



Global outlook: big spenders and penny-pinchers



By [Jill Wong](#)

In the US, extravagance is a normal way of life. In China, it is a sin. Such contrasting consumer psyche between the two economies needs to be evened out before a sustained recovery of the post-bubble global economy can be achieved in the longer run, says Stephen Roach, chairman of Morgan Stanley Asia.

In a talk given to the Asia Society Hong Kong Centre entitled “Pitfalls in a Post-Bubble World,” Roach warns that the pain of the global recession caused by the bursting of asset and credit bubbles has only just begun to take its toll on export-dependent Asian economies.

“Obviously we’re in a global recession. It’s a severe one. But it is a unique one. It is a post-bubble recession brought about by the bursting of multiple-asset credit bubbles around the world. So do not go back to your economic history or your textbook to try to figure out how to calibrate this cycle.”

“The cycle, itself prompted by the bursting of asset and credit bubbles, is very much intertwined with the unsustainability of imbalances that have built up over the last decade, in large part between savings-short current account deficit nations like the US and surplus-savings countries like those in Asia, in particular China,” Roach says.

The next couple of years are expected to be a much weaker period for the global economy – Roach estimates average annual growth for at least the next three to five years to be “a number closer to three per cent” – and how quickly the world returns to a stable economic climate will rest largely on two main pieces of the equation: the American consumer driving the demand side and the Chinese producer driving the supply side, he adds.

“Many of the adjustments that are now occurring, especially those in the US and China, I think, will be viewed with a little bit of hindsight as a long overdue and ultimately a constructive rebalancing of an unbalanced world.”

The US, which has spent itself into oblivion, will have to become a saver and China, which has spent too little and saved too much, will need to develop more of an indigenous, autonomous private consumption culture. “Neither of these developments will be easy, but they are essential and, if the world can pull it off, I think there will be a more stable and sustainable global climate than we have today,” he says, noting that US consumption as a share of GDP peaked at 72 per cent in the first half of 2007, as compared to around 67 per cent during the pre-bubble years from 1975 to 2000.



“Unfortunately, the (US consumption) binge was not supported by the economy’s internal income-generating capacity. The consumption binge was supported by the confluence of property and credit bubbles, both of which have now burst.”

The fact that Asian economies are being hit hard by global recession also goes to show that previous talk of ‘Asian decoupling’ was a myth, Roach adds. “With the monster external demand shock, with America, Japan and Europe all in recession simultaneously, external-dependent Asia, much more dependent today than it was 10 years ago, is in trouble,” he notes.

Anyone who is counting on China to lead Asia, or the world, out of recession, will also be in for a nasty shock. “China gets hit by a powerful external demand shock and the economy has hit a wall. Now you don’t know this from the numbers because they publish numbers on a year-over-year basis. The last number was 9 per cent (growth) in the third quarter. Our guesstimate is maybe 6.5 per cent. If you back out, the quarter-to-quarter comparison from the year-over-year changes tells you that growth in China in the second half of 2008 basically went to zero.”

Roach sees little room this time for proactive fiscal stimulus, a tool used by the Chinese government during 1997-98 and 2001-2002 to boost the economy. "It worked because the external environment was much more supportive and constructive to the Chinese export machine than the case today. So it's much more of an uphill battle," he notes.

The second option for China and other Asian countries, Roach says, will be to push ahead hard in developing internal private consumption.

"I think that will be an important outcome of this global crisis. But it won't be easy, and it won't be quick because what's missing throughout the region, especially in China, is the absence of a safety net. Given the massive lay-offs that have occurred in China through the reform of state enterprises, a safety net is really important to temper the fears of income and job insecurity that have resulted in ... excessive levels of fear-driven precautionary savings."

Asia also needs to be mindful of one wild card, Roach says.

"The risk is that Washington, especially the US Congress, believes that one way to obtain that fair share (of labour compensation in national income) is to impose trade sanctions on America's largest trade deficit nation, China. It's emotional politics of a Congress with broad bi-partisan support to take action that would shelter beleaguered middle-class American workers."

"The big challenge for Barack Obama will be to move to the centre of this debate, and resist the Congressional efforts to use trade protectionism to shield workers. The consequences of him not doing it are severe and very worrisome for all of us here in Asia."

Stephen Roach was speaking at a luncheon organised by the Asia Society Hong Kong Centre on January 15, 2009.

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