

**NDN**  
**Under Secretary of State Robert Hormats Address on Global Economic Challenges**  
**November 15, 2010**

Many thanks, Simon. And, first of all, before I begin let me thank you for the very kind introduction. I didn't know we were both Jumbos either. But I also wanted to take a moment to thank you for your leadership, your intellectual leadership and the very dynamic efforts you've made not just in terms of developing new ideas but really pushing them through the political process in Washington.

You have taken some of the very best ideas that you and Rob Shapiro and others have generated. You and Rob have and not just talked about them but focused a great deal of public attention on them and helped people to understand that we have to make some major changes in this country if we are going to cope with and respond to the changes that are going on in the global economy.

Coming back from the trip I just made, where I was in China and then with the president in Korea and in Japan, and having frequently visited various parts of that region, we're engaged in a competitive world that is unlike any that we have experienced in the past. There are more countries that are more competitive in more products and more services than ever before in world history.

I think that a lot of Americans are perhaps not as aware as they should be about the fact that United States is going to have to make some enormous changes domestically in order to compete in this dramatically changed environment and to ensure that living standards for our own people continue to improve even as other countries through their own methods and through their own policies are advancing living standards for their people. But this is a much more competitive environment. As Lincoln said, "Because the circumstance are new we have to think anew and act anew," and I don't think we are doing that adequately in this country.

Simon and his team have really been beating the drums on that point and many others for a very long time. I commend you for that and I think that from the point of view of at least my role in the State Department, our collaboration with you and Rob, our working together, our various conversations over the last weeks, months and year, since I've been this job, are very, very valuable to me.

Let me just start out by saying I did have the opportunity very recently to participate in the G-20 and the APEC Summits. I will in my remarks describe some of the issues that I see before us and the way in which the United States is going to have to respond. One of the things we clearly are doing through the G-20 and other entities is to try to shape the world's economic future in ways that serve both our national and the global interests. That involves utilizing the G-20 but groups like APEC and other international groupings.

But I also think that while we focus and while my job primarily focuses on the international economic policies of the United States, it is at least as important and perhaps even more important what we do at home. We are not going to have an effective international economic policy unless we have an effective domestic policy. And we are not going to be the

world's leader for the indefinite future in any area unless we can address our economic challenges at home in a more effective way than we have over the last 20 years. Let me just touch on a few elements of that.

First, we have to put our economy and our budget on a sound financial footing over the medium-term. Without that, we will not have the resources or the domestic capability of dealing with our domestic problems or meeting global challenges-- and this is something that goes back for a very long time. Years ago I wrote a book called the *Price of Liberty* and it was about how we pay for our wars. It started off with Alexander Hamilton where (all American history it seems starts with Alexander Hamilton); the point that was made by Hamilton and by many others during that period and beyond, that strong national finances are necessary, indeed, critical for a strong national security policy and a strong foreign policy. That is as true today as ever and, therefore, over the medium-term – as President Obama has emphasized repeatedly - we have to put our finances on a sound footing.

Second, we have to dramatically strengthen our educational system. If you look at what's going on in Asia and other parts of the world, education is job one. Korea is a very good example. The Koreans emphasized this while we were there. In the 1950s, Korea was a destitute country; poverty level was very, very high. The GDP per capita was the same as many of the poorest countries in the world at that point. What did they do? They concentrated primarily on education. What was the advice they got from AID and other foreigners? Don't spend all this money on education because there are no jobs for these people to get once you've given them a good education. What are they going to do? Give them a good college education, high school education, there are no jobs, what are they going to do?

The Koreans thought about it in entirely different way. They said, if we educate our people then our people will be able to compete in the world. Companies will engage; businesses will start basing in the Korean economy on the fact that we have a strong educated workforce. The Koreans did this and the rest is history. But education was at the center and it is the center of what is going on throughout the Asia, enormous emphasis on education.

Engineers, scientist, mathematicians, physicists, and others, we are seeing large numbers come out of Asian universities; and these are talented people. They strengthened the business environment and the competitive environment. We're engaged in a very competitive race with these countries. If we don't maintain a world class educational system today, it will be virtually inconceivable that we will maintain a world class economy 20, 25 years from now. This to me is going to be a very critical element. If we can't strengthen our educational system today, a positive economic outlook in 20, 25 years is going to be much more difficult to sustain.

Third is modernizing our infrastructure. I don't need to tell anyone who has been to Asia that Asia is modernizing its infrastructure at a very rapid rate: roads, airports, ports, telecommunication, and Internet connectivity at a very rapid rate. In fact, on Thursday I'm testifying before the Senate Foreign Relations Committee on what other countries are doing to modernize their infrastructure to move people, to move goods and to move ideas and information around. This to me is very important.

In the 1950s, '60s and '70s we put a lot of money into our infrastructure and we have been living on the basis of that rather than putting sufficient new sums into modernizing our infrastructure. We've got to modernize our infrastructure and broaden it and not just the roads and highways but information. Look at Korea, 96 percent of Koreans have access to high speed Internet - 96 percent - considerably greater than in most industrialized countries including our own.

And then we have to deal with the energy issue through clean energy development both to reduce dependence on imported oil and other source of energy and to deal with our environmental issues. A robust energy policy is critically important for a whole range of reasons that the president had stressed and many other have stressed as well.

These are the kinds of things that we need to do at home. And there are a number of others. And we don't have the abilities to do this in a relaxed fashion anymore. If there were no competitive countries in the world, we could say, well, we'll put this off. We'll kick the can down the road. We can't do this because others are rushing ahead at a very rapid rate and are going to be more competitive because of the investments they are making to these areas. The very best of our efforts internationally to improve the global system would be jeopardized if we fail in addressing these critical domestic issues in the United States.

The other thing that I want to talk about is new patterns of cooperation in this new global economic geography that we face today. We are going to have to continue to work with our global partners to ensure that the evolving international economic system serves our interests and those of our major economic partners.

I want to make a more general point. First of all, the key from our point of view is finding new ways to actively engage with other countries. We don't have a world of blocks anymore where you can simply operate within one alliance. We obviously have alliances like NATO and others. But increasingly, you have a number of major players who are not part of any alliance with the United States or anyone else and we have to engage with these countries on an individual basis - India, China, Brazil, Russia.

We have to have a much more diversified kind of diplomacy, where we work with these countries individually and engage them in a very intensive way. And that means things like the Strategic and Economic Dialogue with China. We have a similar presidential commission to deal with our relations with Russia. We need to find more and more ways of dealing with these major players both within the Group of 20 and other groups of this sort, but also on a very robust bilateral basis.

Let me talk about some of the changes that have taken place in the world economy that necessitate a new way of addressing global economic challenges. I'll just touch on them very briefly.

One, as I mentioned, is the new economic geography that we face. One of the fundamental characteristics of the world economy is that it is indeed a multi-polar world, highly interdependent. And that interdependence has moved very rapidly. But the international governance process, the international process of coordinating among countries and developing

common policies or common approaches, has simply not evolved as rapidly as has the degree of interaction among countries or interdependence among them.

Emerging economies today are, needless to say, enormously powerful commercial players. They are also increasingly important financial players and they are developing new technologies. A lot of new technologies are emerging from these countries. We have to address, as I mentioned, all these challenges. But it is also important to realize that many of these countries have agendas that are different from those of the handful of industrialized countries that were the governing - the steering committee - of the global economy in the 1970s, '80s, and much of the '90s-- that is the G-7 or the G-8. These countries had very strong economies and were relatively rich countries, that is to say they had a very high GDP per capita.

The new group of countries that's playing a powerful role are also major players in the global system but their domestic circumstances, their domestic requirements, their domestic priorities are very different from those of the countries of the G-7. Let's take China for instance. China has population of 1.3 billion people, but its per capita GDP is only about one-seventh that of the United States. China's GDP ranks 92nd on a per capita basis in the world, Brazil is 72 and India's is 121.

What's this telling us is that while externally they are very powerful players, they see themselves as developing countries and they have in many cases, internally, a developing country policy agenda. What do they do to improve living standards for lower income people? How do they develop their agricultural sectors? How do they deal with the whole range of issues that developing countries face?

On one hand, they are major global players and they need to assume more responsibility for the global system commensurate with their growing economic influence and power. On the other hand, when they look at themselves they don't necessarily see themselves as strong economies in the sense that we do looking at them from the outside. They see a lot of development problems, environmental problems, resource problems, problems of health differences. In the case of China, between rich parts of eastern China, the large cities of eastern China and the Yangtze and Pearl River Delta where GDP per capita is relatively high and western China, where there are a lot of very poor people living at or perhaps just above the poverty line. So they have a very different domestic agenda and that in turn affects their world agenda.

Second, financial flows are very different today from in the past. If you look at financial flows in the past, they have traditionally been from industrialized countries to developing countries. That's changed. In 1990, the current account of emerging and developing countries as a group was close to balance. In the year 2008, the developing countries together - mostly the BRICs - had a combined surplus of nearly \$800 billion.

Emerging market reserves now dwarf those of industrialized countries. The developing countries reserves, again, mostly the large developing countries are more than \$6 trillion up from only \$350 billion in 1990, while advanced economy reserves have risen from about \$450 billion in 1990 to only about \$2 trillion today. A lot of capital, instead of going from developed to

developing countries, is going the other way. The United States is the major importer of capital from emerging economies, China being one obvious developing country supplier of capital but also many countries in the Middle East, Russia and the other countries that have surpluses.

The other point that is interesting is that in the past sovereign debt issues have been primarily within the purview of developing countries-- Mexico, Thailand and Russia have all had major sovereign debt crises in the past. This problem now seems to be a bigger issue for industrialized countries. Debt as a portion of GDP for emerging economies is now half of what it is for industrialized countries. This is a very big shift.

Third, we've just come through the worst financial crisis since the Great Depression, and that has produced enormously high levels of unemployment for a lot of countries, and devastated the savings of a lot of people. It has also generated considerable skepticism in the United States and other countries about the benefits of globalization. This was beginning to occur even before the financial crisis, but it is now at a higher level because of the financial crisis. There are lots of doubts in this country about open trade policies, about whether we should continue to further liberalize trade and even about some kinds of foreign investment in the United States a porcupine-ish attitude, shall we say, towards certain kinds of investments in this country.

So, one of the great challenges that the United States faces is to demonstrate first of all that our economy is capable of returning to its previous resilience. We also have to show that our domestic political system is able to make the hard choices needed to put, as I discussed earlier, our financial system on a sounder footing, to produce a robust energy policy, to revitalize infrastructure, to reform education, to devote more resources to R&D and to pursue a proactive trade policy. Unless we are able to deal with our domestic problems, we are going to find it much harder to convince our people that we should have an expansionist, proactive international economic policy.

On the other hand, we need to recognize that what's happening around the world means that if you look at where growth is going to occur and you look at where jobs are going to take place here, it's going to be through companies that are able to access foreign markets. If you look at the growth in the United States versus, say, growth in China, growth in Brazil, growth in India, these are the countries where there are enormous growth opportunities.

We have to look at our economic future in part in the context of finding ways of identifying opportunities to sell abroad, strengthen the capability of our companies to sell abroad, equipping our workers with the skills needed to produce goods to sell abroad and having a trade policy which opens markets around the world so that we can obtain access to a larger portion of the market share around the world.

As it turns out in Asia, our exports are growing as you would have expected, because markets are growing. But as a share of the markets of Asia, our percentage is actually declining. Why is this? It is in part because in many cases in Asia, other countries have negotiated free trade agreements. Free trade agreements give their products a better market access to the economies of these countries than countries that do not have free trade agreements with such countries. That means our share of the overall market declines over a period of time. In the

fastest growing of the world, that is a setback which is going to be harmful to jobs and harmful to growth in the United States.

There is another area that is worth touching on and that is the intensification of global interconnections. Our daily lives are more and more dependent on computers, the Internet, electronic transmission of funds, smart grids. All of them face major threats. Global connectivity makes us all far more efficient and many of us far more prosperous, but it makes us all more vulnerable as well. There are issues of cyber-terrorism, cyberpiracy, assaults on personal data and threats to national security information. These are all dangerous 21st century threats to our economies, our technological leadership and our security.

And then there are these other sets of changes and threats to the global common space, if you want to put it that way, which we need in order to make the global economy to work-- free flow of goods and free movement of vessels in the high seas. And we need to have security of air travel. We are all vulnerable to measures that interrupt the flow of goods on the high seas through piracy, through disruptions of air traffic and through terrorism. A whole range of these global common spaces are important to our interdependence, but also are very vulnerable to catastrophic acts of terrorism, through piracy, through non-state actors primarily, and more is required to strength cooperation amongst the various state actors to deal with these potential threats. The same is true in financial markets, where financial markets are interconnected; we need to find ways of enabling our countries to work together efficiently in these areas.

So let me touch very briefly on the few areas in which we are trying to strengthen global cooperation to address this new set of global challenges.

First of all, we need to demonstrate from the point of view of the United States and other countries that the United States is still able to play the role of a global leader. We need to demonstrate this because if we are not able to lead, there are very few countries that are willing or able to take a strong global leadership position. We've seen this time and time again. Every trade negotiation since World War II has succeeded only because the United States is willing to take a leadership role. This is not to say that other countries are not important. They are. The United States cannot do any of these things itself, but it needs to take a global leadership role if we are going to make progress in virtually any area.

We also have to demonstrate to those in the rest of the world who now, particularly after the financial crisis, believes that other models of economic organization, political organization, are the right ones. We have to demonstrate that democracy, free market capitalism, a strong entrepreneurial environment, the free flow of information, diversity, inclusivity are all the key building blocks of economic growth. There are other countries who don't necessarily accept this and don't necessarily believe our economic model is the right one anymore, particularly since they have seen what is happening in the financial crisis. So we have to demonstrate that the way we conduct our economy and the way we conduct our politics is going to lead to a greater degree of resilience and an ability to come back from current economic difficulties and address the challenges we face.

We also have to realize that we need to find new ways of addressing the new group of emerging economies - principally, but not only the BRICs - and that means new forms of partnerships as I alluded to before. We recognize that these countries are strong competitors. But we also have to begin to see them, as I mentioned earlier, as potentially important and growing markets. To win these markets we need to develop a robust policy of export promotion, pursue trade agreement, as I mentioned earlier, recognizing that while there are those who wanted us to shy away from or reduce our role in the global system the answer or at least one of the key answers to dealing with our domestic problems is to enhance our activities in the global system, to create new opportunities in the global system.

We would be making a mistake of historic proportions if we saw the challenges from China, from India from Brazil and other countries as an excuse for pulling back from the global economy. Turning inward would be an enormous mistake; instead, we need an outward looking policy that takes advantage of opportunities in the global system. We need to develop not only new trade opportunities which we need to do, and the president has a very strong national export initiative to this, but we also have to see these countries as potential partners in helping to address some of the other challenges of the global economic system.

One of the examples of this is development assistance. The United States has played a very active role in providing development assistance for decades, but now we should see these new economies as partners in the process of providing development assistance. There are some very good examples of that.

The United States works closely with Brazil in helping poor countries to develop biofuel programs. We have Brazilian experts and American experts working together to help poor countries to develop their biofuels. We've just agreed with the government of India for the United States and India to work together to help other countries to develop agricultural programs, particularly in Africa. India has a lot of skills in the agricultural area. India and the United States, less we forget, were partners in the Green Revolution.

If we can see these countries as opportunities not just for trade but for partnerships in areas such as global development, it will enhance the process of global development. We don't have to assume as large a share of the burden. Burden sharing is important; responsibility sharing is important. We also have to make sure that we continue to work with these countries to avoid the development of an environment in which competition for markets, for energy, for capital, for food or for water are seen as a zero-sum game. If we begin to think of the world in terms of the zero-sum game - we win, they lose; they win, we lose - then we will not be able to develop these concepts of cooperation. And they need to look at it the same way.

We also need to avoid circumstances in which individual countries engage in systematic efforts inconsistent with global norms and global rules to enhance prospects for their domestic economies or their companies violate international rules at the expense of others. One of the keys to an orderly global system is to ensure that it is a rules-based system. If countries engage in a kind of an economic nationalism which enables them to avoid playing by these international rules, then we will have a breakdown in the system and I think that would be harmful. Not only

would it cause enormous harm to the United States, but it would damage the integrity of the global economic system on which we all depend-- and it also could have serious security and economic consequences.

China, for instance, has a number of policies that they together call “indigenous innovation” which force the transfer of intellectual property to Chinese companies from foreign companies or restrict Chinese government purchases of products if they are not using indigenous technology, so that they discriminate against companies that import technology to China or have ownership of that technology and don’t transfer to Chinese companies. Well, clearly that kind of policy, that kind of nationalistic policy is antithetical to a rules-based system, harmful to American companies because the strength of the United States is to produce innovative new products and services.

We want to be able to enable our entrepreneurs, our investors, our researchers to gain the benefits of the time and effort and the resources they put into innovation. Therefore, enhancing rules on intellectual property protection, in my judgment, is critical not just to the stability of the global system and to the strengthening of the rules of that system but also to our economic future. That depends on our ability to sell high-end, knowledge-based products around the world. If we find intellectual property protection breaking down – an improper enforcement - that is a direct threat to our own economic future. Therefore, while we cooperate with these countries in many areas, we have to be very strong in enforcement of rules in this area and in a number of other areas as well.

Let me now turn to a few of the institutions that we are using and then I will stop and we can discuss any of these ideas that you would like.

One is the Group of Twenty. That has met over the years in Washington, in London, in Pittsburgh, Toronto and just recently met in Seoul. The leaders have charted over the course of that period of time a response to the global financial crisis. I think that while there still issues to be resolved, it’s quite clear to me at least that the international financial crisis would have been a lot worse had these countries not worked together in the context of the G-20.

The meeting in Seoul was important. I’ve seen the press on it, but I think that it was fundamentally important in that it strengthened our international agenda of continuing the process of recovery, of global rebalancing, of working together with countries around the world to make sure that the global economic system or at least the major powers in that system work together.

Summits are not designed to achieve miracles. I’ve been to them since the Rambouillet Summit where I was working for Henry Kissinger as a junior economic assistant. Rambouillet was the first of these G-Summits. It started out with six and then went to seven and then eight. Now we have a new group: the G-20. They were never meant as a way of resolving all the world’s problems in one day and a half session. What they were meant to do was to enable countries to work together to establish a common sense of direction where they would attempt to move ahead to deal with the problems at hand. The G-20 was able to do that.

It also enables us to work more closely with China, Russia, Brazil, India, South Africa, South Korea and other countries to make sure that while we are not all moving exactly in the same pace all the time, with exactly the same policies, the common direction is the same. I do think that this was an opportunity to do that. I was able to go to the meeting and listen in when the leaders talked. And I was fortunate enough to have participated in bilaterals that the president had with other heads of states and governments in Yokohama at APEC.

My view was the G-20 and APEC together did advance American interest substantially because they strengthened the commitment of countries to the notion that if you're going to have a sustained growth in the world over the medium-term, you are going to need to have balanced growth. We made progress and reinforced progress in that direction. That was one of the fundamental things and that will enhance our ability to create jobs in the United States because other countries will rely less on exports to us to continue their growth.

They will realize that they can't grow by depending on the American consumer as much they have in part, because the American consumer has to rebalance his or her balance sheet after the financial crisis. These countries have to pursue more domestically-led growth models at home, which take some pressure off of our market and will give us the opportunity to sell more in their markets. The direction that was established in earlier summits was continued at Seoul. That will be helpful to the United States over the medium-term.

The other element that I think is important is that the surplus countries have agreed to reduce their imbalances to more sustainable levels. That is part of this global rebalancing. The argument in the press was that we didn't get as much detail as we wanted. Well, it's very hard to get details at these meetings, but the direction was very clear and I think we are going to move. We are going to see movement in that direction. If you look at the Chinese five-year plan, it focuses on strengthening domestic demand and domestically led growth and reducing reliance on exports.

We are also developing within the context of the G-20 robust proposals on anti-corruption which avoids putting American companies at a disadvantage, energy cooperation to reduce inefficient energy subsidies, development cooperation including food security, financial inclusion which means that people and other countries benefit more from economic growth than before and have greater access to finances. Other possibilities for cooperation include infrastructure development which is very important. American companies are quite good at selling their infrastructure projects; infrastructure is being developed all around the world. It's a big opportunity for American companies and fiscal governance and tax policy.

Let me just elaborate on another issue for a moment. One of the things that we have been very impressed by is the efforts that countries have been making around the world, in Africa, in particular and also in Latin America, to strengthen their domestic tax systems to reduce tax avoidance to enable them to have a broader-based tax system, to generate more resources internally that they can in turn use for their development and to make sure that when they do collect taxes, and that they are very transparent about the uses of government revenues.

All of this can be very important in terms of the fairness of their tax systems and the way their people see their tax systems-- the way people look at the question of tax governance. Do their people see their tax systems as fair? If they see them as fair, they are more willing to pay. If they see the money being used effectively, they are more willing to pay taxes and in turn they can generate more revenues and those revenues can help them to strengthen development if they are used in a right way. So, these are the kinds of things that he plans to discuss in the future in greater detail.

Then the APEC meeting which took place in Yokohama, this was, another important event in the sense. It demonstrated that the countries of the Pacific Basin which include the East Asians and also countries on this side of the Pacific, the United States, Canada, Mexico, Chile and a number of other countries also participated. This was very important to demonstrate that these countries can work together to enhance trade across the Pacific.

These countries are working together to reduce barriers across the Pacific. The United States will host the next meeting in Honolulu in 2011, President Obama's hometown. Of course, Honolulu is important because it's right in the middle of the Pacific and it sort of brings together both sides of the ocean.

There are other groups, as I mentioned earlier. We're using the Strategic and Economic Dialogue with China. The U.S.-Russia Bilateral Presidential Economic Commission, the U.S.-India Strategic Dialogue. And we obviously have a lot of groups within the context of North America, such as NAFTA. So we are trying to find ways in which we can use these types of dialogues to reduce barriers but also to find ways in which we can work together internationally to deal with some of the global problems of trade, finance, energy and other difficulties.

The big challenges that we now face require global responses and the big question is whether governments can design new patterns of cooperation and new institutional arrangements to keep up with these challenges. If you look at the way the world responded after the World War II, there were no institutions at the end of the War. The ones that existed prior to the War simply were too weak or inadequate to deal with the problems of the era. And we saw what happened in the 1920s and '30s in the absence of global institutional cooperation.

So, our leaders at the end of WWII, led by President Truman, Secretary Acheson and Secretary Marshall, put together new institutions - the Marshall Plan, the GATT, the World Bank, the IMF - in cooperation with other countries. These institutions have been very valuable. Think how much worse the financial situation would have been two years ago if we did not have those institutions, if we did not have the WTO to avoid protectionism, if we did not have the IMF to provide the liquidity, if we did not have the World Bank to help the developing countries. These institutions have been very valuable and we need to keep them, modernize them, and strengthen them.

But we also have new sets of challenges to deal with new types of problems that people didn't dream off in the late 1940s and 1950s when these earlier institutions were established. We have energy issues; environmental issues; a whole range of new kinds of financial issues and, of course, terrorism. We have to find new ways of addressing these; these require new types of

cooperation. That means, in particular, finding ways of bringing new emerging economies into the global system.

In the 1940s and 1950s, no one would ever have dreamt that India, China, Russia and Brazil and others would be major economic powers. In fact, at that point, the Russians in particular - then the Soviet Union - and China were totally opposed to these global institutions. Now they've joined. The Cold War didn't end with World War III, it ended with these countries wanting to join the World Bank and the IMF and the WTO. They are now part of the system and the fact is that now we need to find ways of engaging them to a greater degree and encouraging them to assume increased responsibilities for that system and playing by the same global rules that have been so successful for the United States and for other countries and the global system as a whole. This, this is the big challenge.

I would just conclude by saying that we have to do two things. One is to address this challenge of bringing these countries into the global system. As they obtain the benefits from the system, they also have to assume greater responsibility for the system. The second is what I started out discussing; we in the United States need to rise to these global challenges. These are greater economic challenges coming from more countries than we have ever faced before and we have to internally adjust our way of thinking and adjust our way of making decisions and assume a greater sense of urgency about the need to respond to these new competitive developments.

We need to do both. We certainly need to do the latter which is to respond domestically. And if we do that successfully, we will have a greater degree of influence and legitimacy and capability of reshaping the global system which is also a very high priority of ours. So thank you very much and I am eager to take your questions.