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THE SHIFT OF WEALTH AND POWER TO ASIA

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This morning, through the curtains of my bedroom I saw that the sun had come up. It wasn't a surprise. I expected the sun to be there. I know and you know that our star, the sun will burn in several billion years. It is a matter of science. So I know there will be a day, sometime in the far distant future when the sun will not come up. But it's far beyond my time horizon so I can safely plan my life on the assumption that the sun will come up, even though I know it's a false assumption because I know at some point the sun will not come up. But, for me it's, safe. I can bet that the sun is going to come up.

But we have other suns in our lives. In the lifetime of virtually everyone in this room, the dollar has been the world's money. Oil has always been priced in dollars. Coffee, bananas, airplanes, anything sold in international markets is priced in dollars.

If you go to Tokyo or Dubai or Mexico City or Beijing and you say that your income is \$50,000 a year, people will have an idea of what \$50,000 a year is. If you say your income is 50,000 pesos a year or 50,000 pounds a year, people won't know as much. The dollar, people know. The dollar is the world's money.

All our lives, energy has been readily available and cheap and we've built a lifestyle around it. A suburban, motorized lifestyle on the basis of the assumption that energy is going to be there and it's going to be cheap.

Water. What's the first thing that happens when you sit down at a table in a restaurant? They put a glass of water in front of you. I don't like water. I prefer iced tea. I always tell them to take it away. They insist. They have to put a glass of water down. I don't drink it. They throw it away. The underlying assumption is that the water is there and it's cheap and so you give people water.

The Shift of Wealth and Power to Asia

All our lives we've been looking at the maps, at the globe and we've been looking at the boundary line of countries. The line between Canada and the U.S., the line between Mexico and the U.S. We also look at other lines around the world and we think of those lines as delineating nation-states that are more or less permanent. Belgians will be Belgians from now until eternity. Japanese will be Japanese from now until eternity.

All these are unthinking assumptions that we make before we begin our day. We plan our lives on the basis of those assumptions. All our lives the U.S. has been the world's biggest economy. America's been the world's richest country, the most productive country, the place that produces the most new technology and standards. What do we mean by standards? Well when we turn on our television sets, the broadcast has to be done according to a certain standard. But, here's a better example. We all use Windows. We can't use a computer without using Windows. Well, that Windows system that we use is based on an operating standard, the DOS operating standard, *set* in the U.S. Everybody in the world uses that Windows standard set in the U.S. So all these are assumptions that we make and we base our lives on these assumptions.

What I'm going to tell you tonight is that we are at a moment of enormous change. History goes along in fits and starts. Sometimes things stay the same. Think about the Tocu-gawa regime in Japan from 1600 to 1865. The Samurai had their swords in their belts. They had those funny hairdos and that's what they did for 265 years. Then Perry showed up in Tokyo Bay and you had the modernization of Japan. We are at one of those moments when the course of history is making a huge swing.

To put this in perspective, let me take you back in time. In fact, let me take you back about six hundred years to the year 1415 at which time the areas we now call China and India accounted for about seventy-five percent of global GDP. As I said earlier, we are accustomed to America being the world's biggest economy. But for most of the six to seven thousand years of recorded history, China and India have been the biggest economies. It is only in relatively recent times that the West has played an important role.

So in 1415, China and India are the world's biggest economies. There is no North America that anybody knows about. Columbus hasn't sailed yet; Cheng Ho, the Chinese admiral hasn't sailed yet. The Native Americans are here, but no one knows about them. Europe is known but it is small and insignificant and primitive.

An unknown European king, King John the First of Portugal, gathered his sons together to propose a raid on the North African Coast. One son's job was training. One son's job was to gather supplies and one son's job was to build ships. I don't remember the names of the first two sons, but the third son, the shipbuilder was named Henry (later called Henry the Navigator). So in August of 1415, the knights are gathered, supplies are ready, the ships are ready and the fleet travels down to into the Atlantic, double-backs through the straits of Gibraltar and captures the North African town of Ceuta which at the time is part of the Moroccan Caliphate that stretched from the Middle East to the Atlantic Coast of Africa. They captured this regional town and were astonished. They had never seen such wealth. There were more jewels, more silk, more gold, more everything than they had ever imagined, in the *provincial* capital of the Morocco Caliphate. And the question naturally arose,

“Where did you get come up with this wealth?”

And the answer was, “To the East.”

“Well, how do you get there?”

“Well, you slog across the Sahara, fight your way through Egypt and Syria into Mesopotamia, and then if you’re still alive, you are thrown in jail.”

So this didn’t look too promising. But Henry had an idea. His idea was, could you sail there? Could you get around Africa and get to the east by boat? So he went back when the fleet returned to Portugal and set up a base in Sagres, the far southern tip of Portugal. He gathered together all the great shipbuilders, captains, and map-makers of Europe to launch an effort to see if they could sail around Africa.

Think of going to India or China in the 1400s as going to the moon in the 1960s and think of Sagres as Cape Canaveral. And so Henry launched his captains down the coast of Africa. They invented a whole new type of ship, the caravel. They were light, shallow drafts and fast. Why those specifications? Because the most important cargo of these ships was information; information about winds and the tides and the coastlines. The goal was to get that information back to Sagres and send the next probe down the coast of Africa. If I can paraphrase Captain Kirk in Star Trek, Henry told his captains to “boldly go where no man has gone before.”

Henry’s captains weren’t too bold, actually. They tended to hug the coast. They took every excuse to turn around and come back, but eventually they got around the Cape of Good Hope, and eventually in 1498 Vasco da Gama made it to Calicut, India and that marked a *huge* turning point because the way to India was now open to the Europeans who had superior nautical technology. And so the story of the next six hundred years was that of the rise of the West with the age of European exploration and empire culminating in today’s American hegemony.

As recently as 1850, China was the world's biggest economy. In fact, some of my Chinese friends are fond of saying, "Clyde, you know, we, Chinese, have had one hundred fifty bad years, but now we're back." By 1950, China and India together had dwindled to about seven percent of global GDP while Europe and North America had become seventy-five percent of global GDP. So that six hundred years was a quick turnaround in terms of relative economic weight of the two parts of the world. Today, however, this imbalance is being corrected very rapidly. Already China and India account for seventeen percent of world GDP and are growing at ten percent annually. We are in the midst of a historic rebalancing. By 2025, China *will be* the world's biggest economy. China will be bigger than the United States. By 2050, India will be the world's biggest economy. The U.S. will be number four or five of the world's major economies at the time. So a huge shift is taking place.

I have been watching this all of my life, this process of globalization—as have many of you. Yet, I have to say that the full significance of what is happening didn't really strike me until about four years ago.

I was on my way to Shanghai and I stopped in Truckee, California on the northern end of Lake Tahoe to see my older son. He is a software developer and a big-time skier. Actually, I guess I should say it the other way around: he is a big-time skier and a software developer. So I stopped in Tahoe on the way out to ski with my boy for a long weekend.

Anyhow, we're sitting on the ski-lift in Squaw Valley, and he said to me, "Dad, how would you like to co-invest with me?"

Isn't that nice? My son wants to co-invest with me. Of course in this context, however, co-invest means it's *my* money.

"So what are we co-investing in?"

“Well,” he said, “There’s this snow removal company here in Tahoe that I’m interested in.” And I’m shaking my head. A snow-removal company?

“What in the name of creation is snow removal? Shovels or what?”

He said, “No. It’s a ski resort, and it snows a lot between October and May, and the hotels and the condos and the restaurants have to be plowed. This company has the plows and the contracts to do the plowing.”

“Do they make any money?”

“Oh, yeah, the guy makes enough money in six months that he takes the other six months off.”

“Sounds pretty good. Send me the numbers. Maybe I’ll put in a few bucks. But wait a minute. I don’t get it. You’re a software guy. Remember when you went to college, you asked me what to study, and I told you technology, because that was the future. I said you could write your own ticket. And you did it — the one time in your life that you took my advice. You did it. So yes, maybe I’ll put a few bucks in, but you’re a software guy. Why are we talking snow removal?”

In a tone of exasperation, he says to me, “Dad, don’t you get it? They can’t move the snow to India.”

That got my attention. I hadn’t been to India for a long time, for maybe twenty years. It wasn’t on my travel map. I thought maybe I should check it out. So I thought, I’ll go to Shanghai, continue on to India, and I’ll come back through Europe. So I did. Let me give you a few vignettes from that trip and others because I’ve now been living in India and China for the past five years. Not literally, I’ve actually been living in airplanes, but I spend a lot of time in India and China.

I did go to Shanghai and on that particular trip I met with a guy named Richard Chang. I mention him because I think all of us have this concept of China as a developing country. If you go to Wal-Mart, you know that everything in Wal-Mart is made in China. You go to the Gap and everything there is made in China. And so we have this notion in our minds, that China is a manufacturer of commodities products: textiles, shoes, toys and things like that.

And that fits. We believe this because we have been taught in economics classes a model of economic development we have this paradigm of development proceeding for countries that are poor with a lot of unskilled labor. So it's inexpensive. They begin by focusing on labor-intensive production, textiles and shoes and toys, where you need low-skilled and cheap labor, and then they gradually acquire skills and they move up the hierarchy of technology value added. So if we think of China of today as the location of choice for commodities manufacturing, Richard Chang is important for you to understand because he is the president and founder of a company called SMIC—Semiconductor Manufacturing International Corporation—in Shanghai.

I first met Richard in the early 1980s when I was the Under-Secretary for Commerce in the Reagan administration and I was the chief U.S. negotiator with Japan. Some of you may remember that at that time, the American high-tech industry, particularly the semiconductor industry, was locked in battle with the Japanese.

I was the U.S. negotiator and Richard was the head of manufacturing, globally, for Texas Instruments. Richard is actually from Shanghai. He got to Taiwan in 1947-1948, grew up in Taiwan; went to NYU, got his Ph.D. in electrical engineering at NYU, and went to work for Texas Instruments for a number of years. I got to know him in that context. While I was active in Fujitsu and Toshiba in the late 80s, Richard went back to Taiwan and

became one of the founders of the Taiwanese semiconductor industry. And then in the mid 1990s he raised some venture capital and established his new company, SMIC, in Shanghai.

So I spent a day with him in his factory in Shanghai. I will say this, it is not Intel, it is not the absolute cutting-edge of technology, but it's pretty darned close. Moreover, it is meant to be the low cost semi-conductor foundry of the world. It is 10 percent below the cost of Taiwan, which is 15 percent below Korea, which is 15 percent below Japan and the U.S. My point is this; this is a very high-tech facility. Richard's company is very high-tech. So it is a mistake for us to think that somehow China is going to make toys and that we, in the advanced countries like the Japan and the U.S., can move to higher ground, that we're going to be the leaders in technology, research and development, and so forth. Richard is coming along *really* fast.

From there, I did go to India. I have to say I was blown away. I am on Intel's Advisory Board. Intel arranged a number of meetings for me in India, one of which was their own operation. Intel has two thousand Ph.D. electrical engineers in Bangalore designing absolutely the latest chips. In fact, the Intel team in Bangalore is teamed with a group at Oregon, so when Oregon sleeps Bangalore works, and when Bangalore sleeps Oregon works. Both teams are right at the cutting edge. Intel is working 24/7.

From there I went to the Apollo Hospital in Hyderabad. I'm looking at this audience and it's a nice audience. There are students here and that's nice to see, but I see some grey hairs, and I'm guessing that some of you have reached the stage that I have where you are not getting through the tennis courts as fast as you think you should. You need that knee looked at or maybe it's a hip or a heart valve. I don't know what your problem is, but I have a great answer for you. The Apollo Hospital will pay your first class round-trip airfare

from Newport to Hyderabad. I discovered a whole new export industry that I had never thought of existing. It is called “medical tourism.” It works like this: Maybe you need a new heart—you are in line, but you haven’t been able to get a heart yet—or you need a new hip or something like that.. I don’t know how it works in Newport, but there is an 800 number in New York and Washington D.C. to the Apollo Hospital. You call them up, book your trip. Airfare, heart, side trip to the Taj Mahal, private nursing care, all for about fifteen percent of what it would cost you here. The surgery done by board-certified U.S. surgeons, trained in U.S. medical schools. This is available immediately, covered by your insurance. This is a billion-dollar industry in India this year and growing about sixty percent annually.

Let me take you to another place. Last month was my wife’s birthday and I bought her a brand new Dell computer. My son is the techie. I can never get these things to work. So I get the computer, turn it on and couldn’t make it work. So I called the help line. When I call, I get this funny accent at the end of the line. So I ask him, “What’s your name?”

“Sam,” he says.

I laugh and say, “Your name is not Sam. What is your name?”

He says, “Okay. My name is Rajiv.”

“Rajiv, I bet, you’re in Gurgaon, aren’t you?”

“Yeah. How do you know?”

“Because I was there a couple of weeks ago.”

I went to a call center at the outskirts New Delhi. If you ever get a chance, you have to visit one of these call centers. You go there around midnight because they work on U.S. East Coast time. As you drive there, you quickly realize that this is a developing country. There are no street lights. The driver is slamming on the brakes every four or five minutes because he doesn’t want to hit a cow, an elephant, or other cars. Everything is on the road.

So you drive and drive and when you finally get to your destination it's like walking from the sixteenth century to the twenty-third century. Your destination is all satellite dishes and spotlights and optical fibers and Star Wars kind of technology. There are very dynamic people coming and going and the environment is almost like here, a university. There are young people, casually dressed, seemingly having a lot of fun. The call centers are divided into different sections. There is a Dell support section.

But on my particular visit, I was in a section of the call center known as the AOL Retention Center. What that means is that if you are an AOL customer and you are really fed up and you dial the 800 number to cancel, this is where your call goes. If you think you are calling to cancel, you are mistaken. You are calling to be retained. The job of the people in the retention center is to convince you that you really like AOL and you want to sign up for another year.

So I was talking to some of these young people—they are all young people in the AOL Retention Center—in particular to this Indian girl named Nishat, who explained to me how she loved this job and that she was taking a year off from her university studies to earn some money and to have some fun, because, she said, “This is really a fun job.”

Anyhow, while I was talking to her, a call came in from Bob in Camden, New Jersey. I used to live in Camden, New Jersey. I thought, “I’m going to listen to Bob. Maybe I know Bob.” So I pick up on the other line, and Nishat answers. She has a screen name. Her screen name is Megan.

Bob is really upset; believe me he is really upset, he does not want one more second of AOL. Nishat/Megan says soothingly, “Bob, my name is Megan. I know you’re really upset, and I want to help you as much as I can. Just tell me a little bit about what you do

with your computer. Do you use Instant Messaging? Did you know you could do that? Have you ever tried that? I could offer you this.” She got this whole list of offers.

She gets him talking, and he’s calming down, and he’s beginning to get into it. She’s reeling him in like a fisherman reels in a fish. He’s just about at the boat, and he hesitates. With perfect timing, perfect intonation, and perfect accent she says, “Bob, trust me. Believe me, it will be okay. You can call me if it doesn’t work.” Bob jumps right in the boat and signs up for another year of AOL.

I said, “Nishat, that’s really good. What’s your success rate?” She said, “Oh, about 80 percent.”

I’m thinking she must be one of the most valuable people that AOL has. So I ask her.

“Where did you live in the U.S.?”

“I’ve never lived in the U.S.”

“Come on. You must have. Where did you get that ‘trust me, believe me’ line. You did it so well?”

“Oh, those are the power words they teach us in our accent-neutralization classes. I can do it in Canadian English too.”

On that particular trip I came back through Germany and I was on Lufthansa from New Delhi to Frankfurt. It just so happens that on the Lufthansa flight they had a copy of the latest “Der Spiegel,” the German newsmagazine. And the cover story was “Can Germans work forty hours a week, again?”

As you know, a couple of years ago, Germany went to thirty-five hours work week. But now there’s this debate in Europe as to whether they should increase the working hours per week. I read that and I thought, “This is incredible. I’m just coming from two countries

where they work forty hours *a day*.” The disconnect between that cover story and what you see in those countries, India and China, is enormous. But anyhow, let me give you a couple of the other pictures, snapshots.

Recently, I went to see my tax accountant, a small local firm in Bethesda, Maryland. I am talking taxes and just making small talk. My accountant knows I travel a lot so he says, “Have you taken any trips recently?”

“Yeah, I’m just back from India.”

“India,” he says, “we just moved our whole back office to Bangalore.” He says, “Your taxes are going to be done in Bangalore. We’re going to save eighty percent.” And I’m thinking “How much of that am I going to get?” But it struck me because this is a small, local tax firm and *they* are moving their back office to Bangalore.

Not too long after that, I was in New York. I went to see Steve Roach, the chief economist at Morgan Stanley. I happened to notice a lot of empty offices. I said, “Steve, what’s the matter? Is business bad?”

“No, no, no. Business is booming. We moved half of our staff to Bombay.”

So my point is that we are in the midst of a *huge* revolution. We’ve been accustomed to thinking of developing countries as doing low-technology manufacturing. In fact in the 1970s, 80s, and much of 90s learned economists argued in academic journals that the movement of U.S., Japanese, and European manufacturing out of their homes bases to Asia was nothing to worry about. Because the argument was that manufacturing, after all, is dirty and sweaty and polluting and we should let it go because we, in the advanced countries, are going to be a services economy and we’re going to do the investment banking and sophisticated design, and development, and finance, and consulting. We’re going to do high-

tech, we're going to do software. We're going to go to Silicon Valley and we're going to do venture capital and we'll start the Google and Yahoo! and so on.

I thought of some of these argumentations a couple of weeks ago. I had an auto accident in Washington and—I guess I was babbling much more than normal—they rushed me to the emergency room and they did a brain scan. Two interesting results from the brain scan. The first and most important is that the brain scan established *definitively* that there *is* a brain. The second is that the brain scan was being read online in Bangalore. So I'm in Washington, D.C. and my radiologist is in Bangalore. I think of my doctor as the guy down the street. I don't even think of my doctor as the guy in Newport. I think of my doctor as the guy down the street. But no, my doctor's in Bangalore.

This represents a huge shift away from all the traditional analyses and theories on which we've based our policies and planned our lives around in terms of globalization and international economics. It has enormous implications, both very positive and some very challenging. The positive is dramatic. Hundreds of millions of people in Asia are being lifted out of poverty. There is now a middle class in China of maybe two hundred million people, almost as many as in the U.S.; In India, it may be one hundred million people. There is *hope* and what you feel when you travel in India and China and elsewhere in Asia is tremendous energy and optimism and enthusiasm. People have hope and they think that they and their children can be successful and they're driving for it. It's very powerful thing and very uplifting when you feel it.

We are also seeing a phenomenon that I call "shrinking the world" and my friend Tom Friedman calls "flattening the world." But the point is the Internet, FedEx, and UPS have negated time and distance. So anything that can be done digitally or electronically — software, call centers—can be done anywhere in the world, and delivered anywhere else in

the world in two seconds, speed of light. Newport to Shanghai in two seconds, Washington to Bangalore in two seconds. And even if you are making physical products that have to be physically delivered, FedEx or UPS can take anything anywhere in the world in maximum, thirty-six hours, usually more like twenty-five hours. So for all practical purposes time and distance have been erased. And what that means is that people who in earlier times—and by earlier times, I mean fifteen or twenty years ago—were in knowledge centers or universities like this were not easily linked with similar centers in India or China or Indonesia, or wherever. Now they are. So all the knowledge centers are being tied together and there is the potential for rapid acceleration of innovation and the advance of technology is being multiplied. That has to be a very positive thing.

But having said all that, we also have to look at how this engine of globalization is working in terms of its long-term sustainability. If you look at that question from a number of different angles, you realize that we are all—not just here in North America, but elsewhere around the world in Asia, Europe, and so forth—facing enormous challenges.

Let's just pick one challenge that is pretty dramatic. I talk about the five or six "ends." One of them is the end of the dollar, one the end of oil, one the end of water, one the end of cool, and the last one is the end of people.

The end of the dollar. I said earlier the dollar is the world's money. But if you look at how the global system is operating today, you realize that this global economy system is terribly distorted. I mentioned Tom Friedman's book *The World is Flat*. Yes it is, but it is tilted. It is tilted because, in this whole system, there is *one* center of demand. There is *one* center on net consumption in the world: the United States. All the other major centers of the world, Europe, Asia, China, Japan, India are net sellers. The Americans are the greatest consumers of all time. In fact, we are such great consumers that we consume more than we

produce. This year, we have a trade deficit of around \$900 billion. So we are consuming around \$900 billion more than more than we produce or about 80 percent of GDP. Last year, American households spent \$500 billion more than they earned. When my wife goes shopping she tells me she has to support the global economy and I tell her she's doing a great job. We are the buyer of last resort in the global economy. We are the ultimate engine of global growth. It is *our* demand that is powering much of this growth around the world.

We have *no* savings. We are in negative saving territory in the United States. Households are negative savers. The government is a negative saver. Corporations in the U.S. have savings, but their savings isn't enough to offset the "dis-saving" of the government and households. So the U.S. is a net "dis-saver."

The flip side of this is that the rest of the world, but particularly Asia is pursuing a policy of export-led growth. Their policy is to promote high savings rates, high investment rates to maintain the dollar at artificially high levels against their currencies, to export as much as they can, particularly to the U.S., and to accumulate trade surpluses.

Let me give you examples of the savings rate. China has a savings rate of 45 percent of GDP; almost *half* of every Yuan produced in China is saved. Singapore is at 58 percent, Korea at 35 percent, Japan at about 20 percent. There are enormously high savings rates in Asia. And this is channeled into investment and exports, particularly to the U.S.

And you look at that and say, "What's the problem?" The Americans are having a party. Americans are living above their means. We are not earning our standard of living. I know you think you are working hard, but you are not earning your standard of living. You are living above your means. And it feels great, right? We have low interest rates. We have low unemployment. Housing prices are dropping off a little now, but they've had a great run for the past five years. The Dow is hitting record territory. So what's the problem? And if

you look at Asia, they've got high grow rates. They're moving people from the farm to the factory. They're lifting people out of poverty. They're affecting transfer of technology. They're happy. We're happy. So what's the problem?

The problem is that if you consume more than you produce, if you buy more than you earn, you have to *finance* it. If you are an individual, you have to go to the bank or the credit union or take out a home equity loan or something, but you have to finance it. If you are a country, you have to finance it as well. And what we have right now is a world in which the world is swimming in dollars. The central banks of the world are drowning in dollars. How does that work?

Think about it this way. If you are Japanese or French or German or Mexican and you want to buy oil, you have to pay for your oil in *dollars*. But your currency is not dollars. If you're Japanese, it's the yen. So you have to *make* something in Japan and *sell* it to somebody to get dollars. Then you take those dollars and buy your oil. But if you are America, you print the dollar. You don't have to make anything. You don't have to provide any services. All you do is call up the U.S. Government Mint and you say "Run off a few more of those green pictures of presidents, those dollar bills. Just print them."

So what we are doing in the Unites States is we are taking green paper and giving it to the Venezuelans or the Saudis or the Nigerians and we get oil. Or we take green paper and give them to the Japanese and get Lexuses or to the French and get Brie cheese. But we pay for it in *paper*.

We are the *only* country in the world that can do this. No other country in the world can do this. But what's happening is that the world has a lot of green paper. The Japanese have a trillion pieces of this paper, \$1 trillion of reserves. China is crossing the trillion dollar mark this month [November 2006]. Even little guys, guys like Hong Kong, have a lot of

paper. Hong Kong has \$200 billion. Singapore has \$250 billion; it only has 3.5 million people, but its central bank has \$250 billion pieces of this green paper in their reserves.

Now after a while, if you are the central bank of China or Japan and you are getting all this green paper you remember that this is a claim on future American income. And then you say to yourself, “Are these Americans really going to pay this off?”

What do big countries do when they are in debt? In fact, what do little countries do when they get in debt? They inflate. So if you are holding all this green paper in Saudi Arabia or China or Japan, you have to be thinking that there is a risk. And at some point the risk of holding becomes greater than the risk of getting rid. Once the Japanese or any of the main players begin to feel that there is a risk for holding dollars, the potential for a huge dollar fall is enormous. When I say a huge dollar fall I’m thinking of a fifty to seventy-five percent fall. Today the yen is at 120 for the dollar; think 60. The dollar is 1.25 to the euro; think 1.7. That kind of shift is potentially in the future.

In fact, if you are OPEC or Saudi Arabia and the Gulf States, why do you want to keep accumulating dollars? Maybe you should price oil in something other than dollars. Maybe you should price oil in euros or in a basket of currencies, partly in euros, partly in dollars, partly in yen. You would want to hedge your bets and not put it all in the dollar. This would be a logical thought if you were the finance mister of Kuwait or Qatar or Bahrain. And, believe me, they *are* thinking of this kind of possibility.

So we are feeling pretty good in the U.S. The unemployment is low. Interest rates are low. The economy is going at a pretty good clip. However, just remember our economy is on life support. Every single day we have to have \$3 billion net capital inflow to keep this thing going. That \$3 billion comes from three places: the Central Bank of China, the Central Bank of Japan, and the monetary authorities of the OPEC countries.

I have this vision of Hank Paulson, the new Secretary of the Treasury. He gets up early in the morning and while he's shaving he's thinking, "Let's see. What do I have to do today? It's my wife's birthday. I'll tell my assistant to get flowers. Oh yes, I have to find \$3 billion *again* today. Where am I going to get it? Well, the Chinese will probably give me a billion. The Japanese will give a billion. I don't know about the Saudis. OPEC has been talking about cutting oil production. What a mess!"

That's what Hank Paulson has to do every single day. So that's where we are. So one major shift that we're facing is a shift away from the dollar. Once the world doesn't use the dollar as its money, the United States *cannot* run a trade deficit. There has to be a huge shift in production pattern and global supply pattern.

The second point is the end of oil. I won't dwell on it too much. Obviously we are at a point where the "easy" oil has been found. There is a lot of oil out there. We are not going to run out of oil, but the easy, inexpensive oil is pretty much here and it is diminishing. If you look at the North Sea, those sea fields are diminishing. The major fields in Mexico are diminishing. There are new finds. We just had a big new find in the Gulf of Mexico at *six miles down!* It is much harder to get this stuff from six miles under water than from the Mexican fields right now. So even though there is a lot of oil there, and in Canada with the Tartan fields, this is expensive oil. And even then, it is clear that the trend is to greater dependency on the Persian Gulf. With India and China coming along as major, growing economies with major demands for energy, that dependence on the Persian Gulf is rising very rapidly. So one of the things that is happening is that the current dynamic of globalization driving along this growth is driving us to the end of the dollar. It is also driving us to much more expensive and much less reliable energy. This has enormous implications both geopolitically and for our own lifestyle.

But if you think energy could be a problem, it pales into insignificance when you think about water. We think that maybe the next big war will be triggered by competition for energy. The next war is much more likely to be a fight over water. The Yellow River does not reach the China Sea. The Yangtze is drying out and salting up. The Rio Grande does not reach the Gulf of Mexico. The Nile Delta is moving upstream and becoming saline. Most of the world's major water sources are under pressure. And here we get to the impact of global warming. Obviously, temperatures are rising and we are seeing a retreat of the glaciers. The glaciers in Peru are projected to be gone in twenty years. They are Peru's water supply. All the great rivers of Asia—the Yellow River, the Yangtze, the Irrawady, the Ganges—come out of the glaciers in the Himalayas, but they are all retreating. When you think of the Middle East, you think of terrorism or the Palestinian-Israeli conflict, but what's really interesting is that when you fly over the Middle East and look down, there are dams being built in all the rivers. The fight in the Middle East is very likely to be about water. The days when you would go to a restaurant and the waiter puts a glass of water at your table may be rapidly coming to an end. So that's the end of water. Let's talk about the end of cool.

Global Warming. The global temperature has risen over the last hundred years by three degrees Fahrenheit or one and a half degree centigrade. It doesn't sound like a lot, but it has triggered the melting of the polar ice cap, the rapid melting of the Greenland Ice Sheet, and the melting of the Permafrost in Alaska and Siberia. There are receding tree lines and snow lines around the world. At the rate at which we are putting carbon dioxide in the atmosphere and on the current track of rising temperatures we are very likely, by 2050, to have another degree rise in temperature. The last time the earth had this kind of temperature was four million years ago when sea levels were eighty feet higher than they are today.

So let's suppose that by Herculean effort we immediately implement the Kyoto agreements. We immediately take draconian measures. We put in hundreds of nuclear power plants and we stop burning coal. Let's say we manage to stabilize carbon emissions at their current level. Even at their current level, we're going to see something like a fifteen to twenty foot rise in sea levels over the next thirty to fifty years. So Newport will be under water. Singapore: under water. Hong Kong: under water. Even if we take fairly dramatic steps, many of the world's major cities and living areas will be under water in a relatively short period of time. In fact somebody asked me recently this rhetorical question: Which country is going to be the next superpower? The conversation went like this:

"China?"

"No."

"India?"

"No."

"Russia?"

"No."

"Brazil?"

"No."

"Okay, who?"

"Canada."

Let me explain why. The polar ice cap is melting, so shipping in the future will be via the old Northwest Passage across the North Pole; Canada will control shipping the way Egypt controls the Suez Canal. The Gulf of Mexico will be uninhabitable with frequent, violent hurricanes. Florida will be under water, so will New Orleans. The whole Gulf Coast will be under water. The Sun Belt of the United States will be very hot. Because of the cost

of energy, air-conditioning will be prohibitively expensive so people will move north. The agricultural belt of Iowa and Nebraska—the bread basket of the U.S.—will be too dry and too hot. People will be moving north to Canada. Canada, of course, does have potentially as much oil as Saudi Arabia, and it has a lot water. So Canada will have the water. It will have the oil and the shipping lanes and people will move there. They'll take technology with them to Canada as they move. Canada is your next superpower.

I admit it is a little hokey, but it makes a point. It makes another point as well. I don't think any of the boundaries that we currently look at are immutable. What are the chances that the U.S. in extremis would annex Canada? We are already talking about building fences along our southern border. Think about other borders around the world that are less friendly than those.

So we are looking at enormous shifts and changes that are going to demand much different thinking than we are accustomed to, much different politics than we are accustomed to. The United States is not going to be the dominant, hegemonic power. It will be important, but will not be the hegemonic, dominant power that it has been. We are going to have to find ways to make global institutions work. We are going to have to find ways to deal with these existential challenges coming at us.

This could all sound very serious, and it is. But it is not, in my view, hopeless. In fact, I think there are a lot of reasons to be optimistic. Sometimes people ask me “Can America survive?” or “Can America maintain the American Dream?” I respond that people should look at this game of globalization as a game of bridge and ask themselves whose hand they'd like to play: China's hand, India's hand, the E.U.'s hand or America's hand? I would take America's hand any day. I think the American hand has more trumps and more high cards than anybody else. But if you play bridge, you know that it is possible to have

really good hand and still lose—I do all the time—If you play the cards badly. And right now I would argue that we in the U.S. are playing the cards as badly as it is possible to play. But that doesn't mean we have to keep playing badly. We can change the way we play. We can read the rule book or get some coaches. Moreover, it seems to me, that we have the potential in Europe, Japan, Asia, and everywhere else to join forces.

Let's take this water problem as an example. The biggest obstacle in my view, to China's further development, is water. And to solve that problem will require dramatic changes in China's production model and technology. *We* have that technology or at least we have the potential to develop that technology. The potential for cooperation is great if we get our act together and go down that path.

Let me close by telling you one final story. This is about a climber in California. California has guys who climb sheer rock walls. They put chalk on their hands and climb up these vertical rock walls. I've tried it and I think I have the wrong chalk. My hands don't stick.

This guy was climbing El Capitan in Yosemite and he was just about to put his hand over the top and he slipped. So he's falling and he's thrashing about and finally at the last minute he manages to grab a branch. He's holding with one hand and it's bouncing up and down. It's one thousand feet down to water and rocks. He's not really a religious person, but this is a serious situation. So he looks up at the sky and says,

“Is anybody up there?”

To his utter amazement, a big voice booms out and says, “Yeah. I'm here. What do you want?”

They guy says, “What do I do?”

The voice says, “Jump, of course.”

Clyde Prestowitz

The guy looks down and it's still a thousand feet to the water and the rocks. So he looks back up at the sky and says, "Anybody else up there?"

Well, *we* need something else. We need a new plan and that is the job of the young people in the audience.

Thank you.