When economies slow down: lessons from Asia?

About the Author

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Mr. Stuart will be leading the Advanced Channels Workshop (11/12 March) and a new program Channel Management: the business dynamic (13/14 March) in Singapore. For more information or to comment on the article, e-mail info@channelcorp.com.

The purpose of article series from ChannelCorp is twofold. Firstly, the series is intended to assist vendor channel managers to make strategic decisions on courses of action when they are faced with economies that slow down. What happens to end users in slow down situations and what action vendors, distributors and resellers should take is well understood by ChannelCorp as a result of our extensive channel knowledge accumulated over fifteen years working in international markets (Asia/Australia/Europe/North America/South America/Central America). We have seen inflation, devaluation, deflation and stagnation. The second purpose of the balance of this section is to provide readers with a roadmap of what impact the slow down of a "developing" or "less developed" economy has on the distribution channels for hardware, software and telecommunications products and services. Asia is not the first melt-down (remember Mexico and South America) and it won't be the last (Russia, Japan, Latin America, South America).

In light of recent world financial events and the specific problems in many Asian countries, Russia and parts of Latin/South America, it is critical that vendors, distributors and resellers analyze and act upon the potential impact of widespread deflation and related economic disruption on their businesses. ChannelCorp believes that the current world financial crisis will continue to dog the developed and developing world until at least 2003.

The shape of the future of the channels business is not much in doubt. We know that a well researched, designed, executed and managed indirect channel strategy is critical to profitability and growth in today's computer hardware, software and telecommunications industries. We know that vendors in the marketplace will be rapidly segmented into the channel "haves" and the channel "have nots". We know that vendors whose people have formal training in channels such as ChannelCorp's *Advanced Channels Workshop* or *Channel Management: the business dynamic* do better than vendors whose people are forced to "make it up as they go".

Even without deflation, we know that average selling prices and gross margins will continue to fall. As a result, Alternate or Indirect channels will become increasingly critical to growth and profitability. Direct sales forces of vendors will not be able to deliver the sales revenue at levels of cost low enough to be profitable. The performance gulf between vendors with developed channels and vendors with under developed channels will undoubtedly widen as we enter 2002. Vendors with developed channels, fuelled by their commitment to increasing the channel related knowledge of their managers, will leave behind the organizations that pay only lip service to the continuous development of the channel related knowledge of their people. On these issues there is no discussion.

What is open for discussion is how well vendors and their channel partners will cope with the deteriorating economic situations and the need for new channel organizations, new channel performance metrics, new channel strategies, new business propositions and new channel tactics. More importantly how will you and your people hold up in the face of demands for new channel knowledge, new channel capabilities and eventually new channel decisions?

In order to sustain the value of your company, senior managers in the "channels business" need to be constantly designing, redesigning and re-engineering their channel strategies, architectures, organizations and programs. At the same time revenue per person needs to rise 15 to 20% per year, every year, Selling, General and Administration (SG&A) costs need to be contained (or reduced). Cost Per Order Dollar (CPOD) needs to fall 10 to 15% per year: The result must be an increase in profit per person. These metrics can be attained in a deflationary environment, but planning and execution must be flawless.

Asian Executives Brace for Worse Times Ahead

JAKARTA — About four in five top business executives in Asia expect the region's financial crisis to worsen before tapering off in two to three years, according to a survey released 24 February 1998.

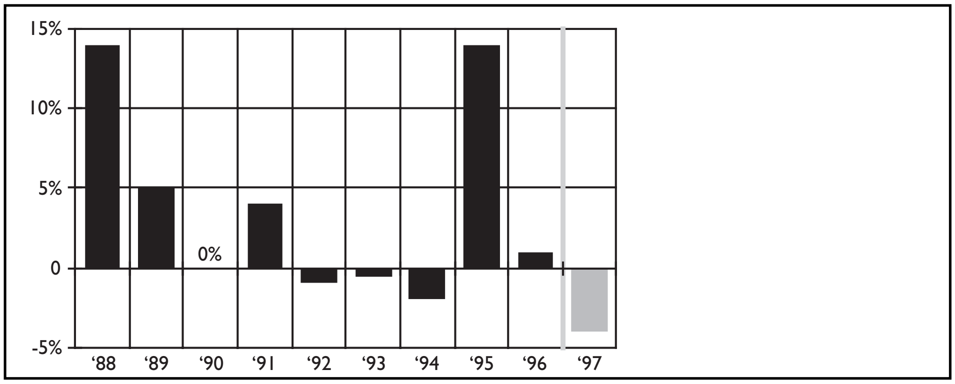
Sixty per cent of Asia's chief executives blamed Asia's financial crisis on governments in the region and their policies, the survey said. The poll was taken during a three-day Presidents Forum, sponsored by *Business Week* magazine, of 140 executives on the Indonesian island of Bali from Feb. 20 to 22.

About 84 per cent of executives polled expect the market crisis to worsen. Nearly 80 per cent expect the crisis to taper off in two to three years, the survey said.

February 1998/Reuters

The events in the Asian economies were not short term in nature. The capacity build-up and borrowing in the region had been unrelenting and had continued for years. Because the problem took almost a decade to create, it will likely take five to seven years to rectify. The length of the deflationary period and the depth of the slump are highly related to how far prices for products eventually fall. Export prices had fallen sharply since the first quarter of 1996. Figure 1 below shows long term movements in Asian export prices. 1997 saw export prices decline from 4–6%. 1998 was worse as various countries' devalued currencies fuelled price-driven export competition.

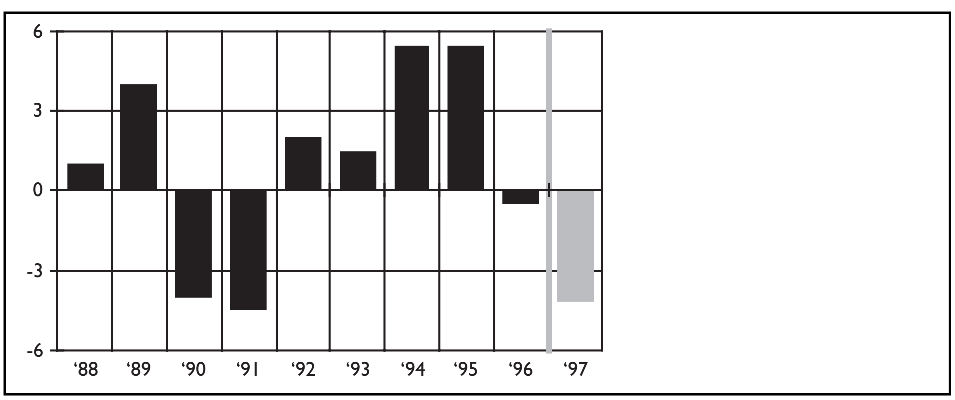
Figure 1 – Downward movement in Asian export prices, 1988– 1997



Source: *The China Analyst*, Bank Credit Analyst Research Group

Deflation is a condition when too few dollars are chasing too many goods. As a result of a merciless capacity buildup, Asia had considerably more production capacity than the combined domestic/export markets required. This condition existed in many sectors of the economy and eventually resulted in producers receiving substantially less for their product than the cost of production and maintained production capacity. In many countries, most notably China, Indonesia and Korea, high investments into industries that were already at excess capacity continued. Figure 2 below provides data on the supply/demand imbalances in Asia's economy. The zero point approximates balanced supply and demand. Negative figures indicate a glut or a situation where supply exceeded demand.

Figure 2 – Supply exceeds demand: Asia's industrial efficiency, 1988– 1997



Source: *The China Analyst*, Bank Credit Analyst Research Group

The supply/demand imbalance in 1998 and 1999 were greater than any year in the past decade (Figure 2).

Much of the disruption in Asian economies can be attributed to 1997 collapses in currency against the U.S. dollar. Figure 3 outlines the relative changes in the value of Asian currencies for the period 1 January 1996 to 1 November 1997.

Figure 3 – Asian currencies fall against the U.S. dollar

Currency	Value against the U.S. $ (1 Jan 1996 = $1.00)	1 Jan 1997	1 Nov 1997
Malaysian riaggit	1.00	±1.00	±.72
Philippine peso	1.00	±1.00	±.74
Singapore dollar	1.00	±1.02	±.89
South Korean won	1.00	±.92	±.74
Taiwan dollar	1.00	±1.00	±.82
Thai baht	1.00	±.97	±.62
Hong Kong dollar	1.00	±1.00	±1.00
Chinese yuan	1.00	±1.00	±1.00
Indonesian rupiah	1.00	±.95	±.25

Source: *Datastream*/ICV

As can be seen from Figure 3, the currencies of some countries had fallen further than others. Those countries whose currencies had experienced the most disruption would face the greatest challenges maintaining growth and momentum. For instance, Indonesia, whose currency was battered worse than any others in the region, would have tremendous difficulty dealing with the joint demons of economic-driven domestic political strife and inflation. Growth forecasts – projections of Gross Domestic Product (GDP) were revised downwards for many countries. Figure 4 provides a quantitative perspective on forecast growth. Indonesia, particularly hard hit by devaluation, was a prime candidate for a bad case of hyperinflation where price increases can rise in excess of 40–50% per year.

Figure 4 – Growth forecasted to fall in Asia

Country	1996(A)[1] %	1997(F)[1] %	1998(F)[2] %	1998(E)[3] %
China	9.7	8.8	8.0	5.0–6.0
Singapore	7.0	7.0	5.0	n/a
Malaysia	8.4	7.0	3.5	5.0
Indonesia	7.8	6.6	3.0	3.0
South Korea	7.1	5.7	3.0	negative
Philippines	4.8	4.7	2.9	4.0
Thailand	6.7	.3	-2.0	negative
Japan	3.6	.8	.7	.6
U.S.	2.4	3.8	2.5	2.0 – 3.0

Sources: [1] MF (1996 data)
[2] Salomon Smith Barney Forecasts
[3] Goldman, Sachs & Co. Estimates

Although 1998 forecasts and estimates for Asian growth were still in excess of projections for the U.S. market, the economies of the developing countries had to grow by in excess of 5% in order to prevent large segments of the population from becoming impoverished through large scale unemployment. In some Asian countries, an "addiction" to growth had developed as big debts (in U.S. $) had been taken on to build new infrastructure and create employment for literally millions of young people entering the workforces. In short, what 3% growth in the U.S. accomplishes required 7–9% growth in Asia. Mass unemployment in 1998 and 1999 was the norm in many economies.

Then what were the facts?

export prices were falling

supply exceeded demand

currencies were falling against the U.S. $

economic growth was forecast/estimated to fall dramatically

Those organizations whose people had formal channels training did better than those that did not. What happened in Asia could and has happened elsewhere in the world.

The next article outlines what happens in various economies as economic disruption continues.

ChannelCorp Education Programs in Singapore – March 2002

We are pleased to announce that two ChannelCorp workshops will be delivered in Singapore March 11–14, 2002. This is ChannelCorp's sixth year of delivering world-class channel education to channel executives in South East Asia.

In 2002 we are offering an important new program. Channel Management: the business dynamic (13/14 March) is unique in the world. It will dramatically increase the business skills and improve performance of quota-carrying personnel such as channel managers, account managers and business development managers. This program will provide two years worth of knowledge and experience in two days.

The ChannelCorp Advanced Channels Workshop (11/12 March) is well known to channel executives in South East Asia. The 2002 Advanced Channels Workshop has been updated to reflect new eChannels findings and the new role of influence channels in the IT industry. This program has SOLD OUT for six straight years.

For more information on either program, go to http://www.channelcorp.com/workshops_01.htm. We can also provide detailed outlines and group pricing details. Simply send a return e-mail requesting data. We hope to see you and your people in Singapore in March.

