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Attention Chinese Shoppers

Robyn Meredith, 10.05.09, 6:00 PM ET

Morgan Stanley economist Stephen S. Roach sounded a stark warning on the global economy Monday.

"For those of you counting on the American consumer to snap back, forget it--it's not going to happen," Roach said. "Consumers are as overextended as they've ever been," and it will take them at least three to five years to retrench and dig out of debt, particularly with high U.S. unemployment rates of 9.8%, he said.

The implications for the global economy are bleak. He predicted that China will be forced to spend billions more on a stopgap stimulus plan next year. "By mid-2010, China will be hit by a reality check," which is that Chinese exports will stall because U.S. consumer spending will not have regained its previous strength.

Roach predicted China would embark on a second stimulus plan to help the nation through the slow recovery in the global economy.

But more than that, Roach said in a speech Monday that the Great Recession is serving as a long-running crisis that will force Asia--particularly China--to change its pattern of serving as the world's factory. It has already forced American shoppers to stop serving as the world's shoppers.

Roach, who is the Hong Kong-based chairman of Morgan Stanley Asia, lays out a vision of the future in his new book, *The Next Asia: Opportunities and Challenges for a New Globalization*.

In the Asia of the future, Asia's 3.5 billion consumers need to be encouraged to spend more and save less, Roach said.

"Today's Asia remains very much dominated by an increasingly China-centric export machine," Roach said. China successfully and dramatically grew its economy with strong government support for export-led growth since it began its move toward capitalism in 1978. But more than 30 years later, Roach said the time has come for a shift in strategy. "Asia must change the model."

China is now the world's third-largest economy, nipping at the heels of second-largest Japan, and China has gone from a nation of peasants to a nation with a large and fast-growing middle class of hundreds of millions of Chinese.

Why aren't they spending more? The lack of a strong safety net has led many Asians to increase their savings as they get richer, rather than spending a larger portion of their newfound income.

To get China's consumers spending more of their incomes "requires a massive investment in the long-neglected social safety net in China," Roach said.

In China, more than 65 million workers lost their "iron rice bowl" of health care, pensions and other benefits when they lost jobs at defunct state-owned enterprises shut down over the past 15 years as China embraced capitalism.

Shell-shocked Chinese who still had jobs began saving more and more in case they or family members urgently needed health care, or faced early retirement.

Eswar Prasad, a professor at Cornell University and senior fellow at the Brookings Institution, has calculated the dramatic rise in China's household savings rate: In 2000, it stood at 27.5%, but by 2008, it had increased to 37.5%. While consumption has been falling as a percentage of GDP, China's exports have been rising.

Because U.S. consumer spending accounts for such a large proportion of the global economy, without a rebound, the outlook is bleak--for a comeback in China's exports and for a comeback in the global economy.

"We are in a weak recovery," Roach said. "There could be a relapse, a double dip."