

The New World Economy in 2050...and the investors who will see it coming



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The year is 2050. The six sizzling markets of a half-century ago — Brazil, Russia, India, China, South Korea, and Mexico — have collectively outgrown those of Japan, France, Italy, Germany, and, yes, even the United States. Investing has become ever more global and interconnected, as virtually all portfolios comprise foreign stocks and funds, many of which were inaccessible or nonexistent at the turn of the century. The investors who foresaw this future, and who overcame their anxiety of investing in emerging markets, have prospered beyond their wildest dreams.

Will you be one of these investors?

Although 2050 remains safely in the distant future, the New World Economy envisioned by prominent analysts and economists is already beginning to take shape — right before your eyes.

Glimpses of this “future” economic upheaval are already being witnessed, not only in the nations of emerging economies, where unleashing market forces are raising the standard of living beyond the previous generation’s wildest dreams, but also within the major economic powers, as well as in the corporate world, stock markets, and small businesses — right down to the novice investor.

As hall of fame catcher Yogi Berra so eloquently opined, “The future ain’t what it used to be.” This is especially true of global economics.

No one person or organization can accurately piece together the chain of events that will lead us to this future, but numerous observations that foreshadow a tremendous acceleration in economic prosperity have been brought to light — and they raise several important questions. Why will the economies of Brazil, Russia, India, China, Mexico, and South Korea become so dominant? What are the reasons for the continuing growth and expansion in these countries, and what roles will investors — particularly American investors — play in this transformation?



The answers lie in understanding seven of the major tenets currently driving growth in emerging economies. Listed in no particular order, they are:

1 | Demographics

Not unlike the British, Portuguese, and Spanish colonies of the past, countries with burgeoning youth populations are poised to take a big chunk out of the world's resources and, in the process, create exceptional opportunities for their own populations, as well as for people around the globe, including American investors.

The world has never witnessed such an explosion of concentrated populations; there are more than 2.3 billion people currently living in China and India alone, which accounts for a full 43 percent of the world's population. Of all emerging economies, China and India are ideally positioned to benefit from a growing, mobile middle class, which will spurn domestic consumption and drive the internal markets to dizzying peaks.

This explosion in emerging countries is happening at a time when the populations of the United States, Europe, and Japan are aging. Conversely, the populations of the newly emerging countries are young, hungry, and enthusiastic. Half of the population of India, for example, is under age 25 — a far cry from the population in the United States, where the median age is around 36, the highest it has ever been.

2 | Technology

Emerging markets are undergoing a transition from slow technology growth and limited connectivity to hypergrowth. In many places, developing nations are leapfrogging technology to surpass developed countries. These advancements — such as bypassing ground lines to move directly into fiber optics and cellular technology — have accelerated the growth rates of the affected sectors and carved out a niche of low-cost solutions without sacrificing sophistication.

Asia, for example, has twice the number of cell phone subscribers as the Americas combined. Brazil represents the largest information technology market in Latin America, where mobile phone penetration surged ahead of fixed lines in 2003 and continues to



grow dynamically.

Technological growth is influencing life on every continent. By now, it's not news that China is a manufacturing capital or that India is the world's call center and software hub. Just this year, the demand for IT engineer and technical support personnel exceeded 1.1 million in India, with demand for another million international customer service workers. International demand for Indian IT workers for positions in other countries is projected to increase by 20 percent during the next five years.

What's not as well known is that companies such as General Electric, Microsoft, and Intel are opening innovation centers in India and China to focus on cutting-edge research by world-class engineers and scientists who not only excel in their fields but also work at a fraction of the cost as those in developed nations. In addition to GE, Microsoft, and Intel, dozens of other companies from the United States, Japan, and Europe hope to leverage the opportunities afforded by these research centers. The result, so far, has been that the companies are locked in feverish competition for innovation, producing hundreds of patents and receiving an edge in their quests to become major global players.

3 | Openness to trade

Although many emerging nations — most notably China, India, and Russia — have been slow in opening their borders for trade, they are in varying stages of openness and transparency. The writing is on the wall: Emerging nations are realizing that to participate in the global economy, they must truly open their markets.

China's entry onto the world stage, punctuated by its eagerness to be an active member of the World Trade Organization (WTO) and its hosting of the Olympics this summer, is creating opportunities that would have been unimaginable decades ago. In India, the preferences, quotas, and tariffs before 1990 made it a virtually closed system with low efficiency, low productivity, and poor living standards. The new changes in India allow foreign entities at least 51 percent ownership in most sectors and up to 100 percent ownership in special, urgently needed sectors.



In the WTO, Brazil has emerged as a leader of the G20 Group of Developing Countries, which includes India, China, and Mexico. The WTO is concerned primarily with agriculture and leveling the playing field between developed and developing economies by negotiating for the removal of farming subsidies in the United States and the European Union. Brazil has formed a powerful coalition for advancing the interests of trade liberalization and development objectives by joining forces with other developing nations.

Mexico's trade policies are among the most open in the world; the country has free trade agreements with the United States, Canada, the European Union, and many other countries. It has abandoned price controls and encouraged competition through regulatory reform and export-led growth.

These changes have created a dynamic for the worldwide exchange of goods and services that will result in lucrative opportunities for exporters, importers, and of course, investors. But the ultimate tipping point will be when these economies allow free and fair competition from outsiders and move beyond the protected enclaves of domestic companies, despite extreme pressure to maintain such protection. In China and India, the state-owned enterprises are entrenched both as a political force and an economic power. However, the expectation is that tomorrow brings a new day, and the rewards of open trade will be seen as expansionary — and the benefits universal.

4 | Infrastructural development

The developing economies of today are on the threshold of an explosion into a new world of superhighways and soaring skyscrapers, of mega power plants and supersize oil refineries. It is estimated that more than half of the construction cranes in the world are in China. The boom in infrastructure development in the emerging nations is breathtaking, and one can only imagine the state of such projects in 2050.

The Golden Quadrilateral highway connecting the four corners of India is another example of a mammoth project catching world attention. In Brazil, the economy is supported by heavy investing in building airports, roads, railways, and seaports.

The building boom sweeping the developing countries reflects industrialization and the continuing urbanization of populations desperate for shelter, roads, vehicles, power, running water, and sewage treatment. Coincidentally, these developments come at a time when similar growth in developed nations has slowed to a trickle — or even halted completely.

The phenomenal opportunities afforded by this infrastructure development are greatly benefiting companies from advanced nations. It's resulting in jobs, growth, and profits for the consuming nations as well as their suppliers. Shanghai already resembles New York City, and other developing cities far and wide are likely to follow.

5 | Transparency and rule of law

It's difficult to suggest that the emerging countries are currently meeting the high standards for transparency and rule of law that are typical among developed nations. The level of transparency — the degree to which government meetings and decisions, corporate budgets, and financial statements are open to public scrutiny — is a signal of fairness and openness; with more transparency there is less opportunity for authorities and executives to abuse the system for their own interests.

Transparency varies from country to country, yet the biggest confidence booster for foreign governments and investors is a country's willingness to be transparent and have an established rule of law, along with an impartial judicial system to enforce laws and contracts.

The Transparency International Corruption Perceptions Index measures perceived transparency. On a scale of one to 10, with 10 being the most transparent, Mexico, China, and Brazil each scored 3.3 in 2006, indicating significant room for improvement. In contrast, South Korea scored 5.1 and Hong Kong scored 8.3, reflecting the relative maturity of their legal and financial disclosure rules. If these nations continue to advance to the levels predicted by prominent analysts, they will undoubtedly come to learn the benefit of a transparent economic system.

6 | Education and training

Investments in education add significantly to a country's ability to generate future growth by strengthening its competitive work force. In fact, funding for undergraduate and graduate education is often tied to industries identified by the government as having strategic value to the country, such as health care or technology. As 2050 approaches, the emerging economies of today — many already wielding a highly educated work force — will continue to strengthen education and training, and consequently their prosperity.



China and India, for example, generate millions of college graduates annually who are entering a work force with greater opportunities. This rise in intellectual capital will contribute to higher wages and successive increases in disposable income. In 2005, for example, China produced 3.1 million college graduates — nearly three times that of the United States. Moreover, China's engineering graduates that year numbered more than 600,000, compared with about 70,000 American engineering graduates.

These figures demonstrate a keen sense of awareness in many developing countries that growth of intellectual capital is the gateway to riches via an expansion of productivity and innovation.

7 | Financial systems and monetary policy

The chances that a country's economic growth prospects will be realized increase greatly if the government sets policies that promote orderly financial markets and manages its finances to control inflation and debt. Adequate regulation of the banking systems, including minimum capital requirements and standards regarding investments and underwriting activity, fosters greater confidence in banks as repositories. When citizens trust banks and keep their savings in bank deposits, financial institutions can in turn lend those funds to businesses that need capital to grow.

Although confidence in monetary policy has historically been shaky in emerging nations, today's trends are indeed favorable.

Controlling inflation in the emerging world is equally important, since high inflation rates erode purchasing power and create a disincentive to saving. In the 1980s and '90s, for example, Brazil's economy was crippled by periods of hyperinflation resulting from poor fiscal policies as the government printed currency to fund spending. From 1980 to '97, the cost of goods in local currency increased by one trillion. The annual inflation rate in 1990 alone was 30,377 percent.

Real GDP growth, or GDP adjusted for inflation, stagnated as a result, barely keeping pace with population growth.

Today, the nature of inflation in Brazil has completely reversed; no currency — aside from the Colombian peso — has appreciated at a higher rate against the U.S. dollar than the Brazilian real. This, in turn, has fostered an economic environment where saving is no longer discouraged and where purchasing power for consumer goods and services is maintained — a far cry from the hyperinflation of previous decades.

Welcome to the future

“The future is here,” writes satirist William Gibson. “It’s just not widely distributed yet.”

The future of the global economy is here as well, as investors are demonstrating every day. Utilizing the right combination of ADRs (American depository receipts) and ETFs (exchange traded funds), investors have at their disposal a plethora of investing options in the developing world. And as these markets continue to open, so too will the profit opportunities.

Those who have warmed to the idea of emerging markets recognize the long-term potential of such activities. For others, emerging markets remain the best investment they never made.

Which investor are you?

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