



China faces an economic crossroads

With the collapse of external demand in the wake of the global financial crisis, China needs to reduce its dependence on exports and investments, and shift towards internal private consumption, says Stephen Roach, a leading economist and Hong Kong-based chairman of Morgan Stanley Asia.

“The next China will increasingly be about internal private consumption,” Roach said in a recent speech to the American Chamber of Commerce in Singapore. In his new book ‘The Next Asia’, Roach explains that China has become too dependent on exports and investments, which drove its economic success and accounted for almost 80 per cent of GDP. But with the end of the global economic boom, China experienced a sharp contraction in export growth late last year and its industrial output growth fell into the low single-digits.

This, says Roach, was a “wake-up call for Beijing,” as well as for the export-led Asian region. Roach notes that Chinese premier Wen Jiabao had cautioned that although China’s economy appeared robust on the surface, beneath the surface it had become increasingly “unbalanced, unstable, uncoordinated, and unsustainable”. The premier gave this warning as early as March 2007 at the conclusion of the National People’s Congress.

“China



a being immensely pragmatic,

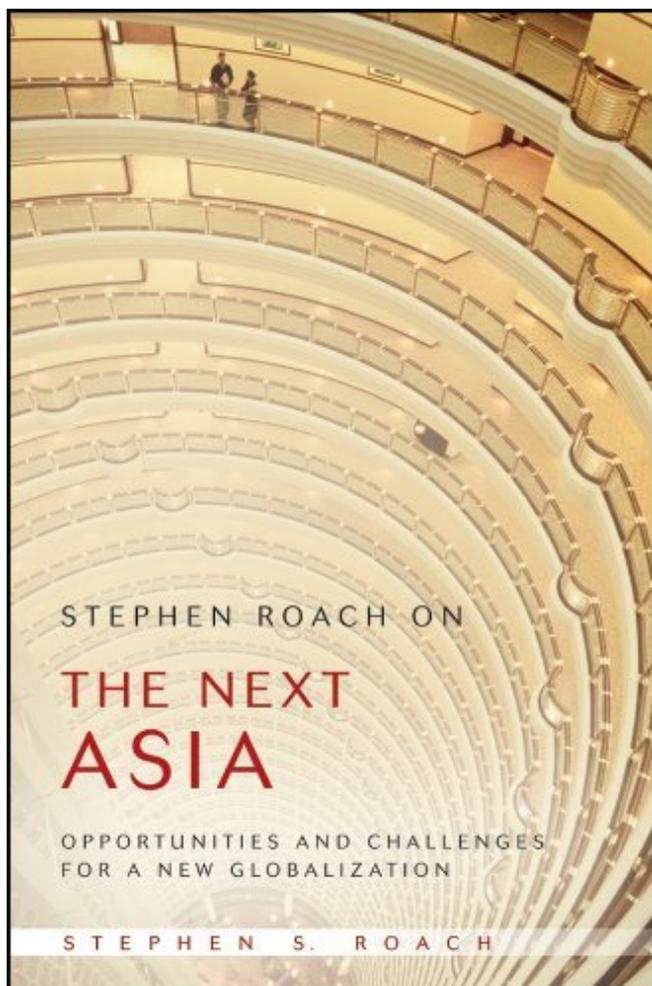
fearful of social instability, will lead the charge in that regard,” says Roach. Three key initiatives will underpin China’s transition towards a more self-sustainable economy, Roach says. These include an aggressive funding of the social safety net (especially social security, private pensions, medical care and unemployment insurance), providing significant support to rural incomes (through tax rebates, land reforms and IT-enabled connectivity), and lastly, explicit development guidelines for the emergence of large-scale consumer products and services industries.

China’s internal private consumption, which accounts for just 35 per cent of GDP, is currently declining, while its services sector, which accounts for 40 per cent of GDP, is also falling. Roach points out that no major economies in the modern history of the world have figures that low, but he believes they will rise “as China responds to the imperatives of the post-crisis world.”

And as China leads the rest of Asia in economic growth, it will provide “huge opportunities” for Singapore, Hong Kong, Japan, Korea and Taiwan to tap into China’s economic ascendancy through exports, says Roach.

Roach adds that as China drives the economic

transformation of Asia, it will bring about several benefits. For starters, there will be a better economic balance in the global economy, as Asia becomes more self-sustaining. For China's part, by broadening its macroeconomic drivers from investments and exports into internal private consumption, China can better deal with the significant inequities and disparities in income distribution, which will address potential social unrest.



Furthermore, by shifting towards a services-based consumption economic model and moving away from the industrial production, export and investment economic model, Asian economies will begin to reduce their demand for natural resources, which would lower commodity prices and improve sustainability for the global economy.

And as China shifts towards internal private consumption, Asian economies will reduce their surplus in savings, current account and trade, and take structural steps to relieve some of the bubbling trade tensions, says Roach.

Lastly, the transition from capital-intensive and labour-saving manufacturing-led growth to a labour-intensive and increasingly services-based consumer growth model will help increase employment and reduce poverty.

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