BRICs Monthly

Issue No: 11/06

June 24, 2011

Goldman Sachs Global Economics, Commodities and Strategy Research at https://360.gs.com

The BRICs Remain in the Fast Lane

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The BRICs continue to advance up the ladder of global economic prominence. Their strong growth performance during the global economic crisis has accelerated this trend. All of the BRICs have now reached, or are rapidly approaching, the range of the G7 countries in terms of the total size of their economies. However, living standards in the BRICs continue to lag far behind the developed world.

In recent years, the BRICs have continued their steady climb up the global rankings of economies by size, as measured by US Dollar-denominated GDP. 2009-10 proved to be watershed years in this regard. China moved past Japan to become the world's second-largest economy. Brazil passed Spain and Italy to become the seventh-largest economy, and is now fast approaching the UK. India and Russia both jumped over Spain to move into ninth and eleventh positions, respectively. Notably, the BRICs' positions look even more favourable if we instead compare countries' GDP using PPP exchange rates. While we have long expected the BRICs to catch up with the majority of developed countries eventually, these shifts are happening even quicker than we envisaged.

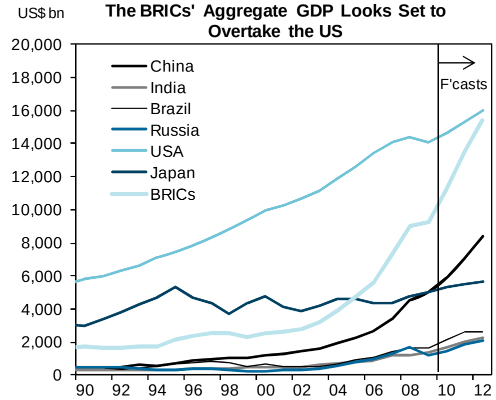
BRICs Move Up USD-denominated GDP Rankings

	2007	2008	2009	2010	2011*	2012*
1	USA	USA	USA	USA	USA	USA
2	Japan	Japan	Japan	China	China	China
3	China	China	China	Japan	Japan	Japan
4	Germany	Germany	Germany	Germany	Germany	Germany
5	UK	France	France	France	France	France
6	France	UK	UK	UK	UK	UK
7	Italy	Italy	Italy	Brazil	Brazil	Brazil
8	Spain	Russia	Brazil	Italy	Italy	Italy
9	Canada	Spain	Spain	India	India	India
10	Brazil	Brazil	India	Canada	Russia	Russia
11	Russia	Canada	Canada	Russia	Canada	Canada
12	India	India	Russia	Spain	Spain	Spain
13	Korea	Mexico	Australia	Australia	Australia	Australia
14	Mexico	Australia	Mexico	Mexico	Mexico	Korea
15	Australia	Korea	Korea	Korea	Korea	Mexico

*based on forecasts from our regional economists
Source: GS Global ECS Research

The recent reshuffling in country rankings towards a more BRIC-heavy top ten is due both to the stronger growth performance during the crisis and recent currency appreciation, although the importance of each factor varies across countries. In China and India, stronger growth has been key. In Brazil, the surge in USD-denominated GDP growth is largely due to a nearly 50% real appreciation in the Real in 2009-10. In Russia, the picture has been more mixed on both fronts.

The BRICs' Aggregate GDP Looks Set to Overtake the US



Source: GS Global ECS Research

While all of the BRICs will likely soon be among the ten largest economies, living standards continue to lag far behind the developed world. Encouragingly, we expect China and India to continue to register among the fastest GDP per capita growth rates in the world, but their low starting bases mean that convergence to developed market levels is still a long way off.

The BRICs Move Up the Ranks of Economic Size...

In recent years, the BRICs have continued to advance up the ladder of global economic prominence, in line with our projections, which we first laid out in 2003 and last updated in 2008. This trend was further accelerated by the global financial crisis, which produced a notable reshuffling of countries according to economic size (as measured by US Dollar-denominated GDP). While cyclical fluctuations and exchange rate variability can produce large shifts in rankings that ultimately prove temporary, our forecasts suggest that the recent advances made by the BRICs should have staying power.

2009-10 proved to be watershed years in this regard. In a much-anticipated and highly-publicised development, China moved past Japan last year to become the world's second-largest economy, with an annual GDP of just under $6trn. Only the US, whose aggregate output was around $14.5trn in 2010, remains larger than China. Less heralded but perhaps more surprising, Brazil passed first Spain in 2009 and then Italy in 2010 to become the seventh-largest economy in the world, and is now fast approaching the UK. India jumped over Canada in 2009 and Spain in 2010 to move to the ninth position. While Russia saw a notable slide in 2009 due to its poor performance and massive depreciation during the crisis, it managed to surpass Spain (for the second time) in 2010. The crisis also provoked a minor reshuffling among the BRICs themselves, as Russia slid from being the second-ranked BRIC in 2008, behind China, to the lowest-ranked by 2010. In aggregate, the BRICs' GDP is now worth over $11.2trn, or over 75% of that of the US. Perhaps more importantly, the BRICs' (with the exception of Russia) continued strength in the recent period, despite weakness in the developed world, means that they have also become the dominant drivers of global growth. The BRICs have contributed over 50% of global growth (measured in USD terms) over the past three years, compared with an average of 27% in 2000-07.

According to our regional economists' near-term forecasts, China, India and Brazil should remain in their current positions through the end of 2012. Brazil and India should continue to encroach upon the UK and Italy, respectively, and in both cases they look likely to overtake far earlier than we originally projected. We expect Russia to surpass Canada for the second time in 2011. All of the BRICs should be among the ten largest economies in the world by the end of this year.

While we have long expected the BRICs to eventually catch up with most developed countries, these shifts are happening more quickly than we envisaged in our last set of projections from 2008, before the crisis unfolded. While we correctly foresaw that China would surpass Japan in 2010, we thought that Brazil would not pass Italy for another ten years, and that it would not threaten to overtake the UK for nearly 20 years. India's strong crisis performance has lifted it into the largest ten economies sooner than expected, while Russia's contraction in 2009 pushed it to a lower ranking than our projections implied. We also did not expect the BRICs as a group to overtake the US until 2018, a development which now looks set to occur within the next few years.

It is important to point out that the BRICs' positions in the global economy look even more favourable if we instead compare countries' GDP using PPP exchange rates (which adjust for the fact that non-tradable goods

BRICs Move Up USD-denominated GDP Rankings

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6	France	UK	UK	UK	UK	UK
7	Italy	Italy	Italy	Brazil	Brazil	Brazil
8	Spain	Russia	Brazil	Italy	Italy	Italy
9	Canada	Spain	Spain	India	India	India
10	Brazil	Brazil	India	Canada	Russia	Russia
11	Russia	Canada	Canada	Russia	Canada	Canada
12	India	India	Russia	Spain	Spain	Spain
13	Korea	Mexico	Australia	Australia	Australia	Australia
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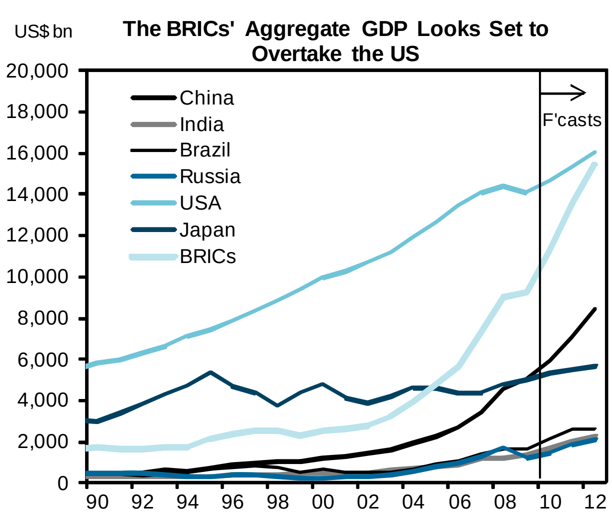
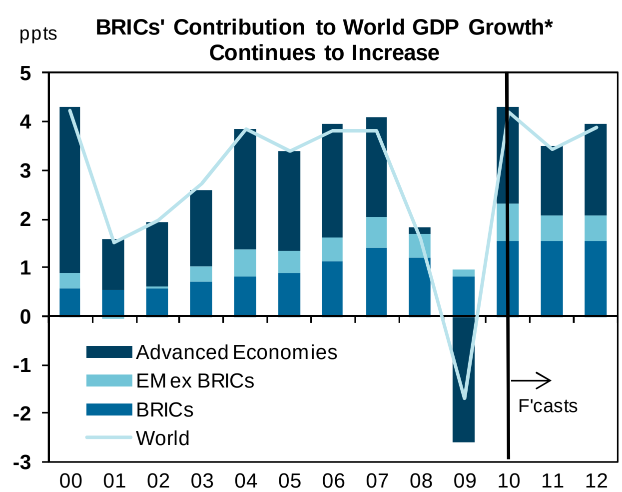


Source: GS Global ECS Research



*measured in USD terms
Source: GS Global ECS Research

tend to be cheaper in developing countries, so that market exchange rates tend to underestimate the true purchasing power of the local currency). According to PPP-based rankings, China has been the second-largest economy in the world since 2001, India will move into the third position this year, and all of the BRICs have been in the top ten since 1994.

...Thanks to Strong Growth Performance in the Crisis and Recent Currency Appreciation

What explains the reshuffling in country rankings over the past few years towards a more BRIC-heavy top ten? It is important to remember that GDP growth in USD terms is driven both by underlying real GDP growth and by currency appreciation. Over the longer term, our optimistic outlook for the BRICs is based on our expectation both that they will grow at a rapid clip as they 'catch up' to developed country productivity levels, and that their currencies will appreciate in the process.[1]

We can separate out the importance of each of these factors across the BRICs to better understand the evolution in USD-denominated GDP levels. In China and India, stronger growth has been key. Both weathered the global financial crisis far better than the developed world and most of their emerging market peers, experiencing only a slight reduction in growth rates in 2009. Brazil was also aided by its growth performance; while it did experience a small contraction in 2009, it bounced back vigorously in the subsequent year and was actually operating back near capacity within a few quarters. Only Russia underwent a severe recession and a tepid subsequent recovery, which was a major factor in its slide from the eighth- to 11th-largest economy in the world. Indeed, its average annual growth rate has been just 0.5% over the past three years, down from 7% in 2000-07.

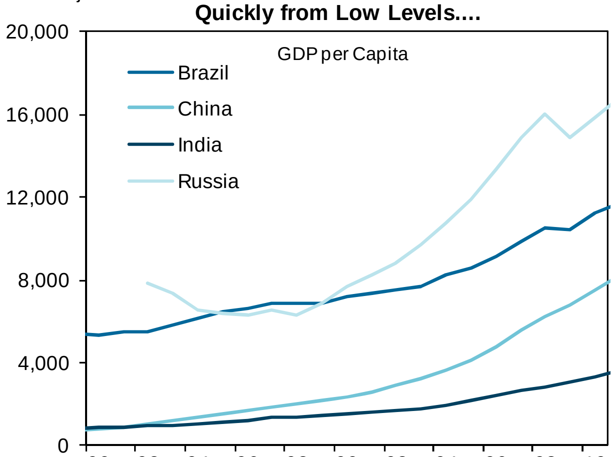
Turning to exchange rate movements, all countries have seen a real appreciation against the USD over the past few years. This occurred despite rapid depreciation during the depths of the crisis in all of the BRICs except China, as the USD strengthened on the back of 'safety' flows. Recent currency strength has played a particularly large role in Brazil, which experienced a real appreciation of nearly 50% over the course of 2009-10 on the back of both higher inflation and significant nominal appreciation. This is a much more rapid appreciation than we envisaged in our 2008 projections. China's USD-denominated GDP figure was also aided by renewed appreciation in 2010, after a pause in 2008-09. Conversely, India and Russia received a much smaller boost in their USD-denominated GDP from appreciation. Both the Indian Rupee and Russian Ruble have strengthened in real terms since 2008, but this has largely been due to higher inflation; their currencies have actually weakened nominally over the past three years. While it is possible that some of these exchange rates shifts could reverse or slow going forward for cyclical reasons, the underlying long-term trend is still towards stronger real exchange rates.

Living Standards in the BRICs Remain Far Behind

All of the BRICs have now reached, or are rapidly approaching, the range of the G7 in terms of the total size of their economies. However, living standards in the BRICs continue to lag far behind the developed world. While all of the BRICs will likely soon be among the ten largest economies, none have yet to break into even the top 50 richest economies in terms of PPP-based GDP per capita (which make more sense than USD-denominated levels when comparing living standards across countries).

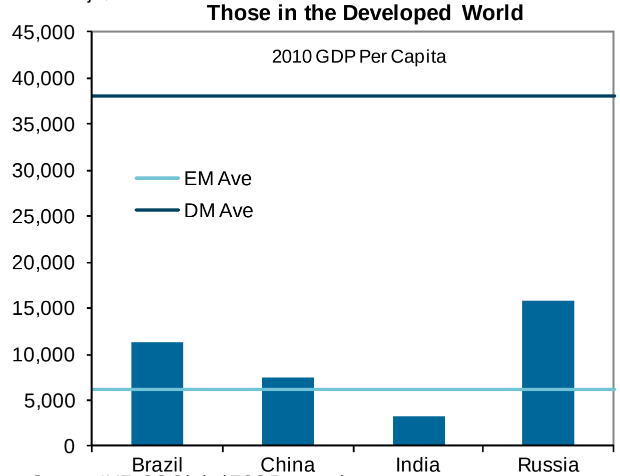
In 2010, the developed market (DM) average per capita income stood at $38,100 in PPP-adjusted dollars ($39,500 in USD). Russia recorded GDP per capita of $15,900 ($10,400), just 40% (26%) of the DM average. Brazil's per capita income was $11,200 ($10,700) in 2010, while China and India lagged even further behind, with GDP per capita of just $7,500 ($4,400) and $3,300 ($1,400) respectively. Encouragingly, we expect the BRICs, particularly China and India, to continue to experience among the fastest GDP per capita growth rates in the world, but their low starting bases means that convergence to DM levels is still a long way off.

GDP per Capita in the BRICs is Growing Quickly from Low Levels....



Source: IMF, GS Global ECS Research

...But Living Standards Remain Far Below Those in the Developed World



Source: IMF, GS Global ECS Research

1. The tendency of real appreciation to coincide with productivity growth over the long term (the Balassa-Samuelson effect), is well-documented and widely accepted.

Main Economic Forecasts

					2011				2012			
	2009	2010	2011	2012	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Real GDP Growth (yoy%)												
Brazil	-0.6	7.5	4.5	4.0	4.2	4.8	4.1	4.9	3.6	4.1	4.3	4.0
China	9.2	10.3	9.4	9.2	9.7	9.7	9.4	8.9	8.9	9.2	9.3	9.3
India	8.0	8.5	7.5	7.8	7.7	7.6	7.4	7.5	7.9	7.9	7.6	7.7
Russia	-7.9	4.0	5.3	5.6	3.7	4.4	6.0	6.6	6.3	5.9	5.3	5.2
BRICs	5.0	8.7	7.6	7.6	7.5	7.7	7.6	7.6	7.5	7.7	7.6	7.6
World	-1.8	4.3	3.6	4.0	3.5	3.3	3.4	3.6	3.8	4.0	4.0	3.9
Inflation (yoy%)												
Brazil	4.9	5.2	6.6	6.5	6.3	6.6	6.9	6.5	6.0	5.7	6.1	5.9
China	-0.7	3.3	4.7	3.0	5.0	5.4	5.0	3.6	3.0	2.8	2.9	3.2
India	3.8	9.6	8.1	5.1	8.8	8.9	8.2	6.3	5.2	5.0	5.0	5.4
Russia	11.7	6.8	8.9	6.5	9.5	9.6	8.8	7.7	6.7	6.6	6.4	6.2
BRICs	2.6	5.1	6.2	4.4	6.4	6.8	6.4	5.1	4.3	4.1	4.2	4.4
World	1.2	2.7	3.9	3.1	3.4	4.0	4.0	3.6	3.1	2.7	2.8	2.9
Exchange Rate (eop)												
Brazil	1.74	1.66	1.62	1.85	1.63	1.55	1.60	1.62	1.70	1.75	1.80	1.85
China	6.83	6.62	6.26	5.87	6.55	6.45	6.36	6.26	6.17	6.07	5.97	5.87
India	45.14	44.70	47.00	47.00	46.00	46.20	47.00	47.00	47.00	47.00	47.00	47.00
Russia	30.24	30.54	26.04	24.85	28.22	28.31	27.69	26.04	25.40	25.25	24.85	24.85
Policy Rate (eop)												
Brazil	8.75	10.75	13.25	13.25	11.75	12.25	12.75	13.25	13.25	13.25	13.25	13.25
China	5.31	5.81	6.56	6.56	6.06	6.56	6.56	6.56	6.56	6.56	6.56	6.56
India	5.00	6.75	8.00	7.50	7.25	7.50	8.00	8.00	8.00	7.75	7.50	7.50
Russia	6.25	5.00	6.00	7.25	5.25	5.50	5.50	6.00	6.25	6.50	6.75	7.00
Nominal GDP per Capita (USD)												
Brazil	8389	10697	12996	13193								
China	3739	4394	5226	6230								
India	1194	1440	1640	1812								
Russia	8777	10412	13268	14814								
BRICs	3238	3873	4582	5269								
EM	3517	4164	4904	5534								
DM	38274	39510	43009	44998								
World	12062	12764	14135	15068								

Source: GS Global ECS Research