SOAPBOX

OFF THE SHELF

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First World, Third World (Maybe Not in That Order)

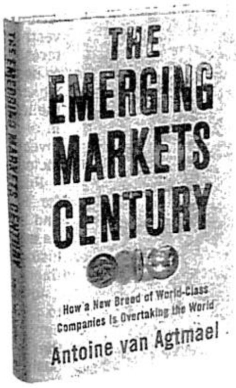
WOULD you risk part of your children's college fund or your retirement in third-world equities? You may already have.

These days, "third world" is usually viewed as synonymous with destitution and perpetual civil war. But the term originated with a positive connotation.

In 1952, Alfred Sauvy, a French demographer inspired by a famous French Revolution pamphlet on the rising Third Estate, likened the developed, or first world, to the nobility and the Communist, or second world, to the clergy. He singled out the rest — which he named the third world (in other words, the "commoners") — as the group to watch.

Antoine van Agtmael, in **"The Emerging Markets Century"** (Free Press, $28), outdoes Sauvy, predicting that the third world "will overtake the developed world by around 2030-35." In fact, some global alignments have already shifted.

Just a few decades ago, a wizened hand at Bankers Trust scoffed at a young Mr. van Agtmael that "there *are* no markets outside the United States!" But the author had grown up in the Netherlands, and as a boy he had owned shares in the Dutch giants Philips, Shell and Unilever. (Bankers was later swallowed by Deutsche Bank.) So, early on, he learned that experts can be wrong. Then he became an expert.



In the late 1970s, Mr. van Agtmael commissioned a study of what he viewed as leading third-world companies. By 1981, at the New York office of Salomon Brothers, he was pitching a "Third World Equity Fund." After someone in the audience told him that it was a good idea but a lousy name, he became a marketing genius: he coined the phrase "emerging markets."

And emerge some did. When Mr. van Agtmael first visited South Korea for Bankers in 1971, "Seoul looked like a city in the Soviet Union, which I had just crossed on the Trans-Siberian Railroad," he writes. "No skyscrapers yet loomed over the cramped city center and anti-aircraft guns were starkly visible on just about every street corner." Under what was then a military dictatorship, per capita income in South Korea was around $225. Today it exceeds $10,000.

Consider, too, that in 1971 India was embroiled in a war with Pakistan, resulting in the bloody birth of Bangladesh. China, under Mao, was a grotesquely violent paroxysm. Vietnam was being bombed into the Stone Age. Today, where would your portfolio be without them?

Asia's economic surge is among the grand stories of modern times; it was part of — yet broader than — the collapse of the Soviet Union, which unexpectedly opened the second world to a slosh of investment capital, too. As late as 1981, Mr. van Agtmael says, the value of all shares on emerging-market stock exchanges was a mere $80 billion. Today it is more than $5 trillion.

But are such investments fated to founder?

Amid the hype about emerging markets, Mr. van Agtmael understands that some had a long history of fabulous wealth before 1800, so they are essentially *re*-emerging, like India and China. Their current trajectory could endure. But for the rest of the old third world, achieving sustained growth and high per-capita gross domestic product have proved no mean feat. Just ask Indonesia, Egypt or Nigeria.

In Mr. van Agtmael's catch-all category of emerging markets, the few countries that have achieved lasting prosperity are the exceptional cases of South Korea, Taiwan, Hong Kong and Singapore. They are all linked intimately to Japan and China, and to the United States.

"Emerging Markets Century," however, adjusts the focus from countries to companies. Nearly 60 of Fortune magazine's top 500 global companies, Mr. van Agtmael underscores, are now based in emerging markets. This was unknown 15 years ago. But, he says, Samsung of South Korea, Infosys of India, Haier of China and Cemex of Mexico are not "overnight wonders."

In selecting 25 top-performing companies in emerging markets, Mr. van Agtmael excludes government-owned behemoths that are world class in size but not in management, usually in natural resources, like Gazprom of Russia. But his is no tale of cheap labor, either.

Fourteen of his emerging-market multinationals specialize in high-technology or capital-intensive industries. They make profits the hard way: they innovate, competing on quality as well as price. Fourteen are in Asia and one is in Africa, but 10 can be found in Latin America.

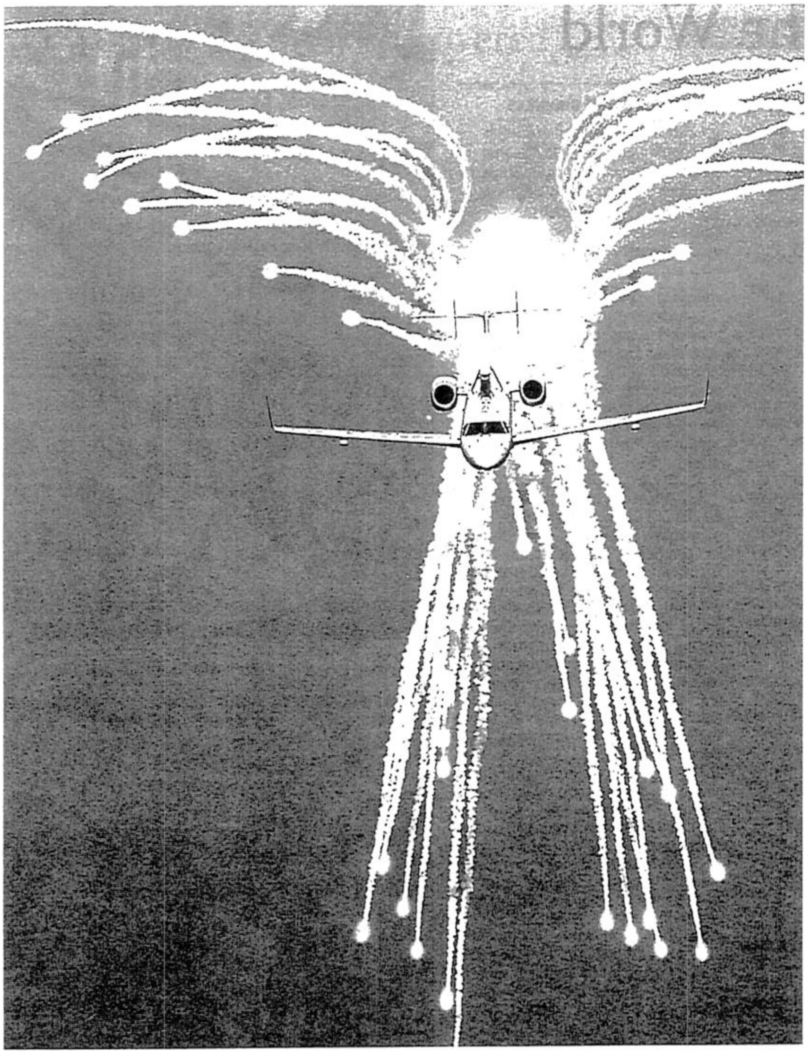
The text is not immune to business-book pap ("Vision is important but execution is paramount," the author writes, which lately might be rephrased as "Forgetfulness is important but immunity is paramount.") But it uses interviews and media reports to illuminate the impressive talent that operates in these companies, showing why they have been gobbling up established-market businesses.

Most important, Mr. van Agtmael reveals the dynamism of South-South business — by which he means the booming global commerce that is not centered on northern regions like the United States and Europe.

The plane builder Embraer of Brazil, he notes, "sells its regional jets in Saudi Arabia, India and China," providing southern counterparts not just value for money but also an alternative for those desperate not "to be dependent exclusively on U.S. suppliers." CVRD, a leading iron ore producer based in Brazil, seeks to pre-empt Chinese dominance of Africa's resources, using Brazil's historical ties to that continent.

But Mr. van Agtmael wonders whether CVRD will beat its Chinese competitors, or whether Embraer can manage to take on Boeing and Airbus. Unclear.

Tough marketplace challenges are the easy part. "No matter how impressive many emerging multinationals may seem," Mr. van Agtmael notes, they "still have to contend with political restrictions, stubborn and recalcitrant bureaucrats," and "dysfunctional court systems." Given these obstacles, it is all the more impressive that the players he spotlights have been moving steadily up the value chain.



Embraer, via Agence France-Presse- Getty Images

A plane by Embraer demonstrates countermeasures to a missile attack. Embraer is based in the emerging market of Brazil

He invokes a Darwinian winnowing, whereby 80 of the top 100 companies in the original Emerging Markets Index he created 25 years ago have vanished. Still, closing with tips on how to make money in emerging markets, he cautions that "the real secret is that the secret is always changing."

Mr. Sauvy, the Frenchman, rightly observed that the "exploited, scorned third world, like the third estate, wants to become something, too." Many third-world multinationals have. Many more seem likely to do so. But they have to be located somewhere.

And when an emerging-market country implodes, as Russia did in 1998, it does so Enron-style, as if management — a k a the government — had been found to have perpetrated fraud, blindsiding even well-run companies.

Ultimately, whether investors worried about volatility have more to fear from emerging markets or from today's developed markets remains to be seen. □