

# Business Pulse

Exploring dual perspectives on the top 10 risks and opportunities in 2013 and beyond

Executive summary



## Executive summary

Two years ago, the general view in international business was that there would be a slump following the 2008-09 financial crisis, and then things would pick up again. Now, more companies – especially in mature economies such as Europe – are accepting that the duration of the downturn is so uncertain that they must fundamentally reposition themselves to survive in a smaller market. This is the main conclusion from the results of our international survey. Such companies are now focused on controlling costs and developing new products to survive in a shrunken, intensely competitive market, while also looking toward rapid-growth markets for new sales and opportunities.

This change in mindset is seen in the difference focus of business activities, especially in Europe where many markets are still performing at low levels amid recession and sovereign debt problems. Such thinking is reflected strongly in our survey results. When asked to nominate the top risks that they face, companies name pricing at the top of the list. This is followed by cost cutting and pressure on profits, as companies adjust to smaller, lower-margin, mature markets.

The flip side to this grim news is renewed interest in emerging-market investment. This is again seen as companies' main source of growth. Indeed, this is now regarded as the second-biggest opportunity, after the innovation necessary to unlock new sales (see table below for a full list of the top 10 risks and opportunities). For example, many consumer products

companies are spending heavily on building plants in China. Elsewhere, there is renewed interest in Russia, a country that suffered badly in the global crisis, but which is now seeing investment streaming into a host of sectors, including pharmaceuticals and food production.

<b>Risk ranking</b>	2013	2015	<b>Opportunity ranking</b>	2013	2015
Pricing pressure	1	1	Innovation in products, services and operations	1	1
Cost cutting and profit pressure	2	2	Emerging market demand growth	2	2
Market risks	3	3	Investing in process, tools and training to achieve greater productivity	3	3
Macroeconomic risk: weaker or more volatile world growth outlook	4	4	New marketing channels	4	4
Managing talent and skill shortages	5	5	Improving execution of strategy across business functions	5	5
Expansion of government's role	6	7	Investing in IT	6	6
Regulation and compliance	7	6	Excellence in investor relations	7	8
Sovereign debt: impacts of fiscal austerity or sovereign debt crises	8	10	Leveraging CSR and public confidence	8	7
Emerging technologies	9	8	Investing in cleantech	9	9
Political shocks	10	9	Global optimization and relocation of key functions	10	10

# The risk and opportunity radar

The risk and opportunity radar allows us to present a snapshot of the current top 10 risks and opportunities for global businesses.

At the center of the radar are the risks and opportunities that our survey respondents felt were having the biggest impact on major organizations worldwide. Arrows indicate the extent to which the ranking is expected to increase, decrease or remain the same between 2013 and 2015.

The radar is divided into four sections, corresponding to Ernst & Young's *Growing Beyond* model.

The sections are:

- ▶ **Customer reach:** maximizing potential market opportunity for products and services
- ▶ **Operational agility:** improving organizations' ability to deliver effectively in a quickly changing market
- ▶ **Cost competitiveness:** sustaining companies' economic viability
- ▶ **Stakeholder confidence:** firms to build stronger relationships with stakeholders

## The top 10 risks



## The top 10 opportunities



2013 ranking and expected 2015 ranking



Up in 2015



Same in 2015



Down in 2015



# Cost competitiveness

Facing up to the downturn

## Self-assessment questions

1. How do you ensure you focus on the right strategic relationships (e.g., encourage innovation to design the right products from the best materials and secure critical supply)?
2. How do you sustain margins and operating results in the face of increased global competition?
3. What factors should you consider when expanding globally?
4. Which supply markets and categories should you target? Are you sourcing from the right locations to be cost competitive?
5. How do you preserve value while minimizing costs?
6. How do you balance pricing pressure with excellent customer service?
7. How frequently do you track metrics that can predict fundamental marketplace shifts?
8. How do you determine which objectives and opportunities to pursue while allowing for the organization's appetite for risk?
9. How efficient is your information security controls framework and what could be additional ways to cut costs?
10. Keeping cost-saving in mind, how can you focus successfully on the information security risks that matter?

Our research suggests that companies are increasingly accepting of the fact that the length of the economic downturn is fundamentally uncertain. Businesses are putting significant efforts into cutting both costs and prices in order to compete in shrunken mature markets and highly competitive rapid-growth markets.

Our survey results show the shift in thinking. Pricing pressure has become the biggest risk noted by companies this year: up from 4th place in 2011 and a lowly 15th in 2010 (when companies were still expecting markets to bounce back). Mature markets nearing saturation have led to fierce price competition, with little or no organic growth expected. Such problems

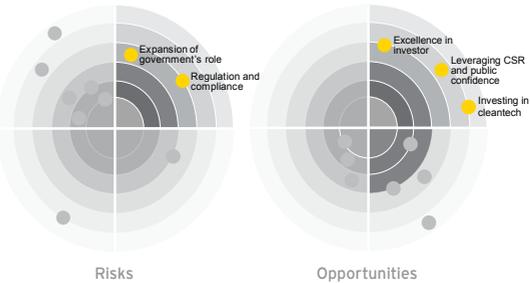
are exacerbated by the strength of both low-cost competition and online rivals, which have made brand-driven price premiums hard to sustain.

Alongside this, high wages and input costs, as well as significant new regulatory burdens on various sectors, mean that the pressure on pricing will impact profit unless companies take firm action. Unsurprisingly, therefore, cost cutting and the related pressure on profits is cited by respondents as the second-biggest risk they face. Five years into the global crisis, most of the simple cuts to costs have already been made. That is now pushing businesses to make tough decisions on how to cut costs without damaging product and service standards. But

for those who get this right, the payoff can be dramatic: Ernst & Young estimates that cutting costs by just 1% can yield the same bottom-line results as a 10% boost in sales. Firms are using technology to improve productivity, introducing more flexible working practices and re-engineering supply chains to encourage growth in emerging markets.

However, businesses also accept that the increasing reliance on emerging markets for growth brings new risks. As a result, market risks

have risen to third place in our survey, not least with oil prices remaining high and continued volatility in currency markets. All of this poses distinct risks to the bottom line. For the first time, firms list sovereign debt, the impact of austerity and political shocks as among the top 10 risks they face. These fears are especially acute within mature markets. This is most notable within the Eurozone, where the threat of a deep recession remains and some countries face the definite possibility of a debt default.



## Stakeholder confidence

### Broader considerations emerging

## Self-assessment questions

1. How do you develop insights on the possible impacts of shifts in government regulations on business strategy and performance?
2. How do you evaluate the way in which new regulations or laws can create new markets for specialized products or services?
3. What capability do you have in scenario analysis and taking pre-emptive action to offset any impact of changes in government role?
4. With whom do you collaborate to track changing regulations and seek compliance assistance?
5. How do you reduce your exposure to share-price volatility?
6. How do you identify cleantech investment opportunities that are supported by proprietary technologies and multiple partnerships to minimize risk?
7. In what ways can you better communicate your compliance program as part of your go-to-market strategy and so build customer confidence?
8. How can you benefit from a regulatory intelligence and reporting system that protects you from unnecessary fines and other legal impacts?
9. What kinds of discussions on IT and information security take place in the board room and in relation to large transformation projects?
10. How effective and efficient is your compliance monitoring system?

The ongoing global economic crisis has had a big impact on the size of mature markets, but it has also raised questions over the role of companies in society and led to increasingly tough regulation as governments seek to avoid another crisis.

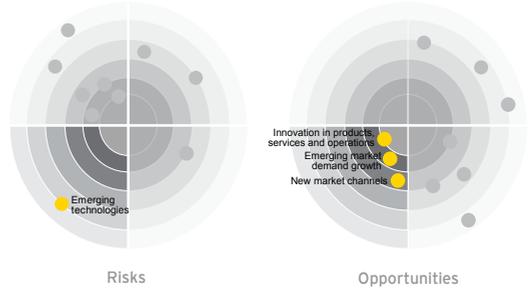
Post-crisis, companies will find themselves needing to listen and engage with a wider field of stakeholders than their shareholders alone. Our research shows that companies are increasingly aware of issues such as the environment and corporate social responsibility (CSR), as well as more immediate problems such as tightening regulation.

The increasing role played by government in business is now cited as the sixth-biggest risk faced by companies (up from seventh place in 2011, the first time it registered as a top 10 risk). This is driven in part by tightening regulation, most obviously in the financial sector. But it is also because governments, especially in rapid-growth markets, are playing an increasingly active role in a host of sectors, from pharmaceuticals through to power and utilities.

This can reshape the nature of competition. In China, for example, some multinationals are required to work in partnership with local firms, as the country seeks to support its local industrial base. As a result, government policy,

and maintaining good relations with government, is increasingly important for businesses. This is especially true within mature markets, although many rules increasingly affect global operations too. For example, multinationals face mounting pressure to comply with anti-bribery measures, which in turn can make it more difficult to operate in some rapid-growth markets. Regulation and compliance is listed as the seventh-biggest risk facing companies, down from the top slot in 2011. But this is forecast to remain a concern in the future: executives polled expect this risk to rise to sixth place in 2015.

Companies' broader sense of accountability in the post-crisis world is also reflected in the opportunities they spot. Leveraging CSR and public confidence, a new entry to the list, is ranked eighth overall and expected to rise to seventh in the coming years. This is especially true in rapid-growth markets, where such activities can be an integral part of receiving a license to operate. Beyond this, excellence in investor relations is also seen as a top 10 opportunity. This highlights the importance of a broad funding base in today's relatively tight-credit world. Certainly, institutional investors now demand greater transparency in areas such as environmental and social issues, which can impact a long-term investment's viability.



# Customer reach

In search of the new

## Self-assessment questions

1. How do you effectively evaluate rapid-growth markets to ensure that they fit with your competencies and strategic objectives?
2. How is innovation embedded in your business model?
3. How can you work more effectively with channel partners to ensure the value proposition is easy for the market to understand?
4. How are you tracking the risk and adoption rates of emerging technologies? Which ones are likely to have limited value or high deployment risk?
5. How do you assess changes in factors such as adoption of IT, workforce demographics and the rise of social media in order to identify which emerging technologies are having the most impact?
6. What financial analysis do you conduct to ascertain the true costs and benefits of sourcing from rapid-growth markets?
7. How do you connect with your customers, suppliers and employees to drive innovation in your business?
8. How extensively do you use technology to accelerate and drive the adoption of new ideas and programs?
9. How do you consider technology and information security while launching a new product or entering a new geographical market?
10. How secure are your new go-to-market strategies (e.g., websites, mobile apps, social media), including digital payment systems, to ensure customer confidence and maintain brand reputation?

With little prospect of organic growth in mature markets, companies are searching for new places to expand. There are opportunities for businesses in new markets in new countries, as well as new niches in established markets.

Innovation offers the most opportunity, both in terms of new products or services and within operations. This is especially important for finding unexploited gaps in existing markets, but it is also becoming an increasingly fundamental part of success within major rapid-growth

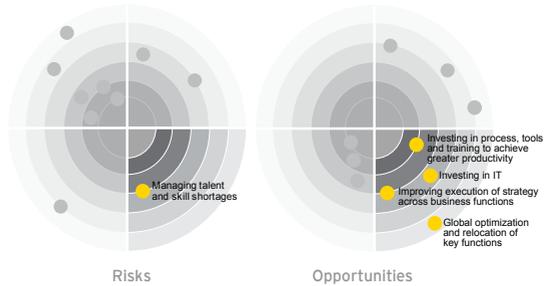
markets. In evidence of this, spending on research and development is growing four times as rapidly in rapid-growth markets as mature markets.

This is directly linked to the way that firms are tapping the second-biggest overall opportunity: emerging market demand growth. The IMF expects major rapid-growth markets to grow by 5%-6% in 2013-14, or about four points faster than mature countries.

Companies from a range of sectors now accept that the bulk of their growth will come from such markets and are readjusting their businesses accordingly.

In a similar vein, companies are getting excited by the emergence of new marketing channels, such as social media, which is ranked as the fourth-greatest opportunity for business (a sharp increase from eighth overall in 2011). This

was especially true of companies operating in rapid-growth markets. Cloud computing and data insights also offer tremendous marketing potential. But inevitably, there are risks too. Emerging technologies are still narrowly considered a top 10 risk, although this is down from fifth overall in 2011. But the disruptive capabilities of ongoing technological development remain a worry for many firms.



## Operational agility

### Tuning for greater performance

1. How do you minimize variability in your supply chain while introducing more cost-effective processes and solutions?
2. How do you plan and prepare for the increased volatility of the market you operate in?
3. Have you effectively consolidated and standardized global activities – including using a shared service center?
4. How do you ensure you have the right people with the right skills in the right roles?
5. How do you ensure you have the right solutions, and integrated systems and processes in place to increase collaboration?

## Self-assessment questions

6. What risk-assessment measures for innovations do you undertake?
7. How do you regularly conduct market technology scans to identify new tools to protect critical systems and data?
8. What does analysis of your business processes reveal about optimal performance (i.e., analyses of marketing spend and supplier spend, etc.)?
9. How well do your information security and compliance functions perform and efficiently integrate with other risk functions?
10. How do you continuously improve service levels and meet ever-greater business demands while optimizing IT service costs?

Operational agility remains a crucial part of surviving and flourishing in a volatile world economy. In particular, many companies see room for improvement in bolstering productivity. In mature markets, where companies face the most acute pressures over pricing and profitability, executives cite this as their second-biggest opportunity, ahead of growth in new markets. Likewise, it is also a high priority (ranked fourth overall) in rapid-growth markets.

So too is the need to make sure that decisions reached at the top are actually implemented on the ground. Improving the execution of strategy fell to fifth place in this year's rankings, down from the top slot in 2011. Mature market respondents still consider this more important than their peers in rapid-growth markets (fifth and seventh place respectively).

IT investment, a crucial element of strategy implementation and overall performance, is seen as the sixth-greatest opportunity. It is among the top five in mature markets, although it has eased off from third overall in 2011. But other risks have also eased. Although a perennial challenge for those seeking to expand and innovate, the risk of managing talent and skills shortages fell to fifth overall, down from third in 2011.

The easing of pressure on skills comes in parallel with a new opportunity making the top 10 list for the first time: global optimization and the relocation of key functions. For multinational organizations trying to balance the desire for cost competitiveness in key markets, as well as growth in new markets, rethinking the cost and location of operations from a global perspective can deliver a range of opportunities.



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