

Richard Rosecrance speaking at the Dupont Summit:

Thank you very much. Well, it's not quite clear whether we're in favor of Atlantic Union now or later or indeed at all. It seems to me that one of the ways of looking at this huge problem is to say there are stages in the development of the international economy and the international polity that goes with it. And to think we can jump suddenly from 193 separate states to a united world government is too great a jump. We've tried that before and the only thing we've got is thin degrees of regulation, thin degrees of commonality, no tariff negotiations – we know the Doha Arrangement has failed. We haven't succeeded in providing single currencies for the world, and the notion that we'll somehow leap from this 193-separate-sovereignty universe which we now have and which John Williamson very carefully and accurately described as a world of national sovereignties – to think that we can move from that world to one in which we're all united, I think, is naïve in the extreme. And therefore, what do we do in between the 193 separate sovereignties and perhaps the unification of the world. I think Streit would have been happy to have the unification of the world if he could, but he recognized that was not going to take place, or at least not going to take place right away.

Now, if you look at Martin Woolf's article in Wednesday's *Financial Times*, he points out that countries suffering a trade imbalance cannot indefinitely stimulate their economy through deficit spending to sustain demand. Sooner or later international willingness to absorb government paper and liabilities will reach a limit, and of course that limit applies particularly to US government paper and liabilities. At that point, international economics must be in some measure rebalanced with far stronger international balances as a counterpart of smaller domestic deficits. This is something we're going to get to ultimately, if not in the next year or so. At this point, when a rebalancing takes place, surplus countries, including China, must spend, spend, consume, and inflate their economies in order for their to be balance in the international realm. This is exactly what John Maynard Keynes was worried about in the scarce currency clause of the Bretton Woods Agreement in 1944. The United States would not act, he thought or was worried about, as a responsible creditor power and hence had to be at least in the short term discriminated against under the scarce currency clause until it increased demand for overseas products.

At the moment, not only China but Japan and Germany consume too little and invest too much. And of course Japan combines this with an artificially depreciated currency, as China does as well. The RMB is far undervalued. These policies, though pursued nationally, throw the burden of adjustment onto deficit countries where they cannot ultimately be sustained. The United States and Britain, as Woolf pointed out, then may well go broke. And when they fail to buy more goods from abroad, they will then bring the rest of the world down with them. Now, how do we adjust the situation? Well, in an ideal world of getting agreement from 193 countries, we would have free trade, currency use would be freely fluctuating, capital would be fully mobile, and there would be no problem adjustment. We are not, however, in such a world, and we will not be in such a world for a very long period of time.

Under these circumstances, together with the failure of the Doha negotiations, what can deficit countries do? They can seek currency unions or preferential tariff zones, exactly the proposal that John Williamson investigated in the 1980s, in which to sell their goods so that the essentially mercantilist strategies of the surplus nations are submerged or vitiated to some degree within a free trade arrangement. If one cannot dismantle the mercantilism, then one avoids it by forming a customs union, one that then allows people to be inside the tariff barrier instead of facing mercantilism outside. This means that the United States and Europe have a reason, at least on a short-term basis, to consider a broader customs union. The Angela Merkel proposals of 2006 which were only mildly taken up by the United States in the TEC negotiations would involve, if consummated, something like 50 to 60% of world GDP. If you say the EU with now 17.5 trillion and the US almost 14 together they constitute over the 30 or so trillion which is more than 50% of world GDP today, which is around 54.3 trillion. And of course, a union of those two huge economic conglomerations would also be a higher percentage of great power GDP – about 43 trillion.

Now, there are so many reasons to think that the two should get together. As a proportion of Internet users, the US and the EU are now more than 50% of the world. As a proportion of the countries that people try to get to because they consider them to be “the place to be” – that is where are migrants aiming to go – they are more than 50% of the total. In terms of R&D expenditure, tertiary education, all of those things, it is the US and Europe that are still calling the tune. But I think one of the key things to point out, and this is where I would agree entirely with John Williamson, is that a unification of the US and Europe in economic terms would not be exclusive. It would tend to draw the rest of the world in – much more effectively than the WTO negotiations on finance would do. Japan, for example, could not long manage to sell its exports to its major markets and remain isolated from a NAFTA arrangement of something of that kind. And if Japan eventually joins, China cannot be far behind. But the key thing here is instead of trying to get 193 countries together to reach an agreement to do this, you start out with building blocks that get bigger and bigger as the trading partners are added progressively to the unit. This is an incredibly important thing in world history because if we look at least at European history as being an example of world history, the balance of power has always been regarded to be the vital mechanism of order in the Western world. But this would be a world in which power, instead of repelling, would be getting to attract other power.

Secondly, this argument takes on additional force when you consider the corporations which already constitute that world. Increasingly, there are economies of scale for industry. Of course in the United States today one doesn't even bother going to the Princeton Institute for Advanced Study; it's been entirely surpassed by the Complexity Institute at Santa Fe, which of course focuses on economies of scale. According to Bryant, Arthur, and many others from that institute, industries like civil aircraft, autos, software, finance, insurance, even conventional arms, are largely made up of two or three or four places in which those things are manufactured. And of course there is a diminishing number of firms. How many auto companies today – as we look at those Detroit people, now not on their separate jets, but sort of eating humble pie by coming up in compacts – how many of those people can be efficient in the long term? Even on the

world market, are we talking about ten companies or only five on a world basis? Remember in the year 1900 there were 200 auto companies on a world-wide basis. To deal with industrial concentration, then, states also have to be more concentrated. The world market is still much larger than the largest state, and in order to get a grip on that market, that market has to become greater.

Clarence Streit wrote, "Politics can be separated from the machine no more than can civilization. The machine's nature is such that to use it or to make the most of it, men need more of the world than they needed before its invention." Still true. To do that work well, or to exist in an increasing number of cheap machines today one needs the whole planet. We will not get that in one sudden move. We will it only in bites.

The logical first step is the US and Europe, but such a consolidation will not rule out others nor should it be limited, I think, to arrangements of democracy alone because sooner or later China and Russia will have to find some place in it. So I think that a proposal for a NAFTA has to be responded to in terms much more substantial than that of the TEC.

The third point, of course, the United States particularly, is that the US does not have an answer to the growth of China. It cannot match China in terms of vertical economic growth, and of course we know that major conflicts have occurred when two great powers have intersected on the curve of power. When Germany passed Britain, when Russia and Germany were nearing equality, those were the periods in which conflict occurred. We have to worry about that, I think, vis-à-vis China. How do we keep up with China, at least using short-term expedience? Chinese GDP, as we know, doubles every 8 years. US GDP doubles every 24 years. Unless the US merges with another great continental economy, it will not keep up. Horizontal growth is the effective response to the Chinese vertical challenge.

Now this will require a major change in American strategy. Mr. Obama has been against all this. But remember, when Bill Clinton came into the presidency, he was opposed to NAFTA. He rapidly changed his position, and Obama can do the same thing as economic growth makes it not only possible but also imperative.

Thank you. 50:20