

Greek Profligacy and the Myth of Cost Free Welfare

WASHINGTON – the Greek public sector deficit crisis has attracted inordinate media coverage largely because it broke out all of a sudden. The Greek Government, led by recently elected Socialist Prime Minister George Papandreou, “discovered” that its predecessor conservative Government had cooked the books and lied about estimated public sector deficits. So, as it turned out, the fiscal imbalance in reality is double the initial projection. And this carries the Greek deficit not only beyond the theoretical European strict limit of 3% of GDP; (already broken by others, for that matter), but it brings it to around 12.7% of GDP; that is beyond any sustainable level. This is big news, even though it affects directly only a small country, at the periphery of Europe, with a relatively marginal economy. Of course, the attempt was made to gauge the likelihood of any kind of “domino effect”, whereby a potential Greek bankruptcy might drag the whole Euro zone edifice down.

Greek “contagion”?

Could we have “contagion”, given the considerable lending by many European banks to Greece? But, outstanding European loans to Greece notwithstanding, the idea that tiny Greece would bring down the whole of Europe was really farfetched. Unless, of course, other Greek-style surprises of heretofore hidden losses might spring up elsewhere. To date at least, this seems unlikely. While we know that there are other problem countries affected by huge fiscal imbalances, there is no forecast of an impending Europe wide unraveling.

Europe holding on

Greece is not that important an economic player to cause the

downfall of Germany and France. The Greek budget crisis is a big problem, indeed, but not a European catastrophe. The Greeks have been told, (or better, "ordered") by their EU partners that there will be no bailout. They must take the necessary, if politically bitter, countermeasures in terms of drastic spending cuts and this should be enough to avert bankruptcy. The Euro as the common currency shared by Greece and 15 other EU member states is not in any imminent danger.

So, case closed?

More than just debt

Well, not entirely. Greece represents an extreme example of total fiscal irresponsibility, cleverly disguised for a while and certainly driven by the politics of the welfare state. And in Greece this free spending style was nicely blended with endemic corruption, extravagant levels of tax evasion and an otherwise mediocre economic performance. But Greece is a member of the European Union. And so this debacle becomes a problem for all the other members of the EU, as it blemishes the image of Europe as a Union of modern countries. No other member of the club wants to have, within Europe, this kind of Banana Republic governance model. And I am sure that this concern has been clearly conveyed to Prime Minister George Papandreou by his European counterparts.

A larger lesson about the consequences of public largesse

But, bad image aside, even if we limit ourselves to the issue of fiscal profligacy, the Greek example indicates that at least some Western Governments are prepared to take huge risks, behaving at times most irresponsibly, in order to placate constituencies who believe that the purpose of Government is "to give" more and more; constituencies who put pressure on elected leaders so that they will deliver more and more. Greece has become a sensational story because of the extreme overspending and the sudden revelations. And again,

beyond the surprise, there has been the unpleasant task of selling to the public this unprecedented austerity program.

The “free lunch” pipedream is still alive

This has not gone down well; and we have seen the vociferous and at times violent street demonstrations, and the emotional reactions of those who would like to cling to the dream that there really is a free lunch; that you can do both: overspend without limits and keep giving extra this and that to all kinds of constituencies, without ever paying the bill. And so now, along with the headlines about the drastic spending cuts, we have the photos of riot police battling demonstrators who would like to believe that somehow there must be a better, less painful alternative for them.

Did anybody learn anything?

In the end, in the case of Greece, it seems that the general public, beyond the current moment of hyperventilation, will have to surrender to the hard facts, unless they want to force the Papandreou Government to exit the Euro and may be the whole EU structure –and this seems highly unlikely. So, reluctantly and despondently the Greeks will fall back in line. If they follow the plan, they will cut spending and eventually rebalance their public accounts.

But I doubt that the larger lesson as to what provoked the crisis –the insane, yet widespread hope that in a modern western society you can indeed get something for nothing– will be properly understood. And, as this fallacy about magically obtainable unlimited entitlements, while someone else (who?) eventually will pay the bill, is not fully understood in Greece, it is probably lost in all the other countries in which, large deficits notwithstanding, (Belgium, Spain, Italy, Portugal, the United Kingdom), there is, for now at least, a semblance of normalcy.

A stable currency does not give you growth

And here is the real problem, a problem that goes way beyond the understandable desire to protect the Euro, potentially weakened by irresponsible fiscal policies, as a credible currency. A stable currency is a good thing. And it is good that the European Central Bank will continue to act as a good steward of the Euro's reliability. But a stable currency, while essential, is no guarantee of underlying dynamic societies and economies. The Greeks will have to swallow the bitter pill. So, they will eventually rebalance the accounts, (we hope). But, at the same time, even staying within the Euro zone, they will have less money and their standard of living will be lowered. Unless the general public will learn the simple lesson that higher standards of living are not grounded on public largesse but on individual and corporate enterprise, the real lesson will stay hidden. The Greeks may become more sober; but the people, unless they are ready to embrace the basic tenets of private sector-led growth, will be both poorer and more disgruntled.

Welfare state yes, but who pays for it?

More broadly, Greek-style extremes aside, not many in the West are getting the message of what it takes to grow. In our ongoing love affair with the notion of a public sector that will provide more and more things: subsidized public sector jobs, free grants to this and that, tax shelters, lavish pensions, health care, free education and what not, we have forgotten that none of these things in the end grow the economy, while in the end someone has to pay the bill.

If it is politically unpleasant to make anyone pay the bill, then the cost of the unpaid fun will pile up and Government will need to finance its largesse through borrowing. And when more and more borrowing becomes not just a temporary expedient for extreme situations, but a routine way to finance ever increasing public spending, this entails a shift in basic Government functions: from focusing on public administration issues to spending more time and energy in the identification

of ways to finance more spending. In the end, financing the debt –not governing– becomes a top Government priority.

If you have larger deficits, you have less economic growth

Furhermore, even in situations in which there is a huge or growing debt but this debt can still be financed (Spain, Portugal, Belgium, Italy, and Japan, among others), this comes at a high cost. While the State may be able to continue to meet its obligations towards bond holders, interest due on the outstanding debt starts eating into a larger and larger share of existing revenue. And so the State can no longer perform basic functions such as investing in R&D, infrastructure development, defense or even education. Indeed, once interest on the debt is paid out, there is the regular operating budget just to keep day to day Government activities going; and so there is very little left for any discretionary spending. The Government can perform, at best, routine operations; but it has no resources and thus no flexibility to lead, in domestic as well as international policies.

Less capital for investments

In the meantime, a larger share of national savings will be directed to financing the debt. This means less and probably more expensive residual capital available for productive investments. In the end, the State and its profligacy, due to the desire of the political leadership to satisfy the desires of more and more constituencies, becomes an objective drag on new growth. Large, (or excessive, depending on your point of view), public expenditures –and the attendant need to finance the deficit– absorb more and more limited capital that cannot be used otherwise.

Europe has chosen welfare over growth

This state of affairs is endemic in Europe. Even though most European countries have not reached the insanity of Greece, on average, the public sector absorbs a very large percentage of

GDP, 40% or more. In general, high spending entails higher taxes. But, even with high taxation, there is still a need to borrow heavily to finance the rest. ***While these societies seem to manage somehow, the real, if hidden, cost of this setup is in a myriad of missed opportunities for new growth, as funds that could otherwise be invested have to be employed to finance entitlements and other transfer payments.***

Indeed, as the primary focus of Government is the provision of services to a variety of deserving constituencies, the pool of residual public sector capital available for productive investments shrinks. Besides, high levels of taxation, (necessary to finance increased spending), along with rigid labor laws, may also contribute to discouraging new enterprises. So, in the end, there is a lot more involved here than finding a way to balance the books, trying to reconcile a high level of spending with the need to find revenue and/or resort to more borrowing.

If we choose to devote resources to service delivery, we have to understand the implications

In the end the real issue on the table is a philosophy of Government and the shaping of a societal consensus whereby the essence of public policy is to provide services and to alleviate hardships, as opposed to the creation and the nurturing of an enabling environment conducive to the expansion of the economy.

Nothing wrong, in principle with espousing this approach focusing on making today's life more comfortable, as opposed to devoting more resources to future growth.

More entitlements, less growth

But, if this is indeed the choice, it should be first of all clearly articulated, (as opposed to being incrementally implemented), and fully understood by all citizens in all its immediate and long term implications. If our goal is to live

today as comfortably as possible, almost like retirees, then we do indeed create public policies geared towards the delivery of services and the growth of entitlements at the expense of investment and growth. ***But it should be clear to all that, unless we become extravagantly rich due to fantastic levels of high value innovation and strong productivity growth, we cannot at the same time spend most of what we have today and have enough left for new investments.*** Maybe Norway can do it, as it has a very small, educated population and the extra bonus of significant revenue coming from oil and gas exports. But there are not many such examples.

What about the US?

And what about the US? Well, we are in an interesting, yet delicate, position right now. By European standards, we still have a miserly state that provides comparatively little in terms of services and entitlements. (Our combined total public outlays: Federal, State and Local amount to roughly 33% of GDP). But, quite apart from the recent extraordinary recession that caused an explosion of public spending to fund huge emergency countermeasures, we know that, unless we change our basic system rather drastically and soon, we are geared towards a dramatic increase of public spending. The cause is in systemic demographic changes (more elderly Americans receiving public moneys) and the after inflation cost explosion of services such as medical care for the elderly.

Which way is America headed?

And here is our problem. Are we going in the direction chosen by Europe, or are we going to revert to a model of a Government that spends less on the provision of services, thus freeing up more resources that will be hopefully directed to the expansion of the pie and thus more prosperity? Long term, quite apart from how soon the current recession and related spending will end, this is the real strategic choice before us.

Former Massachusetts Governor Mitt Romney, warming up for a likely new bid for the Republican nomination for White House, argues in a new book, (“No Apology: The Case for American Greatness”), that we should be repairing our system so that it can be once more geared towards investing in new growth, while providing a modicum of a safety net, via the delivery of social services and some entitlements.

Fine.

Balancing growth and the expansion of opportunity

Yet, even if one agrees philosophically with the limited government model repropounded by Romney, the really complicated issue is to determine the proper balance between being pro-growth and the need to provide to the disadvantaged in a way that will really help them transform their lives, by granting them real solid options –such as good education–that will increase their opportunities. How much and what do you provide? And in what way do you provide effectively? A mountain of historic evidence shows that providing “more”, while nice, does not necessarily help to solve problems.

It is once again the old and worn story: “Give a fish to the hungry everyday, or invest resources teaching them how to fish, so that they will catch their own fish and become self-sufficient”? it is a shop worn, tired little example, and yet its wisdom still escapes us. Try as we may, we are still struggling with this. If we are at all reasonable, we should want to push for growth. But our sense of social cohesion and human decency also tells us that deep down we do not really believe in social Darwinism, whereby the fittest survive and for all the others, well... tough luck. They are lost along the trail because they could not make it.

Understanding the difference between social spending and social investments

The European story tells us about the penalties paid in terms

of missed growth, plus huge debt overhang, via an excessive tilt towards equality and public interventions in the shape of hardship alleviation. Can we, as would be President Mitt Romney suggests, be decisively pro-growth, yet mindful of the need to have everybody on board, by providing to all the tools necessary to advance –first and foremost via a truly vibrant, modern, comprehensive education system? Can we invest in this kind of “fishing” education for those who will otherwise depend on future handouts? And are we willing, as a society, to recognize the qualitative distinction (and choose wisely) between investing in the future (education) and relief payments (welfare, unemployment checks, and so on)?

Our future is not going to be Greek-like. But it could be closer to Italy or Japan: low levels of investment, stagnation and slow decline. Less dramatic; but equally unappealing.

Europe Becoming Truly “Old”

[Fertility] rates below two children indicate populations decreasing in size and growing older. Global fertility rates are in general decline and this trend is most pronounced in industrialized countries, especially Western Europe, where populations are projected to decline dramatically over the next 50 years.

–CIA World FactBook

WASHINGTON – Indeed, Europe is already experiencing a “dramatic” fertility decline. Most European countries are below “replacement level”. Unless this trend will be reversed, overtime this will translate into smaller and older populations, with all the attendant economic, political and indeed psychological consequences associated with the

prevalence of the elderly at every level of society. Societies in which old people are more numerous or prevalent tend to be less future oriented, less entrepreneurial, more risk averse. They stop growing. They become anemic, rationalizing their lack of action through some mix of political ideologies claiming the superior wisdom of a "less is more" approach to almost anything.

United Europe a strong presence in the world?

Given these pronounced demographic trends, all those who look at the enlarged European Union as a new dynamic political and economic entity, now flexing its muscles and getting ready to play a wider role in the international political system should curb their enthusiasm to a more prudent level. Most likely fewer and comparatively older Europeans will translate into a stronger aspiration for a quiet, problem free life. In international politics this will mean doing less, not more; a tendency towards minimizing problems and accommodation –even with hostile forces.

The cost of old people

On the domestic economic front, the prevalence of older people within the general population in the context of developed welfare states in which the social contract stipulates that the elderly will be taken care of means a progressive, but ultimately gigantic shift of resources from production to consumption. And this systemic trend that subtracts capital from new ventures devoting it to increased welfare spending is bound to have negative consequences on the dynamism and flexibility of these societies.

Given these demographic trends, since the public treasury cannot drain from a diminished tax base all that ideally would be required to provide adequately for both the elderly and all the other governmental activities, including research and development and new investments, overtime this will lead to

stagnation and ultimately decline.

Below population replacement level

Most of Europe is now characterized by birth rates below "replacement level". Which is to say that, unless this trend is reversed and/or other factors, such as significant new, reasonably skilled and educated immigration, will intervene, in the long run these societies will be composed mostly of old people and eventually, whatever the time frame, they will become less and relevant and maybe they will disappear altogether, at least in the form in which we have known them.

Let's look at the numbers. In Europe, France is on the edge. Its rate of 1.98 children per woman places it just a little below replacement level. But the rest of the Continent is mostly way below replacement level. Norway: 1.78; Finland: 1.73; United Kingdom: 1.66; Portugal: 1.49; Croatia: 1.43; Germany, 1.41; Greece: 1.37; Italy, 1.31; and so on.

In the US the picture is somewhat better

The US is not doing great in this regard, but it is above water with a fertility rate at 2.05 which places the country a little bit above replacement level. This fertility rate means that there is still a reasonable supply of young Americans capable and willing to start something new and to maintain a reasonably broad tax base that will be able to support the government.

Still, even here in the US we see the consequences of relatively fewer births and an increased percentage of seniors within the overall population. Based on our own experience, we do understand the political and policy pitfalls created by a large population progressively growing older.

Cost of old age in America

On balance, even in America, a country in which the welfare

state is not particularly developed, (at least compared to Europe), the sheer mass of increasing numbers of older people already caused a significant resource shift from investment to consumption, given the promise to take care of seniors through the public purse, be it via Social Security payments or Medicare support when they get sick; keeping in mind that improved longevity means an increase in the demand for medical services, given the ailments and infirmities usually associated with old age. In the aggregate, more capital spent to satisfy the needs of the elderly directly translates into smaller funds available for education, infrastructure, investment in research and new economic activities. In the US we already know that, unless the entitlement programs will be significantly reduced, at the current level of growth they will bankrupt the Federal Government.

And this is happening in America, a country in which the fall in overall fertility is far less pronounced than in Europe and a country in which the state gives comparatively less to senior citizens. In Europe the trend of falling demographics is much more pronounced, while the welfare state promises more to its seniors.

The impact of a shrinking, aging population

Which is to say that, whatever we may be experiencing in the US concerning the increased financial burden of entitlement programs, in Europe the consequences of an aging population are much more pronounced in terms of size, speed, economic and eventually political impact. It is almost inevitable that, without counterbalancing forces, such as a significant influx of young and productive immigrants, societies characterized by low fertility rates will become progressively less dynamic, more risk averse and more concerned with satisfying the immediate demands of the elderly who have acquired the right to get a variety of services; while fewer and fewer active citizens produce the wealth necessary to provide them.

So, oddly enough, higher prosperity, at least in these countries, brought along the lack of desire to have children and thus the inevitable aging of the population. As a consequence, there is a shifting of resources from production to consumption and thus diminished economic vitality.

Children and confidence in the future

Now, I would dare say that there is a correlation between this phenomenon of falling fertility rates and the less empirically verifiable, yet still observable phenomenon of the rise of a risk averse culture of little entrepreneurial daring and more accommodation, including with enemies; all this rationalized and justified under pious ideas of social tolerance, justice, human rights, international dialogue, cooperation with all, and the like.

Is it possible to say that societies in which people decide to have few children or no children at all are more inward looking and less optimistic? Can we say that the desire to have children is a vote of confidence in the future? Who knows for sure. But it is a fact that we are witnessing the emergence of this new undeclared cultural consensus in Europe amounting to doing less for the future, while doing more for the every day necessities of an aging population that needs more.

Mitigating factors?

What about other factors that may mitigate or reverse this trend leading to a population that is on average getting older, while shrinking in overall size? Europe, as far as counter tendencies are concerned, there is not much comfort in what we can observe. Indeed, there is fresh new immigration into Europe –and this would alleviate the shrinking problem. However, the bulk of the new immigration comes from Africa and the Islamic world; that is from societies whose members have

quite often difficulties or no will at all to be assimilated into the mainstream of European society and culture. On the contrary, the new immigrants tend to create their own separate communities, veritable ethnic and cultural islands within an environment that may be either hostile or at least not very accommodating towards the newcomers. Immigrants usually have higher fertility rates. So, to the extent that there may be any segments of European societies experiencing population growth, this growth takes place largely among not very well assimilated and/or not especially welcome immigrants. And so, while the "native" European stock shrinks, Europe is being transformed by the unassimilated newcomers, in some regions already beyond recognition.

Transformation may be good or bad, depending on one's own opinions and on what is it that we are measuring. If we measure academic achievement, a key precursor of future economic productivity, of the rate of innovation and ultimately of future growth, we see that increasing numbers of less literate young immigrants are not improving the broader picture in terms of academic standards and skills. In the long run, for societies to stay prosperous they need to be competitive and this can only happen via the nurturing of human capital. If the indigenous working age Europeans are producing less because the active population pool is shrinking, while the younger immigrants are comparatively less skilled, we have strong indicators of progressive economic decline.

America and "Old Europe"

So, the "Old Continent" is living up to the metaphor, with a twist: not just old countries and old societies. Europe is truly "becoming old" in every respect; and the foreseeable consequences of this pronounced trend are not that bright. In all this, let us bear in mind that this is going to be a long, incremental process. The impact of lower fertility, assuming that it will not be reversed, is not immediate. It will take a

long time for Europe to be totally transformed. But, if current trends continue, the combination of an aging population and of the continuing influx of problematic immigrants who cannot be easily assimilated tells us that our European Allies will be more inward looking. Thus they will be less interested in broader international issues that may not have an immediate impact on their welfare.

After WWII, we forged a US foreign policy predicated on the concept of a strengthened Atlantic Community, based on the two “pillars”: North America and Western Europe. After the fall of communism and the reunification of Germany, it seemed as if this Atlantic Community, having “won” the Cold War, would be dominant in world affairs. The demographic trends in Europe indicate that the European “pillar” of this Community is becoming weaker and thus over time less relevant. Time for the US to seek productive partnerships with more dynamic societies.

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NATO At 60: Not Much Reason for Celebration

WASHINGTON – Quite a long time ago, while in London, I happened to walk in St. James’s Park at a time of some kind of

Veterans celebration. There were hundreds of old men, marching in perfect order, medals tinkling on many chests. There was a military band. And they were all led by a soldier carrying a flag. And on the flag one could read: "Burma Star". The whole thing was solemn and quite beautiful. And yet it was also sad and in many ways incongruous. They were remembering past service in Burma, (officially renamed Myanmar in 1989), a remote part of the world. Indeed so remote to be disconnected from the issues of the day. "Burma Star"? In the middle of London? Sure, the British have maintained a keen interest in matters pertaining to their Old Empire. But not much in remote, secluded, autocratic Burma. A country where Britain has not much clout or influence of any kind. And so I looked at the marching old men, with their medals, their band and their beautiful flag, thinking with some sadness about past glories that lost their relevance with the end of the Empire.

Well, the comparison may appear a bit stretched; but, soon enough, on April 4, the North Atlantic Treaty Organization, NATO, will celebrate its own sixtieth anniversary. Unlike the celebration featuring the British Veterans, this is about both the past and the present. NATO is the premier security institution binding Europe, the US and Canada and, as such, supposedly a key pillar of international order and stability. This celebration should not be just about past history but about the present and the future. It should be about renewed vows about existing commitments premised on shared values; and, as it happens, ongoing missions –Afghanistan being the most obvious. And NATO is arguably quite alive. In fact, in recent years it has expanded its membership welcoming many former Warsaw Pact countries and the Baltic states, among others.

But, If so, what is the similarity between the melancholy echo of a dead Empire and NATO' sixtieth? Very simple. The British Empire is gone. And equally gone is much of the spirit that supposedly was behind the creation of this Atlantic Alliance

–the spirit that made it meaningful for many years. Today NATO may be technically alive; but it is not very meaningful in as much as the institution does not embody shared values, shared interests and –most importantly– a shared agreement on the resources to be dedicated by all members to the effort of protecting them against threats that may not be as self-evident as the Soviet Army Divisions that used to be stationed in then East Germany. So, we have a military alliance with fewer resources and a certain ambiguity about its meaning and mission. Not exactly a revved up champion, ready to move.

Without an immediate, direct challenge that would test the cohesion of the members, this objective confusion does not constitute a threat to the continuing existence of NATO. We do have a NATO today and, for all I know, we shall continue to have a NATO for quite a while. And all members would claim that NATO is very useful; that it provides a proven and tried institutional forum for a transatlantic dialogue on security matters; that it has created channels of communication with Eastern Europe, with Russia and beyond, etc. Fine.

However, the problem is lack of substance. Unless all the members agree on what a real threat is and unless they follow up with real, tangible resources devoted to meeting it, NATO will be a place for meetings and discussions, possibly of some use, but not very relevant. And it should be quite clear that the reason why resources are not allocated to NATO is because it is not at all self-evident to many if not most members –absent and immediate, clear threat– that a strong and credible NATO, capable of projecting credible force, is truly the essential basis for their security.

The problem is that there is a basic equivocation about the motives that supposedly provide the underpinnings of the Alliance –an equivocation that goes back to the very beginning of NATO. Reading the Preamble to what was known at the time as “The Treaty of Washington” that established NATO on April 4,

1949, one would get the idea that NATO was all about getting together to preserve shared values:

"The Parties to this Treaty..... are determined to safeguard the freedom, common heritage and civilisation of their peoples, founded on the principles of democracy, individual liberty and the rule of law. They seek to promote stability and well-being in the North Atlantic area. They are resolved to unite their efforts for collective defence and for the preservation of peace and security. They therefore agree to this North Atlantic Treaty"

But, while the values referred to in the Preamble at the time were in some measure truly shared, the real reason justifying the birth of this unprecedented Alliance linking Europe and North America was to create a credible deterrent against Soviet ambitions in Europe by ensuring that the United States of America would intervene in case of an attack against Western Europe. And NATO, with all its flaws, by creating some kind of a united Western Front, supported and led by an integrated military command, did its job. So, while values were important, the real deal was a shared fear of the Red Army.

Well, we know what happened regarding the Soviet threat. So, as of the 1990s, the geopolitical reality in Europe having been dramatically altered –and entirely in our favor– via the dissolution of the old Soviet Union and of the old Warsaw Pact, was there a residual mission for NATO? And, if so, what would it be?

Quite frankly, a serious discussion about any relevant new post Cold War mission should have been premised by a check on the validity of the Preamble to the NATO Treaty quoted above. Absent an immediate threat, did the western democracies still feel the need to be tied together by a military alliance in order to safeguard their common civilizations? And again, what could be the future threats against which NATO should prepare

itself? Admittedly, not very easy to make commitments about vague, below the horizon stuff that may not look the same to all members.

But, while probably quite useful as a way to ascertain continued relevance for an institution created to face a clear menace that no longer existed, this exercise was avoided. No one intended to seriously verify to what extent there really was any spiritual glue left holding together Europe and North America and whether or not this assumed kinship would make both sides devote real resources (and this means budgetary allocations for state of the art military assets) to preserve peace and stability, in a future post Cold War environment *—an environment in which threats would not be necessarily existential, imminent or self-evident to all.*

So, the “stress test” (to borrow from an expression coined by the Obama administration in reference to a needed check on the health of financial institutions) was not applied to NATO. There being no immediate crisis, it was assumed that all was well, to pretend that we all agreed on the fundamentals; and that, while the Soviet Union had graciously removed itself from the horizon, we should keep working together for the preservation of our shared values through our commitment to this regional security institution. Fine. And how did it go?

Fast forward to Afghanistan. This is admittedly a complicated and in many ways botched affair, largely because of poor American leadership. After the initial success in the quick campaign of 2001 resulting in the removal of the Taliban, the US was distracted by new business. As of 2002, the US thought that Iraq presented a greater strategic challenge.

Focusing on Iraq, and the actual war that began in March 2003, America thought that it could safely “subcontract” Afghanistan to NATO and other assorted non NATO do-gooders. The idea was that the Taliban had been routed; thus, going forward, Afghanistan was all about governance, development and the

training of policemen. Well, the Europeans under the NATO umbrella could take the lead on that. And so they did.

Except that they really did not. Living up to the sarcastic characterization of NATO as "No Action, Talk Only", the Alliance proceeded to create initiatives not backed by resources. Some countries, such as Britain, Canada, the Netherlands, have done a lot; in varying degrees France, Germany, Poland and Italy have done something. All the others just showed up, with literally token this or that: some sent 20 soldiers, others 100 or so. And this may have been fine when things were relatively calm. But we know that the situation has unfortunately deteriorated –and quite significantly in the last few years. We know about a resurgent Taliban. We know about the sanctuary offered to them in lawless North West Pakistan.

This marked deterioration produced a needed reassessment of the effort required to stabilize Afghanistan. And the reassessment is premised on the notion that a safe haven for radicals in the mountains of Afghanistan and Pakistan is dangerous, not just because it may destabilize both countries, but for the security and stability of the region; while the harboring of radicals there may create future dangers for the security of Western Countries –and that would be the NATO countries, front and center.

This analysis has been done. And there is no serious disagreement about the diagnosis. The military commanders on the ground estimate that there is a need for at least 30,000 additional troops to have a chance to stabilize the situation, itself an essential precondition to build more solid national institutions and hopefully economic development. Washington has admitted that mistakes were made and that allowing Afghanistan to fester in large measure contributed to the regrouping of the Taliban and their assorted allies.

While further analysis and a more detailed plan will follow,

Secretary of Defense Robert Gates, under the direction of President Barak Obama, already ordered 17,000 additional US troops to be deployed to Afghanistan. So, there will be more US resources and a deeper engagement in the complicated effort of building a viable economy in Afghanistan. In all this, this continues to be a NATO mission. And what have we heard from the Allies in terms of additional contributions? Well, not much. At least not much in terms of concrete fresh commitments to the operation. And this means that the US urgency about Afghanistan is not shared among all the Allies.

And here is the problem I mentioned at the opening. NATO was and is supposedly based on common values and a shared world view which would include a shared understanding of what constitutes a major threat. This does not entail unanimity; nor should it imply America issuing commands and Europe obeying. But the approaches to this supposedly critical military engagement in Asia are remarkably different.

So different to be almost funny.

For example, to get a flavor of what is going on, one can go and check the website of NATO. Read all the headlines and one could not find the word "war". Even the prominent announcement of a high level visit to Afghanistan by NATO officials fails to mention that this is where the Alliance is engaged in its most significant military operation. A distracted reader could think that this is part of some kind of diplomatic tour. One should read more than half into a speech delivered just a few days ago in Poland by NATO's Secretary General Jaap de Hooft to find the word "Afghanistan". And, when mentioned, it is not referred to as a major issue; but as one of the things on the table, routine stuff. None of this indicates that there is a shared perception about urgency regarding this NATO military operation.

So, rightly or wrongly, here in Washington we are discussing Afghanistan as a worrisome geopolitical threat because of all

the implications for regional security, stability in Pakistan and the need to avoid the recreation of another breeding ground for radical Islam in a country controlled by guerillas. In the US these are considered major, or at least, significant issues. Allowing Afghanistan to fester and to become chaos is deemed to be dangerous for world security and against the interest of the United States.

And the European Allies? What do they think? Well, we do not know exactly, but there is no major new action announced or planned. While the Obama administration recently announced this significant scaling up of American troops to be deployed to Afghanistan, the rest of NATO meager contribution to the common effort will not be significantly augmented. And this is the primary indicator of how strongly the Europeans feel threatened by that caldron of instability. Which is to say that, if the US wants to achieve some results in Afghanistan, it has to rely mostly on its own efforts and essentially forget about meaningful "burden sharing" with the European Allies. Yet, if this is so, if we disagree about the seriousness of this threat, it would make sense to have at some point a frank discussion about what is the real function of NATO.

But this is unlikely. Indeed, serious differences about Afghanistan notwithstanding, in a few days there will be celebrations for NATO's sixtieth. They will be held in Baden-Baden and Kehl in Germany and in Strasbourg, in France. Chancellor Angela Merkel of Germany and President Nikolas Sarkozy of France, the heads of government of the European countries once enemies, now friends, will co-host the events. And there will be speeches and self congratulatory remarks about this long era of peace in Europe made possible, among other factors, by this resilient NATO Alliance.

And, after a few days, the whole thing will be forgotten. This Alliance, lacking a real shared purpose, sadly, has become almost irrelevant; just like the old Veterans of the Burma

Star. They were marching in London behind a flag that today, except as a revered relic of a glorious past, means absolutely nothing.

America: Global Ambitions and No Cash

WASHINGTON – Almost lost within the avalanche of news about more and more rescues: the banks, the auto sector, homeowners, and...welll... everybody else, (followed ominously by deeper and deeper Wall Street dives), was the announcement that the Obama administration has decided to send additional US troops to Afghanistan: 17,000 to be exact. Now, this falls short of the 30,000 additional troops requested by military commanders on the ground; but it is a nice installment. And it should not come as surprise, as Obama repeatedly indicated during the campaign that Afghanistan was and is the place we should focus on; while stating that the Bush administration had squandered resources in the misguided Iraq campaign.

The commander of the Afghanistan NATO force, US General David McKiernan, indicated that these reinforcements are welcome and badly needed, in the light of the precarious and, in fact deteriorating, security environment. And so it goes. The US has already 38,000 troops in Afghanistan. Now the additional 17,000 and probably more to come, depending in part on the draw down timetable from Iraq where we have about 140,000 troops.

And how is the rest of NATO, (that is wealthy Europe), plus assorted non NATO friends, doing in terms of deployments in Afghanistan? Not so great, in terms of numbers. The total non

US force in Afghanistan comes to about 19,000, coming from 42 countries. While this is unfair, as some countries (UK, Canada, the Netherlands, France) contribute a lot more than others, let's average this grand total. So: 19,000 divided by 42. Well, it comes to 452 soldiers per ally. Again this is not a correct representation of country by country contributions. Some allies have sent dozens, others thousands. Still the overall disproportion is immense. Soon the US shall have almost 70,000 soldiers; while the others –42 countries– do very little for a mission deemed to be important by all. Let us note that, while all countries are experiencing significant financial constraints, the Afghanistan deployments disproportion goes back quite a while. It is a matter of political will, rather than resources constraints. (No matter how messy Afghanistan is today, let's imagine for a moment the consequences of a US decision to scale down its military commitments to the average of all the other countries who have contributed forces. Would this be a good thing for regional and global stability? More on this later).

So, we have significant new US commitments for the “good war” in Afghanistan. Still, while here in Washington we are contemplating a budget deficit that is approaching banana republic levels because of stimulus spending and assorted bail outs, how are we planning to pay for these new military deployments?

Let's move to another scenario. On January 10, 2009 there was the solemn and in many ways moving commissioning of the “George Herbert Walker Bush”, or CVN 77, the last Nimitz class aircraft carrier named after “Bush 41”, that is the first president Bush, father of president George W. Bush. The outgoing president “Bush 43”, his son, presided over the ceremony honoring his father just a few days before leaving office. So, the expensive “George Herbert Walker Bush” starts sailing the oceans in the year of the “Great Crisis”. This 78,000 tons nuclear powered ship, built

by Northrop Grumman, with all its airplanes and helicopters and its complement of cruisers, frigates and all the rest that make up a carrier group, is the finest product of US technology, while embodying US power. Indeed, as Secretary of the Navy Donald Winter said during the ceremony: *"The impact of a new carrier is global. For no other ship represents to the world the power of the United States the way this does...."* Indeed...

So, add another few billion dollars to the defense procurement bill (although stretched over a number of construction years) and, of course, from now on, the few hundreds of millions for the annual operating cost of this sailing airbase and the other vessels accompanying it, with thousands of airmen and sailors on them.

And now, the same scenario, from a different angle. Answering a reporter question on February 13, 2009, regarding the chances of buying large numbers of the (very pricey) F-22 Raptor, the new generation fighter jet, Pentagon spokesman Geoff Morrell gave us a hint that the Defense Department is aware of the fact that money is becoming scarce and tough choices are ahead. Maybe we cannot have all the weapon systems that we want:...."*....Fundamentally –Morrell said–, the Secretary [Secretary of Defense Robert Gates] is looking at the things I laid out for you, I mean, the notion that we need to make hard choices in this economic climate, we need to [...] look for cost efficiencies and we need to be more joint in how we acquire...."*

So, is there a common thread in any of this? Not easy to discern one, really. The first two examples –more troops in Afghanistan, the commissioning of a brand new carrier– would indicate that America has money. The prudent reply of the Pentagon spokesman regarding future procurement of major weapon systems would indicate that, because of the fiscal crisis, there will be painful procurement cuts.

Well, and so, what does it mean? It means that, unless we reestablish fairly quickly our economic strength, at some point trillion dollar plus deficits and a country in a deep recession will collide with global foreign policy ambitions, a huge defense budget and the desire to send around a world a powerful symbol of US might. Unless Obama is successful in leading America in an effort that will fix this mess, sooner rather than later we shall get to the point in which the superpower status and international role played by the US will be undercut by lack of money.

Ordinarily, (that is excluding for a moment all the extraordinary federal spending just launched and its impact on federal finances and on the national debt), the Pentagon is used to taking a huge chunk of all discretionary federal spending, that is all the spending that is not committed to transfer payments such as Social Security, Medicare, etc. But, given this deep crisis of uncertain duration, how long can this last? The answer is not so simple. Allocations for national security are a combination of available cash and the setting of policy priorities. If a country has money it can decide to have or not have significant military spending. But if a country has fewer and fewer resources then the policy choices become more limited. As the French say: "*C'est l'argent qui fait la guerre*", "It is money that makes war". And this is not to recommend war. It is simply to recognize that without money to fund a modern military that is supposed to be large enough to constitute a credible deterrent and to be effective as a policy tool when it is so decided, the US cannot continue to be a superpower.

Military spending, however misdirected and often misused, is a large component of US credibility as a world leader. Without military power or with very diminished power, who will listen to America? Well, the proponents of "*soft power*" would argue that there are other, indeed better, ways to influence international affairs through trade, dialogue and diplomacy. I

am not so sure. The governments of the countries that send a few hundred troops or less to Afghanistan do not seriously expect to influence policy. The European Union has no military power to speak of and thus nobody pays any real attention to its proclamations.

One school of thought about the roots of "decline" focuses on "Imperial Overstretch". A great power, keen on preserving its strategic global interests, starts spending too much on national defense at the expense of other productive investments. In the end, because of this underinvestment, its basic economic strength is sapped and –paradoxically– there is less capital to be allocated to defense spending. Hence the need to retreat and the loss of global status.

Well, in the case of the US it could be argued that a few years of expensive wars in Iraq and Afghanistan have absorbed much national wealth. This is true. But, while the cost of these wars is significant, it is clear that the current serious recession is not due primarily to the cost of military adventure, however expensive. It is due to national profligacy and plain old "living beyond one's means".

The Obama administration wants to accomplish many things, all of them strategically important: stop the bleeding, kick start the economy through emergency packages, create a plan that will reestablish fiscal discipline and budget balance in the long term, (through a radical reform of entitlement programs), and maintain US global leadership.

This is an immense challenge. It would be great for America to accomplish all this. But it would be even better for the world if America could pull this off. Those who rejoice looking at America in big trouble should ponder what viable alternatives to US global leadership there may be. Unless people seriously believe that Europe's "soft power", with the attendant unwillingness and inability to support a military effort in Afghanistan with more than token troops, will provide

a stronger and more effective leadership model.

Europe's "Soft Power" and the Georgia Crisis

WASHINGTON— The way Europe is handling the Russian invasion of Georgia, (including the disturbing corollary of a possible unilateral recognition of the independence of South Ossetia and Abkhazia by Moscow), invites some reflections about the merit of "soft" versus "hard" power as primary international relations tools. Has Europe's soft power succeeded in persuading Russia to desist from its design to reassert its influence on one of pieces of the former Soviet Union and change course in this crisis? It would appear that this is not the case. It would appear that Moscow has established who is the boss in the Caucasus, while actual or potential European reactions played almost no role in the way in which the Kremlin managed this operation. European verbal reactions, so far at least, have been treated as inconsequential noise.

Yet, in foreign policy debates, it was and it is still quite fashionable and "progressive" to compare Europe's enlightened policy of engagement, founded on its soft power tools, to America's indiscriminate and rough use of raw military power. According to this well meaning conventional wisdom, soft power suggests dialogue, persuasion and the ability to engage others through agreements, trade and cultural exchanges. The second one suggests a somewhat tyrannical, unilateral approach. "Do as I say, or the marines will be following shortly". Europe is about multilateralism, engagement. America is about coercion (whatever the political purposes).

Indeed.

Of course, this whole idea that raw power does not succeed; whereas soft power yields better fruits, better relations and a smoother world has had its best moments in the early phases of Washington's Iraq's adventure. When America's ill advised (according to most) or even criminal (according to some) Iraq enterprise seemed to be pretty close to ending in failure, ("debacle" was the preferred way to describe it), the whole story seemed to present conclusive evidence that military power is a thing of the past. "There are no military solutions to essentially political problems". The morale was the following: "You (primitive) Americans want to use brute force to impose your own idea of change on people who not only disagree with you but who fiercely resist this imposition. Raw power, military power, therefore is not only horrible in terms of the destruction and the casualties that it creates, but it also futile. It just does not work." Thus, better to forget about military options and convert to soft power. Via engagement and dialogue, with the added spice of commerce and thus enhanced prosperity for all as the clear end game, we have a better chance to resolve the issues that the deployment of military force can only exacerbate.

Indeed.

Easy enough to criticize the modalities in which American raw, military power has been used in Iraq. Trigger happy America has made many egregious mistakes. No point enumerating all them here. However, any dispassionate analysis of the wrong and ill advised use of military power, in Iraq or elsewhere, is not a valid argument to proclaim that military power is a relic of a brutal past to be discarded by enlightened people. And the current Georgia crisis, *cum* Russian invasion, illustrates this point.

Commenting on the rather meek EU reaction to this significant crisis showing Russian unilateral action (even if provoked)

via military power in Georgia, while Europe watches helplessly, EU spokesman Martin Selmayr commented: **“We can’t send storm troopers, but we have a trade and economic policy we can discuss [with Russia]. We are an economic force”**. (Emphasis added). Now let us analyze this statement, painfully true in the first part (the storm troopers, or lack thereof), and questionable in its second part (the option of successfully bargaining with Moscow pressing the Russians on economic issues). Martin Selmayr did not say “Under the circumstances, we think it would be a bad idea to send in our storm troopers. Still, in any event, our military, is prudently standing by”. He said “We can’t send storm troopers...”. He did not say: “We would rather not send them”. “He said “We can’t send them”. **This suggests a categoric impossibility: it cannot be done.** And why is it that wealthy Europe, with its strong Euro cannot send anybody? Well, because, in its pursuit of soft power, Europe these days does not have much in terms of military muscle readily available. Simply stated: there are no storm troopers to be sent. And certainly not because Europe is helpless and poor, just like Georgia. There are 27 countries and close to 500 million people in the European Union. Europe has an aggregate GDP equal to if not greater than America’s. There are plenty of industrial resources. But, confronted with a significant crisis with a clear neo-imperial flavor at its doorstep, caused by unilateral use of military power by Russia, Europe’s first assessment is “We can only use diplomacy and economic bargaining, *because we have nothing else*. There are no other options”. Is Moscow going to be impressed with the EU idea to force change on the ground in Georgia via economic bargaining with Russia? Probably not.

In fact, in the specific case of Russia, Europe’s soft power based on economic pressures may not work well either. Europe’s acute dependence on Russia’s oil and gas does not do much to improve its bargaining power. While Russia certainly needs the cash coming from these sales, Europe would be crushed in a

very short time without Russia's energy supplies. In this context, sadly, Europe is militarily irrelevant and economically dependent. Thus Moscow simply ignores it. Which is to say that soft power alone, when dealing with a rather rough neighbor, may not do the trick.

The awareness of the absence of real means to counter Russia's aggression may be the reason behind a rather resigned European approach to the crisis. "Oh well, this is how the Russians are, you know. When provoked, they jump. Therefore, in order to stay out of trouble, given what happened in Georgia, in the future let's try and avoid other actions that may be interpreted by Moscow as provocations". During the old Cold War there was a term to describe this accommodating approach towards the old Soviet Union. It was called: "Self-finlandization", that is censoring one's own behavior, preventing thus possible negative repercussions from a powerful neighbour. It is impossible to say how widespread this attitude may be in Europe today. (And certainly, today's Russia is not the old Soviet Union). But it is out there.

Certainly the Europeans are not sounding an alarm. "Somebody help us. We only have soft power. The other side knows that we cannot oppose them; thus they behave badly, being fully cognizant of the fact that we cannot oppose them". Instead, they say that the situation in Georgia is regrettable; but somehow unavoidable. Nobody in Europe is saying to Russia: "Get out of Georgia, or else". The painful truth is that there is no "else" in Europe's arsenal.

Well, this is what soft power alone gets you. You are weak and everybody knows it. If someone out there is willing to act aggressively counting on zero reaction from you, as you have no tools, then bad behavior is not discouraged. If word gets around that the local police force is now disarmed, some criminals may take notice of this strategic change.

As the new post surge situation in Iraq is showing, there is a

positive, productive use of military power as a key ingredient in the new mix of a better planned counterinsurgency strategy that is beginning to succeed. The fact that shooting indiscriminately is a bad idea does not automatically exclude that shooting discriminately, along with sound engagement policies, may be productive.

The trick is in creating the proper mix. In a word, it is not an either or proposition: "either raw power or soft power". It is about having both and managing skillfully both. If it is true that raw power alone may not get results, the reverse is also true.

Teddy Roosevelt famously embraced the approach of speaking softly, while carrying a big stick, as the most prudent way to move forward. The preferred approach should always be to resolve issues by speaking softly. But all those concerned should see the big stick and –most importantly– they should be absolutely convinced that one will use it –without hesitation– if all else fails.

America should improve its talking skills, while also devising a more judicious and nuanced use of its stick. But the critical point is that America has a stick. Europe has the much more difficult challenge of finding the will to get a stick and to create a policy consensus that would convince the rest of the world that Europe is prepared to use it –and not just in third world countries police operations of little or no consequence. But this may be asking too much of a loose coalition of countries whose main aspiration is to do their best to stay out of trouble.

Europe's Enduring Democracy Deficit

WASHINGTON – The recent Irish referendum rejecting the new EU Treaty that supposedly will bring the EU member states into a closer union is another indication of the fundamental weakness of the whole European project.

Apparently many of the Irish voted against the Treaty for strange reasons that really had nothing to do with the Treaty itself. Others voted against it because they knew little about it, or did not understand its purpose.

This situation would encourage pro-European constituencies to argue that, as the Irish people voted against the Treaty for strange or extraneous reasons, this vote does not really count. The process of progressive unification of Europe is far too important to be derailed by a glitch caused by a small member, after all only one of twenty seven. Ireland insisted on having a referendum, while these serious and complex matters are better handled at a higher level, by the national parliaments; that is to say by “experts” who appreciate difficult subjects that the general public does not really grasp.

Of course, we know that there was no way around the Irish referendum, as it is constitutionally mandated. Still, even assuming the possibility to go around the annoyance of a popular vote, this way of conceiving and implementing the European project, that is to say as a project better handled by experts, a project in which popular will and sentiments are of marginal importance, reveals the profound political weakness of the whole enterprise.

On the one hand the notion of a new, unified Europe as a new protagonist in world affairs is touted as the result of

creative post WWII genius. What Emperors, Popes and dictators could not do by force will be accomplished peacefully through the enactment of new agreements that progressively will bring together all the Europeans.

Nothing wrong in this whole project. Except that this is an elitist enterprise; promoted by some well meaning people; but not sufficiently endorsed by the citizens of Europe. As in the Irish case, the people do not quite understand the project, its purpose and what the end game might be. Given a chance to express themselves, many tend to be skeptical about something that they have not fully understood and thus not fully embraced.

If Europe, at some point in the future, is going to be a new country, it needs convinced citizens. Right now, beyond the motivated elites who are pushing the project forward, there are the lukewarm, maybe somewhat indifferent, followers and the skeptics.

Admittedly, the whole European enterprise goes outside known categories; and so it is difficult to understand it. Still, precisely because it is difficult, it should be truly understood in order to become truly viable.

At the moment, we have a variety of agreements mostly in the areas of agriculture, monetary issues, trade and economic regulation, etc. All important stuff. And mostly good, it would seem. But Europe looks more like a supercharged European Chamber of Commerce, an eminent economic club, rather than a new state.

A state, one way or the other, has to be defined politically. And here we have the major weakness. There is no definition of a political Europe that most Europeans can share and claim to be their own. Even at a symbolic level, we see the inability to rally around something. The European Anthem is Beethoven's Hymn to Joy, from the ninth symphony. A beautiful work of art.

But it expresses moral and aesthetic values of a universal nature. It has no political content. Therefore it is vacuous and insignificant as a rallying cry for the Europeans.

Likewise, the new currency, the Euro, despite its remarkable success, is equally insipid as a symbol of a new entity. In the past the currency notes portrayed eminent citizens: scientists, artists, statesmen, kings and queens. The Euro notes have abstract bridges that convey nothing in particular. As it was impossible to agree on one symbol drawn from one national experience, then no symbol was chosen. And this is precisely the point. No symbol means no profound, inspiring message and no rallying cry for the people.

The Irish expressed their discomfort by saying no to the Treaty. And they have been treated like naughty boys and girls who have messed up the party. Little ignoramuses who wanted to get involved in stuff that only the grown ups can deal with. And now, look at that, we have to fix this problem caused by incompetent citizens.

Well, if this is really the attitude, then the European "democracy deficit" already discussed and studied by many will continue to be the Achilles heel of the whole enterprise. Sure enough, the European project, managed and directed by the (supposedly) competent "professionals" will continue to advance, with or without popular enthusiasm. But only up to a point. Without a legitimate political structure, it is hard to imagine a legitimate European military command and willing soldiers marching behind a flag that for most people is just an abstraction.

Europe may work well within WTO disputes, but there is more than just commerce in the world.

If Europe wants to graduate from its current state of sophisticated economic club to becoming a state, it will have to get the positive support, as opposed to grumbling

indifference, of its citizens. Without that, political Europe will continue to be an idea cherished by some elites; but it will have very little chance of becoming reality, as it will lack the intrinsic strength that only a truly shared sense of purpose can create.

April 4 is NATO's Birthday

By Paolo von Schirach

April 3, 2008

WASHINGTON – Tomorrow is April 4, another birthday for the North Atlantic Treaty Organization, or NATO. The Western Alliance linking North America to Europe was created on this very day in 1949, as a manifestation of a shared western concern about Soviet expansionism. Of course, it was declared at the time that the Alliance was aimed at the preservation of common values uniting America and Europe. But, in truth, it is was the expression of a shared fear. However, when the major threat to Western security—the USSR— disappeared, it was decided to keep this instrument created to counter it. So, NATO survived the end of the main East-West conflict; but the reason for its existence is less clear today, as perceptions about what constitutes a threat to all perhaps are not really shared by all members.

As a result of a reduced sense of purpose, as this “NATO birthday” passes unmentioned and unnoticed, this institution has become less relevant and less vibrant. With the old existential threat gone, unless all members can clearly define and agree upon what is the new threat and thus the new mission, there is an open question as to why we should keep this Western security system. In other words, if the US

and Europe do not seriously believe that only by pooling their resources they can face the major challenges of this era, this security instrument, created long ago, in totally different historic circumstances, may have become obsolete.

In principle, while we no longer worry about the defunct Warsaw Pact, the Alliance declares that there are other threats facing the West. And the NATO members seem to indicate that cooperation among them is the best way to deal with them. Furthermore, NATO has added many East European members (with more to come) since the end of the Cold War. But what does this prestigious club do these days?

For starters, NATO is committed to prevail in the ongoing war in Afghanistan.

Yet, the NATO commitment to Afghanistan looks a bit like the Italian farce of *"Armi amici e Partite"*, something like *"Let Us All Get Our Weapons...and You Go"*. Lip service to the enterprise is more widespread than real action. In other words, not many NATO partners seem to regard this conflict as critically important. Hence minimal support to the effort. Of course, not all Allies are unserious. Some are very, very serious –and their determination is matched by their commitments. But, for many others, this is at best an opportunity to show the flag with the deployment of token contingents, in order to be able to say, at some future date: "we were there".

This uninspiring reality is the expression of a lack of clearly defined and truly shared interests and objectives. However, this fuzziness about first principles is neither discussed nor recognized. Public NATO events are all about the proclamation of high minded principles, with a clear unwillingness by most to point out the mismatch between the reaffirmation of shared principles and the resources allocated to protect them.

Again, the case of Afghanistan, the most important ongoing

conflict involving NATO, is illustrative. Indeed, after the recent Bucharest NATO summit, at least one media account presented French president Sarkozy's announcement that France will provide additional 700 troops to Afghanistan as something close to heroic. Just when things were looking dire, here comes the unflinching ally to save the day. *With a mere 700 hundred extra soldiers?* In a context in which military commanders on the ground have indicated that they need at least additional 7,500 to 10,000 troops? And this is the best contribution coming from an Alliance that ties together the western developed and rich world?

Of course, 700 hundred French soldiers is a lot better than nothing which is pretty much what many of the other Lion Hearts of NATO (including those whose contributions number anywhere from 25 to 250 or 300 soldiers) are prepared to do. And so this French pledge is rated a real triumph that shows how seriously the Allies take the threat coming from a still violent Afghanistan. But this way all parties are complicit in creating and selling make believe, with the result of a level of non seriousness transparent to all, especially to the potential enemies who can have a practical illustration of what most western countries are prepared to contribute to the common security. Once again, the Emperor has no clothes.

Now, if NATO were convinced that this enterprise –Afghanistan– is a mistake, it could change course and conclude that it wants nothing to do with it. It could withdraw its contingents and leave it to the messy Americans (and may be a few other misguided souls) to deal with it. But to proclaim a continuing commitment and do so little to meet the challenge is border line farcical. If nothing else, it shows the lack of a shared definition of a common security threat. Alliances are based on shared interests. This lack of action is an indication that a serious debate on what these interests might be is overdue.

In truth, US Secretary of Defense Robert Gates recently indicated that this lack of European follow on in Afghanistan

(in terms of resources and troops) could potentially trigger a crisis between Europe and the United States. Yet, there has been no serious reaction from Europe to this rather open US threat which amounted to saying: "If you are not serious about follow on, then we should look at the whole concept of collective western security and see if it is still viable".

While this might have been the beginning of a serious conversation, it has become subsequently clear that the US, on second thought, decided not to push this crucial reappraisal. The Bush administration backtracked. In its last few months in office, it does not have the stomach to start a fight with those who, at least nominally, are Allies. So, for the time being, the US accepts a lack of commitment to the common security on the part of many Europeans as a fact of life that cannot be reversed. While the desire to avoid a crisis can be understood, at some point the members will have to redefine what this Alliance is about. And if they will come to the decision that it no longer serves a valid purpose they can dissolve it.

Whereas, the display of verbal support and little action in Afghanistan indicates at least lack of clarity on the part of many members as to what their interests are. This is a NATO war and NATO is not performing. This Alliance has become soggy. It is mostly a transatlantic forum for meetings followed by generic platitudes, with not much in terms of muscle (military power) and willingness to use it.

Oddly enough, at the recent April Bucharest summit the Allies recognized that NATO has huge unmet needs. The Bucharest communiqué most amazingly admits that:

"We must ensure that we provide the forces required for our operations and other commitments. (Bold added). *To that end we will continue efforts to be able to deploy and sustain more forces. We are committed to support the NATO Response Force by providing the necessary forces, and to improving the*

availability of operational and strategic reserve forces for our operations. We will seek greater domestic support for our operations, including through improved public diplomacy efforts.

We will further develop the capabilities required to conduct the full range of our missions and to remedy specific shortfalls. We will work particularly at improving strategic lift and intra-theatre airlift, especially mission-capable helicopters and welcome national initiatives in support of this work, as well as addressing multinational logistics.(.....).We will continue to enhance the capability and interoperability of our special operations forces. Supported by the defense planning processes, we will enhance our efforts to develop and field the right capabilities and forces, with the greatest practicable interoperability and standardization. This will be furthered by improving trans-Atlantic defense industrial cooperation”.

Now, this open and detailed admission of lack of basic resources and capabilities, (number of forces, airlift, logistics and interoperability), is truly startling. This is NATO. “The” defense apparatus that for decades has been regarded as the backbone of western security. Reading this, the proverbial visitor from outer space might surmise that NATO must be a brand new thing. And so planners are just now getting started to create the tools and the networks that will make future action possible.

If we believe that NATO is still relevant as a security instrument in this entirely different post Cold War context, it needs real teeth. The admission that, today, a few years into a NATO led conflict in Afghanistan, NATO members have to **“provide the forces required”**; while NATO needs public diplomacy efforts to convince –I suppose–the political leadership of member countries that they need to do this and pay for this, is an indication that without a clear formulation and agreement about shared security interests the

Alliance is becoming more and more form without substance.

The Bush administration can be rightfully blamed for its recklessness, unilateralism, misguided policies, the Iraq enterprise etc. It can also be blamed for not consulting Allies and not listening to them. But it can hardly be blamed for the falling defense budgets of many European countries and for the token commitments of many to what should be a shared effort. Defense budgets and military preparedness are a function of perception. If Europe believes that its current efforts are about right, so be it. But if this so, is there still a role for this Alliance?

In a few months President George Bush will be out of the scene, for good. But the lukewarm feelings about the need to provide for defense that we notice in many European countries are likely to stay. This does not augur well for Afghanistan, or for dealing with any future threat for that matter. If the members have developed different views about security needs, a rediscussion about the role of this Alliance is in order.

Europe and World Threats

WASHINGTON – “We must not –we cannot–become a two-tiered alliance of those willing to fight and those who are not”, Robert Gates, US Secretary of Defense told a largely European audience at a recent Munich Conference on Security Studies Policy, where NATO’s effort towards Afghanistan was a central topic. “Such a development, with all its implications for collective security, would effectively destroy the alliance”, he added.

Indeed. Strong language from the US Sec Def.

Anybody cares?

But not much of a ripple effect. Indeed, reading about NATO matters in Afghanistan on the official NATO website, one is lost in generic, (perhaps decidedly), confusing language as to who does what there and under what conditions and circumstances. Afghanistan is there on NATO's busy agenda...and so is Kosovo....and so is more.....Any specific sense of urgency about Afghanistan? Can one detect that this is a strategic priority? If it is there, I missed it entirely. The actions of most member states indicate that the current level of effort is deemed to be "just about right", in present circumstances.

The notion that the loss of Afghanistan would be a significant "symbolic loss", especially for this Islamic, "appearance conscious" worldview –as it is indeed "the place" where this whole terror, anti-terror business actually started– is not available anywhere.

US wanted to subcontract Afghanistan to NATO

The US Government, in its own hubristic idea of quickly transforming the Middle East, grabbing Iraq –after all a key state from any standpoint– conceived that idea, (at the time, in 2003), of subcontracting Afghanistan (relatively sleepy, then), to NATO; figuring out, (hoping?), that some kind of NATO-led occupation force would keep the country together.

Well, as we now know, it did not happen that way. Iraq proved to be a lot more difficult. Afghanistan has turned out to be a lot worse. The post-Taliban mess, in its own internally and externally torn confusion, in the end was extended to more or less equally friendly territory on the other side of the Afghan border. Pakistan's North West is now also a huge mess. For the time being, the idea that an Islamabad led force will put things in order in the large region adjacent to Afghanistan is still a distant dream.

End of NATO is Europe does not do more?

But all this, from the picturesque, post card like, lovely European cities (that Americans get when looking at Europe through the nicely tinted eyes of marketers who insist on Europe as this lovely, slow and enchanting oasis of peace, culture and serenity), looks awfully distant and remote. Europe in danger? From Afghanistan/Pakistan? And why? We'll find some accommodation. There must be....a way....Indeed.

Bob Gates said it in Munich..."Either we resolve this mess of unequal contributions to the war effort –I paraphrase– or it is the end of NATO as the primary tool for North Atlantic co-operation".

If there was trembling within the old European palaces, at the notion that this mighty edifice of Western Power could be unraveled, it did not show.

After the end of the USSR, smaller NATO forces

In 1989, while still working at the Atlantic Council of the United States, I did not expect the so rapid crumbling of the Eastern Empire. Nobody really did. And, at the time, it looked fine. End of an Eastern threat, in a truly existential sense. As a result, defense spending within NATO countries was cut. The Alliance, whatever its then status, could stay, as it was a reasonably proven tool for communication and for sorting out US-European affairs. Although, hardly an ideal set up, a NATO without meaningful force, was fine; to the extent that no large force was really necessary to protect the Allies from an enemy that had retreated and (militarily) basically ceased to exist.

Afghanistan, a new scenario

But now, Afghanistan, this new thing, has created a new set of problems. Europe seems to have no tools, no means –and especially no will– to deal with this awkwardly far away

country in which, unfortunately, (and here it all gets tricky, as people interpret unclear developments as they please), there is a fertile soil for the amalgamation of anti western, jihad ideas and policies.

The issue again is distance, and a strong desire to continue living just as in those lovely "picturesque post cards" of serene Europe that populate US TV programmes on Public Television (PBS). In that Europe that reasonably well heeled Americans want to go and visit to bathe themselves in proper culture and art, all is beautiful; all is neat, all is quiet and enchanting. In that context of order and quiet, vague, remote places, vague threats, mean little to the average person. There are no imminent dangers of "old fashioned armored divisions across the border". And so, the Europeans try again to remove themselves from the danger area. They try so hard. The idea (for some at least) is that, just by being there, (in Afghanistan), we are on the bad guys list. We are known and counted. And later on they'll come after us.

Europe is in denial

Who knows what the best strategy for Afghanistan may be. But a bit more of everything should be at least tried. More material aid, stronger presence, more visible and useful reconstruction, a stronger sense offered to the population that something better for them is in the offing. Are we really saying that the whole of Europe cannot dispatch more than 2000 troops here, 3000 there? And all that with the most intricate set of caveats in terms of "the contingent from this nation will go as far as here...but not beyond", etc; Is that all there is? Is this all that this NATO Alliance can deliver?

Clearly, this is all it wants to deliver. Allowing this wound between Afghanistan and Pakistan to remain infested and to continue to attract more bad stuff, we'll do the west no good. But, again, all dire scenarios are in the category of theoretical, possible, not certain.

Even when things were bad Europe was reluctant

I mentioned earlier “armoured divisions across the border”...Indeed.. But we remember those and the minimal mobilizing effect they had. What did those Warsaw Pact quite visible divisions do? Did that “danger” push the Europeans to spend more and build much stronger defenses? Hardly at all.

In the 1980s, (before the end of the old scenario with the collapse of the Soviet Union), in Washington DC we had a complicated policy debate, (we used to call it “burden sharing”), whose ultimate objective was to find the Europeans materially at fault: that is, facts in hand, not delivering on promises to augment defense spending by certain yearly amounts.

Europe’s relaxed attitude about defense a moot point after the end of the USSR

And that did not go anywhere either. Of course, (and Thank God for that!), we’ll never really know what might have happened, had the then Soviets decided to test the actual strength and resolve of that NATO Alliance. Maybe because it would have been messy; maybe because it was about almost immediate nuclear escalation...who knows, really.

Europe’s wishful thinking

But now, after the Soviet demise, and the current danger, (Afghanistan), conveniently located in really distant areas, it appears that Europe can (try and) continue to be what it wants to be: an island of peace within an uncertain international sea. Nothing wrong with that, but only as an aspiration.

The Romans, who were rather no nonsense about all this, put it bluntly, long ago: “If you want peace...Be ready for war”. (“**Si vis pacem, para bellum**”). Wanting peace is a great goal. Convincing others, in this confused world, that, no matter

what they try and do, they shall not prevail, is an entirely different matter.

Real security requires not just *pretending* that one will take action, but really convincing the other(s) that action will take place and that it will be swift and deadly. This Europe with lovely landscapes and nice parks does not overtly exude this certainty and determination. Or may be I have been watching too much Europe through the gentle marketing lenses of US Public Television...

“The Decline of America” Revisited

WASHINGTON – Remember Yale historian Paul Kennedy and his 1987 tome on “The Rise and Fall of the Great Powers”? At that time there was a lot of interest in this fairly comprehensive narrative focusing on how all major western powers, primarily because of the huge cost of maintaining their Empires, suffered progressive economic decline and eventual decay. Thus Spain –in Kennedy’s argument– thus Great Britain and thus –inevitably– the US. The book sparked a spirited debate about the future of the US as the leading power of the century. The combination of a sputtering economy, strong Japanese competition and raising security expenditures necessary to maintain the American Empire would lead to bankruptcy and thus to the inevitable –if sad–retreat from global ambitions. Kennedy’s work contributed to a new self-reflective atmosphere that gave rise, among other things, to efforts aimed at investigating the soundness of the main pillars that sustain the edifice of America’s might. Think tanks, the Congress, and the Federal Government launched studies, initiatives and task

forces on "US Competitiveness" –or lack thereof. The newly formed bipartisan Concord Coalition started warning Americans as to the structural damage caused by runaway deficits due in large part to the unstoppable growth of spending on entitlement programs.

So, according to the conventional wisdom of the late 1980s, we were overstretched militarily because of the Cold War security commitments highlighted by the 300,000 troops permanently stationed in Europe, as our most visible contribution to NATO and by the questionable idea of spending billions of dollars on the Star Wars program, that is space based ballistic missile defenses. We had lost our edge in economic innovation. We were assaulted by the Japanese bulldozer from the East. This was the time, we should remember, in which the trade deficit was about Japan; while Japanese concerns had started a buying spree in America that, according to many, even serious, observers, had all the markings of a progressive take over of our economy. Meanwhile the "Europe 1992" agenda, the solemn commitment on the part of the then European Community to pull down residual internal barriers and create a brand new, vibrant market, seemed to foretell a new era of economic primacy for the Old Continent, engineered behind the walls of a "Fortress Europe" that –it was feared– would exclude Americans. Here at home, because of misguided fiscal policies and unhealthy personal spending habits, we –the Government and the individual citizens– were slowly but surely drowning in debt. That was the picture then. It was the widely shared notion that the economy was on the verge of collapse, especially after the mild recession of 1991 that propelled technocratic Bill Clinton and his panoply of new, original economic ideas (never really implemented, by the way) to the White House.

But, in the meantime, the unexpected happened –on many fronts. 1989 did not give us just the promise of German reunification. It was the first shock wave that signaled the collapse of the

Soviet Empire and thus the end of the major threat to US security. The final demise of the biggest existential threat was the justification to significantly cut defense spending and international commitments in the 1990s. This dramatic change, combined with a resurgent faith in small government, especially after the republican revolution of 1994 masterminded by Newt Gingrich, meant that runaway federal spending could be contained.

At the same time, without the support of any particular blueprint devised in Washington, the information revolution was unfolding. Rather than creating a new economy, the massive adoption of IT by all businesses meant a massive leap forward in the competitiveness of the US economy. We had spectacular growth year after year, record low unemployment and high tax receipts that gave us for the first time in decades a federal budget surplus. At the same time, without the US lifting a finger, Japan, because of its internal social, rather than economic, contradictions, fizzled, while the predictions of the rise of a robust, innovative and economically powerful Europe proved to be quite wrong. And so, we had the roaring '90s: a prolonged period of American unchallenged economic primacy. The US was first in everything: innovation in high tech, creation of new employment, record productivity increases.

But it all seemed to have ended somewhat ignominiously with the beginning of the new millennium. We have had the dot.com bust, accompanied by the Enron, WorldCom, Adelphia and other well known corporate scandals which ushered the Wall Street contraction and the ensuing long bear market. The 9/11 attacks, occurring during this downward spiral certainly did not help.

And now, where are we now? There are disturbing signs that would indicate that Paul Kennedy and other were after all right in predicting decline. Only they were incorrect as to how close it was and what would cause it. The root cause is

not "Imperial Overstretch", but the erosion of US competitiveness due to lack of investments in both human capital and needed infrastructure, accompanied by the unstoppable growth of entitlement programs. Sure enough, at this time we also have a war. The prolonged Iraqi campaign has become stupendously expensive. But, regardless as to one's own political opinion about the war, this commitment, in an as of itself, is economically affordable.

While a war and an increased Pentagon budget are a drain on public finances at the expense of productive investments, the real problems are in the same factors that were identified 20 years ago, at the time of the "competitiveness debate", by most sensible analysts: a more and more expensive welfare state that cannot sustain itself financially, and the progressive erosion of the education advantage that made America the principal player in the knowledge economy. If we continue to follow the notion that large segments of the American society, mostly the elderly and the retirees, have an inherent right to subsidized benefits that represent an excessive drainage of national resources, the federal government, even assuming the ability to finance these obligations, will have nothing left for productive investments. The secondary public education system, in turn, provides mediocre graduates, while minorities, on balance, do a lot worse than the already low average. It is impossible to sustain this increasingly complex economy without a dramatic improvement in the quality of the labor force.

The fantastic explosion of the trade deficit is the manifestation of eroded competitiveness. The 40 billion dollar deficits that scared us about Japan in the 1980s are pocket change compared to the 220 plus billion that we have nowadays with China alone, (not to mention the increased cost of our energy habits: at 300 billion in 2006, higher than the cost of imports from China).

Unfortunately, the argument on how to best rebalance our trade accounts has been successfully framed by a strange medley of simplistic romantics and demagogues who point the finger at the combined perils of free trade and outsourcing. By opening ourselves to foreign producers –so the refrain goes– we allow cheaper goods to come in. This means that US companies that have much higher costs go out of business or move overseas. Good American jobs go abroad because greedy corporations want to save money by having cheaper foreigners perform jobs previously held by higher paid Americans. The solutions advocated? Essentially close our borders, so that the jobs stay in and the foreign goods out. In this new era of global and irreversible interdependencies, the notion that this way we shall be able to regain, maintain and for ever keep our supposedly God given infinite prosperity is bizarre; but, nonetheless, it has strong emotional appeal.

However, if it is clearly futile to try and close our borders to keep cheap goods out or to prevent businesses from outsourcing, we still have a huge problem which is indeed caused by globalization. But not the globalization demonized by the protectionists. It is caused by the global spreading of the knowledge economy model developed first in America whose successful exploitation gave the US the edge for a number of years.

We have to come to terms with the fact that the genie of IT innovation has been out of the Silicon Valley bottle for a long, long time. We cannot restrict inventiveness and entrepreneurship –the key components of the American success story– to the American soil. The main ingredients of a knowledge based economy are transferable and so (despite copy cat failures and other clumsy attempts) they are transferred elsewhere today and more so in the intervening years.

True, the 1990s triumph of America's reacquired competitiveness was due to a complex mix of factors that cannot all be easily reproduced. The lively, free wheeling,

chaotic mixture of entrepreneurs, academics, venture capitalists and their interactions with established corporate entities that buy, absorb, invest in new ventures, as yet, has no equivalent elsewhere around the world, in terms of depth and scope. But some of its elements can be replicated. No doubt, by trial and error in time others will manage to produce adequately funded innovative clusters that will be able to quickly direct new discoveries to a hungry global marketplace.

The celebrated Bangalore example in India is illustrative. Leaving aside all other considerations, the Indians have managed to create and aggregate in productive clusters world class human capital (scientists, engineers, software programmers) and to harness it effectively in competitive IT enterprises. To keep things in perspective, we should remind ourselves that Bangalore is still mostly about outsourcing and not about innovation. Moreover, the whole Indian high tech phenomenon is only a small speck within a still primitive Indian economy which is constrained by inefficient administration and crumbling infrastructures. India has an enormous population that is still largely poor or very poor. So, the days of Indian supremacy are still in the distant future.

But Bangalore and other such examples around the world will multiply, as more and more people gain access to higher education, IT literacy and mundane computer and business skills that cannot be kept within the West and America. The very information revolution unleashed by the American genius becomes the vessel that greatly expedites the transfer of knowledge that will create new centers of excellence where none existed before. Furthermore, the Indian example proves that we do not need an economy that is overall highly developed to create islands of modernity that can compete on practically any level with counterparts in advanced economies. Indeed, centers of competitive high tech can be established

even without the fertile ground of an already developed economy that has already successfully dealt with macroeconomic issues.

These new enterprises, especially those established in business friendly developing countries where the cost of professional for many years to come will continue to be much lower than America's, are bound to gain world market share, inevitably at our expense. If even a small fraction (as a percentage of the total population) of Indians and Chinese become good scientists, their absolute numbers will be sufficient to tip the balance. Our only hope to stay competitive is in continuing to invest in new technologies and new ideas so that superior innovative products and services will continue to be created in America.

But here we have a serious problem. Americans are so used to primacy that they do not believe that the ingredients that make this primacy possible need to be nurtured, refined and upgraded, especially now that we are confronted with new, capable competitors that have the added edge of a lower cost structure. (For instance, it has taken 20 years to the slow moving, no pun intended, automobile industry to have just recently what appears to be a collective awakening, with the active participation of the unions representing its thousands of workers. But it seems that only the specter of demise convinced the main players that dramatic cost cutting—be it salaries or health care benefits— is imperative in order to have a chance to compete. But, even if successfully implemented, these strategies are clearly not enough to get Detroit out of the woods. In the next few years we shall see whether the bitter cost cutting medicine will be accompanied by a new wave of creativity that is the real hope for recreating a competitive edge for this ailing sector).

While discussions about the international economy abound, for the time being, we have not framed the debate in a way that will foster real progress. Unfortunately, to the extent that

the general public has been brought into the conversation, it is fed gross distortions and oversimplifications pointing at the consequences of lost competitiveness, such as job losses. The conversation is mostly on allegedly bad trade policies and greedy corporations. If we could only change Washington's direction on trade, all will be well. Indeed, the debate is mostly about identifying culprits and quick fixes. So, according to these critics, beyond the international trade policy incompetence (close to treasonous behavior), the enemies are the Asians, (yesterday Japan, today China) who do not play by the rules and the illegal immigrants who steal domestic jobs while depressing wages. This sort of populism may work with many constituencies in uncertain economic times; but it explains nothing about the causes of our ailments and its remedies would cure nothing.

The reality is that we have structural, systemic problems that need to be addressed now, so that we can begin to change course and hopefully improve our conditions for the long term. While the misbehavior of others is real (think of Chinese disregard for intellectual property rights and the ensuing flood of pirated software and counterfeit goods; think of the Mexican government actively encouraging the emigration to America of the country's surplus labor), there are inherently domestic structural deficiencies that slow down America and that have eroded its ability to compete. To name a few critical ones: a deteriorating education system, the unsustainable cost of the welfare state and the lack of a serious energy strategy.

Clearly the soft underbelly of America is a mediocre to bad education system right at the time when new, world class centers of higher learning are sprouting around the world. America for a long time nurtured domestic talent while, by design or by default, (think about the intellectual migration to America from Nazi occupied Europe), it was able to attract first class minds from around the world. After all, Albert

Einstein, Enrico Fermi and Edward Teller were not Americans. But they were welcomed in America and the American intellectual and scientific environment was able to absorb this talent and greatly benefit from it. In more recent years there has been a significant influx of gifted Asians. But now the pull of America is not as compelling as it used to be in the light of the fact that good opportunities exist elsewhere.

At the same time, it is now apparent that the American public education system, the incubator that should nurture the future scientists, engineers and entrepreneurs is at best mediocre, deeply flawed in its worst components and certainly inadequate to create the world class work force that will have to compete on quality, as costs already work against us. The existence of several world class universities is not sufficient to guarantee that the broader US workforce will be able to compete with increasingly more sophisticated foreigners. A sub par work force will make it difficult to compete, let alone strengthen, our positions in high value added strategic areas.

While it is hard to admit it, a huge chunk of the old manufacturing base of America is either gone or going. We lost a lot of steel, machine tools; we lost footwear, apparel; we have disturbing signs that we cannot keep up in automobiles. We have a battle unfolding in aerospace. Still, American success stories in valuable, technologically complex industries (think of GE, 3M, United Technologies, Boeing among many others) show that, despite higher labor cost, superior quality, when it can be reinforced by constant refinement, still counts.

By the same token, we still have an edge in services. But this is entirely dependent on the continuous waves of IT innovation. If we are no longer on the forefront of IT, because we can no longer compete with increasingly more competent but much cheaper Indians and Chinese, we have lost the competitiveness contest.

Much has been said about the increased welfare costs due to the demographic changes that America is experiencing, along with most other developed countries. The question is whether it is smart, in the long run, to have a central government whose main function is to distribute benefits at the cost of everything else. Even now, while immediate solvency is not an issue, the federal government devotes relatively smaller portions of its resources to productive investments, given the weight of the entitlement obligations. As we all know, in the future this is only going to get worse. It is understood that taking something away from people who believe that they have earned a partially subsidized old age is extremely hard. But there is an opportunity cost in spending most of our revenues on welfare and little on competitiveness enhancing investments. Unfortunately few people enumerate the thousand of research projects or new infrastructure that could be financed by the federal government, assuming a reduction in entitlement programs.

The energy picture is dismal. We have excessive consumption, little and declining production and increased dependence on imports that is financially burdensome, while it creates a serious strategic vulnerability. What we need is not just the tinkering provided by this or that pork laden energy bill; but a bold new *energy strategy* that would set realistic goals regarding alternatives to hydrocarbons, while actively discouraging consumption through revenue neutral gasoline taxes. In doing so, America would free itself from this straightjacket, while possibly becoming the world leader in all new technologies related to alternative energy.

But in all these areas: education, welfare reform and energy, while there is a debate and many have offered sensible solutions, we are far from having reached the deep understanding that is the prelude to decisive action. While many are worried, most believe that things are more or less fine and that we have enough slack to muddle through.

In hindsight, similar historic circumstances characterized by a passive attitude that in effects allows the sliding into decay (and here we go back to Paul Kennedy) are recognized as due to a state of mind of myopic denial and complacency of people who have lost their way. But usually this is the verdict of historians. And when they pronounce it, it is too late to change anything.

“At Ease with Globalization”?

by Paolo von Schirach

May 25, 2007

WASHINGTON – French President Nicolas Sarkozy in his first official visit to Manuel Barroso, president of the EU Commission in Brussels, reportedly talked, among other things, about the duty of the EU institutions to protect the citizens of Europe from the dangerous winds of globalization. He did not say protect forever. He said protect them until they are ready, until they have made the necessary adjustments in order to be able to transition to the new free for all environment. Why is it that after twenty years of globalization they are not yet “ready” it is not said.

Depending on how one looks at this approach, it is both right and wrong. Of course, in principle, it is better to have some training before entering the real competition. So this is good. But the competition started long ago. When will the citizens of Europe be ready? How long should this ‘training’ last? It would be wrong to assume an open ended period of protection.

On the domestic front, Sarkozy’s electoral message, the

message that led him to a convincing political victory, is that France needs to get serious about work and that the French need to get busy. But, apparently, the president's judgment is that the French -for the moment at least- are too frail to compete outside of Europe. Hence the need to have transitions. How would these transitions be shaped in order to make everybody stronger and more competitive we do not know exactly. The danger is, of course, that, as 'we need more time', temporary measures will somehow become permanent, without any marked improvement of the overall competitiveness

A message with a totally different tone came recently from the United Kingdom. Outgoing British Prime Minister Tony Blair, in his farewell speech to the constituents who elected him to Westminster, indicated that Britain, (in large part, of course, because of his enlightened policies), is not only ready for the challenge; but thriving in the new globalized economy and winning. 'Look at our economy 'said Blair-*at ease with globalization*. (emphasis added). London the world's financial centre. Visit our great cities and compare them with 10 years ago. No country attracts overseas investment like we do"!

Needless to say, it is easy for Blair, just about to leave office, to give himself high marks, and proclaim Britain, because of the workings of his government, an internationally competitive society. But there is some truth to his words, at least in relation to how the society perceives itself, thus its chances of making it. The message is that the British "understand" global trends and that they have the tools that make them well equipped. Thus they are active participants and not fearful of competitors. They are 'at ease' with the whole process.

In the US we have a mixed bag. The country as a whole is doing reasonably well. Success in globalization is largely about being and staying ahead of the curve. America's culture of innovation and risk taking enterprise, where 'creative

destruction' is practiced daily, seems perfectly suited to doing well in a challenging world.

However, there is no unanimity that overall we are 'at ease with globalization'. The strains of globalization are felt and many are so hurt, or are so afraid of being hurt that would like the whole thing to stop and go away. The arguments are familiar: cheap (Chinese today, Japanese yesterday) imports displace American workers. Factories close or relocate. Jobs are lost, communities are devastated, etc. Why do we allow this madness of a free trade that benefits only the competition? So, while Sarkozy demands a respite from the European institutions, many Americans demand dramatic policy shifts in Washington. Free trade, they claim, has become the instrument used by unscrupulous competitors to undo western economies and societies.

Let us leave aside here any attempt to settle the now worn diatribe on the pros and cons of globalization. In this instance, let's focus on one observation: the emergence of Asia has brought about the net addition of hundreds of millions of relatively cheap workers to the global labor pool. It has been said before; but it is well worth repeating, as the critics arguments somehow seem to ignore that we are confronted with the new reality of hundreds of millions of new low cost workers, added to the global labor pool, with more coming. Unless we assume tightly sealed markets, this significant additional labor supply has to have a dampening effect on workers wages worldwide.

The West, Europe first and then North America, for a couple of centuries led industrialization and technological innovation. After World War II, Japan, previously the spoiler, joined the club as a full member. Then the Asian Tigers came along in the 1980s. These were significant changes that altered the global balance of economic power. But, with the exception of the fear engendered in some vociferous quarters by the perception in the 1980s that the Japanese were cunningly and ruthlessly

pursuing a strategy of world economic dominance, (thus going back to their methods of WWII, albeit confined to the economic sphere) this was still, relatively speaking, incremental change, at least compared to what came after and is still unfolding.

As a consequence of both the spreading of technologies and the enactment of economic liberalization measures in Asia, the world economy is digesting and will digest for many more years to come the net addition of hundreds of millions of skilled or semi skilled workers, perfectly capable of performing at least a number of tasks at much lower cost. At least some of them will learn more complex tasks. This will allow for some sectors to move up the value chain. Hundreds of millions of new workers have transformed Asia into the world's workshop. In services, English language proficiency, computer literacy and high speed, low cost, internet, make it possible to outsource more and more functions to where they cost significantly less.

This is a systemic shift in the global equation. We have moved and are continuing to move from relatively high cost operations in the west that employed millions, to low cost operations in Asia, with the net result of transferring functions and jobs over there. In the light of this systemic shift, amounting to hundreds of millions low cost Asians added to the global work force, even with increased global demand for goods and services, it is not possible for western workers to keep the same jobs at the same level of compensation enjoyed by them when they were not facing competition.

This is not a pleasant fact, as it carries many well known negative consequences: the rapid displacement of millions of western workers (with more dramatic impact in countries like the US where safety nets are minimal) and the lowering of standards of living for those (the lucky ones) who find new employment in jobs that quite often pay less than the factory

union wages that they were accustomed to.

Looking at this devastation, many demand that this trend be stopped and, better yet, reversed, given its obvious catastrophic consequences for our standards of living. But stopping this trend in a world that is interconnected and interdependent to a degree unprecedented in history, is not possible, even leaving aside the question of how intelligent this solution would be.

Of course, we can and should protest about unorthodox and/or unlawful practices of our competitors. But no serious person can say that the economic rise of China, for instance, is only or mostly about dumping, currency manipulation, pirated goods, disregard for safety and labor standards, lack of reciprocity etc. etc. Of course we should do a lot more to create a level playing field and this should improve the chances of many economic actors currently hampered by restrictive practices.

Yet, the fact remains that the global labor pool has widened and this is not a function of added global demand. It would be foolish to assume that the relatively sudden entering of hundreds of millions of people in the global work force pool, in a world in which technologies have lowered the previous disadvantages of distance and other transaction costs, would have no effect on the established economic equilibrium: most importantly on the standards of living of developed countries' workers who are now facing these low cost competitors. In this new environment, made possible by the spreading of the technological know how spearheaded in the west, others for the moment enjoy a relative advantage (low cost) that will not be negotiated away.

The critics call this shift of economic activities to low cost countries the race to the bottom. But how can it be otherwise? Capital looks for the highest remuneration. Wherever new opportunities to create competitive goods and services at a low cost will be found, money will go there. Of course there

have been and there are excesses, (horrible working conditions, inhuman exploitation). But today they are not the norm. And when these bad practices do occur, they are more and more easily exposed by thousands of watchful NGOs and by the international media.

Overtime, cost differentials will shrink and the Chinese (and all the others) will have to compete on quality and not mainly on price. But this is not happening any time soon. There are one billion and three hundred million Chinese out there. Only a fraction of them are participating in this industrialization process that is proceeding at breakneck speed. May more will join the ranks before a rebalancing will occur. India is a very different case. But there are one billion plus Indians. Even leaving aside the crops of the elite technology and management schools, overtime the Indian system will generate an even more massive supply of capable workers and technically skilled individuals.

Westerners have to confront and digest this fact, without trying to exorcise it by attributing the success of others to their nefarious practices in alliance with wicked national traitors who are sending 'our' jobs overseas, thus lining their pockets; with cynical disregard for the plight of their former workers. This may make some people feel good about conducting a moral crusade. But, in the end, it will yield very little. This is not a passing phenomenon that can be blocked by rejecting free trade and erecting barriers against foreign goods. The economies of the world have reached a level of interconnection and interdependence that cannot be undone by a more muscular trade policy.

Everything else being equal, for instance, it is preposterous to believe that in a competitive environment, in the long term, we will be able to have a healthy auto industry when the American auto worker earns several times his Chinese counterpart. (We already see the devastating impact of US based Japanese factories. The success of Toyota is based on

better products but also on non union wages for their US workers). In the end, either the unionized US auto worker will accept lower wages, (incidentally this is what airlines workers have done to recreate a modicum of cost competitiveness in a field populated by more and more domestic low cost carriers), or move on to other sectors where America is ahead and thus not facing low cost competitors for the same products.

So, people are displaced and more will be displaced. This is the area where "transitions" matter and can make a real difference. However, this is where the existing effort does not seem even remotely equal to the magnitude of the task. Displaced people need to be helped to get the skills so that they can find something else that can be meaningful and rewarding. The fact that many jobless people eventually find something that, however, does not pay as much as the former factory jobs, is difficult to digest. But, unfortunately, this is unavoidable, unless we can find a way to rapidly teach them truly valuable skills.

Of course, this state of affairs fuels class resentment. The well equipped western business and professional elites usually win in the new globalized economy. They have the resources to adapt, change, relocate, outsource. And the opportunity divide, if anything, with the passing of time, is getting deeper. With their money, the elites can pay for international education for their children. These children will have a gigantic head start on all the others in the competition for the plum jobs of the globalized economy. The MBA graduates from the top schools can vet tantalizing job offers ranging from finance in New York, London or Hong Kong; oil services in Texas or Dubai, high tech industries in California, Singapore or Finland.

At the opposite end of the spectrum, some American high school graduates cannot even read a bus timetable; not to mention the many, (mostly minorities) who, hampered by negative

circumstances, do not even get to graduate. As a result of a woefully inadequate education system, most of the disadvantaged stay disadvantaged. They can compete only for the scraps, along with the other less educated from all over the world.

In this new era in which the value of education has increased, it is odd to hear fierce critics of globalization reminiscing about the good old days in which an uneducated individual could get a factory job with union wages that more or less guaranteed a lower middle class or even middle class standard of living. This is no longer, and this is bad, claim the critics. Leaving aside the notion that, according to this reasoning, being uneducated was somehow alright, almost a virtue, in as much as it did not economically penalize the uneducated, the truth is that that era is over. In order to have a chance to participate in the modern knowledge economy a good education and a variety of technical skills are mandatory.

The plight of displaced people is real enough. But instead of clamoring for the totally unrealistic goal of turning the clock back so that we can recreate those times in which lack of education did not entail such a major economic price, we should confront head on the real issue. If we cannot compete on price with the low cost Asians, we have to be able to compete on quality and rate of innovation.

And here education comes to the fore. All American politicians talk about it, lamenting its low quality and making speeches about the need to have more math and science, so that, just like the post Sputnik aftershock, we will get all the skilled people that we will need to stay competitive. All this is very true. But somehow, clamoring notwithstanding, not much is happening. Perhaps it is because we are approaching the issue from the wrong end: i.e. devise a system that will produce these many high quality graduates, etc. as if these were merely the human widgets needed to increase the performance of

the economic mechanism.

Whereas, in order to be more successful in this endeavor, it would be good for the nation leaders to extol the intrinsic, as opposed to the commercial value of education. If higher education standards are pushed purely as defensive, reactive measures, then the efforts will not be very productive. Chances are that a mostly reactive education drive overtime will not be sustained.

A vibrant economy is a byproduct of vibrant people. And people are vibrant when they are passionate about what they are doing. (Ask any management guru and they will recite this mantra about 'motivation' and 'passion' over and over at the foundation of success in business). While it may very well be true that necessity is the mother of invention, the ideal environment is one in which people are driven by a genuine interest and curiosity for what they are doing and not primarily by the fear of losing.

Whereas what we hear from political leaders in America is that the primary reason why we have to improve proficiency is because now we have competitors. Which really means that, if we did not have competitors, then ignorance would be fine, because we would not pay a price for it. The message as crafted in this impoverished, merely utilitarian, fashion is that we attribute no intrinsic value to the pursuit of new knowledge. Knowledge (or lack thereof) is relevant only to the extent that objectively it is a competitiveness tool. Presumably, then, once we will have reached a level that seems to be safe for us to keep our coveted standards of living, then it will be alright to slacken the pace again.

This shallow approach devalues the proposition that, for a society to thrive, many of its citizens must be driven by a genuine, personal desire to expand their horizons. The western scientific and technological revolution did not start in the the 18th Century because of fear of competition, but because

of a desire to acquire new knowledge and apply it in order to improve the quality of life. In the United States, free institutions were created because it was believed by the founders that liberty is the necessary precondition so that individuals, free of fear from arbitrary power, can be engaged in whatever lawful quest may appeal to them.

If we manage to instill this spirit of wonder and curiosity in our societies, then new knowledge, to be translated in commercially viable activities, will come about as a result of the combined efforts of millions. As a result, the fears of not being able to make it 'at the foundation of all protectionist ideas and policies' will wither away. Cognizant of our abilities and intellectual prowess, then, (if not all of us), at least many more shall all be, as Tony Blair put it, 'at ease with globalization'.