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## BRICs versus other Emerging Economies: The case of India

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### Abstract

In late April 2013, Jim O'Neill retired as chairman of Goldman Sachs (GS). The 56-year-old British economist, among other accomplishments, left his mark on the still unfolding globalization story by coining the acronym BRIC, referring to the four rapidly developing nations—Brazil, Russia, India and China—that seemed ready a decade ago to challenge the economic supremacy of the United States, Japan, and Western Europe.

Since O'Neill invented the term in 2001, the BRICs have evolved in very different ways and have developed at very different rates. While China's economy continues to boom, though off its torrid pace of a few years ago, Russia's economic growth rate slowed last year to an estimated 3.4 percent, according to its Federal Statistics Service—down from 4.3 percent in 2011 and 4.5 percent the year before. Brazil's gross domestic product grew just 0.9 percent in 2012, while India's expanded at a 5 percent rate. As O'Neill bows out, perhaps a bigger story than the BRICs today—one that deserves more attention in the board room—is the large number of countries that are now competing with the BRICs, even outpacing them, often for the same reasons the BRICs have done well.

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What this means, looking ahead, is that corporate executives, as they review their global plans, have more options than ever before available to them.

**Keywords:** BRICs, India, Emerging Markets, Foreign Direct Investment, Elections

## **Introduction**

The four countries have very different sources of strength. Brazil and Russia, for example, are blessed with abundant natural resources, while India and China are blessed with abundant labor, Chinese labor is neither as abundant nor as cheap as it used to be.

However, European executives expect rapid-growth markets outside the traditional BRICs to be key to future business strategies, according to a new report on globalization trends, by the Ernst & Young (Ernst & Young Report, 2013).

Turkey, for example, despite the recent violence there, is a country with great promise, with a very modern and diversified economy straddling Europe and Asia. It has a rapidly growing high-tech sector and a strong banking sector. Its GDP, which averaged 9 percent growth in 2010 and 2011, expanded at a significantly slower 2.2 percent last year. This was neither unexpected nor unwelcome in view of the European debt crisis.

Mexico, whose 2012 GDP growth rate was 4 percent, is a natural fit for U.S. companies, with its close proximity to the U.S. and with free trade agreements not only with the United States and Canada, but with Chile, Costa Rica, Colombia, El Salvador, Guatemala, Honduras, Nicaragua, Peru, Israel, Japan, and the EU. Manufacturing is developing rapidly, with a focus on appliances and automotive clusters. Mexico's standard of living continues to grow. While violence is still a concern, companies have learned how to work around it.

Indonesia is the world's fourth most-populous country and Southeast Asia's largest economy, with a rapidly growing consumer sector. It has a developing labor force and relatively low wages. As the 2013 Index of Economic Freedom notes, "President Susilio Bambang Yudhoyono has attacked corruption and tried to encourage much-needed foreign investment," which bodes well for the future. Indonesia's GDP grew 6.5 percent in 2011 and an estimated 6 percent last year (<http://www.heritage.org>).

Other rapidly developing economies that are blessed with abundant natural resources and appear well positioned for sustained growth include the Republic of Congo, Guinea, Kazakhstan, Mozambique, Niger, Nigeria, Sierra Leone, Tajikistan, and Zambia.

### **The case of India in this new status quo.**

India has a chronic dependence on foreign capital to bridge its investment needs and cover a permanent trade deficit. Although it has a liberal foreign direct investment policy, its poor business environment ensures that it receives only about US\$20 billion foreign direct investment<sup>2</sup> (FDI) a year (<http://www.tradingeconomics.com/india/gdp>). This year's elections will give foreign companies an indication of whether India will be politically able to allow them larger stakes in the country.

Potential investors should reasonably expect to see greater opening up in five sectors – banking, insurance, defense, railways and retail/e-commerce (The Economic Times, 2013). What these overseas businesses really need is the emergence of a strong leader with the authority to take on the political risks that these reforms will engender.

The main barrier to foreign investment in the past few years has been the breakdown in executive authority in the Congress Party-led United Progressive Alliance (UPA) government, which has resulted in policy confusion on several fronts.

This is why there is considerable interest in the forthcoming national elections and prospect of a new government by May 2014.

Based on present electoral rhetoric, the only fundamental policy difference is on FDI in multi-brand retail.

The Bharatiya Janata Party (BJP), with an eye to the small domestic retailers who constitute a large part of its voting support, has reversed approval for this policy in two states it recently won.

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<sup>2</sup> Foreign direct investment (FDI) is a direct investment into production or business in a country by an individual or company of another country, either by buying a company in the target country or by expanding operations of an existing business in that country. Foreign direct investment is in contrast to portfolio investment which is a passive investment in the securities of another country such as stocks and bonds.

Unsurprisingly, most major global retailers have preferred to wait to see what happens after the elections.

Five sectors that could affect FDI policy are (OECD, 2011)

1. Banking: The current government has retained the status quo limits on FDI: 20 per cent in state-owned banks and 49 per cent in private banks. The government's focus has been to end a practice, common in the banking sector, of foreign investors having several different types of financial holdings for a single bank.

The Mayaram Committee recommendations recently adopted by the government mean that foreign portfolio investment, qualified overseas investors and so on are now to be all treated as varieties of FDI - and collectively disciplined by existing FDI limits.

The idea is to persuade foreign investors to convert their various financial holdings into FDI, making the investments less volatile.

2. Insurance: The Manmohan Singh government has sought to raise the FDI limit in the insurance sector almost every year since 2008. It has repeatedly claimed it has received support from the BJP but then delayed the actual parliament vote.

The FDI limit remains stuck at 26 per cent ([http://finmin.nic.in/the\\_ministry/dept\\_eco\\_affairs/dea.asp](http://finmin.nic.in/the_ministry/dept_eco_affairs/dea.asp)). The UPA's target has been to raise this to 49 per cent.

The government recently announced that FII<sup>3</sup> investment would also be allowed in insurance, though subject to the same cap. This would allow Indian insurance firms to receive foreign capital from companies outside the sector.

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<sup>3</sup> Foreign Institutional Investors: are organizations which pool large sums of money and invest those sums in securities, real property and other investment assets. They can also include operating companies which decide to invest their profits to some degree in these types of assets.

Typical investors include banks, insurance companies, retirement or pension funds, hedge funds, investment advisors and mutual funds. Their role in the economy is to act as highly specialized investors on behalf of others.

3. Defense: The UPA government, led by its leftist defence minister A. K. Antony, had stuck to a policy of 26 per cent of FDI in the defence sector. In July 2012 it opened a small loophole, by resurrecting a previous policy allowing 100 per cent FDI ownership in 'high technology' defence sectors, with clearance to be issued by the cabinet committee on security on a case by case basis.

The UPA is considering allowing an additional FII investment slab of 23 per cent, to take the overall limit to 49 per cent. However, the government is running out of time to persuade the defence ministry.

4. Railways: Until recently, the nationalised Indian rail system was almost completely outside the purview of FDI except in a few infrastructure and construction areas.

Late in 2013, facing chronic underinvestment in its capital projects, the government proposed that FDI be allowed in short rail connectivity, for example connecting a coal mine to a steel plant.

Following the state visit of the Japanese Prime Minister Shinzo Abe in January 2014 (The IMF Survey Magazine, 2014) the government announced its intention to allow FDI in a slew of other areas. So far this has only reached the level of a cabinet note.

5. Retail/E-commerce: The most forward FDI policy taken by the UPA government was the decision to allow 51 per cent foreign ownership in multi-brand retail. There are no restrictions on single-brand retail and business-to-business retail.

However, it added a codicil that it must also be accepted at the state government level. So far, a dozen states have followed the central government but only UK-based retailer Tesco has announced plans to enter the Indian market.

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For instance, an ordinary person will have a pension from his employer. The employer gives that person's pension contributions to a fund. The fund will buy shares in a company, or some other financial product. Funds are useful because they will hold a broad portfolio of investments in many companies. This spreads risk, so if one company fails, it will be only a small part of the whole fund's investment.

Indian elections are notoriously difficult to predict, given their sheer size and the diversity of the electorate.

The real accomplishment of the polls would be to put in place a prime minister with the genuine authority to implement policies, rather than merely enunciate them. This has been a larger barrier to many foreign investors than actual policies on paper.

### **Concluding remarks**

Leading companies are adopting a multi-market approach (Grant Thornton, 2014). While the BRICs remain critical to their strategy (Yan et al, 2012), executives are also looking closely at opportunities in non-BRIC emerging markets, where they are seeing improvements in the ease of doing business, infrastructure, government policies and labor productivity. South Africa, Indonesia, Mexico and Turkey emerge as the locations perceived as most competitive worldwide with a large per cent of executives, expecting to increase their investment in the countries (Koumparoulis, 2012).

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