

# The Dream Of A Modern Saudi Arabia

WASHINGTON – Bloomberg Businessweek placed Saudi Arabia's Deputy Crown Prince Mohammed bin Salman on its cover (April 25 – May 1) underneath a caption that says he is "*preparing Saudi Arabia for the end of oil*". The lengthy cover story is all about this energetic young Prince who –all alone– is determined to spearhead a series of bold initiatives and reforms aimed at re-engineering a country whose vast richness come from gigantic oil revenues, and not the skills of its citizens. Of course, being the son of the King helps a bit in what is still a top-down, absolute monarchy.

## **Plan to diversify the economy**

The long article explains how the Deputy Crown Prince plans to diversify the economy. He wants to start selling shares of Saudi Aramco, probably the single largest oil company in the world. He would then invest the proceeds in a number of global companies. After this diversification, in the future Saudi Arabia's economic fortunes will be less tied to the ups and downs of oil prices.

## **No more subsidies**

At a different level, the Prince wants to cut back the vast web of subsidies provided by the Royal Family to almost every Saudi citizens. But this may be a bit tricky. It is an open secret that direct or indirect payments to millions of people are the means through which the Saudi government keeps a lid on Saudi society. In a region marred by unrest and civil wars, not much anti-government unrest in Saudi Arabia, since almost every citizen gets a regular check from the government.

## **Problem: no real middle class**

Well, so far so good. Except for one thing. Even assuming that all these reforms will work, at best Saudi Arabia can become more efficient. But it simply cannot become a modern society the way we understand it. For the very simple reason that Saudi Arabia does not have basic political freedoms and a modern middle class that can act as the engine of self-sustaining growth.

Here is the simple truth. Except for vast amounts of easy to extract and therefore highly profitable oil, Saudi Arabia does not have a real economy. Saudi Arabia does not have a sizable educated middle class with a fair number of entrepreneurs engaged in profitable, innovative businesses.

### **Monarchy controls oil**

Saudi Arabia is an oil Kingdom (second largest crude reserves in the world) essentially “owned” by a mostly parasitical elite. This elite, (the extended Royal Family), controls all the oil wealth. The same leadership distributes some of the oil revenue proceeds to the rest of the country, in many cases via bogus government jobs that produce no value. It is fair to say that most Saudis do not do any real work. In the Kingdom real labor is provided by foreign workers.

### **No modern middle class**

Now, given this picture, I submit that unless these fundamentals are drastically transformed it is essentially impossible to re-engineer the Saudi society. Capitalistic economies succeed mostly because of the existence of basic political freedoms and because of a solid, entrepreneurial middle class. By that I mean large numbers of reasonably well-educated, driven individuals who engage in money-making enterprises. Their activities are supported by bankers, lawyers, accountants, marketers, public relations professionals and what not.

In other words, modern competitive economies do not exist

without a vibrant middle class that can produce at least some capable entrepreneurs. These entrepreneurs understand the value of innovation. They understand competition within a rules based system fairly managed by an independent judiciary that can act as a reliable referee in case of disputes.

### **Oil is the only productive sector**

Well, guess what, none of this exists in Saudi Arabia. And I sincerely doubt that any of this can be created –essentially out of nothing– by an energetic Crown Prince eager to modernize a rent based economy in which, with the exceptions of the few skilled people who are in charge of the highly profitable energy sector, nobody has done anything even remotely approaching real, productive work for decades.

### **Rules based democracy**

You want modernity? Well, then you need a rules based democracy in which people really understand and agree upon the proper balance between private and public, in which all players agree that the private sector is the driver of economic growth, while all economic actors appreciate the need to have and follow clear rules. You also need a government that is efficient, open, transparent, and fully accountable. Finally, you need basic freedoms, including laws that guarantee freedom of expression, and therefore truly free media.

### **Tinkering is possible; but no transformation**

I see none of this in Saudi Arabia. Despite formidable constraints, I can see that some tinkering is definitely possible within the existing environment. If his reforms work, Prince Mohammed may be able to make the existing system less wasteful, less corrupt, and less dependent on the price of oil. And this is a good thing.

But he cannot create a brand new country and a new Saudi

society. And without these two prerequisites in place, there will be no modern country.

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## Obama's Nairobi Speech In Praise of Enterprise Not Well Reported – A Pity

**WASHINGTON** – US President Barack Obama traveled to Nairobi, Kenya to address a US-sponsored international forum on entrepreneurship. He said a lot about the value of enterprise in modern societies.

### **The key point**

And yet this is what most international media quoted from his speech: *“Entrepreneurship offers a positive alternative to the ideologies of violence and division that can all too often fill the void when young people don't see a future for themselves.”*

### **That's it?**

Let me understand this. According to world media, of all the things that Obama said, the most quotable sentence is that Africans (and others) should foster entrepreneurship because it provides a good antidote to *“ideologies of violence and division”*? That's it? This is the value of enterprise? An antidote to political extremism?

This is how you narrow down what the leader of America, the most successful capitalistic economy in history –an economy,

mind you, founded on free enterprise— has got so say about the value of entrepreneurship?

### **There is a lot more in Obama's speech**

Obama said a lot more in his speech, a lot more. He talked about the power of innovative ideas, creativity, risk taking, meeting challenges. He talked about ways in which America plans to support private sector entrepreneurship around the world. He talked about the role of women.

But none of this has been reported at any length. This is a missed opportunity. A speech extolling the value of enterprise in emerging countries, precisely because it has been delivered by an American President, illuminates why the capitalistic industrial democracy model that we would like other countries to embrace, is better.

### **The enabling environment**

Sure enough, enterprise is not everything. You need a real *"enabling environment"*. You need good laws that defend private property and investors rights. You need an independent judiciary, simple regulations, and a true commitment to fight corruption.

And there is more. You need infrastructure (power generation and distribution, railways, good highways, ports, and what not). Of course you need all this. And Obama talked about this in his Nairobi speech.

### **Enterprise is key**

And yet, the truth is that, if a society is unable to produce a robust group of future oriented entrepreneurs willing to take risks, you can have all these "building blocks" without making any real economic progress.

Look, it is very difficult to "breed" entrepreneurs. But one way to encourage more people to take a chance by starting a

business is to make it clear to them that risk taking can have great rewards. You can make money. You introduce a new product or service. You can offer employment to others. You contribute to the overall progress of your society. And this is what Obama said in his Nairobi speech.

## **Incentives**

And this is why it is a great pity that most media chose to focus only on what Obama said about enterprises as antidotes to political violence. The US President said a lot more.

He said that enterprise is the engine of growth and innovation. He said that it is the best way to have faster economic growth. He said that America encourages women entrepreneurs in emerging countries. He talked about broad-based initiatives that will link US investors and technology leaders with young entrepreneurs world-wide. All this may not be revolutionary. But it is important.

Too bad that Obama's message extolling free enterprise was not properly reported, and therefore it was lost.

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## **No More Start-Ups In America**

**WASHINGTON** – There is an almost unquestioned belief that America is the land of entrepreneurs. This is “start-up” country. Anybody with a good idea, if armed with enthusiasm and persistence, is likely to get results. The assumption is that America loves young people going into business. The system helps. It is easy to get started. Relatively easy to get funding. Plenty of venture capitalists willing to buy into

a promising venture.

## **Young entrepreneurs**

And we have many good examples, from Bill Gates (Microsoft), to Mark Zuckerberg (Facebook), that demonstrate how brilliant innovators can go from zero to building enormous business empires, becoming fabulously rich in a relatively short period of time.

Well, while these are real examples, there are not as many as there used to be. The broader picture is far less inspiring. Indeed, survey after survey indicate that in America the number of new businesses has been declining. The established American firms are old. The number of newly hatched companies is very small. The number of people employed by them is negligible.

## **No more start-ups**

As Holman Jenkins put it in the WSJ (*"Secular Stagnation" and the Cheap Burger*, January 24-25 2015), *"Our new business formations are the lowest in 35 years, more like Europe than the US. According to Gallup, companies are dying faster than new ones are being born"*.

Got that? the lowest in 35 years.

Yes, we still have Silicon Valley (Thank God!) and other high-tech centers in Texas, Massachusetts and elsewhere. America is still the world leader in information technology, and one of the best in biotechnology.

But the famed, irrepressible entrepreneurial spirit that led people in their twenties (in some cases) to drop out of school in order to get started on their (sometimes) revolutionary projects as soon as possible is not what it used to be.

## **What is happening?**

The data supporting this conclusion of fewer and fewer start-ups is out there, and it is not challenged.

What is not clear is why this is happening.

Less enthusiasm for technology? Fewer young people drawn to business? Too risky to set up your own company? Better career opportunities if one chooses to work for an established big company? Lack of financing?

Who knows really.

However, we can say that gradually the old pro-business ecosystem that enabled and supported entrepreneurship has been damaged.

### **Too many obstacles**

Indeed, over time, running a business in America has become more onerous and more complicated. Taxes are high. Indeed, America has the highest corporate tax rate in the developed world. (Sure enough, large companies manage to pay much less; but only because of sophisticated tax avoidance arrangements that require small armies of accountants and tax lawyers).

### **Onerous compliance**

Besides, a thicket of rules and regulations (from safety standards, to environmental impact, to corporate governance, book-keeping, and mandatory disclosures) requires companies to dedicate a lot of resources to administrative matters, just to make sure that they comply and do not get into trouble with regulators.

And then there are permits and licences that must be obtained to have the legal authorization to do almost anything. And finally now the Affordable Care Act (Obamacare) creates new and costly medical insurance burdens for some employers.



There can be other reasons. But it is intuitively obvious that if you make it more complicated to start and operate a new business, you will end up having fewer people trying to set one up.

### **America's advantage**

America's true economic advantage used to be in the optimistic dynamism of its people. This used to be the "can do" country. Yes, this used to be the land in which "creative destruction" took place every day.

It takes a certain mind set to challenge the status quo with new technologies, new systems, and new modalities. It is obvious that the new destroys the old, including the companies that run it, and all the jobs they created.

But this is the only way to move ahead. Successful new companies create new sectors and new jobs.

### **Remove barriers**

If all of a sudden we become timid, because trying the new looks too complicated or too risky, as a country we are done. In this new, fiercely competitive global economy, the future belongs to the fearless innovators.

I do not believe that public policy can breed innovators. But for sure policy-makers should not create unnecessary bureaucratic obstacles for anybody who would like to try to be one.

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# The Fourth Of July Is A Reminder To Appreciate The Gift Of Freedom

**WASHINGTON**— Today is the Fourth of July, the anniversary of the Declaration of Independence of 1776 –and America’s most revered public holiday.

## **People are essentially good**

Despite their determination to fight against an unjust King, the Founders of the United States of America, children of the Age of the Enlightenment, “The Age of Light”, were not bellicose people. In fact they shared a fundamentally positive view of human nature.

## **The pursuit of knowledge**

According to them, human beings are naturally predisposed to pursue greater knowledge that will enrich their spirits, and to use their improved understanding of the laws of nature, of physics and mechanics to produce tools and machines that will improve economic processes and the quality of life.

The only real obstacle between people and their overall benign pursuit of knowledge is political oppression perpetrated by a tyrannical government that, by definition, does not acknowledge, let alone abide by, the will of the people.

## **Freedom**

The American Revolution that started with the Declaration of Independence of July 4, 1776, set in motion a process that was supposed to lead to freedom from oppression. After that, the Founders, after some initial hesitation, decided to create a Federal Government whose main objective was supposed to be the protection of liberty, via an unprecedented experiment in

republican self-government.

And liberty, as we have seen above, was viewed as a blissful state in which people could pursue their interests and aspirations within the boundaries of fair laws, but without fear of governmental interference or arbitrary retribution.

### **Knowledge comes because of freedom**

Assuming fairly educated and entrepreneurial people, freedom would be the magic yeast that would lead to the acquisition of new knowledge, more progress and therefore increased prosperity. (It is no accident that Thomas Jefferson and Benjamin Franklin, among the most intellectually gifted individuals of their age, were also the founders of universities).

### **America attracted original thinkers**

If you wonder why America has been and still is a large laboratory and workshop where innovators from all over the world felt and feel at home, the answer is in the optimistic –and ultimately true– assumptions of our Founders. Indeed, ground breaking new ideas are hatched and grow better within a terrain made fertile by freedom.

Other countries that today want to emulate America and become laboratories of innovation, should reflect on America's history. It is not by accident that America became a magnet for people with big new ideas.

They came (and they still come) here because they understood that a free society that protects freedom and private property, including intellectual property, (as in patents, trademarks and copyrights), would be a better place in which to establish their home and their base.

### **Prosperity is the result of freedom**

It sounds so simple. And yet it is profound. The Founders

believed that human beings were mostly good and driven by a healthy desire to pursue new knowledge. This knowledge would broaden their minds and at the same time it would increase societal maturity and wisdom. Some of this new knowledge, once developed into inventions and machines, would improve the quality of life.

As we know, this linear concept of a free and happy society that would move from success to success was a bit too optimistic. Many failures along the way attest to that. Still, all in all, it was and is mostly true.

### **Nurturing freedom**

The Fourth of July is an opportunity to reflect on the value of this incredible gift of freedom. The Founders believed that it was a “natural right”. And yet they also understood that freedom was difficult to obtain, (hence the Revolution), and still quite fragile once acquired. Freedom is precious. It must be protected and nurtured, because it is the essential precondition that makes everything else possible.

Unfortunately, if we take freedom for granted, then we do not value it, and therefore we lose sight of the infinite possibilities that it opens up.

### **How do we use our freedom?**

The Founders knew from experience that freedom was the coveted condition that made life good and enjoyable. And we? What do we think of freedom –today– as we celebrate the revolution that gave it to us? What can we do –today– because we are free?

These are no idle questions. Indeed, unless we modern Americans can give a good answer –an answer that includes optimistic hope and the unleashing of positive energies, as opposed to confusion and self-doubt– then America’s future becomes uncertain and very cloudy.

Let us treasure and put to good use our freedom –our Founders' precious gift.

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## Financial Aid To The Ukraine? Great Idea But Huge Costs

By Paolo von Schirach

March 10, 2014

**WASHINGTON** – A few days ago, I argued [in a related piece](#) that it is hard to believe how Ukraine can be considered by either Russia or the West as a coveted prize in this emerging new version of an East-West confrontation. The country is vast, (almost the size of Texas), and it is home of a fairly large population, (somewhere around 45 million). Other than that, however, Ukraine is a real mess. It is poorly organized, very corrupt and essentially broke. Indeed, just to get things back together, we are talking about [a \\$35 billion bill](#). I assume that includes all the unpaid natural gas bills that Ukraine owes Russia's Gazprom.

### Save the Ukraine?

And yet, notwithstanding this economic train wreck, now the talk is about the (semi-broke) West bravely stepping up to the plate in order to “save” Ukraine. Indeed, if I understand correctly the still hazy plans articulated by US Secretary of State John Kerry and some European policy-makers, we are in for a lot more than just an emergency financial rescue operation.

***We are talking about a long-term commitment to turn the Ukraine around.***

We are talking a major, multi-year assistance package, (including money, tools, technical expertise), aimed at helping the new leaders of the courageous Maidan demonstrators in planning and then implementing major reforms. The goal is nothing less than a reborn Ukraine that would prove to the world (and of course to its Russian neighbors) that a messed up, post-Soviet Republic can become a viable, modern country by adopting best practices when it comes to ensuring basic freedoms via good governance and the adoption of sound economic management. In a nutshell: if we are serious about this, we are talking years and years of sustained work, and tens of billions of dollars.

## **This is going to be expensive**

Turning the Ukraine around is of course a great idea. The problem is that, even assuming good will and not too much negative Russian interference, (you can count on Moscow's attempts at sabotaging pro-Western policies), this is going to be difficult and very, very costly.

Therefore, Western leaders should make this very clear. For instance, I am not sure that US voters, worried about unemployment, stagnant wages and massive student loans debt burdening millions of young workers are that keen on pouring billions of dollars into the Ukraine mess.

## **Let's try**

That said, I do hope that America and Europe, with the support of the IMF and others, will try this. If the Ukraine succeeds, if it becomes like Poland, a former Communist country that successfully embraced Western values, this would strengthen Europe and America. Furthermore, it would show the world that

our model works. Yes, a well-functioning democracy is the foundation for sustainable prosperity.

## **Nation building? Again?**

Look, I realize that here in the US any undertaking that even remotely resembles "*nation building*" evokes the truly bad experiences of Afghanistan and Iraq. And for very good reasons. Lacking judgment and even elementary common sense, the Bush administration and to a lesser extent the Obama administration poured tax payers' money into costly and generally ill-advised development assistance projects aimed at these two countries. The US "Grand Strategy" at the time of the Bush administration was to crush dangerous tyrants and autocrats, have free elections so that the people would finally have a say, and then help the new, democratically elected policy-makers rebuild their countries following the tried and tested Western model. And so, thanks to America, there would be genuine freedoms, market economies, no more corruption, gender equality –and a lot more. Yes, people would vote, children would get immunizations, girls would go to school. A New World.

Nice and noble ideas. But it could not be done. Not because the aims were bad, but because there was a gigantic disconnect between the lofty goals on one side and the relatively small resources allocated, plus the (almost insane) belief that much could be done in a relatively short period of time on the other.

## **It could not be done**

Simply put, you cannot have gigantic social and economic transformations –premised on new values being genuinely embraced by millions– in a matter of a few years. At the time of the US military occupation in 2001, Afghanistan was a semi-destroyed country with almost no viable economic

activities. Thanks to the Taliban, it lived virtually in the Middle Ages. It was disconnected from the rest of world.

The very fact that some people in Washington embraced the notion of a turbo-charged modernization program as a viable proposition is baffling. And that approach, mind you, was developed before the rebirth of the Taliban-led insurgency made everything a lot more difficult.

## **Ukraine is different**

Well, if we fast forward to today's Ukraine with the still fresh memories of the Afghan and Iraqi failures in our minds, the idea of starting all over along the same path looks really unpalatable. And for very good reasons.

The huge difference, though, is that the Ukraine, while in truly bad shape, is a semi-modern country. It has educated people and some of the building blocks to make things work. Therefore we can assume that our chances of success would be a lot higher. And, again, let's keep in mind that helping to build a viable society in a vast country at Europe's immediate periphery in the long-term would help peace and stability in the Continent.

## **Uncertain mission, but worth pursuing**

That said, if America and Europe are serious about this undertaking, we are talking about tens of billions of dollars over a number of years. Beyond the immediate financial crunch, the Ukraine will need investments and help to modernize its industries, its infrastructure, its governance, its education systems, and what not. And, let's not forget that this noble attempt may fail. If the country will not abandon its deeply rooted culture of corruption nothing much can be done.



Still, even keeping in mind the lessons of Afghanistan and Iraq, and the uncertainties embedded in any undertaking of this magnitude, the Ukraine is a far better place. And the stakes for the West are arguably much higher.

Vladimir Putin's dream is to bring major pieces of the old Soviet Union back into the fold. But he has nothing good to offer. Beyond oil and gas, Russia is not a leader in anything. Whereas Europe and America can offer a new path to democracy and prosperity (via investments, technology transfers and trade) to the Ukrainian people.

And ultimately it is in our own self-interest to demonstrate that our values and our systems really work. This is the best lesson that we can offer to all the people who suffer under autocratic regimes, in Russia and elsewhere:

*Democracy is the right choice, and it is really good for you.*

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## Chinese Experts Say That China Needs A Lot More Natural Gas – Not Renewables

By Paolo von Schirach

February 17, 2014

**WASHINGTON** – In the often schizoid US national debate on energy issues the “good and enlightened people”, (those who would like us to stop using carbon based fuels immediately), frequently point out that China is way ahead of America. China, we are told, is investing massively in renewable energy, most notably solar. You see, the real point

is that the wise Chinese technocratic leaders, capable as they are to serenely contemplate “the big picture”, figured out long ago that their vast nation needs to get out of carbon. The conclusion is that the Chinese are wise and smart. We are not.

### **Bad carbon based energy**

Largely because of the evil works of the oil and gas lobby, we keep focusing on the outmoded, wrong formulas –fracking being the latest. Indeed, by developing this (sinister?) source of natural gas contained in shale formations we continue our perverse dependence on carbon, while we pollute our precious water supplies and create untold dislocations across rural America.

### **What is really happening in China**

Well, the real picture is quite different. China’s state TV, CCTV, reports that in order to curb stratospheric levels of pollution, officials in the Hebei Province, (a large area surrounding Beijing and now officially the most polluted province in China), had to resort to the actual closing down or destruction of 8,347 industrial plants producing cement and glass, among other heavy polluters.

An expert from an official research agency, interviewed by CCTV, indicated that reducing horrible levels of smog will be very, very tough.

*For one thing, he stated, if the province wants to move to renewable energy, making anything there is going to be much more expensive. This will be very tough for business, he pointed out. Furthermore, the general public will be hit by higher utility bills. So, there you have it. Renewable energy costs a lot more and makes it harder for industry to stay competitive.*

### **China needs natural gas**

And so, what is the way out? Well, the expert said that China needs to increase its supplies of “natural gas” and “nuclear power”.

*Got that? “Natural gas” and “nuclear power”. Not a word uttered by this presumably enlightened Chinese expert about solar and wind. And why not? Not because they are bad. It is because, to date, they are still too expensive.*

So, here in America our incredible natural gas bonanza is demonized by the “good experts” as more of the same bad stuff, while they invoke the healing power of renewables supposedly pushed forward by the smart Chinese technocrats. But it turns out that in China the experts say that they would love to have access to a lot more natural gas, so that they could reduce their reliance of dirty coal.

### **Renewable energy has a future**

The day of renewable energy no doubt will come. But we are not there yet. The American do gooders should look at China’s environmental disasters and the lack –today– of cost-effective renewable energy solutions. After that, they should look back at America and consider how lucky we are. Thanks to fracking and horizontal drilling –American home-grown technologies– we are now the largest producer of natural gas in the world.

Because of this abundance of domestic, cheap and relatively clean energy we can retire old, high polluting, coal-fired plants without any adverse economic effects.

What do you know: our natural gas is very cheap and it is much cleaner than coal.

And, yes, as a result of this shift from coal to gas for power generation we have cut our greenhouse gases emissions. China is indeed investing heavily in solar energy. But, thanks to a huge number of high polluting coal-fired plants that cannot be shut down, as there is no economically viable alternative,

millions of wise Chinese live in cities that are virtual gas chambers.

Certainly, we in America have a long way to go in our quest for affordable, clean energy; but –thanks to our natural gas revolution– we are much farther along.

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## **The Tea Party Has Become An Ideological, “Anti-Everything” Group – The Republican Party Needs A Strong Message Of Opportunity And Inclusiveness – Chris Christie Could Articulate It**

**By Paolo von Schirach**

November 11, 2013

**WASHINGTON** – At the very beginning, the Tea Party insurgency had some real merit. But now it has become a motley crew of “anti-everything” libertarians mixed with social conservatives profoundly out of step with the minimum standards of modernity. Anti-abortion, anti-gays, prayers in schools, guns for everybody principles will get you some votes; but not enough to win national elections, or even statewide contests as Virginia has shown.

**A good start**

The Tea party Movement had a good start as a grassroots rebellion against ever-growing government and its exploding cost. The Tea Party activists could claim that their advocacy for limited government and low taxes was and is in keeping with basic American principles and traditions. ***“This is America and not France. We believe in the private sector and in a modest safety net for the truly disadvantaged. The rest is unnecessary welfare paid out to voters, so that they will keep re-electing unprincipled politicians who will keep the gravy train going, even though they know full well that this will cause higher debt and eventually fiscal disaster.”***

### **Now the Tea Party is the anti-everything movement**

But now this “small government” platform has become a bad mix of strident politics and ancient conservative values that as a minimum do not resonate with the broader public, while in too many instances (take abortion) they are perceived as deliberately offensive. The worst thing is that the Tea Party adherents seem to be “anti-everything”, while they are unable to rally large constituencies around programs “for something”.

Beyond that, their anti-spending platform is very thin on detail. It is easy to pick examples of stupid, wasteful and poorly conceived public spending. However, the problem is that the bulk of federal spending is about entitlement programs, and not about funding for –say– “artichoke research in Iowa”. The Tea Party people are really disingenuous when they claim that most of America’s fiscal issues are about eliminating the classic mix of “fraud, waste and abuse”. As for a well thought Tea Party entitlement programs reform plan that would take care of the elderly while bending the spending curve, we have not seen any of that.

### **Bad tactics**

And then we have the additional problem of bad tactics. The attempt to repeal Obamacare “by force”, through a government

shutdown is an indication of political stupidity. Most conservatives agreed that it was a bad idea. But the Tea Party people in the House pushed for it anyway, with disastrous political results.

And now, in case we needed more lessons, we have the defeat of Ken Cuccinelli in the Virginia gubernatorial race. While Cuccinelli in the end did much better than expected as he could capitalize on the Obamacare launch debacle, Cuccinelli' lost in large part because his strident socially conservative themes alienated women, minorities and young voters. How on earth can anybody run against women in today's America, as they are now more than 50% of the voters? Only die-hard ideologues want to fight again over abortion, contraception, and then prayers in school, gay rights and more.

Of course, if your goal is to fight for your principles, you have every right to do so. But if these principles constitute the platform of the Republican Party, then it may as well forget about winning major elections.

### **Chris Christie can lead**

And this brings us to Chris Christie. He sailed to a triumphant re-election as Governor of New Jersey. In a sense, he is a new and improved, truly personable Mitt Romney, minus the Mormon faith and the Massachusetts health care reform (too close to Obamacare) issues. In a word, he is a non ideological reformist who promotes pro-growth policies. Christie combines in a nice way a combative spirit, charisma and pragmatism.

***That said, it would help him immensely if his "style" (and this is not to deny that there is real substance in Christie) could be enshrined in a new, principled, easy to understand policy framework that would outline the goal of making America into an "Opportunity and Inclusiveness Society". The Republican Party would gain a great deal by***

*having a convincing national leader convincingly reasserting its credentials as the political force championing a modern Opportunity Society. Not a Welfare Society; but an America in which the private sector and government work together to enable people to become smart and strong, so that many more of them will make it on their own.*

### **Smart, inclusive conservatism**

This is not about hand outs, special subsidies or tax relief. No, this is about a serious effort to modernize public education so that it will provide a real foundation for competing in this globalized economy. This is about simplifying regulations and the tax system, so that it will be easier to start a business and hire people. This is about an energy policy aimed at capitalizing on the huge advantage created by America's low cost natural gas. At the same time, it would be great if the Republicans could articulate a sensible immigration policy reform that would provide a path to legal status for millions of illegal immigrants while making it easy for smart would-be immigrants who bring their talent, energy and entrepreneurial spirit to America.

Christie can do all that, this way leading a GOP revival.

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**China's Leaders Want More Growth – But Innovation**

# Requires Political Freedom

By Paolo von Schirach

October 9, 2013

**WASHINGTON** – Imagine this. Imagine that not so long ago the US was an over populated emerging market with a state controlled economy. A new crop of technocratic leaders decided to use cheap labor willing to come to Detroit, Atlanta and Houston to work in factories as the main national economic advantage. United Technologies, Procter & Gamble, Hanes and other state controlled firms would make a strong push into foreign markets with the considerable advantage of rock bottom prices for US exports made possible by ultra cheap labor provided by migrant farm laborers coming into cities from Idaho, New Mexico and Oklahoma. Imagine that this economic growth strategy had been successfully carried out for 20 or 30 years.

## **End of growth**

But then massive growth would stop. The engine would start slowing down because the products made by the state-owned companies are no so great when it comes to quality, while the cost advantage slowly evaporated. Indeed, the supply of inexpensive migrant laborers dwindled. Fresh labor shortages now translate into higher wages.

The smart technocrats see all this; but they want to find ways to keep high levels of growth. They turn to a very senior economist for advice. He says that the only way to reignite self-sustaining growth is really to privatize state banks and major state controlled firms, this way injecting genuine competition into the system. This will inspire more investments, innovation and therefore quality improvements that will benefit consumers at home and abroad.

## **Growth or political control?**



The political leaders listen attentively; but then they shake their heads. *“Nice ideas –they say– but this cannot be done. If we relinquish control over the economy –all the banks, the big state corporations– then, our main power base is gone. Soon enough, if we empower the private sector, we are gone too”*. And so, the decision is made: no real economic reforms. This way political control is secure. America may stagnate; but the people in power will do fine, at least for many more years.

### **This is about China**

Alright, just put “China” in America’s place, and you have the distillation of China’s policy dilemmas. China is still doing very well, but it is losing altitude. Forget about dizzy double-digit growth. The IMF is forecasting may be 4% in just a few years. An economy built from the top, based on cheap labor to export massive amounts of manufactured products, coupled with huge infrastructure spending has worked very well; but now it has run its course. From now on, expect China to do OK, at best.

### **Can a smart economist solve this problem?**

The WSJ just published a major front page story on this very topic. It featured Liu He, a very senior economic policy advisor in Beijing, (*A bureaucrat Tricky Task: Reignite Chinese Growth*, October 7, 2013). Reportedly Liu has been tasked with producing a new blueprint for China’s growth. It would appear that Liu and his staff would favor reforms and in particular the privatization of the large state-owned banks that control the entire financial system and the flow of credit.

Most Chinese reformers know that, while China has a vibrant private sector, the gigantic system created by state banks and often inefficient state-owned corporations is a major drag on the economy. To any free market capitalist this is no

surprise. Indeed, who would expect monopolistic corporations run by political appointees to be hubs of creativity and innovation? These companies may do well in a controlled, protected environment. But they are not nimble and flexible. They are slow and bureaucratic. And top-down real innovation does not really exist.

### **Economic control equals political control**

However, state and ultimately party control over huge chunks of the economy is almost a prerequisite for the self-perpetuation of China's leadership.

I am not sure how this attempt to find a new formula for China's growth will play out.

But I very much doubt that China's technocrats, even those who would really like to see modernization, are going to take big chances when it comes to giving up control over the economy. A vibrant economy run by an eager private sector creates a middle class that will eventually demand accountability, and a voice in the political process. And this is not something that the political leadership in Beijing wants to encourage, let alone allow.

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**Mexico Will Amend Its  
Constitution, Allowing  
Foreign Companies To Invest**

# In Its Energy Sector

By Paolo von Schirach

August 13, 2013

**WASHINGTON** – If I were Vladimir Putin or Ali al-Naimi, Saudi Minister of Petroleum, I would be really worried about the latest news from Mexico. President Enrique Pena Nieto is pushing forward an amendment to the Mexican Constitution that would eliminate or at least curtail existing barriers to foreign investments in the country's oil and gas sectors. 75 years ago President Lazaro Cardenas nationalized the Mexican oil industry. The sector became a monopoly managed by Pemex, a state-owned corporation.

## **Amending the Mexican Constitution**

But now the Mexican leaders realize that Pemex is very inefficient. Its technologies are not up to date. However, given the constitutional barriers that prevent outside investments, it is almost impossible to find good ways to involve foreign firms in the energy sector. The push to amend the Constitution comes from the knowledge that Mexico has huge untapped resources, both conventional oil and gas as well as unconventional (mostly shale) gas. Mexico's official reserves are 115 bln barrels of oil equivalent, comparable to Kuwait. But the figure could be a lot higher.

## **US energy independence**

It is obvious that with the active participation of major American, European and other energy companies, Mexico could start developing all these reserves. Beyond the economic benefits for Mexico, from a geo-political stand point The United States of America would have the opportunity to get a larger share of its oil imports from Mexico. Combined with increased domestic production and greater reliance on Canadian

oil, the US would reach "***Hemispheric Energy Independence***" even sooner than expected.

And this means no more OPEC oil for America.

### **More gas**

Furthermore, Mexico has the fourth largest shale gas deposits in the world. As soon as this gas becomes available, this would further increase world supply. As America has plenty of its own shale gas, most the Mexican gas will be turned into LNG and exported to energy starved Europe, China and Japan.

### **Russia and OPEC will suffer**

This is why Russia and Saudi Arabia should be worried. Their only valuable resource is likely to become less valuable on account of increased global supply. Look, even in a best case scenario it will take a while for Mexico to amend the Constitution and then enact the legislation and all the necessary regulations that will eventually enable foreign energy companies to participate in the exploitation of its vast energy resources. But this is going to happen, for sure.

### **A new energy map**

As a result, in just a few years the world energy map will look entirely different. North America will become a net exporter of shale gas. Thanks to increased domestic output and more supplies from Canada and Mexico the US will get all the oil it needs from North America. As a result, Washington will no longer be obsessed with the danger of oil supplies disruptions originating in the Middle East. Consequently the responsibility for ensuring the unhindered flow of oil through the Strait of Hormuz will shift from America to China and Japan –the major oil importers that rely on those supplies.

But, more than anything else, Russia and Saudi Arabia, countries that today make money because of high oil prices,

will see their revenue flow go down and their influence diminished.

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# Elon Musk, Tesla Motors' Founder, Came to America Because He Believed That This Country Would Offer Opportunity

By Paolo von Schirach

*Related story:*

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August 12, 2013

**WASHINGTON** – I wrote recently that it is going to be a while before electric vehicle (EV) maker Tesla Motors and others like it will be able to radically transform the US automotive industry. (See link above to related story). Indeed, while Tesla's model S is doing very well, it is on track to sell at most 21,000 vehicles this year. This is obviously very good for a company that sells very expensive, high performance EVs; but it is hardly transformative.

## **The value of new ideas**

Still, having said that, it is really important to reflect on

the incredible value of entrepreneurs like Elon Musk, Tesla's founder. What needs to be stressed here is that Musk is a true, modern trail blazer. Musk ventured into practically virgin territory with what appeared to most analysts a really crazy idea: making a high performance, high price, sporty EV. Remember that many years ago when Musk got started people thought that EVs should be designed for young or middle aged tree-huggers, people focused on saving the planet. Whereas Musk focused on an entirely different market: quality conscious wealthy people interested in a brand new experience: a high performance (and consequently high price) EV.

Well, this is beginning to work. Of course, when it comes to market expansion, much will depend on Tesla's ability to roll out equally interesting but much more affordable electric cars. We shall see.

### **Enterprise is our future**

But this is not the point today. The point today is to celebrate Elon Musk and many others like him. These are the people willing to take huge chances in order to see if they can indeed push the envelope. It is obvious that when it comes to innovation many "Grand Ideas" are destined to fail. But some will not. And the record shows how, failures notwithstanding, many determined entrepreneurs will keep going at it. May be on their second or third try they will come up with something really important.

### **Focus on stagnant sectors**

And we should be grateful for all these efforts. Indeed, it is mostly because of people like Musk that America can keep its position as technology leader. In a recent TV appearance Musk indicated that innovators should really focus on sectors that have been stagnant, sectors that no longer deliver any special value. Real entrepreneurs should really look at ways in which they can introduce disruptive innovation that will cause a

real paradigm shift. He talked for instance about the “Hyperloop”. This is really science fiction stuff. A totally new idea for an ultra fast inter city transportation system that is light years ahead of even the best super fast trains that still rely on tracks and locomotives, however advanced.

The “Hyperloop” is on the drawing boards, and most likely it will not happen any time soon. Still, this is just an example of Musk’s ability to think big and think boldly, even when some of his ideas may invite jokes.

Once again, many “Bold Ideas” that promise huge technological transformation will be failures. Sometimes costly failures. But it does not matter. Hopefully, those who tried and failed will not be discouraged. They will learn from their lessons and try something else.

### **Policy makers have to keep America’s unique pro-business environment**

That said, US policy makers must realize that they need to put in place every possible incentive for innovators. Indeed, for America to keep its coveted position as the world’s premiere “Innovation Hub”, it needs to attract people like Elon Musk who are willing to think big and take big chances. To this end, we need to do our best to reaffirm America’s credentials as the best place for true innovators. Do keep in mind that Tesla’s Elon Musk was born in South Africa. He came to America because he thought that the US would be an ideal home base. If people around the world stop believing this, if we lose this edge, the smart innovators will go somewhere else.