Booms, busts and protests – normal life in emerging countries

By Ruchir Sharma

Unrest and slowdowns mark the end of a placid decade, writes Ruchir Sharma

Protests erupt in the formerly happy middle classes of Turkey and Brazil. A credit crisis threatens the Chinese economic juggernaut. Money flees the stocks, bonds and currencies of emerging nations. Is this the end of the emerging world miracle? Not exactly. This marks a return to the normal postwar cycle of recession and recovery, political unrest and calm, after a misleadingly placid decade.

This age is chaotic only in comparison to the brief “Goldilocks” era that began in 2003. Before that year, the emerging world’s share of global economic output had been stagnant for half a century and in decline for a decade, undermined by debt crises that struck from Thailand to Russia. By the late 1990s, these emerging nations were turning to a new generation of leaders, headed by the likes of Luiz Inácio Lula da Silva in Brazil and other giants, including Vladimir Putin in Russia and Recep Tayyip Erdogan in Turkey.

These leaders laid a stable economic foundation for the boom that began in 2003 after the US Federal Reserve and other central banks cut interest rates sharply to engineer a recovery from the technology bust. Much of the resulting easy money flowed into the emerging world, doubling the average annual gross domestic product growth rate to about 7.5 per cent from 3.6 per cent in the previous two decades.

This boom was unprecedented. Normally, each emerging nation is at a different stage in its economic life, in which crisis gives birth to reform, which flowers into a boom, which matures into political complacency, which ages into a new crisis. By 2007 virtually every emerging nation was in a boom – only three of 150 emerging economies contracted that year – creating the illusion of a world populated only by the young and content. The middle classes embraced their leaders as heroes; Lula, Mr Putin and Mr Erdogan won re-election by growing margins.

Then, in 2008, the credit crisis erupted in the US, making emerging nations look even stronger. By mid-2009, emerging economies were growing a record 9 percentage points faster than developed economies. Convinced these countries had discovered a fountain of perpetual growth, money flowing into emerging market stocks rose by 500 per cent between 2005 and 2010.

That was then. Now the global flows of goods and money are declining. The annual GDP growth rate of emerging nations fell back to 3.7 per cent in the first quarter, and the normal cycle is back, with some nations in crisis, others in stages of reform, boom or complacency. The largest, China, had by 2008 hit the stage when all miracle economies grow too large to sustain double-digit growth, but it kept growing with huge infusions of state spending and credit. Now, the explosion in total debt from 150 per cent in 2008 to more than 200 per cent of GDP increases the risk that China’s slowdown could end in a stall.

As China slows, economies that fed its demand for commodities are hurting. Declining prices have undermined commodity exporters such as Russia, South Africa and Brazil, which helps partly explain why mine strikes hit South Africa, and anti-Putin protests hit Russia, months before the unrest in Brazil.

Typically, leaders who start a boom grow complacent and cannot keep the run going. Neither Mr Putin, nor the party of Mr Lula and his successor Dilma Rousseff, did enough to diversify away from commodities and relied too much on state intervention to steer growth. In Turkey and Brazil, protesters ask why leaders spend billions on construction megaprojects, rather than education and other social infrastructure needed to take these economies to the next level.

What the negative headlines miss though is the rest of the emerging world. For every nation mired in crisis, there is one reforming like Mexico, under a trustbusting president, and booming like the Philippines, once Asia’s laggard.
Is the miracle over? The tailwinds that lifted all emerging nations are gone. The declining flow of money to emerging nations is bringing back the cycle of boom and bust, and with it political unrest. But emerging nations still represent 80 per cent of the world’s population, and just 40 per cent of global GDP, so there is room for growing prosperity. Just not in every nation, all the time.

*The writer, head of emerging markets and global macro at Morgan Stanley Investment Management, is author of ‘Breakout Nations’*

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