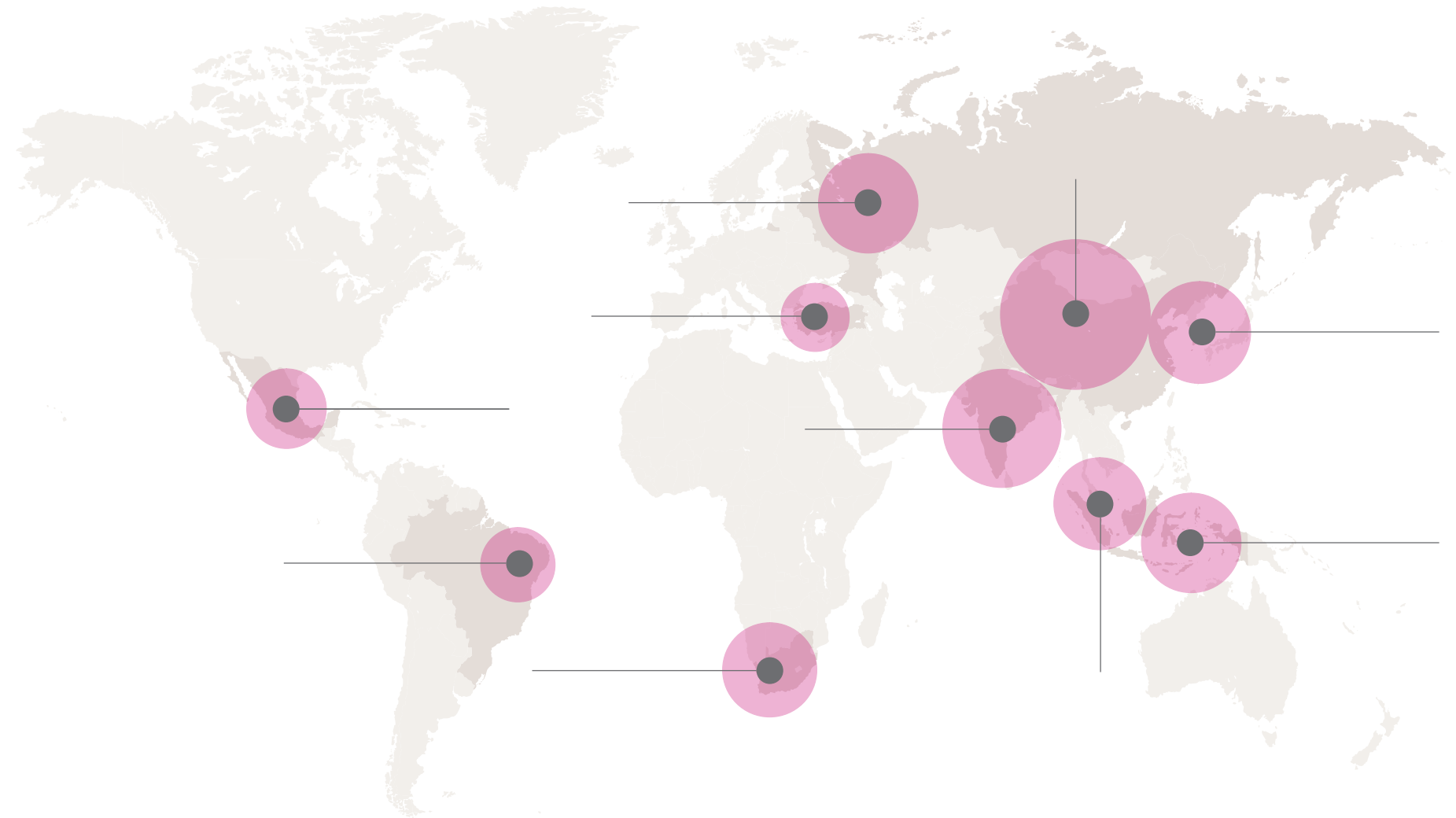


01  
The top ten:  
overview

# Food and beverage.

## The Linklaters Emerging Opportunity Index



● Size of bubble represents forecast five-year annual market growth rate (CAGR) in percentage terms

## 02 Executive summary

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### 02 Executive summary

The Linklaters Emerging Opportunity Index focuses exclusively on emerging markets as these economies are forecast to exhibit the fastest growth rates for food and non-alcoholic beverages over the next five years.

Growth, however, forms only one side of the success story. The forecasting models developed to produce this Index cover 40 of the 50 largest economies in the world today. To identify the ten most attractive food and beverage emerging markets, we assessed both opportunity and risk. What we found is that in the top emerging economies, the opportunities invariably outplay the risks, making those countries essential to the success of global food and beverage companies.

We applied the same opportunity and risk factors to developed economies: on a level playing field emerging markets still take six of the top ten slots worldwide and three out of the top five.

Key emerging markets are also less likely to be adversely affected by macro-economic shock scenarios, such as a Eurozone break-up or a hike in oil prices, than many food and beverage markets in the developed world.

Despite this, very few multinational food and beverage companies are truly leveraging emerging market growth.

However, a shift towards emerging economies is clearly underway.

The alcohol sector, which is more consolidated than food on a global basis, has led the charge. The past year alone saw Heineken's acquisition battle for Asia Pacific Breweries, Diageo's US\$450m purchase of a Brazilian cachaça maker and US\$1.8bn venture with India's United Spirits, and SABMiller's purchase of seven breweries plus a lager brand in China (see "SABMiller in emerging markets").

But if there is no such thing as a free meal, how can companies determine which markets to focus on?

The Linklaters Emerging Opportunity Index, developed in conjunction with the economic forecasting firm Oxford Economics, identifies and ranks the emerging world's most attractive food and non-alcoholic beverage markets, based on both opportunity and risk factors. Here we highlight our key findings.



**In top emerging economies, the opportunities invariably outplay the risks, making those countries essential to the success of the global food and beverage companies**

### Key findings

- > Taking both opportunity and risk factors into consideration, the most attractive emerging markets for food and beverage investment are, in order, China, India, Russia, Brazil, Indonesia, South Korea, Malaysia, Mexico, South Africa and Turkey.
- > While food and beverage markets in the BRIC countries will dominate the emerging world in terms of scale by 2017, others won't be far behind – this is particularly true for Indonesia, Mexico and Turkey.
- > There is a trade-off between opportunity and risk. The fastest-growing markets with the greatest scale involve the highest risks. Companies seeking to access these markets will need to manage these risks carefully on market entry and throughout their investment.



**"Our models indicate that the ten fastest-growing food and non-alcoholic beverage markets in the next five years will be emerging markets."**

“

The fastest-growing markets with the greatest scale involve the highest risks. Companies seeking to access these markets will need to manage these risks carefully on market entry and throughout

”

## 02 Executive summary

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### 02 Executive summary

- > Few advanced economies can measure up to the emerging economies, even when risk factors are taken into account. Applying the criteria used in our Index to advanced economies, emerging markets still take six of the top ten slots globally, and three out of the top five.
- > Emerging markets vary in their exposure to current economic risks such as a Eurozone break-up or an oil price shock, but largely hold to their high opportunity potential. Some of the top ten markets, such as Indonesia, would be less impacted by these threats.
- > Our case study of Yum! Brands highlights the importance of the willingness to commit capital: even when working with local partners, multinationals must be willing to take investment leadership if they wish to grow rapidly.
- > Our case study of SABMiller also highlights the importance of investment, both to attain scale and because the first-mover advantage is greater in emerging food and beverage markets.
- > Our section on routes to market highlights the advantages and disadvantages of each entry strategy and key ingredients of successful JVs and acquisitions.

#### Paul McNicholl

Food and Beverage Global Co-head

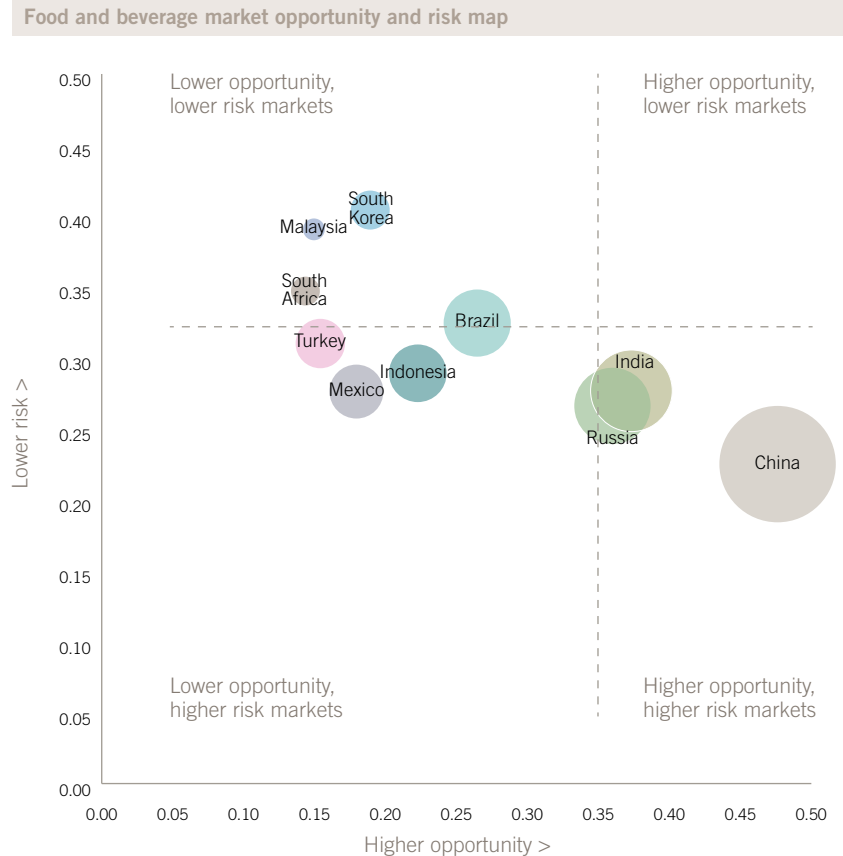
#### Stuart Bedford

Food and Beverage Global Co-head

#### Market opportunity and risk map

In emerging food and beverage markets, risk can often determine the scale of the opportunity. China, India, Brazil and South Korea cluster on a line. This imagined line represents a roughly even trade-off between risk and opportunity. The Chinese market offers the greatest opportunities, both in terms of market growth and as a competitive production location. South Korea offers the lowest risks. Indonesia is just behind this imagined line, but ranks higher than South Korea in the Index because we have over-weighted opportunity factors – as indeed most investors probably will.

Opportunity and risk are assessed on a zero to one scale per the Index methodology described on the following page. Bubbles represent 2012 market size in US dollar terms



03  
The Index

03 The Index

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## 03 The Index

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### 03 The Index

The Linklaters Emerging Opportunity Index is composed of the factors listed below, weighted based on the following principles:

- > the combined market opportunity factors are weighted at 80%;
- > the combined country risk factors are weighted at 20%;
- > the five-year market growth forecasts in dollar terms carry double the weight of all the other factors in the Index.

#### Opportunity factors

##### **Food market size in real terms\***

Estimates based on national statistical sources, including all consumer spending on food products.

##### **Food market growth in real terms\***

Forecast for increase in market size (real US\$) between 2012 and 2017, based on demographic, price level, consumer spending and consumer income factors.

##### **Food market growth in percentage terms**

Forecast for the rate of food market growth (Compound Annual Growth Rate, or CAGR) between 2012 and 2017.

##### **Non-alcoholic beverage market size in real terms\***

Estimates based on national statistical sources, including all consumer spending on non-alcoholic beverages.

##### **Beverage market growth in real terms\***

Forecast for increase in non-alcoholic beverage market size (real US\$) between 2012 and 2017, based on demographic, price level, consumer spending and consumer income factors.

##### **Beverage market growth in percentage terms**

Forecast for the rate of non-alcoholic beverage market growth (CAGR) between 2012 and 2017.

##### **Food production base potential**

Forecast for food industry output growth (CAGR) between 2012 and 2017, reflecting the competitiveness of the market as a production base to serve regional demand.

##### **Beverage production base potential**

As above, but for non-alcoholic beverages.

#### Risk factors

**Growth forecast risk.** Assessment of variance (%) from baseline forecast for growth in 2017 based on oil price shock and Eurozone break-up scenarios (see "Exposure to current economic risks").

**Sovereign risk level.** Country risk indicator comprising credit risk, investment expropriation risk and political stability risk. Compilation of Fitch, S&P, Moody's and OECD Consensus country risk ratings for 2012.

##### **Corruption risk.**

Transparency International Index of level of corruption for 2013.

##### **Food and beverage investment restrictiveness.**

Index of restrictions on foreign ownership in the food manufacturing sector, covering equity restrictions, screening/approval restrictions, operational restrictions and restrictions on employment of foreign personnel. From the Organisation for Economic Cooperation and Development (OECD), 2012.

##### **Quality of investor protections.**

Index of the quality of protections for investors, comprising directors' liability, shareholder lawsuits, extent of disclosure, and legal protection for investment. From the 2013 World Bank Doing Business Indicators.

Notes: All forecasts and estimates by Oxford Economics unless otherwise stated.































"Middle-class" as referred to in this report means households with incomes of US\$30,000 or above.

\*"Real terms" means that figures are adjusted for inflation. Figures are presented in 2012 US dollars unless otherwise noted.

# 04 Market growth outlook

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## Food consumption




















Rank	Market	Current market size (US\$bn) 2012 prices	Market growth (US\$bn) 2012-17	Market growth in percentage terms 2012-17 (CAGR, %)
1	China	666.5 	323.7 	8.2 
2	India	341.6 	96.3 	5.1 
3	Russia	299.4 	58.0 	3.6 
4	Brazil	232.2 	24.4 	2.0 
5	Indonesia	170.8 	33.2 	3.6 
6	South Korea	78.2 	16.0 	3.8 
7	Malaysia	24.5 	4.0 	3.1 
8	Mexico	149.6 	18.1 	2.3 
9	South Africa	43.0 	7.4 	3.2 
10	Turkey	125.7 	11.0 	1.7 

04  
Market growth  
outlook

## 04 Market growth outlook

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## Non-alcoholic beverage consumption

Rank	Market	Current market size (US\$bn) 2012 prices	Market growth (US\$bn) 2012-17	Market growth in percentage terms 2012-17 (CAGR,%)
1	China	30.9 	11.7 	6.6 
2	India	11.6 	3.2 	5.0 
3	Russia	25.3 	4.0 	3.0 
4	Brazil	23.5 	2.9 	2.3 
5	Indonesia	7.6 	1.2 	2.9 
6	South Korea	6.0 	1.4 	4.2 
7	Malaysia	1.7 	0.3 	2.8 
8	Mexico	11.3 	0.4 	0.7 
9	South Africa	3.5 	0.3 	1.8 
10	Turkey	8.0 	0.3 	0.7 

04  
Market growth  
outlook

## China no. 1



### Food market drivers

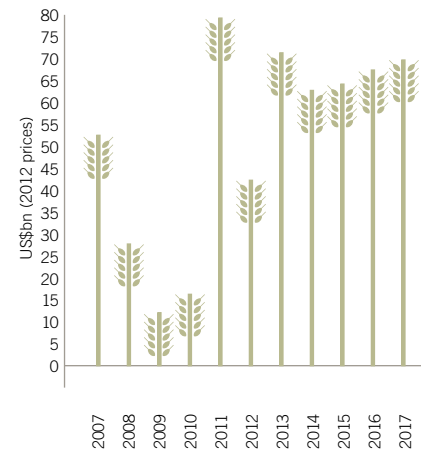
China's top position in our Emerging Opportunity Index is indisputable. Its sheer market size means that even small changes in consumer spending can drive the enormous gains that we expect to see in both dollar and percentage terms by 2017. Because of that, even when weighed against risk factors, China still ranks first. With this growth, however, comes increased competition among the food and beverage players, and a number of Western multinationals have struggled to match the fast evolving expectations of local consumers. Others, such as Yum! (See "Yum! Brands in emerging markets") have turned China into a success story.

### Beverage market drivers

The Chinese non-alcoholic beverage market is not as large as it is for food, but the potential for further growth is significant. Average Chinese incomes are still not high enough for China to have an overwhelming lead in non-staple food products, but this will soon change. The number of middle-class households is forecast to grow from less than three million in 2010 to more than 30 million by 2020. A number of major non-alcoholic beverage companies have, in the past two years, announced multi-billion dollar investment plans for China to capitalise on this projected increase in demand.

### Annual food and beverage market growth in real terms

Despite a slowdown in 2012 (where a number of food and beverage multinationals reported a negative impact on their Chinese earnings), the food and beverage market in China is forecast to grow at almost double the rate of the US, both in real and percentage terms, to make it the world's second largest market (behind the US) by 2017. China's estimated 2012-17 CAGR of 8.1% cements its position at the top of the Index.



### Opportunity factors

A projected CAGR of 8.2% between 2012 and 2017 will make China one of the fastest growing countries in the world, in terms of market size, for the food and beverage sector. In addition to leading on growth, China remains a competitive base to serve the rising food demands of the Asia region.



### Risk factors

China is exposed to global economic risks: in 2012, slowing growth in the Eurozone hit the Chinese economy. Supply chain security is critical to foreign food and beverage brands. Other key risk factors are restrictions on food investment, where gaining approvals can be onerous, and weak legal protections for investors.



“China continues to welcome foreign investment in sectors with high consumer growth, such as food & beverage. Changes to facilitate the entry of global brands into China include lifting certain foreign ownership restrictions and the introduction of a number of new investment structures.”

**Betty Yap**  
Linklaters Partner



05  
The top ten



## India no. 2



### Food market drivers

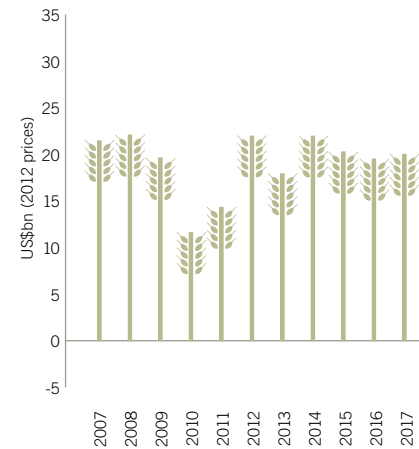
Growing consumer demand leading to a rise in the number of aggressive regional and global players in categories where the entry barriers are low, has been the key reason for the growth of the food sector in India. Favourable demographic factors such as a younger population (in comparison to China) combined with a forecast CAGR of 5.1% for 2012 to 2017 make India an attractive market. Low average household income means that India is a very price-sensitive market, where the cost of basic food items can be a driver of the political economy, rather than the other way round: since 1980, sharp rises in the price of onions, a staple food, have been associated with the collapse of two coalition governments.

### Beverage market drivers

Because the average Indian household income is low, the beverage market in India is underdeveloped by world standards. However, with the number of middle-class households due to approach 10 million by 2020 this will not be the case for long. Investing ahead of this demand, Western beverage companies have announced billions of dollars worth of investment into India over the next eight years. Perhaps they are onto something: in terms of growth rate, India achieves a forecast beverage market CAGR of 5.0% – one of the highest in the Index.

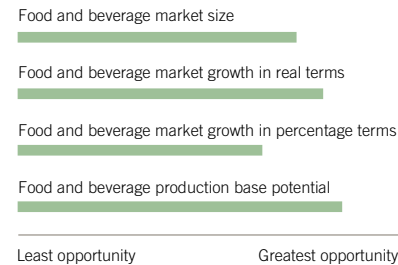
### Annual food and beverage market growth in real terms

By 2017, India is projected to become the world's fourth largest food and beverage market, trailing only the US, China and Japan. Although India's relatively low-income consumers still spend little on non-staples such as non-alcoholic beverages, its food and beverage 2012-17 CAGR of 5.0% is the second highest in the Index.



### Opportunity factors

India almost tops the Index on indicators of absolute food market size and growth. If infrastructure challenges can be overcome, India may also come to rival China as a production location to address broader Asian demand.



### Risk factors

India still maintains some restrictions on foreign equity investment in food manufacturing. While India's economy is less energy intensive than China's, it relies heavily on energy imports, and thus it is also exposed to global economic risks. Additional regional compliance requirements (i.e. labelling) can present operational challenges. Corruption remains an issue.



“

Until the early 90s, the Indian food and beverage industry consisted of regionally segmented units focused mostly on the domestic market. With liberalization and the rise in urban middle-class incomes, India is experiencing an explosion of brands. The entry of international brands has consolidated the market, providing a platform for domestic players to emulate.”

**Savi Hebbur**  
Linklaters Partner



05  
The top ten

## Russia no. 3



### Food market drivers

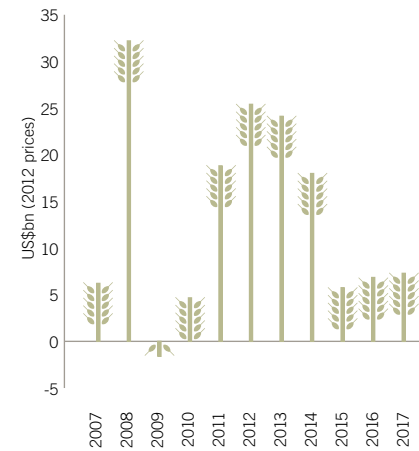
Russia's food market has enjoyed dramatic growth over the past five years, reaching an estimated CAGR of 5.8%. Global oil prices have helped to inject money into the energy-rich Russian economy – which looks set to remain the world's fifth-largest food market in 2017. This energy dependence can, however, produce economic volatility. Perhaps for this reason, partnerships are popular for Western investors and we have seen a number of multinational quick-service restaurant companies investing in Russia through joint venture agreements with local partners.

### Beverage market drivers

Russia's market for non-alcoholic beverages has boomed over the past five years, rising from the seventh largest world market in 2007 to the fifth-largest in 2012. Uniquely among the BRIC countries, Russia is a middle-income economy, and its citizens are wealthy enough to indulge in non-staple goods. With oil prices expected to weaken and unfavourable demographics (an ageing population) beginning to take a toll, Russia is unlikely to repeat the growth in the next five years. However, by 2020 Russia will have more than 15 million middle-class households, which is good news for global beverage companies.

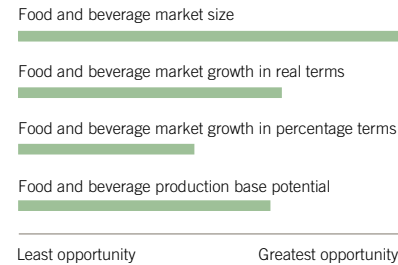
### Annual food and beverage market growth in real terms

Russian food and beverage markets enjoyed extraordinary growth between 2007 and 2012. Despite a potential slowdown in growth, Russia is set to remain one of the most attractive destinations for the food and beverage industry with an estimated 2012-17 CAGR of 3.6%.



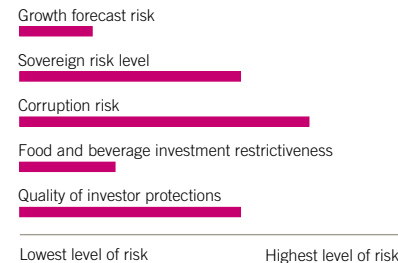
### Opportunity factors

In terms of market size, Russia is a world leader in both food and (unusually for an emerging economy) non-alcoholic beverages. With its oil-rich economy, Russia cannot rival China or India as a competitive production location, but some Russian food and beverage companies are internationalising.



### Risk factors

Russia's corruption risk, sovereign risk and legal risk score fairly highly. In 2012, alcohol brewers faced a sudden tripling of the beer tax, reminding investors of potential risks from Russia's sometimes-volatile regulatory environment.



“Russia, with its fast-growing middle-class, is expected to close the gap with developed economies. However, to harness consumer growth in Russia, local knowledge is king. Food and beverage companies entering the market need to invest in thorough due diligence to understand fully local business drivers and the commercial interests of prospective partners.”

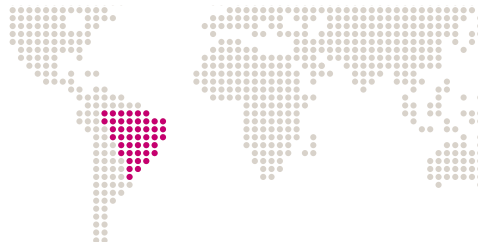
**Denis Uvarov**  
Linklaters Partner



05  
The top ten



## Brazil no. 4



### Food market drivers

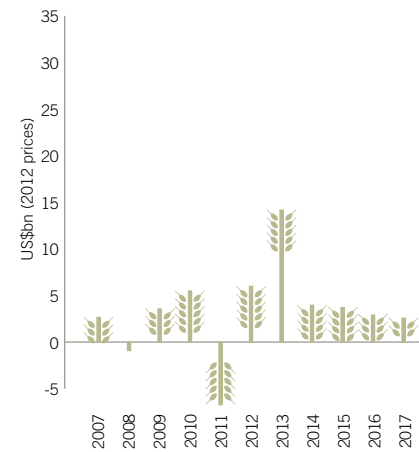
Brazil's middle-class affluence is second only to China, with more than 17 million households predicted to break through the middle-class income ceiling by 2020. Led by Brazil, the Latin American region as a whole has been a growth region for food and beverages: SABMiller reported that its 7% rise in annual group revenues was driven largely by Latin America (see "SABMiller in emerging markets"). However, Brazil is yet to repeat the mini boom of 2010, when it achieved a GDP growth rate of 7.5%, rivalling its BRIC peers China and India.

### Beverage market drivers

With the continuing rise in average consumer income, Brazil is forecast to be the world's seventh-largest non-alcoholic beverage market in 2017. A growing young population and inflation control should also help to drive market growth. On the other hand, reaching Brazil's vast, varied and complex market can be testing as regional penetration and distribution networks remain a challenge.

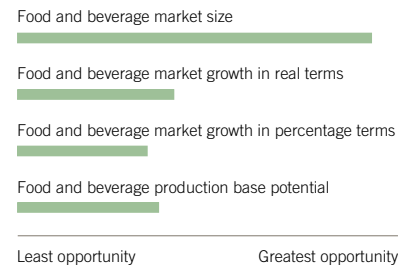
### Annual food and beverage market growth in real terms

Brazil's food market grew relatively slowly over the past five years, at a CAGR of 0.5%. This should rise to 2% over the next five years. As price inflation, which had sapped the spending power of Brazilian consumers, is better controlled, the growth rate for non-alcoholic beverages will also rise to a CAGR of 2.3%.



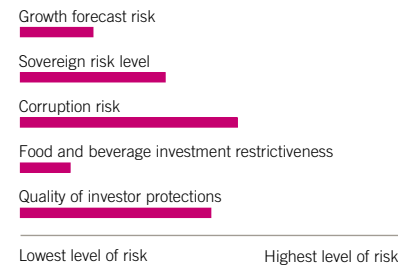
### Opportunity factors

Brazil's attractiveness to food and beverage companies is largely due to a booming middle-class willing to pay a premium for global brands. Its regulatory regime for foreign investment in food manufacturing is the most open of the BRICs and intellectual property rights protection is robust. Although temporary exchange rate factors may be affecting Brazil's score as a production location, Brazilian agriculture remains highly competitive.



### Risk factors

Brazil scores more favourably than its BRIC peers on both corruption levels and sovereign risk. Brazil's tax system, however, should be a critical item on the agenda of those doing business in Brazil. The federation, states and cities are all able to legislate within their jurisdictions and sometimes overlap. Tax planning throughout the life of the investment is critical to success.



“The continued interest in the Brazilian market is based on sound macro-economic principles: market size, a growing middle-class and political stability. However, to succeed in Brazil, companies need to understand its unique legal, operational and cultural environments.”

**Alberto Luzárraga**  
Linklaters Partner



05  
The top ten

## Indonesia no. 5



### Food market drivers

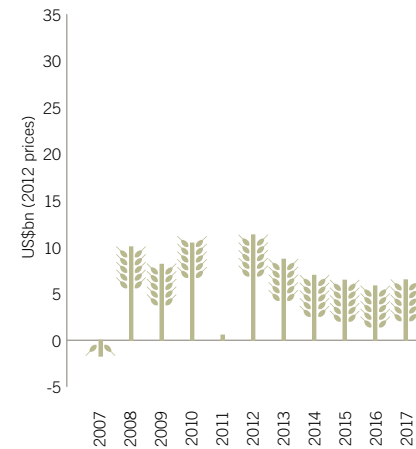
Indonesia has scale: between 2012 and 2017, the forecast market growth rate for food in real dollar terms is expected to exceed even that of Brazil. Indonesia is benefiting from a rapid growth in consumption among consumers whose incomes are, on average, low enough to give a large proportion of any additional income to food. However, over the next five years, food price inflation may affect some of this progress.

### Beverage market drivers

As income grows, Indonesia comes closer to the point at which consumers will spend significantly more on non-staple goods such as beverages. Indonesia's non-alcoholic beverage CAGR should rise from almost immeasurably low levels over the past five years to close to 3% by 2017. The non-alcoholic beverage market, however, should remain small for some time, as average Indonesian incomes are too low to drive purchases of non-staple items such as tea and carbonated soft drinks. Only about two million Indonesian households are projected to reach middle-class income levels by 2020.

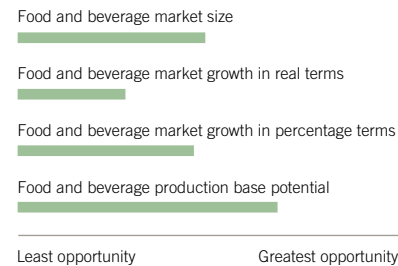
### Annual food and beverage market growth in real terms

While the size of the Indonesian food market compares with countries at the top of the Index (by 2017 it will be almost as large as Brazil's), addressing this market is a challenge, as packaged foods make up little more than 10% of the estimated US\$170bn spent on food by Indonesian consumers. Compound annual growth rates for both the food and non-alcoholic beverage markets will be approximately 3% over the next five years.



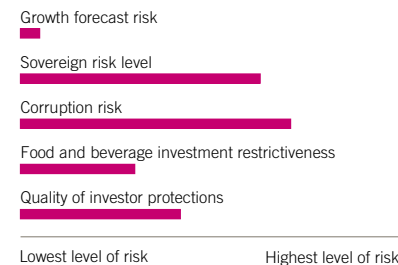
### Opportunity factors

Indonesia competes with the BRICs in scale. After Indonesia, there is a significant drop in market size for the remaining Index countries. Indonesia is also relatively competitive as a production location to serve the booming Southeast Asian demand.



### Risk factors

With its own energy reserves and relatively little integration with the Eurozone, Indonesia is relatively insulated from global economic risks. On the other hand, corruption and sovereign risk levels are high. Foreign investors in food can also face restrictions on employment of foreign personnel.



“

Political and economic stability combined with a growing consuming class transformed Indonesia into a leading emerging economy. Market entrants can benefit from rapid growth opportunities that are no longer available in other developing markets.”

**Sophie Mathur**  
Linklaters Partner



05  
The top ten

## South Korea no. 6



### Food market drivers

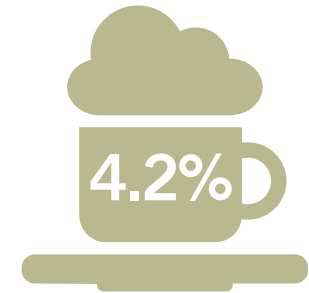
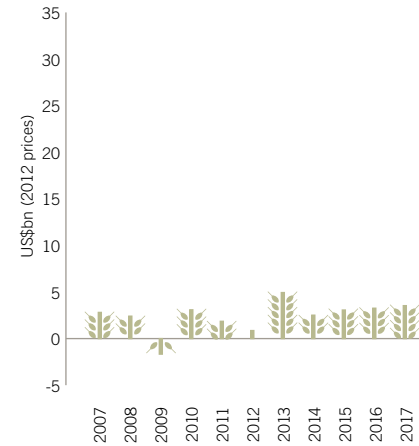
South Korea is a wealthy country – on a par with some economies in Western Europe. So is it fair to consider it an emerging economy? In some respects it would seem so, as South Korea continues to deliver emerging-market growth rates. At South Korea's level of income, demographic and price increases have a relatively minor effect on the share of consumer spending that goes to food. This means growth in overall consumption can produce significant food market growth.

### Beverage market drivers

South Korea is one of the strongest markets for non-alcoholic beverages in our Index. It is forecast to grow by 4.2% over the next five years and benefits from increasingly wealthy consumers who consider tea, soft drinks, juices and even (in contrast to much of East Asia) coffee and milk as regular purchases.

### Annual food and beverage market growth in real terms

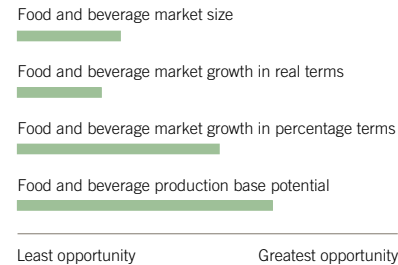
Despite its small market size, South Korea is forecast to achieve a food market growth CAGR of 3.8% over the next five years, on a par with fast-growing emerging economies. The market growth CAGR for non-alcoholic beverages will be even higher, at 4.2%, trailing only China and India on its measure. South Korea's robust food and beverage 2012-17 CAGR of 3.7% justifies its position among the top ten.



South Korea is a wealthy emerging economy with a forecast beverage market CAGR of 4.2%.

### Opportunity factors

Even though its market size is small compared with other countries in the Index, South Korea performs well (especially in beverages). South Korea also remains a competitive production location, given the scale of Asian demand.



### Risk factors

Risk in South Korea is particularly low, despite recent restrictions on store opening hours that negatively impacted foreign retail investors. The investment regime for food manufacturing remains open, and corruption levels and legal protections are on a par with some of the newer EU members.



05  
The top ten



## Malaysia no. 7



### Food market drivers

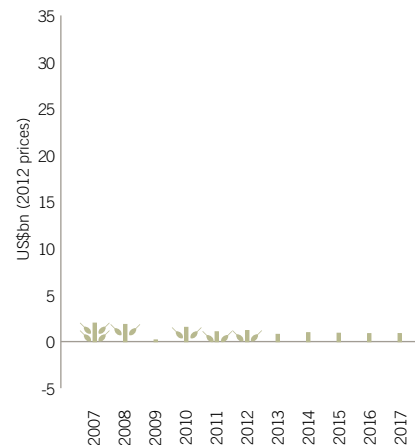
Malaysia is almost certainly the most surprising country entering the top ten. In Malaysia, as in South Korea, a stable population and stable prices have a relatively minor effect on the share of consumer spending that goes to food, so that modest consumption-spending gains can have a positive impact on the food market. By size of the market in dollar value terms, Malaysia ranks only 31st in the world, but by forecasted dollar value growth it reaches 23rd, with a respectable forecast CAGR of 3.1%. Malaysia appears in the Index top ten partly by virtue of its competitiveness as a production location serving booming Asian demand.

### Beverage market drivers

As with food, Malaysia's beverage market is small but with a relatively high forecast CAGR of 2.8%. Price, income and demographic factors all have relatively small effects, leaving consumption increases free to make a significant impact. Malaysian consumers' average wealth is only just reaching the levels which affect the non-alcoholic beverage market. That said, its estimated market growth CAGR over the past five years (5.6%) was among the highest in the world.

### Annual food and beverage market growth in real terms

The Malaysian market is small in relation to the top ten, but the opportunity to address regional Asian food and beverage demand from a Malaysian export platform is significant. Although growth is expected to slow down, its combined food and beverage forecast CAGR of 3.1% between 2012 and 2017 is high, even by emerging markets standards.



Asia-Pacific already accounts for 32% of world food industry value, and Malaysia, a strong export platform, boasts one of the region's fastest-growing food sectors.



### Opportunity factors

Malaysia has the industry infrastructure, competitive exchange rate and location to perform at the top of the Index as a regional export platform. Market size and absolute growth are relatively small, although CAGR forecasts are comparable to the top countries.



### Risk factors

Despite a reputation for unorthodox policy gained during the Asian financial crisis, Malaysia rates very well on sovereign risk and corruption compared with the other countries in the top ten. It performs even better on legal protections for investors.



05  
The top ten





## Mexico no. 8



### Food market drivers

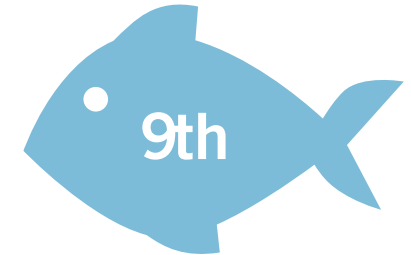
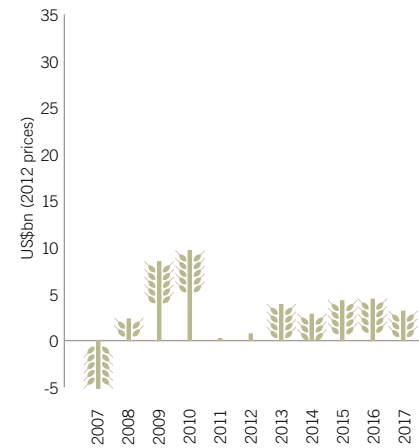
Buoyant consumption growth (outpacing South Korea and Malaysia by a comfortable margin) should enable Mexico to maintain its position near the world's top ten food markets, even if it doesn't perform as strongly in the next five years. Management of price inflation will be a challenge, and, perhaps most importantly, Mexican income levels are moving past the point where a large portion of any additional income is devoted to food.

### Beverage market drivers

Mexican beverage markets have grown rapidly in the past five years, fuelling the growth of local beverage companies, some of which are beginning to undertake global expansion programmes of their own. Indeed, Mexican consumer spending on non-alcoholic beverages is now estimated as the world's 11th largest. As with food, conditions over the next five years are unlikely to be as favourable as in the past. The 2007–12 CAGR of 2.9% is expected to fall to 0.7% over the next five years, as price inflation takes a toll on price-sensitive consumers.

### Annual food and beverage market growth in real terms

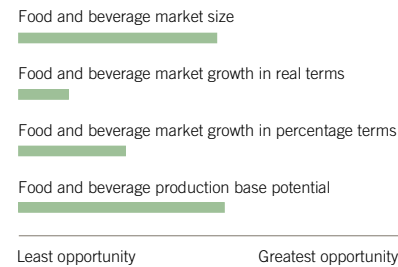
Mexico has enjoyed five years of fairly rapid growth despite continued economic weakness in Mexico's main trading partner, the United States. Food and beverage market drivers may not be so favourable over the next five years, but with a 2012–17 CAGR of 2.3% Mexico secures its position in the Index.



The real increase in the size of its food and non-alcoholic beverage market between 2012 and 2017 is the ninth-largest globally, ahead of Australia and France.

### Opportunity factors

Mexican food and beverage markets approach BRIC scale. Mexico is also relatively competitive as a production location, and regional (notably US) demand, which has recently been weak, is likely to pick up over the next five years.



### Risk factors

Despite its wealth and investment grade status, Mexico scores poorly on corruption levels. Screening and approval processes for foreign food manufacturing investment can also be onerous.



05  
The top ten



## South Africa no. 9



### Food market drivers

The now well-known 'African growth story' started with South Africa. By far the largest African market, South Africa is currently estimated as the 22nd-largest market in the world (Nigeria, the next largest in Africa, ranks 25th). South African companies have been boosted by the recent growth take-off in Sub-Saharan Africa. Many, including SABMiller, now have an extensive presence across the continent.

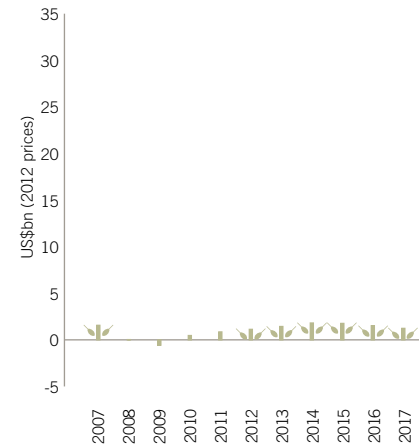
South Africa's prospects should continue to improve. The main drivers of this forecast are healthy consumer spending growth, average young population and moderate price inflation.

### Beverage market drivers

A young growing population and price stability, combined with higher growth rates than for the past five years, should help boost the market for non-alcoholic beverages in South Africa, which currently ranks 25th in the world.

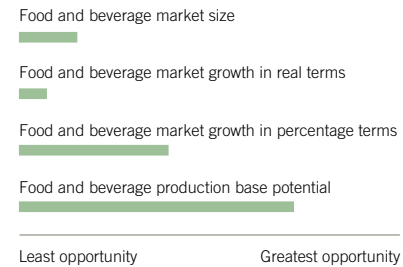
### Annual food and beverage market growth in real terms

South Africa's market size is small compared with the others in the top ten, so on an absolute scale the forecast gains do not look dramatic. On the other hand, the next five years are forecast to be even better than the past five for South Africa, producing a combined food and beverage market growth CAGR of 3.2%.



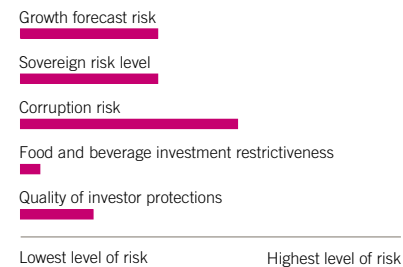
### Opportunity factors

As noted above, South Africa is a good production base from which to capture food demand in Sub-Saharan Africa. Market growth rates are also respectable, although in absolute dollar terms not the highest in the Index.



### Risk factors

South Africa is a unique African market, with some of the best legal protections for foreign investors in the emerging world, and a very open investment regime. Food and beverage companies should be aware, though, that price-sensitive South African consumers are exposed to global economic risks such as oil price shocks.



By 2017, Africa will be home to 1.2 billion people, and South Africa-based companies are enjoying increasing success in accessing the continent's markets.



05  
The top ten





## Turkey no. 10



### Food market drivers

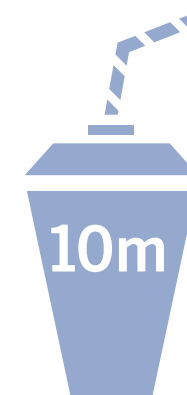
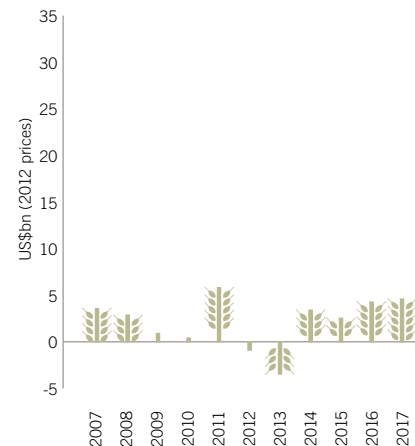
Among the countries in the Index, Turkey has been the most exposed to the effects of the Eurozone crisis. Driven by fairly robust consumption patterns, the next five years should be better, although price inflation could be a problem. With a reputation for being hospitable to Western brands, Turkey is also not far off BRIC scale: forecast to be the 13th-largest food market in the world in 2017, it would rank higher than most advanced economies.

### Beverage market drivers

With a per capita income of about US\$10,000, Turkish consumers are able to afford some luxuries. Indeed, Turkey should be home to more than 10 million middle-class households by 2020 – topping even India. Over the past five years, the estimated size of Turkey's beverage markets rose above Indonesia's to become the 13th largest in the world. Our forecasts suggest, however, that this growth may begin to slow. Measured in volume terms, sales of fast-moving consumer goods fell 1.3% in the year to April 2012, and non-alcoholic drinks fell 1.5%.

### Annual food and beverage market growth in real terms

Despite the effects of the Eurozone crisis, Turkey's food market has grown at reasonable rates, achieving an estimated CAGR of 1.3%, which should rise to 1.7% over the next five years as the Eurozone recovers. Recovery in the non-alcoholic beverage market may take longer, but looking even further ahead, between 2017 and 2022, the non-alcoholic beverage market growth is forecast to rebound to a CAGR of about 3%. Turkey's food and beverage 2012-17 forecast CAGR is 1.6%.



By 2020 Turkey will be home to more than ten million middle-class households – eclipsing even India.

### Opportunity factors

Turkey's food and beverage market size is larger than several countries ahead of it in the Index, including South Africa, South Korea and Malaysia. The widespread presence of modern supermarkets and rising disposable incomes have contributed to a shift in the consumption patterns of Turkish consumers to packaged and processed foods. Additionally, increases in the number of women in full-time employment have supported the trend towards packaged, frozen and ready food.



### Risk factors

Although, as noted above, Turkey is heavily exposed to risks in the Eurozone, some companies have seized the opportunity that this presents and have made strategic acquisitions. Despite these risks, Turkey's risk analysis is favourable when compared with other emerging markets and should remain on the radar of ambitious players.



05  
The top ten

## 06 How do the advanced economies measure up?

In this Index we focus solely on emerging markets, but what if we were to apply the same opportunity and risk factors to the advanced economies? On a level playing field, signs of a shift in power between developed and developing markets are evident: the emerging markets featured in our index still take six of the top ten slots worldwide and three out of the top five.

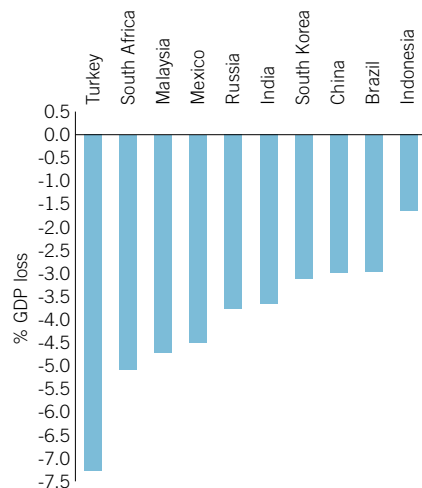
Our models show that demographics and economics have combined to place the emerging economies on top. Advanced economy growth rates, and even market growth in absolute dollar terms, cannot match the emerging world. However, based on their market size, strong control of corruption, good legal protections, and open regimes for foreign investment, a few rich countries, such as the US, Japan, UK and Germany, still belong in the top ten. For now.

Top 10 global food and beverage markets weighted against opportunity and risk factors



## 06 Exposure to current economic risks

Projected GDP loss vs. 2017 baseline forecast in percentage terms

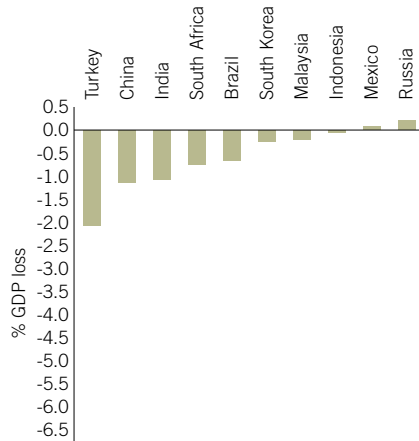


Many emerging markets are relatively insulated from certain macro-economic threats when compared with advanced economies. However, the market growth forecasts presented in this Index are, inevitably, subject to uncertainty. We have attempted to quantify this uncertainty with a measure of 'forecast risk', which evaluates the exposure of each market to current economic risks. Compared with the advanced economies, many emerging markets are relatively insulated from these threats.

### Eurozone break-up

In this extreme scenario we consider what would happen if six countries were to leave the Eurozone: Greece, Portugal, Ireland, Spain, Italy and Cyprus. GDP in these countries would fall between 15% and 20% more than in our baseline forecasts within a couple of years. The remaining Eurozone countries would also suffer very large declines in GDP.

Projected GDP loss vs. 2017 baseline forecast in percentage terms

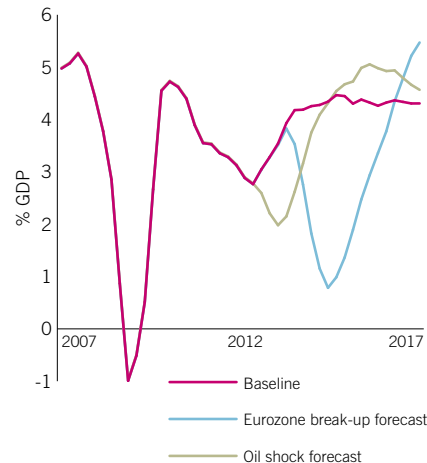


Among the emerging economies, the most affected markets are those in Eastern Europe with extensive trade and financial links to the Eurozone. The least affected are in Asia and Latin America.

### Middle East crisis

We also consider an acute increase in oil prices, approaching US\$250/barrel in the first half of 2013. While this is a smaller shock than a Eurozone break-up, such a scenario could have a big impact on consumer spending. Under this scenario, Chinese GDP growth falls to around 5.5% by mid-2013 and the US falls into a mild recession in 2013. The most affected markets are those heavily dependent on energy imports, such as Poland and Singapore. By contrast, oil-exporting countries such as Kazakhstan and Russia actually enjoy a boost to income even as the global economy enters a downturn.

Impact of current economic risk scenarios on world GDP



### Top ten markets' exposure to current economic risks

The accompanying graph indicates the exposure of the top ten countries in the Index to these risk scenarios. The line shows the 'baseline' level of sovereign risk, which can be read as an indicator of a country's resilience in the face of unexpected shocks.

A Eurozone break-up would have a dramatic negative impact on the world economy, but some emerging markets would be relatively unscathed, including Indonesia and South Korea. The top ten market most heavily exposed to the Eurozone is, of course, Turkey, by a large margin. But even Turkey is increasingly diversifying its trade links away from Europe and towards Asia and the Middle East.

In the event of an oil shock, oil rich economies such as Mexico and Russia would be the least affected. The impact on Indonesia would also be small. The most adversely affected would be Turkey and India, which are energy importers and already have large current account deficits.

## Case Study

**06** Success in emerging markets

**Paul McNicholl**  
Food and Beverage  
Global Co-head

As food and beverage companies expand their global presence, determining the right entry strategy is the first crucial step in securing growth in emerging economies.

**Paul McNicholl, Food and Beverage Global Co-head at Linklaters, discusses the implications of going it alone, partnering with a local player, or making a controlling acquisition.**

Growing organically in a new market can provide a high degree of control over brand management, quality, supply chain, business practices and intellectual property. However, it is also likely to take longer to establish a local market position and a lack of local knowledge and distribution networks could lead to expensive mistakes.

Those wanting to counter-balance such risks may consider the joint venture route. The secret to success in joint ventures (JVs) is to ensure that the economic interests of the partners are aligned for the life of the JV. That doesn't just mean giving the local partner everything they want. There must be "positive commercial tension" throughout the life of the relationship where each party remains interested in what the other has to bring.

At the beginning of a venture, no one wants to think about the break-up. But working out an exit scenario at the outset helps minimise legal risks and avoid disruptions. The cost of partner substitution is enormous, mostly because the end of the JV is unsettling to market presence. To avoid this, many firms like to cut 'step-up' deals that raise the foreign share over time. This both hedges risk and creates long-term sustainability.

Thinking about portfolio compatibility is also key. Local partners will often have a broader and larger business, and there is a risk of cross-subsidising that business. While local brands and international brands can sit comfortably together, there will often be competition at some price points, which can be unsettling – competing with your local partner is a sign of troubled times ahead.

When it comes to acquisitions, the most important factors are market environment and target selection. This entails understanding at the outset whether the key commercial value drivers for the acquisition can be secured quickly post-acquisition. This depends on a huge number of factors, from land ownership restrictions and the



availability of brand protection to the legal structures that enable the desired level of deal pricing and control.

For acquisitions therefore, post-deal integration is critical. This is true not just from a commercial perspective but from a risk management and governance viewpoint. The investor's internal skill set is extremely important but often overlooked. For instance, can human resources handle the secondment of senior employees? Can treasury manage currency hedges without inadvertently creating risks? Can internal audit deal with a foreign operation?

Whatever the chosen route, companies keen to realise the promise of emerging markets need to craft a strategy that is responsive to the constraints of, and the critical success factors of, each target country. Such flexibility is crucial to long-term profitability.

## Case Study

## 06 Yum! Brands in emerging markets



**Neil Thomson**  
VP Finance,  
Yum! Restaurants  
International

Yum! Brands is the biggest QSR (quick-service restaurant) player in the emerging markets. Its international division has recently been growing at 10% per year, and the company believes it still has ample room to grow in the emerging world.

**Neil Thomson, VP Finance, Yum! Restaurants International, discusses what makes his company's emerging-market positioning so successful.**

#### 'Equity leadership'

What is unusual about our emerging markets strategy is that Yum! is prepared to invest its own capital. This is an important ingredient in our success. We call it 'equity leadership'. Our China business was built with 100% equity ownership and it is a pure organic growth story. However, even in markets where we have local franchisees, for instance in India, our equity investment was the catalyst for exponential growth in our KFC Brand. It's a similar story for KFC in Russia, where we have invested equity and seen tremendous growth in unit sales volumes. There are a number of advantages for us in having our own capital invested. For example, we can ensure that we make the right decisions for the Brand, such as selecting the very best sites, over-hiring for great local talent or setting prices at a very attractive level for consumers.

Relying 100% on franchisees to lead growth means it is critical that you have the right partner. In our experience, a local partner will often be looking to make a return very quickly, and that doesn't always work in the emerging world where the economics can be challenging and you first need to establish your brand. In our industry, we find very few competitors who have

significant presence in more than 10 markets. They will often have pockets of strength in certain markets but the key differentiating factor between success and failure in a country is the selection of the local partner.

#### Critical success factors

When you start in an emerging market, it's often the case that only 10% or 20% of consumers can afford your brand. So you need to create ways to enable people to access your products, and that can mean being unprofitable for a while. In our industry, it is critical that we prove the concept first, then prove the business model, and then multiply that model through rapid unit development. But the initial stages require significant up-front investment and a willingness to invest over a long period of time. As a benchmark, we think of it taking around ten years before we reach the third stage of rapid unit development. So when we go into a market, we are not immediately looking at profitability. Instead we are looking at metrics like transactions, repeat business and customer preference for our Brand over local competitors that indicate whether our concept is working.

We don't always use our own equity. We have two ownership models that are 100% franchise models and are typically applied in markets which are smaller or where there is a challenging environment. For instance, in many parts of Africa, we are currently going into countries that no other western QSR company is in, because we want that first-mover advantage. We are doing that through local franchise partners. We incentivise our franchise partners to take a long-term brand-building approach by asking them to commit to a 20-year contract.



#### The Indian market

Our next challenge is India.

Normally we would want to start our Brands in the very largest cities in a country. However, we found the economics of skyrocketing rental rates in Delhi and Mumbai very unattractive. We developed a cluster approach, labelling the next five largest cities, where rental rates were half those of Delhi or Mumbai, as 'growth' cities, and that is where we focused our efforts. Our next cluster of cities were the 'emerging' cities, where we would plant a flag, and then 'future' cities which were not yet ready for our Brand. And over time, the 'future' cities will become 'emerging' and the 'emerging' become 'growth', and our market presence will develop.

Overall, we believe emerging economies can still deliver plenty of growth. In most emerging markets today, Yum! Brands has only one or two stores per million people. Our global benchmark is 20 stores per million people per Brand which is our level of penetration in the US. In China this means expanding from 4,000 stores today to between 10,000 and 20,000 stores as China develops.

## Case Study

## 06 SABMiller in emerging markets



**Nigel Fairbrass**  
Senior Vice President  
Communications  
and Reputation,  
SABMiller

SABMiller is unique among global leaders in the consumer goods sector in that its origins are in the emerging markets. Today, 70% of SABMiller's global revenues are from the emerging world. Latin America is the biggest regional contributor to the company's global earnings, producing over a third of earnings. But the company is most excited about Africa, where with its strategic partner, SABMiller controls over 60% of the African beer market.

**Nigel Fairbrass, Senior Vice President Communications and Reputation; Richard Farnsworth, Business Media Relations Manager; and Tristan Van Strien, Senior Investor Relations Manager at SABMiller talk about their successful partnership strategy in Africa.**



**Richard Farnsworth**  
Business Media  
Relations Manager,  
SABMiller

#### Choosing an entry mode

Our choice of entry mode has varied and generally been determined by legacy issues, rather than strategic considerations. The beer industry is dominated by a high degree of family ownership, and family ownership is usually sticky – they want to stay involved and are rarely going to sell 100%. We have a strategic partnership with the family-owned French firm Castel Group in 16 African markets. Additionally, many of our African assets are majority-owned assets with governments, acquired from privatisations.

The main disadvantage with a joint approach is simply financial: our brands in Africa are seeing incredible growth and we wish we had a bigger share of that. Other than that, the partnerships in Africa mostly have upsides. For instance, Francophone Africa can be more French than France, and Castel understands Francophone Africa.

The subsidiaries with government partners also have upsides. In the alcohol business, licence to trade and a rational tax environment are crucial. Having government partners helps with this. Doing business in Africa also involves much more community investment than



**Tristan Van Strien**  
Senior Investor  
Relations Manager,  
SABMiller

in other world regions. A government partner can make sure this is not wasted. For instance, our government partners have helped us to be effective on water sustainability issues in Tanzania – and water is, of course, critical for beer brewing.

#### Building competitive advantage

There are two reasons our competitive advantage is sustainable. The first is that brands have, if anything, more power in Africa. Most Africans have first-hand experience of truly bad, even dangerous, food and beverage products. They also don't have money to waste. That makes Africans, as a general rule, more loyal to brands they know and risk-averse to new brands.

SABMiller's sustainable advantage in eastern and southern Africa is also based on our capital-intensive approach. In many African countries, you are competing with the informal economy. Much home-made alcohol is truly awful, but people are price-sensitive. You need to invest enough to get to a scale that enables you to compete on price with home-made alcohol.

#### Mistakes companies make in Africa

A lot of companies tend to underinvest in



Africa because they are worried about risk. Even sophisticated global players can take a top-down approach, attempting to identify and pick off 'profit pools' from 10,000 feet. The markets in Africa don't work like that. For example, products such as beer are often very local. Trying to bring a global brand into a 'profit pool' just isn't going to work. A lot of companies also don't understand just how much innovation is going on in Africa. Adding Oreo flavour to breakfast cereals is not innovation; producing beer from an entirely new starch at a 30% cost advantage is.

The key challenge in Africa is keeping up the level of investment. Investing ahead of demand is very capital-intensive. Elsewhere in the world they're reading about pipelines being blown up, and we're asking for more money to put into Sudan. And the pace is extraordinary. We built a new brewery in Juba, South Sudan, and within 18 months it was running at capacity so we doubled it. It's now once again at capacity and we're coming back for more investment. So the global organisation as a whole has to believe in you.



## 07 Conclusion & contacts

Our Index reveals that the appetite of emerging markets for global food and beverage brands will continue to compensate for the drop in demand from the more developed economies.

While the BRICs continue to offer the greatest opportunities in terms of scale, other markets such as Indonesia, South Korea and Mexico are due to become increasingly more attractive to

most multinationals. Unsurprisingly, competition in these economies – from local, regional and international players – has increased in recent years.

The appeal of global brands is no longer enough. Although the potential to grow is there, it is important to remember that companies need to stand out in local markets: one size definitely does not fit all.

Issues such as the best route to market and choice of local partner can make or break an emerging market investment. When it comes to choosing an investment destination, balancing risk and opportunity is key, but ultimately success cannot be achieved without local knowledge.



Linklaters food and beverage network  
Rollover images for a short biography

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