Strategies for Asian business navigating a new era

Asian business leaders are optimistic about a new era, but most see the need for major strategic change.

by Chris Bradley, Nick Leung, Janet Pau, and Jeongmin Seong


September 2023

McKinsey & Company

McKinsey & Company is a global management consulting firm committed to helping organizations accelerate sustainable and inclusive growth. We work with clients across the private, public, and social sectors to solve complex problems and create positive change for all their stakeholders. We combine bold strategies and transformative technologies to help organizations innovate more sustainably, achieve lasting gains in performance, and build workforces that will thrive for this generation and the next.

Asia Business Council

The Asia Business Council is an independent organization of top executives, typically from leading Asian companies or multinational corporations with significant Asian operations. The council's goal is to provide a setting for members to think about how the private sector can contribute to Asia's continued economic development and competitiveness.

This report is authored by McKinsey & Company, in collaboration with the Asia Business Council. This research draws on multiple sources, including a survey among the members of the Asia Business Council. It reflects the views of the authors and does not necessarily reflect the views of individual Asia Business Council members or other contributors. This report contains proprietary information of McKinsey & Company and the Asia Business Council. Any use of the contents without specific permission of McKinsey and the Asia Business Council is strictly prohibited. All rights reserved.

Asia's business leaders should prepare themselves for potential turbulence as global dynamics shift and challenges escalate. Over the past three decades, Asia has reaped more benefits from a globalizing world than any other region, but that landscape is becoming more contested, and risks are rising. The region's rise to prominence could mean that it finds itself in the eye of the storm.

This article was developed by McKinsey, in collaboration with the Asia Business Council. It draws on new research from the McKinsey Global Institute (MGI), "Asia on the cusp of a new era," and features the results of a new survey conducted by the Asia Business Council, in collaboration with MGI and interviews of members of the Asia Business Council.

The survey reveals broad optimism among business leaders and a conviction that the region can maintain its momentum even in the face of disruptions and volatility. More than 80 percent of respondents say that they are optimistic about a new era for Asia. Among them, about 20 percent are highly optimistic, but many more—61 percent—are cautiously optimistic. One executive said, "Confidence coexists with uncertainty. Even top leaders are unsure of how unpredictable political and economic transitions will impact their strategy."

Business leaders were questioned about the potential impact of changing trends—a new era—on five dimensions identified by MGI as reflecting the most relevant and dynamic global trends (see infographic at the end of this article for some highlights of MGI's new research on these five domains in Asia). New challenges arise in each, including the following:

— *World order* covers the institutions, frameworks, and rules that shape international affairs—and that includes trade. Asia today is the world's trade crossroads, but it could find itself in the crosshairs of trade tensions. One survey respondent said, "In a more polarized world, companies need to evaluate and manage their exposures; should conflicts rise, they would need to have a plan."

— *Technology platforms* enable development and innovation. Asia has proved itself a consumer of technologies that rely on its manufacturing strength, but the value created by technology is moving beyond manufacturing into software and solutions. There is some catching up to do. Improving tech skills will be crucial. Another business leader said, "Many governments have grand desires and strategies, but until there is an improvement in education, it will remain a dream."

— *Demographic forces* change society. Asia has largely been in a demographic sweet spot, with a large pool of young workers and, regarding China and India, a productivity boom. But now the region faces a powerful headwind of aging, particularly in the highest-productivity economies of the Pacific Rim. A top executive from South Korea said, "Korea's manufacturing strength was due to its young, well-trained

A new survey reveals broad optimism among business leaders and a conviction that Asia can maintain its momentum even in the face of disruptions and volatility.

workforce, but now we need to pivot to higher-value-added industries."

— *Resource and energy systems* power our world. Asia's net-zero transition is bigger and arguably more challenging than that of any other region because it remains the world's industrial base and has surging energy demand. One survey respondent observed that stakeholders only take action when a "pain threshold" is reached, but by collaborating with public- and private-sector partners, it is possible to preempt that threshold. This will encourage change before the damage is done.

— *Capitalization* tracks economics, finance, and wealth. Asia has mobilized more capital in recent years than the rest of the world. It still needs more but offers relatively poor capital returns. This may not be sustainable if the cost of capital and balance sheet stresses rise. One Asian business leader said, "People overbank in Asia, so resources are not an issue. But if we look at how money is flowing, returns are poor and risks are high. Asia needs to improve its returns and long-term viability to tap more capital."

How will Asia's business leaders manage new challenges and complexity and build on the impressive momentum of their companies and their home region? The survey results give a sense of their thinking (exhibit).

Asian businesses surveyed fall into three broad groups.[1] A staggering 73 percent of survey respondents regard trends in more than three domains—even all five—to be "strategically critical," suggesting a recalibration of strategy on a broad front. Only 16 percent say that they think trends in one or two domains are relevant. Technology and energy and resources systems are considered to be more critical areas on which to focus. Just a small minority of respondents—about 10 percent—say that they believe they can take a business-as-usual approach, suggesting that none of the domains require a significant adjustment of strategy.

World order: Navigating rivalry and dependency in a multipolar world

Fast-growing Asian economies are emerging as prominent players in a multipolar world that is now reshaping the unipolar system that has been centered on the United States for 30 years. Asian economies are part of 49 of the world's 80 largest trade corridors. Asia is also home to 18 of the 20 fastest-growing corridors and 13 of the 20 largest. But more key players mean more complexity. There are increasing strains particularly regarding strategic goods and technology trade—notably, intangible flows such as intellectual property (IP)—and energy. There are disagreements not only between Asia and other parts of the world but also among Asian countries. For example, Japan stopped selling to South Korea key materials that they need to make chips. Business leaders could consider two priorities.

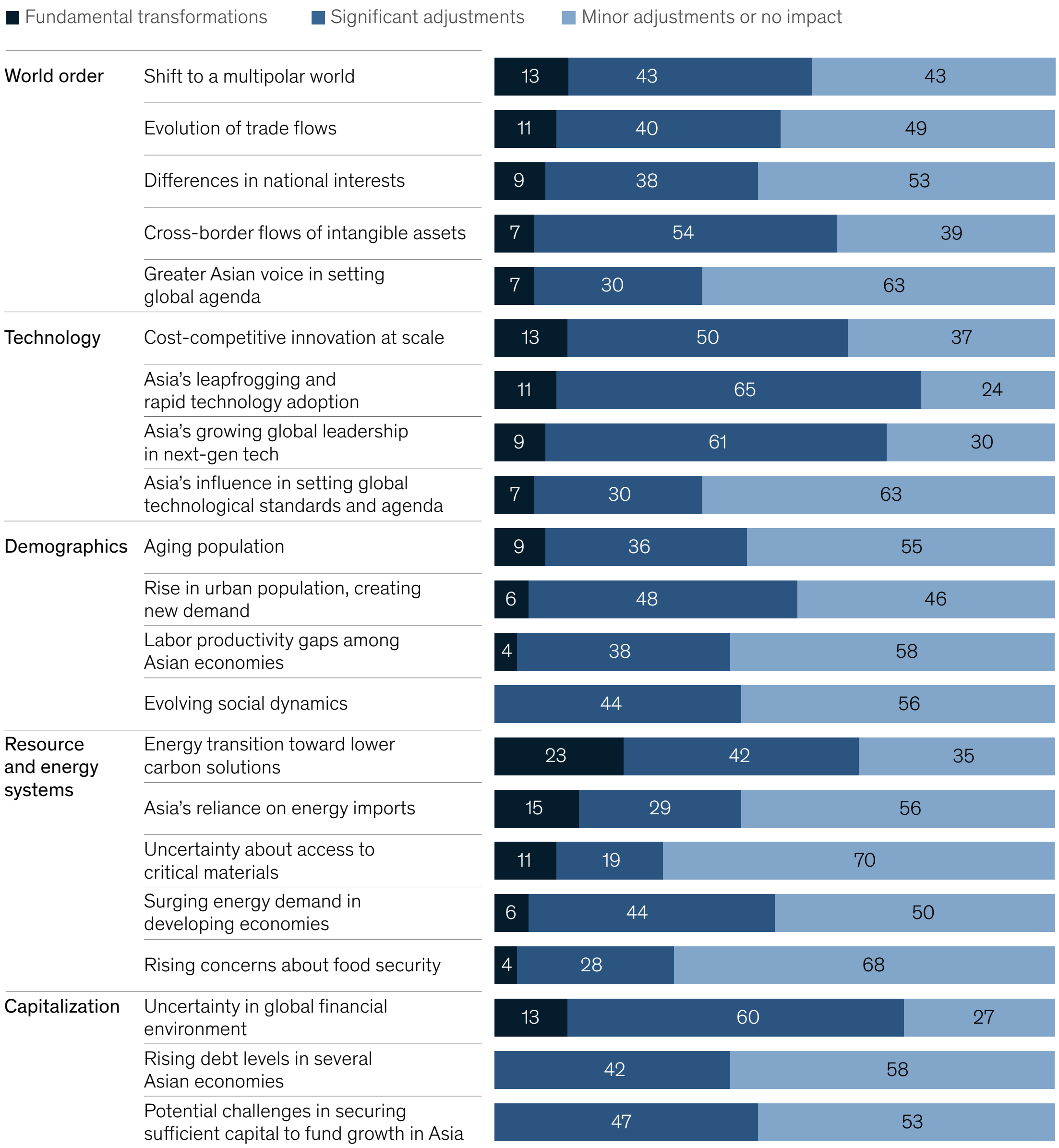
Shore up resilience amid risk of disrupted trade. In 2022, the International Monetary Fund (IMF) warned that geopolitical tensions could lead to strategic competition and national security concerns that could trump the shared economic benefits of global trade. It urged policy makers in Asia (and other regions) to ensure that trade continues to drive growth and to avoid adverse impact from fragmentation.[2] Business leaders can take a portfolio of actions to derisk. In areas where trade flows might be subject to restrictions, they could develop privileged supplier relationships, diversify key steps of supply chains, redesign products to substitute critical inputs, and localize operations to serve specific markets in a nimble way.[3]

[1] We considered a domain to be strategically critical if each survey respondent chooses at least one area of fundamental transformation or two areas of significant strategic adjustment out of several questions in a given domain. Companies are grouped into three categories: those with no strategically critical domain, those with one to two strategically critical domains, and those with three or more strategically critical domains.
[2] IMF analysis has found that a typical shock to trade policy certainty, like the 2018 buildup of US–China tensions, reduces investment by about 3.5 percent after two years and GDP by 0.4 percent. See *Regional economic outlook for Asia and Pacific*, International Monetary Fund, October 27, 2022.
[3] "The complication of concentration in global trade," McKinsey Global Institute, January 12, 2023.

Exhibit

Survey respondents highlight strategically critical areas in five domains.

Reported impact on business strategy, % of respondents (n = 49)



Note: Figures may not sum to 100%, because of rounding.
Source: Asia Business Council survey, July 2023

McKinsey & Company

Leverage complementarity. Asia has become a very significant regional trading power on the back of complementary comparative advantage. But some of Asia's trade corridors—where a product comes from and goes to—are now so concentrated that this teeters on dependency. These corridors could be tested when tensions arise. One example of concentration within Asia's trade is the fact that in 2021, 59 percent of steel material trade flowed between a single route from Australia to China, the latter accounting for 57 percent of global crude steel production.[4]

Views from the boardroom

Asia's business leaders were asked to what extent their business strategy might be influenced by the following five elements: differences in national interests, a shift to a multipolar world, the evolution of trade, cross-border flows of intangible assets, and a greater Asian voice in setting the global agenda.

More than 50 percent of respondents say that a shift to a multipolar world and cross-border flows of intangible assets calls for significant strategic adjustment or fundamental transformations. One business leader said that his company needed to "operate like a local enterprise while harnessing international resources."

Cross-border flows of intangible assets—such as IP, research, technology and software, and human capital—are the elements that the largest share of respondents say may require significant adjustment or fundamental transformations to strategy. This appears to reflect the growing importance of intangible assets to business performance.[5] MGI research in 2022 found that cross-border flows of IP grew about twice as fast as goods flows in 2010–19, while data flows grew at nearly 50 percent annually.[6]

Technology platforms: Boosting innovation amid barriers to knowledge flows

Corporate Asia is already adopting digital technologies faster than anywhere else in the world and is beginning to develop strength in IP and software. But over the coming decade, there will be a need to develop capabilities allowing for continuous use of those technologies to propel cross-sector opportunities and monetize the huge data pools that are being created.[7] Business leaders could consider two priority areas.

Access critical technology. Asia should manage dependency on imported technology to ensure that it sources the technology it needs. In a digital-first world, technology is one of the most acutely strategic of goods, and Asia depends heavily on imports of core technology. China, for instance, imports three times more IP than it exports.[8] As such, the region depends on the free flow of technology. One instance is the 2022 announcement of new controls on US exports to China of some high-end semiconductor devices. Technology supply chains are global, but several countries have been seeking to shore up homegrown manufacturing of strategically important technologies, including semiconductors, as a hedge against interruptions to supply chains.[9] The potential for the free flow of technology to be compromised is even more of a challenge because the value created by technology is shifting notably from hardware to software and solutions. Asia needs to improve its positioning to keep pace with that shift.

Leapfrog in innovation. Asia needs to leverage its scale and speed to continue to leapfrog in innovation while securing access to high-quality talent. Thus far, the region's economies have excelled in areas of technology that rely on its strength in manufacturing, such as consumer and industrial electronics, electric vehicles, and semiconductors. The region accounts for more than 40 percent of the world's top companies' share of global revenue, R&D spending, and patents in the four arenas.

But it's less well positioned in a range of transversal technologies such as artificial

[4] *World steel in figures 2022*, World Steel Association, May 2022.
[5] "Getting tangible about intangibles: The future of growth and productivity?," McKinsey Global Institute, June 16, 2021.
[6] "Global flows: The ties that bind in an interconnected world," McKinsey Global Institute, November 15, 2022.
[7] "Building 21st century companies in Asia," McKinsey, January 19, 2022.
[8] "How Asia can boost growth through technological leapfrogging," McKinsey Global Institute, December 2, 2020.
[9] China, the European Union, Japan, South Korea, and the United States have all announced measures to bolster domestic value chains. See "Global flows," November 15, 2022.

intelligence, cloud and edge computing, clean energy, and quantum technologies, which permeate into virtually every sector.

Leadership is contested. The United States is ahead on cloud and edge computing and quantum technologies. Asia has established a strong position in clean energy and mobility technologies

To make more headway, improving the quality of Asia's technological and scientific talent will be vital. Between 2016 and 2018, Asia was home to more than three-quarters of the world's STEM graduates, and that share is expected to remain high. But the quality of those graduates hasn't always been high enough to push ahead on frontier tech.

Views from the boardroom

It's not surprising that technology is on the minds of Asia's business leaders. More than two-thirds of respondents to the Asia Business Council survey indicate that their strategy needs to adjust significantly to enable two elements: leapfrogging and rapid technology adoption and regional leadership in next-generation technology.

More than 70 percent of respondents say that they see the need for significant adjustment or fundamental transformation in view of Asia's leapfrogging in technology adoption, and more than 70 percent in the case of Asia's growing leadership in next-generation technology.[10] Respondents highlighted the importance of shifting from "innovation by tech" to "innovation by science," and said that enhancing the quality of talent was crucial, particularly in emerging Asian markets.[11] Another said, "Except for perhaps China, Asia has been a consumer of technological innovations, not a producer. The talent drain to the West impedes technology production, but the growing economic opportunities of Southeast Asia may bring back Asian STEM talent for innovation and commercialization."

Demographic forces: Raising productivity to cope with aging and drive industrialization

In recent decades, Asia has largely been in a demographic sweet spot. Asia's stellar growth was powered by an abundance of young workers coupled with a very significant productivity boom—all aided by urbanization that provided a huge labor supply shock for the world's industrial workforce. Between 1990 and 2022, more than half of the world's growth in the working-age population was in Asia.[12] The region's large-scale migration from rural to urban areas was a huge, positive supply shock. But parts of Asia are aging rapidly—and the demographic landscape is shifting. Two challenges that demand a response stand out.

Address labor mismatches. Asia's most productive economies are aging. China and advanced Asian economies, such as Japan and South Korea, are aging twice as fast as those of Europe and the United States. Theoretically there are still enough young people to continue to fuel growth, with many still working on farms. But they are not in the right places to ensure that Asia's productivity boom continues. The most young people are in less-productive economies; the least in high-productivity economies. So, Asia's task is to spread the high-productivity formula across the region, shifting where work takes place and raising the productivity of those that today lag behind.

Drive a productivity revolution across Asia. A large productivity gap separates Asia's advanced and less advanced economies. For instance, the nonfarm productivity of advanced Asian economies is about eight times that of India. Asian business leaders need to consider how they can drive productivity in their organizations by, for instance, adopting more digital solutions, raising skills, and using innovative strategies to retain productive workers.

---

[10] Corporate Asia is already adopting digital technologies faster than anywhere else in the world, and over the coming decade there will be a need to develop capabilities to use those technologies continuously to drive cross-sector opportunities and monetize the huge data pools that are being created. See "Building 21st century companies in Asia," January 19, 2022.
[11] A McKinsey survey of 3.5 million job postings in the 14 most important technology areas for 2023 found that many of the skills in greatest demand have less than half as many qualified practitioners per posting as the global average. See Michael Chui, Mena Issler, Roger Roberts, and Lareina Yee, "McKinsey Technology Trends Outlook 2023," July 20, 2023.
[12] UN population database; the working-age population is defined as those aged 15 to 64.

Views from the boardroom

Productivity is an issue on the minds of Asia's business leaders, with 42 percent of respondents recognizing that they may need to make either significant or fundamental adjustments to their strategy to tackle labor productivity gaps among Asian economies. One executive described demographics as the "Achilles' heel of Asia" in light of some economies' hesitation about immigration. More than 50 percent of respondents say that there were significant strategic or fundamental implications for their companies resulting from Asia's rising urban population.

Although only 45 percent of respondents say that they intend to make fundamental or significant strategic adjustments due to aging, business leaders acknowledge the pivotal role of technology—embracing robots, AI, and digital tools—in counteracting the effects of the demographic shift and enhancing productivity. One respondent said, "Automation, robotics, and simplified processes will be a must to boost productivity."

Resource and energy systems: Securing a lot more energy with a lot less carbon

Asia is the world's top energy consumer—and carbon emitter—but still needs a great deal more to support continued industrialization and the needs of consumers. There are two major challenges. First, Asia relies heavily on energy imports. China, India, and Japan source approximately 90 percent of their oil and gas from abroad. Second, the prospect of a continued surge in energy demand comes at a time when Asia plays its part in the global energy transition. So Asia has a dual imperative.

Secure energy supply. In the years ahead, Asia will need a great deal more energy. On the back of strong growth, Asia's share of all the energy consumed by the world has more than doubled in 40 years. In a new era, demand will remain strong for two reasons. Per capita energy consumption is still only about one-third that of the average of the OECD economies. Industry has a greater weight in Asia's economies than anywhere else in the world, and industry is a voracious energy consumer. In 2021, Asia's industry consumed 57 percent of the energy of all industry in the world, according to McKinsey Energy Solutions. In a more contested world, Asia may need to work even harder to ensure that it gets the energy it needs, strengthening trade relations with energy exporters both in Asia and globally. Bolstering investment in more efficient energy technologies is another key priority.

Pursue decarbonization. While securing considerable energy resources, Asia also needs to press ahead with the energy transition. Doing both simultaneously is challenging. Industry is the most challenging sector to decarbonize, suggesting that fossil fuels will remain part of Asia's energy mix for some time—even while use of renewables ramps up. Several executives emphasized the need to double down on the energy transition in response to consumer and voter demands for action to tackle climate change. Asia's businesses have a large opportunity to identify and invest in clean-energy innovations and to position their companies as pioneers in new, scalable solutions that can be exported globally.[13] And energy efficiency can help solve the energy demand issue as well as decarbonization.

Views from the boardroom

The energy transition and the need to tackle climate change is the aspect that respondents say will require the largest transformation to their strategy. Sixty-five percent of those surveyed see the need for significant strategic adjustment or fundamental transformation in this area. Several business leaders noted that Asia's actions in the energy arena will have a large impact on the world and that Asia may be the first to define an accelerated path beyond fossil fuels. They observed that the region had put a lot of capital into—and backed champions of—innovation, and that this is good news for the world. Another executive said that if effective incentive frameworks are in place, the private sector will naturally follow.

[13] McKinsey research has found that the addressable market size for green business in Asia is expected to be between $4 trillion and $5 trillion by 2030. See Ashwin Balasubramanian, Jun Hao Chua, Tomas Nauclér, and Daniel Pacthod, "Green growth: Capturing Asia's $5 trillion green business opportunity," McKinsey, September 14, 2022.

Asia's business leaders can play a more important role in standard setting—for Asia and the world. The current ecosystem for the green transition is rather fragmented, with no one set standard. Asia's sheer size calls for proactive global leadership to streamline fragmented global practices around the energy transition.

Another business leader noted, "Asia's large carbon footprint makes it a major player in the carbon credit market. There is potential for trading of carbon credits within Asia, especially between carbon-producing and carbon-offsetting countries."

Asia's business leaders can play a more important role in standard setting—for Asia and the world. The current ecosystem for the green transition is rather fragmented, with no one set standard. There are, for instance, different methodologies in certification programs. Asia's sheer size calls for proactive global leadership to streamline and align fragmented global practices around the energy transition. One business leader observed, "Standards today primarily come from Western global organizations, but Asia is now the majority, and collaboration between organizations and entities could pave the way for Asian organizations to shape global standards."

Asia's reliance on energy imports was another point of concern for respondents; more than 50 percent of them say that they see the need for significant strategic adjustment or fundamental transformations.

Capitalization: Mobilizing capital amid financial stress

In many economies, interest rates and inflation have risen, and there are signs of stress in the balance sheets of governments, households, and corporate players. These are potential headwinds to the continued capital deepening that Asia needs to maintain its growth momentum.

Asia has deepened capital the most among—and more quickly than—other regions, benefiting from high domestic savings and large volumes of foreign investment. But that was during a time when the macroeconomic environment was stable, with low interest rates and low inflation. Potentially, Asia could mobilize more capital between now and 2030 than any other region, but this time against a more challenging macroeconomic backdrop. This suggests two priorities for Asia to consider.

Make financial and capital markets more efficient. Asia's financial and capital markets must be sufficiently efficient and dynamic to mobilize and allocate the capital that Asia's economies need. There is a lot of work to do. Returns on capital have been lower than those in Europe and the United

States.[14] Between 2015 and 2019, North America generated 30 times more economic profit than Asia, previous MGI research has shown.[15] Beyond centers such as Hong Kong and Singapore, many of Asia's financial systems are underdeveloped.

Bolster balance sheets. There is a greater need for further resilience and risk management measures in a less certain new environment. While a lot of good work was done by Asian companies after the Asian financial crisis and by governments that built up solid stocks of foreign exchange reserves, there's still a strong need for companies to reinforce their financial positions by identifying key indicators to watch, planning for a sufficiently broad and long-term set of scenarios, and testing and strengthening risk management approaches.[16]

Views from the boardroom

Asia's business leaders are clearly mindful of the need to adjust strategy, with 73 percent of those polled anticipating the need for significant or fundamental transformations in this domain. One business leader said that macroeconomic trends may remain challenging, and that improved corporate governance was the way to ensure differentiation and to continue access to funding.[17]

Business leaders work at the sharp end, tracking trends in their region and beyond. While changes along many of these dimensions may be more complex for any individual business to tackle, business leaders could shape Asia's future together. Businesses have considerable power to shape the future when they collaborate. The challenge is to do so proactively rather than in response to events.

Asia's business leaders appear to share a high degree of confidence in prospects for their region even in potentially turbulent times, suggesting an appetite to be in the vanguard of the response to both the opportunities and risks of the period ahead. The choices they make could well have global consequences.

Chris Bradley is a director of the McKinsey Global Institute (MGI) and a senior partner in McKinsey's Sydney office, **Nick Leung** is a senior partner in the Hong Kong office, and **Jeongmin Seong** is an MGI partner in the Shanghai office. **Janet Pau** is executive director of the Asia Business Council.

The authors wish to thank Nienke Beuwer, Sonja Cheung, Debadrita Dhara, Cathy Gui, Vasudha Gupta, Kathryn Haynes, Gabriel Huang, Christine Jeong, Jeyachandran K, Rebeca Robboy, Rachel Robinson, and Peixi Wang for their contributions to this article.

Designed by Global Editorial Services
Copyright © 2023 McKinsey & Company. All rights reserved.

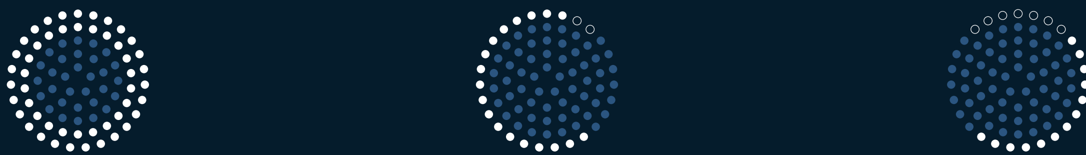
---

[14] Marc de Jong, Tido Röder, Peter Stumpner, and Ilya Zaznov, "Working hard for the money: The crunch on global economic profit," *McKinsey Quarterly*, April 21, 2023.
[15] "The future of Asia: Decoding the value and performance of corporate Asia," McKinsey Global Institute, June 3, 2020.
[16] *The future of growth and wealth hangs in the balance*, McKinsey Global Institute, May 24, 2023.
[17] McKinsey research on more than 1,000 publicly traded companies in North America and Europe found that the companies that proved most resilient to the financial crisis that began in 2008 had one common factor: they moved quickly. Resilient companies also had cleaned up their balance sheets before that crisis, enabling them to engage in programmatic M&A, divesting more than others during the ensuring downturn, and acquiring more during the subsequent recovery. See Gautam Kumra, "How Asian business leaders can prepare for a volatile future," McKinsey, September 16, 2022.

A new era for Asia in five domains

1 World order

Asian economies are part of 49 of the world's 80 largest trade routes



49 of the world's 80 largest trade routes by value involve Asian economies

18 of the world's 20 fastest-growing trade routes involve Asian economies

13 of the world's 20 largest trade routes by value involve Asian economies

However, they depend on a few complementary and concentrated products

90 percent of the world's nickel trade flowed into Asia

85 percent of the world's steel materials trade involves Asia

33 of the world's largest 40 chip trade corridors involve Asia only

70 percent of the world's liquefied natural gas imports flows to 5 economies in Asia

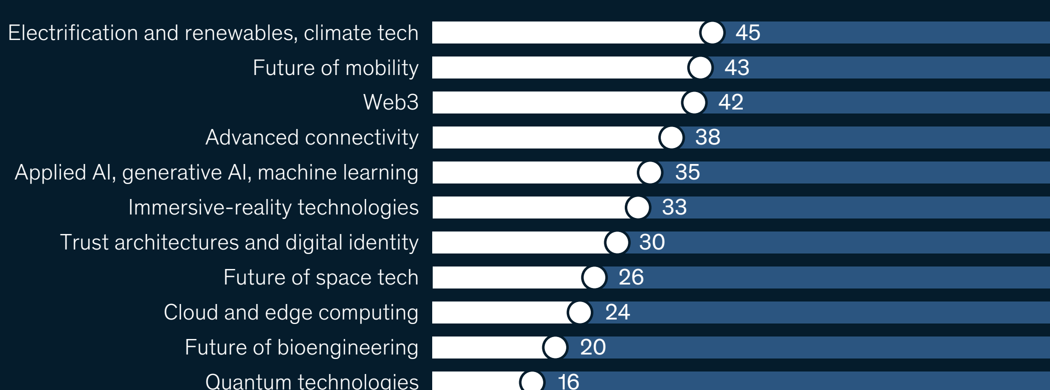
2 Technology platforms

Asia has been the world's hub for manufacturing-related tech

Asia's share of revenue in the top 3,000 global companies, by industry, 2020, %

Asia needs to continue building presence in transversal technologies

Asia's share of world-class patents in transversal technology, 2019, %

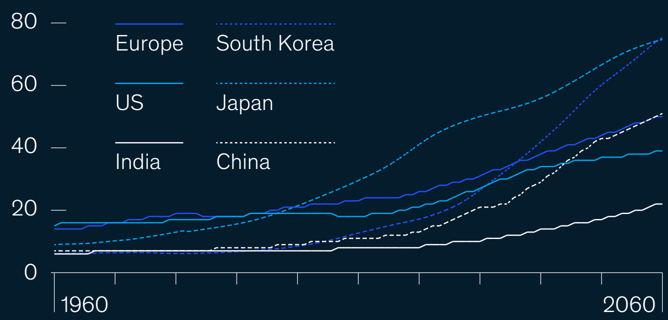


McKinsey & Company

3 Demographic forces

Asia is home to some of the world's most rapidly aging economies

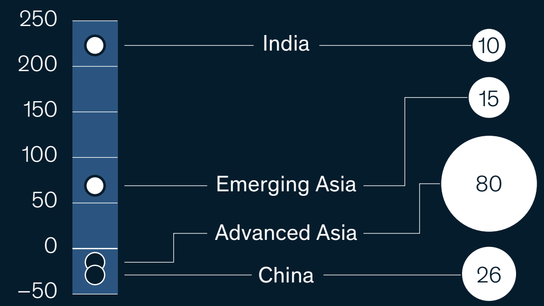
Number of individuals over 65 years old, per 100 working-age people



Asia's workforce will grow in less productive places

Change in nonfarm workforce, 2022–50, million people

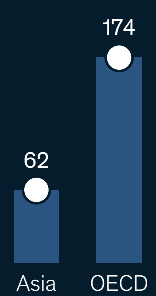
Nonfarm productivity, 2022, $1,000 per person



4 Resource and energy systems

Asia is 'underenergized' today

Energy consumption per capita, 2019, gigajoules



Asia faces an uphill battle of energy transition due to high industry usage

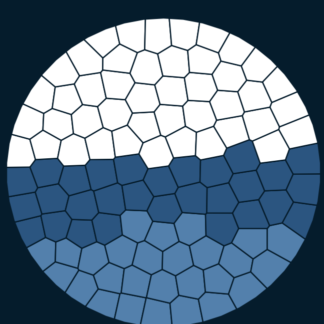
Industry's share of total final energy consumption by region, 2021, %

5 Capitalization

Asia is expected to mobilize more capital than EUR and US combined

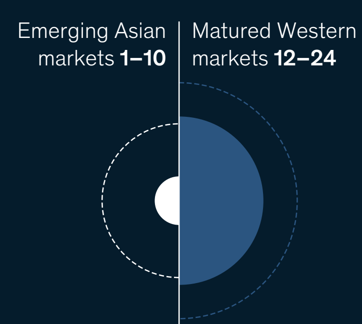
Share of incremental total fixed investment, 2020–30, %

- Asia **44**
- Europe and US **29**
- Rest of world **27**



Asia will need to continue developing depth of financial market

Value of bonds and equity as a share of GDP, 2020, %



McKinsey & Company