

BY JEFFREY E. GARTEN

OVER THE NEXT decade, the biggest change in the world's corporate hierarchy will be the rise of companies from developing countries. Corporations such as China's Huawei (telecommunications equipment), India's Infosys (IT and business outsourcing services) and South Africa's SABMiller (beer and beverages) are already big global enterprises. But this juggernaut is just gathering momentum. As Antoine van Agtmael, president of Emerging Markets Management, says in a fascinating new book, due out in early January and called "The Emerging Markets Century: How a New Breed of World-Class Companies Is Overtaking the World," the household names of today—be they companies such as IBM, Shell or Sony—are in danger of becoming the has-beens of tomorrow, and the next Microsofts and General Electrics are more likely to appear in emerging markets than in the advanced nations.

Despite their promise, however, in 2007 emerging multinationals could face strong headwinds. In some respects, they have done the relatively easy stuff, breaking out of their national confines by taking advantage of strong global growth, low interest rates, declining trade barriers and more market-oriented policies in their home countries. They have also been the beneficiaries of American firms' internal preoccupation with corporate governance issues in the wake of business scandals and a consequent caution about risk taking. But five years into the post-Enron era, corporate America's animal spirits are back, and its focus on global expansion is reaching a feverish pitch. So now comes the hard part for emerging blue chips—competing with the big boys in the most advanced markets, which entails highly sophisticated management, strong brand awareness,

cultural sensitivity and playing by Western rules in everything from antitrust to transparency.

Here are four trends to watch.

Chinese companies will have difficulty in globalizing. There is no doubt that the Chinese government is supporting the

international expansion of natural-resource companies such as Sinopec with favorable financing and with generous foreign aid to host governments that will award them contracts. But for other companies, such as Haier, the white-goods company that failed in its bid for



Bracing for a

The Microsofts and GE's of the future are rising in the developi



INSTRUMENT OF PRESSURE:

Gazprom's political ties could provoke a Western backlash

The bellwether company is Lenovo Group, which acquired IBM's laptop division in May 2005 for \$1.75 billion, making it the world's third largest PC maker. The Chinese company has had all the advantages of a carefully planned strategic acquisition, including substantial management help from IBM. It has concluded alliances with major private-equity firms and put experienced foreign managers in pivotal positions. It has moved its global headquarters to Raleigh, North Carolina, and made English the company's official language.

So far, however, success is by no means assured. Lenovo's American operations are losing money, and it is losing market share both in the United States and Europe to Dell, HP and others. Reversing its initial plans, it has had to institute large-scale layoffs. If, with all the advantages it has had, Lenovo cannot succeed, investors should be more cautious about assessing the prospects for other globalizing Chinese firms outside of state-supported energy and natural-resources corporations.

India is in the grip of super-power ambition. Its possession of nuclear weapons, its importance to the United States as a counterweight to China and its booming economy have given the nation a sense of confidence not seen in centuries. But Indian companies risk becoming dangerously overconfident, particularly in chasing megamergers with foreign corporations.

In the first nine months of 2006, Indian companies announced a record 112 foreign acquisitions, with a combined value of \$7.2 billion. By the year-end the total value of such deals will probably exceed \$16 billion, three times the amount in 2005. Companies have benefited by liberalization of domestic regulations, low

Rough Patch

world, but they face a tough stretch ahead. Here's why.

America's Maytag, there are big questions ranging from their depth of management, understanding of global strategy and lack of brand recognition outside the Middle Kingdom. Fact is, some of the big Chinese efforts to expand abroad, such as electronic giant TCL's acquisi-

tion of large divisions of Thompson and Alcatel in France, have flopped. Others, such as automakers Geely or Shanghai Automotive Industry, are delaying their plans to enter the United States or Europe because they recognize they cannot compete in sophisticated markets.



MICHAL OZDEK - AFP - GETTY IMAGES

interest rates and a booming stock exchange. Among the Indian industries that are bent on major international expansion are auto parts, tractors, pharmaceuticals and IT.

But are Indian companies ready for supersize deals? Can they weather the inevitable higher interest rates or other adverse economic conditions, and do they have the depth of management to oversee global goliaths?

The company to watch is Tata & Sons, a conglomerate spanning dozens of industries from steel to beverages. Tata has been expanding into Europe and the United States, and plans to move into Vietnam, Indonesia, South Africa, Brazil, Argentina and Iran. Two months ago Tata Steel bid \$9.5 billion for Corus Group PLC, the Anglo-Dutch giant that produces three times more tons of steel than Tata. Last month a higher bid from a Brazilian rival set the stage for a heated bidding war.

If Tata doesn't succeed, it's a good bet it will be hunting big prey again. If it does win the deal, it will have concluded the biggest Indian takeover in history and catapulted itself to No. 6 on the list of the world's largest steel companies. The ac-

FERMENT: SABMiller brewing of South Africa is one of the hot corporate names now run out of the emerging nations

quisition will also saddle Tata with an additional \$5 billion of debt and force it to make some painful layoffs in Europe. Even Tata officials are saying that the group

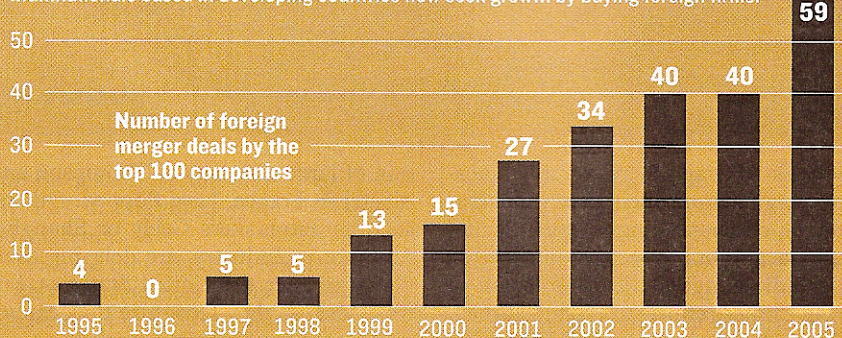
will need several years to achieve the margins of profitability in the combined entity that Tata Steel enjoys today. Tata is likely to succeed—with a lot of painful stress. The problem is that other Indian companies may well try to follow Tata, but without Tata's management experience and talent. Just one big misstep for a marquee

Indian company could create fears in the market about Indian overreach.

Russian natural-resource companies could hit a wall of resentment abroad. As in China and India, there is a connection in Russia between the confidence and the strategy of the state and the global behavior of its major companies. Prime Minister Vladimir Putin and his entourage—who have effectively nationalized the energy and minerals sector—leave no doubt they aim to use their resource wealth not just to enrich their country economically but also for diplomatic leverage.

EMERGERS AND ACQUISITIONS

Multinationals based in developing countries now seek growth by buying foreign firms.



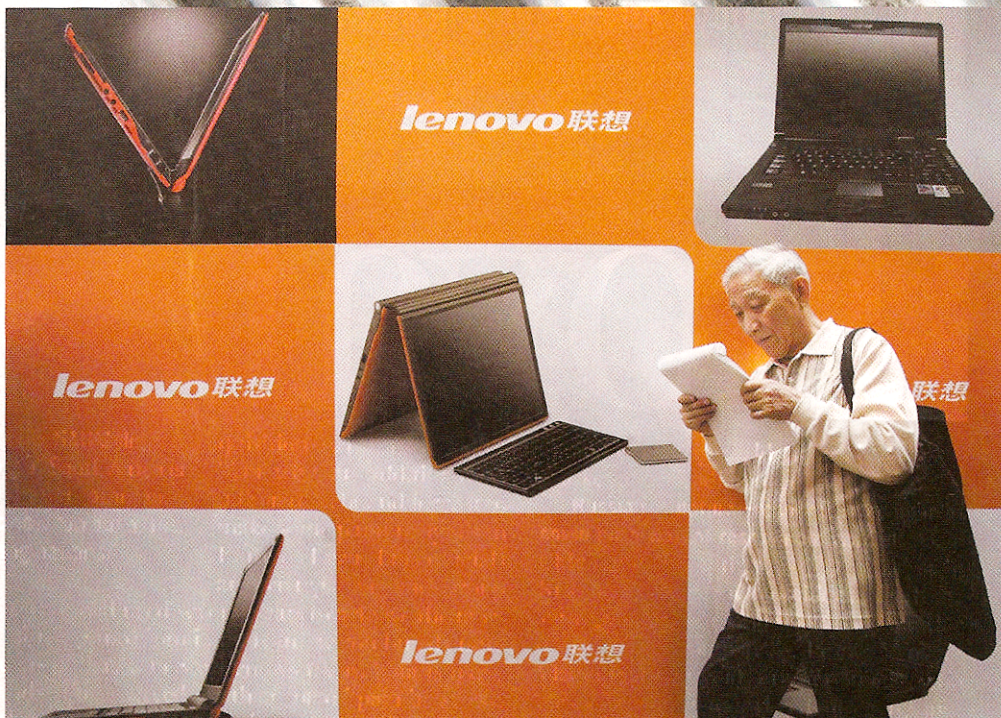
So far, they have succeeded. In November, Rusal, an aluminum company, merged with a smaller domestic firm, Sual, and simultaneously bought the mining assets of Switzerland's Glencore. These deals made it the largest aluminum company in the world—soon to be called Russian Aluminum. In the past few weeks alone, Evraz, Russia's largest steel producer, announced the acquisition of Oregon Steel Mills in the United States, and Norilsk Nickel, the world's largest nickel producer, said it would buy the nickel division of the OM Group of Cleveland, Ohio.

The company to keep an eye on within Russia Inc. is Gazprom, the state-owned natural-gas monopoly, which has a market value of \$250 billion, nearly the size of ExxonMobil. All year long Putin has been using this company as an instrument of pressure on his neighbors such as Ukraine and others such as Italy and Germany for higher-priced gas deals and access to distribution systems. The EU now worries openly that overdependence on Gazprom could be a threat to its energy security.

The next stage of Russian expansion will entail more public listings to raise capital and more acquisitions abroad. It will be interesting to see whether Russia will clean up its notoriously poor corporate governance in preparation for these IPOs, including the lack of financial disclosure, opaque ownership structures and disregard for minority shareholders. As it stands, Moscow's disregard for corporate governance and its bare-knuckled commercial diplomacy could run into a chorus of complaints in the West, and trigger nasty trade disputes.

Emerging multinationals will have to spend more time than ever defending their home turf. Look for global companies from the West and Japan to up the ante by further penetration of developing countries. Intel has recently become the biggest investor in Vietnam. Wal-Mart is expanding at a breakneck pace in China and doing major joint ventures in India. Indeed, the strategic plans of virtually all top multinationals, including GE, PepsiCo, Procter & Gamble and IBM, all show a strong increase in future earnings from emerging markets.

Emerging multinationals will also



have to contend with competition from smaller local companies that have become the beneficiaries of investments and strategic advice from major Western private-

equity firms such as the Blackstone Group, Warburg Pincus and TPG Newbridge. The most aggressive of these firms, the one that seems to set the pattern in Asia and Latin America, is the Carlyle Group, which has just bought out Taiwan's Advanced Semiconductor Engineering group for \$6.4 billion.

Just as important as the capital these private-equity firms provide is the chance they give to smaller companies in emerging markets to develop global strategies without the burdens of having to go public and earn short-term profits for shareholders. PE firms are also

BELLWETHER INC.:

Lenovo has much left to prove in the U.S., Tata Steel could spark a wave of Indian buyouts

skilled at providing financial-performance incentives that attract the best and the brightest corporate leaders. They can plug the companies in

which they invest into networks of management talent and industry expertise, and facilitate friendly combinations with similar firms around the world. They establish effective corporate-governance systems. In short, they will create fierce competitors to entrenched companies.

Bottom line for next year: investing in emerging multinationals is a good long-term bet. But for the next year or two, be prepared for a rocky ride.

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