

# Asia – A View of the Future

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The Economist published a special report titled: The world turned upside down in the April 17th 2010 edition. One of the things that I recommend investors do to improve their knowledge is read this kind of in-depth article in magazines and newspapers. Even more important is that these articles can give us valuable perspective on the world and insights into what is unfolding around us, but which most people do not become aware of until after it has happened. This is far more important than reading reports of what the markets did yesterday, something on which we have the data and should be able to form our own view. If we find that we need this kind of explanation, it could be because we are still learning the independent thinking skills that are essential in the journey from beginner to seasoned investor.

The special report is sub-titled: A special report on innovation in emerging markets. The author Adrian Wooldridge suggests that developing economies, which we have long regarded as based simply on low cost labour, are now beginning to challenge the developed world economies in the field of business innovation. I found this of great interest and it reminded me of the excellent special report on the developing world bubble in real estate prices and borrowing written in May 2003 and the level of risk taking in banks including CDOs and CDSs in May 2007. These gave ample time to know what was coming, although maybe not how soon. Having read these reports, there was no excuse to be caught unawares in late 2007 and 2008 as the global financial crisis played out.

The discussion about Asian innovation trends opens with a reminder of how the Japanese car manufacturers changed the world car industry by inventing and exploiting lean manufacturing, also sometimes referred to as just-in-time manufacturing. It is suggested that a similar revolution is beginning in the developing economies. Moreover, it is not just in one industry or one kind of commercial activity, it is right across all industries and all business functions.

The innovation that is blossoming is developing new products and services that are a fraction of the cost of the same things produced or provided in the western economies. This is being driven by two main influences:

- Ambition to become multi-national players
- Fear of other developing countries which also have cheap labour and might supplant them in simple products and services

The result is that Asian countries are moving to higher value and higher technology products and services. They are re-engineering everything from products and services through to the underlying business processes and models. Their new products and service offerings are often far cheaper than the equivalents in western economies, albeit often simplified to the basic functions consumers want rather than the 'does everything' model we are accustomed to in the western economies.

The statistics are likely to jolt many of us:

- Number of multinationals based in the developing world: 21,500
- Number from BRIC countries in the FT500 list 2006: 15, 2008: 62
- Number of graduates in engineering & science each year China: 75,000, India: 60,000

Although western multi-nationals are recognising and moving into these developing markets, they find that these markets are difficult in many ways. Some of the challenges are:

- Weaker or non-existent distribution systems
- Highly variable income streams
- Shocking pollution
- Difficult governments – frustration, meddling and lack of basic services and rule of law
- Pirating of intellectual property
- Widespread poverty

Some western multinationals have not even gone into these markets or have largely retreated from them in the face of these difficulties. Nevertheless, these emerging economies present some important and huge opportunities if they can be exploited effectively:

- Huge population growing quickly
- Hundreds of millions of Chinese and Indians will become much richer in the next few decades
- Fast growing economies
- Few expensive “legacy” systems – opportunity to start at the ground floor without writing off past investments
- Low cost and plentiful graduates – China 5 million and India 3 million annually

Those who are succeeding have to be creative. Some things they are doing which turns western approaches on their head:

- Aim for volume rather than margin because most consumers are plentiful but poor
- Continual improvement of products because piracy is rife i.e. instead of the western reliance on intellectual property rights, their products are updated and improved frequently and faster than pirates can move to exploit them

In much the same as was done in Japan in the 1980s, these entrepreneurs are converting difficulties into opportunities in creative ways.

The old idea is that the west creates dramatically new technological products which are initially sold at high margin to the elites and then are repriced as they drift down to the mass market, including exporting them to developing economies. However, what is happening in developing countries is that innovation takes the form of continual small improvements in goods and services plus the business processes that create and distribute them. These are aimed at the huge low income base of the populations in these economies.

This is a region that, to echo Churchill’s phrase, *sees opportunities in every difficulty rather than difficulties in every opportunity*.

This is a summary of the two and a half page introduction to this special report. The remaining eleven and a half pages flesh it out in a series of articles that are headed:

- First break all the rules – the charms of frugal innovation
- Easier said than done – emerging market consumers are hard to reach

- Grow, grow, grow – what makes emerging market companies run
- Here be dragons – the emerging world is teeming with new business models
- New masters of management – pervasive innovation adds up to a new management paradigm
- The power to disrupt - business innovations from emerging markets will change the rich world too

I found this special report to be fascinating and have read through it several times. There is not space here, nor do I have time, to take you through it all. I found as I read the report that I had the uncanny feeling that I was reading about our future as well as that of the developing world. Some dislike globalisation while many of us embrace its opportunities, but the future cannot be avoided, whichever way we regard it.

If you would like to read the full report I think there is a way to do so. Go to <http://www.economist.com/members/members.cfm?act=registration> and register. Registering will allow you the read three articles every week. Registration is free, and there's no obligation to subscribe.

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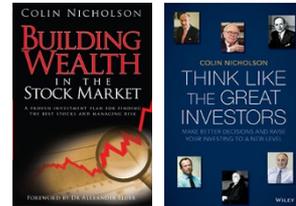
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