The World's Fastest-Growing Economies Won't Be Scary Unless They Slow Down
By Charles Kenny, July 21, 2014

As Brazilians were recovering last week from the World Cup, the country held another global event: the BRICS summit, a gathering of leaders from Brazil, Russia, India, China, and South Africa. The outcome was no doubt more pleasing to Brazil’s President Dilma Rousseff than her country’s soccer performance. The countries agreed to set up a $50 billion “BRICS bank” to invest in development projects in the developing world, alongside a $100 billion pool of reserve currencies earmarked as “a kind of mini-IMF,” according to Russian Finance Minister Anton Siluanov. It was a strong statement of the grouping’s growing global economic heft and a challenge to the order established by the International Monetary Fund and the World Bank.

Some in the West have perceived that challenge as a threat. The U.S. has veto power over major decisions at the International Monetary Fund. Without European or American backing, it is almost impossible to get a loan through the World Bank. The North Atlantic powers will have no such say in the operations of the BRICS bank, another sign that the global balance of economic and financial power is shifting.

The BRICS do pose a threat, but their own development bank isn’t it. The more worrisome risk is that the BRICS won’t grow as quickly as they have in the past, that the grand plans hatched in Brazil will dwindle along with the economies supporting them. If pessimistic forecasts of Asian and Latin American economic performance turn out to be justified, that’s no reason for cheer in Washington or Brussels—collapsing growth in the developing world would be terrible news for the West.

Brazil, Russia, India, and China are the world’s four largest emerging economies. (At No. 11, South Africa is an outlier; it was included in the group in 2010 to ensure African representation.) Together the members account for a little more than one-quarter of global gross domestic product and around half of developing country output. All have been on a tear. From 2003 to 2013, China’s GDP increased 164 percent; it now accounts for 15 percent of global GDP. India’s GDP approximately doubled over the same decade. The economies of the three remaining BRICS grew by 40 percent or more.

The rapid growth is slowing. IMF forecasts suggest China will grow at above 7 percent this year, India at 5 percent, and Brazil at less than 2 percent. Russian growth is projected to be flat. Predictions farther into the future are all over the map—and notoriously unreliable. In one study of the reliability of forecasts of Chinese growth, a pair of researchers from George Washington University concluded (PDF) that any ‘expert’ prediction more than six months out was likely to be less accurate than the simple approach of suggesting the previous year’s growth would remain unchanged. Recent analysis by the IMF itself found that errors in its medium-term forecasts—a year or less—are large: 2.2...
percentage points of GDP for emerging economies. The fund also found that inaccuracy is sticky. Over-optimistic forecasts remain over-optimistic and pessimistic forecasts remain grim, even as new information comes in.

And so on. Past performance has never guaranteed future returns. Former Treasury Secretary Lawrence Summers, writing with Harvard’s Lant Pritchett, has noted that rapid growth in one decade is, as often as not, followed by slower than average growth in the next. If history is any guide, some of the BRICS are due for a slowdown.

China in particular has been an outlier, the only country that has ever managed to extend a period of 6 percent-plus growth for more than 32 years. Any number of factors could end that run. Government intervention and a slowing property boom have propped up growth, while banks still carry a lot of bad debt. Nonperforming loans in the country are worth almost $100 billion, according to a February estimate from the China Banking Regulatory Commission. Over the longer term, the country can’t count on its export-led model to sustain growth: From 1990 to 2010, China’s share of world exports climbed from about 1 percent to about 10 percent. The same rate of growth over the next 20 years would leave it with a 100 percent share. And at any point, turmoil linked to regional disputes over territory or democratization could send the economy into a spiral.

Collapsing growth in the developing world would be a huge crisis for the West. If China were to grow at the rate it did in the first decade of the 21st century for the next 20 years, its GDP would be $60 trillion by 2033. If it were to grow at the rate of the average country—around 2 percent per year—it’s economy would be one-quarter that size. The difference is $45 trillion—about three times the size of the U.S. economy in 2012. As the BRICS summit declaration noted, “Our economies have consolidated their position as the main engines for sustaining the pace of the international economy as it recovers from the recent economic and financial global crisis.” It used to be that if the U.S. sneezed, the rest of the world caught a cold. Increasingly, sickening economies in the South can doom prospects for recovery and growth in America and Europe.

Consider the turnaround in Detroit. In 2004, GM sold one car in China for each 10 in the U.S.; five years later, the ratio was approaching one-to-one. If China’s growth stalls, car sales will, too. In 2012, the developing world imported more than half of the world’s exports, up from one-third in 2000. Almost three-fifths of American exports headed to emerging markets in 2012, more than double the proportion in 1990. If those markets nose-dive, America’s recovery is likely to follow.

There are reasons for greater optimism regarding the future performance of the BRICS—after all, the East Asian Miracle of rapid growth has been declared dead many times (not least after the financial crisis of 1997), and countries have bounced back to rapid growth. More than one-third of workers in China and roughly half of the labor force in India are still employed in agriculture, which suggests considerable opportunity for workers to move to higher-output sectors in two countries with a strong base of productive industries.

The U.S. and Europe should be doing what they can to ensure that the economies of the developing world continue to outperform. That includes support for a stronger International Monetary Fund, which can monitor crisis risk and help respond if it occurs. Even as the BRICS were establishing their “mini-IMF,” they made clear that IMF reform toward a more equal representation of the world’s economies remains a priority for them. U.S. legislation to allow that is stuck in Congress, and it will be America’s loss if the IMF is weakened as a result. Just as important, it means a changed mindset—from viewing the BRICS as economic competitors to a perspective that sees them as vital partners in sustaining the growth of global prosperity in North and South alike.
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