Institutions, Society and Markets: Towards a New International Balance - International Industrial Strategies - Asia

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Introduction

Dr. Sugranyes (Chairman of the Fondazione Centesimus Annus - Pro Pontifice), members of the board, Excellencies, Panel Chair Ing. Federico Flack, distinguished guests, a very good morning to you.

Let me begin by congratulating the Fondazione and its Scientific Committee: the theme you have selected for this Conference is as bold as it is singularly relevant. I speak to you this morning, not as a professional economist (which I am not), but as a practitioner who has spent most of his professional life involved in cross-border transactions with or within the Asian region.

There are indications of an incipient global recovery - the International Monetary Fund´s ("IMF") latest forecasts project 2012 global growth at 3-1/2% - down from 4 % in 2011. Absent major unforeseen crises, it sees global growth of 4% in 2013. It expects the:

1. Euro-area to go into a mild recession in 2012.

2. Advanced economies, as a group, to grow by 1-1/2% in 2012 and 2% in 2013.

3. Real GDP growth in emerging/developing countries to slow from 6-1/4% in 2011 to 5-3/4% in 2012, before rising to 6% in 2013.

That said, even the most optimistic of forecasters would characterize the state of the global economy as ***fragile***. The major economies in particular are in the midst of serious challenges.

The Need for Re-Balancing

For much of the last two millennia, Asia accounted for the bulk of global GDP – with China, India and Japan representing the largest regional economies.

The industrial revolution saw "the West" achieve dramatic economic dominance – a position generally expected to revert to Asia in the foreseeable future. An Asian Development Bank ("ADB") study indicates that, barring the unexpected, Asia is on track to boost its share of global GDP to 52% by 2050, while increasing per capita income six-fold, in the same period of time.

According to the IMF:

1. Asia accounted for 60% of the global population and 24% of global GDP on a PPP basis in 2010.

2. More specifically, China, Japan and India represented 19%, 2% and 17% (a total of 38%) of global population and 14%, 6% and 5% (a total of 25%) of global GDP respectively.

3. The EU and the US accounted for 11% and 4% (15%) of global population and 15% and 19% (34%) of global GDP respectively.

Globalization and the growing integration of national economies have contributed greatly to increased global prosperity – ***at least on an aggregate basis***.

The World Trade Organization ("WTO") indicates that the ratio of international trade of goods and services to global GDP has risen from 8% in 1947 to about 25% at present.

It is therefore evident that the debt and fiscal problems of Europe, the US and Japan (representing 51% of global GDP, in nominal terms) affect us all.

At the same time, the massive and painful restructuring that took place following the 1997 Asian financial crisis has paid handsome dividends to the region. In large part, this accounts for the region's relatively strong position – this time around. Asia now accounts for the largest proportion of global international reserves.

Quite apart from purely financial considerations, there are strong demographic reasons supporting collaboration: properly trained, the young populations of the Indian sub-continent and Southeast Asia represent valuable human resources juxtaposed against the aging populations of Europe, Japan, Korea and even China. Duly employed, they represent valuable new markets for everyone to benefit from.

Rising economic tensions (between the US and China/the West and Asia) notwithstanding, it is evident that:

1. Simplistic prescriptions for global re-balancing like: a major revaluation of the RMB; a drastic increase in the share of consumption in the Chinese GDP; a drastic reduction in Chinese savings to finance dramatic increases in consumption or (similar) changes in the Brazil, Russia, India, China ("BRIC") and other major emerging market economies, <u>will not work</u>.

2. Based on the United Nations Conference on Trade and Development ("UNCTAD") data:

    a) The US accounts for 45% of global deficits while China accounts for 25% of surpluses.

    b) Re-balancing between the US and China alone would:

        i. Have a deflationary overall global impact

        ii. Be insufficient to unwind the global imbalances.

        iii. Leave important trade imbalances in some countries with very modest reductions in the trade surpluses of Germany, West Asia and North Africa.

3. A real solution will require a consensus "Roadmap" for fiscal, structural and political reform in Europe, the US, Japan and complementary policies in China, India, East Asia, West Asia, Africa and Latin America. Given the complexities of current geopolitics, a herculean task indeed.

In addition to the traditional economic arguments, we are confronted by the fact that - over three centuries after the industrial revolution - and after dramatic technological and economic progress, poverty remains at unconscionably high levels. Consider that:

1. Almost half the world – over 3 B people – live on less than $ 2.50/day.

2. More than 80% of the world's population live in countries where income differentials are growing.

3. The poorest 40% account for 5% of global income.

4. The poorest 20% account for 1.5% of global consumption.

5. The richest 20% consume 76.6%.

6. The world's middle 60% consume 21.9%.

7. The gap between the richest and poorest countries has risen as follows:

    a) 1820: 3 to 1

    b) 1913: 11 to 1

    c) 1950: 35 to 1

    d) 1973: 44 to 1

    e) 1992: 72 to 1

Against these stark numbers are the difficult illegal immigration problems of the US/Mexico, Europe/Africa and many other locations. ***In the long run, pockets of prosperity cannot subsist in a "sea of poverty".***

The New Economic Paradigm

Through various economic/financial crises, we have learned that the "invisible hand" is not the perfect allocator of resources in an economy, let alone the global economy.

1. An economy that values/rewards publicly-listed company performance on the basis of quarter-to-quarter financial "results", provides strong – often irresistible - temptations for Managements to sacrifice strategic objectives of the enterprise/society in favor of parochial short term gains.

2. Legitimate economic/financial innovation is often subverted by greed-driven excesses (e.g. the Latin American sovereign debt crisis arising from the recycling of oil surpluses in the 70s; the US Junk bond/LBO market collapse of the mid-80s; the U.S. Savings and Loan crisis of the late-80s; the 1997

Asian financial crisis; the US sub-prime crisis of 2008; the European Sovereign Debt crisis of 2010).

3. The temptation of masking underlying fundamental economic problems (e.g. fiscal, leverage, savings/investment, balance of trade/payments) with prolonged periods of "accommodative" monetary policy is difficult for politicians and policymakers to resist.

On the other hand, faced with an inability to finance expensive entitlement systems, a number of developed economies have experienced reduced private investment, declining economic competitiveness and ultimately fiscal and credit crises.

Models from the right and the left have failed. On the other hand, the absurdity of doing the same thing, and expecting a different outcome, is apparent. And yet, that is what "tinkering" with the periphery of the existing neo-classical and socialist economic models - without addressing its fundamental assumptions - amounts to.

In this context, let me propose the underlying premises of a different economic model grounded on Christian, social and ethical economic principles:

1. The objective of society/government is to:

   a) Achieve sustainable and inclusive growth

   b) Create an environment where people can work, satisfy their needs and realize their human potential.

   c) Eliminate poverty.

2. Property ownership:

   a) A legitimate, even necessary, human right.

   b) Is inextricably linked with corresponding serious fiduciary responsibilities.

   c) Is not absolute. It is justified by the use of assets for the benefit of the individual ***and*** of society as a whole.

3. The attainment of sustainable and inclusive growth requires:

   a) Food security.

   b) Proper management of the environment.

   c) Access to quality education and relevant skill development.

   d) Meaningful employment opportunities.

   e) A change in the private enterprise paradigm from "***maximization of shareholder value***" to "***maximization of stakeholder value***".

Some Ideas

Coming as I do from a region blessed (and challenged) by vast human and natural resources, I will focus my industrial policy recommendations on related sectors.

I propose three specific themes based on an evaluation of demographics, long-term comparative advantage, sustainability, as well as maximization of "global stakeholder value".

1. <u>Agro-industrial and extractive industries</u>

The traditional business model of a number of these enterprises involves relatively minimal processing of the raw materials at source. Many of the value-added processes of the operation are conducted "close to the market".

Accordingly, much of the commercial benefit remains with the (usually) large, multinational developed economy-based processor/distributors. This is justified by their substantial investment in brand development, distribution, processing capacity and technology.

The idea is to:

a) ***Formulate a plan for agro-industrial (e.g. tropical hardwood, coconut, oil palm, sugar, coffee, etc.) and extractive industries (mining) to re-locate value-added processing close to the raw material/labor source, under joint-venture terms that are equitable, transparent and sustainable***.

b) ***Invest in reducing poverty/creating new developing country-based demand***.

2. <u>Health Services</u>

Rising health care costs in the developed economies represent a serious, continuing fiscal challenge. In the meantime, the quality of health care in a number of lower-cost, developing countries has improved substantially.

The idea is:

a) ***For the appropriate developed country health care regulators to***:

i. ***Determine which type of services can/should be outsourced to qualified, lower-cost health care providers in selected developing countries***.

ii. ***Enable their institutions/providers to establish joint-venture out-sourcing arrangements with their duly accredited developing country counterparts (the former to provide, if necessary, technical support and administrative oversight)***.

iii. ***Accredit health care institutions/providers in selected countries – subject to the former complying with the latter's***

standards - and providing the necessary commercial benefits to the outsourcing institutions.

iv. ***Offer their citizens the "option" of securing the "covered" services from the said accredited institutions – sharing the benefits of lower cost delivery***.

b) ***To initially focus on: uncomplicated procedures and services; non-medical (e.g. nursing, care-giving, laboratory and diagnostic services, etc.) and senior citizen services***.

3. <u>Business/Knowledge Process Outsourcing</u>

Labor market rigidities have compounded rising wage costs in many developed economies – hence the need for the difficult labor restructuring policies being pursued in Europe and the U.S.

The idea is to:

a) ***Develop a "win-win" formula that would allow major developed country enterprises to effectively outsource non-core operations to lower-cost economies at or better output standards***.

b) ***Establish joint-venture partnerships among developed economy-based educational/training service institutions and their selected developing country-based counterparts for purposes of optimizing research and training services***.

c) ***Deliver superior results by utilizing state-of-the-art learning management systems ("LMS") and information and communication technology ("ICT") platforms***.

It is contemplated that the three ideas will be executed in some form of joint venture designed to align the economic interests of developed and developing country-based partners.

A final consideration has to do with the evolution of public companies and international capital market development. To the extent that ownership of enterprises listed in major global stock exchanges becomes increasingly international (directly, or via pooled vehicles like mutual funds and other similar investment vehicles), such companies have become ***transnational***.

The nature of the proposed initiatives are eminently compatible with the desire of such transnationals for the development of new markets and the achievement of sustainable long-term growth.

Execution

I propose the following implementation program for the abovementioned initiatives:

1. Select a few specific projects – on the basis of where one can get compatible developed and developing country sponsor-partners.

2. Secure the support and sponsorship of credible independent institutions (e.g. leading management schools and development finance institutions).

3. Solicit the endorsement/support of key developed/developing economy-based industry "players". Such support may consist of:

   a) Financial
   b) Technical/Advisory
   c) Organizational/ staffing
   d) Data and research resources

4. Assemble capable multi-disciplinary teams of professionals (technology, finance, community development, labor and governance experts) ***led by seasoned industry/management experts***, to implement the selected projects and formulate the implementation plans.

5. Ensure that important, albeit sensitive, issues (e.g. intellectual property, management, governance, brand equity, etc.) are comprehensively and practically addressed.

6. Document the recommendations and actual results of the Project.

7. Solicit the appropriate private and public sector support for the Projects that are found viable.

While not a panacea, the proposed exercise may be an important step in achieving an equitable and sustainable global re-balancing. It is an exercise premised on the often-forgotten truth that we ***are*** interdependent.

Thank you