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Brics summit faces challenges over growth

By Stefan Wagstyl and FT reporters

Leaders of the Brics countries gather in South Africa on Tuesday for their annual summit, knowing that some of the shine has come off their economies.

While they are still surging by the developed world's flagging standards, they rarely generate the same excitement as before among investors. The heady days before the 2008 global crisis, when the Bric movement was launched amid an emerging markets boom, are a distant memory. So even is the mood of 2011, when Brazil, Russia, India and China asked South Africa to join the club at a time when China was helping to pull the world out of recession.

The Brics growth rates have fallen, with Brazil leading the way down. And this year's recovery looks fragile. The International Monetary Fund forecasts gross domestic product growth of 5.5 per cent in the emerging markets in 2013, barely higher than 2012's estimated 5.1 per cent.

Investors, who ploughed money into Brics equities last year on hopes of a faster recovery, have more recently bet on the US and Japan and on smaller developing economies, notably the Philippines.

The Brics' economic slowdown is mainly due to the stagnation in the developed world, with the eurozone, in particular, holding back recovery. On average, emerging markets are growing about 4 percentage points faster than the developed world – just as they did pre-crisis.

The Brics still dominate the emerging markets, with China alone accounting for more than 40 per cent of the collective GDP. But some growth momentum is passing elsewhere. As China gets richer and its population ages, growth is slowing. Meanwhile, India, which could be picking up the baton as a far poorer country, faces structural challenges to fulfil its potential. Brazil and Russia have failed to generate the investment levels needed for sustained accelerated growth and South Africa struggles with deep-rooted social and economic difficulties.

So investors are looking to regions where GDP growth rates are higher than before 2008: south east Asia, for example, and parts of Africa, headed by Nigeria. For the moment, these economies are too small to dent the collective dominance of the Brics. But the emerging markets are clearly becoming more diverse.

China

Among the Brics countries China is the heavyweight, with an economy nearly a quarter larger than the other four combined. Three decades with average annual growth of about 10 per cent has lifted China into the lower ranks of the middle-income countries and drastically improved the living standards of almost one-fifth of humanity.

But partly because of its sheer size and partly as a result of a growth model that is reaching the limits of its effectiveness, China appears to be heading for a period of weaker growth after notching up an expansion of 7.8 per cent in 2012, the slowest pace in 13 years.

In order to stop the growth rate heading even lower, China's leaders, who completed their ascension to their posts last week, are expected to introduce reforms aimed at further reducing the country's reliance on environmentally destructive investment-driven, export-led growth.

"China certainly has a lot of challenges but at least the political elites appear to understand the problems and are working to fix them," says Eswar Prasad, a professor at Cornell University and a former head of the IMF's China division. "If they can successfully implement reforms then growth will settle in a 7 to 8 per cent range in the next few years. That is a comfortable rate that still solves a lot of problems."

If Beijing's new mandarins can maintain this lower but still impressive growth rate, then the Chinese economy is predicted to overtake that of the US after accounting for price differences to become the world's biggest by as early 2016, according to the OECD.

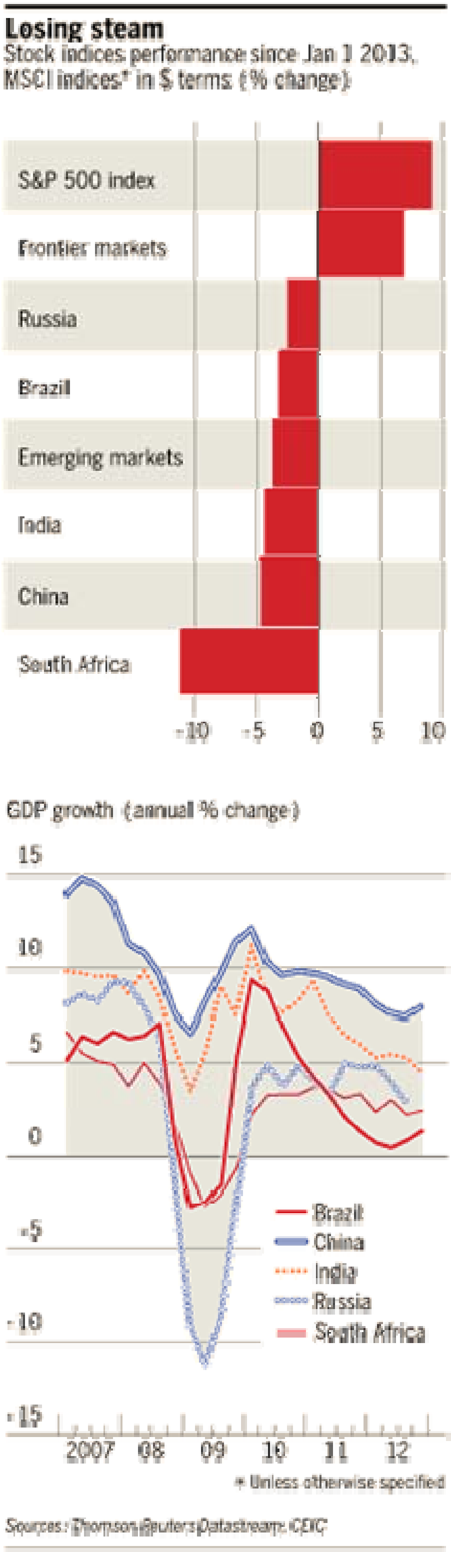
By Jamil Anderlini

India

Hardly a day passes in India without the chief executive of a big Indian company – or the local boss of a foreign multinational – grumbling in private about the

difficulties of doing business in what was until two years ago a high-growth economy.

True, there is almost unanimous praise in the business world for the reforms undertaken by Palaniappan Chidambaram, finance minister, since he reclaimed the post eight months ago. His changes include reduced subsidies for diesel, faster privatisation, efforts to curb the budget and current account deficits, and an easing of restrictions on foreign investment in retail and airlines.



Yet such changes take time to bear fruit and Indian economic expansion remains sluggish. GDP growth is expected to slow to 5 per cent in the fiscal year to the end of this month, its lowest pace for a decade.

Entrepreneurs say a longstanding reluctance by the government to make sweeping reforms to labour and land laws has left them reluctant to invest and even when they do want to invest their projects lie idle because bureaucrats are reluctant to grant the necessary approvals. Nor is the likely shift towards populist policies before the general election due by May 2014 likely to do much long-term good for the economy.

"We need a greater strategic direction in selling the country's strengths," Siddharth Birla, senior vice-president of the Federation of Indian Chambers of Commerce and Industry, said on Friday, calling for a doubling of exports and a rise in the share of manufacturing in GDP from 15 per cent to 25 per cent.

"Exports and business investment must be the dual drivers of future growth necessary to lift the economy from the deep economic crisis and provide job opportunities for our rapidly expanding and young workforce," said Mr Birla.

By Victor Mallet

Russia

While Russia remained the fastest growing large economy in Europe last year, it has recently showed signs of slowing. As the title of a research note from Renaissance Capital says: “Russia’s economy grinds to a halt in February”.

Ministry economy figures are indeed worrying – initial statistics report that February GDP growth was almost flat on a year-on-year basis – a minuscule 0.1 per cent. This was down from the already worrisome 1.6% year on year growth recorded in January. According to Renaissance Capital, the slowdown in the Russian economy has now been going on for five consecutive quarters and the first two months of 2013 have yielded 0.9% growth compared with January and February 2012.

The signs of sputtering growth have put pressure on the central bank to loosen monetary policy and target growth instead of inflation. Dmitry Medvedev, prime minister, said in January he would like to see 5 per cent growth, and this has been echoed in a number of statements by cabinet officials.

Elvira Nabiullina, former economy minister and adviser to Vladimir Putin, president, is set to take over as central bank governor in June, and is thought to be more dovish on inflation than her predecessor Sergei Ignatiev.

Overall there are signs that the liberal consensus in Russian economic policy over the past decade under Mr Putin has been chipping. Last week came the completion of the $55bn purchase of TNK-BP by the state, the largest nationalisation in Russia’s history. The government has recently started to ramp up spending on the military: Rbs23tn ($766bn) of additional spending on armaments are planned over the next 10 years.

By Charles Clover

South Africa

South Africa joined the Brics political grouping in 2011 in spite of lagging behind the group’s other members, both in terms of economic size and demographics. Although it boasts Africa’s largest and most developed economy, South Africa’s GDP of about $400bn is dwarfed by China, India, Brazil and Russia, while its population is 50m.

Its economic performance has been sluggish since the 2008 global economic crisis, which cost South Africa about 1m jobs.

Delivering his budget last month, Pravin Gordhan, the finance minister, revised downwards his growth forecast for this financial year to 2.7 per cent, in contrast to the 3 per cent the Treasury estimated in October.

That followed on from 2.5 per cent in 2012, a turbulent year that was marred by political infighting within the governing African National Congress and violent wildcat strikes in the mining sector which claimed about 50 lives and cost the industry billions of rand in lost production. It has also contributed to a widening current account deficient, which hit 6.5 per cent of GDP in the fourth quarter and the sharp slide in the rand, which has depreciated by about 9 per cent against the dollar this year.

With a third of manufactured exports shipped to Europe, South Africa is one of the emerging markets most exposed to the eurozone crisis. Its economic health is also adversely affected by domestic issues, including infrastructure constraints and poor investor sentiment, which has contributed to rating agency downgrades in recent months.

However, South Africa's inclusion in the Brics is seen to be less about its own economic prowess and more a reflection of Africa's role as a source of raw materials and high growth rates. The second-largest continent has enjoyed average growth of about 5 per cent, with sub-Saharan Africa forecast to grow at 5.8 per cent this year.

By Andrew England

Brazil

Of all the Brics, Brazil's economy seems to have been the worst affected by the global slowdown resulting from the eurozone's woes.

But at least some of Brazil's problems are self-inflicted, economists believe. A softening of commodity prices and global risk aversion coincided with a crackdown by Brazil on capital inflows, which it feared contributed to an appreciation of its currency against the dollar and was making local industry uncompetitive.

At the same time, a decade-long boom in consumer credit was losing steam and investors were becoming more cautious about a perceived increase in government intervention in the economy. Industry meanwhile struggled because of high costs, rising wages and weak productivity gains.

The result was a perfect storm in which the economy slowed from an above trend 7.5 per cent in 2010 to 0.9 per cent in 2012. The finance minister forecasts 4 per cent for 2013 but the consensus is for 3 per cent.

President Dilma Rousseff remains popular because unemployment is still at record lows and wages continue to rise.

But she is desperately trying to reignite investment in an effort to revive headline economic growth. The signs in January were positive with GDP starting to grow more quickly but much more will need to be done.

Ilan Goldfajn, chief economist at Itaú-Unibanco, said if the government can push through major airport, port, road, rail and other infrastructure projects, it might be able to kick-start rapid growth again.

“If you get infrastructure projects correct, other investors waiting to see if there will be a recovery will follow this accelerator factor, this will surprise people on the upside for the first time in two to three years and then people will be more confident,” he says.

By Joe Leahy.