

Emerging countries: the new wave

by

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When, in the 1950s, the cinema critics and directors Claude Chabrol, Jean-Luc Godard, Jacques Rivette, Éric Rohmer, and François Truffaut endeavoured to free filmmaking from its long-standing conventions, they paved the way for a new movement, the “new wave”, and for a new sense of freedom. Movement and freedom are what also contributed, at the dawn of the 21st century, to the emergence of the BRICs (Brazil, Russia, India and China), as a seismic shift in critical masses and in the location of the world’s engines of growth took place. As early as 2007, the BRIC countries matched the USA size with a 21.5% share of global GDP. Today the world's emerging countries generate half of global growth and hold more than two-thirds of foreign exchange reserves. Their dynamism remains strong thanks to an average annual growth of 7%; and a yearly increase in industrial production of 10%.

Although the BRICs continue today to be decisive players in globalisation, their divergences mean that they have yet to transform this opportunity into a collective destiny. And, far from being merely a conceptual development, globalisation is very much a reality in motion. We are witnessing a "new wave" of emerging countries; who makes up this amalgam of hopes and energy? What territory does it cover? And what impact will it have on the strategies of decision makers?

BRIC: formidable engines of growth but inaccessible for a large number of companies

For at least one more decade, the emerging markets are expected to perform better than the global economy. It is therefore only natural to look to these markets for growth and development. However, although the intrinsic characteristics of the BRIC countries have allowed them to prove highly resilient to economic crises, these massive countries are still exposed to significant risks through the lack of strong diversification in their economies, their vulnerability to the volatility of commodity prices, and sub-standard business environments. In addition to these risks, they are faced with the overheating of their economies, inflationary tensions and a rise in social inequality and; potentially; social unrest.

Above all, the BRICs have become inaccessible to many companies. The early movers are already there – and are firmly established. Investment in these markets continues to offer potential, but now requires an even more thorough risk analysis. And securing a market leading position is often prohibitively expensive. In Brazil, Russia, India and China, the greatest risk facing new players is that they will get lost in the market.

Nothing is worse than investing heavily for a period of 10 or 15 years only to end up as a marginal competitor in a concentrated market where only the leading firms secure a return on investment.

Does this mean that the emerging markets are now closed to potential investors lacking the necessary financial resources? That the only option is to retreat and dig into the more established markets? The answer; of course, is no.

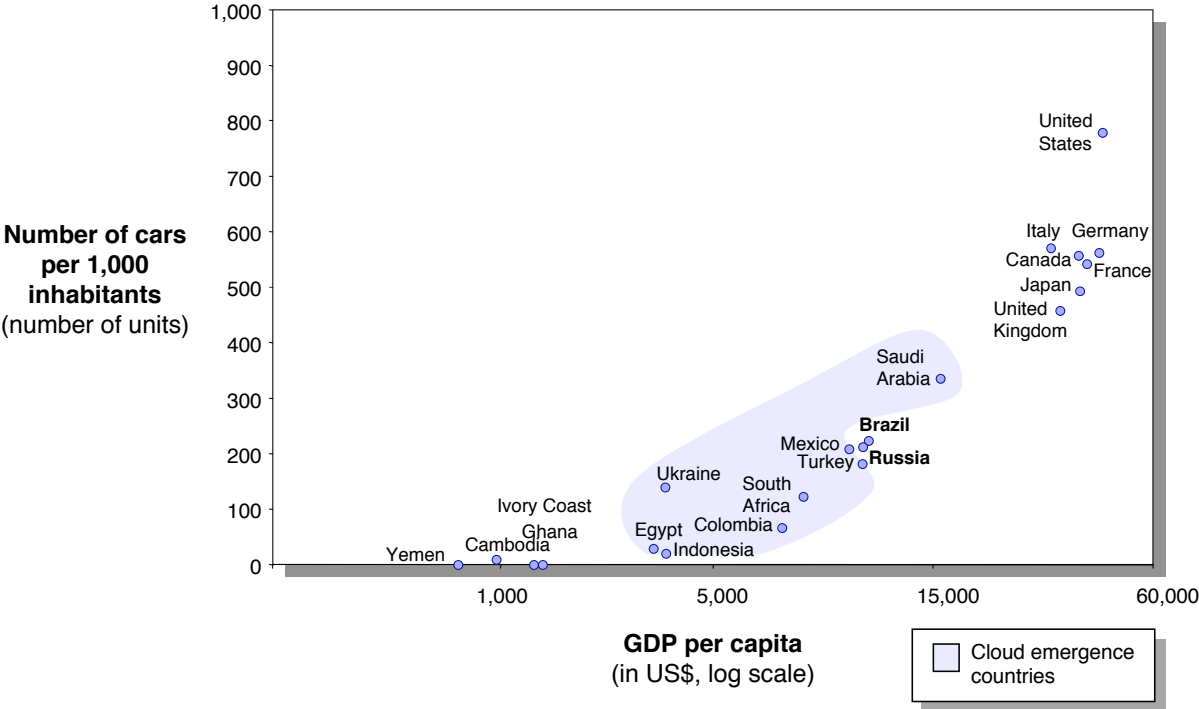
Towards a “cloud emergence”

The BRICs may be progressing, but they are being pursued by a cohort of other countries as yet ill-defined by awkward acronyms; BRICSAM, IBSA, Next 11, G20, G77 and so on. This “cloud emergence” is made up of the following:

- Countries that already have a footing on the growth ladder;
- Economies that are stimulated by powerful domestic markets;
- Societies drawn to the middle-class model.

Growth ladder. In the medium term, the "new wave" of emerging markets can be identified by the distinctly superior growth they enjoy when compared to the global economy. Although some markets are slow in getting off the ground (for example Mexico and South Africa), growth figures in or close to the 10-15% range can be observed across the board. Furthermore, these problems are more often due to surmountable flaws (in the financial system or in the business environment, for example) than a weakness in the economic fundamentals, which continue to benefit from very positive catch-up effects. It should also be noted that rudimentary social systems mean greater resilience in times of crisis. Indeed the new emerging countries inspire confidence, gain attractive country risk ratings (70% receive an A or B rating from Coface¹) and as a result receive considerable foreign direct investment (FDI) inflows. Whatever hiccups it may be experiencing, the "new wave" is making headway— and fast.

- Table 1 -

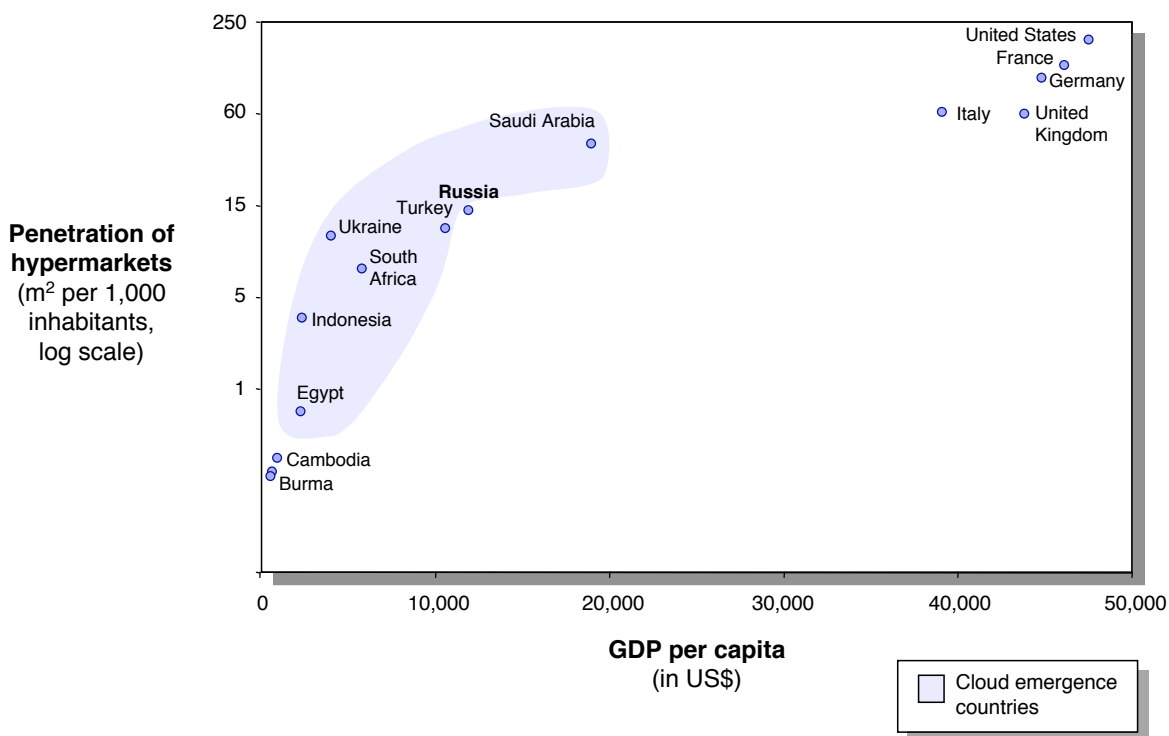


Sources: IMF, World Bank, Estin & Co. analyses and estimates

Powerful domestic markets. The economies of the new emerging countries are supported by vast and dynamic domestic markets which are progressing both in quantitative and qualitative terms, and represent both human capital and growth that have plenty more to offer. Although the international economy has a role to play, these countries are relatively well protected from the tensions affecting it, since the depth and scope of domestic demand act like a powerful and accelerating juggernaut as average solvency levels increase. This is particularly true in the most urbanised countries (urbanisation rate more than 60%), with the associated geographically dense consumption. Investment in infrastructure, public utility services and, more generally, gross fixed capital formation (GFCF) constitute decisive levers for stimulating domestic demand that is already strong and only wants to go in one direction: up.

¹ France's leading export insurance company.

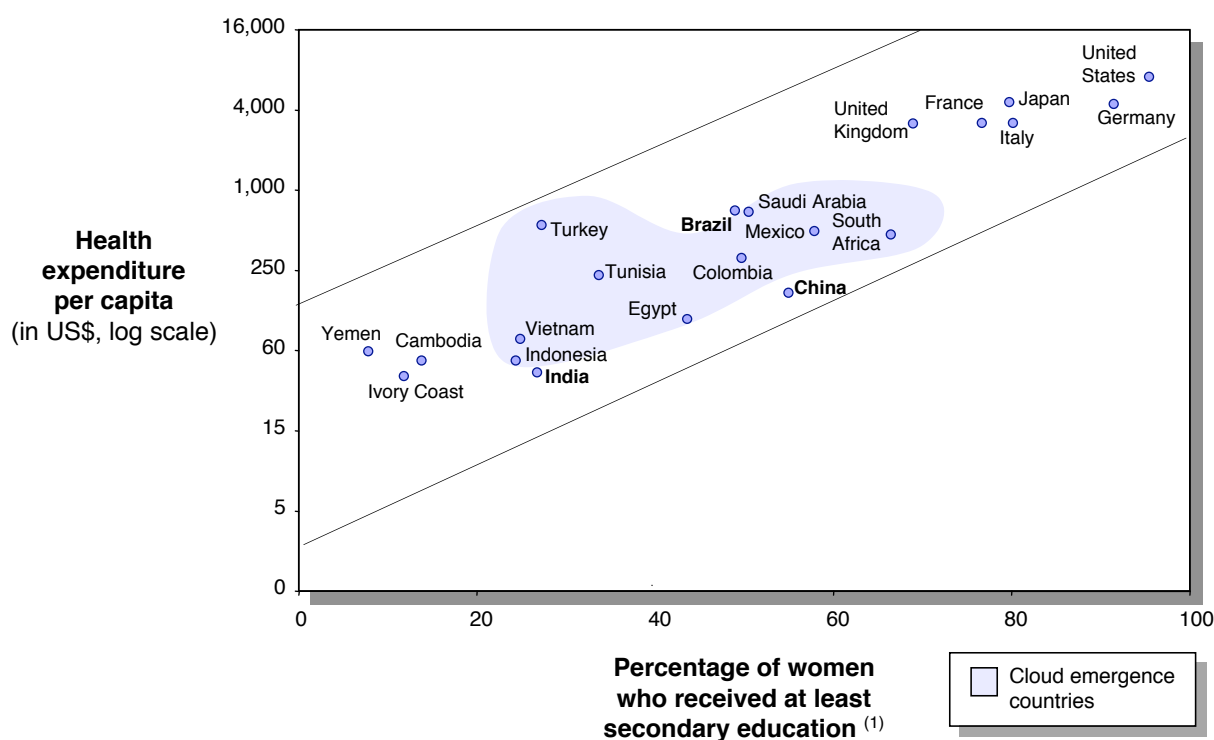
- Table 2 -



Sources: IMF, Planet Retail, World Bank, Estin & Co. analyses and estimates

The middle-class model. The major new emerging countries, encouraged by dynamic demographics, a sustained increase in the active population and a historic rise in the number of women working, are flourishing in a system based on a middle-class population that is both full of optimism and concerned about stability and the future. The aspirations of this group ensure a sustained development. The middle classes are also calling for greater mobility, improved education and health services, the erosion of the informal sector and corruption, more sincere consideration of individual needs, and a greater overall interest in protecting human capital (the average human development index, HDI, among the new wave of emerging countries lies between 0.85 and 0.72 – source: UNDP). While joining the growth ladder initially and inevitably leads to a widening of the social spectrum, the cloud emergence is actually calling for greater social cohesion built around a solid and sustainable middle class.

- Table 3 -



(1) Population of women over the age of 25
Sources: UN, IMF, World Bank, Estin & Co. analyses and estimates

10 candidates for the cloud emergence

The aim here is not to identify a roll-call of the best-placed countries, but rather to compile a list of the markets that are currently offering concrete and accessible opportunities. This list, which is based on historical, demographical and economic data, should be viewed as an indication only and is likely to change over time.

However, there is no denying the strong trends underlying this data. The new wave of emerging countries is very likely to include the following:

- Table 4 -

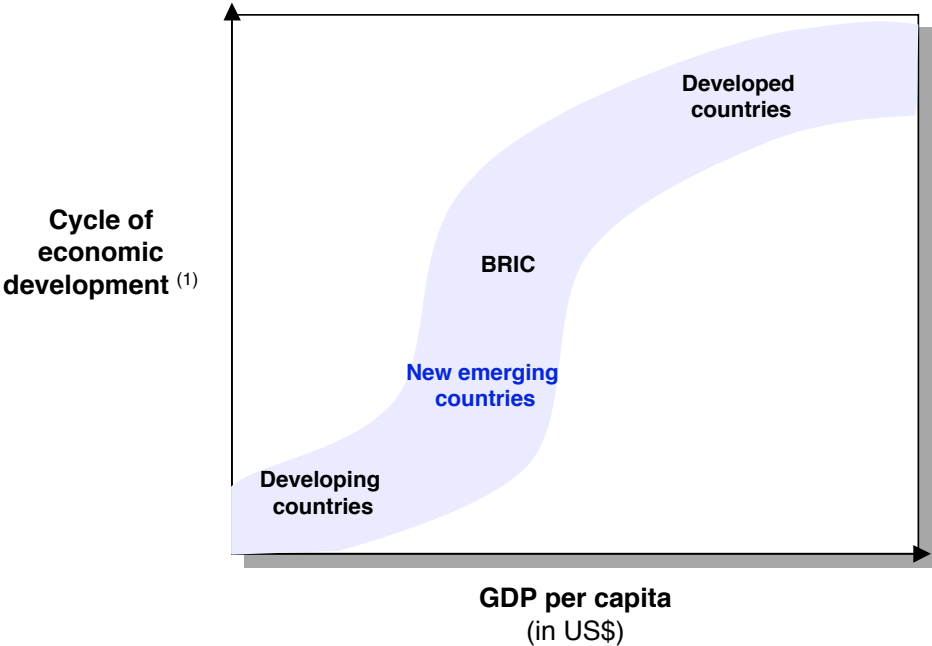
	Active population (2010)	GDP/cap (2010)	GDP (2010, \$bn)	GDP growth		Population growth	Coface rating (2010)
				2005-2010	2010-2015	2010-2015	
				(p.a)	(p.a)	(p.a)	
Indonesia	116	3,015	707	19.8%	11.4%	1.3%	B
Nigeria	50	1,389	217	14.1%	11.0%	2.7%	D
Mexico	47	9,566	1,039	4.1%	6.6%	1.0%	A4
Vietnam	47	1,174	104	14.4%	11.2%	1.2%	C
Egypt	27	2,789	218	19.5%	7.6%	2.0%	B
Turkey	26	10,399	742	9.0%	7.9%	1.1%	A4
Ukraine	23	3,000	136	9.6%	7.1%	-0.5%	D
Colombia	19	6,273	286	14.3%	6.1%	1.2%	A4
South Africa	19	7,158	357	7.7%	5.8%	1.2%	A3
Saudi Arabia	7	16,996	444	7.0%	10.1%	2.1%	A4
Mean	-	4,701	-	8.2%	6.8%	1.5%	-
Total	380	-	4,249	-	-	-	-

Sources: UN, IMF, World Bank, Estin & Co. analyses and estimates

What impact should this have on a company's international strategy?

We may have answered the "where" question, but what about the "when"? In truth the two are closely linked. There is no point in entering markets that are cheap but offer few business prospects, just as it is difficult to penetrate markets that are mature but not experiencing any growth, or some of the BRIC markets, where growth is strong but with significant financial barriers to entry. The new wave of emerging countries offers markets with considerable potential at a time when promising positions can be secured at a reasonable price. Timing is therefore essential: if you invest too early you risk several years of losses before the markets pick up; too late and the competition will be well established, as is the case in several BRIC sectors.

- Table 5 -



• **The new emerging countries will benefit from the growth ladder**

(1) For example: number of cars or mobile telephones or electricity consumption per capita
Source: Estin & Co. analyses and estimates

Conclusion

In the turbulent developed world in which we live, many democratic states are cash poor and their markets are failing to keep up with global growth. This is not to say we must bow down to an inevitable decline, but rather come to the realisation that the decision-makers in the industrialised world will have to look elsewhere for growth for at least another decade.

The BRICs, however, are no longer accessible to all, especially if you are looking to secure a sustainable and profitable position as market leader.

The new wave of emerging countries offers a series of opportunities that are as yet imprecise but very much real. This cloud emergence exists and is an invitation to develop more audacious and fertile strategies; strategies that ensure you are one step ahead.

In some cases a strategy involving the new emerging countries can pay off. In others, particularly in industries that are characterized by significant global economies of scale, it will be difficult to bypass China.

At the end of the 1950s, several “new wave” films were badly received or misunderstood. Since then, however, many of them have been hailed as great art and some have won awards.

So what can we learn from this? The avant-garde is often surprising but never disappointing.

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Estin & Co is an international strategy consultancy based in Paris, London, Geneva and Shanghai. The firm assists the boards of major European, North American and Asian groups in their growth strategies, and private equity funds in analysing and improving the value of their investments.