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Brussels Forum

Economies in Crises, Societies in Transition

Mr. Craig Kennedy: So welcome back. After that very stimulating session on China and under the larger view in the opening of where Europe's going, now we are going to focus on economies in crisis. And as one of our innovations this year, we've asked Jean-Luc Vanraes, President of the Parliament of the Flemish Community Commission of the Brussels Regional Parliament to give the introductory remarks.

He was most recently served as the minister of finance and budget of the government of Brussels, very thoughtful and analytical perspective on the state of the current European economies. Jean-Luc?

Mr. Jean-Luc Vanraes: Thank you. I heard you had a lot of work already this morning. My focus will be today on the subsidiarity and we all know that we're witnessing a very changing society. We have increasing knowledge and Democratic participation. And this global

evolution comes with an increase of the urban population and it's about this, I want to highlight this evolution with a focus on Belgium and on Europe.

If you speak about Belgium, you speak about 11 million people, very small. Some of them, 60 percent living in Flanders, 30 percent (inaudible), 10 percent Brussels and 50 percent of the people are concentrated in cities. If you have the urban region of Brussels and the six biggest cities of Belgium, this represents 50 percent of the people living in the country. Actually, it's an example of what's happening in the world. Remember in 1900, about 10 percent of the people lived in cities and in 2000, we were about 50 percent and by 2025, we will be 5 billion urban dwellers.

As now, Brussels is a capitol. It's the capital not only of Europe, but it's a capital of Belgium and also of Flanders and we are confronted, as many, many, many other cities in the world, with a huge impact of its population growth. Just a small example, the last five years, we had about 90,000 people coming in from

outside, merely European people, 20,000 new Belgium inhabitants coming over. By 2020, we will have 240,000 more. What does that mean?

What does that mean? It means that we have to create jobs. It means that we have challenges, challenges about mobility, employment, education (inaudible). And actually the main challenge is maintaining or even improving the quality of life.

We all know that our cities are affected by economic crisis and it's true, for any of us to confess it--we do it in Brussels, but I think the other big cities do it as well. It's not possible, on our own efforts, to find a solution to all of those challenges.

We need to have a positive attitude. We know cities are a source of wealth, not only for our region, but also for our country. There are polls of attraction for tolerance and openness. They are agents of growth and centers of creativity. This is precisely why cities have become an important element in European decision-making. The search of civilian participation in the

European Democratic process has been strengthened as a result of the greater civilian involvement of the townspeople. This opens the discussion about who is taking the decisions and at which level. The question of who does what opens the debate about the core duties, the role of cities and regions in the contemporary Europe of the national member states.

Actually, I'm talking about subsidiarity and this question is not new. Aristotle already mentions the principals of subsidiarity. He's speaking about humans, humans as political entities. His idea is an idea of human kind, people living together in the (inaudible) city state. Urbanization has, for (inaudible) not only a geographical dimension, but also refers to the living together, the good life and the (inaudible). Urbanization is not only the geographical expansion of the urban fabric, but also the very real and very humane aspect of living together. Nearly 2,500 years later, the poet Dante did just the same thing in Italy. He lived in Florence, 80,000 inhabitants, the second

biggest capital in Europe after Paris in that time. And I can quote quite simply his (inaudible) which is quite clear about this. He says (inaudible) speaks about the society, creates for one and for one individual, for another the family, for another the village, for still another in the city, for another the kingdom and finally, for ultimate end by means of his heart, his heart which is nature, the eternal God brings into the being the human race in its totality.

So he already speaks about the problems of organizations of his city states. This brings up--we have a big jump in the 21st century and in the contemporary relations between European Union and the regions and cities and the place of local and regional autonomy and EU policymaking.

Let us be clear, the cities are becoming increasingly important and will in the (inaudible) gain status as crucial factors in European decision-making. So we must carefully think about how to (inaudible) these cities in European Democratic decision-making,

about how do we empower them effectively in European story. At present, the national member states take the decisions. They take decisions for the regions. This contrasts with the growing social and economic importance of regions and cities. The development of the regions and cities is, to me, an enormous challenge for the further developments of the European community. Cities are the decisive factor in European decision-making and this requires us to adapt European decision-making to fit this reality.

This is why regions are to work more closely together, hence safeguarding their economic interest. The classic structure of Europe, of the 27 member states with the regions and cities in the periphery, is, in my opinion, not the most beneficial structure to fit in. To fit in the new players on the European Democratic market, we must ask ourselves the fundamental question of how to organize the new Europe. I'm speaking about Europe, but I'm sure you are having the same questions wherever in the world. We must

foremost establish (inaudible) decentralization. I refer to what's said by the commentary of regions. Decentralization means all measures at the political level that the role of national territorial bodies in the national and European decision-making to be sacred and that results in the transfer of powers of the central government level to local and regional bodies.

We must not forget that citizens identify strongly with their region and city. Those regions and city and the cities represent a crucial counterweight to the increasingly international and therefore anonymous nature of labor markets and economic relations. I would also like to emphasize that decentralization and autonomy of European regions are ever increasing. It's a reality that we cannot ignore and we will have to take into account. Therefore, we have to strengthen local autonomy on the basis of democracy, civil proximity and decentralization.

I want to emphasize that I regret that because of the financial crisis, there is a tendency towards

greater centralization. This trend is based on the mistake and assumption that public service is always cheaper when in the hands of the central states. I think this is not the case. We should have enough confidence in our regions and cities that they will do well. I oppose the use of the present crisis as an excuse for further centralization of powers, decentralization without the required financial resources and for simplification, reduction or either elimination of certain national structures. This ultimately results in weakening of the regional and local democracy. It's also contrary to the European subsidiarity principal, which says that decisions of political and regulatory order should be taken at the level which is most appropriate to the objective pursuit and as close as possible to the citizens lives.

We see in Europe a certain separatist tendency. I refer to my own country where certain political parties defend the complete secession of Flanders as an independent region. I refer to similar tendencies in

Spain and maybe Great Britain. On the other hand, in other countries, the autonomy of the regions is questioned. Neither view holds any progress. I put forward an inclusive Europe with regions and with cities. Not a Europe of Nation States, not a European of the regions, I speak with the regions and with the states. We ought to develop a structure which allows the regions and cities to have a fundamental place in European parliament. I plead for the creation of some sort of European senate, a second chamber of the European parliament which is attentive to the problem of the autonomy of the regions and growth of European cities.

I also suggest to strengthen the dialogue between the European institutions and regional and local territorial authorities to the purpose of direct cooperation between regions, cities and municipalities and the European institutions.

Through this organized approach, I am convinced that we can build a better Europe, a Europe which will

be better mirror its first and foremost state color, and I'm speaking there about the European citizen. Thank you.

Mr. Craig Kennedy: Thank you so much. Now we are getting ready for our next session. We have asked one of our GMF board members, long-time moderator, someone that I think has been to every one of the Brussels forum. Is that right, David?

Mr. David Ignatius: That is indeed.

Mr. Craig Kennedy: David Ignatius to lead this discussion. We are looking forward to a very lively coverage of this topic. David, it's yours.

Mr. David Ignatius: So I think we should roll the video, as we say in Hollywood.

(video)

Mr. David Ignatius: So I'm David Ignatius, as Craig said. I'm a columnist for *The Washington Post*, but for these purposes, more important, a trustee of GMF. The broad theme of our discussions this weekend is fragility and that's nowhere more evident than in the

subject we are going to talk about over the next hour. Over the last five years, we have seen the global economy, but in particular the economies of the EU, the United States, Japan, the areas represented on our panel, under severe stress. There are different names that we give, the Great Recession, the Long Recession, but this has been a period of enormous difficulty all the more so because it almost seemed to sneak up on people unexpectedly.

In terms of politics, it's been a period of political polarization. I think it's safe to say in all the countries we are going to talk about, it's been a period in which political institutions that are charged with coming up with a response to this great economic crisis that's befallen our societies has been seen as failing to do so. It's a period of political blockage and difficulty and perhaps as a result, it's a period in which we have seen the rise of extreme parties, visibly here in Europe, but I think it's certainly true

in the United States, as well, with the Tea Party movement and others.

And then finally, the broader background for the immediate crisis that we're talking about is the process of long-term demographic change, which is effecting the EU societies, is effecting the U.S., is effecting Japan in which our societies are aging. The number of working-age people who will be able to support the pension and welfare promises that are made by the welfare states that exist to a greater or lesser extent in each of our societies are changing.

The median age in the EU, to cite just one statistic, has risen from 35.4 in 1991 to 41.2 in 2011 and there's every indication that that's going to continue to climb fairly steeply. So we have radically aging populations.

I want to introduce the panel, which is a group of people who have very different and interesting perspectives on these changes, both broadly considered and in terms of the particular ways that countries are

going to deal with them. And I'm going to start with the person on my far left. Minister Elsa Fornero is minister of Labor and Social Services in Italy. She is an economist, an expert on pensions, aging and retirement issues and has done serious and interesting academic work in this field.

Next, Miriam Sapiro is Deputy Trade Representative for the United States. Her specialization, prior to coming into government, was in part in Internet and telecommunications policy and so I hope she'll talk about those new parts of our economy in speaking about change.

Next, Minister Koji Tsuruoka, who is the Deputy Foreign Minister of Japan, has served in a number of senior positions and is the number two person in the foreign ministry of a new Japanese government. I hope can tell us what the government of Prime Minister Abe is thinking and planning to do in dealing with these problems.

And then finally, an old friend of GMF, Frans van Daele, who is currently a senior advisor with Deloitte dealing with intergovernmental issues, but in his career was the Belgian diplomat and was for four years the chief of staff to the president of the European Council so has dealt with the EU and its mechanisms closely for years.

I want to start with Minister Fornero and I want to start by quoting a favorite saying of mine from Herbert Stein, who was chairman of the Council of Economic Advisors many years ago, who said once, "If something is unsustainable, that usually means it can't be sustained." And looking at the situation that the developed world faces in which very large promises have been made to the working population, to the citizens, about the kind of welfare, pension, other social benefits that they can expect, a reasonable person might say those promises will not be sustainable, that they need to be changed.

So I want to start off the question with you, but I'd like to ask the panel as a whole. As we look at this crisis, economic and political, what needs to be changed in the basic social contract that's been on offer for several decades now? Minister?

The Hon. Elsa Fornerio: Thank you very much and thank you all for having me here. Perhaps I have to start by saying that I am a member of a government, of a technocratic government. That means that we have not been elected. The government is Mario Monti's government and it's at its end since we just had new elections.

We started because Italy was on the verge of a very severe financial crisis. The crisis was clear. It was not just a threat. It was very clear. And politics was blocked in Italy somehow. The government couldn't, let's say, perform. Although it had made commitments to Europe, it could not continue. And so Mario Monti was asked and he formed a cabinet that was called technocratic government.

There is a lesson in this. Well, I wouldn't say Italy is a fragile country. It's certainly true that Italy is a very divided country. Italy is divided geographically, generationally, and also by gender. So it's the three Gs of Italy division. And it has always been said that Italy does not like, does not tolerate, cold showers, but prefer, let's say, gradualism in reforms. So all the, let's say, structural weakness of the Italian economy and also Italian society were known. And the previous government had enacted many reforms, but with, let's say, extreme gradualism in tackling, for example, the pension expenditure and unsustainability of the pension system.

So when we started, we had no other choice than to act immediately with severity and I was asked to perform the pension reform. We did this in 20 days. I can remember clearly all of them, maybe hour by hour. And then we ended with this reform, which is severe. In a way, it is a cold shower. It is a shock. And it proves, because we did not have a general strike.

And this, in a way, changed the, let's say, feature, the profound feature of our pension system. Meaning that, well, you all know that a pension system is a public expenditure program and so it allows for a lot of political interference. What we did, and was already in there from previous reform, was to change and to give the system transparency and to say, okay, your pension will depend on the contribution that you pay all over your life, working life, end at the age of retirement. Very simple. Everyone can understand. It's not the state that is paying, giving you your pension. It's your saving.

Mr. David Ignatius: Minister, these were courageous reforms and I think many people in this room probably admire the government of technocrats in Italy for posing these reforms. But you'd have to say, looking at the Italian elections, that the response of the Italian public to the cold shower, to the reality therapy and that you and Prime Minister Mario Monti offered, was no.

So I want to ask you to come back to this after the elections. Is the right thing for people, you know, like, people who are economists, people who are ministers, to say, I'm sorry that you don't like it, but it's necessary and we're going to keep doing it?

The Hon. Elsa Fornerno: Well, I have thought a lot about the prevalence of the economic reasoning or economic rationality and prevalence of politics. When we joined government, it was the prevalence of economics over politics. But then politics come back.

And there is certainly something that perhaps--also because of lack of time because we had very little time and I can assure that we had worked a lot, and because of lack of time we could not really--we did not succeed, perhaps, in explaining to people what we were doing. And not beauty, but certainly the fact that after the sacrifices, something good will arrive.

For example, I used to explain the pension reform, which is really severe, by saying, "Okay, but we have now a new balance between generations." Because what

had been done before was you sat before a lot of promises and asking the young and future generations to pay and this is unfair. So I said, if you look at the reform, not just on the ugly side, that ask people to work longer and to have their pensions depending only on their contributions, but if you look at this restoration of a generational balance, maybe since families are still there and there are generational relationships, maybe people will understand.

But it's true, I admit. Politicians, when the general elections--but I will say it's party. Here you have bad political parties and I have really to blame them, also because in the electoral campaign, they did not even want to explain to people. I know that explaining is difficult, particularly when people have no jobs, the young, they are losing their jobs (inaudible). For women, it's difficult because we are losing local services for families. So life for people is becoming more difficult and I know it's not, you know, you cannot just go and lecture people. No.

That may be at least part of the population will understand, but I am sure that for politicians and for political parties--and this is because we had very bad politics for the last 20 years concentrating on just one person. Too much personalization on our political life. It was being pro or against Berlusconi. And this has resulted in--

Mr. David Ignatius: Well, now that's over. Or I guess it's not. So we'll come back to these issues and Italy in a moment, but I want to turn to Miriam Sapiro and ask you, as the American representative on this panel, we are struggling to address the basics of our own fiscal financial policy without a lot of success. You'd have to say that our institutions, at the least the congressional part, have been at an impasse now for several years.

I know, because of your role as Deputy Trade Representative, you have what might be called a new old idea to deal with this fragile world where economic

crisis and political dislocation are causing difficulty, namely trade. And maybe you'd speak about trade, but I'd also be interested in--I know the audience would be interested in your just saying a word or two about the political situation in Washington as people try to confront the core economic issues.

The Hon. Miriam Sapiro: I'm happy to, David. And thank you and the German Marshall Fund for having all of us here today. Let me start by saying that we have worked very hard and made important progress in turning the corner from what was a deep recession on to a much firmer path towards economic recovery and towards avoiding another Great Depression.

I say that by citing nearly six million new jobs that we've created over the last few years. Our exports have reached an all-time high. Our housing market is starting to recover. And there are various other indications that we are on the road to recovery. We managed to lower our unemployment rate to 7.7 percent,

which is still unacceptably too high and we're taking steps to continue to create more jobs.

Mr. David Ignatius: I should note the EU unemployment rate in January was 11.9 percent.

The Hon. Miriam Sapiro: We're also obviously very concerned about the state of the global economy because our economy is so closely linked to that of our major trading partners.

What we've done is to focus, and will continue to focus like a laser, on jobs and growth. To do that includes not only having a strong trade policy with ambitious goals, but also making sure that we have a strong education system, that we have a fair tax code, that we continue on the path towards deficit reduction and that we do it in a balanced way. We continue to empower our entrepreneurs to innovate. We continue our strong commitment to research and development, and we take a number of other steps to make sure that we stay on this path towards economic recovery.

Mr. David Ignatius: And I wonder, looking at the

numbers that you cite and the evidence that the U.S. economy is turning around, the fact that U.S. unemployment is now beginning to fall fairly sharply, is there anything that you think that the U.S. has done successfully that would be a useful model for the other economies in crisis, political societies in transition, the subject of our panel, that you'd like to mention? I mean, if there's one thing that the U.S. has done right, we've done a lot of things wrong, what would that be?

The Hon. Miriam Sapiro: Well, it's hard to generalize every country because obviously, different-- I would say one factor, if I had to just pick one, is the willingness of this administration to make tough decisions. If you'll recall when the president first came into office, he inherited a very challenging economy. The stimulus package was not a popular decision, but nonetheless, one that was the correct one. And I think continuing to make difficult decisions--I think Elsa alluded to some that are facing

Italy, and it goes for many countries. I think that's going to be a critical part of recovery. And also, as I said, focusing like a laser on jobs and growth and making sure that each country is doing what it can to promote that important linkage.

Mr. David Ignatius: I'll just note one interesting statistic that I found in researching this panel, which I think probably makes it easier for the U.S. to rebound and that is that it makes so much less substantial promises to its citizens in terms of their social protection. Just one number that indicates that. Among the EU 27, 30 percent of GDP is spent for what Eurostat describes as spending for social protection. These are 2009 numbers, but I think they're still basically the same. By comparison, the U.S. spends 18 percent. Eighteen percent versus thirty percent. And China, interestingly, China, the communist welfare state, par excellence, spends seven percent. So you see a lot of difference in terms of flexibility and policy response for the U.S.

I'm going to turn now to Minister Tsuruoka from Japan. Japan, as countries went through this enormous economic crisis, one grim thing that they often said to themselves, as they went through this sense of having been over-indebted and then deleveraging, was that they might be entering the lost decades of Japan. And there's this view that Japan became so over-leveraged during its boom years, its bubble years, that it's really still trying to recover from that.

Your new Prime Minister Abe, who just visited Washington, is seen as somebody who has some new ideas about getting the Japanese economy moving more quickly, becoming more dynamic in the way we remember Japan in the 1980s. Maybe you could speak a little bit about Prime Minister Abe's policies, what's different about them and how you think they're going to break out of this crisis that's our subject?

The Hon. Koji Tsuruoka: Well, thank you very much. And thank you, the Brussels Forum, for inviting me to address this very distinguished crowd. I will be very

brief.

First of all, we have had a change of government. LDP, the longstanding ruling party, was in the opposition for the last three years and they came back. Change of governments allow the new government to adopt new policies. And this time, what Mr. Abe has decided to do is not necessarily very new. The measures on monetary policies, easing, setting inflation target of two percent or mobilizing public investment, these are all very well-known measures the government may mobilize to stimulate the economy. And the third pillar that he's proposing is encouraging private sector for economic growth. Again, that's nothing new.

If there is anything new, it's the totality, the firm determination, the comprehensive and swift actions that he has taken. And he has seen no taboos. First, he approached the central bank of Japan, which traditionally, of course, and it is continuing to be independent from government, but still, Abe saw no restriction in approaching the bank and asking them to

be more flexible in the conduct of their monetary policy, like raising the inflation target to two percent.

Second, on public works. As you've just--as the moderator has indicated, we have a need for fiscal consolidation and this being a very serious issue in Japan that had deprived the flexibility of mobilizing public resources for stimulating domestic demand. This time, he took exception to that and said, we still can't afford. Of course, commitment for fiscal consolidation that we made in G20 Ottawa Summit will be maintained, but at the same time, let's mobilize all resources without taboo so that we will indeed realize the Japanese departure from deflation, which has been hurting Japan and by that same token, hurting the regional economy as well as the global economy. So mobilize Japanese potential to the fullest by mobilizing all possible measures that are in hand.

The third pillar, which is economic growth, is the most difficult because economy is a living animal. You

can't force them to grow all of a sudden. And the stimulation of the mass economy, again, is a very difficult issue. This is compounded by the demographic that you've mentioned. Money is in the hands of the older people. Older people, when they age, don't spend much. They may spend gifts to their grandchildren, but they've already had enough and there's a saturation of demand for the older people themselves. So how you shift the purse, the demand, into the hands of the younger generation that are in need? Well, again, Mr. Abe broke the taboo. He approached the industry himself and asked, why don't you raise wages for your workers? Toyota was the first to say, "Yes, indeed, you are right. We've been keeping the wages of Japanese labors too low." And if you continue to do this, in fact, there will be no domestic demand, "So we will go ahead and raise wages." Then we had the retail companies follow suit and then the whole industry is now very enthusiastic about crossing the river together.

Well, if you had none saying this, of course, it

wouldn't happen. But it's not that the industry don't have the money. They have the capital and they have no place to invest, unfortunately, in Japan. They're investing abroad. How can you turn around and have them start investing in Japan as they'd been doing in the 80s and 90s? Stimulation of domestic demand. This will enable Japan to grow back again out of deflation and then that will provide us with the necessary capital for sustaining the welfare that we definitely need.

Now, of course, Japan is an aging society. We're extending retirement age, but then if the seniority system is maintained, the longer you work, the more you earn, but the less effective you are as you get old. So you have to have a different social contract that if you are past the age of 60--and this is now in discussion in Japan so I'm not telling you the final result of the debate. They're still ongoing. But after certain years, like, say, 60, 63, perhaps extending this even to 65, you may retire, but then could be rehired on a different basis. Well, in Japan, people--

the most disappointing fact, is that you're out of work. It's social status. It's the well being of the individual. You don't want to lose work, although you may be getting old, although it may be better for you to look after your grandchildren, you'd like to say, "I go to that company every day, I work in that factory every day," and that's the cause of the pride. This is the work ethics of the Japanese people. So combine that with the diminishing returns that is inevitable with the age, at the same time, continue to make these older generation productive.

Another source that we can rely on is gender. We have not sufficiently used the female workforce in Japan. We admit that. And we are making various means possible to have them work, continue to work, even when they have children. And if we can be successful in structuring this better, then, in fact, we will have more children, more babies, and then back on a growth track with a corrected demography. Thank you.

Mr. David Ignatius: That's fascinating because you

really have said, Minister, that Japan is now in the process of revising its social contract with its citizens, if I understand you. You're looking at the basics. You're saying fundamentals won't change, but some of the assumptions will.

I am curious about one thing. I see female labor force participation in Japan, according to my numbers, is 63 percent compared with about 80 percent in Sweden. So there's a big additional boost of workers and output that you could get by raising female labor force participation. But wouldn't that be likely to further reduce fertility trends in Japan and make that problem even worse?

The Hon. Koji Tsuruoka: That's a very good point. Well, I think we've gone through that in the last 20 years. Of course, there was encouragement for highly educated women to work, perhaps high-paying jobs. They will remain single and, as you say, it will adversely affect the fertility rate. That is now very well-known so there are a number of measures that are already

existing in Nordic countries, for example, where you could leave your child or baby in the hands of experts, well-trained people, and then continue working and picking them up in the evening after you finish work. And we were late, admit, in setting in these systems up. But we, even now, have those in the middle of government agencies. We are still short of that and therefore, the ladies are not reassured that they should marry and bear children as of yet. But it is an awareness that is widely shared among the Japanese public and that will allow the necessary investment to go in.

Prime Minister Abe, who took over from the government of Democratic Party of Japan, which put these social welfare issues up front, is not departing from putting priority on those issues because these are indispensable for the comeback of Japan and the revival of Japanese economy.

Now, the one question I just wanted to just briefly mention, the response of the market for the last half a

year or so since Abe took office. The Japanese stock market hit the highest in four-and-a-half years just last Friday. It's been rising all along so the perception on the market is now very favorable. But more important than that, it's been a tradition in Japanese politics that the popularity rate of the cabinet is highest on the day it is elected and it is appointed. Next day, they start losing. In a few months, half of the support rate is gone and then they have to leave. That's why we always change prime minister every year.

Now, this time, Prime Minister Abe's cabinet received 50 percent support when he was appointed, and now he enjoys more than 70 percent support on the opinion polls. This is a drastic change from the past governments. That's why he can mobilize unprecedented means because he's confident the public will support that. And we will continue to do so and we will be having an election of the upper house coming July. And if the trend continues, we will no longer have a

divided government. The Parliament by the ruling party or, of course, the government by the ruling party, and that will assure a very steadfast, comprehensive policy implementation, the ones you already know.

Mr. David Ignatius: So President Obama has those same numbers, but in reverse. Ever since getting reelected, his popularity has been falling, to his sorrow. So I want to turn, finally, to Frans van Daele, and we've been talking about the social contract. If there's one thing that I think the world of Brussels, that you've worked in all these years, symbolizes, it's the way in which the new Europe guaranteed--promised to the citizens of Europe, I shouldn't say guaranteed, that there would be this contract between the government and the people, laissez qui, we often speak of, the things that you've acquired. They're your rights as a citizen and a worker. And so I'd ask you to speak about this crisis with particular reference to whether some of laissez qui, some of the things that people came to believe were their rights, are going to

have to be given up so as to have the more flexible and dynamic economy that Europeans want.

Amb. Frans van Daele: Yes. Thank you, David. I'm happy to be here together with you all. Just before addressing the points you were making, just one small detail which was prompted by one of your figures about points of GDP, which go to social protection in Europe as compared to the United States. Allow me to add another figure which is about money spent on healthcare. In Europe, it's more or less 9 percent. In United States, it's 16 percent and it's growing--or it was growing till Obamacare came. It was growing two times and a half as fast as the American GDP. So, well, we all have to struggle with keeping the cursor in the right place as far as social protection's concerned, whatever system it is.

I think what we are in--and now I'm going to the point of the social contract. Basically, we adopted a German currency, headed into a crisis. I think the most dangerous moments of the crisis are behind us. spoke to

that yesterday. We now have to do, which in a way stands to reason, if you import the German currency, you end up with having to import a German economic model. It's not just copy/paste, but it has a lot to do with that, which means that growth will only come from structural reform. And the structural reforms we are going to have, there are many, many of them. But the most essential ones are retirement age, and that is a consequence of demography. By the way, you mentioned Japan, United States and Europe. You should have mentioned China as well, which has the demography, which is probably even worse.

Mr. David Ignatius: Yes, quite right.

Amb. Frans van Daele: But they have a lot of labor reserve at the same time. The retirement age, obviously in all European countries are grappling with this problem. See the rather courageous decisions and negotiations President Hollande had with the French trade unions. The second thing we will have to do is structural as well, is that we have to introduce more

flexibility into the labor market. Again, I think these are the two priorities. They will not destroy the social model. They will adapt it. It's a question of adjustment. It's not a new paradigm. It's the shift of one paradigm from one position to another.

Is it difficult? Yes. Because the structural reforms are very much linked to political nexuses and cultural nexuses. And in a way, the things you are asking some people to do is sawing off the branch on which they are sitting. But that is going to happen because we have all looked into the abyss and we didn't like what we saw. So it needs structural reform. This is going on--

Mr. David Ignatius: Could you just--just to--

Amb. Frans van Daele: Yeah?

Mr. David Ignatius: Could you ever ask someone--I mean, that is, in effect, what you are asking people to do, to saw off the branch on which they're sitting. And who in his right mind would ever do that? I mean,

that's crazy. People won't do that so you're going to have to saw it off against their protest, won't you?

Amb. Frans van Daele: Yes. But that's why it's going to last long. And it's particularly the case where you have a nexus of political and economic interest. We have a number of economies which are intertwining political power and economic power. That creates some optimal economies. If you still practice some bits and pieces of economic conferences, then you end up where you end up. So that's why it's a painful and cultural process. But at the same, look at a number of countries. It's happening. It is shifting. It changes political positions. People are losing power.

I was involved with every European council for three years. If I see now the people who are sitting there, I think two-thirds are new faces.

Mr. David Ignatius: You know, you put it bluntly and well. The question I have, when I look at Europe, is whether Europeans want to be Germans. You know, they may need German economic structural reform to be as

prosperous as Germans, but do they want to give up--but before we turn to the audience for questions, I just want to ask Minister Fornero, 'cause we've spoken about many issues on which you've done academic research, I don't want to ask an academic question so much as a political and even an emotional one.

Italy now, like Greece, like Spain, is going through a trauma that it hasn't seen since World War II. The numbers that I saw talked about youth unemployment measured various ways, but youth unemployment in Greece and in Spain approaching 60 percent, youth unemployment in Italy and Portugal, on the order of 40 percent. So I want to ask you, in commenting on these questions about laissez qui and what's going to be given up, what's it like to live in a country where you have 40 to 60 percent of young people with no job? And what's that going to be like, you know, three years, five years from now? I'm sure we'd be interested in any thoughts you have. Then we'll turn to the audience.

The Hon. Elsa Fornero: Well, since you also said, from a personal point of view, I think that being a labor minister in Italy having to do with social policies with little, little money and also having to do with the equal opportunities issue, well, is a very uncomfortable position personally, emotionally, you said. And this has been true. There is, well, hope. Economists are usually very rational and they believe in rational process. And I am a professor so I believe in talking to people. I've always said, I'm waiting to talk.

I can quote an episode which, to me, was very important. There was a trade union, very far left, even far left-er than our biggest left trade union, and they sent an invitation to me, supported by more than 1,000 signatures, by workers who wanted to meet me in their factory, possibly. And I said, yes, of course, I'll go there. I'll go and talk to you. But then I was sort of scolded by the trade union, saying, oh, no, no. This is not for ministers. This is our job to talk to workers.

And I said, no, I have a different opinion of what good behavior is and so I went to meet them. And it was very difficult because they were very angry because we had just enacted the pension reform, the labor market reform, which is not impoverishment of labor relationship because that, I haven't done. And I don't believe that's the key to compete with China.

We don't compete with China by impoverishing our labor market relationships. No, I don't believe this. We compete by getting better relationship, going through apprenticeship and all this kind of things. Okay. So they were angry because they accused us of not having done sufficiently, in terms of having privileges, of politicians, of, let's say, the upper class that has not paid. It's true.

And this is a question that we haven't dealt with enough. That is distribution. So I think--I believe that we can have social contracts that are transparent, efficient and democratic. I believe even that our welfare system can be based on this more than on

political redistribution. And so I believe this is possible, but of course, we have to have less tax evasion, which is an issue, less corruption, which is another issue, less privileges hidden in many--less protections for some groups. And so it's a long way because we have 20 years of bad politics, as I said before.

Mr. David Ignatius: Thank you for that. That's for me. That's a takeaway for me. And I just want to note it 'cause it's something I want to, perhaps, write about. But your basic point is, I think, the beginning to the answer of the answer to the question that this session poses, which is how do you rewrite the social contract so that Europe, Japan, the United States can grow again? And that means giving up some of these privileges. These are key. And people will accept that if, and only if, they feel that the system is just, that fundamental sense of that social justice, fair treatment of different classes, different backgrounds,

different groups is essential. And I think you put your finger on it.

So let me turn to the audience for questions. I want to start with the former minister of national economy in Greece, my friend Yannis Papantoniou.

Mr. Yannis Papantoniou: Thanks, David.

Mr. David Ignatius: Hold on. Let's get a mic.

Mr. Yannis Papantoniou: Thank you very much, David. The topic that we talk about is huge, but I will try to be as concise as possible. Now, despite the reasonably optimistic prospects of the United States economy, I think the other prospects of the global economy are rather gloomy, particularly for Europe, for Japan and many other areas. Before asking a question, I would like to lay down what I think are the main elements of a strategy for global economic recovery. The first two elements are those which are already mentioned, which is austerity and supply side reforms, the new social contract you talked about through which people would have less rights, but more obligations but better

economic prospects such as employment and incomes. This is the new deal that there will have to be applied in our countries.

There is, however, two other elements which are necessary. We need more effective demand from the service countries and we also need a judiciary reform both at the (inaudible) level, more economic, fiscal and political union, and at the global level so far as global economic governments is concerned, so far as global financial reform is concerned, regulation, supervision, and so far as trade liberalization is concerned, because we all know the Doha Round has led nowhere.

Now, what we see in that European and global level is the following: From the four elements, austerity, domestic supply-side reforms, more demands, more institutional reform, only the two are applied. But what we have seen in Italy is that austerity has defeated reform. Why? Because in conditions of excessive recession, government employment and poverty,

people are not willing to enter into a new social contract.

Mr. David Ignatius: I want to--since I want to give our panel a chance to respond, should we put that as a question to Minister Fornero, whether--and it's a good question. Did austerity defeat--

Mr. Yannis Papantoniou: Reform.

Mr. David Ignatius: --the purpose of reform? A good question.

The Hon. Elsa Fornero: Well, I would say, in the very short run, perhaps yes. But I'm confident that, for example, the young understand. And we have this populist party that now enter parliament, but I make a difference between the leader and the followers. And I know that mainly our followers are young people and they do not tolerate the privileges. They do not tolerate old kind of old jargon that is the characteristics of the old politics. They do not stand people that just say, we need to do this, we need to do

that, we need to do the following. They want to see actions in practice.

And so, okay, in the short run, well, let's say, the government, this supposed supremacy of the economics over politics has not really worked. But I'm confident and--well, personally, I have to be. Otherwise, it's 15 months of hard job that is thrown away and this is really very hard to bear. I have to believe that the young will understand. And so maybe we will have a new model coming.

I think we have--many times, we said that the crisis is also kind of opportunity. Now, in Italy, elections have been a shock. I admit, a shock. But it's possible that a country that prefer gradualism sometimes awakes from a shock and this is for the better for real change that we started. We only started because one year is not enough.

Mr. David Ignatius: That's just a beginning of an answer to Young's question, but we'll come back to it,

perhaps, in later discussion. Our colleague from Latvia.

Mr. Artis Pabriks: Yes, Defense Minister of Latvia. Now, this was very interesting to hear your arguments and one of the first suggestions that I would propose, if somebody now in Europe dislike to take a German example or model for certain reasons, especially in southern Europe, I would suggest you take something smaller. Take the Latvian model.

And I don't think that we have been extremely successful, but our austerity, let's say, in defense sector were minus 50 percent in 2008 and 2009. By telling that, I wanted to say that we never cut our international contributions because of this.

And just a few lessons from our side that I can say. First of all, if we make such type of reforms, we have to ensure that the most poor part is the least affected. In our case, we did not touch pensions. And for me, actually, as a question, it would be interesting to hear. Because you were telling that the

reform part was to ensure that there is a correlation between the age and between your contribution to pension. So what type of pensions and contribution you had before? Because we had always such type of connection between individual payment and the outcome.

The second thing is that it's very difficult to touch social and educational part because this is the part of the possible growth.

And the third thing is the communications part. That is the most tough issue because, in fact, our parliamentarians and ministers, we lost about 25 percent of our salaries. And I would say that this-- also our bureaucracy lost that. And I would say that this was still not satisfactory because even by trying to say that politicians are losing just like the ordinary population, there would be some part of population which you always tell they should work for free in general.

So nobody loves politicians. Nobody loves bureaucracy. So you have to be balanced between cuts in

solidarity and between the state efficiency. And this is one of the problems where we see still a necessity to work on.

And the final thing is that I think we need still in Europe, for those countries who went through the reform like we, we have now growth plus 5.6 percent. We hope we will keep to that, but we need a communication strategy also for our own population and the population across the borders because if we give populist [sic] promises, if we are not capable of giving one message, we simply open the gates for rise of populist parties like we see now in Germany is coming up before elections, like in Italy and somewhere else.

So I think that's an important issue to speak also in one voice, not only act in one voice. Thank you.

Mr. David Ignatius: Let's take a couple more questions. Bruce and then this gentleman here and then Chairman West.

Mr. Bruce Stokes: Hi. Bruce Stokes of the Pew Research Center. A question we really haven't gotten

into is the rise of inequality in all parts of the world, particularly in the United States, where it's been rising for 40 years. So it does seem to me you can't say it's a cyclical phenomenon, but we've seen the rise in inequality in India, China, Europe.

If one accepts the fact the definition of a legitimately functioning economic system is that it addresses the economic needs of its people, doesn't our economic system that we all share, there's somewhat of a market system in all of our countries, that the economic legitimacy of this system is now in real question and more importantly, that the political legitimacy of the democratic system that has failed to address this is also in question.

Mr. David Ignatius: Good question about legitimacies. Sir, the gentleman in the second row, please. Do we have a microphone for this gentleman here? Here you are.

Minister Giulio Terzi: Giulio Terzi, International Affairs in Rome, Italy. I have a question for Mr.

Tsuruoka, a very specific one. You mentioned the very worrying demographic trends, which are, indeed, widely seen as a stumbling block to growth in Japan, as in other places. And you mentioned some measures are being taken or can be taken to cope with this problem.

May I ask you, do you think a change in migration policy can be considered? We all know there is a strong resistance to changing the current pattern of migration policies in Japan. And this may be a question also for the other panelists, because you don't mention this factor. An aging society might benefit from a more liberal migration policy.

Mr. David Ignatius: Good question. And Robin West in the first row.

Mr. Robin West: My name is Robin West. I'm on the board here at the GMF. There's another question that sort of touches a bit on Bruce Stokes' point. But in the United States, for example, there's a huge swath of the population which is now poorly educated and really ill-equipped to deal with the new economy. And Germany

has tried to create a system where you have workers that are equipped for the future economy. How are we going to deal with this in the United States? This is a huge challenge and we haven't answered it, but it's something that seems to me modern democracies, in order to justify themselves, they have to find a solution to this.

Mr. David Ignatius: Four good questions. Just to recap: The first question about the Latvian model which, I take it, is one of really sharp reductions in spending initially. Second, Bruce's question about the fundamental legitimacy of the system as it goes through this period of difficulty. Question about whether these demographic trends mean that there really does need to be a total reexamine of immigration policy in a country like Japan. And then, finally, Robin's question about the ill-equipped part of the labor force.

And let's let each of the panelists choose among those subjects as you like, starting with Mr. Van Daele.

Amb. Frans van Daele: Yes. About the Latvian model, we distributed the prime minister's book on the Latvian crisis to all members of the European Council so we thought it was a very interesting read.

They did something which proves that, even if the politics are difficult, you can reform structurally. Latvia had the alternative of devaluing. It did not. It chose an internal devaluation, which arguably is much more difficult, and it succeeded.

And when we were talking the branch we are sawing off, I mean, if you have 50 percent or 60 percent youth unemployment, the pressure in your system politic and your system social are such that you have to reform. And I think it is a hugely contributing factor and it's good to have the Latvian example because it proves it can be done.

Mr. David Ignatius: Yes. Minister Tsuruoka.

The Hon. Koji Tsuruoka: Thank you. First, I would like to mention or talk about inequality or question of equity because this is the, mind you, most important

issue we always need to keep in mind. Equity within a country and equity among the countries because unless this question of equity is kept in mind of the policymakers, you are just digging holes in which you will fall in, in due course.

Stability, social fabric, is extremely important. If people are jealous about others--and now that we have the Internet and the Facebook and all the means of communicating with each other, rightly or falsely, there is this jealousy element that you are inviting in the minds of individuals. So if there's no sense that the world is fair, you are breeding conflict that will eventually surface.

This is an issue that I believe is very important and Japan has been based on egalitarian concept, which allowed us to be fairly stable in the past decades or so and we intend to keep it.

We are raising consumption taxes. It is currently five percent. In 2014, April, it will be eight percent and then another year goes and it will reach 10

percent. You may think it's still cheap and I agree, but the consumption tax has had very strong resistance because, by definition, it is not egalitarian. And that is the level of equality, equity, that we put value on and I think we need to keep this in mind.

Migration policy. Yes, fine. The diminishing labor force in Japan is detrimental for growth. I fully agree. The Japanese public agrees. But of course, there is very strong resentment for bringing in foreign labor in Japan. Why? Because Japan is not a capitalist market based on capital. It is a market based on employment. I said earlier, the aging people, the last thing they want to do is to leave the company, leave work. They're not waiting to have free time where they will play golf or go to tourists' sites. They want to continue working. This is the life for them.

So if you have people coming from elsewhere, and not necessarily fact, but seemingly depriving these people from work, it is going to disrupt the social fabric of Japan. So we have to be very careful about

this, although we fully take into account the need of doing this in a win-win operation.

There are excessive labor forces that are available to work in Japan. We don't have sufficient experience in the past of integrating them, not forever, for a limited time and then use these labor for our advantage as well as for these people to gain income that they could use back home.

Europe is more experienced in that. Germany is very experienced. We've been looking at those experiences, what model we could introduce. We haven't been successful, to be very honest. This is a debate that is going on. Again, this is a fight against vested interests and the unprecedented means, whether we can mobilize them. If we can, we need a very strong political support among the public. Mr. Abe, as I said, may have the strong political support to introduce something unprecedented in Japan. Thank you.

The Hon. Miriam Sapiro: Let me try to tie together a couple of the very good questions we got and also a few of the points I've heard my colleagues say.

In terms of austerity, I think it's really important that the cuts be strategic rather than automatic. We're facing an automatic situation now in the United States that we are trying to address, but I think that observation also applies to other economies in terms of the difficult choices, which I mentioned earlier, that need to be made.

It's also imperative that we focus on job creation. How do we create more jobs? We talked about the importance of people having a job, having a real living wage, being able to support a family. And whether we're talking about the United States or we're talking about Europe or we're talking about the Middle East, Africa, Asia, Latin America, this is a global challenge that countries are working hard and really must find a way to address.

David, you poked a bit of fun at trade. Is it a new old idea or an old new idea? The data shows, at least for the United States, and the statistics vary by country, but for every billion dollars in goods exports that we achieve, we create roughly 5,000 new jobs. So we will continue to focus on trade policies that work, on enforcing trade obligations that we already have so that we can continue to create these new jobs and sustain the ones that we have.

Our exports last year reached \$2.2 trillion, which was a banner year, and we're going to keep moving that direction. We reached a realization about a year ago, as the WTO all members, that the Doha Round just wasn't working, wasn't going to take us where we all wanted to go. So since then, we've continued to step up our work in Geneva in terms of reaching, hopefully, a new agreement on trade facilitation to help goods move more easily across borders.

We are expanding the information technology agreement, which is going to be really important to

technology companies around the world. There are about \$4 trillion in trade flows currently under the ITA, but the list of products covered hasn't been updated since 1996 so we're very eager to see that happen.

We've launched recently international service agreement negotiations so that we can take advantage of more liberalization in the services sectors. This is a huge comparative advantage for the United States. We actually have a surplus of our services exports and it's also a growing area for Europe and for other markets. So we're doing a lot multilaterally and we're also pursuing a very ambitious trade agenda with some of our key partners.

In Europe, for example, the president has announced his intention to begin negotiations on a new trade investment partnership and we're also working very hard to include the transpacific agreement that was started a couple years ago and now includes total of 11 trading partners.

But it's obviously more than trade. It's empowering our small/medium enterprises. Currently, only about 1 percent of our SMEs export. In the United States and most countries, SMEs are the backbone of the economy. So what can we do to make sure they have the tools to compete effectively overseas is going to be a critical challenge.

I mentioned earlier, education, making sure that we have excellent preschools and education at the lower levels and then in high school, that we're really training people to have the skills they need to compete in a global economy. We actually have jobs in the United States that we can't fill because we don't have trained workforce that can step in. So that is another big challenge that we have.

In terms of growing inequality, that is something that we are very concerned about. We'd like to see the minimum wage rise so that people who work full-time don't have to worry about falling into poverty. That shouldn't happen. We're also trying to restructure the

tax code so that we can close loopholes and we can make it more equitable. So I think these are challenges in the U.S., but they are also common challenges. And I think together we can continue to find new ways to approach them, hopefully successfully.

Mr. David Ignatius: Minister Fornero, let me ask you to conclude.

The Hon. Elsa Fornero: Just a very quick answer to Latvian Minister. You said you don't know what a noncontributory pension is, but indeed you should because before the reform in your country was done, I remember I was asked by the World Bank to go as an expert and visit and provide assistance to the World Bank. And I clearly remember that your pension system was, before the reform, was just a kind of defined benefit, defined benefit by, let's say, political choice, not by economic choice.

But there was an episode when I was there that was very touching and I always remember and it gives me the occasion maybe to conclude my intervention. And that

is, I had the opportunity to, well, to talk to people and I remember there was an elderly woman was representative of a trade union of retired people. And she talked to me and she asked, "Do you think there is room for a small increase in our pensions or shall we ruin our prospect of joining Europe?" This was the question, which moved me. And it gave me the idea that there was a sense of direction in that country that even that elderly woman had understood very well. And this is exactly what maybe we in, Europe, have lost, a sense of direction, of unity.

Just briefly, Germany. In early 2000, Germany was considered an ill economy in Europe. They have reforms, tough reforms, they shoulder reforms in the labor market, which in Italy we took as an example, as a benchmark certainly. We are not Germans. We are Italians, but we took as an example that the two years or three years after the reforms, an employment increased and then started decreasing, which it did steadily until now. And particularly youth unemployment

now is two points higher than general unemployment, not three times higher. And this is due to, well, mainly due to training and education, taking seriously the way people are trained because not everybody wants to have a degree or a master course or Ph.D. and they take very seriously training, technical skills. And this has proved useful, very useful as an instrument against youth unemployment. But it also says that we have no immediate response to unemployment, except possibly one. And that is to have resources to lower, now in the recession, to lower labor costs. So we need to have actions to improve productivity in the medium-term. And we need, terribly, resources to lower costs right now in the recession.

Mr. David Ignatius: So thank you to all the members of the panel. I apologize to those I couldn't call on because we ran out of time. Just the briefest closing comment.

In what Ms. Sapiro said about trade, I thought I heard something that characterizes all of the important

policy recommendations. Things that, over the long run, benefit everybody, like more open trade, in the short run hurt some individuals. And I'm so struck, listening to this panel, that the definition of leadership in periods like this is to have a clear enough definition of the long-run benefits for everybody, that the short run costs, which are real, will be ones that people are prepared to accept.

So thank you all, members of the panel, for a wonderful discussion.

Mr. Craig Kennedy: Thank you, David. We're getting ready for lunch, but let me do two quick things. First, we always want feedback so let us know how you think this having a theme of fragility is working. We've heard about fragile economies, fragile states. I think we've even heard some pretty good solutions of how to address them, especially with a great summary like David just did. But we want to hear your thoughts on whether this has worked.

I want to take this opportunity, before we go to lunch, to also thank the three American embassies here in Brussels--yes, three--NATO, Belgium and EU and we have Ambassador Gutman with us right now. They provide terrific help in all sorts of ways to make this conference happen. They make sure that our American government guests and others get around and they provide just an enormous amount of support. So many thanks, Ambassador Gutman.

Lunch is out in the lobby.