

Pottinger

PERSPECTIVES

Bringing ideas, people and data together to change the world

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PREPARING FOR THE HURRICANE





Many countries and industry sectors are heading into the most turbulent environment seen in the last century. Three simultaneous industrial revolutions, dramatic increases in competition, huge fiscal imbalances, growing geopolitical tensions and a fractured social contract are combining to create a veritable smorgasbord of risk and uncertainty.

The hurricane is gathering force and stormy weather lies ahead. Yet these same factors also imply that this will be the best possible environment for strong businesses to outperform their peers by huge margins. Asset prices will fall, de-risking larger investments. Weaker competitors will be held back by stretched balance sheets and pure fear. Ongoing pressure for short-term performance will distract almost everyone from pursuing obvious long-term prizes. Similarly, in politics, countries that seize the opportunity to renew their economies into a form truly fit for the 21st century will benefit for decades to come.

Capitalising on these opportunities is no simple task. Holding on ever more tightly to the status quo will not help your business to survive the impending storm. Nor is economic isolationism the answer to endemic economic and fiscal problems, no matter how popular it may be with some parts of the electorate over the short term.

So, how do you prepare for the unsavoury

weather that lies ahead? How can you plot the right course through the storm, and navigate to a safe harbour that provides a gateway to decades of prosperity? Can wise old heads prevail in the face of radical youthful disruption?

First, you must understand the forces that are driving the hurricane.

If you do, you'll see that how the storm will develop and where it will move is surprisingly predictable.

The revolutionary trifecta – the internet of things, AI/robotisation, and the rebuilding of the world's energy infrastructure – will drive a decade of dramatic change and restructuring of many industries. Meanwhile, many new competitors will emerge, including start-ups financed with enormous sums of low-cost venture capital, as well as incumbents from other industries as the lines between sectors are erased by technological developments.

Dramatic shifts in employment will occur, including the literal decimation of many

administrative and mid-level professional jobs. In short, without the right strategic and policy choices, existing jobs will be robotised far more rapidly than new jobs can be created, adding to the social challenge and threatening some companies' licence to operate.

Similarly, the economic and fiscal challenges are writ large. Developed economies are over a decade into an up-cycle, which cannot last forever. Many nations' balance sheets are stretched, and welfare systems are showing their fragility. In Australia, long the poster child for inclusive economic growth, national debt remains low, but personal debt (mostly mortgage borrowing) is now over 120% of GDP, second only to Switzerland. In the UK, uncertainty over Brexit is driving large-scale employers to invest elsewhere in the EU. And in the USA – where social welfare provision is already minimal – huge tax cuts targeted primarily at the very rich will add materially to debt.

More importantly, perhaps, wealth



polarisation has returned to levels not seen since shortly before the Great Depression of the 1930s. This matters, not simply because rising inequality leads to social tension, but also because concentration of wealth *reduces* economic growth, for the simple reason that the rich spend a much smaller proportion of their income than the average worker (see Robert Reich's *Aftershock*). Thus, though the world escaped relatively unscathed from the Great Recession of the late 2000s, the deepest underlying problem – downward pressure on demand due to polarisation of wealth – was never addressed.

Wealth polarisation has returned to levels not seen since shortly before the Great Depression

And don't forget that wealth is polarising between nations too – whilst leading companies in the USA and China have created enormous value for their shareholders in the last two decades, many of their peers in the UK, Europe and Australia have singularly failed to do so.

With the UK embroiled in the [Brexit Bungle](#) and America caught up in [Trump's War on Everyone](#), China is quietly writing its own [Tale of Two Centuries](#) and is leaving the West's politicians to fight the wrong battles. Sadly, as the Great Reckoning approaches, internal party-political skirmishes dominate the political debate in the West.

Understand these forces, and it should

become much clearer how the storm will move and as a result the course you need to plot to avoid the worst of the weather.

Second, you must shut out all the noise.

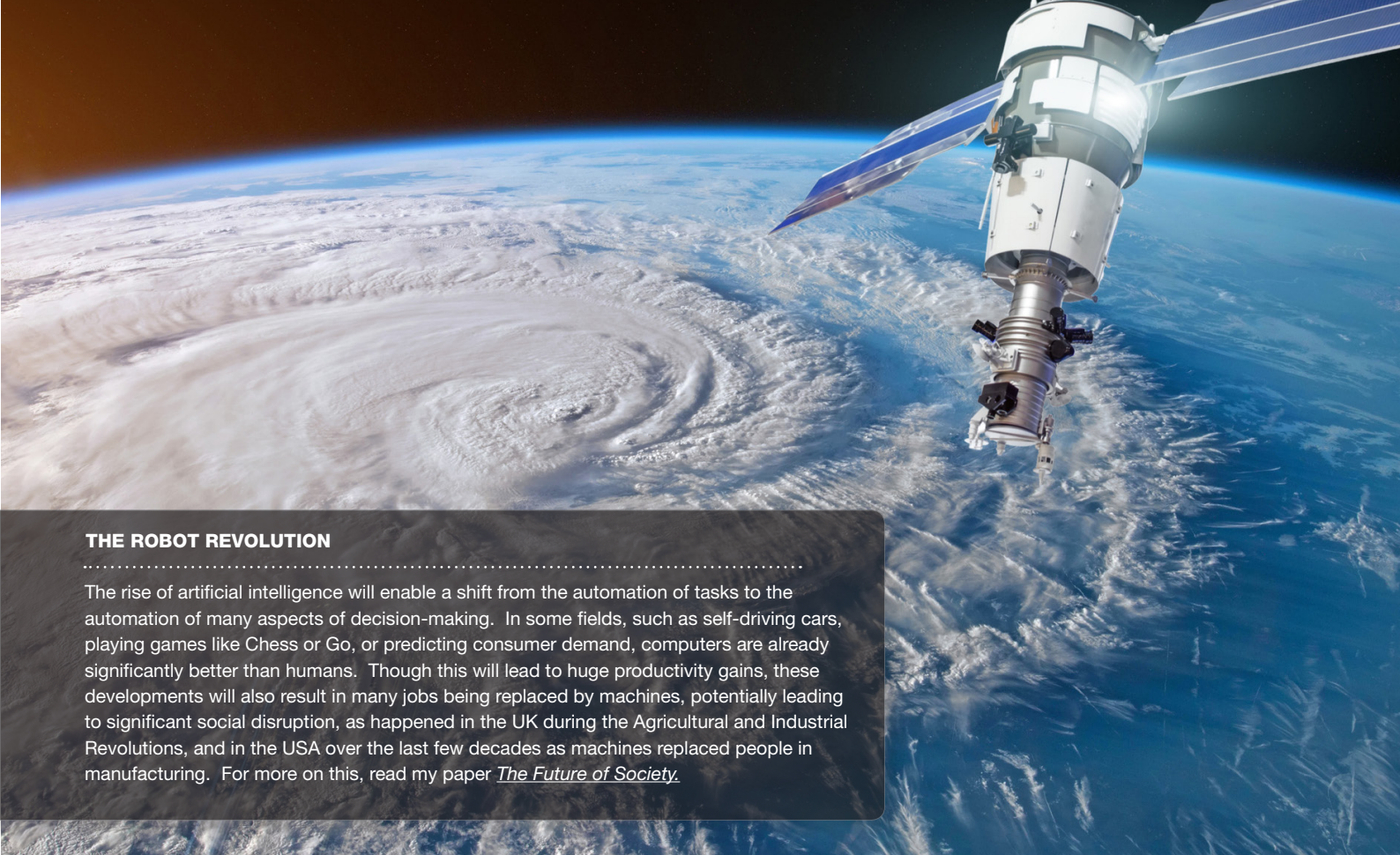
Though the hurricane that is approaching will wreak havoc on much that stands in its path, the storm will eventually pass by and clear weather will return. So, if you focus resolutely on the long-term, you should be able to identify an end-destination that will be attractive in the future, rather than one that was desirable in the past. In making this choice, make sure you understand all the

possible options, not just those that you find most familiar or comfortable.

As an example, many large Australian companies earn nearly all their profits in their home market of Australia (and to a modest degree New Zealand). Though this has made for a comfortable ride, it's notable that the Australian stock market has barely kept pace with domestic economic growth. In contrast, leading US companies such as Apple, Google and Microsoft have much greater international diversification and have thus benefited much more strongly from the global economic growth that has resulted from technological advancement. So too have Australian companies with global businesses,

THE ENERGY REVOLUTION

The cost of renewable energy generation and battery storage have fallen exponentially for *decades*. Increasing scale economies and technological developments mean that prices will continue to fall by around 15% a year for at least the next decade, potentially longer. In developed countries the direct economic impact will be modest – power will become cheaper and more plentiful, and the environment will improve. In contrast, less developed countries will benefit massively, as electrical power will become accessible to most of the population, without the need for huge one-off investments in large scale generating plants and electricity distribution networks. The indirect effects will be enormous, as the world's entire US\$5 trillion energy industry is turned inside out in the next couple of decades, and the shift to electric vehicles accelerates.



THE ROBOT REVOLUTION

The rise of artificial intelligence will enable a shift from the automation of tasks to the automation of many aspects of decision-making. In some fields, such as self-driving cars, playing games like Chess or Go, or predicting consumer demand, computers are already significantly better than humans. Though this will lead to huge productivity gains, these developments will also result in many jobs being replaced by machines, potentially leading to significant social disruption, as happened in the UK during the Agricultural and Industrial Revolutions, and in the USA over the last few decades as machines replaced people in manufacturing. For more on this, read my paper [*The Future of Society*](#).

such as Cochlear, CSL, Macquarie bank and Atlassian. In short, the domestic status quo is not necessarily your friend.

Looking ahead, market leaders in numerous industries – and particularly in financial services – will be challenged by a raft of new businesses who will bring a completely new competitive dynamic to bear.

your own race, observing the weather that is emerging, but remaining confident in your judgement as the storm evolves.

And remember this: The most important lesson of the last twenty years is that the fundamentals of business haven't changed. Today's stratospherically valued start-up must eventually become a profitable business

The most important lesson of the last twenty years is that the fundamentals of business haven't changed.

So, you must set an end-destination that will remain strategically and commercially attractive as the effects of technological change work their way through the economy, and consumers' needs and expectations continue to evolve.


Third, don't forget where you're going.

When bad weather closes in, it's easy to lose sight of your destination. Though you may need to adjust course a little to navigate the storm safely, if you are well prepared in advance, you will have more confidence to execute your plans and make sure you reach your intended goal. In business, this translates into the confidence to make investments when everyone around you is panicking – probably the best opportunity you will ever have. Hopefully the chaos will remind you of the old adage that opportunity favours the brave.

This highlights how important it is to make sure that you have the right team around you, and that everyone understands where you are trying to go. They will help you to sail

that is valued on conventional valuation metrics, or it will die. So, trust your instincts, and pursue opportunities to meet customer needs in a way that – in the fullness of time – can generate adequate returns for your own shareholders.

So, where do you start?

Though the journey through the storm may be stomach-churning, those that recruit the right crew, have the right map and plot the right course will sail through the quietest quadrant of the hurricane, and make landfall safely in the incredibly attractive technological new world that lies just over the horizon. Our team has centuries of combined experience of navigating precisely these sorts of challenges, spanning every industry sector and major economy. Can we help you plan and execute your expedition? 

Nigel Lake is co-founder of Pottinger and Atomli, and author of *The Long Term Starts Tomorrow*.

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THE INTERNET OF THINGS

Low cost sensors and ubiquitous wireless networks means an explosion in the availability of information as well as the ability to control billions of devices in real time. This will, in turn, enable dramatically more precise and proactive management of many aspects of our lives, from the way we interact with machines in the home to the way that our food is grown and factories are operated. In the near term, the greatest challenge will be to sort out the commercially attractive wheat from the over-hyped tech chaff. Over the medium to long term, however the benefits will touch almost every part of our lives.

Previously in Pottinger Perspectives:



I'm sure you've heard that old chestnut before – "all you need to succeed is hard work" – sometimes delivered with the implication that if you are unsuccessful (or poor) you must be lazy. Or the less pejorative quotation from the September 1932 edition of Harpers Monthly Magazine attributed to Thomas Edison that "Genius is one percent inspiration and ninety-nine percent perspiration." When applied to the world of today's start-ups, however they are both wrong.

By Andrew Paddon

http://www.pottinger.com/all_it_takes_is_hard_work.pdf

About Pottinger

Pottinger is a global advisory firm headquartered in Sydney and New York. We combine strategic, commercial, financial and transaction perspectives, and focus first on long term outcomes, to deliver commercial advice that is practical and complete. We navigate the uncertainty inherent in commercial decisions, helping our clients to identify value overlooked by others, and to avoid risks which others may not see.

Pottinger helps organisations to adapt, innovate and transform, by providing insight and advice on strategy and public policy matters, as well as the negotiation and execution of M&A and financing transactions. Our combination of strategic thinking, M&A advice and financing capabilities allow us to find innovative solutions to the challenges arising in industries facing dynamic change and disruption.

Our team has exceptionally broad and deep strategic advisory and transaction execution experience, encompassing all of the world's top thirty countries. Examples include:

- Advice on market entry, strategic repositioning, identification of new growth opportunities, spin-outs and other forms of restructuring and advice on strategic investments, using our proprietary Destination-led Strategy® methodology, together with analogous advice to governments on public policy;
- Advice in relation to large and small-scale acquisitions, divestments and takeover responses for both publicly listed and private companies;
- Capital optimisation and financing advice for large enterprises, together with advice on commercialisation planning, capital strategy and capital raising for emerging companies;
- Specialist input in relation to the design, formation, restructuring, sale and dissolution of large scale joint ventures and partnerships; and
- Identification and quantification of risk, by applying advanced statistical techniques to relevant data pools, thus simplifying decisions impacted by significant uncertainty.

Pottinger is 100% independent, owned by its employees and operates a completely conflict-free business model



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