HOW SOLID ARE BRICS?

Over the past decade, the fast-growing economies of Brazil, Russia, India and China have attracted the attention of investors worldwide, but with the dramatic slowdown in growth, is the BRIC success story coming to an end? Andrea Ashfield reports.

Since the term BRIC was coined by Goldman Sachs in 2001, the increasingly prosperous economies of Brazil, Russia, India and China have offered an abundance of opportunities for investors. In a much-quoted 2003 report, Goldman predicted that by 2050, the BRIC countries will be among the biggest economies in the world, with only the US and Japan remaining in the top six. In recent months, however, the onset of recession has resulted in a sharp slowdown in these nations, and in January this year, data from the Organisation for Economic Co-operation and Development revealed that the index for China decreased by 3.1 points in November 2008 – 12.9 points lower than a year ago. India and Brazil fell by 1.2 and 1.1 points respectively, while Russia saw the largest drop of 4.3 points, down 13.8 points from the same month the previous year. In an increasingly tough climate, it seems the reliability of BRICs is waning, but in spite of a growing lack of confidence, some experts believe the emerging markets still have a lot to offer.

Collectively, the four BRIC countries make up around 40% of the world's population, while individually, each of these loosely-affiliated nations has its own areas of expertise. Brazil is the world's biggest exporter of sugar, coffee and beef, and is also a major supplier of iron ore. Russia has large repositories of oil and gas, while China and India are leading providers of services and manufactured goods. However, throughout the economic turmoil

of 2008, these countries took a severe hit, with China's markets losing 62% of their value and Russia dropping by a massive 70%. In the long term, however, Ernst and Young's Item Club recently predicted that the BRICs will collectively be responsible for 40% of global economic growth between 2009 and 2020.

'These are some of the largest economies in the world,' explains Graeme Currie, a director at Alan Steel Asset Management. 'By 2050, arguably only the US will be in the top six alongside these nations. If you take all the people that live in these countries, there is huge domestic consumption and demand for the things we take for granted.'

Looking forward

Opinions, it seems, are mixed, so what opportunities do BRICs hold for investors in 2009? Bryan Collings, co-manager of the emerging markets specialist, Hexam Capital, is passionate about the future potential of these countries and is confident that good returns are still achievable in the long term.

'BRICs have a superior equity market performance because they are seriously endowed with resources,' he explains.

'The demographic is good – they have young, growing populations with lower income groups which in the context of each country, offer huge opportunities. Geographically, these countries are massive. Infrastructure has to be put in place because there are many people in rural areas. In the long term, BRIC has an interesting and compelling equity market profile.' Collings also believes these attributes give BRICs an advantage over some of the more developed markets.

Some experts believe that in light of the current downturn, it is no longer appropriate to group these four large nations together.

markets may appear to be more risky but they are actually less so over a five-year period. My feeling is that if you are looking at three to five years, this is more important than short term price variability.'

2008 was undoubtedly a bad year for BRIC investors, and it seems inevitable that 2009 will continue to present difficulties.

'The US is the biggest economy in the world, and many of these countries depend upon it, so there will be a knock-on effect,' says Currie. 'However, they are also likely to grow more quickly when the turnaround comes.'

Experts at UBS, which recommends that its clients invest a portion of their real estate portfolio in emerging markets where appropriate, also believes these countries have more to offer, albeit at more modest levels. 'We are still predicting positive GDP for these nations – they are able to withstand the slowdown better than developed economies,' considers O'Reilly. 'However, these countries are not completely immune and everyone will be affected by the current crisis. We view it on a relative basis – if these developing nations continue to grow at current levels there will still be very good opportunities in these markets in the years ahead.'

'There is potential for growth over the next three years – it could be a significant surge,' adds Collings. 'We will come out of this recession and government will restructure. From a BRIC viewpoint, this is a blip.' Indeed, a December 2008 forecast by Ernst & Young's Item Club predicted that by 2020, the BRIC nations could account for 65% of global basic metals output, 38% of chemicals production, 30% of motor vehicles and 28% of electronics. Over the same time period, Bryan Collings expects returns of between 10 and 20%, and if these statistics prove to be accurate, there could be more twists in the BRIC story yet to come. ■

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'The growth prospects are very different from country to country,' explains Brian O'Reilly, head of wealth management at UBS. 'From an economic standpoint, the long term outlook for Brazil and China remains very positive. India is at least ten years behind in terms of development, whereas Russia is facing problems given its overreliance on the energy sector.' China's high rate of savings mean it could be better equipped to bounce back from the economic downturn, with lower prices presenting potentially good opportunities for buyers. Interestingly, a recent report by UBS, entitled 'Proceed with Caution', states that while the emerging markets will slow markedly throughout 2009, the BRIC countries appear likely to avoid an outright recession, with a muted recovery expected during the second half of the year.

The preferred way to buy into BRICs is to drip-feed your capital into a fund, which can be focused on a particular sector or country. However, without expert knowledge, it is often better to opt for a general fund, in order to achieve a more even spread. 'You can buy funds that have a significant bias towards BRIC,' says Collings. 'For example, the Hexam Emerging Markets Fund is around 85% BRIC-orientated, with some Taiwan tech as well. This gives you a lot more flexibility. An actively-managed fund will have higher exposure – Hexam has around 35 stocks in it, which is very concentrated in order to pick out the best of BRIC.' It is also possible to opt for an exchange traded fund (ETF), which has around 300 stocks and provides much broader exposure to the markets.

Assessing risk

BRICs may be looking unstable at the moment, but Collings feels it is possible to avoid some of this risk by opting for a longer term investment. 'As a crude measure you can look at price volatility,' he explains. 'Emerging

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