

## India and China are the only real Brics in the wall

By John Lloyd and Alex Turkeltaub

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Few concepts have gained more currency among business people and politicians in recent years than the idea of the Brics – the giant, emerging economies of Brazil, Russia, India and China, whose weight and influence is supposedly changing economic and political realities. Grouping the four, however, obscures a simple fact: while the rise of China and India represents a real shift in the power balance, Russia and Brazil are marginal economies propped up by high commodity prices. This difference has profound implications.

The fundamental difference between China and India on one hand and Russia and Brazil on the other is that the former are competing with the west for “intellectual capital” by seeking to build top-notch universities, investing in high, value-added and technologically intensive industries, and utilising successful diasporas to generate entrepreneurial activity in the mother country. Chinese officials, for example, are committed to developing 100 world-class universities, with a focus on science and engineering; India boasts one of the most dynamic information technology sectors outside the US. Both countries face challenges but they are taking the steps necessary to generate sustainable economic growth.

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Russia and Brazil are benefiting from high commodity prices but are not attempting to invest their windfall in long-term economic development. In Russia, the focus has been on concentrating natural resources in state hands, thereby reducing productivity and discouraging foreign investment; in Brazil, the government has been reluctant to make the structural changes necessary to generate strong economic activity across multiple sectors. The infrastructures of both countries remain third world. Neither has proved successful in the “brain wars” – attracting leading professionals.

What do these differences imply? Russia could experience a severe economic correction resulting in geopolitical repercussions once the commodity cycle ends in the short term, and a structural crisis once the age of oil ends in the longer term. Just as the Soviet Union in the 1970s experienced aggressive expansion driven by record oil revenues, followed by a rapid economic collapse in the 1980s when oil prices reached historic lows, the same pattern could take hold in the near future. This problem is aggravated by the fact that the productivity of Russian oil assets is declining rapidly. While we do not wish to overestimate the size of a possible economic correction, it is important to remember that few predicted the Soviet Union's demise. The political status quo in Russia could face a shock. In a Russia that undergoes economic stagnation, there may be dangers of a new wave of nationalism as well as a possible period of chaos. Such an outcome would create risks and opportunities. The risks are obvious – geopolitical instability as an insecure Russia yet again seeks a new place in the world. As for opportunities, the current trend of power concentration in the Kremlin could be reversed. Investors could find Russia more open to outside investment in the natural resources sector, as Russia would seek to improve the productivity of underperforming assets while lacking the financial resources to make such investments itself.

The assumption of continuity in Russia, premised on the notion that Vladimir Putin's administration will clone itself by installing its selected candidate as president after 2008, underestimates the possibility of substantial political changes once the commodity price cycle ends.

Brazil may also face substantial challenges at that time. It could repeat the boom-and-bust cycle that has marked South American economies unless it utilises the current period of high commodity prices to restructure its economy, improve governance and invest in infrastructure. Given the economy's dependence on commodity exports – these account for about 40 per cent of all exports – a substantial correction in metal prices could also destroy the political consensus in favour of pro-market policies. Brazil, a counterweight to

the more radical elements in South America, could become preoccupied with domestic problems while foreign investors got caught in a downward spiral. To consider Brazil as one of the pillars of an emerging global order – which membership of the Bric fraternity implies – underestimates these risks.

Finally, the focus of western policymakers on energy security must not displace a commitment to leadership in “intellectual resources”. Energy security is a critical issue, but maintaining leading capital markets, the rule of law, funding of basic research and the creation of regulatory environments conducive to entrepreneurial activity must be the priority in the US and western Europe. These issues will determine how well the west does with respect to the emerging markets that pose a true challenge to western leadership – China and India. There is no question that the so-called Bric countries are large, emerging market economies that are shaping the economic and geopolitical order. Nevertheless, as political and business leaders devise strategies they would be well advised to focus on China and India.

*John Lloyd is an FT commentator. Alex Turkeltaub is a managing director at the Frontier Strategy Group, a consultancy focused on emerging markets*

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