

# focus on...

Grant Thornton 

## ...the global market

This supplement is part of a series of publications focusing on the key findings of the Grant Thornton International Business Owners Survey (IBOS) 2006. This edition is dedicated to the global market and examines views on:

- the proportion of businesses **exporting** in each of the 30 countries in the survey
- the contrasting performance across the **global regions**
- recent economic developments and key survey results in three economies – **Mainland China, India** and the **US** – that are driving global trade growth.

### Key findings

Just over one third of the businesses surveyed are exporters.

The largest increases in the proportion of exporting businesses were in Hong Kong and the Philippines.

Exchange rate movements largely explain marked falls in the proportion of exporting businesses in four countries, led by Australia and Poland.

### International trade and medium-sized businesses

International trade is a key driving force in the international economy. Trade both stimulates and responds to global economic growth, but trade growth tends to be much faster. In the past 20 years, world output (GDP) growth has averaged 3.5% a year, while trade volumes have risen by an impressive 6.6% a year. This divergence partly reflects important factors that have boosted international trade over the period – the lowering of trade barriers through the efforts of the World Trade Organisation; the development of regional trading blocs such as the European Union and NAFTA; increasing globalisation; and the rapid expansion of trade between developing countries.

Medium-sized enterprises play a significant role in the international trading scene. According to our survey, over one third of them export, and 37% report that over a quarter of their turnover comes from exports.

Trade in goods accounts for around 80% of global trade, leaving one fifth for services such as tourism, finance, consultancy, legal services and transport. But in an increasingly integrated world market, with a marked shift in economic activity towards the service sector, international trade in services is growing rapidly. Our survey suggests that medium-sized enterprises are contributing to the strong expansion of international trade in this area. The results show that in the EU for example, over 40% of businesses export, and an analysis of survey respondents by industry sector shows that medium-sized businesses in the EU are predominantly in the service sector.

Prominent among trading nations are Mainland China and the US. Together they account for 16% of world exports. India accounts for only a small proportion of world trade but is growing rapidly since the liberalisation measures that began in the 1990s. Recent trends in these important trading economies are highlighted in this supplement.

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### The proportion of exporting businesses is very stable...

International trade has expanded at a rapid pace, averaging 7% per annum in volume terms, in recent years. Yet at the global level the proportion of medium-sized businesses that export is 36%, the same as in 2003. A number of factors could explain this mis-match. Firstly, the proportion of businesses that export in the US, which has a large weighting in the global calculation, showed no change over the period as businesses have found ample opportunities in the large and strongly expanding domestic market. Secondly, much of the growth in world trade is accounted for by Mainland China, which is included in the survey for the first time this year. And thirdly trade in commodities, not an area in which medium-sized businesses are strongly represented, has made a significant contribution to world trade growth in line with robust output expansion.

**Figure 1: Proportion of businesses exporting (change from 2005) \***

Hong Kong	16
Philippines	10
New Zealand	-10
Spain	-12
Canada	-13
Poland	-16
Australia	-18

\* change in percentage between those responding "yes" in 2005 and those responding "yes" in 2006

### ...but some countries show considerable volatility

Among the individual countries there are often marked fluctuations from year to year in the proportion of companies reporting that they export. The major change in this year's survey was a sharp reduction in the proportion of Australian businesses that export (see figure 1). The proportion fell from 44% last year to 26%, the lowest for the country in the four years of our survey. Unit costs have been on a sharply rising trend in recent years, and in conjunction with an appreciating exchange rate, this has made life difficult for exporters. Poland also experienced a marked decline in the proportion of exporting businesses, from 52% to 36%, but this proportion remains higher than in the 2004 survey, at the time of Poland's

accession to the EU. Currency depreciation and an initial surge in exports to the EU were followed last year by less favourable conditions including a strong zloty. Appreciating exchange rates also explain the decline in the proportion of exporting businesses in Canada and New Zealand, while relatively high inflation and weak demand from its eurozone partners depressed Spain's exports last year.

Two countries reported sizeable increases in the proportion of exporting businesses. Hong Kong's export trade continues to benefit from the boom in Mainland China and exports remain a major driver of growth. In the Philippines, the marked increase on this occasion reversed a decline in last year's survey.

There are also marked divergences from the global average in the proportion of businesses that export, ranging from almost two thirds of companies exporting in Argentina to just 12% in Japan (see figure 2).

Argentina is included in our survey for the first time. Consequently, it is not possible to gauge the extent to which the recent improvement in economic performance in neighbouring countries and the strength of demand from the buoyant US economy has changed the position. But the country appears to be one where fundamental factors encourage a high proportion of medium-sized businesses to export. The relationship between Hong Kong and Mainland China produces the same effect, as does Mexico's membership of NAFTA, which encourages businesses to trade with the US.

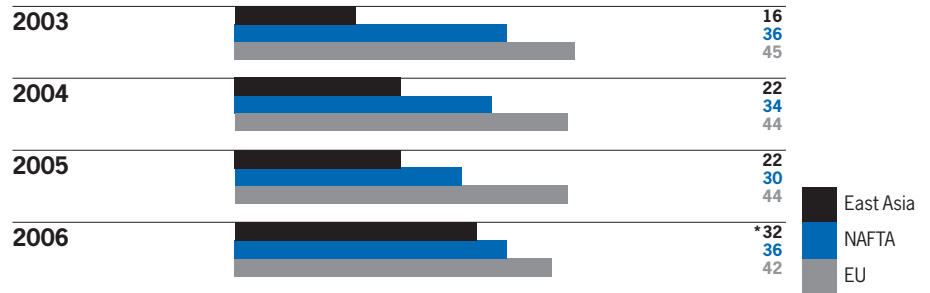
**Figure 2: Proportion of businesses exporting (%)**

<b>Argentina</b>	<b>64</b>
<b>Hong Kong</b>	<b>62</b>
<b>Italy</b>	<b>54</b>
<b>Mexico</b>	<b>47</b>
<b>Germany</b>	<b>46</b>
<b>Netherlands</b>	<b>45</b>
<b>Singapore</b>	<b>45</b>
<b>Luxembourg</b>	<b>43</b>
<b>Turkey</b>	<b>43</b>
<b>Mainland China</b>	<b>40</b>
<b>Sweden</b>	<b>39</b>
<b>UK</b>	<b>39</b>
<b>Greece</b>	<b>38</b>
<b>India</b>	<b>38</b>
<b>Spain</b>	<b>38</b>
<b>Malaysia</b>	<b>37</b>
<b>South Africa</b>	<b>37</b>
<b>Taiwan</b>	<b>37</b>
<b>Thailand</b>	<b>37</b>
<b>Global average</b>	<b>36</b>
<b>France</b>	<b>36</b>
<b>Ireland</b>	<b>36</b>
<b>Philippines</b>	<b>36</b>
<b>Poland</b>	<b>36</b>
<b>US</b>	<b>35</b>
<b>Canada</b>	<b>32</b>
<b>Australia</b>	<b>26</b>
<b>Botswana</b>	<b>20</b>
<b>Russia</b>	<b>17</b>
<b>New Zealand</b>	<b>16</b>
<b>Japan</b>	<b>12</b>

“Despite an encouraging world backdrop, New Zealand exporters faced difficult conditions in 2005. Inflationary pressure forced interest rates up to record levels and the exchange rate appreciated sharply.”

Peter Sherwin  
Grant Thornton, New Zealand

Figure 3: Proportion of businesses exporting by global region (%)



\* this figure includes data for Mainland China which is not included in the data for IBOS 2003-2005

The adverse background noted above for medium-sized businesses in Australia and New Zealand that export has pushed them into the bottom five where they join Japan and Russia, two countries that have invariably featured in this group. We have noted in previous surveys that the low proportion in Japan reflects the fact that surveyed businesses are medium-sized and focus on domestic business, providing products and services to large companies. This structural factor appears to be gaining strength, as the proportion of exporting businesses has fallen to its lowest level in the four-year history of the survey. Similarly, the consumer market in Russia is growing strongly and medium-sized businesses prefer to expand local trade rather than explore the unfamiliar international market.

### Contrasting regional performance

The proportion of exporting businesses varies appreciably across the main global regions. Figure 3 shows that in the EU the proportion is significantly higher than in East Asia and NAFTA. In the case of East Asia, this is due to the fact that Japan, with its heavy weighting and low proportion of exporters, depresses the regional figure. But with the inclusion of Mainland China in the 2006 survey, the gap against the EU narrows considerably. The difference between the EU and NAFTA is magnified, perhaps even fully explained, by the fact that cross border trade in the EU (for example a Polish firm sending goods to Ireland) counts as an export, while trade across state borders in the US, an equally large market, does not. The gap between NAFTA and the EU has narrowed markedly in this year's survey to just six percentage points, its lowest on record, largely due to an upturn in the US figure.

### Proportion of turnover coming from exports

We asked exporting businesses to indicate what proportion of their turnover came from exports. In the highly export-oriented economies of Hong Kong and Singapore, almost two thirds of businesses said that over 25% of turnover was accounted for by exports. Over 60% of respondents in Italy and the Netherlands, two other major trading nations, also reported this. At the other extreme, Japan and Russia, whose medium-sized businesses are firmly focused on the domestic market, have only 5-6% of exporting companies where over a quarter of turnover comes from exports.



**Peter Sherwin**  
Grant Thornton, New Zealand

## Country focus...

Mainland China and India are achieving exceptionally rapid export growth. Given the importance of trade in driving global economic expansion, we highlight these dynamic economies, together with the US, which retains its role as the main engine of global growth.

### India – Key facts and economic overview

**Population:** 1.1bn

**GDP size:** \$630bn

**Global GDP rank:** 9th

**GDP real growth 1995-2005:** averaged 5.9% per annum

**Exports (share of world total 2005):** 1.1%

**Export volume growth 2000-05:** averaged 18% per annum

The Indian economy has been one of the world's fastest growing since the early 1990s. Growth potential has been boosted in recent years by the opening up of the economy to the global market as controls on foreign trade and investment have been relaxed. Export growth has averaged almost 20% per annum, boosting the overall growth rate.

Given its size, GDP growth rate of around 6%, and greater exposure to international markets, India is exerting an increasing influence on global economic prospects. Although its contribution is less substantial than Mainland China's, it has emerged as a major engine of world growth in the current global expansion.

The economy's growth is broadly based. Industry's contribution to total output at 27% is modest by the standards of other newly industrialising Asian economies, but the sector is growing strongly. The service sector, boosted by business process outsourcing, has been a major driver of economic growth in recent years.

The growth rate of the economy has accelerated to over 7% in each of the past three years and even faster growth is in prospect, spurred by government spending on infrastructure improvements and further liberalisation in key sectors.

### Survey results

- Indian business owners are the most upbeat about their country's economic prospects, with a balance of +93% expressing optimism.
- India features in the top three countries in terms of expectations over the next 12 months for turnover, exports, employment, profitability, investment and ability to raise selling prices among all 30 countries surveyed.
- Business travel, cited by 41% of respondents, is a significant source of stress among Indian business owners.
- 38% of medium-sized businesses in India are exporters.
- India is the leading destination after Mainland China for outsourcing or transferring operations to another country. Almost 30% of respondents who have transferred operations, or plan to do so, have opted for India.

### Mainland China – Key facts and economic overview

**Population:** 1.3bn

**GDP size:** \$2,250bn

**Global GDP rank:** 4th

**GDP real growth 1995-2005:** averaged 10% per annum

**Exports (share of world total 2005):** 5.9%

**Export volume growth 1995-2005:** averaged 20% per annum

The economy is powered by strong export growth and buoyant investment. Consumer spending is becoming an increasingly important driver of activity, but households still save a high proportion of their incomes. A rebalancing towards consumer spending with less reliance on investment and exports is likely in the medium term.

Mainland China has become a leading destination of foreign direct investment (FDI) as foreign enterprises seek to take advantage of relatively low labour costs. FDI inflow of \$60bn in 2004 accounted for 10% of the world total and was exceeded only by the US and the UK. Most FDI goes to manufacturing, but other sectors such as construction and distribution and catering are taking an increasing share.

### US – Key facts and economic overview

**Population:** 295m

**GDP size:** \$11,374bn

**Global GDP rank:** 1st

**GDP real growth 1995-2005:** averaged 3.3% per annum

**Exports (share of world total 2005):** 10%

**Export volume growth 2000-05:** averaged 5% per annum

The US economy has exhibited much greater dynamism than other mature economies since the early 1990s. Growth has averaged well over 3% a year, compared with 2% for the eurozone and little over 1% for Japan, thanks in large measure to greater flexibility in its labour and product markets.

The US economy continued to thrive in 2005 despite high oil prices and the disruption caused by serious hurricane damage. Strong consumer spending and an increase in business investment at over 8% for the second year in a row underpinned GDP growth at 3.5%.

In conjunction with continuing above-trend growth, evidence of inflation pressure has prompted the Federal Reserve to raise short-term interest rates steadily. Since June 2004, the main interest rate has been raised 16 times and now stands at 5%. This is likely to constrain consumer spending, with GDP growth moderating to 3.2% this year. With consumer spending easing further in 2007, GDP growth is expected to decelerate, but should still be near 3%.

### Survey results

- A measure of Mainland China's importance in international trade is that nearly one in five medium-sized businesses now imports from Mainland China...
- ...and 14% of medium-sized businesses export to Mainland China.
- 40% of medium-sized businesses in Mainland China are exporters.
- One in ten businesses worldwide have transferred or outsourced operations to another country, and Mainland China is the leading destination (31% of respondents who have transferred operations or plan to do so).

### Survey results

- US business owners were optimistic about economic prospects, but much less so than in recent years. Sentiment was depressed by expectations that the economic cycle was past its peak and by the impact of hurricanes shortly before the survey was conducted.
- Expectations about profitability in the next 12 months were very positive, with a balance of +58% expecting an increase.
- Respondents' views were also more positive than the global average regarding employment prospects and ability to raise selling prices.
- US businesses identified lack of availability of workforce skills and regulations/red tape as the main constraints on business expansion.

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The Grant Thornton **International Business Owners Survey (IBOS)** was carried out among more than 7,000 owners of medium-sized businesses from 30 countries/territories during Q4 2005. IBOS began in 2002 and builds on the European Business Survey (EBS) which Grant Thornton International ran from 1993 to 2002. The research was conducted by Experian Business Strategies Limited and Harris Interactive.

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