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RIS Policy Brief

Economic Cooperation among the BRIC

Prospects for cooperation between Brazil, Russia, India and China (BRIC) in international economic governance have improved as all four countries are now members of the major institutions involved in international economic governance, except Russia that is still not a member of the World Trade Organization (WTO), and they all are members of the G20 which has taken on the responsibility of steering the world economy and overseeing the operations of the major international economic institutions. The ability to influence the operations of these institutions had been limited till now as none were members of the G7 which dealt with economic issues and did not include Russia as it was not considered to be a market economy, and the G7 had earlier sought to chart the course for these institutions. Their quotas at the International Monetary Fund (IMF) and the World Bank (WB) which determine voting power were very low and limited their opportunities to influence the policies at these institutions. Now these quotas have also been adjusted so that developing countries as a group have about 4 per cent more of the voting share.

The economies of Brazil, Russia, India and China (BRIC) are large as they are, at official exchange rates, the tenth, thirteenth, eleventh and fourth largest economies respectively with large populations as they are all among the six most populated countries of the world. The four economies have been reforming; Brazil to tackle its debt crisis and the hyperinflation in the 1980s and 1990s and the others to create more market oriented open economies. These economies have now reached a successful stage of macro management with low rates of inflation, high rates of growth and a satisfactory balance of payments position. China and India have grown rapidly at an annual average of over 10 and 7 per cent respectively for a period of three decades. The other two have performed well in the last few years before the current financial crisis after prolonged periods of low growth in Brazil because of debt and hyperinflation and declines in GDP in Russia because of the dislocations caused by the collapse of the Soviet Union. Despite this rapid growth the per capita income in these countries is low, being only 8, 10, 2 and 4 per cent of that in the US in Brazil, Russia, India and China respectively.

These countries have been integrating with the world economy both in the trade and finance areas. The share of exports in GDP has increased for all these economies; the share of Brazil and India more than doubled between 1990 and 2006 as the share in Brazil increased from 7 to 15 percent and in India from 11 to 23 per cent. The share in China almost doubled from 23 to 40 per cent during this period. Russia was the laggard as its share increased only from 29 to 34 per cent. Clearly Brazil and India are lagging in their integration with world markets in goods. Russian exports are concentrated in the area of natural resources as fuels accounted for 63 per cent in 2006 and

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ores and metals another 8 per cent. Chinese and Indian exports are concentrated in manufactures. Brazil has a more diversified export structure as it is one of the world's largest exporters of agricultural products while also a significant exporter of manufactures. India is much more integrated with the world market in services than the other three economies, as service exports are almost two-thirds of goods exports for India whereas for the others they are only about 10 percent.

Financial integration has also grown. India is catching up with Brazil and China as destinations for foreign direct investment and Russia has surpassed them if one looks at the ratio of FDI to GDP. But the really significant aspect of their integration with the world's financial markets has been in outward flows of FDI which have increased very substantially for these economies.

The interest of the BRIC countries in international economic governance is driven by their need to develop as per capita incomes are still very low and their development strategy which stresses the beneficial effects of integration with the world economy. This requires that the world economy provide a stable environment for trade, capital flows and an international system which provides them with a safe vehicle for their reserves. A depressed world economy, particularly in the developed countries, has very deleterious effects on these economies. Low levels of economic activity in the developed countries would reduce demand for their exports and is likely to increase protectionist pressures; though there have been few protectionist measures in the current recession, this may not always hold true, which would further harm their exports. Furthermore, Brazil and Russia would suffer a terms of trade loss as the prices of their primary products, whether natural resource based or agricultural, would fall.

They are likely to push for a change in the orientation of the G20 as compared to the G7 given their concern about economic development. The main pre-occupation of the G7 had been on macroeconomics in order to prevent the emergence of large imbalances in interest rates or exchange rates among them. Occasionally they did seek to give direction to multilateral trade negotiations exhorting their negotiators to complete the negotiations expeditiously or seek to accelerate growth in Africa through debt cancellation or promising larger aid flows. But interest in development of African countries was sporadic and there was no significant follow up to ensure that their commitments were fulfilled. This was also true of their pronouncements about the Doha Round of multilateral trade negotiations. The BRIC and other developing countries are more interested in development and improved access to the markets of the developed countries. Focus of the G20 might be very different from that of the G7.

Since demand in the developed countries is likely to grow very slowly exports to these markets is unlikely to be an engine of growth. Furthermore, as an important aspect of the globalization of these economies has been the growth in their ties with other developing countries. Trade among Asian countries has been very dynamic and Brazil has been the hub of trade among Latin American countries. Time seems ripe for these economies to take the lead in enhancing economic linkages among themselves and invite other developing countries to also join in. There is considerable scope to cut tariffs in developing countries. But cooperation among developing countries should not be limited to trade. Since Brazil, Russia, India and China are important providers of FDI, FDI flows to other developing countries could be part of increased South-South interaction promoted by BRIC countries. This would be an important contribution as products produced by enterprises in these countries are more suited to the income levels in developing countries.

The BRIC countries along with other developing countries would like a well functioning international economic system. One of the most important aspects of this is to limit barriers to trade. Markets in the developed countries are not very hospitable to developing countries. The developed countries maintain high subsidies to protect their agricultural sectors. Given the small employment in this sector and the rise of big agribusiness it is clear that this is not to protect employment or small farmers. While not reducing these subsidies the developed countries are pushing for liberalization of agriculture in developing countries where a large part of the population depends on agriculture for its livelihood and has no other option - job creation in manufacturing has been low. Furthermore, tariffs in developed countries on products of interest to developing countries, namely labour intensive products, are high. Therefore, developing countries wish that these tariffs be lowered. So the trade agenda which the developing countries would like to push would include reduction of subsidies to agriculture in developed countries, reduction of import duties in developed countries on labour intensive manufactures, liberalization of restrictions that limit exports of labour intensive services from developing countries. Furthermore, there is need for changes in TRIPs to make it easier to improve and develop technologies in developing countries so that productivity can increase faster in developing countries.

Uncertainty about the value of the dollar and of the impact of high budget deficits in the US were matters of concern to the BRIC countries, China in particular had expressed concern on a number of occasions. Developing countries had been diversifying away from the dollar and holding increasing amounts of euros. But the recent turmoil in the eurozone and the sharp decline in the value of the euro have created additional uncertainties for developing countries. The international adjustment system was not working well and developing countries, not China alone, were holding increasing amounts of foreign exchange reserves as a precaution against any balance of payments crisis. This is not only a waste of these countries' savings but also unprofitable as the return on reserves was lower than the interest rate that developing countries had to pay on their borrowings; because at the same time as reserves were increasing so were their short term borrowings.

An important issue for poorer developing countries is that aid flows have been shrinking whether measured as a proportion of GDP or investment or imports. While private capital flows have been increasing in importance, developing countries have only a limited capacity to afford them because of their servicing implications. The inability of poorer countries to service debt at market rates of interest is not a new phenomenon, but that has occurred throughout history. The history of debt crises and restructurings since the third quarter of the nineteenth century has been studied intensively, and it is clear that borrowings at market rates of interest can only be serviced if borrowings are very small and conditions favourable. Very often in recent years equity flows have been tied to privatization and may stop once privatization programmes are completed. An important feature of the economic performance of many developing countries despite the improvement is that investment levels remain much lower than what these countries had achieved in the past in the late 1960s and early 1970s. It is imperative that investment levels rise if incomes are to grow and poverty reduced. Aid flows need to be increased and their efficacy improved. The experience of the BRIC countries combined with that of other developing countries in the G20 could help in the formulation of policies that enhance the efficacy of aid. Also ways have to be found for private capital to be channeled to the poorer developing countries.

Though the BRIC are becoming more important it must be remembered that they account for less than 10 per cent of world GDP at the moment whereas the US and the EU account for about a quarter of world GDP. Except for China their share of world exports is also very small. As yet they may have limited power to affect outcomes. As can be seen from the negotiations in the Doha Round they were able to block negotiations on issues such as labour standards or many of the "Singapore issues", but were not in a position to achieve their objectives. Being included in the G20 will in part be a learning process where they can firm up their own perspective and gradually change those of the developed countries. An overtly confrontationist approach, as happened with the negotiations about the New International economic Order in the 1970s, may face the same fate of a failure at least in the short run. Negotiations in the 1960s about softer aid and preferential access to markets in the developed countries which came to be known as the generalized system of preferences were more successful as they harnessed the interest of the developed countries.

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