

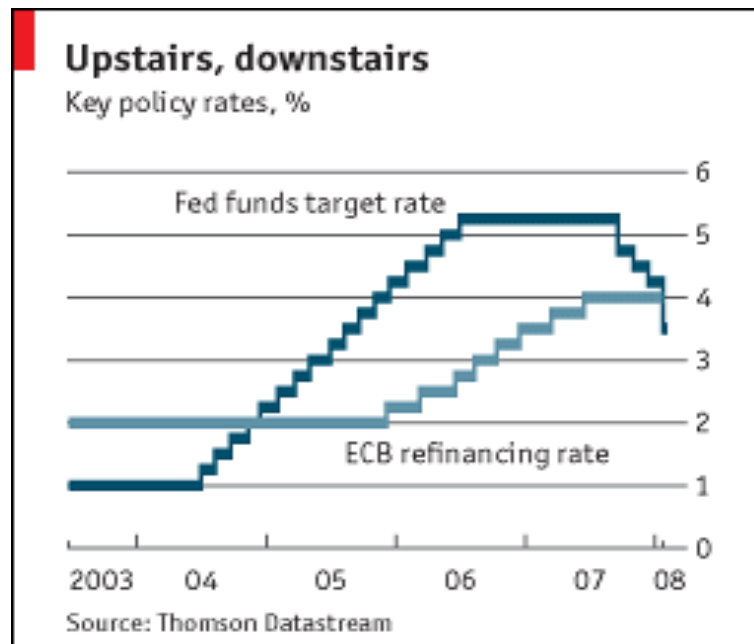
GLOBAL CHALLENGES

- **Uneasy times**
- **China on the move**
- **Russia – with less sound fundamentals**
- **No sacrifice please, we're Europeans**
- **USA – needs to see the world as it is**
- **Challenges ahead**

Uneasy times

22 January: Fed cuts interest rate by 75 bp to 3,50 %. Panicking? Ar a wise move?

- Halt free fall in stock prices
- Support the housing market
- Inflation on the decline
- Unemployment on the rise



Bush and Congress agree on 150 billion dollars in fiscal stimuli. Checks to be sent out in April/May.

300 dollars per American.

Less of an effect since this is a one-shot transfer.

But "un-Bush" like profile – equally much to everybody

Underlying real problem: American households are living beyond their means. Okay from 1999 to about 2006, as emerging economies needed to build up reserves of foreign exchange. Now they have accumulated about 4000 billion dollars in reserves.

SWFs emerge. Creditor nations will no longer suffice by accumulating debt instruments. They want equity. And also strategic investments, cf. China in Africa and in Brazil.

Underlying real problem: American households are living beyond their means. How come?

China runs trade surpluses, exports exceeding imports.
Buys Treasury bills, keeping interest rates low in America.

De Gaulle: The US has an exorbitant privilege –
can issue debt in own currency

Low interest rates make for higher prices on homes.
Innovative agents push loans on households, based upon
inflated house prices. Consumption is kept up.

And so it goes.

August 2007 and things start to unravel.
Subprime crisis.
Households have problems servicing the debt.
Defaults on CDOs etc. also for banks abroad.

And last week, the world stock markets felt the heat

China on the move

Real econ growth of about 10 % per year since 1978

Deng Xiaoping, paramount leader of China from 1978 until 1992. Very pragmatic man:

"What we are embarking upon is not written in books."

"It does not matter whether the cat is black or white as long as it catches mice."

"It is glorious to get rich."

Jiang Zemin took over in 1992.

At the helm for ten years (with Zhu Rongji as PM).

2002 and Hu Jintao in charge (with Wen Jiabao as PM).

Orderly transfer of power.

Hu has five more years to go.

Surplus on trade balance more than 10 % of GDP

200 billion dollars (of 1.400 bn in total reserves) in a separate fund for more exiting investments than the accumulation of American Treasury bills:

- *stocks*
- *buying companies with cutting-edge technology*
- *mines and oil fields and other natural resources*

Politically – sort of democracy *within* the CCP (Chinese Communist Party)

- No acceptance of competing parties
- CCP "owns" the power to govern China
- What would you value most; Democracy or Rule of Law?

Rule of law possible without Democracy?

Enormous increase in productivity making room for

Increase in pay

Increase in profit

Lower prices

Legitimacy of CCP based upo econ growth

Jiang neclected "welfare" issues like public provison of health, pensions and education.

Also, the environment was not looked after

Hu Jintao – every day – talks about "Harmonious society", with such issues in mind.

Also, income distribution has become very uneven.
Corruption explains part of it.

Russia - with less sound fundamentals

Oil more valued and econ boost to Russia

- GDP from 200 billion dollars to 1200 in eight years
- Close to 500 billion in reserves. SWF in the making.
- Command over pipelines for oil and gas makes for power
- Russians are back on the global stage. Proud.

Vladimir Putin in 2000: To rebuild Russia at home so that it could regain its status as a great power abroad.

- But the political system has disintegrated
- Putin has become the new "tsar", not yielding his power
- Lacks Democracy as well as Rule of Law
- Population on the decline
- Alcoholism and Corruption are huge problems

No sacrifice please, we're Europeans

European economies are doing reasonably well

- Unemployment down
- Inflation under control
- Econ growth at a reasonable rate
- Getting to grips with carbon emission trading systems

But into uncharted waters

- Will the ECB follow Fed in lowering the interest rate?
- Housing prices on the decline
- Public sector finances have improved, but hard to get rid of your garbage in Napoli
- And too strong euro – RMB should share more of the burden of a weaker dollar

Henry Kissinger in interview in WSJ in November 2007:

The real difference, Mr. Kissinger interjected, lay in "what government[s] can ask of their people."

It is because "European governments are not able any more to ask their people for great sacrifices," he argued, that they have so readily opted for a "soft power" approach to so many foreign policy issues.

This will, of necessity, make it harder for Europe to reach a consensus with the U.S.

USA – needs to see the world as it is

Elizabeth Economy, Foreign Affairs, 2007:

”By 2020, China is expected to have 130 million cars, and by 2050 -- or perhaps as early as 2040 -- it is expected to have even more cars than the United States.”

Why ”even”? After all, three Chinese for every American

The US takes three fourth av excess global savings.
For how long can that continue?

Other countries start buying up real assets in the US
How come that comes as a surprise?

USA concerned about SWFs

- Wants to have "code of conduct"
- Increased transparency
- But what would the US have made of it were these SWFs of American making?

NYSE: Value of about 18.000 billion dollars

US government debt, about 9.000 billion dollars

SWF at about 2.000 billion dollars, and growing fast

Joseph S. Nye Jr., former assistant Secretary of Defense, now dean of the Kennedy School of Government:

"If you treat China as an enemy, China will become an enemy."

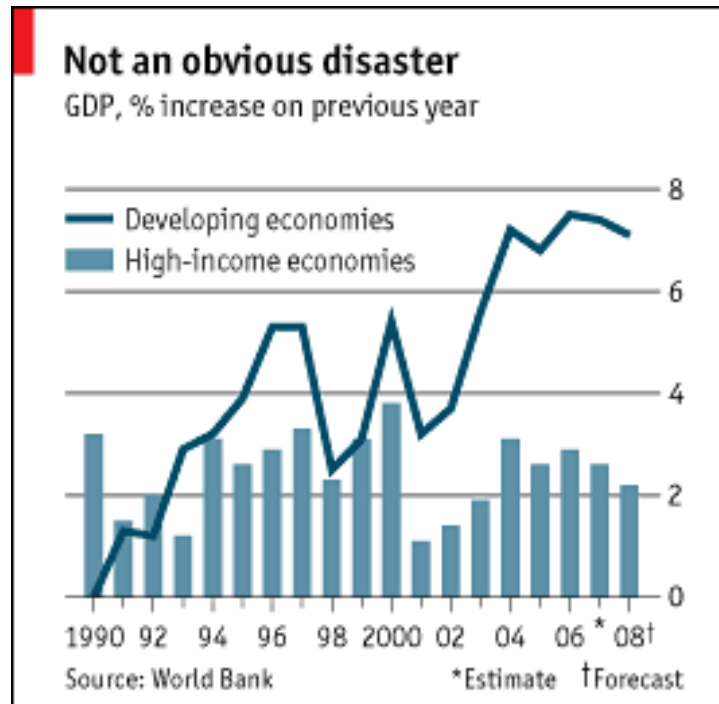
John Ikenberry, Foreign Affairs, 2008:

How to accommodate China as a rising power?
What kind of international order would the United States like to see in place when it is less powerful?

Challenges ahead

1. Avoid protectionism

George Soros in FT 23 January 2008: “So, the current financial crisis is less likely to cause a global recession than a radical realignment of the global economy, with a relative decline of the US and the rise of China and other countries in the developing world.”



And Soros continuous:

“The danger is that the resulting political tensions, including US protectionism, may disrupt the global economy and plunge the world into recession or worse.”

2. How to make China a global player enjoying the existing liberal world order?

So far, China has reaped huge benefits from it, cf. Deng Xiaoping's slogan:

Open up and Reform

Member of WTO in 2001, to keep China on track.

3. Device fair schemes to deal with global problems

“If one takes per capita emission of greenhouse gases rather than overall emissions, it will be the developed countries paying taxes on their exports.”

What is fair?

- Ownership of clean air based upon previous pollution?
- Or have each person on the globe having property rights to equally much clean air?

4. Keep cool

To make one litre of biodiesel you need one thousand litres of water. The problem of pollutions overrides the problem of water shortage?