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Will Recovery Go Global?

If not, it won't amount to much.

By Robert J. Samuelson | NEWSWEEK
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Before we get too giddy about any U.S. economic "recovery," we should remember that the preceding collapse was global. No recovery can succeed unless it, too, is global. Will that happen? The world can no longer rely for growth on free-spending Americans, who are overburdened by debt and sobered by trillions of dollars of losses on homes and stocks. Without a substitute for American buying, any global revival will be feeble, because the U.S. needs export-led growth and other countries must somehow offset their lost sales to the United States.

Developing countries would seem to be the obvious replacement for American spending as the world's economic motor. These countries already account for nearly half of global economic output, estimates the International Monetary Fund, with China (11.4 percent), India (4.8 percent), and Brazil (2.9 percent) together representing nearly a fifth. By comparison, the United States is also a fifth.

All these societies have huge needs for housing, consumer goods, and health care. Except as a job creator, export-led growth doesn't make much sense. Logically, these countries should produce more for local markets and less for export. Stronger domestic spending would also increase their demand for imports. As a result, the United States would export more and import less. What economists call "global imbalances"—big U.S. trade deficits matched by big surpluses in China and elsewhere—would shrink. World economic growth would revive. Problem solved.

Just possibly, this transformation is starting. Reacting to America's shellshocked consumers, other countries have stimulated their economies, most conspicuously China. Government spending increased; credit eased. China expanded at an impressive 7.9 percent rate in the second quarter. As for India, the IMF reckons it will grow 5.4 percent this year and 6.5 percent next. Brazil's prospects are good, judges Norman Gall, an American who heads the Fernand Braudel Institute in São Paulo. The country has a "strong industrial base and energetic and creative entrepreneurs"; government debt has dropped from 85 percent of gross domestic product (GDP) in 2002 to 65 percent now.

Sounds reassuring. Still, there's room for skepticism. If Americans are spending less and saving more, then a balanced global economy requires people elsewhere to spend more and save less. That's the permanent fix, not repeated bursts of temporary economic "stimulus." The large trade imbalances fundamentally stemmed from high savings rates, especially in Asia, that dampened domestic spending and encouraged export-led growth. In 2008, China's saving rate was an astounding 54 percent of GDP, Hong Kong's 35 percent, and Taiwan's 28 percent, reports economist Eswar Prasad of Cornell University. The U.S. saving rate, including households and corporations, was 12 percent of GDP.

In theory, these vast savings could be absorbed by equal amounts of investment spending—on factories, machinery—but for most Asian countries (an exception: India), there was an investment shortfall. The surplus savings were then invested abroad, exchange rates were artificially depressed, and exports substituted for domestic demand.

China is the key country in any transition. Prasad doubts that rising domestic spending can now quickly fill a void left by falling exports. He notes that despite China's rapid economic growth, employment increases (which are what political leaders crave) have been sluggish, about 1 percent annually since 2000. "The export sector is what created jobs," he argues. "It's going to be difficult to get away from export-led growth."

This suggests aggressive export promotion, at other countries' expense. China's currency, the renminbi, remains undervalued, and export rebates on its value-added tax recently increased. Ben Simpfendorfer, an analyst in Hong Kong for the Royal Bank of Scotland, agrees. As U.S. and European markets have weakened, Chinese exporters have shifted to "emerging market" countries, such as Brazil and Egypt, Simpfendorfer says. China's exports could hurt other developing countries.

Economist Nicholas Lardy of the Peterson Institute is more optimistic. China's leaders, he says, recognize their dangerous dependence on exports. They're trying to boost domestic spending by decreasing saving. One reason for high savings, Lardy says, is the shredding of the social safety net. Historically, state-owned companies provided health and pension benefits; as these firms shut, benefits vanished and workers saved more for sickness and old age. Now China is rebuilding the safety net. Since 2005, spending on health insurance, pensions, and education has roughly doubled.

What counts is the political and even cultural capacity of countries—especially China—to wean themselves from export-led growth. The world economy is at a fateful juncture. For years, Americans' shopping spree and the jobs it created elsewhere provided a solid political foundation for globalization. With this prop gone, the world needs a new basis for mutually beneficial growth. Without it, we may face more protectionism and economic nationalism.

Samuelson is the author of the Great Inflation and Its Aftermath.

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