BRICS: Dead or Alive?

Growth without Representation: The Limits of the BRICS Challenge to the West

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Key Points:

- The author of the BRIC(S) concept correctly predicted in 2001 that the group of developing countries would account for a significant share of global GDP by the end of the decade, and would consequently demand greater representation in existing global economic institutions.

- Initially, the BRIC(S) countries largely ignored the new acronym, and sought to promote political and economic integration through existing foras.

- A sense of disappointment with the voting distribution in Western institutions—particularly after promises made during the 2009 G20 Summit—led the BRICS countries to pursue alternative integration projects. This gave rise to the Contingent Reserves Arrangement (CRA) and the New Development Bank (NDB).

- Despite an overall increase in intra-BRICS trade, the group's economic foundations remain shaky. The share of mutual trade within the BRICS does not exceed 20% of total foreign trade for any member country, and the group is never projected to reach the levels of internal trade observed within the EU or NAFTA.

- China is the dominant member and the engine of the BRICS, whose economic weight in the group surpasses that of the United States in the G7. However, Beijing's competing "One Belt, One Road" project promises to overshadow the BRICS while bypassing all current members but India.

- Moving forward, the BRICS will remain a transitional union as long as the group continues to provide marginal economic gains for China. After that point, China will shift its resources to other integration projects that promise to be more effective by being regionally focused.

Introduction

The acronym "BRIC" was proposed in November 2001 by then-Goldman Sachs' Chief Economist, Jim O'Neill, who in looking for potential sources of future economic growth had predicted the inevitable shift of global economic power toward emerging markets.[1] He grouped together four countries (Brazil, Russia, India, China[2]) based on their growth rates and the size of their economies, and forecasted that by 2010 the combined weight of these countries in the global economy would be significantly greater. As a result, he concluded that "world policymaking forums should be re-organized, and in particular, the G7 should be adjusted to incorporate BRIC representatives."

O'Neill's prediction horizon is well behind us. Today, the BRICS have become not merely an acronym but a process of integration, albeit not a very formalized one. But is the BRICS group of countries a real power in the current world? And could it grow in importance over time?

Correct Predictions

O'Neill's prediction about the subsequent decade turned out to be fairly precise. In the paper that first introduced the BRIC concept, O'Neill outlined four different scenarios based on differences in GDP growth rates and exchange rate movements (which influence purchasing power parity, or PPP) to arrive at the following prediction: "the relative weight of the BRICs rises from 8.0% at present (in current US$) to 14.2%, or from 23.3% to 27.0%, converting at PPP rates."

The real picture from 2010-2013 resembles something very close to that (*See Charts 1-2*). By 2010, the weight of the BRICs had reached 26.64% of global GDP by purchasing power parity. This was despite the fact that O'Neill had overestimated the growth of China (mainly due to exchange rate movements), while underestimating the growth of Russia (due to the jump in oil prices) and India.

If we go further back in time, it is worth emphasizing that the process of the BRICs' weight increase had even accelerated in later years, though the nature of this process had changed. After the global financial crisis of 2008-2009, the BRICs' weight in nominal GDP continued to grow and reached 20.5% of global GDP (an increase of four percentage points). That was not a surprise—many of the developed countries had lost their economic dynamism in the aftermath of the crisis. What is key is that by 2013 (the most recent data available), the increase of the aggregated weight of the BRICS in global GDP (by PPP) was significantly smaller—only two percentage points, approaching a total weight of 30%.

The faster growth of the BRICS' share in nominal GDP is evident in theory—the more developed the country, the smaller the gap between its market exchange rate and PPP rate—and we may envision that the gap between the BRICS' share in PPP-based GDP and nominal GDP will continue to shrink in the coming years, though at a slower rate.

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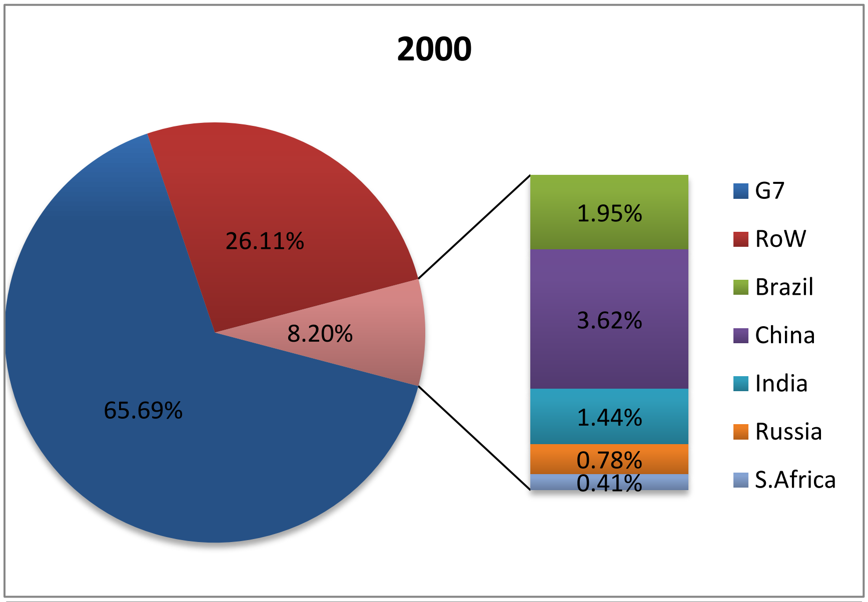
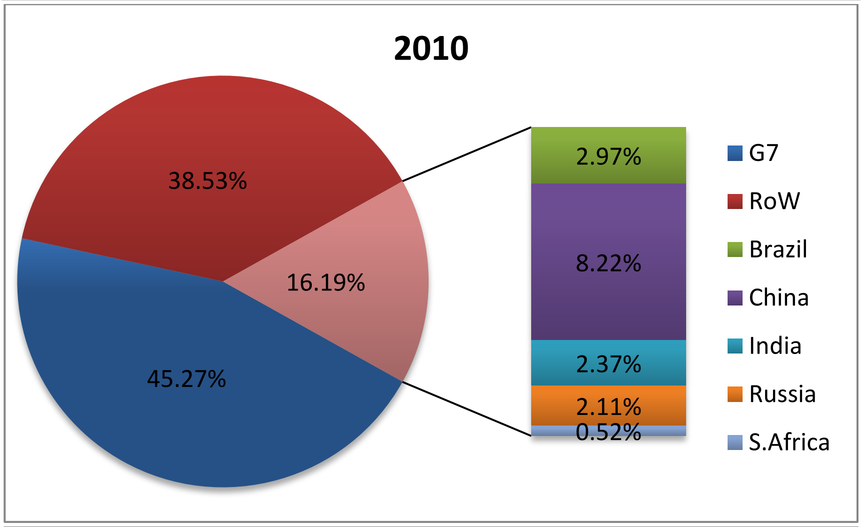
[1] Jim O'Neill, "Building Better Global Economic BRICs," GS Global Economics Paper No: 66, November 30, 2001, http://www.goldmansachs.com/our-thinking/archive/archive-pdfs/build-better-brics.pdf.

[2] South Africa was added later, in 2011, and apparently mainly on the basis of the first letter in the country's name: if we look at the size and dynamics of the South African economy, such countries as Indonesia, Mexico, Iran or Nigeria promise to be significantly more important economic players in the future. This paper will use the acronym "BRIC" when referring to the group prior to 2011, and the acronym "BRICS" for subsequent years.

Chart 1. Share of BRIC(S) Countries in Global GDP (nominal $)





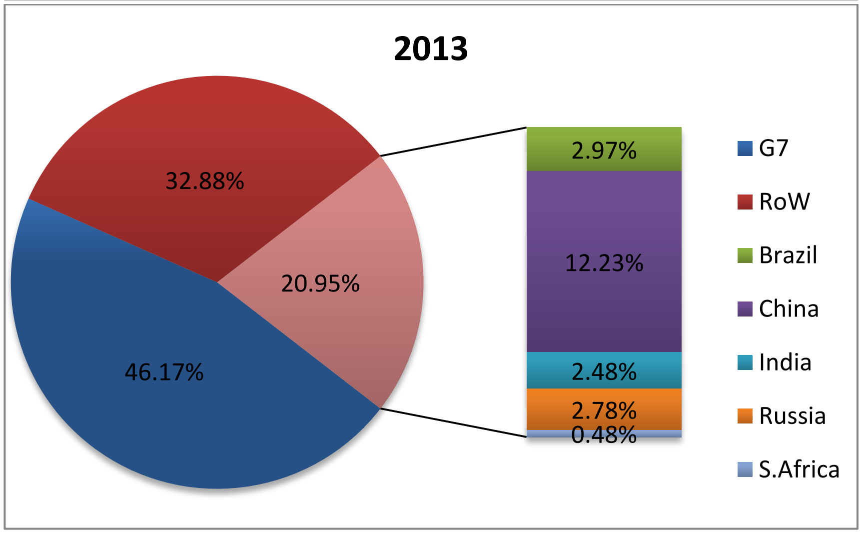
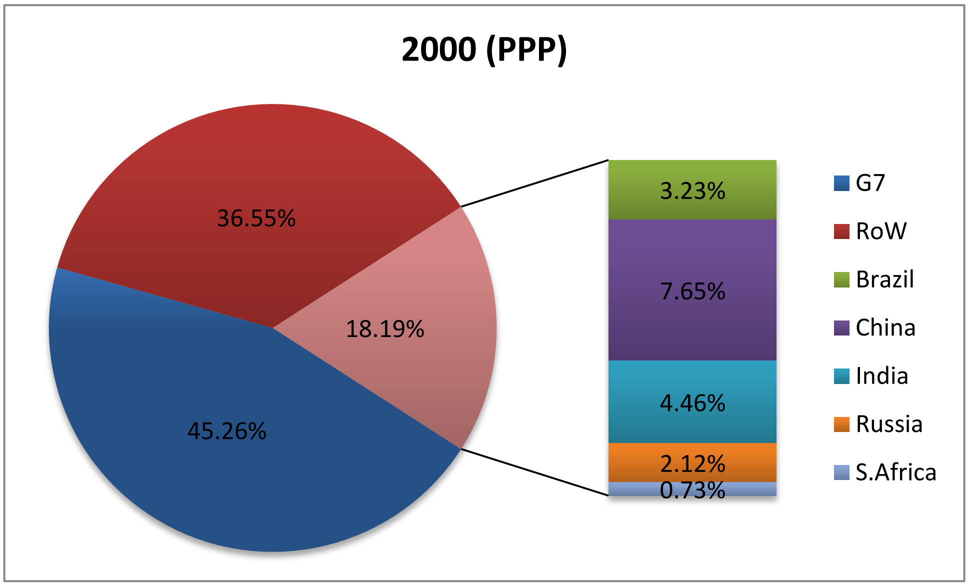
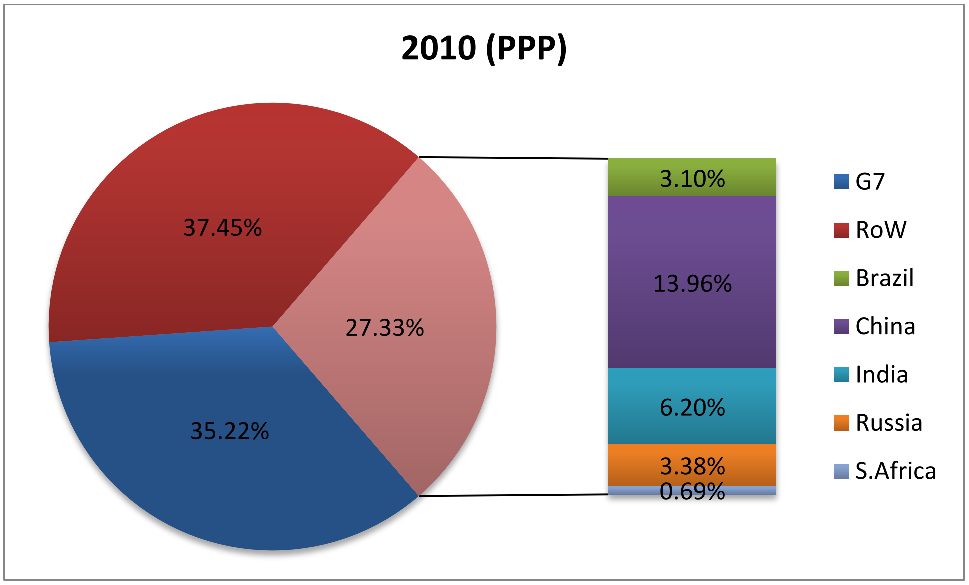
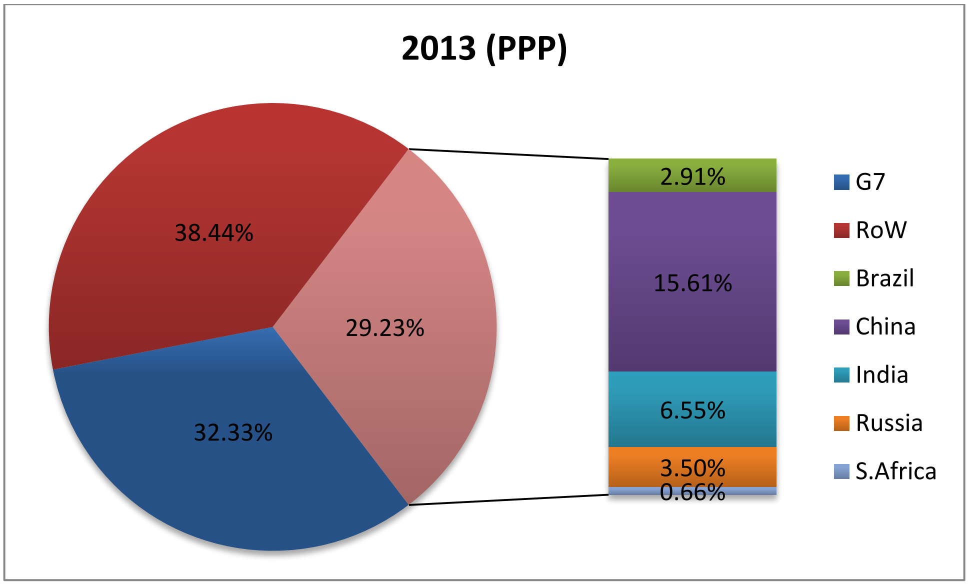


Chart 2. Share of BRIC(S) Countries in Global GDP (PPP-based)







Greater Weight without Greater Role

Today, the share of the developed countries (G7) in the global economy (according to PPP-based GDP) exceeds that of the BRICS. But we can predict, based on easily observable factors, that the situation will change no later than by the end of this decade. Of course, the BRICS' share in the world economy will not reflect in any manner the technological and intellectual leadership of the developed countries. Indeed, the BRICS have failed to become the main drivers of the global economy, as nowadays their share in global trade (17%) is even smaller than their share in nominal GDP.

But it is difficult to argue with O'Neill's second prediction: that the BRICS would naturally begin to request greater representation on the global stage. To a certain extent this development became evident to international leaders (including leaders of the G7 countries) in April 2009, during the G20 summit in London. Today we know that by that point, the global economy had weathered the lowest point of its decline. But at the time, many believed the economic crisis would continue and that further deterioration would occur.

During that summit, G20 leaders recognized that the best mechanism they had to cope with the crisis—the International Monetary Fund, which was in theory ready to get the job done, but in reality did not have the money to do so. The institution needed new funding but, being very similar to a shareholder structure, it could not rely on all member countries to make their contributions due to budgetary and/or institutional constraints. As a compromise, it was agreed that the BRIC countries would provide loans to the IMF in exchange for a promise by the G20 to change the capital structure (and, as a result, the distribution of voting rights) in the institution in favor of the emerging countries, with China set to become the main beneficiary.

Six years have passed since then. Today it remains to be seen when, if at all, the G20 countries will make good on that promise.

Waiting No Longer

Initially, the BRIC countries were not strongly integrated economically or politically. In fact, for the first several years they paid little attention to the new acronym. As a result, the first meeting of their foreign ministers in 2006 was not able to produce any concrete results.

This situation changed in 2009. On the one hand, the emerging economies, though being badly hit by the global crisis, had learned the lessons of the previous two decades. They faced the global storm in a much stronger financial position, thanks to having promoted a prudent macroeconomic policy that allowed them to build up significant fiscal and foreign exchange reserves. That put them in a stronger bargaining position during the G20 summit in London. On the other hand, by that time Russia had reformulated its foreign policy to declare that it did not see any potential for strengthening its relations with the West.

Moreover, then-Prime Minister Vladimir Putin began to blame Washington for its mistakes in economic policy and to advocate for another type of global economy, one that would not be based on the dominance of the West. His call was aided by the fact that U.S.–China relations had not significantly improved since the events on Tiananmen Square in 1989, while the economic rise of China had resulted in significant tensions in bilateral talks (reflected in disputes over climate change, currency manipulation, and the call to "Buy American").

All of these factors came together to bolster the resolve of BRIC leaders when they met for their first top-level meeting, in Russia in 2009. During that event, the leaders agreed that there was no need to build a separate institution and instead reached a consensus around two points: (i) strengthening coordination within multilateral foras, with a focus on economic and political governance; and (ii) promoting cooperation between BRIC member-states.

Alternative Institutions

Once the global crisis was over and the United States had *de facto* withdrawn its promise of IMF reform, China felt itself cheated and humiliated. That became the main foundation for the idea, announced in March 2013, to build an alternative financial institution within the BRICS that would serve as a counter to the IMF and the World Bank. The New Development Bank (NDB, formerly known as the BRICS Development Bank) was established in 2014 with a subscribed capital of $50 billion, and was aimed at financing infrastructure and development projects in the BRICS members and other developing countries.

The BRICS members also agreed to create the Contingent Reserves Arrangement (CRA), a fund with an initial sum of $100 billion that the BRICS countries would be able to draw upon to resist short-term liquidity pressures. So far, there has been little visible justification for creating such an instrument, not least because use of the CRA is limited to its members only. This can hardly be of any assistance to China, which is allowed to borrow an amount that is slightly more than 0.5% of its own foreign reserves. Brazil, India and Russia can hardly benefit from CRA as well, as their limits to borrow from CRA are equal to 5% of their own reserves. The only BRICS member that stands to benefit from the fund is South Africa, which is able to borrow an amount that is equivalent to 25% of its own reserves.

Though it is too early to analyze the activities of either institution—in fact, it would be fair to say that neither yet exists—it is clear that by establishing these institutions, the BRICS countries (and China above all) want to demonstrate their belief that the Western approach does not incorporate (or postpones the incorporation) of rising powers into the global decision making process, and therefore cannot be tolerated any longer.

However, the biggest obstacle to the future development of both the NDB and the CRA is the obvious mismatch of interests among the BRICS member-states. Russia and to a lesser extent Brazil actively promote an anti-American agenda, advocating the idea of an international alliance of countries willing to get rid of the dollar.[3] Other BRICS members, starting with China, are primarily seeking economic benefits and have so far been unwilling to deploy their resources in support of political adventures that might lead to confrontation with the West.

Table 1. Bilateral Trade within BRICs in 2008: Share of Export and Import as % of Total Export/Import

	EXPORT TO					
	Brazil	**China**	**India**	**Russia**	**S. Africa**	**BRICs**
Brazil		8.29	0.56	2.35	0.89	12.09
China	1.31		2.21	2.31	0.60	6.43
India	1.79	5.55		0.60	1.36	9.30
Russia	0.44	4.52	1.12		0.01	6.09
S. Africa	0.89	5.83	3.08	0.33		10.13
	IMPORT FROM					
	Brazil	**China**	**India**	**Russia**	**S. Africa**	**BRICs**
Brazil		11.57	2.04	1.92	0.45	15.98
China	2.64		1.79	2.10	0.82	7.35
India	0.37	10.00		1.41	1.76	13.54
Russia	1.75	13.02	0.64		0.17	15.58
S. Africa	1.90	11.31	2.58	0.35		16.14
Share of the country in World GDP	1.95	3.62	1.44	0.78	0.41	8.20

[3] "BRICS Morphing into Anti-Dollar Alliance," *Sputnik News,* July 3, 2014, http://sputniknews.com/voiceofrussia/2014_07_03/BRICS-is-morphing-into-an-anti-dollar-alliance-6229/.

Table 2. Bilateral Trade within BRICS in 2013: Share of Export and Import as % of Total Export/Import

	EXPORT TO					
	Brazil	**China**	**India**	**Russia**	**S. Africa**	**BRICS**
Brazil		19.01	1.29	1.23	0,76	22,29
China	1.63		2.19	2.25	0,76	6,83
India	1.82	4.88		0.72	1,71	9,13
Russia	0.38	6.76	1.32		0,05	8,51
S. Africa	0.69	12.66	3.15	0.42		16,92
	IMPORT FROM					
	Brazil	**China**	**India**	**Russia**	**S. Africa**	**BRICS**
Brazil		15.57	2.65	1.12	0.3	19.64
China	2.78		0.87	2.03	2.48	8.16
India	0.82	11.08		0.82	1.58	14.3
Russia	1.11	16.88	0.06		0.25	18.3
S. Africa	1.55	15.48	5.2	0.37		22.6
Share of the country in World GDP	2.97	12.23	2.48	2.78	0.48	20.94

An Economic Foundation for BRICS?

While political interactions between the BRICS members have become more frequent and tightknit—if the countries are not able to formulate common goals, for example, they run permanent consultations within many international institutions and foras—their underlying economic fundamentals do not appear as encouraging.

At first glance, the BRICS do matter. The share of bilateral trade with other member countries (as a percentage of total imports) has increased for all BRICS members between 2008 and 2013. But in analyzing the data (Table 1 and 2) it is easy to see that the share of mutual trade within the BRICS does not exceed 20% of total foreign trade for any member country. Meanwhile, only Brazil and South Africa have an import share from other BRICS members that is bigger than the share of BRICS in global GDP. The two biggest BRICS economies, China and India, have virtually failed to increase the share of other BRICS members in their export. And for four of the five member countries (Brazil, India, Russia, South Africa), the overall increase in imports from other BRICS countries was smaller than the growth of the share of Chinese imports alone.

Still, since the BRICS countries have a greater economic growth potential than do developed economies, it would not be a mistake to predict the further growth of bilateral trade within the group. But this growth will be slow and will likely never reach the level of mutual trade that is observed within the European Union (60%) or between Mexico and Canada within NAFTA (50%). The main reason for this—aside from geography—is the reliance of all BRICS countries except China on primary products (fuel, metals, wood, minerals, food, animals) in their exports. The share of primary products in their exports is significantly greater for Brazil, Russia and South Africa than the share of these products in their imports.

But looking ahead, we can expect the relative growth of primary products in overall trade to naturally decline as the BRICS economies move to produce goods and services with greater added value, resulting in the decline of relative resource consumption. While this process may lead to the contraction of intra-BRICS trade, the continuously accelerating growth of the Chinese economy and its rising share in world GDP will inevitably lead to the growth of its share in the foreign trade of all BRICS countries. And if India follows China's path, it may become another driver that boosts the global economy, along with the trade volume within the BRICS.

Table 3. Share of Primary Products in BRICS Foreign Trade (% of)

	Export		Import		Import from BRIC(S)	
	2008	2013	2008	2013	2008	2013
Brazil	62.89	67.18	34.1	31.9	21.0	16.6
China	16.01	13.32	36.8	36.8	71.2	50.5
India	44.04	43.27	49.4	52.2	22.5	18.4
Russia	81.85	84.46	24.4	25.2	10.1	9.6
S. Africa	49.48	50.14	36.0	35.9	25.1	25.8

BRICS as a Vehicle for China

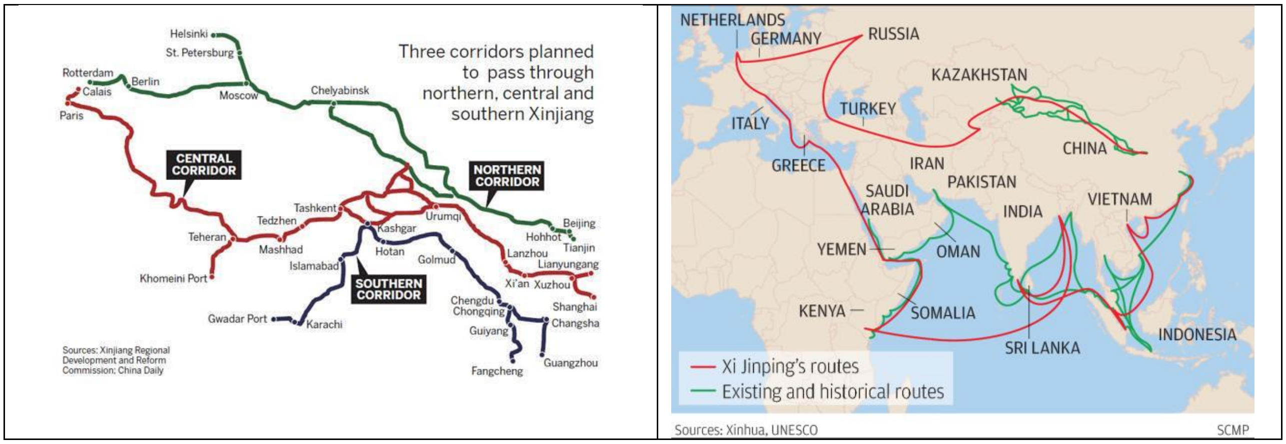
China has existed as a continuous and self-sufficient civilization for the last five thousand years. Throughout its history, China was the center of its own mono-polar world, having no need to build alliances or to rely upon foreign partnerships by virtue of being much bigger and much more powerful than its neighbors. Adding to this the fact that China dominates within BRICS by its economic power even more that the United States dominates within the G7, one should not be surprised that the BRICS forum—based on multilateral consensus and China's preference of economic pragmatism to political posturing—can hardly be considered a long-term strategic instrument for Chinese policy.

Facing the slowdown of its economic growth, China recently became much more active in identifying new sources of development, including new markets for its goods as well as new places for investing its capital, largely in neighboring regions. The rapid rise of the "One Belt, One Road" project, accompanied by the creation of the Asian Infrastructure and Investment Bank (AIIB)[4]—a direct competitor to the New Development Bank of the BRICS—demonstrates that China is ready to make any decisions necessary and quickly deploy its own capital in the effort to reach its economic targets.

[4] The creation of the AIIB is another result of China's reaction to its perceived humiliation by the West: the United States and Japan had prevented the increase of China's share in the Asian Development Bank (the Chinese share is currently 6.5%, compared to Japan's share of 15.7% and a U.S share of 15.6%).

The possibility of future Asian economic integration occurring around the "One Belt, One Road" plan has a much stronger basis than potential BRICS-led integration, as it relies upon two sound assumptions: 1) that trade relations between neighboring countries are usually stronger than between countries located distantly one from another, and 2) that better infrastructure promotes trade.

Chart 3. Different Views on "One Belt, One Road" Paths



While the details of the "One Belt, One Road" plan are not fully clear, Chinese officials have declared it will include not only the construction of roads and ports but of oil and gas pipelines, power production and electricity grids, and telecommunications infrastructure. China will provide the bulk of the financing, having already announced an injection of $40 billion into the Silk Road infrastructure fund and another $50 billion into the AIIB, with other countries to invest the same amount. This makes China the dominant player and decision maker in the process of regional economic integration, placing a number of options at its disposal. There should be no doubt that the main underlying idea of this plan is to benefit China: to support the country's economic growth by supplying investment goods and speed up the development of the problematic Xinjiang-Uygur province.

Due to geography, only one BRICS country—India—may directly benefit from this plan. Russia will not be an obvious beneficiary, as its eastern regions are rich in natural resources but lack the necessary connecting infrastructure, such as roads, and are located significantly to the north of any potential New Silk Road path.

At the same time, the economic potential located in the European part of the country has not, and by all accounts will not, get access to the next generation of fast-growing emerging economies: namely Iran, Pakistan and Turkey. As a point of comparison, the combined PPP-based GDP of these three countries is equal to that of Russia, while their population (and by extension, their future market potential) is 2-3 times bigger. Therefore, it should not be a surprise if the world's new economic tigers soon emerge from this part of the world—or if one day they decide to launch new projects of economic integration, with China (and India) as their key engines.

Conclusion

O'Neill's prediction was spot on: the weight of the BRICS in the global economy has increased significantly since 2001, approaching 30% of world PPP based GDP by 2013, and will continue to grow further. The author of the acronym did not propose any level of formal economic integration between these countries, and today there is no evidence that trade within BRICS is expanding based on some type of invisible synergy. Therefore, hardly any economic rationale exists for the establishment of formal ties between the members of this union. On the other hand, the BRICS countries have been able to launch a mechanism of multilateral political dialogue that—while not yet allowing them to promote new initiatives—nonetheless provides them with a tool to avoid public tensions.

Meanwhile, the United States and the G7 neither followed O'Neill's advice on incorporating the new economic powers into high-level economic dialogues, nor delivered on their promise to change the voting rules within the IMF and the World Bank. Nor have they accepted China's request to include the Chinese renminbi into the Special Drawing Rights (SDR) basket maintained by the IMF, which already includes the U.S. dollar, the euro, the pound and the Japanese yen. These rebukes may make a growing China less inclined to participate in Western-financed institutions, thus making these institutions weaker and less influential. At the very least, the incorporation and capitalization of new China-supported international financial institutions (such as the NDB, CRA, and AIIB) should make developed countries cognizant of China's negative attitude toward any further discussions on the marginal increase of its role in existing institutions.

For many years, the United States had wanted China to become a more responsible international player. And now China is doing just that, mainly in the economic sphere, by becoming active in multiple international foras and more clearly asserting its national interests and goals. It seems the BRICS as an economic platform is a transitional step for China. None of the BRICS members can provide China with the modern technology or potential markets for Chinese goods that it will need as its economy continues to expand. The one exception is India, a close geographical neighbor which may benefit from the Chinese-led economic integration project "One Belt, One Road."

Moving forward, we can expect the BRICS to remain a transitional union as long as the group continues to provide marginal economic gains for China, its dominant member. After that point, China will shift its focus and resources to the nascent economic integration projects discussed above, which promise to be more effective by virtue of being closer to home. Meanwhile, in the sphere of political dialogue, the BRICS may be supplanted by the Shanghai Cooperation Organization—a regional club of Asian big nations whose membership already includes China, India and Russia.

About the Author

Sergey Aleksashenko is the former Deputy Finance Minister of Russia (1993-1995). While working for both the Russian Central Bank and the Ministry of Finance, Aleksashenko was in charge of negotiations with the International Monetary Fund. From 1995 to 1998 he served as First Deputy Chairman of the Russian Central Bank, where he was responsible for monetary and currency policy. He later served as Deputy Director General and Managing Director of Interros, a Russian private investment company, from 2000 to 2004, and was head of Merrill Lynch's Moscow office from 2006 to 2008. The author of numerous articles on Russia's economy, he is also the author of *Battle for the Ruble* (Alma Mater, Moscow, 1999; Vremya, 2008). A former scholar-in-residence in the Carnegie Moscow Center's Economic Policy Program, he is currently an independent consultant for Private Solutions LLC.

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