. What happened in Korea is causing governments and central bankers to be more cautious in liberalizing the regulatory environment for such products. Consumer credit products have tremendous growth potential in the likes of China and India but this will be more of a mid to long-term development.

Also in this edition of the Spire E-quarterly: an article on picking winning consumer market spaces in China. Future issues of the Spire E-quarterly will explore other facets of the marketing challenge in China and the rest of the Asia Pacific.

Spire Research and Consulting joins the many companies and individuals contributing towards the relief of Indian Ocean tsunami victims.