

Tax Cuts Will Increase The U.S. National Debt To Unsustainable Levels

WASHINGTON – It is really hard to properly assess the Republican tax reform proposal now discussed in Congress. Many details have yet to be ironed out. Sure, in principle we can agree that a basic reform leading to a simplification of the almost incomprehensible U.S. Tax Code would be much better than the confusing morass we have now.

Lower corporate tax rates

We can also agree that a lower corporate tax rate would be good for American firms, in as much as lower rates would simply realign the U.S. with corporate tax rates prevailing now in most advanced countries. And, finally, limiting the interest deduction on home mortgages in excess of a certain amount is good. This deduction in practice is only a subsidy to wealthy home owners who get a nice “rebate” –a huge deduction based on the amount of interest they paid on their mortgages– when they borrow large sums of money to finance their mansions.

That said, in all the back and forth about potential winners and losers and possible –just possible– incentives that may be created by this new legislation that may end up boosting investments, economic activities and therefore overall growth, one major consequence of this new tax law is barely mentioned.

This is mostly a tax cut

Whichever way you look at it, this “tax reform” plan is mostly a tax cut that will end up cutting national revenue –by trillions of dollar, over several years. In turn, lower revenue caused by lower tax rates will force America, an

already highly indebted country, to go much deeper into debt in order to meet current and projected spending obligations. This is a horrible, totally undesirable outcome.

America is in deep fiscal trouble

In case you did not know, America is already in deep fiscal trouble. Lower revenues would simply make a bad situation much worse. Indeed, absent sorely needed federal spending reforms aimed at slimming down (read: reduce size, scope and cost) our gigantic, and financially unsustainable entitlement programs –Social Security, Medicare and Medicaid– this Republican tax reform plan will further deteriorate our horrible fiscal outlook, simply because an even greater revenue shortfall –without significant spending cuts to go along with it– will amount to larger deficits, year after year.

Absent spending reductions, it is obvious that future larger annual deficits can be financed only through additional public borrowing.

So, here is the net impact of these ill-advised tax cuts. When all is said and done, some Americans will see their federal tax bill cut, in small or large measure. And this will be good for them.

A much larger national debt

But, as a result of this “reform”, America will have a much bigger national debt. And this is a disaster, not in the shape of a sudden catastrophe; but in the shape of a sliding slope that will amount to diminished federal resources down the line, and consequently much more limited options for the Federal Government in domestic as well as international affairs.

Simply stated, a country with an enormous, and growing, debt burden will no longer be able to afford a large defense budget. Therefore, with a shrinking military at its command,

the U.S. President will have to “redefine down” the national interest.

Indeed, trying to cope with mountains of red ink, America will be no longer able to afford meaningful amounts of federal spending on international affairs, foreign aid, health research, sorely needed new infrastructure, space exploration, energy, and what not.

You get the picture. No money means scaled down domestic and global ambitions.

If we look at history, all Great Powers that went deeply into debt simply ceased to be Great Powers. (Check Spain, Portugal, France, Great Britain, the Russian Empire, and more).

No longer a Great Power

This should be obvious to all. But let me restate it anyway. America cannot be a debt ridden country concerned about the mounting financial cost of extravagant debt service obligations and still remain a Great Power. This is just impossible.

Great Powers are rich.

The foundation of any Great Power is the flexibility provided by huge economic resources that the Government can use to pursue its objectives. Sure enough, resources are often squandered in the pursuit of ill-advised enterprises.

However, in the case of highly indebted countries, with no real money to spend, the national leadership has few or no options. No option among other things means fewer and fewer power projection means, (read: reduced military spending), and reduced leverage in international negotiations. Simply stated, the World does not give much thought about a country that used to be rich and powerful but is no longer.

When will the world stop taking America seriously?

Since Uncle Sam's debt already topped the astronomic figure of \$ 20 trillion, how much farther can we go before the World stops taking America seriously? Nobody really knows. It is a matter of changing perceptions about the speed and the likely impact of America's fiscal deterioration.

Why do we hear almost nothing about this fiscal crisis?

Well, if the fiscal consequences of this impending tax cut are so dire, why do we hear only vague and somewhat muted comments about the fiscal impact of this tax "reform"? Very simple. Elected leaders do not like to be the bearers of bad news.

And the added complication is that it is really hard to explain in layman's terms the damaging effects of an impossibly large national debt. Voters cannot "touch" the national debt and realize that it is really bad for them. These enormous figures –\$ 20 trillion dollars of red ink, and climbing– seem to be abstractions.

The sky is not falling

Besides, if the sky has not fallen until now, why should it fall tomorrow if just added a little bit more to the debt? Can't we just muddle through, just as before? Whereas a tax cut is a tangible benefit. This is something that can be sold to the voters. The bigger the cut, the better. If this means reducing already insufficient revenue, therefore worsening an already dire fiscal outlook, so be it. Tax cuts may get you reelected. Reducing spending on unsustainable entitlement programs in the name of fiscal sanity, will not get you any votes.

Only Skilled Workers Will Make It In The Global Economy

WASHINGTON – We can argue that in America may be about half the work force is doing alright because it is positively connected to the fast-moving global economy. For them globalization is good. Most of them are “knowledge workers”. They design the sophisticated technologies which power global or globally connected businesses, or at least are familiar with them and know how to work productively with them.

Some do well, many do not

If they are in high-tech, renewable energy, complex global logistics, medical science and diagnostics, digital design, supply chains creation, management and sustainability these American workers are probably doing alright.

However, most of the others –those who perform low value, repetitive tasks or who are engaged in manual labor – are or will soon be at the bottom of the skills pyramid. Unfortunately this means that their jobs are not and cannot become stepping stones to future employment in more challenging and more rewarding sectors. In many cases, the jobs that involve repetitive tasks will probably be outsourced, or will disappear altogether, as victims of the relentless automation wave.

Lack of skills, lack of opportunity

If you belong to the bottom half of the “old economy”, your current position is bad and likely to get worse. If you do not have and cannot acquire the skills that give you dexterity with machines that work with numbers, (most likely because you had a poor education and therefore you do not know how to work with these systems), you have no career future. You are or will soon be pushed down into dead end manual labor jobs like

janitor, landscape worker, bus boy, or nursing home attendant.

The unlucky former manufacturing workers who lost their jobs due to globalization and automation are equally in bad shape. If they cannot be retrained so that they could aspire to the more sophisticated positions in new high-tech manufacturing or services, in most cases they will end up in one of those dead end, low paying occupations.

Getting the jobs back

Of course, when then candidate Donald Trump came along in 2016 arguing that the only reasons these fine factory workers lost their jobs is the greed of their corporate employers seeking easy profits by exporting jobs overseas, along with unfair trade competition from China, Germany, South Korea, Japan, Mexico and everybody else, these displaced workers were eager to listen. And they were willing to believe that, indeed, all it takes to restore their old manufacturing jobs, (with all the perks and benefits), is a new President who really wants to help the little guy by turning things around in Washington.

Yes, they believed that a President can reverse the negative impact of globalization. Yes, he can force U.S. companies to stay at home and hire more American workers. Yes, he can re-negotiate unfair trade deals, so that the avalanche of cheap imports will stop, while American companies will find new markets abroad.

A nice dream

This is unfortunately only a nice dream. No, no President, however well-intentioned, can stop, let alone reverse, globalization. Yes, he can strong arm corporations in order to slow down or stop the outsourcing process. But this is no long term solution.

In the end, American companies will succeed only if they can be and stay competitive. Forcing them to keep expensive or

money-losing operations in America, so that workers can collect a pay check, while their nimble foreign competitors conquer markets leads only to eventual economic decline.

The way out

So, what is the proper way of addressing this crisis brought about by the competition of cheap labor (mostly from Asia) and the relentless march of automation?

The only way is for the unskilled to become skilled.

Those who are not employable today because they lack the knowledge and the basic understanding of how the high-tech knowledge economy works need to get those skills. And fast. Those who do not, are left behind. For them there is no upward mobility, no career ladder.

The old adage that "hard work" is the key ingredient to success in America is no longer valid. Yes, diligence and discipline still matter. But only when accompanied by the sophisticated knowledge that allows mastery of complex systems.

How is France doing?

Well, if this is the rather gloomy picture for millions of Americans who may have missed the bus leading to the global economy, what about elsewhere? What about France, for instance?

France recently embarked in a an incredibly ambitious political experiment. The French voters ditched the established political parties, of the left and the right, and elected President the young and completely untested Emmanuel Macron. And the reason is that this investment banker turned politician, promised nothing less than economic renaissance.

While he phrased his campaign slogans differently, he promised the same end results promised by candidate and now President

Donald Trump: a complete bottom-up economic transformation.

Newly elected French President Emmanuel Macron claims that his policies will kick-start France into high gear. This rather old and unimaginative country will become a "Start-Up Nation". As a result of fresh pro-growth policies, there will be a fresh crop of entrepreneurs and innovators.

Reform labor laws

Well, in principle this is possible. However, how do you make this happen? One good place to start is by reforming the antiquated French labor market. France is still prisoner of the old, pro-union leftist agenda which is all about the protection of workers rights. Nothing wrong with that, in principle.

The problem is however that by focusing on the protection of those who are employed, French labor laws make it much harder for employers to hire new workers. Indeed, when a new worker is hired, given all the protections he/she is entitled to, it becomes almost impossible or at least extremely costly to dismiss him/her when business is down.

In other words, by offering maximum protection to employed workers, French labor laws made sure that fewer workers would be hired, even in good times. In addition, the perks and benefits going by law to employees made French labor costs too high, this way making French companies less competitive in the global market place.

Bite the bullet

It seems that President Macron is willing to bite this bullet. His government wants to tackle labor laws reform.

But here is the political and psychological problem. Even if well designed and skillfully implemented, labor law reforms will threaten the job security of existing workers before they

will be able to broaden the labor market, therefore offering new opportunities to those who cannot get into it today. Which is to say that there will be pain first (guaranteed), and (possible, hoped for) gains later.

Can Macron convince France?

Can President Macron convince the French people that he can manage this complicated process well? Can he convince workers who may lose their jobs now, on account of more flexible labor laws, that in the future, given greater overall flexibility, more appealing jobs will sprout across the nation, this way creating brighter prospects for millions of old and new workers? This is going to be a tough sale.

In the end, it is obvious that a brittle French jobs market will not help advance Macron's vision of France as a "Start-Up Nation". Economic renaissance is very appealing until voters realize that change may entail threats to their current security. I am a bit pessimistic about the depth of France's newly discovered enthusiasm for enterprise and innovation, once the French realize that this hoped for transformation is not pain free.

I doubt that Macron will have the ability to convince most of the country that a more fluid society with fewer protections is also a more flexible society that creates more opportunities. No doubt most French would like to see more competitive companies and more jobs created. But those who are employed now do not want to lose whatever job security they have.

The challenge

As noted above, even here in America, until not too long ago the quintessential "Start-Up Nation", in many sectors of our society and economy we are failing to live up to the old and time-tested "can do" spirit of flexibility and quick adaptation to new circumstances.

We failed to build the education, vocational training and retraining structures that would have allowed millions of workers to have a relatively smooth transition from old-fashioned, large scale manufacturing to a new, complex and more demanding knowledge economy.

Can an even more ossified France do a better job? Can a young, optimistic President Macron inject a new vigor into a declining economy?

Time will tell.

[Will Washington Give Arms To Ukraine?](#)

WASHINGTON – Back in February 2014, right after a popular rebellion ousted pro-Russian President Viktor Yanucovych, this way taking over political control in Kiev, the then Obama administration was long on promises of aid and support; but very short on delivering almost anything of real value to the new supposedly pro-American and pro-European Ukrainian government.

Economic basket case

On the economic front, Ukraine was then (and still is today, by the way) a virtual basket case: an impoverished, non competitive, underperforming economy, poisoned by systemic corruption. On the military side, whatever your political preference on who is to blame for the ongoing fighting between government forces and pro-Moscow ethnic Russians in Eastern

Ukraine, back in 2015 it became obvious that Washington was not going to support the new anti-Russian Kiev government in any meaningful way.

Non lethal military aid

President Obama offered some non lethal equipment, (such as radar, night vision goggles), MREs, (military food rations), blankets, uniforms, and socks, (yes, socks), to the Ukrainian army –but no real weapons.

New Trump approach?

Now, with Trump in the White House, most recently the noises have been changing. It is no accident that U.S. Secretary of Defense Mattis recently made a high-profile visit to Kiev on that country's Independence Day. During public celebrations which included a military parade, Mattis stood at the side of Ukrainian President Petro Poroshenko. Mattis trip to Kiev followed another important visit to Ukraine by Secretary of State Rex Tillerson in July.

In public remarks in Kiev Mattis stated that the Pentagon is reviewing options that could include supplying real weapons to Ukraine; including anti-tank Javelin missiles, and possibly anti-aircraft missiles.

Of course, Mattis insisted that this American hardware –assuming a US Government decision to send it to Kiev– falls under the category of defensive weapons. America's stated goal –again, assuming a green light on this– would be to give Ukraine the tools to defend itself from Russian attempts to unilaterally change borders in the East.

Mattis justified any possible U.S. policy shift regarding weapons sales to Ukraine by pointing out that Russia is not living up to its commitments under the Minsk agreements aimed at solving through peaceful means all issues related to the future of ethnic Russians in Eastern Ukraine.

Policy shift

Well, should these supplies of U.S. weapons to Ukraine actually take place, this would indicate a major policy shift from the “do nothing” Obama years. For several years, Obama’s deeds (forget his speeches in support of Ukraine) indicated that America would not get involved, even indirectly, in any conflict involving Russia in Eastern Ukraine, a region with deep historic, ethnic and religious ties to the Russian state. With Obama in the White House, Ukrainian President Petro Poroshenko realized that he was on his own.

Now Donald Trump is President. So, a new more muscular approach to Ukraine in Washington vis-a-vis Russia? We shall see. Despite what Secretary Mattis just said in Kiev, I am inclined to believe that the Trump administration does not want America enmeshed, even if indirectly, in yet another, almost impossible and probably endless conflict, far from home.

A crowded national security agenda

Let’s look at the long “to do” list for the U.S. military, when it comes to hot spots. Washington is and will be engaged in the Middle East, (Iraq and to a lesser extent Syria) for quite some time. The President just announced a more muscular and open-ended policy towards Afghanistan, with the stated goals of defeating the Taliban insurrection. And then you have creeping and potentially explosive crises with North Korea, Iran, and may be with China on the South China Sea. Based on recent Washington moves and public pronouncements, we may also have to add Venezuela to this already long and challenging national security agenda.

Does Washington want to add an insoluble conflict in Eastern Ukraine to the headaches list, while cash strapped America has a hard time keeping up with existing and potential commitments? I do not think so.

Will NAFTA Be Fixed?

WASHINGTON – It is not a bad idea to look at ways to improve NAFTA, the Free Trade Agreement linking Canada, the U.S.A. and Mexico that came into force in 1994. Back then, we had a different world. The Internet was just beginning to blossom; the on line giant Amazon did not exist, and Apple's future was uncertain. Energy production and possible new cross border investments within North America did not even remotely resemble what we have now. Think of the incredible shale oil and gas revolution in the U.S., large scale oil extracted in Canada from oil sands in Alberta, and then exported to the United States, and the recent liberalization of the energy sector decided upon by Mexico, simply because they are shipped from Mexico.

Make it better?

What is not entirely clear at this early stage in the process is the spirit animating the American negotiators. As a presidential candidate, Donald Trump argued that NAFTA is a horrible arrangement that hurt the U.S. economy and workers, a key item within a long list of fatally flawed trade agreements.

So here is the question. Is the goal here to improve NAFTA or to try to kill it? We shall soon find out.

Key issues

Among the many issues that will be addressed by the U.S., Mexican and Canadian negotiators, "rules of origin", "dispute resolution" and "government procurement" stand out.

Rules of origin

In order to qualify for the NAFTA free trade preference, (this means no customs duties within the free trade area), goods coming into the United States –say from Mexico– must qualify as “made in Mexico”. For example, they cannot be sneakers or T-shirts made in China, exported to Mexico and then re-exported tariff free to the U.S.A., pretending that they are made in Mexico.

However, in this global economy sustained by global supply chains, how does one establish clear rules aimed at determining the origin of complex products? Think for a moment of automobiles assembled in Mexico. Almost by definition they contain many foreign made parts –parts not originating from other NAFTA countries.

Well, here is the question. What is the limit of foreign (non NAFTA) made components (in terms of value of the components, and in terms of overall percentage of parts) beyond which the car assembled in Mexico no longer qualifies as “originating in Mexico” and therefore not qualifying for the NAFTA preference?

How strict?

How high do you set the bar? Is a car with 30% non NAFTA components still qualifying for tariff-free NAFTA status? Or can the NAFTA negotiators be more lenient and set the bar at 40%? This is a big deal.

More or less stringent rules of origin will affect established trade relations with a global web of suppliers. No wonder the Japanese are following the NAFTA renegotiation issue very closely. The Japanese brands assemble cars in Mexico. Ostensibly those cars are “made in Mexico” and so they can be exported to America customs free, as they benefit from the NAFTA trade preference.

Components made in Japan

But here is the thing. Everybody knows that these cars contain

a large amount of components made in Japan. If adopted by the three partners, more stringent NAFTA rules of origin will inevitably disrupt established supply chains created by the Japanese brands to export components that end up in cars that until today met the minimum NAFTA origin criteria to be considered as "made in Mexico".

So, here is the issue that will affect the negotiations. America wants much stricter rules of origin, because it does not want what the U.S. considers to be essentially Japanese cars, disguised as "made in Mexico", to come into the USA tariff free, (because of the NAFTA preference),

Can a compromise be reached regarding what percentage of a finished product must be made of components made in Mexico, Canada or the U.S.A. in order to give this product "NAFTA origin"?

Dispute resolution provisions

The Americans also do not like the "dispute resolution" mechanism included in the original NAFTA Treaty. Many in the U.S. look at it as a binding arbitration process which amounts to an infringement of US sovereignty. Americans do not like to be bound by a process whereby non-U.S. judicial bodies decide the outcome of trade disputes. The other two NAFTA countries would like to preserve this dispute resolution mechanism. Is compromise possible?

Public procurement

Public procurement is another sticky issue. The three countries would like to have free and equal access to public procurement bids (think of government contracts which may include IT services, or infrastructure projects) put out by their NAFTA partners. Except when they do not.

Especially with President Trump pushing for an "America First" general approach on all trade and non trade issues, when it

comes to public procurement, Washington wants to privilege U.S. companies through “Buy American” policies.

And this would include all or most government contracts. This is obviously against the spirit of wide open procurement with a bidding process open to all firms within NAFTA.

Uncertain outcome

In the final analysis, all these are very complex and technical issues –on a good day. If the parties are willing to compromise, there is an opportunity to improve NAFTA.

But if there is a negative bias against NAFTA, it is relatively easy to tear apart this free trade area linking the 3 economies of North America.

OPEC Defeated By US Shale Oil?

WASHINGTON – It seems that American shale oil producers, an assorted group of small and medium-sized firms which gained strength in the last decade and are now operating in many states, have become the swing producers in a position to influence global oil prices. How did that happen?

Cutting costs

U.S. shale oil production is relatively new. At the beginning

of the “shale revolution” the cost of extracting oil from shale formations was quite high. But now they have come down significantly, mostly because of aggressive cost cutting measures adopted in response to OPEC imposed low prices. (More on this below). On account of this incredibly fast makeover, today a large number of the shale companies, especially those operating in West Texas, are profitable even with oil well below \$ 50 per barrel.

Most interestingly, shale oil producers now have the ability to ramp production up and down with relative ease, this way adjusting to global market conditions, without causing major disruptions to their operations. They can increase output when prices are higher and cut back when prices are too low. Conventional oil producers do not have this option.

With crude around \$ 50 per barrel, it is good news to have a substantial number of U.S. based oil producers supplying the domestic market, while making a profit even in this new era of low prices. This is a big plus for the American energy sector, and for all American consumers of energy products.

OPEC reactions

With good cause, OPEC saw the spectacular increase of U.S. production caused by the large scale exploitation of abundant shale oil reserves (an additional 4 million barrels a day in just a few years) as a threat to its market dominance.

Hence a very simple strategy aimed at eliminating the American shale oil threat. The plan was to deliberately over produce, this way causing a global glut and consequently falling oil prices. The bet was that a long stretch of low prices would kill the U.S. high cost shale newcomers who –according to all analysts– could not survive with oil below \$ 60 per barrel.

After having eliminated the U.S. menace, OPEC would go back to business as usual, reaffirming its position as the oil cartel which alone has the power to dictate prices by manipulating

supply.

The strategy failed

But it did not work out this way. Not by a long shot. And this is because the U.S. shale producers, surprising everybody, managed to quickly adopt major technological improvements which increased well productivity, while aggressively cutting other production costs, this way staying profitable even with oil below \$ 50 per barrel.

All in all, the Saudi/OPEC plan failed. While several marginal U.S. shale producers could not make the adjustments fast enough and went bankrupt, most of the shale sector survived the OPEC imposed squeeze on profits.

The high cost of low prices

In the meantime, the extended period of low prices hurt OPEC producers very badly. They saw their precious oil based revenue dwindle rather dramatically. It soon became clear that most OPEC countries could not sustain an extended period of low prices.

Therefore, led by Saudi Arabia, the OPEC cartel, (this time working in concert with non OPEC Russia), tried to change strategy and jack up prices by cutting production, this way eliminating the oil glut they had created.

But this new approach is also failing. As oil prices go up on account of OPEC/Russia production cuts, the U.S. shale companies ramped up production, this way offsetting the OPEC/Russia cuts. As OPEC imposes cuts on its members, the U.S. shale sector produces more, while Saudi Arabia is denied the revenue gains that should have resulted from production cuts. So, the OPEC strategy aimed at eliminating the U.S. shale threat to its market dominance did not work.

Loss of precious revenue

That said, the sustained “attack” against US shale has been horribly expensive for the OPEC cartel members. Years of low prices hurt major Middle Eastern oil producers, (not to mention Nigeria and Venezuela, and non OPEC Russia, among others), in a significant way.

Most of these countries rely heavily on oil revenues to finance all or most public spending. Many of them had adopted national spending programs and budgets which assumed oil prices at \$ 90, or \$ 80 per barrel.

This means that all of them are facing fiscal problems or outright crises. Lacking oil revenue in the expected amounts, they have to cut spending and borrow more in international financial markets. But this is not an easy adjustment.

For example, in Saudi Arabia major spending cuts caused by declining oil revenue could lead to unprecedented political problems down the line. Almost the entire Saudi population depends one way or the other on direct or indirect government subsidies funded entirely via the oil revenue.

Reforms will take time

We know that the Saudi Monarchy is now openly committed to a major economic and fiscal transformation which will (hopefully) reduce and eventually eliminate all state subsidies, while promoting plans aimed at diversifying the economy. But, even in the best of circumstances, this is going to be a long journey. Cutting government largesse too much too soon could be politically dangerous.

Bottom line; U.S. shale wins; OPEC cartel and its new allies lose.

Trump Takes U.S. Out of Paris Accord on Climate

WASHINGTON – U.S. coal miners and out of work factory workers: this is for you! President Donald Trump publicly announced that the U.S. will withdraw from the Paris Climate Accord that his Democratic predecessor, Barack Obama, promoted and warmly endorsed. Trump's argument against the Paris deal is that it will penalize the American coal mining industry, and the overall American economy in the short term, with only vague hopes of somewhat lower world temperatures, way down the line.

Bad deal for America

As Trump sees it, this is a bad deal for America; and so the right thing is to get out of it. Sticking to the obligations created by the Accord would amount to enacting the equivalent of a huge energy tax on the US economy, because compliance with new, strict emission controls (in order to limit the amounts of greenhouse gases released into the atmosphere) will be very expensive.

As a candidate, Trump promised that he would withdraw from this climate deal, and now that he is President he is doing it. We know that his close advisers are divided on this issue. His daughter Ivanka and son in law Jared Kushner, along with Secretary of State Rex Tillerson, recommended not withdrawing. Still, in the end Trump sides with the opponents.

What does this mean?

That said, from a practical standpoint, America's exit, at least in the short term, will not amount to any worsening of the global climate. Indeed, the Paris Accord, if all goes

well, promises only modest progress on lowering the temperature of the world, and only after many years. And this will happen only if we assume that all the other participants will actually do what they promised to do in terms of enacting new policies aimed at lowering their consumption of fossil fuels, this way reducing greenhouse gases emissions. Do keep in mind that the Paris Accord has no enforcement mechanism. The commitments made by the signatories are purely voluntary. In the case of China, the world's biggest polluter, Beijing is theoretically bound to implement new policies several years from now.

Political consequences

Still, Trump's decision on this rather emotional issue has had immediate political consequences. From the stand point of other nations, particularly the leaders of the G 7 Trump just met in Taormina, Italy, this amounts to America choosing to go it alone, openly dissenting from a global consensus on the global threats to the earth created by the unrestrained consumption of fossil fuels.

U.S. no longer leading

In the short and medium term, this means that America is no longer leading the world on a critical policy issue, As most world leaders see it, America has now retreated in its narrow universe characterized by a bizarre anti-science fixation pursued by a strange president who is "anti everything".

Anti-everything Trump

Indeed, Trump is so anti-immigrant and xenophobic that he wants to build a wall along the entire border with Mexico.

Furthermore, according to the now widely accepted narrative, this is a president who is openly against free trade, against the EU, against NATO, and against Muslims, (sort of). Given all this, Trump being also against joint international efforts

aimed at stopping and hopefully reversing climate change is disappointing; but not surprising. This new development fits the now accepted narrative.

America is no longer leading. Trump's America has retreated behind a myopic worldview of narrow self-interest.

From the standpoint of old friends and allies, Trump's announcement on exiting the Paris Accord is yet another (sad) sign that America is no longer the "Leader of the free World".

In fact, even before this new development on the Paris Accord, German Chancellor Angela Merkel had already publicly argued that it is time for Europe to think of and plan for a future without close ties to the U.S., since Trump's America is no longer a reliable friend.

Political symbolism

Again, keep in mind that all this is mostly about political symbolism. It will take four years for America to fully extricate itself from the obligations contracted under the Paris Accord. This is fairly long time. And again, keep in mind that under the terms of this Paris deal, major polluters like China and India have modest obligations when it comes to reducing their own emissions that will kick in much later. Which is to say that you should not expect world temperatures to start rising tomorrow, simply because today President Trump announced that America will pull out in four years.

No gain

However, as indicated above, this decision is not without political consequences. In the end, all this is will amount to an additional loss of international prestige for Trump's America.

With all this in mind, whatever you may think about the intrinsic policy value of the Paris Accord, it would have been

better for Washington to be part of it, as opposed to becoming now a big pariah in the eyes of the world.

Trump is talking to his base

Well, then why did he do it? Very simple.

Trump's narrow concern here is to reassure his domestic political base –the millions of Americans who voted for him last November. This base includes out of work coal miners and people displaced by the closure of old manufacturing plants.

Trump's message to them is that his job is to revive the American economy. If this means heavy reliance on dirty energy, so be it. Out of work factory workers want money to pay their bills. They do not care about the fate of polar bears or about extreme weather phenomena in Africa. And they do not care about rising sea levels.

Finally, dire scenarios of New York City and Miami under water in just a few years (because of the rapid melting of the Polar Caps) are definitely a hoax –at least according to Trump and his supporters.

No Serious Discussion About Entitlement Reform In The U.S.

WASHINGTON – Much has been said about the first Trump budget recently released. The expected partisan critiques –in fact outcry– focus on proposed cuts in Medicaid and disability

benefits. Therefore, this becomes a “cruel budget”, an open attack against weak, low income Americans, and so forth.

No discussion about Entitlement Reform

Well, this may be true. However, the biggest problem with this proposed federal budget, (and with many budgets that preceded it, coming from both Democratic and Republican Presidents), is that –leaving aside symbolic fights– it is a reflection of an unchanged (unchangeable?) fiscal *status quo* that will stay pretty much the same until the American political leadership –Democrats and Republicans acting together– will finally address its ***Number One Policy Priority: Entitlement Reform.***

Symbolic cuts

The Trump Budget, even assuming that it will be passed by Congress as is, (it will not), will never “solve” the structural fiscal imbalance –namely: permanent high deficits– that has regrettably become the norm in America. You may indeed cut spending for the State Department, the Education and Energy Departments, and more. You may reduce Medicaid and the Food Stamps Programs. But none of this would really “bend” the overall spending curve. Hence the deficits and a growing national debt, soon to be out of control.

How so? Very simple. Anybody who has given even a mildly serious look at U.S. Federal Budgets notices a trend. The main drivers of (over) spending are large and growing federal entitlement programs that are not even voted on. They are on automatic pilot.

Social Security and Medicare bigger than ever

The fact is that these programs (first and foremost Social Security and Medicare, accompanied by many other smaller federal assistance program), have become so large that now they comprise almost 2/3 of total federal spending. If you add to this colossal total another 16% of overall federal spending

devoted to national defense (sounds like a lot; but in relation to GDP defense spending is historically quite low), plus about 6% of total outlays that have to be set aside for debt service, (this is about paying interest on all the debt we have accumulated until now), and you realize that there is almost nothing left to squabble about.

Indeed, “the rest” –what the budget professionals call “non defense discretionary spending”– is less than 15% of the total. Since the bulk of all spending (with the exception of defense) is essentially off-limits, all the budget battles are fought on this residual 15%.

Which is to say that, unless we want to entirely abolish most of the U.S. Government, (Agriculture, Justice, Transportation, money for NIH and medical research, NASA, and more), we cannot possibly change the present pattern of spending without seriously looking at entitlement reform, with the goal of reducing future outlays. Since most of the real money goes to these programs, they should be reformed so that there will still be benefits for seniors in the future, but sustainable benefits. Simply stated, for social programs to work in a sustainable way, in the future most Americans will get less.

Everybody knows this

Again, every student of US public policy, beginning with House Speaker Paul Ryan, (He used to be Chairman of both the Budget and later on the Ways and Means Committees), knows all this.

And yet, for fear of causing massive social unrest, nobody –Republicans and Democrats– want to go even near the entitlement reform issue. The topic is worse than a non starter. It is almost unanimously viewed as political suicide.

Not straying from the conventional wisdom, as a candidate, Donald Trump promised that he would leave all key federal entitlements untouched, claiming that these benefits have been earned by individual Americans, and therefore they should not

be messed with. A very conventional approach.

“The Moment of Truth”

A few years back, (2010), President Barack Obama convened a special bipartisan commission (it became known as the “Debt Commission”) that was chaired by Erskine Bowles (Democrat) and Alan Simpson (Republican) in order to give a serious look at the issues of taxation and spending.

These two elder statesmen took the lead and eventually issued a powerful report in December 2010 aptly titled *“The Moment of Truth”*. They, and most of the members of their Debt Commission, argued convincingly about the need to seek and find broad bipartisan support for a thoughtful plan aimed at reforming entitlement programs that had been designed in another era with different demographics (starting with life expectancy, much shorter at that time), and much lower health care costs. They pointed out that, if we change nothing, we are headed towards financial ruin.

They argued intelligently and convincingly. But nothing, absolutely nothing happened.

No action

As it turned out, President Obama (even though he created the Commission) did not want to tinker with issues viewed by most political insiders as “radioactive”.

The Tea Party Movement, at that time growing in national popularity, was led by amateurs who understood practically nothing about the real dynamics of public spending. Their home spun wisdom was that America’s run away public spending and ensuing annual deficits, were all due to “fraud, waste and abuse”. As simple as that. Their remedy? Eliminate silly programs and politically motivated earmarks, tighten the system, punish a few offenders who get benefits via false claims, and all would be fine.

Well, it would not be.

Given the overwhelming and growing weight of federal entitlements benefiting mostly senior Americans, you could abolish the entire Defense Department and you would still not be able to alter the overall pattern characterized by over spending and perennial budget deficits.

Spending favors senior citizens

Simply stated, in America, just like in most other rich democratic countries, there is now an unwritten social contract whereby large and increasing amounts of national resources are devoted to assistance to the sick and to the elderly.

The problem is not that the priorities are wrong. The problem is that this level of assistance has become unaffordable, because it is no longer matched by revenue. Hence our annual deficits that add to the already exploded national debt. Of course, we could raise taxes in order to rebalance the federal deficit. But this would mean significantly "higher taxes", another radioactive issue that no mainstream politician wants to address.

More debt is the path of least resistance

So, here is the thing. Politicians want to keep doling out large entitlement benefits. But they do not want to tell the country that there is not enough money to pay for them. Instead, they have chosen the path of least resistance: use most of the federal revenue to pay for the entitlements, this way starving the rest, and borrow the balance.

This may look clever in the short run. But this approach means that we are well on our way to becoming Europe or Japan: societies with enormous public spending and huge national debts that simply do not have any resources to invest in their own future.

Let me say this clearly: these are society headed towards decline. In fact, some of them are already beyond repair, mostly due to the impossible fiscal burdens represented by gigantic national debts.

Where are we headed?

Well, unless we want to become the next Italy or Japan, we need a serious conversation about the level of future federal benefits. This does mean *“throwing sick grandma in the snow, in the middle of winter”*. But it surely means readjusting benefits so that, going forward, we take care of the neediest first, while all the others will get smaller benefits, and later in life.

Anyway, all this is purely theoretical. The current budget debate, with all its theater of partisan acrimony, posturing and grand standing, does not even begin to address entitlement reform. And this means that what we are having is not a serious, adult debate. This is mostly rubbish.

We need a serious debate

The American people deserve national leaders –in both parties– who will tell them the truth about what we can afford going forward, and how we can and must share sacrifice, (fewer benefits, higher taxes, at least for some), in a fair and equitable manner.

This is what mature political discourse in a republic should be about. But nobody wants to even think about it.

How Will Macron Govern France?

WASHINGTON – Emmanuel Macron’s meteoric ascendance –literally from nothing prior to a short stint in the Hollande administration, to President of a major European country—is by itself a stunning political achievement. The very fact that obscure Macron saw an opening for himself as the leader of a brand new movement (he called it *En Marche!*) in a crowded field populated by seasoned politicians at least twice his age speaks volumes about Macron’s political instincts.

He was lucky

That said, we also know that Macron was very lucky. The center right party candidate, the Republican Francois Fillon, the favorite to win this presidential race according to most, suddenly imploded on account of the scandal related to fake staff jobs he offered to his wife and children. With Fillon sunk and a very weak Socialist party candidate running, Macron became the only credible alternative to Marine Le Pen, assuming that he could make it to the second round of the vote. Indeed there was a brief but all too real scare that grew as the first round got closer. It was all about Jean-Luc Melenchon, an unreconstructed Marxist who connected surprisingly well with the old French leftists (still many of them!) and with many young voters. Had Melenchon managed to overtake Macron in the first round, it would have been a disaster for Macron, the would-be new leader of a the newly reconstituted reformist center. (Imagine the scenario of a second ballot with Le Pen and Melenchon as the two finalists fighting for the French presidency).

Predictions were correct

In the end, as we now know, Macron managed to get to the

second round, even though not by much. And then, after this critical first round semi-victory, everything happened according to most predictions. Macron won on May 7 by a large margin, (64%), while support for Marine Le Pen did not pass the symbolically significant 40% threshold. In fact she only got to 34%. Now she is defeated and humiliated, although still alive politically and –she says– willing to keep fighting.

Happy ending?

So, happy ending? Not quite. France and the world dodged a major bullet. A Le Pen presidency, at least at the start, would have been very disruptive, given her very negative views on Europe, the Euro, trade relations, and the NATO Alliance. Not to mention the heavy and disturbing baggage of xenophobia, racism, anti-Semitism, and more.

How to rejuvenate France

That said, while Macron's victory for sure is a precious reprieve, it is no guarantee that a severely weakened France, burdened by unaffordable social spending, unwieldy labor rules, and inefficient state owned corporations will become all of a sudden nimble, regain the enthusiasm needed to get out of the swamp of low growth and high unemployment; not to mention be able to overcome the unresolved issue of millions of (mostly Muslim) non assimilated immigrants, in many instance the breeding mix for radicalized youth who engage in acts of terror.

It is important to stress that Macron won on a positive message. He stated that France must embrace –not reject– globalization, foreign trade and strong relations with Europe. He forcefully argued that France is part of the global economy. Withdrawing behind protectionist walls is no solution.

Untested leader

All true. The unknown here is whether this new –and completely untested– young president (the youngest leader of France since Napoleon) will be able to galvanize his country, while at the same time gathering the necessary parliamentary support to pass critical labor and tax reforms, the minimal policy preconditions to create the enabling environment for French business and enterprise to flourish.

In order to secure these reforms Macron needs a major win at the forthcoming parliamentary elections. He needs a workable majority in the National Assembly in order to govern. Can his brand new political party repeat the leader's May 7 surprising victory?

The best choice?

Finally another somber consideration. The very fact that we applaud Macron's victory as a major turning point in French and indeed European politics is in itself stunning. Macron is completely unknown, untested and inexperienced. Not that the establishment politicians inspire such great confidence.

However, the 64% obtained by this young new president is by itself a manifestation of a country adrift, grasping this modest straw (Macron) because this was the only way to avoid the abyss of a Le Pen victory.

When the French elevated General De Gaulle to the presidency, at least they knew they got a proven leader with a long, distinguished, and very public record. Today Emmanuel Macron is the new occupant of the same Elysee Palace once occupied by De Gaulle. The difference is that the French people who voted for Macron in large numbers have no clue as to how he will perform, because he has no real record.

The Dream Of New U.S. Manufacturing Jobs

WASHINGTON – We know that President Donald Trump pledged to renegotiate (supposedly unfair) trade agreements worldwide with the goal of re-balancing the U.S. trade accounts, while forcing companies to move lost U.S. jobs back to America.

Millions of jobs

His narrative –accepted as truthful by millions of U.S. voters– is that America lost millions of jobs in the last couple of decades, while buying from China and Japan (among others) goods worth hundreds of billions, with no reciprocity, because incompetent U.S. trade negotiators (Democrats and Republicans) were so ineffective (in fact so stupid) that they allowed this disaster to happen.

Brand new trade deals

According to the White House, the remedy is quite simple. You reopen old deals, get better terms through tough negotiations, and you force the offending countries (Mexico, Japan, China, South Korea, among others) to sell less to America, buy more from America, and spit back all the U.S. jobs that moved to their countries on account of badly conceived trade negotiations led by incompetent and unpatriotic Washington trade representatives.

Not that simple

If it were indeed so simple. The problem is that jobs are not akin to cash that can indeed be moved from one country to another in a matter of minutes. Regarding the loss of U.S. jobs, the fact is that in the last 20 to 30 years millions of U.S. manufacturing jobs moved to China because of China's extremely low labor costs. At the time, this was a most

compelling reason.

Cheap labor

American and other Western companies, always seeking new ways to keep costs and therefore prices down, chose China as their base of manufacturing operations because China's labor costs at the time were very low. Therefore, making industrial products in China –especially goods that required labor intensive operations– was comparatively quite cheap.

In a fiercely competitive global economy, all companies seek and want to take advantage of low production costs which allow them to sell at lower prices, this way undercutting their competitors.

All this happened in large measure because (after China joined the World Trade Organization, WTO, in 2001) the rest of the world accepted China as a member in good standing of the international economic and trading system.

No one seriously wanted to penalize made in China products because of the harsh working conditions in Chinese factories and China's rock bottom wages. Was that a bad decision? Possibly. Still, be that as it may, the long term consequences of that decision, for all practical purposes, are irreversible.

Trade war and no new jobs

A trade war with China, while the notion seems appealing to many, would cause a huge global crisis (you can expect retaliations and counter retaliations). And it would not produce the effect that President Trump would like to obtain: millions of jobs, now held by Chinese workers, "returning" to America, while America enjoys enhanced prosperity, and a positive trade balance.

And why is this impossible? In large measure this is due to

the cumulative impact of China's role as a global manufacturing hub. This enviable position led to the creation, over time, of complex supply chains that link Chinese factories, (and therefore Chinese workers), with a web of suppliers and vendors, within China and/or other countries in the region (Taiwan, Vietnam, Thailand, South Korea, and others). These sophisticated supply chains provide the components and semi-finished products that are finally assembled and completed in China. The finished goods are eventually shipped to the United States and other countries.

This being the case, it is simply impossible, even if we assumed the unanimous will to do so, to yank the jobs now with any Chinese factory which performs the final assembly of industrial products and move them to America.

You cannot recreate complex supply chains at will

And here is why. For this "operation" to be successful, one would have to move and/or recreate –from scratch– in America the entire supply chain that now supports that particular Chinese factory. And this would require the creation, here in America –again, from scratch– of fine tuned business relationships between the lead manufacturer and a brand new network of U.S. suppliers and vendors based on their proven ability to perform at the level required (quality, standards, specifications, delivery time) and at costs low enough to guarantee the competitiveness of the made in America finished product.

No U.S. companies operating in many sectors

If this were not enough, given the lack of meaningful industrial activity in many of the manufacturing sectors that moved to China or elsewhere decades ago, many of the needed suppliers that would be part of the brand new U.S. based supply chain simply do not exist anymore. They went out of business. How about that. No companies making the necessary

components, no supply chain.

Impossible

From all of the above, you can see that the idea of transplanting complex networks of companies, working in harmony with one another, from China to the U.S. is an impossibility.

Again, let me stress that those supply chains were not improvised in China a couple of weeks ago. They were created over decades of tests, trials and error. The notion that the entire web of complex business relationships now at the core of Chinese manufacturing can simply be dismantled and transported to the U.S. is a childish fantasy.

An additional problem: automation

And if this were not enough, you have to consider automation, a relatively recent development which did not play a significant role at the time of the jobs migration incentivised by low Chinese labor costs.

Keep in mind that automation has nothing to do with unfair trade practices. But it has the practical effect of killing U.S. factory jobs that used to be performed by humans. This is an unstoppable trend. Yes, the robots do many and in the future most of the jobs that factory workers used to do.

In a relatively short time, tomorrow's modern factory will probably be completely automated, with only a few highly specialized IT experts and engineers in charge of supervising the robots, and the overall production schedule.

Which is to say that, even if we assume that some manufacturing activities would "return" to America and/or new ones are created on U.S. soil, not much will change in terms of net new employment in manufacturing. In a best case scenario, maybe some factories will come back. But most of

the workers who used to be employed in that sector will be replaced by automation.

We are in a new era

Keep in mind that now we are in a new era; an era in which humans will do less and less factory work. As robots now and in the future will do most of the work, labor costs will become less and less of an issue in determining the location of new industrial plants. Still, as tomorrow's factories will be even more automated, it is hard to see net gains in manufacturing jobs in America, or in the rest of the high cost western world, for that matter.

No jobs coming back

In conclusion, here is the thing. The creation of complex supply chains created by Chinese companies to support China-based production over many decades cannot be dismantled and quickly reassembled at will here in America.

Furthermore, from now on automation is and will be the new manufacturing jobs killer. While automation, at least in some areas, may result in creating new forms of employment in new sectors that we cannot even think about today, the old factory jobs we used to know at some point will become extinct.

Can we do anything to reduce the trade deficit with China?

That, said, what about the chronic trade imbalance with China? Very hard to do this. And this is in large measure due to the fact that millions of American consumers love to buy cheap consumer goods. And China, for the moment at least, is still the low-cost producer.

However, what can and should change in this enormously large bilateral trade relationship is the unfair treatment of foreign companies trying to establish themselves in China, or trying to sell their products and services to China.

Unfair treatment

There is plenty of evidence indicating that U.S. exporters are penalized in a variety of ways. For instance, the Chinese use their own competition laws as an effective non tariff barrier against foreign companies. Chinese authorities selectively target U.S. and foreign companies accusing them of anti-competitive behavior, forcing them to pay fines and to license their technologies to Chinese entities, this way undermining their ability to work in China and their overall competitiveness.

Demand better terms

This is an area where the Trump administration has legitimate ground to complain and demand better terms from China. Still, even if successful, this effort would lead at best to the narrowing of the trade imbalance gap, not to its disappearance.

As for the millions of new manufacturing jobs coming back to America on account of broad new trade agreements, well, dream on. This is just not going to happen.

Wanted: Credible Centrist Political Leaders

WASHINGTON – Recently, a Democratic party elected leader of national renown argued in a public forum that in order to regain lost momentum and credibility with the American voters the Democrats have to redefine themselves as the party of economic growth and inclusiveness.

Common sense messages

At a national event focused on the future of U.S. small businesses, a Republican national leader claimed that America's greatness rests on its foundations as an opportunity society in which people can advance because of a rules based system that recognizes and rewards merit.

John Hickenlooper, the Governor of Colorado, a successful state chief executive, stated that through collaboration between Republican and Democrats we can find workable compromises on the future of the US health care system, and other national priorities.

Well, what do I make of all this? Very simple. These statements made by credible centrists in both parties raise the hope that it may be possible, even in this incredibly poisoned political climate, to rally millions of Americans, hopefully a majority, around the basic ideas of an optimistic country in which policy-makers promote economic growth, while upward mobility is based on genuine merit; and nobody is excluded or kept from advancing because of social class, gender, race, or anything else. In fact, the opposite –equal opportunity for all- is embraced by all.

And this must include quality education, the best foundation of future success in life, available to everyone; while bridges are built across every divide, and doors are wide open to all who are willing to make an effort.

It is an old idea

This idea of America as a level playing field and fair rules used to be a shared vision embraced by most. Indeed, it was the belief that America offered genuine opportunity that attracted millions of immigrants who wanted to create in America a better life for themselves. It is about time to re-propose this vision in a manner that can be shared by today's Americans –Democrats and Republicans.

Indeed, who could object to public policies that promote economic growth, social advancement based on merit, while all citizens have genuine access to quality education, careers and consequently a good seat at the table?

Lost hope

Of course, the last few years have told us an entirely different story. It is a story of lost hope, deep disappointment, and resentment. A story of popular distrust in the honesty and abilities of most elected leaders. A story of exaggerated promises not kept.

This has created an emotional anti-government rebellion on the right, (*"Washington is a rotten place"*), and the triumph of policy agendas on the left which advocate economic and social re-balancing achieved through redistribution by taking (ill-gotten gains) from the few ultra rich and giving to the rest of society. All this will be wisely designed and orchestrated by government, through taxation and subsidies.

Despondent America

The outcome of all this is not pretty. The unexpected outcome of the November 2016 presidential elections is evidence of the widespread feeling of deep despair. Indeed, according to millions who voted for Donald Trump, "the system" failed—period. Its failure is so deep that it is not worth salvaging. In fact, it should be dismantled. In fact, millions of Americans voted for Trump mostly because he is not a professional politician. Therefore he is untarnished by Washington's rot and well equipped to "*clean the stables*", "*drain the swamp*" and all by himself—with his power and superior intelligence—transform America.

Paradoxically, notwithstanding continuous economic growth and much lower unemployment since the end of the Great Recession in 2010, rightly or wrongly millions of Americans who used to be part of a self-confident middle class now are and feel

poorer, left behind and alienated. At the same time, millions of young people feel hopeless facing a world of diminished opportunities, while laboring under the crushing weight of absurdly large student debts.

There is a way out

That said, I sense that there is a way out of this. Difficult, yes; but not impossible. Yes, America needs house cleaning. It needs fresh faces not tainted by the old ways of doing business.

The unimaginative political elites still populating Washington, DC have survived by over promising everything to everybody, while pretending to pay for all the goodies they offered to various (of course deserving) constituencies, knowing full well that the only way to finance all this public largess (unaffordable entitlements) was and is to borrow more and more, this way getting the country deeper and deeper into debt.

Sadly, the Washington elites have no real economic growth strategy, while their policies aimed at buying votes through entitlements funded by public money and more and more borrowing are driving America towards the abyss of insolvency.

Credible people who will tell the truth

Most Americans have common sense. However, they need credible new leaders who will tell the unvarnished truth about the dangers of systemic and growing fiscal imbalances, (i.e we have to agree on a sensible plan to reform all major federal entitlement programs, by far our biggest fiscal problem), while pointing the only way to get out of this ditch: economic policies (think tax reform and smart deregulation affecting business activities) that will promote a more robust economic growth in a genuinely open and inclusive society. An inclusive society in which elected leaders are committed to destroying all artificial barriers to entry, while opening new avenues of

opportunity to all.

(President Donald Trump, a new leader who is not carrying the baggage of the distrusted establishment politicians, could lead the way in shaping a new American political conversation. As his presidency is just getting started, it is impossible to say whether he will engage in this effort or not. We should all hope that he will. This would benefit the country and him).

Impossible?

Well, in the end all this “back to basics” idea founded on the values of openness, fairness and merit sounds too lofty, in fact unrealistic. Yes, this is an appeal to an admittedly mythologized idea of an America “*where anything is possible as long as you work hard and play by the rules*” which (truth be told) never fully existed in the way many refer to it.

And then there is the huge problem of yanking benefits away from millions (deserving or undeserving, it does not matter) who got used to getting them. “*Come on...get real. Nobody gets elected by promising less, let alone by promising to cut existing benefits. And we in Washington just do not know how to deliver stronger economic growth. We only know how to distribute subsidies*”.

The way ahead

And yet, if we do not want to see America follow Europe on the path leading to historic decline, it is imperative to make real progress on these two related fronts:

1) restore fiscal sanity by reforming all the major entitlement programs

2) genuinely and forcefully promote economic growth and real opportunity for all

The alternative is political chaos, the de-legitimization of

our institutions, and rapid economic decline.

Some elected leaders of both parties know this. I just hope that their common sense message will be heard, understood and embraced.