Mint condition

15 December 2014

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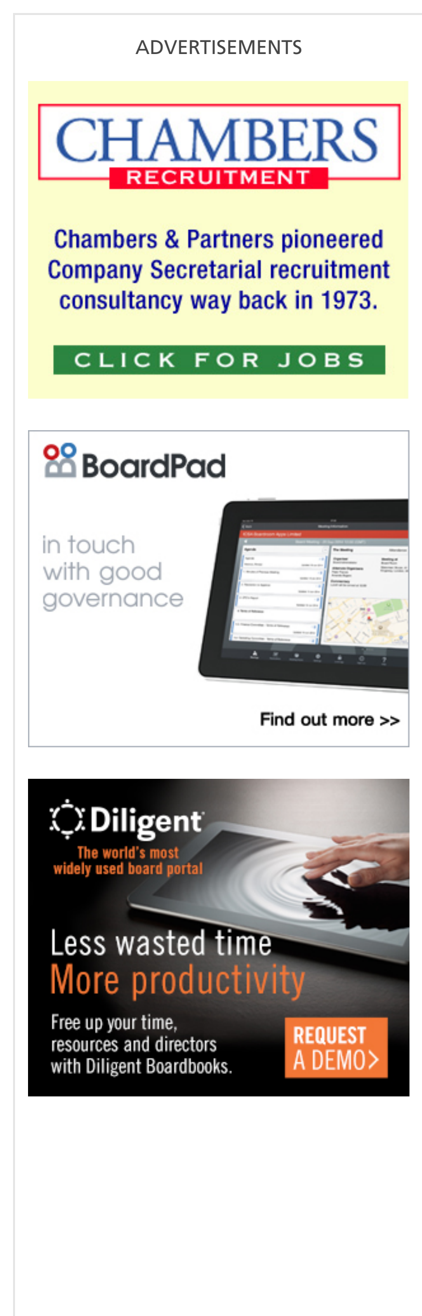

The markets of Mexico and Indonesia present opportunities and risks

Much has been written about the potential and economic performance of the BRIC countries – Brazil, Russia, India and China. As growth in these markets slowed, the question being asked was where next? Investor attention began to shift to other so-called frontier markets, particularly the MINT countries – Mexico, Indonesia, Nigeria and Turkey.

Goldman Sachs economist Jim O'Neill predicts that the MINT countries will be the next economic giants to emerge. Focusing on Mexico and Indonesia, both of these countries offer huge potential.

They are rich in commodities, geographically well located and their own consumer markets are ripe for development. As a number of major international corporations have discovered, however, the challenges of operating in these markets can lead to reputational damage and high profile investigations much closer to home.

Mexico

According to the International Monetary Fund, Mexico should become the 10th largest economy in the world in 2015 and analysts predict that it will be the seventh largest by 2050. In Latin America, it is the largest economy after Brazil and GDP per capita is larger than the other nations in the BRIC group.

Trade between the UK and Mexico is significant; in 2011, the UK Government put the figure at $12.2 billion. Monetary policy has been accommodating, the exchange rate has remained stable and investor confidence is currently on an upward trajectory. Structural reforms to energy, finance and telecommunications should boost productivity and growth still further.

> *Mexico offers a market equivalent to Western*

> *Europe and a bridge between Latin America, the US and Canada*

For UK companies wishing to export to Mexico, it offers a market equivalent in size to Western Europe and provides a bridge between Latin America, the US and Canada. It is a member of the OECD and interestingly, has more free trade agreements than any other country – 12 agreements covering 44 countries.

The main areas for UK businesses operating in Mexico are aerospace – Mexico's aerospace sector has grown around 20% annually for the last seven years – healthcare, retail, infrastructure and energy.

Corruption and bureaucracy

According to the World Economic Forum Global Competitive Report 2014–15, the three most problematic factors when doing business in Mexico are corruption, tax regulations and inefficient government bureaucracy. Obtaining permits can be burdensome and time consuming. Registering property and gaining access to utilities can be long and arduous – the World Bank ranks Mexico at 130th place in the world for ease of gaining electricity. Financial practicalities such as obtaining credit and paying taxes can also prove difficult.

It is not surprising perhaps – given the complexity of obtaining permits, licences and contracts – that corruption presents a real problem for business. This is made all the more challenging by the fact that both the police and the judiciary have a reputation for being corrupt and are believed to be involved in a wide range of illicit activities, including organised crime, extortion and drug trafficking.

According to Transparency International, Mexico ranks 106 out of 177 in its Corruption Perceptions Index 2013 and a recent world integrity study estimated that Mexico lost $462 billion from its economy in 2011 due to crime, corruption and tax evasion.

With the extra-territorial reach of the UK Bribery Act and the US Foreign Corrupt Practices Act (FCPA), businesses need to understand their exposure to corruption risks in Mexico and to evaluate their procedures to ensure their effectiveness.

Mexico, like many Latin American countries, has strengthened its anti-corruption laws. The Federal Law Against Corruption in Public Procurement, which came into effect in June 2012, is analogous with much of both the Bribery Act and the FCPA. It holds individuals and companies accountable for offering money or gifts to obtain a business advantage in the procurement of public contracts from the Mexican Government.

The law applies to Mexican and non-Mexican companies and individuals engaged in federal government contracting in Mexico. This includes bidders, participants in tenders, suppliers, contractors, permit holders, concessionaires, their shareholders and agents. Penalties for infringement will be high, ranging from $5,000 to $250,000 for individuals and from $50,000 to $10 million for companies. However, the law also provides for plea-bargaining as an acceptable means of resolving a case. If the plea is entered during the investigative phase, the monetary penalty may be reduced by up to 70%; if it is entered during sanctions, by 50%.

This law was introduced to strengthen the regulatory framework and incorporate international standards regarding government procurement. It does not replace existing law. Corrupt practices are also addressed by the Codigo Penal Federal, which criminalises attempted corruption, passive and active bribery, extortion, bribing a foreign official, abuse of office, money laundering and facilitation payments.

Enforcement and reform

As with much anti-corruption legislation, enforcement is the real issue. According to the World Economic Forum Competitiveness Report 2013-14, business executives

state that it is common for public funds to be diverted to individuals, groups or companies in the form of corrupt payments. Transparency International's most recent survey revealed that 92% of Mexicans feel that corruption has increased or stayed the same over the past 12 months. Although the current president appeared determined to implement reform, announcing plans for an Anti-Corruption Commission within weeks of taking office, this is currently being held up in the Chamber of Deputies, despite being approved in the Senate much earlier.

Companies doing business in Mexico, either directly or through a Mexican affiliate should ensure that their anti-corruption procedures comply with local as well as the more well-known FCPA and Bribery Act requirements – in particular they need a detailed understanding of the many parties that can be involved in any bidding process.

Indonesia

Ranked 114 out of 177 in the 2013 Transparency International Corruption Perceptions Index, Indonesia can be a challenging part of the world in which to do business. However, as the largest country in South East Asia, with 240 million inhabitants and predicted to become the fifth largest economy in the world by 2030, it should not be ignored.

Indonesia's economy has enjoyed a growth rate of 5–6% per annum for the past 10 years – a more stable rate than any of the BRIC or OECD countries. It is rich in natural resources, providing huge opportunities in the extractives sector. There is also considerable scope in infrastructure and transportation, power generation, renewable energy, advanced engineering as well as healthcare, education and financial services.

However, doing business in Indonesia is far from straightforward. The UK government advises that companies need to invest time and resources, paying regular visits over many months and sometimes years before seeing returns.

In particular, as the SFO investigation into Rolls Royce shows, businesses must be wary of the corruption risks associated with operating here. Although Indonesia's government has improved measures to combat corruption over the past 10 years, it remains a major deterrent to foreign investment. According to Transparency International, perceptions of corruption in Indonesia are worsening.

Abuse of office

The most common offences are abuse of office, money laundering and bribery. Foreign companies report that red tape and widespread extortion present a major challenge for doing business in Indonesia. Irregular payments are routinely demanded in connection with imports and exports, public utilities and tax payments, as well as the awarding of contracts, permits and licences. Facilitation payments are illegal under Indonesian law, but routinely demanded – companies report real difficulty in determining whether or not their payments to government officials are legal. Obtaining official receipts can be difficult and per diem is a potential problem. Officials are entitled to per diems for site inspections; however, the law does not specify whether it is the government or the company who is responsible for paying. Companies are often asked to pay per diems over a weekend for a site visit on a Monday morning.

Gifts and hospitality can be another challenging area with dinners and other forms of entertainment widely expected. A strong policy that is regularly reinforced is essential to ensure that all staff follow the correct guidelines.

Indonesia's government recognises that corruption is an impediment to foreign investment and therefore a huge cost to the national economy. The Anti-Corruption Commission, known as the KPK, was established in 2012 and has evolved into an independent, resilient and effective institution in the investigation and prosecution of corruption among public officials. However, it handles only a small percentage of the corruption cases with the Attorney General's Office and

the police handling the majority, typically resulting in lower conviction rates and more lenient punishments.

Mitigating risk

Indonesia and Mexico offer risk and reward in equal measure. A robust and strictly enforced anti-corruption policy is essential. Senior management operating in these markets need head office support and the opportunity for regular review. They must demonstrate their commitment to a zero-tolerance approach and, in Indonesia in particular, build contingencies into their business plans to allow for the additional time that this necessitates.

Before entering either market, organisations should conduct a detailed assessment of the corruption risks their business might face and ensure that anti-corruption procedures are sufficiently robust and, if necessary, adapted to mitigate all possible risk. Training and communication will be essential to ensure that the company’s expectations are made clear. Repeated communication of the company’s position on facilitation payments can reduce the prevalence of demands.

In both countries, the use of third parties can be problematic, so risk-based, anti-corruption due diligence is needed to provide sufficient information on any third parties contracted to act on your behalf. Anti-corruption clauses and where possible auditing rights should be included in third party contracts and, if appropriate, e-learning or training on anti-corruption compliance could be offered.
To avoid the reputational damage and financial penalty of an investigation, anti-corruption compliance must be put in place. It will need time and resources, but with the right approach can have a positive effect.

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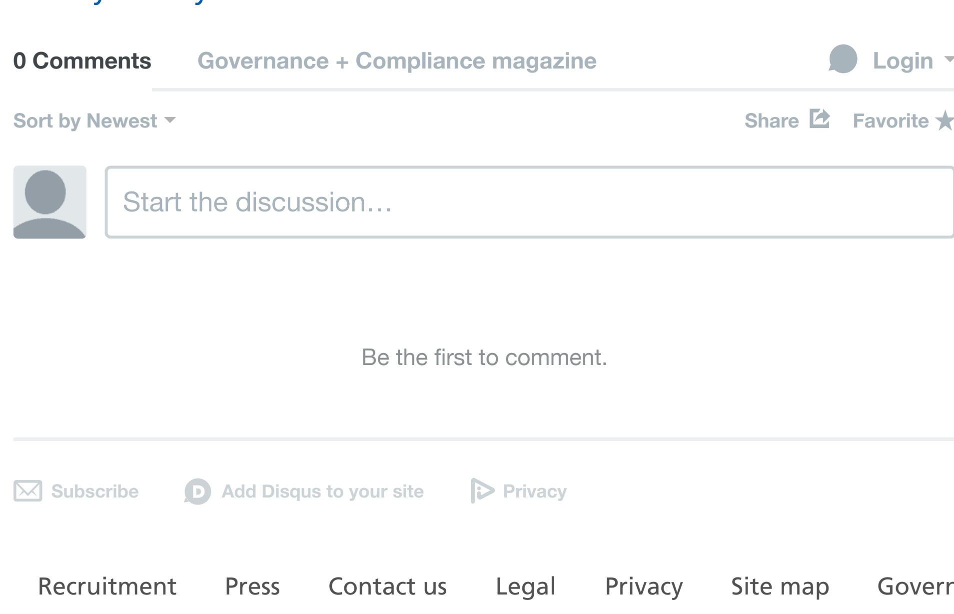

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