

## **Bric's Experience in the Financing of the Economic Growth**

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**Abstract:** The study deals with the experience of BRICS countries in the financing of the economic growth. The rapid development of these countries in 2000-2010 is the latest example of the catch-up in the global economy. The mechanism of income generation is considered which is the basis for self-maintaining growth. The primary and secondary financial sources of such growth are outlined, the dynamics of savings and investments in BRICS countries is analyzed. It is emphasized that the action of this mechanism developed investment multiplier in the respective economies.

**Key words:** Financing of the economic growth, BRICS, savings, investments, experience, mechanism

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### **INTRODUCTION**

The relevance of theme is predetermined by the fact that BRICS countries showed the latest example of catch-up development in the world economy at the moment. Their experience can help in understanding the peculiarities of formation the conditions for rapid economic growth.

### **MATERIALS AND METHODS**

The main methods of research are formal and dialectical logic, deduction and induction, analysis and synthesis. The key materials are the macroeconomic data of BRICS for 2000-2010's.

### **RESULTS AND DISCUSSION**

The experience of BRICS countries development in 2000-2010's suggests the need to consider the potential for economic growth in close connection with financial potential of the economy. The ability of these counties to provide self-maintaining system of GDP growth is directly related to the conversion of primary and secondary financial sources in the national savings and investments which serve as a basis for creation of new areas for business activity.

In 2000's BRICS countries were considered as potential leaders of the future world economy. Economic growth in these countries were higher than in countries with advanced markets. That allowed the possibility of

“overtaking development” a gap in the scale of GDP had been declined, so, by the end of the first half of the 21 century, China and India could overtake the United States in the fight for the title of the largest economy in the world while Brazil, Russia and South Africa might got ahead the leading countries of Western Europe and Japan.

The development of the world economy after the global financial and economic crisis 2008 determined the different effects of BRICS. At the current moment, not all members of groups fully retain the ability to achieve such outstanding results that have been identified in the forecasts of the IMF and Goldman Sachs Bank (Table 1). Despite this, the decade of rapid growth causes to consider the development of these countries in terms of the economic growth financing as a valuable macroeconomic experience.

Based on the figures from Table 1 the following conclusion should be made. According to the IMF forecast, only China matches the required paces of growth. Basing on the prediction of Goldman Sachs, China, India and Brazil are in fit. In this regard, the importance of the analysis of the specific features in supporting economic growth is important. This supporting is based on the generation of income in the national financial system.

The mechanism of income generation in the form of money creates the financial flows in the national and international financial systems including the redistribution of temporarily free money resources by using of credit relationship. The essence of this process is not only in

Table 1: Level of GDP in BRICS countries according to the forecasts of Goldman Sachs (2007), IMF (2010) and actual (billion dollars)

Countries	2015 (Goldman Sach)	2015 (IMF)	2015 (fact)
Brazil	1.720	2.789	1.774
Russia	1.900	2.498	1.326
India	1.900	2.412	2.073
China	8.133	9.982	10.866
South Africa	Not applicable	455	312

For South Africa there is no data in Goldman Sachs forecast (Wilson and Stupnitskaya, 2007); IMF, Goldman Sachs, World Bank

Table 2: Level of investments and savings to GDP in BRICS countries in 2000-2015

Countries	2000 (%)	2005 (%)	2010 (%)	2015(%)
<b>Brazil</b>				
Investments	18.9	17.2	21.8	19.2
Savings	15.1	18.7	18.3	15.9
<b>Russia</b>				
Investments	18.4	18.5	20.3	18.6
Savings	35.2	28.8	24.4	23.8
<b>India</b>				
Investments	24.2	34.6	36.5	32.4
Savings	23.7	33.5	33.7	31.3
<b>China</b>				
Investments	34.3	41.0	47.8	45.0
Savings	36.0	46.7	51.8	47.9
<b>South Africa</b>				
Investments	16.3	18.3	19.5	20.7
Savings	16.2	15.1	18.0	16.4

IMF

raise financial funds of government, companies, households but also in the formation of financial sources for generating new resources to ensure further development (Fernald, 2012).

The basis of such financing mechanism is in accumulation of the financial resources for investments in cost-effective new technologies and production, creation of new types of goods and services with high added value and with demand on the domestic and foreign markets, taking profit with refinancing of its part in the development and production of new technologies (Solow, 1956). Thus, the emergence of new financial sources is provided in the economy which in turn are used to generate high-tech products. As a result the creation of additional financial resources. This way, the self-financing of the national development is ensured as a permanent process. Table 2 analyzes the data on the volume of investments and savings to GDP in BRICS countries in 2010-2015s.

Basing on data presented in Table 2 it must be concluded that the most significant growth in the volume of investments and savings over the period occurred in China and India. A slight increase was observed in South Africa and Brazil. In Russia, these indicators have deteriorated. In this regard, it is necessary to distinguish between the initial and additional financial resources which are formed while generation of cash flows resulting from the creation and sale of products in the national

scale. The primary funding sources appear when distribution of value added between the factors of production takes in place. As a result of this distribution, the formation of income of individuals and companies occurs as well as taxes. The secondary sources of financing are borrowed funds which are attracted by the participants of business relations in the form of bank loans and bond issues. They are formed while placing temporarily free funds in the banking system and the stock market and their subsequent redistribution as a result of operations carried out in these sectors. Due to redistribution processes, temporarily free financial resources of some economic entities become financial sources for other subjects (Aghion and Durlauf, 2006).

In Brazil, the primary sources of funding for economic growth were revenues from food exports. In Russia oil revenues in China income from export trade in India earnings from foreign companies which use local labor force for outstaffing; in South Africa export of precious stones and metals. As secondary sources BRICS countries used resources of banking systems and the stock markets as well as borrowing. At the same time, it should be noted that the varying degrees of use redistributive mechanisms were inherent to them. In China and Russia, public sector usually plays an important role due to the fact that it provides significant portion of the labor places. For other countries such specificity is not observed. In whole the main sourcing areas are:

- Company's share capital
- Retained earnings
- Depreciation and amortization
- Revenues from exports
- Joint ventures with abroad partners
- Foreign loans
- Corporate bond issues
- Share issues of national companies
- Foreign direct and portfolio investments
- Public investments in infrastructure projects
- Sovereign wealth funds
- Resources of the national stock market
- Resources of the national banking sector
- Household savings
- Export credit insurance institutions
- Cross-border mergers and acquisitions
- Venture capital funds
- International strategic alliances
- Business angels

The complex of financial sources for economic system development forms its investment potential. Using of that actuates investment and fiscal multipliers

(Auerbach and Gorodnichenko, 2011). As a result, increased corporate profits, household incomes and budget revenues predetermine the rise of financial sources for economic development. Their growth amplifies the investment potential for the subsequent period.

To a large extent, that is reflected in the increase in capitalization of domestic companies. The Goldman Sachs forecast (Oppenheimer, 2009) outlines 50 companies with the greatest market potential in this regard. There were 10 Brazilian, Russian 8, 21 Chinese and 11 Indian corporations, share prices of which had grown in proportion to the GDP of the corresponding countries.

The process of formation of the financial resources of the national economic development is strongly influenced by both the outflow of capital abroad and foreign investment inflows (Reinhart and Reinhart, 2008). Various elements of the total outflow of domestic capital abroad have a different impact on the formation of the financial sources of development. In this regard, it is necessary to distinguish between, firstly, the "capital escape" including tax evasion; secondly, investments of the national companies in foreign assets including shares of companies and banks.

As regulatory measures aimed at reducing the scope of the "capital escape" there were a range of measures used in BRICS countries: the imposition of restrictions on transactions with offshore companies from jurisdictions that do not disclose information about final beneficiaries of business structures; direct ban on the establishment of resident legal entities in certain offshore areas; required security deposits for payments on transactions with offshore companies; the introduction of special taxes on transactions with companies from offshore jurisdictions.

The company's investments in foreign assets were another peculiarity of BRICS countries. In particular, Chinese companies took active expansion in Africa in order to gain control over local resources Russian corporations in the Near East and Middle Asian oil fields; Brazil in the neighboring countries of South America. In general, the state policy of foreign investment regulation is based on the range of interrelated parameters. They are the ratio of the volume of foreign direct and portfolio investments; The ratio of the volume of direct foreign and domestic investment. The ratio of the volume of accumulated foreign direct investment from the country and accumulated direct foreign investment in the country.

The risks in relation to financial sources of economic growth in BRICS countries appeared in the corporate sphere as well as in the areas of public and personal

finances. In the area of personal corporate finance these included high cost of raising equity and debt insufficient generation of economic value added low market weight of the value added indicator lack of working capital; high leverage, significant volatility of exchange shares quotations low effectiveness of R&D insufficient accumulation of intellectual capital inefficient mergers, acquisitions, international strategic alliances (Savva, 2009). In fact, BRICS countries are not among the most reliable in the tables of rating agencies and that implies higher risk premium when borrowing funds. BRICS markets have been hit hard during the 2008 crisis because of investor's fears of possible "overheating". Investment were not always effective Brazil, China and Russia held the Olympic Games, South Africa World Cup. All these events required large costs and showed negative profitability. Although, these activities allowed advanced infrastructure solutions they gave only slight effect to the country's GDP. Significant number of companies were facing financial difficulties due to local crises financial crisis in China in 2011-2012, currency downfall in Russia in 2014-2015, political instability in Brazil in 2015-2016.

In the area of public finance key risks were in insufficient budget spending on basic research, underfunding of infrastructure including transport, energy and communication systems inefficiency of public-private partnership, insufficient financing of measures implemented in the scientific, technical and industrial areas; inefficient depreciation policy; excessive tax burden. The severity of these issues was different in BRICS countries.

In the area of personal finance key risks were in low level of personal income; low rate of personal savings; legal and illegal export of personal savings abroad; lack of investment activity of households. The low level of GDP per capita is extra characteristic of BRICS countries which is a plus in terms of lower cost of labor but minus from the part of domestic demand potential.

Risks connected with subsequent use of new financial sources are: wrong choice of priority directions in the medium and long-term financing of the economic system; lack of sufficient financial support in the leading areas of scientific and technological development; incorrect assessment of the market demand for particular types of innovative products; lack of coordination between national scientific, industrial and financial policies, cyclical fluctuations in the world economic system; changes in international terms of trade as a result of worsening geopolitical situation, including the introduction of international sanctions. Realization of such risks was typical for BRICS countries in the 2010s. The threat of failure for these countries currently exists to

support the economic growth at the level of the 2000s. The methods of managing these risks are: forecasting the development of scientific and technical spheres; monitoring of the results of theoretical and application research; monitoring of license markets, patents, know how; diversification of the international scientific and technological cooperation.

From the perspective of the future the national fiscal and monetary policies occupies the important places as they have direct impact on both the conditions, formation and use of the financial sources for development of the national economy in areas of public, corporate and personal finances. Improving the efficiency of their design and implementation is essential for restructuring of the economic system and its innovative development. The main directions of the budget policy impact on the formation of financial sources include:

- Tax burden on economic agents (individuals and entities)
- Creation of favorable tax conditions for the development of innovation
- Amount and structure of budget expenditures on the national economy
- Formation of reserve funds
- Realization of specified state programs
- Investing of budgetary funds in the national development institutions
- Placement of the public pension system resources
- Public debt management

The main areas of monetary policy impact include:

- Ensuring the optimum level of money supply, supporting effective demand but neutral in relation to the price dynamics
- Setting interest rates which adequate in the light of profitability level in the real sector

- Exchange rate adjustments for balancing interests of exporters and importers
- Prevention of illegal export of capital

## CONCLUSION

The risks are identified in relation to financial sources of the economic growth which are affected in the public, corporate and personal finances. The main regulatory instruments are found that were used in BRICS countries.

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