Global Economy Watch
June 2014

Game time in Brazil: can the economy capitalise on the World Cup?

At a glance…

All eyes on Brazil…

Brazil hosts the FIFA World Cup this month. This mega sporting event will put the spotlight on a BRIC economy that has been going through a tough period since the financial crisis.

Sub-par economic growth of less than 3% and flagging export performance means the second largest emerging market economy is under pressure.

Many commentators have suggested that this event, and the Olympics in two years' time, might bring a boost to the economy. But are they right? And how can hosts of mega-events make the most of their time in the spotlight?

…could it win off the pitch?

We think that the direct economic impact of the World Cup is likely to be small, but Brazil could win elsewhere:

- A short term "feel-good" factor similar to that seen from London 2012 and other recent "mega event" hosts could reverse the decline in domestic confidence which has lasted for two years.
- The showcasing that key host cities will enjoy could pave the way for the next wave of Foreign Direct Investment (FDI) into Brazil. A 10% boost to FDI would lead to a $6.5bn injection to the economy.
- Finally, the experience that local companies accumulate through hosting these mega events could be leveraged in the future. For example, UK companies sold £130m of work to Brazil on the back of the skills learnt in 2012

Who will win on the pitch?

On a slightly lighter note, we have investigated what it takes to win the World Cup.

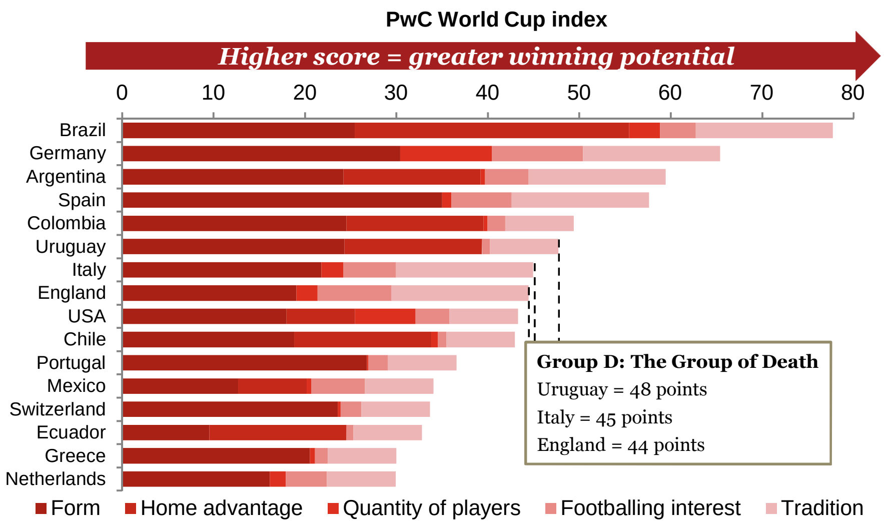
Our analysis shows that there are 5 important factors here: form, home advantage, the number of domestic players in the country, the quality of domestic leagues and footballing tradition.

Based on this, our model suggests that the hosts will win the cup this Summer, while England look set to exit in the quarter finals again.

The UK and Eurozone outpaced the US in the first quarter

The UK and Eurozone grew faster than the US in the first quarter, but the bloc exposed its reliance on its biggest economy. Without Germany, the Eurozone would have contracted. We think there is growing evidence of a "soft core" following disappointing figures from France and Italy.

Fig 1: Brazil is the economy with the most footballing potential in the world cup, while England really do sit in the "group of death"



Source: PwC analysis

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Economic update: Is the Eurozone becoming a one man band?

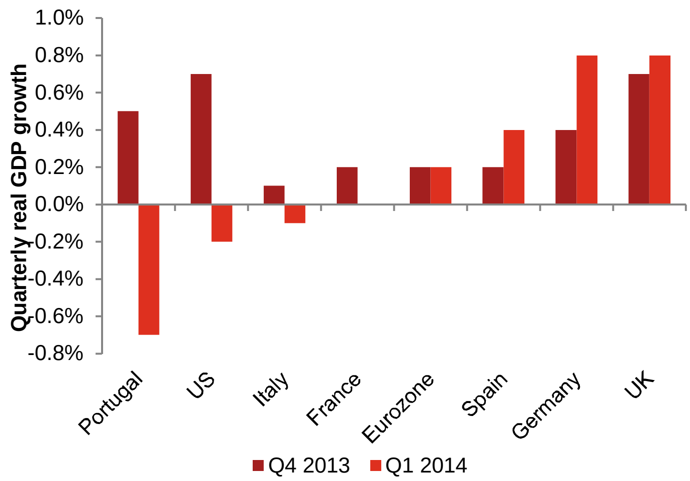
The release of Q1 data for most of the advanced economies revealed something we haven't observed since the first quarter of 2011 – the Eurozone grew faster than the US (0.2% on a quarterly basis compared with -0.2% for the US).

The devil lies in the details. Our analysis shows that it was Germany which drove growth as its output expanded four times faster than the overall Eurozone rate. In fact, had Germany not grown, Eurozone output would have contracted. Other large economies like France and Italy posted disappointing performance which, as discussed in our May Global Economy Watch, could indicate a "softer core" developing in the Eurozone.

Performance in the US was disappointing, but we think that this was partly driven by one-off extreme weather in the Mid-West. We are forecasting that economic activity will rebound in the second quarter and that the US remains on track to grow 2.7% in 2014.

UK growth remained robust at 0.8% quarter-on-quarter in Q1 2014, driven primarily by consumer spending but also with an increasing contribution from business investment. More recent business surveys and retail sales data suggest that this momentum has continued into the second quarter, so we have upgraded our UK GDP growth projection further to 3% for 2014 as a whole.

Fig 2: The US economy stalled in Q1, although the Eurozone did not fare much better



Source: Thomson Datastream

How to win the World Cup

As the 2014 World Cup in Brazil draws closer, there is increasing interest in what makes a successful World Cup team. We have used economic techniques to test the relationship between key variables and historic World Cup performances. We measure performance by awarding three points for a win and one for a draw for each World Cup game played.

Home advantage bodes well for Brazil...and for the rest of South America

In every World Cup apart from 2006, home countries have progressed further as the host than in their previous tournament. In fact, our modelling shows that hosts can expect to progress a further two rounds than if they were not hosting. There is also a clear 'home region' effect, which may reflect stronger crowd support and familiar climatic conditions. A European country has never won a World Cup held in the Americas, while a South American country has only won once in Europe.

Money can't buy World Cup success

In our previous analysis of the Olympics, we found a strong correlation between medal totals and the size of the economy. However, no such relationship was found for the World Cup, with GDP per capita and population failing to explain how well a country performs after controlling for other factors.

Instead, we found that the number of registered football players available to each country was a much more important factor. The popularity of football was also important, which we measured using the average attendances at domestic club matches.

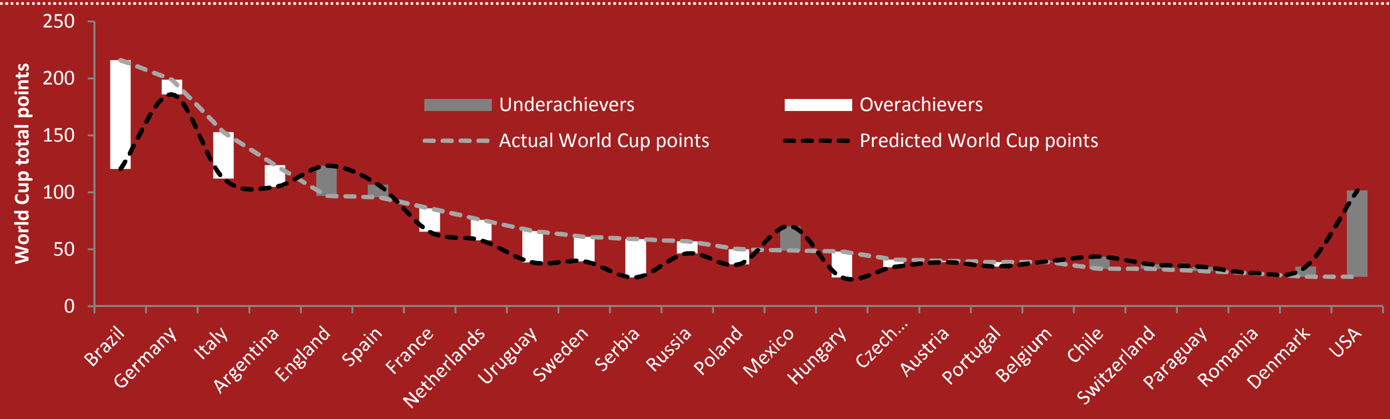
We also found that countries with a footballing 'tradition' tended to outperform others even given the quantity of players and the popularity of football, which we captured in our model through how many times each country has bid to host the World Cup.

The USA and England are perennial underachievers

Our modelling has identified a number of variables which explain historic World Cup performance. We have used this model to estimate the total World Cup points that each country would be expected to achieve given their endowment of each variable. We can then compare this estimate with their actual points, to determine whether countries have over or underachieved.

As shown in Figure 3, this reveals that Brazil have been the biggest overachiever in the World Cup, with an additional 95 points than expected. The USA are the biggest underachievers according to our model, while England are the second most underachieving side. England have collected 26 fewer points than expected, which is equivalent to an additional eight wins and two draws over World Cup history.

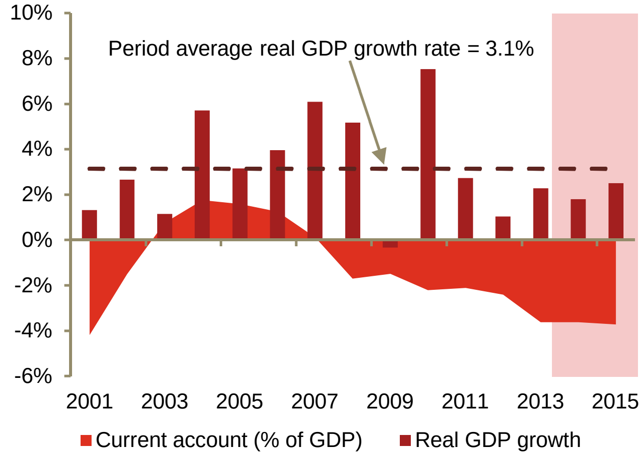
Fig 3: Our analysis shows that Brazil is the biggest overachiever at the World Cup, while the USA is the biggest underachiever



Source: PwC analysis

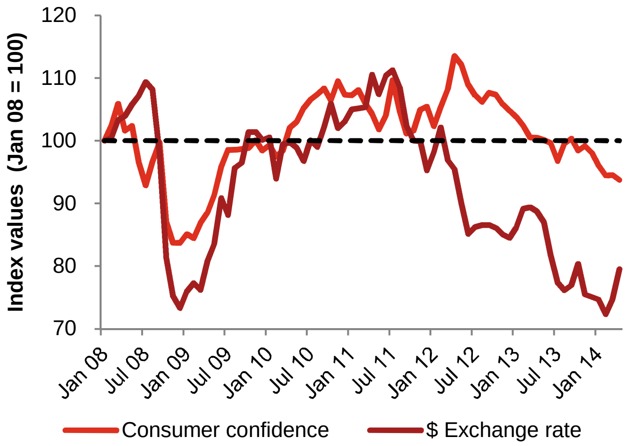
Brazil: how can it capitalise off the pitch?

Fig 4: Since the financial crisis, Brazil has seen a period of sluggish growth and a worsening current account



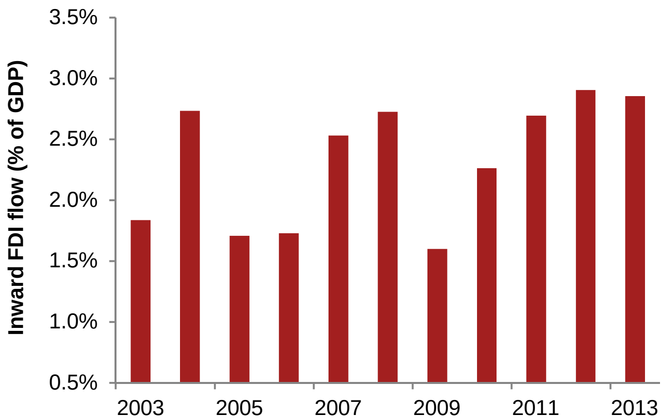
Source: PwC analysis, IMF

Fig 5: Confidence levels have been falling while the exchange rate has been weakening



Source: PwC analysis, Datastream

Fig 6: FDI into Brazil has been increasing in the run up to the World Cup



Source: OECD

This month, Brazil is hosting the FIFA World Cup and all eyes will be on an economy that has been experiencing a period of relative economic disappointment.

In the past decade, Brazil's economy has grown by 44% in real terms. This is a substantial increase, but it is the slowest in the BRIC group (Russia, India and China grew by 48%, 105% and 164% respectively). As Figure 4 shows, most of that expansion came prior to the financial crisis. Growth since then (apart from 2010) has been sluggish at less than 3%. We expect growth to be 1.8% in 2014, continuing this trend.

A key soft spot for the economy has been its lacklustre export performance. In the 7 years prior to the financial crisis, Brazil's exports grew at an average annual rate of 10%, but in the past 6 years they have grown at only 1.7%. This slowdown has been a key driver of its worsening current account deficit (see Figure 4). Brazil's exports have been hampered by a volatile exchange rate, driven in part by investor risk appetites and cheap dollar flows stemming from the Federal Reserve's QE policies.

Brazil also faces domestic challenges. Public sector intervention in the economy is extensive, but problems with policy co-ordination and supply side constraints mean initiatives often under deliver or distort markets (for example, fuel price subsidies have caused problems for its bio-ethanol industry). The private sector also contends with a difficult regulatory environment - Brazil ranks 116th in the World Bank ease of doing business index and 22nd out of the 32 Latin American economies.

Against this backdrop, could the upcoming World Cup (and Olympics in 2016) act as a catalyst for the economy? The evidence is mixed as to whether "mega-events" bring substantive economic benefits, but we think there is the potential to realise some intangible but important benefits:

- The global showcasing that key host cities achieve could pave the way for the next wave of FDI into Brazil if successfully leveraged. For example, a 10% boost to FDI would translate to an additional $6.5bn injection into the economy. There are some indications that Brazil has been taking steps to maximise the gains in this area. The country's export promotions agency has scheduled a showcase program for over 700 Brazilian companies to international investors next month.
- Additionally, the experience that local companies accumulate through hosting these mega events could be used in the future. For example, on the back of their experiences of London 2012, UK companies have sold £130m as part of Brazil's 2014 and 2016 hosting preparations.

Fundamentally, any benefits to Brazil from hosting these mega events will be affected by the perceived successes or failures of infrastructure and logistics in the economy. Although recent headlines have not been encouraging in this regard, with the Olympics following in two years, for Brazil this is a game of two halves.

Projections: June 2014

	Share of 2012 world GDP		Real GDP growth				Inflation			
	PPP*	MER*	2013e	2014p	2015p	2016-2020p	2013	2014p	2015p	2016-2020p
Global (market exchange rates)		100%	2.4	2.9	3.2	3.2	4.8	5.2	5.6	4.6
Global (PPP rates)	100%		2.9	3.3	3.7	3.6				
United States	19.5%	22.5%	1.9	2.6	3.0	2.4	1.5	1.8	2.2	1.9
China	14.7%	11.4%	7.6	7.4	7.3	7.0	2.7	2.5	2.7	3.4
Japan	5.5%	8.3%	1.6	1.5	1.5	1.2	0.4	2.1	2.1	1.5
United Kingdom	2.8%	3.4%	1.7	3.0	2.6	2.4	2.6	1.7	1.9	2.0
Eurozone	13.5%	16.9%	-0.5	1.1	1.4	1.5	1.4	0.9	1.2	1.5
France	2.7%	3.6%	0.1	0.9	1.1	1.7	1.0	1.1	1.2	1.5
Germany	3.8%	4.7%	0.5	2.0	1.9	1.3	1.6	1.2	1.4	1.7
Greece	0.3%	0.3%	-3.9	0.3	2.1	3.0	-0.9	-0.4	0.1	1.3
Ireland	0.2%	0.3%	-0.3	1.7	2.5	2.5	0.5	0.5	1.3	1.5
Italy	2.2%	2.8%	-1.8	0.1	0.9	1.0	1.3	0.7	1.0	1.4
Netherlands	0.8%	1.1%	-0.8	0.2	1.5	2.0	2.6	0.8	1.2	1.4
Portugal	0.3%	0.3%	-1.0	0.3	1.4	1.8	0.4	0.6	1.2	1.5
Spain	1.7%	1.8%	-1.2	1.0	1.3	1.5	1.5	0.3	0.8	1.0
Poland	1.0%	0.7%	1.5	2.7	3.2	3.5	1.2	1.4	2.5	2.5
Russia	3.0%	2.8%	1.3	0.5	1.5	2.5	6.8	5.9	5.5	5.0
Turkey	1.3%	1.1%	4.0	2.3	3.8	4.5	7.5	7.9	6.6	4.8
Australia	1.2%	2.1%	2.4	2.6	2.2	3.1	2.2	2.8	2.6	2.7
India	5.7%	2.6%	4.6	5.3	6.6	6.5	6.3	5.6	6.1	6.0
Indonesia	1.4%	1.2%	5.8	5.4	5.8	6.3	7.0	6.2	5.3	5.1
South Korea	1.9%	1.6%	3.0	3.6	4.1	3.8	1.2	2.3	3.0	2.9
Argentina	0.9%	0.7%	5.0	0.7	1.8	3.3	10.6	11.9	13.3	9.7
Brazil	2.8%	3.1%	2.3	1.8	2.5	4.0	6.2	6.6	5.7	4.8
Canada	1.8%	2.5%	1.8	2.2	2.5	2.2	0.9	1.7	1.8	2.1
Mexico	2.2%	1.6%	1.3	2.6	3.7	3.6	3.8	3.9	3.7	3.6
South Africa	0.7%	0.5%	1.9	2.0	2.5	3.8	5.8	6.1	5.5	4.8
Saudi Arabia	1.1%	1.0%	4.0	4.1	4.2	4.3	3.5	3.1	3.5	4.0

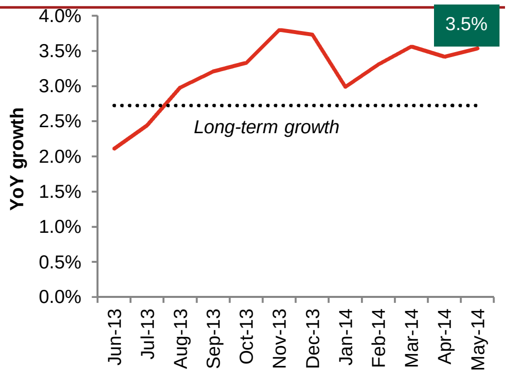
Sources: *PwC analysis, National statistical authorities, Thomson Datastream and IMF. All inflation indicators relate to the Consumer Price Index (CPI), with the exception of the Indian indicator which refers to the Wholesale Price Index (WPI). Argentinian inflation figures are based on the old price index which measure CPI in Greater Buenos Aires. A new index the "National and urban Consumer Price Index" (NuCPI) has now been released by INDEC the Argentinian statistical agency. We will monitor this new price index and will base our projection on this once we have several months of data available. Argentinian GDP projections are based on the reference year 1993. Also note that the tables above form our main scenario projections and are therefore subject to considerable uncertainties. We recommend that our clients look at a range of alternative scenarios.*

Interest rate outlook of major economies

	Current rate (Last change)	Expectation	Next meeting
Federal Reserve	0-0.25% (December 2008)	QE tapering to continue during 2014	June 17-18
European Central Bank	0.25% (November 2013)	Possible easing soon but exact form unclear	June 5
Bank of England	0.5% (March 2009)	On hold	June 5

PwC Global Consumer Index

Our index ticks up slightly to 3.5% this month, led by stronger levels of industrial production and business confidence. US and Eurozone PMIs are continuing their upward trend and equity markets remain buoyant. There are risks on the horizon: weakening economic outlook and falling industrial production in key economies such as China could weigh on future consumption growth.



The GCI is a monthly updated index providing an early steer on consumer spending and growth prospects in the world's 20 largest economies. For more information, please visit ***www.pwc.co.uk/globalconsumerindex***

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