Business Across Borders

Executive Summary

Pilfering on the docks of New York City was once so rife that, so one story goes, an Italian shoemaker shipped his goods in two separate consignments – left and right shoes – to prevent them from being stolen. Today, companies doing business across borders might yearn for such a simple problem. On top of a global economic slowdown, they must now contend with everything from regulatory uncertainty and commercial disputes to intellectual property theft.

In *Business Across Borders*, The Economist Intelligence Unit – on behalf of global law firm Reed Smith – investigates companies' international strategy, the regulatory obstacles to cross-border business and the risk of international commercial disputes. As part of the research, the EIU conducted a global survey of 451 executives and interviewed a number of experts and senior business leaders.

The key findings of this research are:

International strategy

Despite the crisis, western Europe remains a top investment destination. Survey respondents identify western Europe as their preferred market for cross-border activities over the next two years, with 32% of the vote. China followed in second place. North America and western Europe are also the markets of choice for European and North American respondents.

Relatively safer risk profiles help Europe and North America attract investment, according to Juan Pablo San Agustin, executive vice-president of strategic planning and new business development at Cemex, a building materials company. "When you look at the potential returns in any country, they might be very high theoretically but when you adjust them for the risk, you might prefer to invest in Europe and the US, as we have decided to many times," he says. For others, cultural affinity also plays a part. "We decided to buy a company in the UK chiefly because there is no language barrier," says Michael Fertik, founder of Reputation.com, a Silicon Valley-born online reputation management company. Mr Fertik also notes that, for internet companies, high e-commerce presence and penetration are just as important.

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“Big corporates and institutional investors are diversifying their asset allocation and putting more emphasis on emerging economies”

Luis Alvarez de las Asturias, head of global client and cross-border business at BBVA

Brazil set to beat China on investments from manufacturers. The survey results revealed that the South American giant will become more popular over the next two years. This shift in popularity is particularly marked among respondents from the manufacturing sector. While over the last two years 49% of business in this sector said China was an investment priority, only 31% say this will be the case over the next two years. This decline comes as 33% of respondents indicate that Brazil will figure prominently in their cross-border activities. “Wages are probably the main factor behind slowing interest in China as a manufacturing base, while Brazil promises both a relatively low-cost and skilled workforce, as well as a large and growing domestic market for manufacturers,” says Alasdair Ross, the global product director at the EIU.

On the other hand, survey respondents from financial services say that China will become an investment priority over the next two years. “Big corporates and institutional investors are diversifying their asset allocation and putting more emphasis on emerging economies,” says Luis Alvarez de las Asturias, head of global client and cross-border business at BBVA, a Spanish bank. BBVA has a 15% stake in China CITIC Bank, as well as a strategic partnership that allows it to access the Chinese market through two joint ventures, in auto-finance and private banking. It is also collaborating with China CITIC Bank on the corporate and investment side.

Increased due diligence and greater experience are making companies more comfortable with cross-border business. Over one-half of respondents (54%) say that international transactions are likely to become a little or much easier over the next two years. Of these, 41% cite familiarity as the reason it has become easier, while 31% say they have increased due diligence efforts to ensure a smoother market entrance. Out of the respondents that think international transactions are going to become more difficult, 53% cite current global economic conditions as the most important factor.

49%

of businesses in the manufacturing sector said China was an investment priority over the last two years. 31% say this will be the case over the next two years.

Bucking the trend, over one-half (55%) of energy sector respondents think that international transactions are likely to be become more difficult. The energy and resources sector is looking more critically at cross-border projects given recent high-profile incidences of resource nationalism and political uncertainty in resource-rich regions.

Regulatory challenges

Regulation is more friend than foe, say most business executives. For 68% of respondents, regulation is a key factor in deciding whether or not to invest in a new market. “If there is regulatory visibility, you can adjust and anticipate and make investment decisions,” says Mr Agustin. In fact, 62% of respondents say that a lack of certainty and transparency on where regulation is heading is more damaging than the nature of regulatory reform.

Nearly two-thirds of respondents (65%) in the EIU survey also report that regulatory developments at home have made it easier for their company to expand into new markets. Nearly three-fifths (58%) say the same of international regulation, and three-fifths say new regulation has spurred their company to invest in and encourage innovation.

Respondents from the financial services sector buck the trend, however. Over one-half (54%) of such companies say that domestic regulatory developments hinder their international expansion plan. Nearly one-half (49%) also report that international and national regulatory reform makes their company less competitive, and creates a more difficult market in which to innovate. Such responses from financial services executives could be put down to the increased regulatory requirements they have had to endure since the global financial crisis. “Regulators are trying to control the behaviour of the financial sector more than any other,” says Mr de las Asturias.

Three-quarters of financial services executives in the EIU survey say company investments to keep abreast of regulation have been effective.

Changes to data protection requirements could be troublesome for media and technology executives. Over two-fifths (44%) of media and technology respondents in the survey say they are not prepared enough or at all to cope with changes to data protection requirements. The biggest changes are set to come about in Europe with the General Data Protection Regulation (GDPR), which is due to be implemented in 2014. The GDPR will put in place a single law across the EU, detailing citizens' rights over their personal data.

Mr Fertik isn't worried however. According to Reputation.com's CEO, Internet companies are one step ahead already. For example, Mr Fertik's company is developing a model where the disclosure of personal data to third parties is carried out on the consumer's terms. "The individual is empowered in the data eco-system. Access is only granted with explicit permission from the individual and in exchange for a fair and desirable incentive," says Mr Fertik.

Financial services firms are better equipped to deal with regulatory reform than media and technology companies. Three-quarters of financial services executives in the EIU survey say company investments to keep abreast of regulation have been effective. In the media and technology sector, only 45% of executives say the same about their company investments. This could be a symptom of the fact that the sector is simply not as heavily regulated as financial services. The rapid advancement and take-up of new products and services has meant that, so far, regulators have had to play catch-up with the media and technology industry. If and when the tables turn, executives at these companies will have to improve their systems and processes to cope with regulatory reform.

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of companies have been embroiled in an international commercial dispute over the last two years.

International disputes

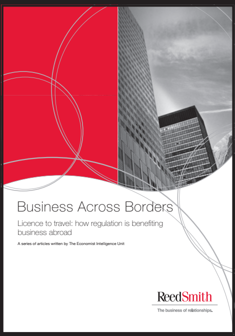
One in four companies has been embroiled in an international commercial dispute over the last two years. The proportion rises to 29% among Europeans and 30% among respondents from the shipping and transport sector. A breach of contract was the most likely cause of these disputes across both developed and emerging markets, followed by a default on payment.

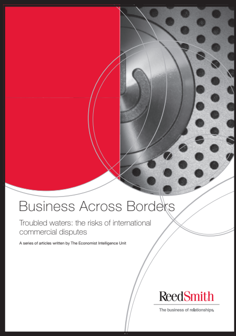
Intellectual property (IP) theft is set to become the biggest cause of such disputes in BRIC markets (Brazil, Russia, India and China) over the next two years. "As a society we are still figuring out what the extent of patents in technology should be and can be. And what the enforcement action should be and can be," says Mr Fertik. There will be greater conflict and agitation concerning IP in the US – and consequently overseas – as these questions are answered, adds Mr Fertik.

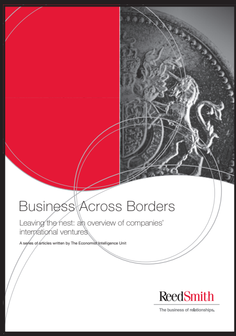
Executives from the media and technology, and the healthcare and life science sectors appear to be most concerned about the future threat to their IP. "Every time we look at the opportunities from a business development point of view, IP rights are always high on the agenda," says Jacob Tolstrup, the vice-president for corporate business development and strategy at Lundbeck, a Danish life sciences company that has products registered in more than 100 countries.

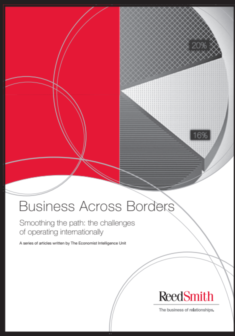
Conclusion

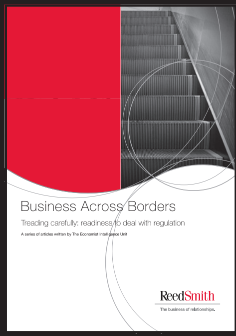
Despite the difficulties that have faced the global economy over the past five years, the research conducted by the EIU on behalf of Reed Smith finds that executives will be pursuing international ambitions in all four corners of the world. Yes, they will meet a number of obstacles: from the risk of becoming entangled in a commercial dispute to the possibility of a significant slowdown in emerging markets. But the great majority are confident that international transactions will become easier. More stringent due diligence, favourable regulatory developments and friendlier attitudes to foreign investors are all helping to smooth the path to international markets.











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About the research

In January 2013 The Economist Intelligence Unit conducted a global survey of 451 executives on behalf of Reed Smith. All respondents represented companies that conduct business internationally. Over one-half of respondents (56%) are C-level executives and 53% are from companies with annual revenues in excess of US$500m. Just under one-third of respondents are from Asia-Pacific (30%) and from North America (30%), and nearly one-third (32%) are from Europe. The remainder of respondents are from the rest of the world, including the Middle East, Africa and Latin America. Respondents represent a range of industries, including: 15% from financial services, 14% from energy and natural resources, 14% from media and technology, 13% from shipping and transport, and 13% from healthcare and life sciences.

In parallel to the survey, The Economist Intelligence Unit also carried out several interviews with senior business leaders and experts.

We would like to thank all survey respondents and interviewees for their time and insight.

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