
BRIC Revisited

By Lothar Katz

"The economy is strengthening!" "But are we out of the recession yet?" "Well, we saw positive growth in 3Q and 4Q." "Yes, but things are still weaker than in 2007 and unemployment remains high." ... (etc.)

If you're like me, you're sick and tired of this debate. Whether economic growth rates have been slightly positive for the last two consecutive quarters, which technically defines the end of a recession, seems secondary to the bigger questions of how much of a recovery we will see in the near term and how sustainable it will be. The leading economies of North America and Europe, all of which were hit hard by the downturn, have shown a few encouraging signs of improvement. The solidity of these indicators remains subject to much debate, though, and we don't seem to have reached solid ground by any means.

For anyone keeping an eye on the global economy, it is interesting to check how others are doing. The BRIC group of Brazil, Russia, India and China remains the poster child for the league of developing and emerging (D&E) markets. Before the global crisis, there was much talk about "decoupling," a theory postulating that the fate of those countries no longer depended on Wall Street or the London Stock Exchange, as their markets were believed to be strong enough to guarantee independent stability. However, the stock market slides in the fourth quarter of 2008, only a few months after the demise of Lehman Brothers that started the global economic crisis, quickly shattered this theory: the BRIC group seemed to fare no better than the rest of the world did.

How did things pan out since then? A quick look reveals a few surprises:

The Biggest Loser

The Russian economy experienced an unprecedented contraction in 2009, when its GDP shrunk by about 9%. (In contrast, the GDP of the United States was essentially flat over 2008.) The main culprit was a lasting dependency on oil and other natural resources, coupled with a continuing lack of strong domestic players in the industrial and service sectors. Wealthy Russians kept spending, so the luxury goods sector was left relatively unharmed. Middle-class and low-income families, however, had to cut back substantially, which resulted in an overall drop in household spending of more than 8%.

The country is expected to recover at a rate of about 3-4% this year, although some analysts are less optimistic. It may take several years for Russia's economy to return to pre-crisis levels. Unfortunately, it appears that the government has not yet identified strategies that would allow the country to do any better than this.

Strength in Times of Weakness

Latin America's economies also suffered badly last year, contracting by almost 2%. A notable exception was Brazil, which maintained a positive GDP growth rate of about 1%. Offsetting tough market pressures on energy, natural resources and other commodities, the country's industrial and service sectors continued to show strong performance. In

addition, tax breaks introduced by the government kept consumer spending going. Predictions for 2010 point to healthy growth in the 4-5% range.

The third member of the BRIC group performed even better. With last year's growth rate of more than 6% and 2010 forecasts north of 7%, India's economy proved most skeptics wrong and demonstrates continued strength in sectors such as industrial manufacturing, service and process outsourcing, and for-hire R&D. Part of that success was driven by high levels of government spending, so India is now wrestling a sizeable fiscal deficit that nurtures growing inflation woes. Nevertheless, the damages India suffered in the downturn were less severe than those with which many other countries had to cope, and its economic outlook remains favorable.

And the Winner Is ...

Ignoring complaints about unfair trade practices and calls to adjust the artificially inflated value of its currency, China trudged along at a remarkable pace in the midst of the recent economic storms. While down from the double-digit rates of earlier years, it achieved still-stellar GDP growth of 8.5% in 2009 and expects to see another 8-10% in 2010. Such rates make almost all other countries envious, including some with much smaller markets. Considering the size that its economy has reached, China's economic pace is all but unprecedented.

Much of this success is owed to the government's bold and swiftly-executed fiscal stimulus plan, combined with loose monetary policies. As in other cases, these measures came at a price, making foreign goods more costly and triggering inflation fears. To a large degree, though, China's undeniable progress is owed to its well-established strength in manufacturing, its continuing investments in infrastructure, and the ever-growing focus on the development and/or acquisition of technological know-how. None of these factors are expected to change any time soon and China will likely represent one of the world's most attractive markets for a long time to come.

A Lesson to Learn

Every economy is different and the global crisis has presented each government with its own set of challenges. Nevertheless, it is apparent, not only from looking at the BRIC group but also from tracking the progress of other D&E markets, that countries with a strong focus on nurturing their industrial base and expanding their service and consumer markets have mastered the global crisis far better than others. In a way, those countries indeed managed to "decouple" their economies from a global downturn.

Anybody notice that this observation offers a valuable lesson to every country, no matter how large or mature its economy?

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