



Brazil Russia India China

Rebounding From the Global Financial Crisis

Kelly M. Gushue
June 2009
www.kmgadvisors.com

TABLE OF CONTENTS

A. BRIC SLOWDOWN IN 2009: BLIP IN GROWTH TRAJECTORY	3
B. DESPITE 2008 MARKET MELTDOWN: BRICS RALLY IN 2009	5
C. SIZE MATTERS: BRICS ARE RESHAPING GLOBAL TRADE	6
D. CHINA: STIMULUS SUCCESS: FULL SPEED AHEAD FOR 2H09	10
GDP	11
Stimulus Policy	12
Banking System	13
Stock Market	13
Opportunities & Risks	14
E. INDIA: STALWART DOMESTIC ECONOMY SUSTAINS GROWTH	15
GDP	16
Stimulus Policy	16
Banking System	17
Stock Market	17
Opportunities & Risks	18
F. BRAZIL: FOUNDATION IN PLACE FOR GROWTH IN 2010	20
GDP	21
Stimulus Policy	21
Banking System	22
Stock Market	22
Opportunities & Risks	23
G. RUSSIA: CONTRACTION IN 2009: A REBUILDING YEAR	24
GDP	25
Stimulus Policy	25
Banking System	26
Stock Market	26
Opportunities & Risks	27

A. BRIC SLOWDOWN IN 2009: BLIP IN GROWTH TRAJECTORY

The view in 2008 was that a recession in the U.S., the world's largest consumer country, would cause a dramatic slowdown in growth in countries around the world. While the BRIC countries have experienced a slowdown in 2009, it appears as a blip in the rapid growth trajectory of the four BRICs. China and India are expected to continue to grow in 2009, with China expected to grow 6-8% and India up 5.5%. Brazil and Russia may experience a contraction in growth in 2009, with a return to growth in 2010.

Individual GDP Growth: 2008-2012

	2008	2009	2010	2011	2012
China	9.0	7.6	8.3	9.5	9.0
India	7.1	5.5	6.6	7.3	8.4
Brazil	5.1	-1.5	4.0	4.0	4.0
Russia	5.6	-6.5	0.8	4.0	4.0

Source: Citi Investment Research

Each country has used aggressive policy and stimulus measures to boost domestic consumption and support growth. While India and Brazil are relatively insulated from global trade with low levels of exports as a percentage of GDP, China and Russia have used various stimuli to offset this global exposure. A key component of funding has been the large foreign reserves the BRICs have amassed over the last five years. The BRICs also have ongoing investment needs that support consistent high levels of government spending for infrastructure, urban development in non-primary cities, transportation and expansion of retail sectors. China in particular has tried to increase domestic consumption from a level of just 40% (compared to 60-70% in other BRICs), in order to offset the decline in exports.

Comparison Economic Indicators: 2009

	China	India	Brazil	Russia
Real GDP	7.6	5.5	-1.5	-6.5
Private Consumption	9.3	5.6	-0.9	-10.0
Fixed Investment	13.8	4.0	-10.8	-12.0
Exports	-17	6.3	-2.1	-10.0
Imports	-16.8	5.6	-5.6	-19.4
CPI	-0.4	2.0	4.7	12.4
Unemployment Rate	4.6	7.5	9.3	12.0
Foreign Reserves (May)	\$2 trillion	\$252 billion	\$190 billion	\$384 billion

Source: Citi Investment Research

2009 Country Economic Indicators

China	Positive GDP of 7.6 expected. While exports and imports numbers appear weak, growth in private consumption and fixed investment remains strong. Deflation will help control prices.
India	Positive GDP of 5.5 expected. Maintains strong growth indicators across key segments. Domestic consumption of 50% contributes to growth.
Brazil	GDP of -1.5 expected. Mixed economic figures point to uneven recovery, particularly the decline in fixed investment. Private consumption (70% of GDP) will help return to growth.
Russia	GDP of -6.5 expected. With double digit declines across indicators, Russia has been hit hard by global crisis. Employment is expected to rise from 6.4% to 12%. The significant decline in imports and fixed investment will take time to recover.

Source: Citi Investment Research

Stimulus Policies Buoy Growth

With the surpluses the BRIC economies have accumulated over the last five years of growth, they have ample funding to implement aggressive fiscal policies to support growth. With Russia as the exception, they have maintained disciplined financial systems and healthy domestic financial sectors. The total amount of fiscal and monetary stimulus packages vary since figures include different metrics. Currently there are broader fiscal and economic incentives that are being used to support growth than the amount announced.

China has been the most aggressive in its \$586 billion stimulus for infrastructure, banking and consumer spending. India announced \$4 billion in stimulus and has announced various tax cuts. Brazil has focused more on monetary policy and announced a \$3.6 billion fiscal stimulus. Russia announced a \$20 billion stimulus in 2008 followed by \$74 billion in 2009.

Amount of Stimulus Plans by Country

China	\$586 billion or 15% of GDP
India	\$4 billion or 0.6% of GDP
Brazil	\$3.6 billion or 0.3% of GDP
Russia	\$94 billion, or 6.7% of GDP

Source: Citi Investment Research, RGE Monitor, Bloomberg, Reuters, FT.com, Brookings Institute

BRICs to Maintain Sustainable Growth

There is debate that the boom in emerging markets is not due to structural changes in the BRIC economies, but rather due to economies inflating their own asset bubbles. This may have been the case with the Asian financial crisis, as the decline in the Thai baht caused a major outflow of international capital that was supporting inflated asset levels in Asia at the time. The continued growth of the BRIC countries, however, demonstrate the structural shift occurring in these economies. Russia may be an exception with the problems with the financial system. The structural economic changes underway in China, India and Brazil, including increases in trade, industrial production, domestic consumption and urbanization, are expected to continue over at least the next decade.

B. Despite 2008 Market Meltdown, BRIC Markets Rally in 2009

The global financial crisis of 2008 led to a huge capital outflow from the emerging markets and a crash of 40-60% in the stock markets of the BRIC countries. Despite the significant stock market declines in 2008, investors have begun to feel more comfortable with the economic recovery underway in the BRICs and taking on more risk. Economic indicators in April/May showed positive growth. In April, there was growing optimism that the US plan to purge toxic assets from balance sheets was working. Large US banks were announcing profits for the first time since the financial crisis began. Moreover, the price of oil has continued to rise from \$40 in March to \$65 in May with a belief of increased demand. Gold, platinum, lead, zinc and aluminum have also advanced on optimism of a revival in demand for commodities in the US and China.

BRIC Stock Market Performance: 2005-2009

	2005	2006	2007	2008	2009 (May)
China (SSE Composite)	-10%	350%	100%	-65%	42%
India (Sensex)	40%	110%	48%	-52%	47%
Brazil (Bovespa)	30%	90%	45%	-40%	41%
Russia (RTS)	80%	90%	28%	-72%	72%

Source: FT.com

BRIC Stock Market Monthly Performance: 2009

	January	February	March	April	May
China (SSE Composite)	9.33%	4.63%	13.99%	4.40%	6.27%
India (Sensex)	-5.40%	-5.70%	9.20%	17.00%	28.25%
Brazil (Bovespa)	4.66%	-2.84%	7.98%	15.55%	12.22%
Russia (RTS)	-14.65%	1.78%	26.64%	20.77%	30.58%

Source: FT.com

C. SIZE MATTERS: BRICS ARE RESHAPING GLOBAL TRADE

BRICs are reshaping and influencing the flow of global trade with their sheer size - 40% of the world's population, a growing consumer middle class of 900 million people, 158 cities with over 1 million people, foreign direct investment of \$225 billion and over \$2.8 trillion in foreign reserves. Particularly interesting is the increasing amount of intra-trade between the four BRICs. China has become the second largest trade partner for India and Brazil's top trade partner. Since China is the world's second largest consumer of oil, Russia is also a key trade partner. The result is that the BRIC countries are gaining greater influence and supporting each other's economic development. Evidence of this influence includes the assembling of the G20 summit – rather than the G7 - to discuss a global response to the 2008 financial crisis.

A. BRICs population: 40% of world's population

Total population of the BRIC countries is 2.7 billion people, or 40% of the world population of 6.7 billion people. The BRICs need to find sustainable resources to feed this large population. Moreover, the increasing amount of disposable income is causing a shift, and shortage, in world agricultural production.

- Increased demand for food products (agriculture, dairy, beef, poultry, etc.)
- Increased domestic and international demand for BRIC trade
- Record food prices in 2008, a trend that will return post-recovery

POPULATION (2007)

China	India	Brazil	Russia
1.3 billion	1.1 billion	185 million	141 million

B. BRICs cities with 1+ million people: 158 cities

Currently the BRICs have 158 cities with a population of over 1 million people, or almost 40% of the 408 world cities with 1+ million people (UN estimates, 2005). This number is rising and is compared to 35 cities in Europe and 9 cities in the US with over one million people. The industrialization of these cities is causing a shortage of commodities and natural resources, and thus record level prices.

- Increased demand for natural resources to build infrastructure
- Record prices for natural resources/commodities, a trend that will return post-recovery
- Shortage of commodities/natural resources, a trend that will return post-recovery

NUMBER OF CITIES WITH 1+ MILLION PEOPLE

China	India	Brazil	Russia
93	37	15	12

Source: UN, 2005

C. BRICs consumer middle class: 900 million people

The total size of the middle class for the BRICs is 891 million people, or 13% of the world population. Comparatively, the middle class in the US is 100 million people. With higher incomes, consumers are purchasing a greater number of products, higher-end products and more diverse products to support the expansion of the retail/consumer industry.

- Demand for retail/consumer goods
- Growth of other retail sectors (real estate, banking, etc.)

SIZE OF MIDDLE CLASS (MILLION)

	China	India	Brazil	Russia
Size	400	350	86	55
Annual Income	\$3,000	\$2,500	\$7,200	\$2,500-\$5,000

Source: Euromonitor, Economist, RIA Novosti

D. BRICs amount of inbound FDI: \$225 billion

Total amount of \$225 billion represents 16% of global FDI of \$1.4 trillion (UNCTAD 2008). This amount continues to grow robustly with a 20% increase from 2008 despite the global financial crisis showing the importance of increasing trade links with the BRICs.

- Continued growing demand for FDI
- Amount makes BRICs more powerful in global trade force (i.e. G20 Summit)

AMOUNT OF INBOUND FDI (\$BILLION) (2008)

	China	India	Brazil	Russia
2008	\$92.4	\$27.5	45.1	\$60
Growth Rate	12%	10%	30%	33%
2007	\$82.7	\$25	\$34.6	\$45
Growth Rate	19%	29%	98%	84%

Source: Ministry of Commerce (China), Reserve Bank of India, RIA Novosti (Russia), UNCTAD (Brazil)

E. BRICs amount of Sovereign Wealth Funds: \$838 billion

Nearly 33% of the estimated \$2.5 trillion in sovereign wealth funds around the world comes from the BRICs. (Sovereign Wealth Fund Institute, 2007 figure plus decline of 20%) This is the amount set aside for investments outside the domestic country and as a cushion for adverse financial conditions.

- Continued shift in global liquidity and price appreciation due to huge inflow of capital invested in foreign currencies, gold, and other commodities
- Opportunity for BRICs to play key role in providing funding to ailing sectors during slowdown, i.e. oil companies in Russia

AMOUNT OF SOVEREIGN WEALTH FUNDS

China	India	Brazil	Russia
\$627 billion	\$5 billion (To Be Created)	\$5.9 billion (Created Jan. 09)	\$200 billion

Source: Sovereign Wealth Fund Institute, 2009

F. Amount of BRICs intra-trade: \$166 billion

- Rapid trade growth among BRIC countries of 20-40% per year demonstrates power shift of BRIC block trade
- Intra-trade occurring at detriment of reliance on trade with US and EU
- Complimentary comparative advantages (Russia – oil; Brazil – food; China – manufacturing; India – technology services)
- Stronger trade links between China and Russia due to China's status as world's second largest consumer of oil, Russia's global leadership in commodities, and regional proximity
- China became Brazil's largest trading partner in 2009 (increase of 56% in trade)
- China is India's second largest trading partner (increase of 33% in trade)
- IBSA (India/Brazil/South Africa) Trilateral Commission- formed in 2006 with target trade of \$10 billion by 2007 in science, tech, education, agriculture, energy, culture, health, and social issues

Some BRIC intra-trade tensions:

- India/China tensions: India imposed a six-month ban on toy imports from China (Jan. 2009). Speculation is that government is trying to shield Indian manufactures from cheaper Chinese products including toys, steel, chemicals and textiles.
- US civilian nuclear co-operation deal with India alarms Russia and China

AMOUNT OF BRICS INTRA-TRADE 2008 (\$BILLION)

	China	India	Brazil	Russia
China		\$52	\$40	\$57
India	\$52		\$4	\$7
Brazil	\$40	\$4		\$6
Russia	\$57	\$7	\$6	

Source: RIA Novosti, India Times, CIA Factbook

GROWTH OF BRICS INTRA-TRADE

	2007 Amount	2007 Growth	2008 Growth	2010 Goal
China-Russia	48.2	44%	18%	\$80 billion
China-Brazil	23.4	15%	56%	
China-India	38.7	34%	33%	
India-Brazil	3.1	30%	20%	\$10 billion
India-Russia	6.4	30%	10%	\$10 billion
Russia-Brazil	5.2	N/A	20%	\$10 billion

Source: RIA Novosti, India Times, CIA Factbook

Comparison of BRIC Key Statistics

	China	India	Brazil	Russia
Economy Size (World Bank)	4th largest economy	12th largest economy	10th largest economy	11th largest economy
Population	1.3 billion (1st largest)	1.1 billion (2nd largest)	185 million (5th largest)	141 million (9th largest)
Geography Size	3rd largest	7th largest	5th largest	1st largest
Cities with 1 million+ people	93	37	15	12
GDP Growth (2009)	7.6%	5.5%	-1.5%	-6.5%
WTO Entry	2002	1995	1995	N/A
Investment Grade Debt (2009)	A+	BBB- (Investment grade)	BBB- (Investment grade)	BBB
Foreign Reserves (2009)	\$2 trillion	\$252 billion	\$190 billion	\$384 billion
Sovereign Wealth Fund (2008)	\$627 billion	\$5 billion (To Be Created)	\$5.9 billion (Created 1/09)	\$200 billion
Size of Middle Class	400 million	350 million	86 million	55 million
FDI (2008)	\$92.4 billion	\$7.5 billion	\$45.1 billion	\$60 billion
Size of Stimulus	\$586 billion	\$4 billion	\$3.6 billion	\$94 billion
Time of Last Financial Crisis	1989-1991	1992-1993	2002	1998-1999
Type of Government	Communist	Democratic	Democratic	Authoritarian
Presidential Elections	TBD	May 2009	2010	2012
Stock Market Growth	<ul style="list-style-type: none"> • Shanghai Stock Exchange • Fifth largest in world • \$2.25 trillion market cap • 870 companies • Created in 1990 • From trough of 1209 in 1/06 reached peak of 5903 in 10/07 	<ul style="list-style-type: none"> • Sensex (Bombay Stock Exchange) • \$1.03 trillion market cap • 6,000 companies • Revised in 2005 • Peak in 1/08 	<ul style="list-style-type: none"> • Bovespa • \$1.5 trillion market cap • Revised in 2000 • 450 companies • From level of 5,000 in 2003 to peak of 73,516 in 5/08 	<ul style="list-style-type: none"> • Russian Trading System (RTS) • \$571 billion market cap • Est. 1995 • 1335 companies • From low of 37 in 10/98, reached peak 5/08
Internet Users 2008 (penetration rate)	298 million (23%)	81 million (7.3%)	62 million (33%)	47 million (33%)

Source: Economist, IMF, World Bank

D. CHINA: STIMULUS SUCCESS: FULL SPEED AHEAD FOR 2H09

OVERVIEW

China's V-shaped recovery appears to be taking hold. Economic metrics and local business conditions show Q408 was the worst quarter; Q109 was weak; and Q209 is back to business and growth. The 2H09 appears to be strong based on effective stimulus, pent-up business demand and continued expansion opportunities across China. While there may be some setbacks, it appears that investment growth is more than offsetting export declines. The \$586 billion stimulus appears to be working as the government continues to pull out all stops – including adding a new national holiday on May 28 – to achieve 8% growth. With China's huge foreign reserves of USD, the Chinese government has called for a new international currency and has provided first-time renminbi loans for trade with six countries. While a convertible currency is years away, China has the world's best capitalized banking system and an aggressive central bank to sustain growth.

Challenges and risks remain with social instability being a common concern in cities with significant economic dislocation. The number of unemployed migrant workers is as high as 40 million people. Reforms are also needed to alleviate issues restraining domestic consumption including undeveloped rural infrastructure and limited social services.

China's GDP Growth: 2008-2012

2008	2009	2010	2011	2012
9.0	7.6	8.3	9.5	9.0

Source: Citigroup Investment Research

China Economic Indicators 2008-2010

	2008	2009	2010
Real GDP	9.0	7.6	8.3
Private Consumption	12.7	9.3	9.8
Fixed Investment	15	13.8	14.2
Exports	17.3	-17.0	9.6
Imports	18.5	-16.8	15.5
CPI	5.9	-0.4	2.0
Unemployment Rate	4.2	4.6	4.6

Source: Citi Investment Research

Stock Market Performance (%)

	2007	2008	2009 (thru May)
SSE Composite	100%	-65%	42%

Source: FT.com

E. INDIA: STALWART DOMESTIC ECONOMY SUSTAINS GROWTH

OVERVIEW

India's insulated domestic economy has continued to thrive despite the global financial crisis. With domestic consumption at a level of 70%, versus 37% in China, the domestic consumer is supporting India's growth. A fiscal stimulus of \$4 billion, tax cuts and loose monetary policy has also allowed the government to supplement growth. Political instability had been an issue until the May election. An overwhelming victory by the United Progressive Alliance (UPA), and 17% market rally, gives the UPA momentum to push through policy measures. The new budget is expected in July. Much needed investment in infrastructure continues with the five-year infrastructure plan of nearly \$500 billion. With India's well-capitalized banks, companies can continue to expand despite the global slowdown.

India's risks continue to be spreading growth beyond the major cities across India. Despite improvements, underfunding in education and health care remains a problem.

India's GDP growth: 2008-2012

2008	2009	2010	2011	2012
7.1	5.5	6.6	7.3	8.4

Source: Citi Investment Research

India Economic Indicators 2008-2010

	2008	2009	2010
Real GDP	7.1	5.5	6.6
Private Consumption	6.8	5.6	6.5
Fixed Investment	6.9	4.0	5.4
Exports	20.8	6.3	10.2
Imports	27.9	5.6	5.6
CPI	8.2	2.0	4.0
Unemployment Rate	7.3	7.5	7.5

Source: Citi Investment Research

Stock Market Performance (%)

	2007	2008	2009 (thru May)
India Sensex	48%	-52%	47%

Source: Yahoo Finance

F. BRAZIL: FOUNDATION IN PLACE FOR GROWTH IN 2010

OVERVIEW

Brazil continues to have mixed economic results with weak signs of growth for 2009. While 2009 may show a GDP contraction, there continues to be momentum for broader, sustainable growth in 2010. While exports make up only 19% of GDP, Brazil has been less exposed to the dramatic slowdown in global trade. Domestic consumption, which makes up 60% of GDP, has slowed. Brazil is the largest food and agricultural producer, and is growing in significance with its oil field discoveries and ethanol technology. The Central Bank has demonstrated a steady hand managing the domestic economy with prior experience navigating Brazil's 2002 financial crisis that included 40% monthly inflation. Further indicators for growth and international marketing include Brazil as host of the 2014 World Cup and leading status to host the 2016 Summer Olympics. In Jan. 2009, the government created a \$5.9 billion sovereign wealth fund for protection against future adverse economic conditions. While the stock market has rallied 41% year to date, perhaps ahead of itself, there are strong indicators of Brazil's continued growth after 2009.

Brazil's GDP Growth: 2008-2012

2008	2009	2010	2011	2012
5.1	-1.5	4.0	4.0	4.0

Source: Citi Investment Research

Brazil Economic Indicators 2008-2010

	2008	2009	2010
Real GDP	5.1	-1.5	4.0
Private Consumption	5.4	-0.9	0.4
Fixed Investment	14.7	-10.8	-6.5
Exports	-0.6	-2.1	0.3
Imports	18.5	-5.6	-3.0
CPI	5.7	4.7	4.1
Unemployment Rate	7.9	9.3	8.5

Source: Citi Investment Research

Bovespa Stock Market Performance (%)

	2007	2008	2009 (thru May)
Brazil Bovespa	45%	-40%	41%

G. RUSSIA: CONTRACTION IN 2009: A REBUILDING YEAR

OVERVIEW

Russia continues to be the BRIC to monitor carefully with an economic contraction of 6.5% expected in 2009. Lack of transparency with banking, limited industry diversification and decline in exports appear to be obstacles to growth and have turned 2009 into a rebuilding year. Russia's role as the world's second largest oil producer, however, will continue to support its development and give it time to address other industry issues. With ample reserves from the oil boom from 2006 to mid-2008, the Central Bank has used aggressive fiscal and monetary policy to support the Russian economy, including \$94 billion in stimulus and more than \$200 billion to support the fragile banking industry. The banking system currently faces the challenge of repaying \$130 billion in foreign loans in 2009. With the recovery in oil prices from a low of \$35 to over \$60 in 2009, Russia has additional cushion to support a recovery. Unemployment is expected to rise from 6.4% to 12% and may create social unrest. In contrast to the Beijing Olympics, the 2014 Winter Olympics in the resort town of Sochi have garnered controversy. The ongoing debate of Russia's WTO Accession has been tabled. While Russia continues to assert itself in foreign trade, it is facing the challenge of managing a domestic economy and political tensions with neighbors.

Russia's GDP Growth: 2008-2012

2008	2009	2010	2011	2012
5.6	-6.5	0.8	4.0	4.0

Source: Citi Investment Research

Russia Economic Indicators 2008-2010

	2008	2009	2010
Real GDP	5.6	-6.5	0.8
Private Consumption	11.2	-10.0	2.0
Fixed Investment	11.3	-12.0	4.0
Exports	0.1	-10.0	6.0
Imports	14.7	-19.4	9.0
CPI	14.1	12.4	9.8
Unemployment Rate	6.4	12.0	10.0

Source: Citi Investment Research

Russia RTS Performance: 2007-2009

	2007	2008	2009 (thru May)
Russia RTS	28%	-72%	72%

Source: FT.com