

think:act **CONTENT**






Fresh thinking for decision makers

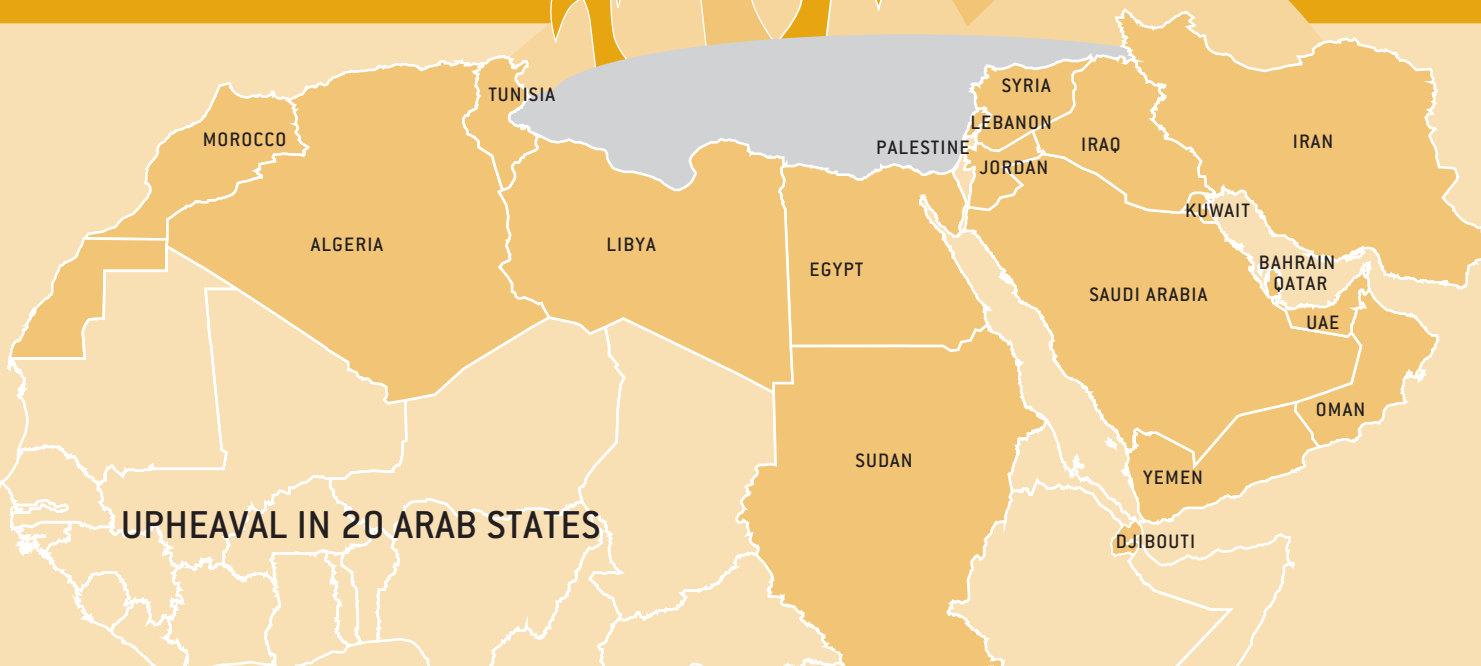
Upheaval in the Arab
world |

SCENARIO UPDATE MARCH 2011

What this
means for German
firms | Survey of
German executives |
"Oasis", "Sandstorm"
or "Desert"?

MENA AT A GLANCE

INDICATORS	RANKING			FOR COMPARISON				
	1.	2.	3.	Tunisia	Egypt	Libya	20.	Germany
 ECONOMIC POWER Real GDP 2010, EUR bn	Saudi Arabia 272.6	Iran 179.8	UAE 133.3	Rank 11 27.5	Rank 4 94.9	Rank 9 44.4	Palestine 0.9	2,227.8
 DYNAMIC Avg. GDP growth 2000-2010 p.a., %	Qatar 11.5	UAE 8.5	Bahrain 6.1	Rank 11 4.5	Rank 7 5.0	Rank 13 4.2	Palestine 1.1	1.1
 POPULATION 2010, m	Egypt 86.2	Iran 75.9	Algeria 36.3	Rank 9 10.5	Rank 1 86.2	Rank 11 6.7	Djibouti 0.9	81.8
 OIL PRODUCTION Barrels/day 2010, m	Saudi Arabia 9,713	Iran 4,216	VAE 2,599	Rank 14 86	Rank 10 742	Rank 7 1,652	Yemen 14	n. v.
 UNEMPLOYMENT 2010, %	Tunisia 14.0	Iran 13.2	Jordan 12.5	Rank 1 14.0	Rank 7 9.7	n. v.	Qatar 0.5	7.7



UPHEAVAL IN 20 ARAB STATES

Three weeks ago we published our latest economic scenario, "Three times three percent", which forecast three years of 3% GDP growth in Germany. The basis for this optimistic view was that our export markets are growing strongly, the domestic economy is providing fresh impetus and all signs point to Germany being able to exploit its fundamental strengths over the next few years. Our optimism has not changed significantly over the past few weeks. But when we produced our scenario, the dramatic situation in North Africa was not yet fully apparent. The consequences for German companies and the German economy as a whole are now becoming clearer. That is why we decided to publish a quick update.

After the protests and changes of government in Tunisia and Egypt, the situation is being repeated in almost a dozen Arab countries – Libya is currently only the most dramatic example. But where is this all going? The region's future does not depend so much on the consequences of the "Day of Rage" protests in Tunisia, Egypt, Libya, Morocco, Algeria, Syria, Bahrain and Yemen and the new power structures that emerge. Instead, the critical question is what will happen in Saudi Arabia, the region's resource-giant. Will there be increasing Islamization? And what new political and economic freedoms will emerge – if any? The latter is particularly relevant to us Europeans, as a neighboring region, and may be an opportunity for Europe.

We are not attempting to paint a comprehensive [political] picture of the situation in the Arab world here. Instead, we are focusing on the economic impact. That is why we have conducted a survey among 100 German managers over the past few days that shows what fallout German companies are currently dealing with, what they expect over the next few months and what long-term strategic challenges they face. We have also developed three economic scenarios for the Arab world – "Oasis", "Sandstorm" and "Desert" – which we need to be prepared for.

THE MIDDLE EAST AND NORTH AFRICA AT A GLANCE

This region – often abbreviated as "MENA" – comprises 20 Arab states from Morocco in the west to Iran in the east. It rarely receives attention in business terms, given the existence of the powerful G3 (USA, Europe and Asia) and the dynamic BRIC countries. But it accounts for 3.1% of global economic output and is home to 380 million people, almost as many consumers as Western Europe, and has 68% of the world's oil and 44% of the world's gas reserves. But oil and gas are not everything – the MENA countries also play a prominent role in the tourism, finance and logistics industries. Finally, the region is of strategic importance, with the Suez canal in Egypt and US military bases in the Gulf.

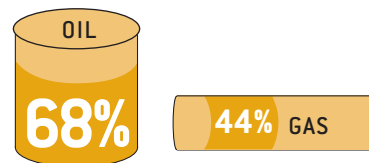
Dynamic economic growth of 4.5% on average over the past five years also highlights the region's hidden potential – possibly. Jim O'Neill of Goldman Sachs, who coined the term "BRIC" several years ago, now says: "If I look at the whole region together (...) MENA has the combined potential to be a BRIC-like economic group." However, the 20 countries' economies vary more than those of the BRICs – and require tailored business strategies: Saudi Arabia, Libya and Kuwait live mainly off oil; Tunisia, Egypt and Morocco rely on tourism, while the Gulf states are focusing increasingly on finance, education and sports. Qatar, the richest MENA country, is 50 times wealthier, and its consumers are much bigger spenders, than Djibouti, the Palestinian territories and Yemen rolled into one. While some economies

CURRENT SCENARIO

3x3



MENA REGION'S SHARE OF WORLD'S OIL AND GAS RESERVES



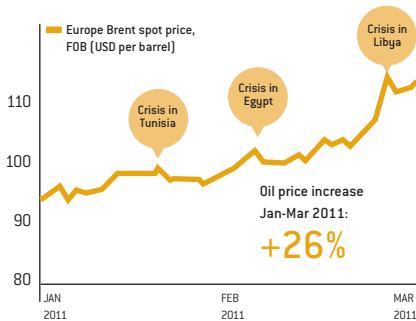
Source: German Mineral Resources Agency (DERA)

have opened up to world trade and become the base for thousands of foreign corporations, others deter business involvement through restrictive rules and a lack of stability.

In addition to the current political turmoil, MENA countries are facing huge economic challenges: They need to modernize outdated infrastructure and create jobs and prospects for their overwhelmingly young and often jobless or underemployed population. They also need to improve educational levels to become more productive, and move away from oil and toward more sustainable economic structures. There are huge opportunities for German companies in many of these tasks. And for this reason too, it is in Germany's interest to ensure that peace and freedom prevail in the region.

OIL PRICE DEVELOPMENT

Every crisis has pushed it up



GERMAN BUSINESS IN THE MENA REGION – AND HOW THE UNREST IS AFFECTING IT

The MENA region is not of the utmost significance to German business, but is more important than widely assumed: 3.6% of Germany's trade is with MENA states – totaling EUR 36 billion last year, mostly of which went to the United Arab Emirates (EUR 7.4 billion) and Saudi Arabia (EUR 5.7 billion). Nearly all DAX-listed corporations and the majority of German SMEs do business in the Arab states. They sell machines and equipment to every corner of the region, make car parts and consumer products in countries such as Egypt and Morocco, extract and process oil and gas in Libya and the Gulf states, fly tourists to North Africa's sun-kissed beaches, invest in infrastructure and real estate projects in the Gulf and much more.

Now, however, the mood of German companies in the region is characterized by uncertainty and tension. At his final press conference a few days ago, former BASF CEO Jürgen Hambrecht said, not only referring to Libya: "The situation is extremely serious and hard to assess." Two Metro stores were looted and set on fire during the protests in Egypt. Companies including Daimler, Henkel and Wintershall temporarily evacuated their staff from the crisis-hit countries for security reasons. And the oil price has moved with the protest and risen 26% since the start of the year to its current USD 115 a barrel (see graph) and is giving companies an increasingly hard time.

EXPORTS TO MENA, 2010

36 billion euros from Germany

32 billion euros from France

30 billion euros from Italy

Crisis action taken by German companies so far can be classified as follows:

- **Quickly adapting their service portfolio:** tour operators, for example, are flying customers to the Canary Islands instead of Tunisia and Egypt
- **Temporarily halting production:** A few German companies have temporarily stopped production in the crisis-stricken countries. Assembly lines at BMW in Cairo, BASF's construction chemicals production and Henkel's laundry detergent plant in Port Said, Egypt, remain idle
- **Postponing investment:** A few German companies have put their growth strategies on hold in the MENA region because of the unrest. The Desertec consortium, which plans to generate solar power in the deserts of North Africa, is still publicly optimistic that they can stick to the schedule. But this remains to be seen

THE ROLAND BERGER STRATEGY CONSULTANTS QUICK QUESTIONNAIRE

N = 97 GERMAN MANAGERS SURVEYED ON MARCH 3-6, 2011, MULTIPLE RESPONSES POSSIBLE

WHAT DO GERMAN COMPANIES DO IN NORTH AFRICA AND THE MIDDLE EAST?

+++ **42.9%** of the German companies surveyed do business in North Africa and the Middle East +++ Mainly in Egypt, the UAE, Saudi Arabia and Bahrain +++ **75%** of them sell goods and services in MENA, **21.9%** buy raw materials and supplier products, **18.8%** manufacture locally +++ **26.7%** of companies say the MENA region is important or very important now, and in the future even **50%** +++

HOW HAVE GERMAN COMPANIES BEEN AFFECTED BY THE UNREST?

+++ **70.4%** are not directly affected +++ Business has become tougher for **17.3%**, **3.7%** have seen sales slump in the MENA region +++ **9.9%** had to interrupt business operations, **16.7%** have put their growth strategy on hold +++ One in four local suppliers is in trouble, but no German company has yet had to change suppliers +++

WHAT DO GERMAN MANAGERS EXPECT OVER THE COMING MONTHS?

+++ Only **19.2%** think the protests have peaked; **86.1%** expect them to spread through the MENA region; **49.3%** even expect them to expand beyond the region +++ **90.4%** think Gaddafi will soon topple +++ **54.8%** fear Saudi Arabia will soon be rocked by protests +++ A massive **73%** do not expect the unrest to influence the oil price long term +++ But **70.3%** expect to see an impact on the German economy ++ **53.4%** expect a tide of refugees to wash over Europe +++

WHAT WILL HAPPEN IN THE LONG TERM?

+++ **65.8%** of German managers think that the upheaval will lead to more democracy in the Arab world; **54.2%** expect increasing Islamization +++ **53.6%** of German managers think our Sandstorm scenario is the most likely (that the region will return to business as usual after the unrest) +++ **31.1%** think the positive Oasis scenario is likely, versus **19.5%** who predict the negative Desert scenario +++

"OASIS" SCENARIO

MENA flourishes



– **Evacuating expatriate staff:** Companies such as Wintershall, Bilfinger Berger, Henkel, VW and Daimler have been evacuating their staff. At German shirt maker van Laack, which manufactures in Tunisia, staff members are guarding the plant

WHAT COULD HAPPEN IN THE REGION – OUR THREE MENA SCENARIOS

Together with colleagues from our MENA offices, we have developed three scenarios that could help with assessing the long-term prospects. The core questions are: How long will the crisis last? How many countries in the region are affected? And how comprehensive and long-lasting are the upheavals? We first analyzed the underlying strengths and weaknesses of the MENA region, and then evaluated the consequences of global trends on the area. Lastly, we analyzed the impact of the crisis: is the crisis-hit country itself affected first and foremost, such as by declining numbers of tourists or a brain drain? In what cases will the crisis affect not just the countries themselves but also their trading partners (as we can see from the examples of German companies)? And finally: What will be the consequences of the upheaval in the MENA states on the global economy, for example via the oil price, refugee flows or terrorism?

This led to three scenarios that describe how the MENA region may develop over the next few years:

"OASIS"

Scenario 1 describes a positive economic trend that unlocks dynamic growth and a multitude of opportunities for German companies. Led by countries whose former leaders have been toppled, democratic structures spread across large swathes of the MENA region; a growing and increasingly prosperous middle class emerges, euphoric and committed youths drive forward educational initiatives and start up new businesses, high (youth) unemployment falls sharply, the structural transition from the oil industry to sustainable economic structures gathers pace and there is little to nourish terrorism or radical Islamism.

"SANDSTORM" SCENARIO

Business as usual



"SANDSTORM"

By contrast, scenario 2 predicts that many things will be shaken up, as if by a sandstorm, but little will really change. In other words, the current crisis will bring about virtually no substantial changes, neither positive nor negative. Most German companies will return to business as usual. It may be a few months before peace returns to Tunisia, Egypt, Libya, Bahrain and other countries. But as the travel industry shows, business in all protest-hit MENA states will be up and running again. For instance, charter flights to Tunisia and Egypt are pretty full again just weeks after the crisis peaked. After all, little has changed: economic power and control is still in the hands of an elite (although the faces may have changed), social inequality and a lack of democracy will persist. Economic growth returns to stable levels, albeit below the region's potential. Rebellion by some parts of the population will be followed by resignation, and many will just try to make the best of the status quo.

"DESERT"

Scenario 3 shows a negative economic trend: the political and economic woes of the region get out of hand. German companies turn away because they cannot guarantee the safety of their employees or business. The storm of protests that has spread to almost all MENA countries has greatly increased social tensions. Economic inequality is not eliminated as the old elites cling to power. The stability formerly enforced by authoritarian methods will be replaced by chaos in many places. The fragmented societies provide new breeding ground for terrorism and radical Islamism. There are few jobs or prospects for young people, who become radicalized or flee the region.

Which of these trends is the most plausible? We asked German managers this question, and they responded optimistically overall: 31.1% predict the positive "Oasis" scenario, which would open up new opportunities for them, and 53.6% expect no major changes ("Sandstorm") – which for companies means continued economic growth of 4.5% or more per year. Only 19.5% think the negative scenario "Desert" most likely (see box for more survey results). But will the majority be proved right? The coming months, and short-term developments in Libya in particular, and the question of whether anything will happen in Saudi Arabia, will provide further food for thought.

But we have to answer one more question: will the upheaval in the Arab world have a negative impact on our current scenario for Germany, which predicts GDP growth of at least 3% in 2011 and 2012, following growth of 3.6% last year? We do not think so. First, Germany's trading volume with the MENA region is low. And second, German companies are coping well with the current difficulties. However, the rising price of oil will no doubt slow down the economy. But we, along with most of the German managers we surveyed, expect the rise to be only temporary. As for Saudi Arabia, no real predictions are possible. We will keep an eye on developments and publish further scenario updates as necessary.

"DESERT" SCENARIO

MENA dries up



IF YOU HAVE ANY FURTHER QUESTIONS,
WE ARE AT YOUR SERVICE ANYTIME:

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