

## **Crisis as an exam for the BRIC**

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The BRIC as an interacting community of the new centers of the world economy and international politics is a historically recent phenomenon. But over the four years it passed a long way from the start of regular political consultations on the level of Ministers of foreign affairs to the start of an annual summit. The process of intensive “quadrilogue” presents a tendency to diversification covering ever more wide range of problems dealing with the national interests of the four group members and the interests of the international community in general.

Meanwhile the analytical and scientific perception of the BRIC phenomenon presents a contradictory picture. On the one hand, it showed capacity of foreseeing (analyses by Goldman Sachs); on the other hand, it frequently lags behind the practice. Recognizing the presence of extraordinary market and industry potential in each of the four countries, some do not see a sufficiently wide basis for coincidence of the national interests; they do not see quite high rates of growth of the commercial and economic relations between the four members, what objectively does create a platform for cooperative interaction. Such interpretations shall be associated with the following two reasons. First, it`s the West-centric inertia of the contemporary global development perception. Second, it`s the aspiration of certain circles in traditional centers of the global economy and politics to impede the rapprochement of the four countries and to sow the seeds of distrust between them.

In academic community the investigation of the BRIC phenomenon till now was mainly individual and country-based passing to the genre of international comparisons. But taking into account the existing practice of interaction between the four members and probable perspective of its enrichment, the researcher`s aim is to determine the possibilities of their joint potential realization, interaction effect within the group of four and its aggregate influence on the global development

process. From this point of view, it's difficult to overestimate the importance of the present academic forum taking place in parallel with the II BRIC summit that has a chance to become a regular event.

Recognizing the relevance of the above mentioned task we involuntarily refer to the consequences of the present global economic crisis. Economic crisis which is still present brings a new quality to the global range of problems of development and highlights in a new way the role of the BRIC. It's some kind of litmus test and a difficult exam. The prism of the present crisis allows to understand better the new imperatives of the global development and how the BRIC countries could react to them, what could be their strategy in changing circumstances, logic of joint activity at the world arena.

### **1. Peculiarities of the present crisis**

Analyzing the present crisis we should be aware of the fact that it has a strongly marked **extraordinary nature**. It is prominent in the line of cyclic drops of the second half of the XX century (refer to the drawing 1), 2).

For the first time over the three decades the stronghold of the contemporary capitalism which is the USA economy became epicenter of crisis.

The present crisis holds the records in what refers to the depth of recession of the global economy, to the rate of spread and coverage of the national markets of the countries of the world.

The extraordinary nature of the crisis gave enough arguments for those who compare it with the Great Depression of the years 30s of the past century. Nevertheless, comparing parameters of these two crises we are obliged to affirm that the present one doesn't beat the records of the Great Depression in what refers to the depth of recession and its duration

(taking into consideration a modest growth since the second half of the 2009). But, apparently, it beats the records in rate of spread and coverage.

Figure 1.

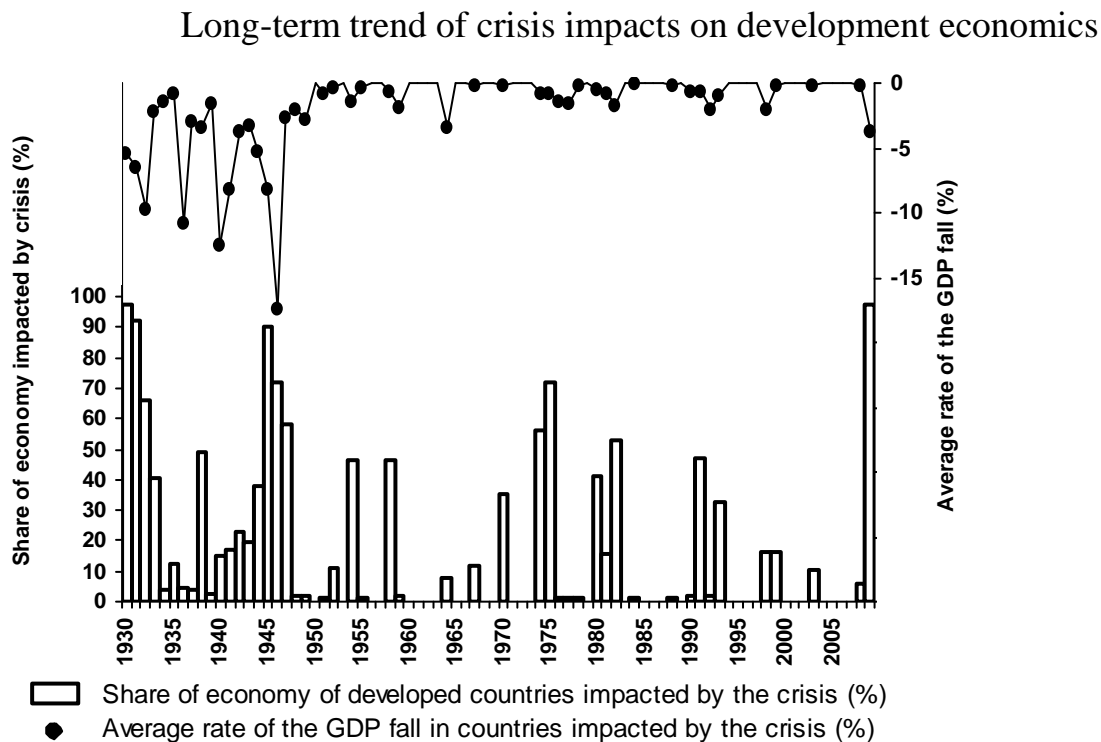
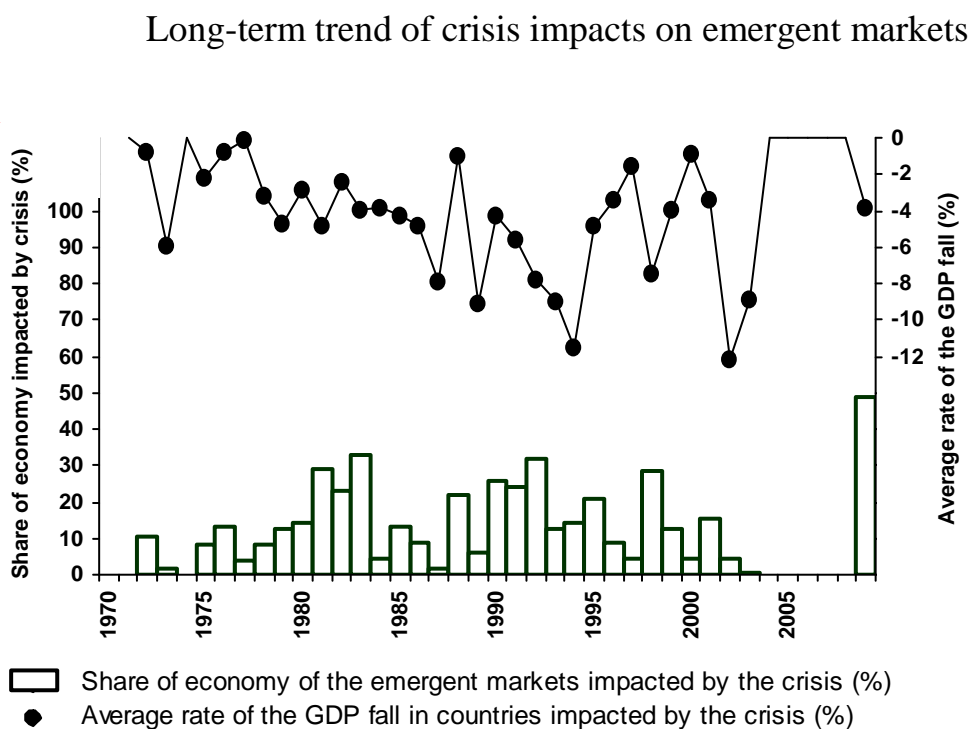


Figure 2



The last fact leads us to the effect of globalization that transformed the mechanism of reproduction in the global economy and in national economy systems. Globalization created new risks of break out of the market power in conditions when regulation on the national and international levels was based mainly on the «pre-globalization» standards.

We can affirm that the extraordinary nature of the present crisis consequences is determined exactly by this circumstance. Apparently what is meant here is the first crisis of the globalization era, a crisis that revealed so noticeably the contradictions and risks accumulated with the beginning of the globalization process based on the technological results of the «microelectronic» revolution.

The situation was undoubtedly aggravated by the neoliberal deregulation in pre-crisis period and the state`s deviation from the economic and social responsibility.

The existing national and international regulators couldn't control the dramatically accelerating processes of **overaccumulation of the financial instruments** (first of all derivatives) and **effect of overindebtness** in traditional centers of the global economy – masses of households, corporate sector and separate states. The giant sector of the offshore business became even less controllable. This is not surprising that failure in one link (at the USA mortgage market) along the whole chain of interconnection destabilized the whole globalized system of the international finances, then the international trade and then the real sector, manufacturing in the key branches of the industrial production. That`s why we find it difficult to agree with definition of the crisis as just financial one. We believe that what is meant here is **global general economic crisis**.

## 2. Reaction of BRIC countries

How did the economies of the group of four react to this extraordinary crisis? How much effective were the anti-recessionary measures taken in each case? I suppose that in the process of discussion at our academic forum our colleagues from Brazil, Russia, India and China will give their opinions based on direct knowledge of the concrete situations in each of these countries.

My task here is to give a brief preliminary characteristic of the experience of the countries of the group with an aim to compare and come to general conclusions in what refers to the lessons of the crisis, the general imperatives of the economic policy and the forthcoming agenda of interaction in the BRIC format. I'll be grateful to the colleagues for the criticism and correctives in my interpretation.

First of all I'll mention that in general the BRIC economies bear the misfortunes of the crisis better than an average of the global economy. However the countries of the group showed different level of soundness during the crisis. Let`s present some considerations according to the order of letters in the BRIC abbreviation.

So, let`s start with **Brazil**. As it was specified in The Economist magazine (London), Brazil was one of the last countries to enter the crisis and was one of the first ones to start recovering from it.<sup>1</sup> The growth of the GDP here over the 2009 practically didn't overpass the fatal zero mark staying at the minimal positive value (0.3% by some estimates, or 0.6% by other ones).

Relative soundness of the Brazilian economy after the first shocks of the crisis was ensured, in our opinion, by the least (as compared to the zone of highly developed economies) involvement in speculative financial turnover and high share of the real economy, as well

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<sup>1</sup> Brazil takes off. "The Economist 2010". London, 14-20.11.2009, p.5.

as stability of the credit and banking system and preservation of the national control in its regulation.

Furthermore, an important role was played by an effective use of the pre-crisis period of «fat cows», firstly, to transmit the external debt in a regulated channel, and then on the basis of accumulation of significant liquidity reserves to enter the category of net creditor. Second, the country managed to eliminate the old defect of the Brazilian economy achieving self-sufficiency in provision with raw hydrocarbons. Third, Brazil considerably advanced in diversification of foreign trade, substantially widening the segment of relations with the most dynamic markets (including those within the BRIC). Finally, considerable results were achieved by the realization of the large-scale social programs that contributed to the reduction of poverty area and therefore to consolidation of domestic market.

Special attention should be paid to realization of the PAC (Plan to accelerate Growth program) for the 2007-2010 period aimed mainly at modernization of infrastructure. Financial resources mobilized for this program (280 million US dollars) allowed significant advancement in modernization of transport, power system management and communications as well as expansion of house building. Thereby significant support to the business activity was ensured and, respectively, the functioning of the internal market was enhanced by the time of the crisis.

A constructive role in recovery from crisis was played by the state banks that still possess high share in the credit and banking system of the country. A share of the state banks in total volume of credit activities increased from 34% (12% of the GDP) in June of 2008 to 41%

(18.5% of the GDP) in September 2009\*. The state banks activity stimulated recuperation of the private lending by the end of the last year.

Estimates of the Brazilian GDP growth for the year 2010 fluctuate between 3-5% predicting sustainable recovery of the economy. Foreign and national businesses have already supported that, accumulating direct and portfolio investments in the Brazilian economy.

Naturally, the Brazilian case is far from the ideal situation. The Brazilian economy has quite a lot of obstacles, among them extreme social polarization and preservation of a wide zone of poverty. Enhancement of the investment climate is impeded by the high crime rate. Expenses for research and development (R & D) were increased in the country, but their level is obviously insufficient for adoption of the model of innovation development. To confirm the status of one of the global economy new leaders Brazil will need to widen the accumulation of productive investments that should increase general dynamics of the economic growth.

Reaction to crisis in **Russia** seems to be less successful, although the Russian economy had considerably higher growth rates and considerable accumulation of foreign exchange reserves during the pre-crisis period. Naturally, in this case the economic growth was favored by the high pricing environment of energy products on the world market, as well as domestic political stability ensured during the last decade.

Drastic recession in the main centers of the global economy was especially harmful for Russia due to the narrow specialization of its export on oil and gas, as well as to the fact that minimization of the external public debt was accompanied by excessive increase of the external corporate debt. The last fact could be explained by low availability and expensiveness of the long-term credit money (and vice

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\* CEPAL. Balance preliminar de las económicas de América Latina y el Caribe – 2009. Santiago de Chile, - 12.12.2009. Brasil – p.1.



versa their excess offer at the foreign market), lack of due control of the foreign loans of corporate sector by the national regulators.

Resources accumulated during the pre-crisis period gave opportunity to mobilize large amounts to overcome the liquidity shortage. As the Head of the Russian government V. Putin said, by the spring of the 2009 resources directed for recovery from the crisis equaled to 12% of the GDP. It's important to note that government has chosen to successively support the most vulnerable parts of population. While adjusting the state budget for the years 2009-2010 the main articles of the social expenditures remained in their initial amounts, some of them were increased. That naturally restrained the effect in other areas in short term perspective.

Among the programs launched were partial etatization of distressed assets of the strategically important companies, support of the cities with extremely narrow specialization of economy that allow to prevent catastrophic spread of unemployment. Some measures, although insufficient, for support of the small and medium business (taxes exemptions and enlarged access to credit financing) were also taken in the 2009. The results of the measures taken became notable since the middle of the 2009. Drop in production in some industries was arrested. The unemployment growth stopped by the end of the year; it began to reduce gradually by the beginning of the 2010.

Meanwhile those who criticize the anti-recessionary measures reasonably note that their realization was accompanied by sensible delay and considerable expenses. In the process of «pumping» liquidity in the banking sector, no strict limits were set for special-purpose use of the credit means provided by the government. As result they were used for financial and exchange transactions, and leak of the capital took place. Bureaucratic vertical in anti-recessionary measures implementation was late several months.

Nevertheless, resuming we can affirm today that positive tendencies dominate. Learning lessons from the grave crisis the government of the state adopted a policy aimed at modernization of economy, diversification of exports, successive transition to innovation-based development. It's an absolutely necessary strategic change.

The traditional orientation of the **Indian** economic policy (founded yet by J. Nehru), directed towards the auto sufficiency of the country, revealed itself in the anti - crisis policies of nowadays. The state support of the banking system was realized rather narrowly, whereupon the volumes of micro credits were widened. The internal consumption was stimulated by the tax regulations. Considerable investments were directed to the infrastructure area. Meanwhile this area (including its transport and energy branches) is still a weak and a vulnerable point of the Indian economy. There are some reasons to foresee by the 2010 to the previous GNP growth rates, though the long- term dynamics is impossible without the modernization of the infrastructure.

The recent decision about the free secondary education - is a great step forward in the accumulation of the "human capital" directed towards the surmounting of social backwardness. Though hard for the state budget, this decision in the long term will change the situation on the labor market. But in the short term it will aggravate the budget deficit, which is nowadays the highest among the BRICs (evaluated as 6,4% of the GNP for 2010).

The **Chinese** economy was previewed to maintain the stability of income on the maximum level for the crisis period (about 86%). The results of the 2009 affirmed that. Surely, the situation was smoothed by the avalanche currency reserves of more than 2 trillion dollars and the grown up internal market. But for China this indicator is not fully satisfactory. Its demographic and social imperatives do demand higher development dynamics. Its slow down will undoubtedly sharpen the

internal contradictions and disproportions in the economics as well as in the Chinese society.

Meanwhile, the image of China as one the most powerful locomotives of the modern economy is getting even stronger. The Brazilians not without reason think, that the exports to China - is its strongest anti-crisis reserve. Indeed, in 2009 the PRC overshadowed the USA as the leading importer of the Brazilian goods. Meanwhile in other directions there were noted severe limitations.

The anti-crisis policy in China was limited by the following main actions: directed financial support of the strategic enterprises; transfer from the “hard” to the “soft” financial and credit policy; from the practices of slow raising of the national currency course to its binding by the dollar course (with a view to maintain exports); development of the inner consumption, including the special prices for the long-term goods; broadening of the social security scales (among the country people); return to export stimulation policy through the mechanism of taxation.

The colossal financial reserves, accumulated by this country by the beginning of the crisis permitted to destiny a sum up to half billion dollars to maintain the real sector of economy. A special attention was paid to the projects of infrastructure, which became an additional impulse to the accelerated modernization of the transport and energy systems began even before the crisis. In sum, the volume of the anti-crisis measures, taken by the beginning of the last year is evaluated as 13% of the GNP.

The existing political system helped the state to operatively direct its decisions for the fulfillment on the local level. The “power vertical” in China provides for the “transmittance” of its decisions not only at the upper and medium level of governance, but also at the level of the economic agents. It ties up not only big, but, practically, all medium private sector enterprises. Surely, one shouldn't overvalue the Chinese

“vertical”. But one needs to recognize: during the world economy crisis the government did much to strengthen the economy discipline. It could mobilize the reserves of the internal market, the preferential development of which was planned still in the decisions of the XVII Congress of the Communist Party of China.

### **3. Some lessons of the crisis and interaction among the BRIC countries.**

With all the positive or negative features, which revealed themselves during the crisis, we can state, that the BRIC`s do remain the part of the world economy, which can seriously contribute to its dynamics. The overall input of the BRICs in the world GNP growth in 2008 was more than 52% (see table 1).

Table 1.

Contribution to the dynamics of world economy

	Share in world GDP	Share in the increase of world GDP
USA	20,7	2,7
Japan	6,2	- 1,5
Euro zone	15,6	3,9
EU (27)	21,9	7,6
<b>BRIC</b>	22,3	52,5
Brazil	2,8	4,6
Russia	3,3	5,8
India	4,9	11,0
China	11,3	31,1

Source: Estimated basing on IMF and WB statistics. Год планеты. Ежегодник. Выпуск 2009. Гл. ред. В.Г. Барановский. М., 2009, с. 302.

If we compare the forecasts about the dynamics of the GNP of the world economy leading centers, we will see that in the “peak” of the crisis - in 2009 and in the period after it (2010 - 2011) the BRICs have a good chance to continue as the main “donors” of the world economy growth, more to that - to enhance their contribution.

Table 2.

## Estimations and forecasts of increase (decrease) of GDP

	2009	2010	2011
USA	-2,4	3,1	2,9
Japan	-5,7	1,7	1,6
Euro zone	-3,8	1,2	1,4
<b>BRIC</b>			
Brazil	0,3	5,0	4,5
Russia	-7,0	3,5 (5,0*)	4,3
India	5,5	7,7	8,0
China	8,2	9,6	8,1

\* WB estimations

Source: The Economist Intelligence Unit – The Economist. London. 28.11.2009, p.97; 27.03.2010, p.97.

As it seen, the main locomotive nowadays and in the nearest future will be the Chinese economy, immediately followed by the Indian. The vulnerability of the Russian economy, which revealed itself in the “peak” of the crisis, demands an adequate evaluation with a view of radical correction of the situation. But on our point of view it shouldn't be dramatized. First, the reanimation of the business activity from the second part of the last year and the continuation of this trend in the

present give some grounds for optimism. The inflation gets lower, unemployment lesser, the internal market grows and credits go cheaper, foreign investment enters the country.

It's crucially important that, counting with the situation in Russia, the political leadership of the country came to the decision to make a strategic shift in the economic development towards the innovative model of the economy.

Russia can be an important link in the platform of the strategic and the innovative mutual adaptability of the BRICs, not speaking about its important geopolitical role. Along with Brazil it possesses extraordinary natural resources, which gains the significant value for China and India, counting with the growing resource and ecological limitation of growth in both countries. The scientific potential of Russia, its know-how in the space and energy (including nuclear) technologies and in other strategic fields, give us serious reasons to think about the possibility of a large scale cooperation based on a mutual interest.

Table 3.

## BRIC: volume of mutual exports.

	2007	2008	2009
<b>Brazil</b>			
Exports to BRIC (\$ bln.)	15,4	22,2	26,5
Share of BRIC in total exports	7,8	11,2	17,3
<b>India</b>			
Exports to BRIC (\$ bln.)	12,4	14,5	13,0
Share of BRIC in total exports	8,5	8,0	7,0
<b>China</b>			
Exports to BRIC (\$ bln.)	64,0	83,5	71,1
Share of BRIC in total exports	5,2	5,8	5,8
<b>Russia</b>			
Exports to BRIC (\$ bln.)	19,3	28,4	23,7
Share of BRIC in total exports	5,5	6,0	7,9

Source: WTO (stats.wto.org); UN (unstats.un.org). Federal custom service of RF.

During the last years the mutual trade between the BRICs proves the objective character of the need of cooperation between the “four”. In the last decade (until 2008) the mutual trade growth rates as a rule were significantly higher than the medium world ones and the rates of the BRICs trade with the traditional centers of the world economy.

More to that, one should pay attention that in 2009 the indicators of the mutual trade between the “four” showed major stability compared with the general world conjuncture. One could definitely say that this sector of the world trade resulted the most durable in the atmosphere of the crisis.

In general, within the BRICs we have the reduction of the commodity export values at 20,4%. The general world indicator is 23, the EU (27 countries) - 21,3%, Japan - 25, 7%.

In Brazil the exports to the BRICs zone even grew absolutely from 22,2 billion dollars in 2008 to 26,5 billion in 2009. As a result, the share of BRICs in the Brazilian exports grew from 11,2 to 17,3%.

Russia, which experienced a significant fall of its exports (mainly by the value of it), nonetheless augmented the share of sales in with the BRICs destination - from 6,0 % (2008) to 7,9 % (2009). The share of the BRICs in the Russian of trade turnover rose from 9,5 to 11%.

Somehow this indicator lowered for India - from 8 to 7%. But in case trade with Russia the situation is the opposite - the volume of Russian exports rose in 2009 by 13,5%. And the Indian exports to Russia stayed at the 2008 level.

The situation of 2009 in China is different. After the stable raise of the commerce volumes to the BRICs zone during the pre-crisis period (up to 2008), there was observed a significant fall - approximately to

26,5%. Nevertheless, the conjuncture of the first months of 2010 shows, that the commercial activity in the BRIC direction has a recovery tendency.

Surely, every BRIC country draws its own lessons from the crisis. We'd like to pay attention to the conclusions, which are common to all of them, which refer to three levels of analysis. The first one deals with the problems of the national development, the second - with the relations within the BRIC, the third one - with the coordinated positions on the reconstruction of the international regulatory mechanisms in the world economy. Precisely in this respect we'll try to expose some ideas.

The crisis with all the evidence strengthens the organizational work of the state in the processes of the economic development, industrial modernization and the process of innovation. It presupposes the determination of the strategic perspectives of the development and creation of the beneficial conditions for the business activities, though not replacing the business in the spheres, where it can effect significantly. All the BRIC countries do possess the prerequisites of such approach in the traditions of their economic policies and in their social psychology.

Special significance here acquires the economic security mechanism and the ability of the preventive anticyclic actions. The problem is not in the accumulation of vast international reserves, but in the ability to use of them in a productive and rational way.

Besides, also critical is the capability to control the involvement of the national economy and its financial sector to the transnational speculative interchange. The lessons of the crisis are significant enough in this sense. The future perspective of the development does not provide any guarantee of non revision of those ups and downs. The long statistical rows directly point up to that historic regularity, to the probability of the cyclic fall up to the end of the next decade. The corrections, made in the economic policy and in the mechanism of the



state regulation still do not make us believe that this can prevent the transformation of the next ordinary crisis into extraordinary.

In all the four cases the first place is occupied by several key issues, without which it's impossible to maintain high standards of the economic growth for a long time and to provide a progressive modernization. We speak about the primordial development of the infrastructure, the backwardness of which in all the four cases has become one of the strongest obstacles, that places in question the possibility of high dynamics of economical growth in a long term.

One of the main imperatives – the increase of efforts and means with a view of limiting the levels of poverty and income disproportions (social and territorial). Without this the BRICs won't make active the potentially enormous reserve of its inner markets for a long time and in so doing to elevate their stability during next cyclic ups and downs (especially extraordinary ones).

The BRIC countries enter in the innovative époque with the different histories and different prerequisites. The aim of Russia - to stop the erosion of the R&D sphere (having a great heritage), to re-establish the intermediate links in the chain, which connects the fundamental science and the sphere of production, to construct a system for effective incentives in the enterprises.

In other cases the task of the “four” can be exposed in other way. China has seriously moved forward in the imitation phase of the innovation cycle and does a lot to “construct” the higher stages. But, still, it demands long time and significant work. In India and Brazil there have been created the minimum prerequisites for the deployment of the innovative process in some perspective directions, though the lack of resources, qualified cadres and institutional incentives still limit the leap forward. So there is a need of concentrated efforts along all the innovative chain, but, specially in the upper “stages” of the R&D.

Since the launch of the consultative mechanism of the BRICs on the diplomatic level, the political “quadrilogue” has begun, it seems, to take the upper hand of the economic cooperation, which up today was being realized on the bilateral level.

Though one must recognize that recently there took place four-lateral consultations on several economic issues (finance, energy, agriculture). For the first time there takes place the businessmen meeting during this very summit in Brasilia. But, it`s evident that the future must be connected with the mutual realization of the big scale projects (not necessarily with the participation of all, “triangles” also permitted). The areas of common interest could be the aerospace sphere, the sphere of the traditional and non- traditional energy, the resolution of the food problem.

The trade between the “four” has already proved its growing significance for the BRICs. Its possible growing in the perspective - is a great reserves for the stability of the four economics (especially during the extraordinary falls). This must be surely counted for in the trade and economic policy of the BRICs. Still there is no talk about any of the integration programs. As it seems, there hasn`t yet formed the necessary objective prerequisites for that. But we can`t exclude the appearance of the necessity to elaborate the four sided programs of the branch cooperation.

The coordinated position of the BRICs on the correction of the deficiencies in the world economics and financial architecture has already demonstrated itself in the G-20 summit in Pittsburgh. There was made a first step towards the redistribution of voices and capital in the key world financial institutions. But it is obvious that the process is still in its beginnings. The world community, the G-20 (as its economically most ponderous part) still lack the comprehensive receipts of the world mechanisms reconstruction. There exist much talking about this, but still

there is a lack of a political will to make serious changes and also the principal actors seem technically not to be ready for them.

I don't think that we can speak about the sui generis "world economic government" with more proportional representation. Still in the agenda is the improvement of the existing institutions with critical approach to their experience or using them as the raw materials for the building of new architecture. The process of the restructuring has already begun on the regional level. The EC actively discusses the perspective of the European IMF, some experiments in this direction are also taking place in Latin America on subregional level. The BRICs undertake preventive measures to safeguard themselves from the dollar fluctuations, diversifying their financial actives and transferring part of their payments to the national currencies.

In these conditions the BRICs as a sui generis coalition of the ascending economies, not only interested in the world economic stability, but possessing a unique potential, is capable to play an historic role in the movement of the world community towards a mechanism of global regulation, adaptable to the needs of the XXIst century, in minimization of the transitional period risks and elaboration of a flexible formula of the world economy stable development.