



SPECIAL ANNIVERSARY ISSUE

FOREIGN AFFAIRS

The Clash of Ideas

The Ideological Battles That Made the Modern World—
And Will Shape the Future

FEATURING

Shlomo Avineri, Isaiah Berlin, Benedetto Croce,
Francis Fukuyama, Charles Kindleberger,
Harold Laski, Leon Trotsky, and many more

The Future of the Euro, the Dollar, and the Yuan
Feldstein, Eichengreen, Mallaby & Wethington

Getting Tough With Pakistan
Stephen Krasner

A New U.S. Grand Strategy
Zbigniew Brzezinski

Time to Attack Iran
Matthew Kroenig

The Real George Kennan
Nicholas Thompson

FOREIGN AFFAIRS

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Nicholas Thompson

*Mana Yahu
for eni*

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FOREIGN AFFAIRS



JANUARY / FEBRUARY 2012
VOLUME 91, NUMBER 1

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The articles in Foreign Affairs do not represent any consensus of beliefs. We do not expect that readers will sympathize with all the sentiments they find here, for some of our writers will flatly disagree with others, but we hold that while keeping clear of mere vagaries, Foreign Affairs can do more to inform American public opinion by a broad hospitality to divergent ideas than it can by identifying itself with one school. We do not accept responsibility for the views expressed in any article, signed or unsigned, that appears in these pages. What we do accept is the responsibility for giving them a chance to appear.

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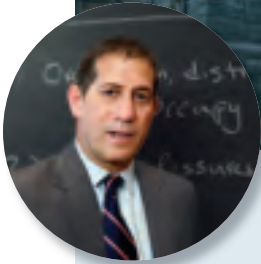


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The Clash of Ideas



THE NEW YORK TIMES/REDUX

At a communist rally, Dortmund, West Germany, 1950

The basic question of modernity has been how to reconcile capitalism and mass democracy, and since the postwar order came up with a good answer, it has managed to weather all subsequent challenges.

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Making Modernity Work

The Reconciliation of Capitalism and Democracy

Gideon Rose

We are living, so we are told, through an ideological crisis. The United States is trapped in political deadlock and dysfunction, Europe is broke and breaking, authoritarian China is on the rise. Protesters take to the streets across the advanced industrial democracies; the high and mighty meet in Davos to search for “new models” as sober commentators ponder who and what will shape the future.

In historical perspective, however, the true narrative of the era is actually the reverse—not ideological upheaval but stability. Today’s troubles are real enough, but they relate more to policies than to principles. The major battles about how to structure modern politics and economics were fought in the first half of the last century, and they ended with the emergence of the most successful system the world has ever seen.

Nine decades ago, in one of the first issues of this magazine, the political scientist Harold Laski noted that with “the mass of men” having come to political power, the challenge of modern democratic government was providing enough “solid benefit” to ordinary citizens “to

make its preservation a matter of urgency to themselves.” A generation and a half later, with the creation of the postwar order of mutually supporting liberal democracies with mixed economies, that challenge was being met, and as a result, more people in more places have lived longer, richer, freer lives than ever before. In ideological terms, at least, all the rest is commentary.

To commemorate *Foreign Affairs*’ 90th anniversary, we have thus decided to take readers on a magical history tour, tracing the evolution of the modern order as it played out in our pages. What follows is not a “greatest hits” collection of our most well-known or influential articles, nor is it a showcase for the most famous names to have appeared in the magazine. It is rather a package of 20 carefully culled selections from our archives, along with three new pieces, which collectively shed light on where the modern world has come from and where it is heading.

THE BIRTH OF THE MODERN

In the premodern era, political, economic, and social life was governed by a dense web of interlocking relationships inherited

Gideon Rose

from the past and sanctified by religion. Limited personal freedom and material benefits existed alongside a mostly unquestioned social solidarity. Traditional local orders began to erode with the rise of capitalism in the eighteenth and nineteenth centuries, as the increasing prevalence and dominance of market relationships broke down existing hierarchies. The shift produced economic and social dynamism, an increase in material benefits and personal freedoms, and a decrease in communal feeling. As this process continued, the first modern political ideology, classical liberalism, emerged to celebrate and justify it.

Liberalism stressed the importance of the rule of law, limited government, and free commercial transactions. It highlighted the manifold rewards of moving to a world dominated by markets rather than traditional communities, a shift the economic historian Karl Polanyi would call “the great transformation.” But along with the gains came losses as well—of a sense of place, of social and psychological stability, of traditional bulwarks against life’s vicissitudes.

Left to itself, capitalism produced long-term aggregate benefits along with great volatility and inequality. This combination resulted in what Polanyi called a “double movement,” a progressive expansion of both market society and reactions against it. By the late nineteenth and early twentieth centuries, therefore, liberalism was being challenged by reactionary nationalism and cosmopolitan socialism, with both the right and the left promising, in their own ways, relief from the turmoil and angst of modern life.

The catastrophic destruction of the Great War and the economic nightmare of the Great Depression brought the contradictions of modernity to a head, seemingly

revealing the bankruptcy of the liberal order and the need for some other, better path. As democratic republics dithered and stumbled during the 1920s and 1930s, fascist and communist regimes seized control of their own destinies and appeared to offer compelling alternative models of modern political, economic, and social organization.

Over time, however, the problems with all these approaches became clear. Having discarded liberalism’s insistence on personal and political freedom, both fascism and communism quickly descended into organized barbarism. The vision of the future they offered, as George Orwell noted, was “a boot stamping on a human face—forever.” Yet classical liberalism also proved unpalatable, since it contained no rationale for activist government and thus had no answer to an economic crisis that left vast swaths of society destitute and despairing.

Fascism flamed out in a second, even more destructive world war. Communism lost its appeal as its tyrannical nature revealed itself, then ultimately collapsed under its own weight as its nonmarket economic system could not generate sustained growth. And liberalism’s central principle of *laissez faire* was abandoned in the depths of the Depression.

What eventually emerged victorious from the wreckage was a hybrid system that combined political liberalism with a mixed economy. As the political scientist Sheri Berman has observed, “The postwar order represented something historically unusual: capitalism remained, but it was capitalism of a very different type from that which had existed before the war—one tempered and limited by the power of the democratic state and often made

subservient to the goals of social stability and solidarity, rather than the other way around." Berman calls the mixture "social democracy." Other scholars use other terms: Jan-Werner Müller prefers "Christian Democracy," John Ruggie suggests "embedded liberalism," Karl Dietrich Bracher talks of "democratic liberalism." Francis Fukuyama wrote of "the end of History"; Daniel Bell and Seymour Martin Lipset saw it as "the end of ideology." All refer to essentially the same thing. As Bell put it in 1960:

Few serious minds believe any longer that one can set down "blueprints" and through "social engineering" bring about a new utopia of social harmony. At the same time, the older "counter-beliefs" have lost their intellectual force as well. Few "classic" liberals insist that the State should play no role in the economy, and few serious conservatives, at least in England and on the Continent, believe that the Welfare State is "the road to serfdom." In the Western world, therefore, there is today a rough consensus among intellectuals on political issues: the acceptance of a Welfare State; the desirability of decentralized power; a system of mixed economy and of political pluralism.

Reflecting the hangover of the inter-war ideological binge, the system stressed not transcendence but compromise. It offered neither salvation nor utopia, only a framework within which citizens could pursue their personal betterment. It has never been as satisfying as the religions, sacred or secular, it replaced. And it remains a work in progress, requiring tinkering and modification as conditions and attitudes change. Yet its success has been manifest—and reflecting that, its basic framework has remained remarkably intact.



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Gideon Rose

THE ONCE AND FUTURE ORDER

The central question of modernity has been how to reconcile capitalism and mass democracy, and since the postwar order came up with a good answer, it has managed to weather all subsequent challenges. The upheavals of the late 1960s seemed poised to disrupt it. But despite what activists at the time thought, they had little to offer in terms of politics or economics, and so their lasting impact was on social life instead. This had the ironic effect of stabilizing the system rather than overturning it, helping it live up to its full potential by bringing previously subordinated or disenfranchised groups inside the castle walls. The neoliberal revolutionaries of the 1980s also had little luck, never managing to turn the clock back all that far.

All potential alternatives in the developing world, meanwhile, have proved to be either dead ends or temporary detours from the beaten path. The much-ballyhooed “rise of the rest” has involved not the discrediting of the postwar order of Western political economy but its reinforcement: the countries that have risen have done so by embracing global capitalism while keeping some of its destabilizing attributes in check, and have liberalized their polities and societies along the way (and will founder unless they continue to do so).

Although the structure still stands, however, it has seen better days. Poor management of public spending and fiscal policy has resulted in unsustainable levels of debt across the advanced industrial world, even as mature economies have found it difficult to generate dynamic growth and full employment in an ever more globalized environment.

Lax regulation and oversight allowed reckless and predatory financial practices to drive leading economies to the brink of collapse. Economic inequality has increased as social mobility has declined. And a loss of broad-based social solidarity on both sides of the Atlantic has eroded public support for the active remedies needed to address these and other problems.

Renovating the structure will be a slow and difficult project, the cost and duration of which remain unclear, as do the contractors involved. Still, at root, this is not an ideological issue. The question is not what to do but how to do it—how, under twenty-first-century conditions, to rise to the challenge Laski described, making the modern political economy provide enough solid benefit to the mass of men that they see its continuation as a matter of urgency to themselves.

The old and new articles that follow trace this story from the totalitarian challenge of the interwar years, through the crisis of liberalism and the emergence of the postwar order, to that order’s present difficulties and future prospects. Some of our authors are distinctly gloomy, and one need only glance at a newspaper to see why. But remembering the far greater obstacles that have been overcome in the past, optimism would seem the better long-term bet. 🌐

How We Got Here

The Rise of the Modern Order

*What follows are selections from our archives that tell the story of the ideological battles of the past century and the emergence of the modern order. To make the package as a whole coherent and accessible, we have included only the most relevant parts of articles directly related to this theme and presented the articles in substantive, rather than strictly chronological, order. The contents of each article have not been rearranged, however, and all elisions have been clearly marked. The full text of all the articles in the package, and more, can be found in the accompanying e-book, *The Clash of Ideas*, available at ForeignAffairs.com.*

THE EDITORS

Lenin and Mussolini

Harold J. Laski

September 1923

HAROLD J. LASKI, *Professor in the London School of Economics and Political Science.*

. . . The mass of men has now been entrusted with political power; and the governments of the modern state must discover ways and means of translating the will of an electorate . . . into terms of statutes. It is possible that so long as the process of legislation can offer . . . solid benefit the transition to a new social order will be accomplished in peace. But . . .

the benefits must affect those who feel that they have now too small a stake in the present order to make its preservation a matter of urgency to themselves.

Such an attitude is the more important because the desirability of social peace has recently been attacked from what, at first sight, might seem two opposite directions. In Russia, a revolution made in the

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name of the workers has enthroned in authority men whose boast it is that they hold power without regard to the will of their subjects. In Italy, there developed alongside the constitutional government an extra-legal organization to which, at the first definite challenge, the former was compelled to yield. . . . It is common to both movements that their power is built upon the force they can command. It is common to them, also, that they have rigorously suppressed all opposition to themselves and dismissed as unimportant the forms of constitutionalism. Each has exalted the end it has in view as superior to all problems implied in the means that have been used. Each has declared its own will so clearly identical with the good of the community as to make invalid, on *a priori* grounds, the notion of its critical analysis. . . .

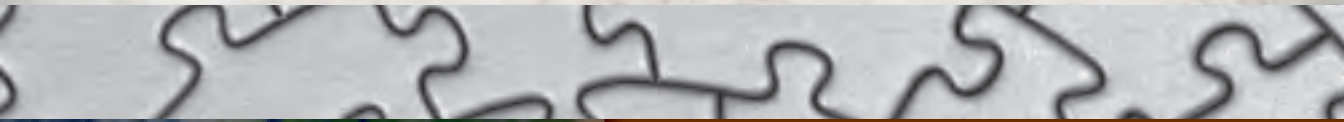
A revolution in Russia was doubtless implied in the logic of events. No government which is vicious in principle and corrupt in practice can hope, particularly in the atmosphere of military defeat, to retain the allegiance of those who do not share in the benefits of its dishonesty. But the Russian Revolution differs from all its predecessors in that it came in the name of a consistent system of doctrine; and it was largely made by men to whom that system contained the quintessence of social truth. . . . Lenin and his disciples came to do battle in the name of a social philosophy each item of which was built upon historic interpretation. Accident might have defeated their effort, Kerensky might have been a strong man; the Allies might have had a definite policy; the nation might not have been welded into unity by external invasion. But granted that the opportunity was given, Lenin was the first author

of an attempt to translate the Marxian creed into the institutions of a state. His was a root-and-branch challenge to western civilization. It was not merely a rejection of social reform; it was not merely an insistence on the over-whelming superiority of communism. It was pre-eminently the argument that communism is so obviously desirable that the cost of its establishment must not be counted; and the methods to that end were drawn from the system inherited by Lenin from Marx.

The theses upon which Lenin has proceeded have at any rate the merit of comparative simplicity. The political institutions of society, he argues, are merely a facade to conceal the real nature of the state's organization. The state is in fact a method of protecting the owners of property; and the true division of men is into those who own and those who do not own possessions other than their power to labor. The life of the state is an eternal struggle between them. They have no interests in common. The class which owns property moulds the civilization of society in the service of its own interests. It controls the government, it makes the laws, it builds the institutions of the commonwealth in accordance with its own desires. It divides the society into free men and slaves; and with the advent of capitalism the last stage of that historic antithesis is reached. Just as the social order of the past has secreted within its womb the germ of its successor, as, for example, feudalism produced capitalism, so does the latter contain within itself the germ of its communist successor. Capitalism, as Marx said, produces its own gravedigger. The conflict between owner and proletariat is an inevitable one, and it is bound to result in the victory of the pro-

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letariat. The process is predetermined; and there is nothing in Lenin's writings to suggest that a doubt of ultimate success has ever crossed his mind.

The method he advocates is, of course, the method of Marx. The workers are to assume the reins of power by a revolutionary act; and a dictatorship of iron rigor is to consolidate the new system until the period of transition has been effectively bridged. . . .

The Italian movement is different in origin, but its ultimate spirit is in no-wise dissimilar. Leninism has been the dictatorship of a party, Fascism is the dictatorship of a man. Its rise is in part due to the endeavor to escape from the disillusion which seized Italy after the Treaty of Versailles, and in part to the ill-considered effort of the left-wing Italian socialists not merely to link themselves to the Third International but also to seize control of industry in some of the great towns. Violence assumed the character of a habit in post-war Italy. . . . The older politicians were thoroughly discredited. . . . Italian parties . . . were in the control of machines bankrupt of ideas and—the clericals apart—little different from each other. A revivification of political life was essential if Italy was to realize the new possibilities opened by her part in the victory.

It was as the symbol of that revivification that Mussolini came to do battle with the old order. In part he represented the passionate optimism of youth, eager to control what seemed a great destiny, and in part the desire of the small property-owner for security against the advance of socialism. Fascist ideas found a ready acceptance wherever men were ambitious of power or apprehensive of novelty. As a soldier in the late war, Mussolini could

claim a part in the victory. As a former member of the Socialist Party, he had the credit which always attaches to those who abandon unpopular views. The small bands of his supporters grew rapidly until they were the one organized and disciplined party in the state. They were able by direct action to drive out the socialists from their municipal strongholds. They met criticism and dissent not by words but by deeds. They destroyed the printing-presses of their opponents. They broke up public meetings. They beat strikers into submission. Where they encountered resistance, they did not hesitate even at assassination to enforce their will. The district authorities were cowed into submission to their local leaders. They infected the army and navy with their spirit; and the government did not dare to challenge their power. Mussolini, as chairman of the central council, exacted and received an iron obedience from his followers. They were organized like an army; they wore a uniform. By the summer of 1922 Mussolini had half a million soldiers under his command. The time had come to move from the atmosphere of influence to the realm of government. He marched to Rome. The cabinet resigned its authority into the King's hands; and the latter had no alternative save to make Mussolini Prime Minister.

He was not even within sight of a parliamentary majority; but the Chambers abdicated before his avowed contempt for them. Either, he asserted, they must accept his will, or he would act without regard to their constitutional power. The ethos of Italy was incarnate in himself; and to oppose him was to invite disaster. The result was a remarkable triumph of dominant personality. The deputies did not hesitate to surrender their authority;

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if they criticized, they were beaten in the street or subjected to humiliating personal attack. Foreign policy and domestic policy alike were simply the will of Mussolini. His followers became the national militia. . . .

He has openly thrown overboard all pretense of majority-rule. He will obtain power not because the mass of the electorate supports his views, but because his followers will not allow opposition to make itself heard. Government, for him, exists to fulfil needs, not to give effect to wills; and its first requirement is an overwhelming strength incompatible with liberty. For liberty, indeed, Mussolini professes no affection. He has called it a nineteenth-century concept which has exhausted its utility. Liberty, for him, is the parent of anarchy if it implies hostility from opponents, and the proof of disloyalty, involving expulsion from the party, if it comes from his declared supporters. . . .

The historian of the next generation cannot fail to be impressed by the different reception accorded to the changes of which Lenin and Mussolini have been the chief authors. Where Lenin's system has won for itself international ostracism and armed intervention, that of Mussolini has been the subject of widespread enthusiasm. He himself has been decorated by the governments of foreign powers; ambassadors have exhausted the language of eulogy at official banquets; and great men of business have not hesitated to say that only the emulation of his methods can reduce the working classes to a proper state of mind. Yet, save in intensity, there has been no difference in the method pursued by the two men; and it is difficult to avoid the conclusion that the different reception of their effort is the outcome of their anti-thetic attitudes to property.

Yet the danger implicit in each philosophy is a similar one. . . .

Lenin

Victor Chernov

March 1924

VICTOR CHERNOV, *Russian Social-Revolutionary writer; Minister of Agriculture in the Kerensky Government.*

. . . Lenin was a great man. He was not merely the greatest man in his party; he was its uncrowned king, and deservedly. He was its head, its will, I should even say he was its heart were it not that both the man and the party implied in themselves heartlessness as

a duty. Lenin's intellect was energetic but cold. It was above all an ironic, sarcastic, and cynical intellect. Nothing to him was worse than sentimentality, a name he was ready to apply to all moral and ethical considerations in politics. Such things were to



BRUNO BARBEY/MAGNUM PHOTOS

Modern man: Arbat Square, Moscow, 1967

him trifles, hypocrisy, “parson’s talk.” Politics to him meant strategy, pure and simple. Victory was the only commandment to observe; the will to rule and to carry through a political program without compromise, that was the only virtue; hesitation, that was the only crime.

It has been said that war is a continuation of politics, though employing different means. Lenin would undoubtedly have reversed this dictum and said that politics

is the continuation of war under another guise. The essential effect of war on a citizen’s conscience is nothing but a legalization and glorification of things that in times of peace constitute crime. In war the turning of a flourishing country into a desert is a mere tactical move; robbery is a “requisition,” deceit a stratagem, readiness to shed the blood of one’s brother military zeal; heartlessness towards one’s victims is laudable self-command; pitilessness

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and inhumanity are one's duty. In war all means are good, and the best ones are precisely the things most condemned in normal human intercourse. And as politics is disguised war, the rules of war constitute its principles. . . .

. . . His power lay in the extraordinary, absolute lucidity—one might almost say the transparency—of his propositions. He followed his logic unflinchingly even to an absurd conclusion, and left nothing diffuse and unexplained unless it were necessary to do so for tactical considerations. Ideas were made as concrete and simple as possible. This was most evident in Lenin's rhetoric. He never was a brilliant orator, an artist of beautiful speech. He would often be coarse and clumsy, especially in polemics, and he repeated himself continually. But these repetitions were his very system and his strength. Through the endless re-digesting, uncouth pounding and clumsy jokes there throbbed a live, indomitable will that would not be deviated by an inch from the appointed path; it was a steady, elemental pressure

whose monotony hypnotized the audience. . . . Besides, Lenin always *felt* his audience. He never rose too high above its level, nor did he ever omit to descend to it at just the necessary moment, in order not to break the continuity of the hypnosis which dominated the will of his flock; and more than any one he realized that a mob is like a horse that wants to be firmly bestrode and spurred, that wants to feel the hand of a master. . . .

Yes, Lenin was good-natured. But good-natured does not mean good-hearted. . . . So far as we can guess, real good-heartedness most probably was considered by him one of the pettiest of human weaknesses. . . . He devoted his whole life to the interests of the working class. Did he love those working people? Apparently he did, although his love of the real, living workman was undoubtedly less intense than his hatred of the workman's oppressor. His love of the proletariat was the same despotic, exacting, and merciless love with which, centuries ago, Torquemada burned people for their salvation. . . .

Stalin's Power

Paul Scheffer

July 1930

PAUL SCHEFFER, *for some years correspondent of the Berliner Tageblatt in Moscow, now stationed in Washington.*

. . . Stalin is not a man who appeals to the sympathies of crowds or stirs their imaginations. He is not an electric person.

Let us be more blunt: he is frankly unattractive, and all the more so since he knows he is, and shows by his demeanor that

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he does not care! Even his voice, a voice as hard and brittle as glass, lacks the undertones, the rhythm, that work so powerfully upon the music-loving populace of Russia. . . . You feel at once that he is “dangerous.” . . .

Stalin never belonged to the brilliant group which gathered in Russia from all lands after the February Revolution and to which history has ascribed the triumph of the Revolution of October 1917. . . . He saw himself as the one to whom the “dirty work” had been left. He liked to refer to himself as the “hall sweeper” of the Revolution. And now, in the hour of victory, he was being admitted to the inner councils of the leaders grudgingly if at all. The eyes of the aroused populace stubbornly looked past him to men who had the knack of holding the immense followings who came trooping to “the Cause” that year, men who knew how to make ringing speeches, mouth big ideas, rattle off fine theories—the Lenins and the Trotskys, the Zinovievs, the Radeks, and the Bukharins. For Stalin, all such were “Europeans,” “émigrés.” He had been the one, after the grievous failure of 1905, to keep the fires of revolution glimmering in Russia. In the first year of the new régime, he felt that they regarded him as necessary but did not take him at full value. In their eyes, he was still the “savage from the Caucasus,” the man with more fist than brain, more nerve than intelligence—a fanatic. All the more keenly, therefore, did he feel the slight that was never uttered. . . .

It is evident, now, that all along he felt that his hour would come. He had at his disposal, in a way no one else could have, an immense acquaintance with the 150 million inhabitants of Old Russia. In those

swarming masses he knew just which individuals were the men to realize and sustain a proletarian revolution such as he conceived in that still barbaric country. The hypnosis of crowds and the frenzy of words of the first year, then the inspired and inspiring civil crusade against the remnants of Tsardom and its allies, must some day come to an end. It would then be a question of governing people no longer hypnotized, of using ways and means for forcing the masses together independently of such ephemeral throngs. No one knew Russia as Stalin did. No one realized as he realized what it meant to set up a single class of people, the proletariat—3 millions of human beings in a land far from being industrialized—as the only class entitled to live, the only class entitled to rule, and then to drag 135 millions of peasants along in the same direction. Stalin also knew, as no one else knew, where to find the people who could be used in such a project: people of his mind and of his hardness, who were willing to look at the world only from below up; people of his origins, with undying animosities against everything “bourgeois” and against the arrogance and pretentiousness of the “intellectuals” who now claimed they had “made the Revolution!” . . .

Some four months before his death, Lenin broke with Stalin. . . .

What worried Lenin in Stalin’s case was the latter’s secret, slinking, anonymous expansion of his personal power in the party and his preference for the backstairs to more conspicuous routes. The tactics which Stalin was later to use with such success against Trotsky, first to silence him and then to reduce him to complete helplessness, he used against Lenin, the moment the latter fell sick. . . .

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. . . Looking back over these past years, one can remark only with astonishment how every one of Lenin's close associates, and later of Stalin's own associates, was shortly treated as a rival and a climber. . . .

. . . Stalin . . . is the dictator of dictators. Only, he prefers not to look the part. He is not Mussolini. Yet he has one trait in common with Mussolini—an extraordinary suppleness and pliancy—and he demonstrates it under a more difficult test. He has acted in full cognizance of the danger that lies in the usurpation of power by a small minority over a vast majority whose interests do not coincide. . . . He has not taken much stock in the myth of unity between workers and peasants, however much he may have supported the notion for propaganda purposes so long as it worked. He realized, with courageous insight, the futility of Lenin's conception of the NEP. He understood, without

shirking any responsibilities, that active socialism and private initiative were incompatible in the same economic area, and he acted resolutely on the perception that the only salvation for the Soviet power lay in the ruthless socialization of the entire country, irrespective of the immediate consequences. These became very evident at once through the crisis in agriculture and through hunger in the towns. . . . The fact that he reckoned with all these factors more accurately, more resolutely, with less disposition to compromise than his opponents and even than his some-time associates, has enabled him to achieve what he has achieved. His success is closely bound up with his perception of these factors. At the same time his success seems to be inseparably bound up with Lenin's characterization of him: "crude and narrowminded." . . .

Making the Collective Man in Soviet Russia

William Henry Chamberlin

January 1932

WILLIAM HENRY CHAMBERLIN, *for some years correspondent of the Christian Science Monitor in Soviet Russia; author of "Soviet Russia."*

The individual human personality is fighting a losing battle against heavy odds in Russia today. When one hears of state planning in the Soviet Union one usually thinks of factories, steel plants, large grain farms and cotton plantations, tractors and other accessories of industrialization. What

is perhaps not generally realized is that man himself is the first and most important objective of Soviet planning and that the tendency to replace man, the individual, by collective man, the product of social groups and forces, is one of the most important and interesting currents in Soviet life. . . .



ESTATE OF ALEXANDER RODCHENKO/RAO, MOSCOW/VAGA NEW YORK

On parade: Soviet sailors in Red Square, 1936

From the cradle to the grave the life and thought of the Soviet citizen are mapped out for him so far as external influences can be mobilized to achieve this end. The Soviet child about the age of eight is apt to join the Young Pioneers, an organization which numbers more than four million members and is steadily growing. From the moment when young Vasya and Sonya put on the red scarf that is the distinguishing sign of the Young Pioneer a process of intensive propaganda begins, of which a part consists in giving them definite tasks to do. Thus Young Pioneers are not only taught to disbelieve religion; they are encouraged at Christmas time to go around and convert those “backward” children who may still want to have Christmas trees and celebrate the holiday in the traditional manner. . . .

No meeting of workers or employees for the election of delegates to the Soviet is complete unless a troop of Young Pioneers marches in and, through its leader, gravely

announces its “nakaz,” or set of instructions for the future Soviet delegates. . . . When a “chistka,” or purge, of Soviet institutions and offices is in progress it is not uncommon for a ten-year-old Pioneer to stand up, after some preliminary coaching, and solemnly denounce some middle-aged official or professor as a bureaucrat or a saboteur. . . .

Of course not all Russian children are Young Pioneers. But almost all children in Russia now attend primary school, at least for three or four years; and the present school is almost as much of a forcing-ground for the inculcation of communist ideas as the Young Pioneer organization itself. . . . A good dose of the Five Year Plan is inserted into every course of study, and a bust or picture of Lenin is to be found in almost every schoolroom. Children are politically propagandized in the schools from a very early age, even to the point of being pressed to vote approval for sentences of execution which are passed upon accused counter-revolutionaries and saboteurs.

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From the Young Pioneers it is a natural upward step to membership in the Union of Communist Youth, an organization with a membership of more than four million young people between the ages of sixteen and twenty-three. Here the clay of human personality that has been given preliminary shape in the Pioneer stage is subjected to further and more vigorous psychological kneading. . . . Not only is theoretical training in the teachings of Marx and Lenin intensified for the Young Communists; but they are given the most effective kind of propaganda, the propaganda of action, that finds expression in various ways. Sometimes groups of Young Communists, without their distinctive uniforms, will descend on a store, factory, office or public institution, take notes on any real or supposed cases of inefficiency or bureaucracy which they may discover and report their discoveries to higher authorities. . . .

The tremendous pressure of “obshestvennost,” which might be loosely translated as organized public opinion, does not slacken when the Soviet citizen grows out of the Communist Youth age and takes up his regular work in life. True, the proportion of the adult population enrolled in the Communist Party and subject to its severe discipline is much smaller than the percentage of young people who wear the red scarf of the Young Pioneers or the khaki uniform of the Young Communist. But other agencies, such as the trade-unions, which were rather aptly described by Lenin as “schools of communism,” continue the work of molding individuality and repressing it when it comes into conflict with the supposed interests of the social organism as a whole. . . .

Moreover, it is difficult for anyone living outside of Russia to understand the tremendous machinery for the regimentation of the individual which exists when every agency of information and entertainment—the press, the radio, the drama, the motion-picture—is centrally controlled for the purpose of making people communistically minded. . . .

When the Soviet citizen picks up his newspaper, no matter which one it may be or whether it is published in Moscow, Kharkov, Tiflis or Vladivostok, and no matter whether it is printed in Russian, Ukrainian, German, Tatar or any one of the other numerous languages of the Soviet Union, he gets precisely the same picture of political and economic events, often expressed in virtually identical phraseology. . . .

The radio, which is entirely under state or public control, broadcasts a vast amount of political agitation and economic exposition. The Soviet citizen cannot escape from the Five Year Plan by going to a new play, which in most cases will be a dramatized story of the building of some new enterprise, or by going to the motion-picture theater, where the newsreel certainly and the film quite probably will be full of excavators, cranes, pulleys and blast-furnaces. Even concerts are often accompanied by short explanatory lectures in which the class origin of the composer is analyzed and his music is discussed as reflecting both his origin, whatever it may be, and the general historical problems of his time. . . .

So the individual personality is attacked from every side by forces which are all controlled from a common center and which are working in accordance with a prearranged plan to remake the traditional human individualist into a collective man, a citizen of the future communist society. . . .

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The Philosophic Basis of Fascism

Giovanni Gentile

January 1928

GIOVANNI GENTILE, *philosopher and member of the Italian Senate; Minister of Public Instruction in the first Cabinet of Premier Mussolini, during which time he put into effect the so-called "Gentile Reform" of Italian education.*

. . . In the definition of Fascism, the first point to grasp is the comprehensive, or as Fascists say, the "totalitarian" scope of its doctrine, which concerns itself not only with political organization and political tendency, but with the whole will and thought and feeling of the nation.

. . . Fascism is not a philosophy. Much less is it a religion. It is not even a political theory which may be stated in a series of formulæ. The significance of Fascism is not to be grasped in the special theses which it from time to time assumes. When on occasion it has announced a program, a goal, a concept to be realized in action, Fascism has not hesitated to abandon them when in practice these were found to be inadequate or inconsistent with the principle of Fascism. Fascism has never been willing to compromise its future. Mussolini has boasted that he is a *tempista*, that his real pride is in "good timing." He makes decisions and acts on them at the precise moment when all the conditions and considerations which make them feasible and opportune are properly matured. . . .

Is Fascism therefore "anti-intellectual," as has been so often charged? It is eminently

anti-intellectual . . . if by intellectualism we mean the divorce of thought from action, of knowledge from life, of brain from heart, of theory from practice. Fascism is hostile to all Utopian systems which are destined never to face the test of reality. It is hostile to all science and all philosophy which remain matters of mere fancy or intelligence. . . . Fascist anti-intellectualism holds in scorn . . . the man who plays with knowledge and with thought without any sense of responsibility for the practical world. It is hostile not so much to culture as to bad culture, the culture which does not educate, which does not make men, but rather creates pedants and aesthetes, egotists in a word, men morally and politically indifferent. . . .

For Fascism, . . . the State is a wholly spiritual creation. It is a national State, because, from the Fascist point of view, the nation itself is a creation of the mind and is not a material presupposition, is not a datum of nature. The nation, says the Fascist, is never really made; neither, therefore, can the State attain an absolute form, since it is merely the nation in the latter's concrete, political manifestation. For the Fascist, the State is always *in fieri*.

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It is in our hands, wholly; whence our very serious responsibility towards it. . . .

The Fascist State . . . is a people's state, and, as such, the democratic State *par excellence*. The relationship between State and citizen (not this or that citizen, but all citizens) is accordingly so intimate that the State exists only as, and in so far as, the citizen causes it to exist. Its formation therefore is the formation of a consciousness of it in individuals, in the masses. Hence the need of the Party, and of all the instruments of propaganda and education which Fascism uses to make the thought and will of the *Duce* the thought and will of the masses. Hence the enormous task which Fascism sets itself in trying to bring the whole mass of the people, beginning with the little children, inside the fold of the Party. . . .

The Fascist conception of liberty merits passing notice. The *Duce* of Fascism once chose to discuss the theme of "Force or Consent?;" and he concluded that the two terms are inseparable, that the one implies the other and cannot exist apart from the

other; that, in other words, the authority of the State and the freedom of the citizen constitute a continuous circle wherein authority presupposes liberty and liberty authority. For freedom can exist only within the State, and the State means authority. . . .

Liberalism broke the circle above referred to, setting the individual against the State and liberty against authority. What the liberal desired was liberty as against the State, a liberty which was a limitation of the State. . . . Fascism has its own solution of the paradox of liberty and authority. The authority of the State is absolute. It does not compromise, it does not bargain, it does not surrender any portion of its field to other moral or religious principles which may interfere with the individual conscience. But on the other hand, the State becomes a reality only in the consciousness of its individuals. And the Fascist corporative State supplies a representative system more sincere and more in touch with realities than any other previously devised and is therefore freer than the old liberal State.

Radical Forces in Germany

Erich Koch-Weser

April 1931

ERICH KOCH-WESER, *former Minister of Justice of the German Republic, recently leader of the Democratic Party.*

Economic depression and political radicalism go hand in hand. When economic distress reaches a certain point, the individual citizen no longer uses his political

power to serve the public weal, but only to help himself. His ideal of political liberty pales before his ideal of economic equality.

How We Got Here

Once this sentiment has eaten its way into the hearts of the majority of a nation, any political system is doomed to failure. It is useless to tell the embittered masses that their political and economic rulers are not responsible for their misfortunes. It is equally useless to point out to them that a revolution with its attendant disorders would not improve their situation, but would hopelessly compromise it. The world is not ruled by reason, but by passion, and when a man is driven to despair he is ready to smash everything in the vague hope that a better world may arise out of the ruins.

Intelligent and orderly as the German people are, patiently as they have borne the sufferings of war and of inflation, they are in danger today of falling into this reckless state of mind. It would seem that the economic crisis, the reduction of large classes of the German population to the level of the proletariat, and the unemployment of nearly five million persons, cannot go on for many more years without ruining the German nation as a whole. Here is a population, well-equipped from the point of view of health and intellect, which in general is forced to be satisfied with an income barely sufficient for a minimum existence. One-eighth of those who are able and eager to work are unable to find any opportunity to do so. And those who are employed see no possibility of little by little rising to positions where their abilities will have fuller scope. Above all—and this is perhaps the worst aspect of the situation—not only are great numbers of persons forced to abandon any hope of advancement themselves but they must also relinquish the idea of giving their children an adequate education and thus opening up a way for them to better their situation. . . .

The consequence is a pronounced and inclusive dissatisfaction with the prevailing economic system. All the blame for every ill is laid on the shoulders of the capitalistic system, despite the fact that it has been hampered and weakened to a considerable degree by governmental interference. The number of people who feel confident that they can get on by their own abilities is steadily declining. You will recall the saying that Napoleon's soldiers were inspired by the belief that each of them carried a marshal's baton in his knapsack. Perhaps this was not really the case. But certainly it is one of the secrets of success of any efficient régime not to allow the feelings of self-reliance and self-help which exist in a nation to go to waste. America has managed things better in this respect than have the nations of the old world. In Germany, the self-made man is no longer the ideal of the people. This marks the end of the "bourgeois" way of thinking in the best sense of that word. The number of those who are beginning to think in terms of socialism is increasing. The adherents of the middle parties, who oppose this development, are dwindling in the same proportion that the number of independent, progressive and self-reliant citizens is being diminished through the increasing pauperization.

Of the non-bourgeois parties, the Social Democratic Party, notwithstanding its general socialistic attitude, is the one that cares least about remodeling the state in the socialistic sense. This is not so strange as it sounds. This party, which is still by far the strongest political group in Germany, consists of brain and manual workers, employees, foremen, small officials and peasants. It is proletarian in name, but actually the individuals who compose it

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have attained a greater degree of lower-middle-class security than have many of those in the ranks of the old bourgeoisie. This is partly the result of extensive social legislation, but in the main it is due to the protection offered by the trade-unionist organization. In these times of economic distress it has been unable to hold its own in open economic strife with the capitalists, but thanks to its power at the polls it nevertheless has been almost completely successful in averting the reductions of wages which would otherwise have accompanied increasing unemployment.

. . . For the time being, . . . it is almost completely absorbed in the ungrateful but historically significant task of keeping alive, in wide circles of the population, a sense of order and an appreciation of the value of the state. . . .

The attitude of the Communist Party is totally different. It constitutes a reservoir for all those proletarians who—either without fault or by their own fault—have failed to find suitable employment or adequate wages. Of the great altruistic idea of communism there is not a trace to be found in this party. The watch-word is not the Christian one, “What is mine shall be thine,” but rather one of envy, “What is thine shall be mine.” The blind submission shown by the leaders of the party towards edicts issued by Soviet Russia increases its danger to Germany, as does also their financial dependence on Moscow. But—leaving out of account some disgruntled writers who are not in touch with world currents—the party members are recruited from the lower strata of the working classes. Unless the distress among the German people should become insupportable, any sudden advance movement on their part that relied on force

would be doomed to failure without armed support and assistance from outside.

Greater danger is threatening at the present time from the National Socialists, popularly called the Nazis. This movement comprises the large ranks of the disinherited and the *déclassés*—middle-class citizens, officials, officers and landowners. All of these deserve our sympathy and pity. Enormous numbers of them have been uprooted from a satisfactory social position by war, revolution and inflation, and thrust out to seek an uncertain and penurious existence. . . . The success of the party lies principally in the fact that those who belong to it despair of ever again being able to win a substantial share of the goods of this world or to secure a higher post than the one they fill today.

The National Socialist Party offers the advantage that one may indulge in cheap socialism, or rather in a socialism of envy, without having at the same time to forego class-consciousness or a sense of superiority over the proletariat. Both the membership and the political aims of the party show extraordinary variations. Some of its members condemn the present Republic on account of its ruthlessness in breaking loose from the old traditions of the German people. Others blame it for being lukewarm about the necessity for a new social order. That is why nobody knows exactly what their “third empire” would be like. They call themselves socialists, and probably really mean to be. But they use the word “Marxists” as a term of opprobrium and reserve it for their adversaries. Their “socialism” is hatred of capitalism; their “Marxism” is hatred of social democracy. Whether this party will ever make up its mind to take the leap and try an assault upon the Republic is extremely doubtful.

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And after all, it comprises at present not more than one-fifth of the population. Moreover, it is animated by a club or fraternity spirit more than by the sort of will which resorts to revolutionary measures. But no matter whether its deeds remain undone or whether it succeeds in temporarily

usurping power or a slice of power, the main danger in the long run will be that it has no goal to attain. It therefore is bound to lead the hosts of its disappointed adherents not to a victory of reason but to some sort of embittered union of forces with left-wing radicalism. . . .

Hitler: Phenomenon and Portent

Paul Scheffer

April 1932

PAUL SCHEFFER, *Washington correspondent of the Berliner Tageblatt, formerly correspondent in Soviet Russia, author of "Sieben Jahre Sowjet Union."*

. . . Hitler is the most successful orator that Germany has ever possessed. . . . It is an interesting and a stirring experience to listen to Hitler—his bitterest enemies have often fallen under his spell. And it is very instructive to examine his audiences. The hall where he is to speak often closes its doors an hour before the meeting is scheduled to begin because it is already filled to overflowing. One always sees a clean, neatly-dressed crowd with faces that betray intellectual pursuits of one kind or another: clerks, professors, engineers, school teachers, students, civil service employees. These audiences are preoccupied, chary of words, quiet. Their faces are tense, often drawn. The only bustle in the room will come from the "hall guards," a typical product of these new times—rough young fellows—the *Sturm Abteilungen*, or "shock troops." The predominant element in the picture

is what is so aptly described in Germany as the "de-classed" middle class: creatures visibly down at the heel, spiritually crushed in the struggle with everyday reality, distraught under a perpetual worry about the indispensable necessities of life. One notes many young people among them. All in all, it is an exceedingly variegated mixture of types from the past, from the present, and one might almost say from the future of Germany: it is that famous "brew" into which Germany, once so stably articulated in her classes and callings, has dissolved during these past ten years as a result of economic disaster, unemployment and shifts in power. They are all people who have had conceptions of life, and conceptions of their personal rôles in life, with which their present situation stands in violent contrast. Often they are people who

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have been pushed aside, people who have not been admitted to German life under present-day conditions. . . .

Even if the observer had never heard of Hitler's program he might guess what this depressing assemblage of people is waiting for. It is waiting for a gospel, a message, a Word that will release it from the pinch of want, something that will compensate for the unbearable limitations of its present mode of existence. It wants to get hold of an ideal that will guide it forth from the quagmire where it finds itself. It wants to hear an assurance that it is entitled to a place in this new world. The man who can lift these people from their depression of spirit even for the space of an hour can win them to himself and to the cause that he tells them represents the substance of "liberation." A situation for a great orator! A great situation for an orator!

Hitler's adversaries are right in charging that such an audience can easily be misused. Hitler's utterances on the subject of propaganda, both from the platform and in print, show in fact that he is willing to use any means which he judges serviceable in winning adherents to his cause. He fans the flames of hatred just as unscrupulously as he arouses the most exaggerated hopes.

However, let us keep to his audiences. What is it that stirs them? What keys can Hitler strike with such effect that he can drag millions of people whithersoever he chooses?

Fundamentally it is a question of the hard times which have settled over Germany ever since the war. Great fortunes have come into being, though they are probably more apparent than real. Meantime, statistics show that as regards the middle classes, which used to be Germany's backbone, the standard of living is far below

the pre-war level. Since 1929 it has sunk to unprecedented depths. Hitler turns his guns against those people who have increased their fortunes disproportionately to the general average of wealth accumulation in Germany, and especially against the anonymous wealth of the trusts—"coupon slavery." He attacks reparations which are sapping the life-blood of Germany. . . .

Hitler berates "Marxism," denounces and vilifies it. In this lies a very instructive portion of his propaganda and of his fanaticism. Unquestionably it is his most emphatic theme. The people before him are Germans. Can they, as Germans, consent that a large number of their fellow-citizens, the industrial workers, should be taught that in the last analysis they are more closely bound up with the working classes in other lands than with their own countrymen who do not happen to be "proletarians?" The people who are sitting in front of Hitler have, for the most part, sunk below the standard of living of a German workingman with a job. As for some of the others, there is only a slight difference between their income and the wages of a workingman. For all that, they do not think of themselves as proletarians. That they do is one of Moscow's illusions. Quite the contrary! On that very account they insist that they prefer to live in a state that is not governed by workpeople, a state that knows no discriminations of class—not a state according to the ideals which Marx set up for his state of workmen, where the proletariat hold the power and set the tone. On just such grounds they want to be "national." From just such feelings nationalism has taken on a new meaning and impetus, not only in Germany, but in Italy and other countries.

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To the same extent these people feel strangers to the “forces of wealth.” They have nothing—just as the working classes have nothing. Hence the surprising mixture of concepts apparent in the baroque expression, “National Socialism.” The effects of the capitalist system also weigh down upon them. They hate “the plutocrats.” Their battle cry is about what they call the “Jewish financial tyranny,” an artificial scarecrow, devised *ad hoc*, and aimed at one individual or another. Propaganda requires such things. . . .

In Germany, as everywhere else, there are great differences in degrees of popular education; but such differences have greater social significance in Germany than in other countries. They create sharper distinctions between one individual and another. Hitler is against all that. He is fighting for the right of the half-educated to their own picture of the world, to a culture which is illumined by love of country. He shouts at the university students that they are not worthy of pursuing their scholarly studies if they cannot find a common ground with the mechanic who is intent on serving his country. . . . Hitler himself is a self-educated person, a thorough-going “autodidact,” and he has read in many directions. In his eyes the essential thing is not high intellectual finish, but active love of country and mutual understanding among all. . . . Hitler’s idea is to give the people a common meeting ground of convictions which abolish all distinctions and in which all share. Cultural differences must yield to patriotic sentiments, not result in divisions between individuals and classes. This expresses itself in attacks on the intellectuals whom the plain man least understands.

What unites all of Hitler’s listeners is a feeling of humiliation, of injured self-respect. This comes into play in many directions, economic, social, cultural. And even diplomatic! For it is a quite natural thing that all these feelings of hurt should gather and precipitate about the rôle which Germany has been playing in the world since Versailles. While, with some undulations, the international position of Germany has been improving, this relative increase in her prestige has made no great impression on the German masses. Discriminations against Germany within the world of nations have, on the other hand, been generally noticed by the plain people. By dint of careful nursing, the notion of reparations has been transmuted into the notion of “payments of tribute;” and economic distress has found in reparations an explanation that is clear and convincing to everybody. The same is true of social unrest. The people who sit before Hitler have in their minds a very clear picture of the forces that are determining their present situation, and it is not difficult to carry them on to the corollaries. Hitler can lay hold on them in their innermost sensibilities when he raises his cry for unity, promises them the “respect” of the world as the fruit of unity, and tells them that Germany can have no foreign policy—on this theme he harps in every conceivable connection—until she has made herself one. No party in Germany has a formula so simple. No party has gone to the trouble of understanding this particular class of people as Hitler has done. That is why he has succeeded in leading such an astonishing following whithersoever he will. . . .

Hitler's Reich: The First Phase

Hamilton Fish Armstrong

July 1933

HAMILTON FISH ARMSTRONG, *Editor of Foreign Affairs.*

A people has disappeared. Almost every German whose name the world knew as a master of government or business in the Republic of the past fourteen years is gone. There are exceptions; but the waves are swiftly cutting the sand from beneath them, and day by day, one by one, these last specimens of another age, another folk, topple over into the Nazi sea. So completely has the Republic been wiped out that the Nazis find it difficult to believe that it ever existed, at any rate as more than a bad dream from which they were awakened by the sound of their own shouts of command, their own marching feet. . . .

Not merely is he wiped out, but the memory of him is wiped out. It is pretended that he never was. His name is not mentioned, even in scorn. If one asks about him, a vague answer is given: "Oh yes—but is he still alive? Maybe he is abroad. Or is he in a nursing home?" This does not merely apply to Jews and Communists, fled or imprisoned or detained "for their own protection" in barbed-wire concentration camps. It applies to men like Otto Braun, leader of the great Social Democratic Party, perennial Premier of Prussia. . . . It applies to the series of Chancellors furnished by the once-powerful Center Party. . . . The generals who were talked about as embryo dictators—von Seeckt, Groener,

even the powerful von Schleicher—are no more heard of or seen. . . . Stresemann is not merely dead, but has been dead as long as the last Pharaoh. The men who ruled Germany in these fourteen years have been swept away, out of sight, out of mind, out (according to the program of Dr. Goebbels, propagandist-in-chief) of history. . . .

The Stahlhelm, the organization of front-line veterans, credited with having saved the country from anarchy and communism in several post-war crises, but feared by the Nazis as a possible rival to their *S.A.*, has been broken and subjected. . . .

The Reichswehr, on which General von Schleicher counted and which as recently as last December could and would have supported him in a determined move to establish authority in the name of the flickering Republic, now stands glumly aside. . . . All that its leaders can do is wait (as the Royal Italian Army has waited without result) to see whether there will ever come a moment of chaos when they might step in to reestablish the state they were enlisted to serve. It is a forlorn hope.

One by one continue to fall the last possible citadels of defense against uncontradicted Nazi dictatorship.

Federal Germany is gone. The *Gleichschaltung* law disposes of the prerogatives of the separate States, and Nazi leaders



ASSOCIATED PRESS

Fighting words: Adolf Hitler in Berlin, May 1, 1938

have been named *Statthalter*, with power from Berlin to dismiss State governments should they not prove fully amenable. Eminent Lutheran and Reformist theologians are hastily forming a new and unified *Reichskirche* to meet the fear of the Nazis that opposition or weakness might develop in the former 28 autonomous churches in the various States, and to simplify their drive against religious organizations which are not two parts blood and iron and only one part milk of human kindness. The Socialist trade unions . . . were finally seized outright on May 2, the day after the celebration of the "Festival of National Labor." Their buildings were occupied by storm troops, their officers were jailed, and their funds were appropriated to the new Nazi union which is now organizing all labor as an instrument of party will. . . .

The judiciary has been weeded over with minute care, and as a result many judges . . . have either resigned or been dismissed. Henceforth, says a circular of the Prussian Ministry of Justice, judges will be tested for their patriotism and social principles and will be put through periods of service in military camps to school them in "martial sports." In Nazi eyes the conception of abstract justice is outworn. The essential justice is that which serves the higher ends of the state.

Even the great Nationalist Party, co-partner with the Nazis in the March election which followed the fall of von Schleicher, and supported by all the clans of Junkers, monarchists, landed proprietors, former army officers and officials, is left hanging in the air, its toes barely touching the ground, slowly strangling

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in the noose of its own devising. When on the night of January 30 von Papen persuaded Hitler to join him in making the election, he thought that he had prepared the way for his own conservative forces to swallow up the Nazis. But it was the reverse which happened. . . .

These new rulers of this new people have also a new vocabulary. In literature and art, in the professions and even in sport, new specifications replace taste and skill and experience. . . . A work of art or a performance of any sort is not good unless the creator is an Aryan, preferably Teutonic to the last drop of his blood (if such a being exists), preferably a Nazi, and in any case not a liberal or a Jew. Music, the theatre, the cinema, all have been bent to Nazi propaganda aims. The universities are being "cleansed." . . . The press has also been "assimilated," unfriendly or lukewarm or liberal or pacifist or "internationalist" or Jewish proprietors, editors and correspondents have been expelled, and Nazi commissars put at the side of the

writers who remain. Attention is centered almost exclusively upon news of the revolution—texts of proclamations, speeches of leaders, accounts of mass meetings and celebrations. . . .

The German Republic was a puny plant. Beneath the inch or so of top-soil in which its seeds were hastily placed were a dozen unyielding strata, packed down and solidified by tradition and usage. The servitudes of a punitive peace treaty, the galling preponderance of France and her allies in Europe, the economic distress following the defeat and the inflation, all these hindered its growth. The cultivators, from Ebert and Scheidemann through Stresemann and Brüning down at last to von Papen and von Schleicher, cared less and less about saving it. . . . But the final determining condition which caused the Republic's death was that it had no nourishment from below. As an eminent German said to the writer two or three years ago: "We made a republic; but there were no republicans." . . .

Political Ideas in the Twentieth Century

Isaiah Berlin

April 1950

ISAIAH BERLIN, *Fellow of New College and University Lecturer in Philosophy at Oxford; attached to the British Embassy in Washington, 1942–45, and in Moscow, 1945–46, with rank of First Secretary; visiting professor at Harvard, 1949; author of "Karl Marx" and other works.*

. . . The practice of Communist states and, more logically of Fascist states (since they openly deny and denounce the value of the rational question-and-answer

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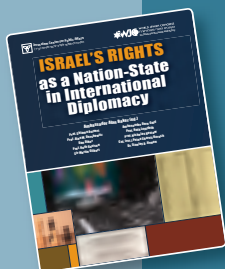
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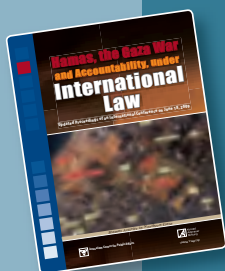
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Israel's Critical Security Requirements for Defensible Borders: The Foundation for a Viable Peace - Updated Edition

*Lt.-Gen. (ret.) Moshe Yaalon, Maj.-Gen. (res.) Yaakov Amidror, Maj.-Gen. (res.)
Uzi Dayan, Maj.-Gen. (res.) Aharon Ze'evi Farkash, Brig.-Gen. (res.) Udi Dekel,
Dr. Dore Gold, Dan Diker*

President Obama has declared that "the borders of Israel and Palestine should be based on the 1967 lines with mutually agreed swaps, so that secure and recognized borders are established for both states." But what are Israeli requirements for "secure" borders? This study presents a comprehensive assessment of Israel's critical security requirements for defensible borders.



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This monograph, based on updated proceedings of the Jerusalem Center's Global Law Forum conference, critically examines the laws of war, as well as their application to Hamas and its supporters and allies. It aims to produce workable suggestions for increasing legal accountability for Hamas and other similar non-state violators of international law in the age of terrorism, with contributions by Dr. Roy S. Schondorf, Col. (res.) Daniel Reisner, Maj.-Gen. (res.) Yaakov Amidror, Col. (ret.) Pnina Sharvit-Baruch, and others.

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method), is not at all the training of the critical, or solution-finding, powers of their citizens, nor yet the development in them of any capacity for special insights or intuitions regarded as likely to reveal the truth. It consists in something which any nineteenth century thinker with respect for the sciences would have regarded with genuine horror—the training of individuals incapable of being troubled by questions which, when raised and discussed, endanger the stability of the system; the building and elaboration of a strong framework of institutions, “myths,” habits of life and thought intended to preserve it from sudden shocks or slow decay. This is the intellectual outlook which attends the rise of totalitarian ideologies—the substance of the hair-raising satires of George Orwell and Aldous Huxley—the state of mind in which troublesome questions appear as a form of mental perturbation, noxious to the mental health of individuals and, when too widely discussed, to the health of societies. This is an attitude which looks on all inner conflict as an evil, or at best as a form of futile self-frustration; which considers the kind of friction, the moral or emotional or intellectual collisions, the particular kind of acute spiritual discomfort which rises to a condition of agony from which great works of the human intellect and imagination, inventions, philosophies, works of art, have sprung, as being no better than purely destructive diseases—neuroses, psychoses, mental derangements, genuinely requiring psychiatric aid; above all as being dangerous deviations from that line to which individuals and societies must adhere if they are

to continue in a state of well-ordered, painless, contented, self-perpetuating equilibrium.

This is a truly far-reaching conception, and something far more powerful than the pessimism or cynicism of thinkers like Plato or Machiavelli, Swift or Carlyle, who looked on the majority of mankind as unalterably stupid or incurably vicious, and therefore concerned themselves with how the world might be made safe for the exceptional, enlightened or otherwise superior minority or individual. For their view did at least concede the reality of the painful problems, and merely denied the capacity of the majority to solve them; whereas the more radical attitude looks upon intellectual perplexity as being caused either by a technical problem to be settled in terms of practical policy, or else as a neurosis to be cured, that is made to disappear, if possible without a trace. This leads to a novel conception of the truth and of disinterested ideals in general, which would hardly have been intelligible to previous centuries. To adopt it is to hold that outside the purely technical sphere (where one asks only what are the most efficient means towards this or that practical end) words like “true,” or “right,” or “free,” and the concepts which they denote, are to be defined in terms of the only activity recognized as valuable, namely, the organization of society as a smoothly-working machine providing for the needs of such of its members as are permitted to survive. . . .

Of Liberty

Benedetto Croce

October 1932

BENEDETTO CROCE, *Italian Senator, former Minister for Public Instruction, and author of "Filosofia dello Spirito," a philosophic system translated into many languages.*

... Communism, it is the fashion to claim, has passed from theory to practice and is being applied in Russia. But it is being practised not as communism but—in keeping with its inner contradiction—as a form of autocracy, as its critics had always predicted would be the case. . . .

... The Russian Communists have not solved, nor will their violent and repressive methods ever enable them to solve, the fundamental problem of human society, the problem of freedom. For in freedom only can human society flourish and bear fruit. Freedom alone gives meaning to life: without it life is unbearable. Here is an inescapable problem. It cannot be eliminated. It springs from the very vitals of things and stirs in the souls of all those countless human beings whom the Communists are trying to control and reshape in accordance with their arbitrary concepts. And on the day that this problem is faced, the materialistic foundations of the Soviet structure will crumble and new and very different supports will have to be found for it. Then, even as now, pure communism will not be practised in Russia.

... Even if such experiments should develop in other parts of Europe, the fact that other countries differ so from Russia in religion, civilization, education, customs,

traditions—in historical background, in short—would produce something quite new, whatever its name and appearance; or else, after an indeterminate period of blind groping and struggle, there would sooner or later emerge that liberty which is only another name for humanity.

For liberty is the only ideal which unites the stability that Catholicism once possessed with the flexibility which it could never attain, the only ideal which faces the future without proposing to mould it to some particular form, the only ideal that can survive criticism and give human society a fixed point by which from time to time to reestablish its balance. There are those who question the future of the ideal of freedom. To them we answer that it has more than a future: it has eternity. And today, despite the contempt and ridicule heaped upon it, liberty still endures in many of our institutions and customs and still exercises a beneficent influence upon them. More significant still, it abides in the hearts and minds of many noble men all over the world, men who though scattered and isolated, reduced to a small but aristocratic *res publica literaria*, still keep faith with it, reverently hallow its name, and love it more truly than ever they did in the days when no one denied or questioned

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its absolute sovereignty, when the mob proclaimed its glory and contaminated it with a vulgarity of which it is now purged. . . .

. . . In all parts of Europe we are witnessing the birth of a new consciousness, a new nationality—for nations are not, as has been imagined, data of nature but results of conscious acts, historical formations. Just as seventy years ago the Neapolitans and the Piedmontese decided to become Italians, not by abjuring their original nationality but by exalting and merging it in the new one, so Frenchmen and Germans and Italians and all the others will rise to becoming Europeans; they will think as Europeans, their hearts will beat for Europe as they now do for their smaller countries, not forgetting them but loving them the better.

This process of amalgamation is directly opposed to competitive nationalism and will in time destroy it entirely; meanwhile it tends to free Europe from the psychology of nationalism and its attendant habits of thought and action. If and when this happens, the liberal ideal will again prevail in the European mind and resume its

sway over European hearts. But we must not see in this rebirth of liberalism merely a way to bring back the “old times” for which the Romantics idly yearn. Present events, those still to take place, will have their due effect; certain institutions of the old liberalism will have to be modified and replaced by ones better adapted to their tasks; new governing classes, made up of different elements, will arise; and experience will bring forth new concepts and give a new direction to the popular will.

In this new mental and moral atmosphere it will be imperative to take up again the so-called “social” problems. . . . This is primarily a question for technical experts and statesmen, who will have to devise solutions suitable to the times and favorable to an increase of wealth and its more equitable distribution. It is a question for experts and statesmen; but they will be unable to fulfill their function or attain their ends unless liberty be there to prepare and maintain the intellectual and moral atmosphere indispensable to labors so arduous, and to quicken the legal systems within which their duties must be performed.

The Position and Prospects of Communism

Harold J. Laski

October 1932

HAROLD J. LASKI, *Professor of Political Science in the University of London; author of “The Dangers of Obedience” and other works.*

. . . The pre-war state-system emerged from the great conflict far more shattered than was apparent in the mood of vindic-

tive triumph embodied in the Peace of Versailles. . . . The necessities of war had given an enhanced status to the working-

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classes of the belligerent countries; and it was necessary to satisfy their new claims. . . .

For a brief period, the sudden prosperity of America (though much more confined than was generally realized) concealed from many the realities of the situation. It was argued that the condition of Russia was a special one; that, elsewhere, the problem was rather one of dealing with the excrescences of the capitalist system than with capitalism itself. As late as 1928 President Hoover felt able to announce to an awe-struck world that America had (under God) solved the problem of poverty. Two years later, it was clear that his announcement was premature. The world (including America) was caught in the grips of a depression more intense and more widespread than any recorded in history. The unemployed could be counted in millions in capitalist countries. The mood of pessimism was universal; men spoke gravely of a possible collapse of civilization. At a time when science had made possible a greater productivity than in any previous age, the problem of distribution seemed insoluble. . . . Thirteen years after the end of the war, the perspective of capitalist civilization revealed an insecurity, both economic and political, which made justifiable the gravest doubts of its future.

Russian development was in striking contrast. The Five Year Plan gave it an integrated and orderly purpose such as no capitalist country could rival. Productivity increased at a remarkable rate; unemployment was non-existent. If the standard of living was low compared with that of Great Britain or the United States, its tendency was to increase and not to decline. The whole population was united in a great corporate effort at material well-being in which there was the promise of

equal participation. Where Europe and America were sunk in pessimism, the whole temper of Russia was optimistic. The authority of its government was unchallenged; its power to win amazing response to its demands was unquestionable. Granted all its errors, no honest observer could doubt its capacity both to plan greatly and, in large measure, to realize its plans. No doubt its government was, in a rigorous sense, a dictatorship. No doubt also it imposed upon its subjects a discipline, both spiritual and material, such as a capitalist civilization would hardly dare to attempt. No doubt, again, its subjects paid a heavy price for the ultimate achievement to which they looked forward. Yet, whatever its defects and errors, the mood of the Russian experiment was one of exhilaration. While the rest of the world confronted its future in a temper of skepticism and dismay, Russia moved forward in a belief, religious in the intensity of its emotion, that it had a right to ample confidence in its future.

No one can understand the character of the communist challenge to capitalism who does not grasp the significance of this contrast. A hundred years ago the votaries of capitalism had a religious faith in its prospects. They were, naturally enough, dazzled by the miracles it performed, confident that the aggregation of its individual successes was coincident with the social good, happy in a security about the results of their investment which seemed to entitle them to refashion the whole world in their own image. The successful business man became the representative type of civilization. He subdued all the complex of social institutions to his purposes. Finance, oil, coal, steel, became empires of which the sovereignty

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was as unchallenged as that of Macedon or of Rome. Men so different as Disraeli and Marx might utter warnings about the stability of the edifice. Broadly speaking, they were unheeded in the triumphs to which the business man could point.

But those triumphs could not conceal the fact that the idol had feet of clay. The price to be paid for their accomplishment was a heavy one. The distribution of the rewards was incapable of justification in terms of moral principle. . . .

. . . The condition for the survival of an acquisitive society is twofold. There must be no halt in its power to continue its successes; and it must be able so to apportion their results that the proletariat do not doubt their duty to be loyal to its institutions. This condition has not been realized. Economic nationalism has given birth to a body of vested interests which impede in a fatal way the expansion of world trade. . . .

The failure to maintain the allegiance of the proletariat, though different in degree in different countries, is, nevertheless, universal. Its danger was foreseen by Tocqueville nearly a century ago. "The manufacturer," he wrote, "asks nothing of the workman but his labor; the workman expects nothing from him but his wages. The one contracts no obligation to protect, nor the other to defend; and they are not permanently connected either by habit or by duty. . . . The manufacturing aristocracy of our age first impoverishes and debases the men who serve it, and then abandons them to be supported by the charity of the public. . . . Between the workman and the master there are frequent relations but no real partnership." Everything that has happened since Tocqueville wrote has combined to give emphasis to his insight. . . .

Men, in short, accept a capitalist society no longer because they believe in it, but because of the material benefits it professes to confer. Once it ceases to confer them, it cannot exercise its old magic over men's minds. . . . Once its success is a matter of dubiety, those who do not profit by its results inevitably turn to alternative ways of life. They realize that the essence of a capitalist society is its division into a small number of rich men and a great mass of poor men. They see not only the existence of a wealthy class which lives without the performance of any socially useful function; they realize also that it is inherent in such a society that there should be no proportion between effort and reward. . . .

The social service state can only be maintained at a level which satisfies the worker in a period of increasing returns. Once its benefits have to be diminished, the moral poverty of capitalism becomes apparent to all save those who live by its preservation. There arises an insistent demand for economic and social equality—such a distribution of the social product as can rationally be referred to intelligible principle. Resistance develops to the normal technique by which capitalism adjusts itself to a falling market. The growth of socialism in Great Britain, the dissatisfaction with the historic parties in the United States, the rise of Hitlerism in Germany, the profound and growing interest, all over the world, in the Russian experiment, are all of them, in their various ways, the expression of that resistance. Men have begun to ask, upon a universal scale, whether there is not the possibility of consciously building a classless society in which the ideal of equality is deliberately given meaning.

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It is not, I think, excessive to argue that the experience of this generation leads most socially conscious observers to doubt the desirability of relying upon the money motive in individuals automatically to produce a well-ordered community. It is at least a matter of universal recognition that the collective intelligence of society must control all major economic operations. But the translation of that recognition into policy encounters difficulties of which the importance cannot be emphasized. For it asks men to part with power on an unexampled scale. It changes a system of established expectations profoundly rooted in the habits of mankind. It disturbs vested interests which are well organized, both for offense and defense, and accustomed by long tradition to have their way. No governing class in the history of the world has consciously and deliberately sacrificed its authority. . . . But the call to socialism, which the anarchy of capitalist society has produced, is, at bottom, a demand for economic egalitarianism in which the possessors are invited to sacrifice their power, their vested interests, their established expectations, for the attainment

of a common good they will no longer be able to manipulate to their own interest. . . .

Capitalist society . . . is running a race with communist society for the allegiance of the masses. The terms upon which the former can be successful are fairly clear. It has to solve the contradiction between its power to produce and its inability to distribute income in a rational and morally adequate way. It has to remove the barriers which economic nationalism places in the way of an unimpeded world-market. It has to remove the fear of insecurity by which the worker's life is haunted. It has to end the folly of international competition in wage-rates and hours of labor; it has to find ways of saving Western standards from the slave-labor of the East. It has, not least, to cut away the jungle-growth of vested interests which at present so seriously impair its efficiency. . . . Above all, perhaps, it has to find some way of removing from the clash of competing imperialisms those structures of armed power which, clothed in the garb of national sovereignty, make certain the perpetual threat of insecurity and, born of it, the advent of war. . . .

Nationalism and Economic Life

Leon Trotsky

April 1934

LEON TROTSKY, *leader in the October Revolution in 1917; Commissar for Foreign Affairs, 1917–1918; Commissar for War, 1919–1923.*

. . . The nineteenth century was marked by the fusion of the nation's fate with the

fate of its economic life; but the basic tendency of our century is the growing



NATIONAL ARCHIVES AND RECORDS ADMINISTRATION

America on line: at a soup kitchen, June 1936

contradiction between the nation and economic life. In Europe this contradiction has become intolerably acute. . . .

. . . The war, it is true, like all the grandiose upheavals of history, stirred up various historical questions and in passing gave the impulse to national revolutions in the more backward sections of Europe—Tsarist Russia and Austria-Hungary. But these were only the belated echoes of an epoch that had already passed away. Essentially the war was imperialist in character. With lethal and barbaric methods it attempted to solve a problem of progressive historic development—the problem of organizing economic life over the entire arena which had been prepared by the world-wide division of labor.

Needless to say, the war did not find the solution to this problem. On the contrary, it atomized Europe even more. It deepened the interdependence of Europe and America at the same time that it deepened the antagonism between them. It gave the impetus to the independent development of colonial countries and simultaneously sharpened the dependence of the metropolitan centers upon colonial markets. As a consequence of the war, all the contradictions of the past were aggravated. One could half-shut one's eyes to this during the first years after the war, when Europe, aided by America, was busy repairing its devastated economy from top to bottom. But to restore productive forces inevitably implied the reinvigorating of all those

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evils that had led to the war. The present crisis, in which are synthesized all the capitalist crises of the past, signifies above all the crisis of *national* economic life.

The League of Nations attempted to translate from the language of militarism into the language of diplomatic pacts the task which the war left unsolved. After Ludendorff had failed to "organize Europe" by the sword, Briand attempted to create "the United States of Europe" by means of sugary diplomatic eloquence. But the interminable series of political, economic, financial, tariff, and monetary conferences only unfolded the panorama of the bankruptcy of the ruling classes in face of the unpostponable and burning task of our epoch.

Theoretically this task may be formulated as follows: How may the economic unity of Europe be guaranteed, while preserving complete freedom of cultural development to the peoples living there? How may unified Europe be included within a coordinated world economy? The solution to this question can be reached not by deifying the nation, but on the contrary by completely liberating productive forces

from the fetters imposed upon them by the national state. But the ruling classes of Europe, demoralized by the bankruptcy of military and diplomatic methods, approach the task today from the opposite end, that is, they attempt by force to subordinate economy to the outdated national state. . . .

In its day democratic nationalism led mankind forward. Even now, it is still capable of playing a progressive rôle in the colonial countries of the East. But decadent fascist nationalism, preparing volcanic explosions and grandiose clashes in the world arena, bears nothing except ruin. All our experiences on this score during the last twenty-five or thirty years will seem only an idyllic overture compared to the music of hell that is impending. And this time it is not a temporary economic decline which is involved but complete economic devastation and the destruction of our entire culture, in the event that toiling and thinking humanity proves incapable of grasping in time the reins of its own productive forces and of organizing those forces correctly on a European and a world scale.

The Reconstruction of Liberalism

C. H. McIlwain

October 1937

C. H. McILWAIN, *Eaton Professor of the Science of Government in Harvard University; former President of the American Historical Association; author of "The American Revolution," "The Growth of Political Thought in the West" and other works.*

The present generation is rightly concerned, and concerned far more deeply than its immediate forbears ever were, in the ending or mending of the monstrous economic



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and social inequalities and iniquities which permit and even foster the distress we see about us in the midst of plenty. In sharp contrast with the older notions of an inevitable progressive development that had best be let alone, or even with the recent naïve belief that depressions were a thing of the past, there is a determination among men of the present day, particularly the younger ones, to do something about this; and some would even go so far as to threaten the very existence of plenty itself, in their hatred of the glaring unevenness of its distribution. . . .

One thing is clear enough: the world in its present mood will never put up with a mere “muddling through” as an answer. The preservation of the *status quo* is a solution that can satisfy none but the contented; and just now most men are not contented. . . .

. . . Liberalism means a common welfare with a constitutional guarantee. . . . So-called liberals have ignored the first part of the definition and have fouled the nest by invoking the guarantee for privileges of their own, conducive only to the destruction of any true common weal. None have ever prated more of guarantees than these so-called liberals; but they have forgotten, if they ever believed, that these guarantees must secure the rights of all, not the selfish interests of a few. They are the traitors within the gates who have probably done more than all others to betray liberalism to its enemies and put it to its defense. . . .

It is unlikely, however, that this exploitation could ever have reached the proportions it did without more protest, had really liberally minded men not been beguiled by the extreme doctrine of *laissez-faire*, surely one of the strangest fantasies

that ever discredited human reason. Thus the self-seekers and the doctrinaires were drawn together into an alliance to maintain the *status quo*, and all its abuses and inequalities were made sacrosanct. This pseudo-liberalism usually exhibited itself in the ineffectiveness of legal guarantees for almost every human right except the right of property, and the acceptance of an unhistorical definition of contract under which the sanction of the law could be obtained for almost any enormity to which men could be induced to agree. . . .

Under *laissez-faire* and our distorted notions of contract, a lunatic may be protected against the results of his agreement, but of economic inequalities the law can never take notice—*De minimis non curat lex*; there is little or no safeguard for the weak against the strong; protection of the public against an adulterated product would be unthinkable—*Caveat emptor*.

Now this is a return toward Hobbes’s “war of every man against every man,” without the equality that Hobbes premised. Yet, we are told, the state cannot and should not do anything about it. State interference in such matters would be a violation of a sacred right. What a caricature of liberalism! . . .

. . . The question before us now, the decision we shall have to make before long, is whether we shall renounce these errors and remove these abuses that liberals have allowed to grow up, or whether, once and for all, we shall level with the ground all the bulwarks of our liberty, because some traitors have crept in behind them. . . .

The Economic Tasks of the Postwar World

Alvin H. Hansen and C. P. Kindleberger

April 1942

ALVIN H. HANSEN, *Littauer Professor of Political Economy at Harvard University; special economic adviser, Board of Governors of the Federal Reserve System; American chairman of the Joint Economic Committee of Canada and the United States; author of "Economic Stabilization in an Unbalanced World," "Fiscal Policy and Business Cycles" and other works.* C. P. KINDLEBERGER, *Associate Economist, Board of Governors of the Federal Reserve System; author of "International Short-Term Capital Movement."*

... There are still a good many people deeply concerned with problems of international security who think exclusively in terms of political arrangements and economic mechanisms such as tariffs and currencies. We would call that the passive approach. The arrangements and mechanisms which they favor are important, and appropriate means must be found to give them effect. But many economists are coming to think that action along these traditional lines would by itself be wholly inadequate. It is increasingly understood that the essential foundation upon which the international security of the future must be built is an economic order so managed and controlled that it will be capable of sustaining full employment and developing a rising standard of living as rapidly as technical progress and world productivity will permit. The very survival of our present institutions, including political democ-

racy and private enterprise, depends upon our taking a bolder attitude toward public developmental projects in terms both of human and physical resources, and both in our own country and throughout the world.

Many questions at once arise. What will be the rôle of government in postwar economic life? Will business enterprise outside of government be organized predominantly along cartel lines, with increasing restraints on competition? Will international trade be based on principles of non-discrimination or will each country make the best bargains it can obtain on a bilateral and separate basis with each of its trading partners? Will the world break up into autarchic countries, pairs of countries, or regions, including empires, continents and hemispheres? Or will each country tend to specialize in the production of those particular commodities which it can produce most efficiently



NATIONAL ARCHIVES AND RECORDS ADMINISTRATION

Out of the rubble: rebuilding West Berlin, 1950

and trade on the widest possible basis?

These questions are practical ones, and like most practical questions it is impossible to answer them categorically either as a forecast of the future or as a guide to desirable policy under the unforeseeable conditions of the future. It can merely be said that in time of war governments must and do assume more direction of economic life; that after

this war they will probably be given increased responsibility for trying to get rid of unemployment in their respective nations and to establish higher minimum standards for the low-income groups; and that while the degree of control exercised in the postwar period will be less than that exercised during the war, it nevertheless will be greater than it used to be before the war. . . .

Freedom and Control

Geoffrey Crowther

January 1944

GEOFFREY CROWTHER, *Editor of The Economist, London; author of "The Outline of Money."*

... It is the thesis of E. C. Carr's influential book, "Conditions of Peace," that the dominant ideas of the nineteenth century are dead—or at least that they no longer have sufficient validity to serve as our guiding lights. He defines these dominant ideas as being, in domestic politics, representative democracy; in economics, free individual enterprise; and in international affairs, the sovereignty of self-determined nations. ...

My quarrel with Mr. Carr is not ... that I wish to refute his main thesis but that I do not like being left where he leaves me. The dominant doctrines of the nineteenth century, if not dead, are so battered that they will not serve us any longer as our main props. We are, indeed, living in a vacuum of faith. But the trouble about a vacuum is that it gets filled, and if there are no angels available to fill it, fools—or worse—rush in. Let us, then, take Mr. Carr's threefold division of politics, economics and international relations, and consider in each case the alternatives to the old principles which he condemns. What are, not merely the theoretical alternatives, but the actual enemies that have been pushing them off their thrones?

The trend away from liberal democracy has been a trend towards totalitarian dictatorship. The trend away from indi-

vidualist capitalism has been a trend toward rigid state control exercised in the interest of a war economy—or at least of a war-minded economy. The trend away from the sovereignty of the nation-state has been a trend towards the concentration of aggressive strength in the hands of a few Great Powers. These are not, of course, the only conceivable alternatives; but they are the alternatives that the pressure of the age has been forcing upon us.

That pressure, it will be objected, is about to be lifted by a victory for the United Nations. I am not so certain. I have the suspicion that the Nazi alternatives, diabolical though they are, have far too much of the logic of events in them to be brushed aside by the military defeat of Hitler. If we are realistic, we shall recognize, even though it increases the difficulty of our task, that there is a great deal in the circumstances of our century that leads straight to Fascism. The enormous development in the technique of propaganda and advertising, in the power to sway the minds of people in the mass, plays straight into the hands of the would-be dictator or any other manipulator who, for large ends or small, seeks to muddy the waters of democracy. The growth of large-scale industry, the need

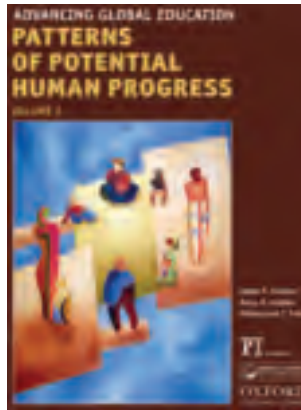
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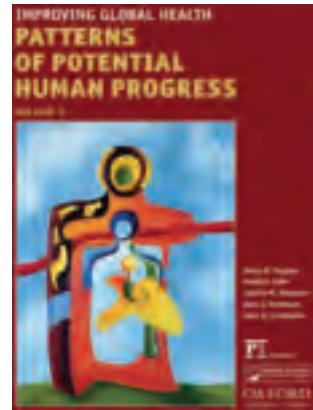
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for gigantic aggregations of capital, the implications of a maximum employment policy—all these create the danger of a concentration of economic power. The technique of modern war, with its emphasis on the possession of certain complicated weapons which only a handful of highly industrialized states can produce, makes the small nations, or even the league of small nations, quite helpless, and compels the Great Powers to devote quite unprecedented proportions of their resources to the barren purposes of war. We cannot abolish these things, we cannot dodge them. . . . The plain truth is that Hitler has an answer to the problems of the twentieth century and we, as yet, have not. It follows that whatever happens in the present war, Hitler will be hot on our heels for the rest of our lives. We shall have to think very fast, and run very fast, to keep ahead of him. One slip, one stumble, and he will be on our necks.

The central dilemma of the present age is that we can no longer rely on the old principles alone, but that we abominate the alternatives that time and tide, if it is left to them, will produce. This dilemma can be solved in only one way, by the birth of a new faith, adjusted in its instrumentalities to the needs of the new century, but preserving the ultimate objectives of the old. The only way to avoid the murder of nineteenth-century Liberalism by twentieth-century Fascism is through the birth of a twentieth-century democratic faith by the new out of the old. . . . What we need is not a compromise between the old ideas and the new, but a fusion; not a mixture but an amalgam. The nineteenth century, before it dies, must take what is virile in the hostile movements

and give birth to something new. Only then can it die in peace.

To state the need for such a new democratic faith is one thing. To meet it is another. The task of developing the thesis here presented in every sphere of public policy, political and economic, domestic and international, is probably beyond the power of a single pen; and certainly far beyond the reach of a single article. It may, however, be permissible to proceed a little way further in one particular direction, that of economic organization. . . .

The air is full at present of wordy warfare on the relative merits of unhampered private enterprise and of government planning of economic developments. Both are being argued in extreme and absolute terms—that is, as principles capable of being applied universally and in unadulterated form. Possibly the protagonists have reservations and modifications in mind, but, if so, they escape but rarely into print or speech. Not often does an advocate of private enterprise make the admission that there are certain economic problems (and among the largest) which must either be tackled by the organizing powers of the government or else left untackled. Still less frequently does an advocate of “planning” pause to concede that over a vast range of industries and occupations either the mainspring of activity will (in any easily foreseeable future) remain that of individual enterprise and ambition or there will be no mainspring at all. No, the argument proceeds in absolutes: the free enterprise party has no use for “bureaucracy” anywhere at any time; and the planners will not admit that a businessman, by serving the interest of his own profit, can ever serve the general interest.

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It is, of course, a sham fight. I do not mean that the contestants are not sincere; many of them doubtless (and unhappily) are passionately sincere. It is a sham fight because there is not the slightest chance of either side winning its fight. In the circumstances of the twentieth century, there is no prospect whatever of an industrial democratic state basing its affairs on the principle of unrestricted individual enterprise to the exclusion, or even to the subordination, of other principles. Even less can an industrial democracy contemplate governmental "planning" of the bulk of its activities—at least it cannot do so and remain a democracy. . . .

. . . I remain . . . obstinately skeptical about the ability of a free-enterprise economy—that is, of an economy where the requirements of free enterprise have priority over other objectives—to bring about any substantial improvement in the unequal distribution of wealth and welfare. Yet if there are two things in the sphere of economic policy that the electorate is going to impose as categorical imperatives on its representatives, regardless of party, they are contained in the current expressions Full Employment and Social Security. . . . The Russians have shown that it is possible to secure a very rapid increase in the national income; the Germans have shown that it is possible for a highly industrialized state to remove within a few years one of the largest masses of unemployment known to economic history. We may abominate the methods by which these achievements were secured. But we cannot pretend they do not exist. On the contrary, the electorate is going to insist on emulation of the results, if not on imitation of the methods. . . .

But if the wholly free economy is an impossibility, the wholly controlled econ-

omy is no less unacceptable. There are two main reasons for this. In the first place, experience seems to show—and common sense would confirm—that it is considerably less efficient in the production of wealth for consumption. The planned economy has had its triumphs. But none of them, I think, has been a triumph in supplying in large quantities at low prices consumption goods of the kinds and in the variety that people want. Yet that must remain one of the fundamental and co-equal objects of any democratic economy. There are examples of planned economics where the strength of the state has been increased, where the capital equipment of the community has been enriched, where mass unemployment has been avoided. I do not know of a wholly planned economy where the consumer has been satisfied. And, in the second place, a wholly planned economy is incompatible with any degree of political freedom. The possibility of a man's earning his own living in his own way, without let or hindrance, is the essential condition of there being any freedom of discussion, any freedom to oppose. If more than a fraction of the electorate come to depend for their livelihood upon the temporary masters of the mechanism of the state—that is, upon the politicians—then democracy is at an end.

It follows from this discussion that the economic system of the next few decades will inevitably have elements both of individual freedom of enterprise and also of purposive direction by the state. . . .

There will be those among the critics of this doctrine who will shake their heads and say that it cannot be done. They will quote Abraham Lincoln to the effect that a nation cannot live half slave and half free. . . . I take a more optimistic view. It

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is true that the opposing principles of economic freedom and of economic organization have, in fact, generated frictions which have perceptibly slowed down the progress of the democratic economy. But this is because they have been stupidly handled and the frictions would not arise if the object of all parties were to avoid them, instead of, as at pre-

sent, to seek battle on all occasions. Both the British and the American democracies have, each in its own way, over the past 150 years resolved the very similar conflict between freedom and order in the political sphere. I see no overriding reason why the same success should not be achieved in the economic sphere, provided the same essential moderation is shown. . . .

The Split Between Asian and Western Socialism

David J. Saposs

July 1954

DAVID J. SAPOSS, *Special Assistant to the Commissioner of Labor Statistics, Department of Labor; formerly Special Advisor in the European Labor Division, E.C.A., Paris.*

The dominating ideology in the international labor movement in the West is still Socialist, but a Socialism with a new look. Marxism has been discarded, although more by force of circumstances than conscious design, and the movement is still influenced by some Marxian reasoning; but, in general, Western Socialism has ceased to be class conscious and become reformist. It seeks the welfare state, but not revolution. The growing Christian (predominantly Catholic) labor movement in Western Europe has also arrived at maturity, and its social philosophy is likewise oriented toward the welfare state.

The old controversy over the interpretation of Marx was not revived in the

labor movements in continental Europe after this war, as it was after World War I. This tacit abandonment of Marxism became fully apparent when the Socialist International was revived as a permanent organization in Frankfurt during the summer of 1951. The program and pronouncements of the convention used none of the Marxian terminology so characteristic of prewar Socialist literature, and this momentous omission was not challenged in the discussions there. The 1952 Milan Conference of the Socialist International followed the precedent established at Frankfurt, and at the 1953 Stockholm Conference it was repeated. Such clichés as the materialistic or economic conception

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of history, exploitation of the workers, expropriating the expropriators, the class struggle, are no longer mentioned. The former sacred tenet that the workers are the class chosen to fulfill the holy mission of bringing about the inevitable capitulation of capitalism has fallen into limbo. The central theme of the new official

pronouncements revolves about problems of social justice, economic planning, full employment, democracy and human rights. Emphasis is placed on the need to avoid deflation with its consequent depression and unemployment, and, of course, on the rôle of the trade union movement in promoting social justice. . . .

The Myth of Post–Cold War Chaos

G. John Ikenberry

May/June 1996

G. JOHN IKENBERRY is Co-Director of the Lauder Institute of Management and International Studies and Associate Professor of Political Science at the University of Pennsylvania.

A great deal of ink has been shed in recent years describing various versions of the post–Cold War order. These attempts have all failed, because there is no such creature. The world order created in the 1940s is still with us, and in many ways stronger than ever. The challenge for American foreign policy is not to imagine and build a new world order but to reclaim and renew an old one—an innovative and durable order that has been hugely successful and largely unheralded.

The end of the Cold War, the common wisdom holds, was a historical watershed. The collapse of communism brought the collapse of the order that took shape after World War II. While foreign policy theorists and officials scramble to design new grand strategies, the United States is rudderless on uncharted seas.

The common wisdom is wrong. What ended with the Cold War was bipolarity, the nuclear stalemate, and decades of containment of the Soviet Union—seemingly the most dramatic and consequential features of the postwar era. But the world order created in the middle to late 1940s endures, more extensive and in some respects more robust than during its Cold War years. Its basic principles, which deal with organization and relations among the Western liberal democracies, are alive and well.

These less celebrated, less heroic, but more fundamental principles and policies—the real international order—include the commitment to an open world economy and its multilateral management, and the stabilization of socioeconomic welfare. And the political vision behind the order was as important as the anticipated economic

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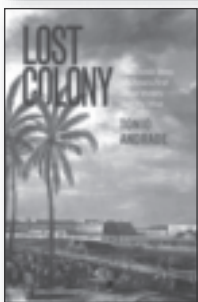


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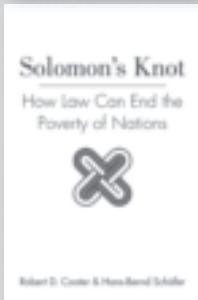
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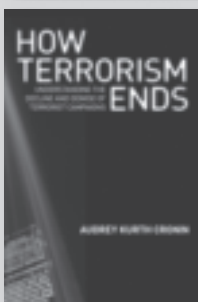
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gains. The major industrial democracies took it upon themselves to “domesticate” their dealings through a dense web of multilateral institutions, intergovernmental relations, and joint management of the Western and world political economies. . . .

World War II produced two postwar settlements. One, a reaction to deteriorating relations with the Soviet Union, led to the containment order, which was based on the balance of power, nuclear deterrence, and political and ideological competition. The other, a reaction to the economic rivalry and political turmoil of the 1930s and the resulting world war, can be called the liberal democratic order. It culminated in a wide range of new institutions and relations among the Western industrial democracies, built around economic openness, political reciprocity, and multilateral management of an American-led liberal political system. . . .

. . . The liberal democratic agenda was less obviously a grand strategy designed to advance American security interests [than was containment], and it was inevitably viewed during the Cold War as secondary, a preoccupation of economists and businessmen. The policies and institutions that supported free trade among the advanced industrial societies seemed the stuff of low politics. But the liberal democratic agenda was actually built on a robust yet sophisticated set of ideas about American security interests, the causes of war and depression, and a desirable postwar political order. . . .

The most basic conviction underlying the postwar liberal agenda was that the closed autarkic regions that had contributed to the worldwide depression and split the globe into competing blocs before the war must be broken up and replaced by an open, nondiscriminatory economic system. Peace

and security, proponents had decided, were impossible in the face of exclusive economic regions. The challengers of liberal multilateralism, however, occupied almost every corner of the advanced industrial world. Germany and Japan were the most overtly hostile; both had pursued a dangerous path that combined authoritarian capitalism with military dictatorship and coercive regional autarky. But the British Commonwealth and its imperial preference system also challenged liberal multilateral order.

The hastily drafted Atlantic Charter was an American effort to ensure that Britain signed on to its liberal democratic war aims. The joint statement of principles affirmed free trade, equal access to natural resources for all interested buyers, and international economic collaboration to advance labor standards, employment security, and social welfare. Roosevelt and Churchill declared before the world that they had learned the lessons of the interwar years—and those lessons were fundamentally about the proper organization of the Western political economy. America’s enemies, its friends, and even America itself had to be reformed and integrated into the postwar economic system.

The postwar liberal democratic order was designed to solve the internal problems of Western industrial capitalism. It was not intended to fight Soviet communism, nor was it simply a plan to get American business back on its feet after the war by opening up the world to trade and investment. It was a strategy to build Western solidarity through economic openness and joint political governance. Four principles pursued in the 1940s gave shape to this order.

The most obvious principle was economic openness, which would ideally take

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the form of a system of nondiscriminatory trade and investment. . . . American thinking was that economic openness was an essential element of a stable and peaceful world political order. “Prosperous neighbors are the best neighbors,” remarked Roosevelt administration Treasury official Harry Dexter White. But officials were convinced that American economic and security interests demanded it as well. Great liberal visionaries and hard-nosed geopolitical strategists could agree on the notion of open markets; it united American postwar planners and was the seminal idea informing the work of the Bretton Woods conference on postwar economic cooperation. . . .

The second principle was joint management of the Western political-economic order. The leading industrial democratic states must not only lower barriers to trade and the movement of capital but must govern the system. This also was a lesson from the 1930s: institutions, rules, and active mutual management by governments were necessary to avoid unproductively competitive and conflictual economic practices. Americans believed such cooperation necessary in a world where national economies were increasingly at the mercy of developments abroad. The unwise or untoward policies of one country threatened contagion, undermining the stability of all. As Roosevelt said at the opening of Bretton Woods, “The economic health of every country is a proper matter of concern to all its neighbors, near and far.” . . .

A third principle of liberal democratic order held that the rules and institutions of the Western world economy must be organized to support domestic economic stability and social security. This new commitment was foreshadowed in the Atlantic Charter’s call for postwar international

collaboration to ensure employment stability and social welfare. It was a sign of the times that Churchill, a conservative Tory, could promise a historic expansion of the government’s responsibility for the people’s well-being. In their schemes for postwar economic order, both Britain and the United States sought a system that would aid and protect their nascent social and economic commitments. They wanted an open world economy, but one congenial to the emerging welfare state as well as business.

The discovery of a middle way between old political alternatives was a major innovation of the postwar Western economic order. British and American planners began their discussion in 1942 deadlocked, Britain’s desire for full employment and economic stabilization after the war running up against the American desire for free trade. The breakthrough came in 1944 with the Bretton Woods agreements on monetary order, which secured a more or less open system of trade and payments while providing safeguards for domestic economic stability through the International Monetary Fund. The settlement was a synthesis that could attract a new coalition of conservative free traders and the liberal prophets of economic planning.

A final element of the liberal democratic system might be termed “constitutionalism”—meaning simply that the Western nations would make systematic efforts to anchor their joint commitments in principled and binding institutional mechanisms. In fact, this may be the order’s most basic aspect, encompassing the other principles and policies and giving the whole its distinctive domestic character. Governments might ordinarily seek to keep their options open, cooperating with other states but

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retaining the possibility of disengagement. The United States and the other Western nations after the war did exactly the opposite. They built long-term economic, political, and security commitments that were difficult to retract, and locked in the relationships, to the extent that sovereign states can. . . .

For those who thought cooperation among the advanced industrial democracies was driven primarily by Cold War threats, the last few years must appear puzzling. Relations between the major Western countries have not broken down. Germany has not rearmed, nor has Japan. What the Cold War focus misses is an appreciation of the other, less heralded, postwar American project—the building of a liberal order in the West. Archaeologists remove one stratum only to discover an older one beneath; the end of the Cold War allows us to see a deeper and more enduring layer of the postwar political order that was largely obscured by the more dramatic struggles between East and West.

Fifty years after its founding, the Western liberal democratic world is robust, and its principles and policies remain the core of world order. The challenges to liberal multilateralism both from within and from outside the West have mainly disappeared. Although regional experiments abound, they are fundamentally different from the autarkic blocs of the 1930s. The forces of business and financial integration are moving the globe inexorably toward a more tightly interconnected system that ignores regional as well as national borders. . . .

Some aspects of the vision of the 1940s have faded. The optimism about government activism and economic management that animated the New Deal and Keynesianism has been considerably

tempered. Likewise, the rule-based, quasi-judicial functions of liberal multilateralism have eroded, particularly in monetary relations. Paradoxically, although the rules of cooperation have become less coherent, cooperation itself has increased. Formal rules governing the Western world economy have gradually been replaced by a convergence of thinking on economic policy. The consensus on the broad outlines of desirable domestic and international economic policies has both reflected and promoted increased economic growth and the incorporation of emerging economies into the system.

The problems the liberal democratic order confronts are mostly problems of success, foremost among them the need to integrate the newly developing and post-communist countries. Here one sees most clearly that the post-Cold War order is really a continuation and extension of the Western order forged during and after World War II. The difference is its increasingly global reach. The world has seen an explosion in the desire of countries and peoples to move toward democracy and capitalism. When the history of the late twentieth century is written, it will be the struggle for more open and democratic polities throughout the world that will mark the era, rather than the failure of communism.

Other challenges to the system are boiling up in its leading states. In its early years, rapid and widely shared economic growth buoyed the system, as working- and middle-class citizens across the advanced industrial world rode the crest of the boom. Today economic globalization is producing much greater inequality between the winners and the losers, the wealthy and the poor. How the subsequent dislocations,

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dashed expectations, and political grievances are dealt with—whether the benefits are shared and the system as a whole is seen as socially just—will affect the stability of the liberal world order more than regional conflict. . . .

The Return of Authoritarian Great Powers

Azar Gat

July/August 2007

AZAR GAT is Ezer Weizman Professor of National Security at Tel Aviv University and the author of *War in Human Civilization*.

Today's global liberal democratic order faces two challenges. The first is radical Islam—and it is the lesser of the two challenges. Although the proponents of radical Islam find liberal democracy repugnant, and the movement is often described as the new fascist threat, the societies from which it arises are generally poor and stagnant. They represent no viable alternative to modernity and pose no significant military threat to the developed world. It is mainly the potential use of weapons of mass destruction—particularly by nonstate actors—that makes militant Islam a menace.

The second, and more significant, challenge emanates from the rise of non-democratic great powers: the West's old Cold War rivals China and Russia, now operating under authoritarian capitalist, rather than communist, regimes. Authoritarian capitalist great powers played a leading role in the international system up until 1945. They have been absent since then. But today, they seem poised for a comeback.

Capitalism's ascendancy appears to be deeply entrenched, but the current

predominance of democracy could be far less secure. Capitalism has expanded relentlessly since early modernity, its lower-priced goods and superior economic power eroding and transforming all other socioeconomic regimes, a process most memorably described by Karl Marx in *The Communist Manifesto*. Contrary to Marx's expectations, capitalism had the same effect on communism, eventually "burying" it without the proverbial shot being fired. The triumph of the market, precipitating and reinforced by the industrial-technological revolution, led to the rise of the middle class, intensive urbanization, the spread of education, the emergence of mass society, and ever greater affluence. In the post-Cold War era (just as in the nineteenth century and the 1950s and 1960s), it is widely believed that liberal democracy naturally emerged from these developments, a view famously espoused by Francis Fukuyama. Today, more than half of the world's states have elected governments, and close to half have sufficiently entrenched liberal rights to be considered fully free.

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But the reasons for the triumph of democracy, especially over its nondemocratic capitalist rivals of the two world wars, Germany and Japan, were more contingent than is usually assumed. Authoritarian capitalist states, today exemplified by China and Russia, may represent a viable alternative path to modernity, which in turn suggests that there is nothing inevitable about liberal democracy's ultimate victory—or future dominance. . . .

Liberal democracy's supposedly inherent economic advantage is . . . far less clear than is often assumed. All of the belligerents in the twentieth century's great struggles proved highly effective in producing for war. . . . Only during the Cold War did the Soviet command economy exhibit deepening structural weaknesses—weaknesses that were directly responsible for the Soviet Union's downfall. The Soviet system had successfully generated the early and intermediate stages of industrialization (albeit at a frightful human cost) and excelled at the regimentalized techniques of mass production during World War II. It also kept abreast militarily during the Cold War. But because of the system's rigidity and lack of incentives, it proved ill equipped to cope with the advanced stages of development and the demands of the information age and globalization.

There is no reason, however, to suppose that the totalitarian capitalist regimes of Nazi Germany and imperial Japan would have proved inferior economically to the democracies had they survived. The inefficiencies that favoritism and unaccountability typically create in such regimes might have been offset by higher levels of social discipline. Because of their more efficient capitalist economies, the right-wing totalitarian powers could have

constituted a more viable challenge to the liberal democracies than the Soviet Union did; Nazi Germany was judged to be such a challenge by the Allied powers before and during World War II. The liberal democracies did not possess an inherent advantage over Germany in terms of economic and technological development, as they did in relation to their other great-power rivals.

So why did the democracies win the great struggles of the twentieth century? The reasons are different for each type of adversary. They defeated their nondemocratic capitalist adversaries, Germany and Japan, in war because Germany and Japan were medium-sized countries with limited resource bases and they came up against the far superior—but hardly preordained—economic and military coalition of the democratic powers and Russia or the Soviet Union. The defeat of communism, however, had much more to do with structural factors. The capitalist camp—which after 1945 expanded to include most of the developed world—possessed much greater economic power than the communist bloc, and the inherent inefficiency of the communist economies prevented them from fully exploiting their vast resources and catching up to the West. Together, the Soviet Union and China were larger and thus had the potential to be more powerful than the democratic capitalist camp. Ultimately, they failed because their economic systems limited them, whereas the nondemocratic capitalist powers, Germany and Japan, were defeated because they were too small. Contingency played a decisive role in tipping the balance against the nondemocratic capitalist powers and in favor of the democracies. . . .

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It is widely contended that economic and social development creates pressures for democratization that an authoritarian state structure cannot contain. There is also the view that “closed societies” may be able to excel in mass manufacturing but not in the advanced stages of the information economy. The jury on these issues is still out, because the data set is incomplete. Imperial and Nazi Germany stood at the forefront of the advanced scientific and manufacturing economies of their times, but some would argue that their success no longer applies because the information economy is much more diversified. Non-democratic Singapore has a highly successful information economy, but Singapore is a city-state, not a big country. It will take a long time before China reaches the stage when the possibility of an authoritarian state with an advanced capitalist economy can be tested. All that can be said at the moment is that there is nothing in the historical record to suggest that a transition to

democracy by today’s authoritarian capitalist powers is inevitable, whereas there is a great deal to suggest that such powers have far greater economic and military potential than their communist predecessors did.

China and Russia represent a return of economically successful authoritarian capitalist powers, which have been absent since the defeat of Germany and Japan in 1945, but they are much larger than the latter two countries ever were. . . . Ultimately, . . . both Germany and Japan were too small—in terms of population, resources, and potential—to take on the United States. Present-day China, on the other hand, is the largest player in the international system in terms of population and is experiencing spectacular economic growth. By shifting from communism to capitalism, China has switched to a far more efficient brand of authoritarianism. As China rapidly narrows the economic gap with the developed world, the possibility looms that it will become a true authoritarian superpower. . . .

How Development Leads to Democracy

Ronald Inglehart and Christian Welzel

March/April 2009

RONALD INGLEHART is Professor of Political Science at the University of Michigan and Director of the World Values Survey. CHRISTIAN WELZEL is Professor of Political Science at Jacobs University Bremen, in Germany. They are the co-authors of *Modernization, Cultural Change, and Democracy*.

In the last several years, a democratic boom has given way to a democratic recession. Between 1985 and 1995, scores of countries made the transition to democracy, bringing

widespread euphoria about democracy’s future. But more recently, democracy has retreated. . . . These developments, along with the growing power of China and

Russia, have led many observers to argue that democracy has reached its high-water mark and is no longer on the rise.

That conclusion is mistaken. The underlying conditions of societies around the world point to a more complicated reality. The bad news is that it is unrealistic to assume that democratic institutions can be set up easily, almost anywhere, at any time. Although the outlook is never hopeless, democracy is most likely to emerge and survive when certain social and cultural conditions are in place. . . .

The good news, however, is that the conditions conducive to democracy can and do emerge—and the process of “modernization,” according to abundant empirical evidence, advances them. Modernization is a syndrome of social changes linked to industrialization. Once set in motion, it tends to penetrate all aspects of life, bringing occupational specialization, urbanization, rising educational levels, rising life expectancy, and rapid economic growth. These create a self-reinforcing process that transforms social life and political institutions, bringing rising mass participation in politics and—in the long run—making the establishment of democratic political institutions increasingly likely. Today, we have a clearer idea than ever before of why and how this process of democratization happens. . . .

In retrospect, it is obvious that . . . early versions of modernization theory were wrong on several points. Today, virtually nobody expects a revolution of the proletariat that will abolish private property, ushering in a new era free from exploitation and conflict. Nor does anyone expect that industrialization will automatically lead to democratic institutions; communism and fascism also emerged from industrialization. Nonetheless, a massive body of evidence



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suggests that modernization theory's central premise was correct: economic development does tend to bring about important, roughly predictable changes in society, culture, and politics. But the earlier versions of modernization theory need to be corrected in several respects.

First, modernization is not linear. It does not move indefinitely in the same direction; instead, the process reaches inflection points. Empirical evidence indicates that each phase of modernization is associated with distinctive changes in people's worldviews. Industrialization leads to one major process of change, resulting in bureaucratization, hierarchy, centralization of authority, secularization, and a shift from traditional to secular-rational values. The rise of postindustrial society brings another set of cultural changes that move in a different direction: instead of bureaucratization and centralization, the new trend is toward an increasing emphasis on individual autonomy and self-expression values, which lead to a growing emancipation from authority. . . .

Second, social and cultural change is path dependent: history matters. Although economic development tends to bring predictable changes in people's worldviews, a society's heritage—whether shaped by Protestantism, Catholicism, Islam, Confucianism, or communism—leaves a lasting imprint on its worldview. . . . Although the classic modernization theorists in both the East and the West thought that religion and ethnic traditions would die out, they have proved to be highly resilient. . . . Cultural heritages are remarkably enduring.

Third, modernization is not westernization. . . . The process of industrialization began in the West, but during the past few decades, East Asia has had the world's highest economic growth rates, and Japan

leads the world in life expectancy and some other aspects of modernization. The United States is not the model for global cultural change, and industrializing societies in general are not becoming like the United States. . . .

Fourth, modernization does not automatically lead to democracy. Rather, it, in the long run, brings social and cultural changes that make democratization increasingly probable. Simply attaining a high level of per capita GDP does not produce democracy. . . . But the emergence of postindustrial society brings certain social and cultural changes that are specifically conducive to democratization. Knowledge societies cannot function effectively without highly educated publics that have become increasingly accustomed to thinking for themselves. Furthermore, rising levels of economic security bring a growing emphasis on a syndrome of self-expression values—one that gives high priority to free choice and motivates political action. Beyond a certain point, accordingly, it becomes difficult to avoid democratization, because repressing mass demands for more open societies becomes increasingly costly and detrimental to economic effectiveness. . . .

Fifty years ago, the sociologist Seymour Martin Lipset pointed out that rich countries are much more likely than poor countries to be democracies. Although this claim was contested for many years, it has held up against repeated tests. The causal direction of the relationship has also been questioned: Are rich countries more likely to be democratic because democracy makes countries rich, or is development conducive to democracy? Today, it seems clear that the causality runs mainly from economic development to democratization. During early industrialization, authoritarian states

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are just as likely to attain high rates of growth as are democracies. But beyond a certain level of economic development, democracy becomes increasingly likely to emerge and survive. Thus, among the scores of countries that democratized around 1990, most were middle-income countries: almost all the high-income countries already were democracies, and few low-income countries made the transition. Moreover, among the countries that democratized between 1970 and 1990, democracy has survived in every country that made the transition when it was at the economic level of Argentina today or higher; among the countries that made the transition when they were below this level, democracy had an average life expectancy of only eight years. . . .

. . . Although many observers have been alarmed by the economic resurgence of China, this growth has positive implica-

tions for the long term. Beneath China's seemingly monolithic political structure, the social infrastructure of democratization is emerging, and it has progressed further than most observers realize. China is now approaching the level of mass emphasis on self-expression values at which Chile, Poland, South Korea, and Taiwan made their transitions to democracy. And, surprising as it may seem to observers who focus only on elite-level politics, Iran is also near this threshold. As long as the Chinese Communist Party and Iran's theocratic leaders control their countries' military and security forces, democratic institutions will not emerge at the national level. But growing mass pressures for liberalization are beginning to appear, and repressing them will bring growing costs in terms of economic inefficiency and low public morale. . . .

The Post-Washington Consensus

Nancy Birdsall and Francis Fukuyama

March/April 2011

NANCY BIRDSALL is *President of the Center for Global Development*. FRANCIS FUKUYAMA is *Olivier Nomellini Senior Fellow at the Freeman Spogli Institute for International Studies at Stanford University*. They are the editors of *New Ideas in Development After the Financial Crisis* (Johns Hopkins University Press, 2011), from which this essay is adapted.

The last time a global depression originated in the United States, the impact was devastating not only for the world economy but for world politics as well. The Great Depression set the stage for a shift away from strict monetarism and laissez-faire

policies toward Keynesian demand management. More important, for many it delegitimized the capitalist system itself, paving the way for the rise of radical and antiliberal movements around the world.

This time around, there has been no

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violent rejection of capitalism, even in the developing world. In early 2009, at the height of the global financial panic, China and Russia, two formerly noncapitalist states, made it clear to their domestic and foreign investors that they had no intention of abandoning the capitalist model. No leader of a major developing country has backed away from his or her commitment to free trade or the global capitalist system. Instead, the established Western democracies are the ones that have highlighted the risks of relying too much on market-led globalization and called for greater regulation of global finance.

Why has the reaction in developing countries been so much less extreme after this crisis than it was after the Great Depression? For one, they blame the United States for it. Many in the developing world agreed with Brazilian President Luiz Inácio Lula da Silva when he said, “This is a crisis caused by people, white with blue eyes.” If the global financial crisis put any development model on trial, it was the free-market or neoliberal model, which emphasizes a small state, deregulation, private ownership, and low taxes. Few developing countries consider themselves to have fully adopted that model.

Indeed, for years before the crisis, they had been distancing themselves from it. The financial crises of the late 1990s in East Asia and Latin America discredited many of the ideas associated with the so-called Washington consensus, particularly that of unalloyed reliance on foreign capital. By 2008, most emerging-market countries had reduced their exposure to the foreign financial markets by accumulating large foreign currency reserves and maintaining regulatory control of their banking systems. These policies provided insulation from

global economic volatility and were vindicated by the impressive rebounds in the wake of the recent crisis: the emerging markets have posted much better economic growth numbers than their counterparts in the developed world.

Thus, the American version of capitalism is, if not in full disrepute, then at least no longer dominant. In the next decade, emerging-market and low-income countries are likely to modify their approach to economic policy further, trading the flexibility and efficiency associated with the free-market model for domestic policies meant to ensure greater resilience in the face of competitive pressures and global economic trauma. They will become less focused on the free flow of capital, more concerned with minimizing social disruption through social safety net programs, and more active in supporting domestic industries. And they will be even less inclined than before to defer to the supposed expertise of the more developed countries, believing—correctly—that not only economic but also intellectual power are becoming increasingly evenly distributed. . . .

What the crisis did . . . was to underscore the instability inherent in capitalist systems—even ones as developed and sophisticated as the United States. Capitalism is a dynamic process that regularly produces faultless victims who lose their jobs or see their livelihoods threatened. Throughout the crisis and its aftermath, citizens have expected their governments to provide some level of stability in the face of economic uncertainty. This is a lesson that politicians in developing-country democracies are not likely to forget; the consolidation and legitimacy of their fragile democratic systems will depend on their ability to deliver a greater measure of social protection. . . .

SWITZERLAND

Strengthening relations with the U.S.

Two hundred years ago, a deep bond developed between the two countries based on their shared values and strong belief in federalism and democracy. In 1822 Switzerland opened its first consulate in the United States, and sixty years later it opened an embassy in Washington, DC, marking the opening of its first embassy outside Europe.

Switzerland is one of the top foreign direct investors (FDI) in the U.S. (\$123 billion to date), and the U.S. is Switzerland's number-one destination for FDI, leading Switzerland to post the largest FDI in the U.S. in 2010. The U.S. is also the largest investor in Switzerland, with \$101 billion. And Switzerland is the fourth-largest destination for U.S. investments.

"If you look at the core of the Swiss-U.S. relationship, then it is a healthy one. In our business, close to 50 percent comes from the U.S., and it will continue to be our biggest market in the long-term."

Dr. Stephan Lippe
CEO of Swiss Re

A little-known fact is that Switzerland represents the U.S. government and American interests in Iran and Cuba, and it also represents Cuban interests in Washington. Furthermore, part of the Iran mandate sees Switzerland protecting the interests of seven thousand people living in Iran with dual U.S.-Iranian nationality; such is the historic level of trust between the two nations.

It is no wonder, then, that the shockwaves from the apparent and temporary fallout after the UBS saga ran so deep, thus taking a toll on Swiss-U.S. relations. However, this period became nothing more than a blip in the relationship. Both Washington and Berne have moved on and refocused on the positive aspects of the relationship. Given Switzerland's credibility in tackling matters of international sensitivity, the U.S. administration has again realized Switzerland's plus points, though in Switzerland many business leaders are still hoping for a return to the pre-UBS saga days. "We hope that the Americans will come back to their old [commercial] values," said Calvin Grieder, CEO of Bühler Group.

The Swiss education system is one of the best in the world and hosts two of the world's top 100 engineering schools, ETHZ and EPFL. President of EPFL Patrick Aebischer explained the reason for Switzerland's educational success: "In Switzerland, both the government and all our companies are committed to fostering and improving education." Another example of how Swiss education is respected on a global platform is the Geneva Centre for Security Policy (GCSP), whose alumni have gone on to represent many international organizations. This is an international foundation established in 1995 whose primary purpose is maintaining peace security and stability through training, research, and dialogue. Faculty and senior staff come from all around the world, and they have brought an extensive contribution to global debates.

Importantly, Switzerland learned many years ago that a small country needs to have a diversified economy. So while the country may be well-known for chocolate, cheese, and watches, its wider business offering is much more diverse. Industry ranges from biochemical companies such as Bachem to huge agribusiness enterprises like Syngenta.

Another lesson we could all learn from Switzerland is financial prudence and fiscal responsibility. As Thomas Pletscher, member of the executive board of economuisse explained, "Switzerland follows a very strict, orthodox but ultimately balanced and solid, financial policy that has allowed the country to manage the economic crisis very well."

Hosting the World Economic Forum

Just as it has every January since 1974, Switzerland will host the 2012 World Economic Forum (WEF) at the alpine resort of Davos. Often referred to by the resort's name, this event has the power to bring together world leaders, economic gurus, captains of industry, and the rich and famous to debate and offer solutions to the world's socioeconomic issues.

Founded by Klaus Schwab, a professor at the University of Geneva, the summit fast became a neutral platform, also bringing together political enemies and averting crises. Nelson Mandela and FW de Klerk shared their first international appearance at the summit in 1992, and two years later Shimon Peres and Yasser Arafat reached agreement on Gaza. Therefore, it is unsurprising that, given its neutrality, the summit is held in Switzerland.

With the theme "The Great Transformation: Shaping New Models," this year's event not only has to tackle the stalled global economy by looking at how developed economies can lower their debt burden while avoiding a slip back into recession; it will also be discussing how to best ensure that those emerging economies that are growing can do so without creating the same bubbles.



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SWITZERLAND

U.S. - Swiss relations: Good, but could try harder**A CONVERSATION WITH
Martin Naville**

CEO of Amcham



If the relationship between the two countries was a tenth-grader, “good, but could try harder” would sum up the most recent report card. Historically they have enjoyed very good ties, but certain recent events and some missed opportunities are allowing this relationship to fall just short of its true potential.

The two countries classified each other as sister republics back in the nineteenth century: they both shared the ideals of democracy, the rule of law, and respect for human rights, and they both vigorously supported a federal system that kept the executive separate from the legislative.

For Martin Naville, CEO of the Swiss-American Chamber of Commerce, the similarities between the two countries are clear. “The United States and Switzerland will always be on top; top in innovation, top in competitiveness, and top in matters that are important for international diplomacy,” he explained. When you consider that the United Nations is headquartered in both the U.S. and Switzerland and that there are many international organizations based in Switzerland that are funded by U.S. tax dollars, you begin to understand the importance of the ties between the two countries.

Not only have these two countries historically respected one another; they have also forged a common path of investment and trade that has benefited both their economies. The United States is the largest investor in Switzerland, with the level of investment having soared 25 percent in the last eight years alone. Six hundred and fifty U.S. companies operate in Switzerland and in turn over six hundred Swiss companies employ almost half a million Americans in the United States. Between them, Switzerland and the United States enjoy a \$40 billion trade relationship. Martin Naville and his Swiss-American Chamber of Commerce are keen to foster even further growth.

Today the United States cannot help but look at Switzerland as a potential partner in scientific and educational advancement. There are so many cutting-edge areas where Switzerland leads the way and U.S. companies are vying for a piece of the action. “All you have to do is look at the number of corporations that have their R&D facilities in Switzerland,” said Naville. “There is strong cooperation between the leading U.S. seats of learning and Swiss educational establishments; between Berkley and EPFL and between MIT and Zurich,” he added.

It is clear that there are huge opportunities for both countries to build on their successful ties and continue to invest heavily in each other; doing so would very likely result in growth. However, it is not all a bed of roses. As in any relationship, there are shortcomings and misunderstandings that are distracting both countries from the

ultimate goal of honest friendship and full commercial potential.

The simple matter of arrest warrants for two men opened a can of worms and brought the UBS affair to the forefront in the United States. Consequently the 2009 charging of UBS AG with conspiracy to commit fraud against the United States became a watershed moment in the relationship between the two countries, and, typically, it was blown out of proportion.

According to Naville, the important players in the relationship have moved on and it’s back to business as usual, but, as he explained, “the intergovernmental relationship is strong, the business layers are strong, but in a broader sense there is a lot of ill-will that has been created because it is only a very small piece of the relationship that is being commented on in the press on a daily basis.”

Both countries need to be careful. The United States needs to

“We bring business leaders together and facilitate the deepening of mutual interests.”

be watchful that it does not lose the very strong feelings of goodwill that Switzerland has for the country—one must not forget that half a million Swiss have emigrated to the U.S. over the years, indicating how highly they regard the country. Equally, Switzerland must not be unduly recalcitrant, as that is not the way to win or keep friends. Naville sensibly pointed out that “Switzerland is a great partner in the multinational forums that are necessary for the United States, and we are showing a willingness to clean up our act. But let’s find some solutions that are feasible for both countries and let’s not find solutions that, while politically desirable in the U.S., are impossible for Switzerland.”

One area where Naville’s opinion might apply is to the unpopular Foreign Account Tax Compliance Act (FATCA) of 2009. Seen by the populist press as a victory for U.S. taxpayers and by others as a knee-jerk reaction to the UBS affair, this act is proving to be very divisive. No one is denying that the U.S. has a right to claim the tax that is fairly owed to them—in fact, many other governments are also creating mechanisms to deal with the same issue. However, Naville criticizes the act—not necessarily for the rationale behind it, but for its workability and the effect it will have on future investment.

“I am supporting full tax compliance and so are most people in Switzerland,” Naville said, but he added that “I am against FATCA because it does not make sense. It is unbelievably complex, and if everybody were to participate, which remains a big maybe, it will cost so much money (up to \$1 trillion) to implement it that it will become pointless.” Naville argued that “it has huge global implications and nobody has analyzed the secondary and tertiary implications.”

If Naville—a Swiss who by the nature of his work is pro-American—has one more gripe, it is that the U.S. has seemingly not been taking the World Economic Forum at Davos as seriously as he thinks it should. He is calling for more high-level engagement for the world’s leading economy—particularly during these difficult times.

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Michael Buscher

Dr. Michael Buscher
CEO Oerlikon

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SWITZERLAND

Moving a billion people a day

A CONVERSATION WITH Jürgen Tinggren

CEO of the Schindler Group



Many people never give a thought to the way people move around inside buildings, be it in elevators or on escalators, between floors or across halls. Jürgen Tinggren, CEO of the Schindler Group, the 138-year-old Swiss elevator company, ponders this every day.

We barely realize how important mobility is within a building and how it affects the way people interact with it, not to mention how many hours of thought, research, and work it requires. When people consider an elevator, they think of pulleys and weights. When we do notice an escalator, it is not because it is working, which we take for granted; it is generally because it is being repaired and we have to walk up the stairs.

During our interview, Mr. Tinggren shared some insights into the fascinating world of mobility—fascinating not only from an engineering point of view but also from an architectural and sociological perspective. Schindler's 43,000 employees are not just designing elevators; they are interacting with society and responding to important needs, which, if unmet, would pose significant problems.

Schindler, with almost \$10 billion in turnover in 2010, is present worldwide, its products hidden gems we barely appreciate. The next time you walk into the elevator of your building, look at the brand; it is most probably a Schindler elevator. If you arrive at LAX or you are in Manhattan's Grand Central Station, check out the escalators and mechanized walkways. The brand? Schindler, and these are only two of its latest multimillion-dollar projects. But Schindler is not only about new products: the company is strategically positioning itself as a service-oriented company. As Mr. Tinggren explained, "Being exclusively an engineering company would have limited Schindler's capacity for expansion; plus, there was an important business opportunity in the services sector, and not moving that way would have been a grave mistake. We provide much more than elevators: we provide mobility, energy efficiency, and building safety," three important megatrends. "Maintenance, proper implementation of mobility solutions, and optimization of energy expenditure in buildings are important aspects of the services Schindler offers."

Although Schindler's main markets for expansion are Asia, India, and the Middle East, where cities are continuously expanding and emerging, the U.S. and other developed markets are still a very important part of the company's business, not only in terms of supplying new installations but in improving the way they are used. "Consider the aging populations in the developed markets. We have a population that is growing older and requiring more comfortable and safer mobility solutions. That is extremely important when it comes to innovation, but it is just one aspect; energy efficiency is also a big focus of ours and we are spearheading the industry. For example, many of our elevators use traction belt technology instead of steel cables, which makes them considerably more efficient, and we are experimenting with solar technology. We have built solar-powered elevators, and we offer elevators that actually feed energy back into the grid."

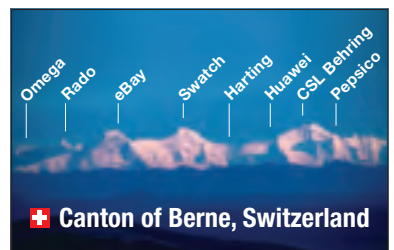
"Americans may think that New York's public transport system moves a lot of people, but Schindler, a leading global mobility provider is responsible for moving one billion people every day."

When it comes to efficiency, Schindler stands out. The company is a main partner of Solar Impulse, the zero-fuel aeroplane that aims to fly around the world, powered solely by solar energy. "That is a very important initiative for us, since the technologies being developed overlap with our own. Lighter and tougher materials, high-efficiency solar cells, energy efficient motors, and energy conservation software are indispensable for us, and we are not only collaborating with money, we have Schindler engineers working full-time on the project."

The use of clean technologies is not just a fashion statement; the new American headquarters in Morristown, New Jersey, are living testimony. The facilities are so energy efficient that they sell energy they save back to the grid, thanks to the use of technologies such as LED lighting, solar panels, and energy conservation software that is used to monitor the building. Schindler spares no expense when it comes to R&D. "We are not only investing in developed markets, we have opened a new R&D facility in India, which reaffirms our belief in the revenue streams from emerging markets."

It is Schindler's innovations that will bring the company exponential growth over the coming years. By looking to the Middle East, India, and Asia, where rapid urbanization has been taken to unparalleled levels, Schindler finds itself supplying entire new cities. In August, Schindler finalized a joint venture with a new Chinese partner by acquiring a 46 percent stake in Xuchang Xiji Elevator Company—with an option to purchase the remaining shares. Nevertheless, "developed markets are still extremely important for the company, and we will be launching several new products in the U.S. in the next year," Mr. Tinggren explained.

Although the strong appreciation of the Swiss franc has impacted Schindler's financials in 2011, the increase in orders and the rise in operating revenue in local currencies bode well for the future, setting the stage for even greater growth in 2012. We will not see Schindler stop growing anytime soon.



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SWITZERLAND

Financial Center Infrastructure**A CONVERSATION WITH
Dr. Christian A. Katz***CEO of SIX Swiss Exchange***H**ow would you describe the Swiss marketplace?

Switzerland is home to a wide array of companies that engage in cross-border activities. For example, take the pharma, biotech, and medtech sectors—you will find established global leaders as well as innumerable fast-growing smaller enterprises. This is fully reflected on SIX Swiss Exchange: with approximately 40 percent of the European life sciences market capitalization, we are by far the leading exchange in this sector. In other sectors too, such as luxury consumer goods or banking, you can see a strong symbiotic relationship between the Swiss “Main Street” and “Wall Street.” It is areas such as these, in which we have a strong local concentration of extensive specialist expertise, that make Switzerland a desirable business location and place to invest.

What is the role of SIX Swiss Exchange?

We are a key pillar of the Swiss financial sector’s infrastructure and a front-runner for the internationalization of the market place. In 1996 we introduced fully electronic trading, and today we are offering new connectivity options for

international trading participants that allow them to trade as fast as if they were located in Zurich. This has resulted in an unprecedented increase of new members joining our exchange in the past two years, many of them from abroad.

How does SIX Swiss Exchange distinguish itself from its competition?

We are one of the last independent mutualized exchanges. Being user-owned and user-governed allows us to be close to our international and domestic clients—a perfect condition for adding value for our clients as well as becoming the independent investment network of choice. Our focus is to make markets, in particular our own market, safer without penalizing their price-finding potential, efficiency, transparency, and power to act as centers for raising capital. Being a self-regulated market in the most competitive economy in the world, SIX Swiss Exchange is able to create exactly these market conditions. As a result, our trading platform has the best availability record of all venues in Europe, which means that our customers can confidently trade in our attractive segments with some 40,000 securities.

Are you also partnering with US companies?

In fact, NASDAQ OMX has been the technology partner of SIX Swiss Exchange since 2005, making this an excellent example of a reliable and successful Swiss-U.S. partnership. It is also one of the reasons why we have decided to implement their new technology, X-Stream INET, in the first half of 2012. We will be the first exchange in the world to do so, setting a new standard in terms of trading speed and capacity. This upgrade is an investment in the future, so that we can continue to offer our all market participants a first-rate equity trading technology.

**Global reach, local focus.**

For well over a century, the Schindler Group has been developing innovative mobility solutions for urban environments. Our elevators, escalators and technologies provide some of the safest, most reliable and environmentally sound means of transport available.

Schindler believes that sustainable urban development depends on continuous, assured mobility.

**Schindler**

SWITZERLAND

A Top Global Brand

A CONVERSATION WITH

Martin Senn

CEO of Zurich Financial Services

**H**ow would you describe current Swiss-American relations?

The relationship between Switzerland and the U.S. has traditionally been very close and well linked in terms of politics, science, and technology. It goes back a long time and I would say that overall it has been very constructive.

Switzerland is one of the largest foreign investors in the U.S., partly because of the strength of the Swiss economy and partly due to the fact that we have a lot of internationally active institutions. There are more than 350,000 people employed by Swiss organizations in the U.S. On the other hand, Switzerland serves as an important hub for many leading companies acting outside the U.S.

To what extent is Zurich a symbol of this relationship?

We have a significant footprint in the U.S. This year we are celebrating one hundred years of doing business in the U.S. We became the first foreign carrier to set up business in North America when we established operations in the U.S. in 1912.

In the U.S., Zurich insures commercial lines customers, including many Fortune 500 companies. On the personal lines side, Zurich owns Farmers Group, Inc., which provides non-claims management services to the Farmers Exchanges, which are owned by their policyholders. Farmers operates under two customer-facing brands, Farmers and 21st Century.

Our U.S. operations are one of our most important business areas. More than half of our employees are in the U.S. (35,000), and we are very pleased with this presence. We have an excellent relationship with all constituencies in the U.S. and I think this is true of most companies transacting business in the country. Overall the relationship is very important and very good.

Zurich has recently been classified among the top 100 brands by Interbrand. What does this say about the company?

We are very proud and very pleased to have been recognized as one of the top global brands. Zurich is leveraging its brand as an essential tool in building and maintaining its relationship with its customers. A strong brand is important for any internationally active organization.

The award is probably a manifestation of our campaign to position ourselves as a service organization and as a Help Point for our customers, as well as making sure that we deliver to our customers when it matters for them. This Help Point campaign has been seen as a very successful step in executing our global strategy. That has contributed to Interbrand putting us on their top 100 list.

Don't forget that Zurich has a history of nearly 140 years and we are doing business in over 170 countries. We are very strong in the U.S. and Europe and we are enhancing our presence in other parts of the world.

To be recognized by Interbrand as a top 100 company is proof for us that we are on the right track in the execution of our strategy. We are the only Swiss insurance company that has that recognition. We are also differentiating ourselves by being a global insurance company in the real sense of the word and truly covering all aspects of insurance on a global basis.

In 2011, Zurich introduced its first product for the U.S. market since 2003. What are your expectations and targets?

The U.S. is by far the largest insurance market in terms of total premiums paid. Insurance penetration is high. With that, our brand, our presence, and our expertise made it an obvious choice in which to reestablish ourselves in the life segment. We have been pretty prominent in the property and injury segments and in general insurance, but we didn't have a commensurate presence with the Zurich brand in the life segment in the U.S.

We feel that with our capabilities and the opportunities in the market, this is the right approach. We also want to roll out products offering protection for high-net-worth individuals.

What more can you tell us about the International Program Zurich (IPZ)?

The IPZ network is one of our strategic growth areas in General Insurance, together with expansion into the European middle market of property and casualty commercial lines, and it also fits into our expansion into the so-called financial lines in Europe. This network enables us to carry out transactions in over 170 countries where we operate, through partnerships with other insurance companies and brokers, and in some instances with banks. Distribution is very important for insurance companies and in general we always look for multiple distribution channels.

Many big brand names were affected by the global financial crisis. Has it been different for Zurich?

We have managed the crisis without any single quarterly loss. We have been able to pay attractive and competitive dividends throughout, and our financial position has remained as strong as before. We have been one of the only insurance companies that has been upgraded by Moody's to an A-A3 rating (the equivalent of an A-A rating from S&P) in a market where the sector has been on a negative outlook.

Our success is also due to the strong and demanding regulatory environment we are exposed to as a Swiss-domiciled insurance institution. That has helped. Having mentioned the regulatory regime, I don't think we need more regulation. We need better regulation, recognizing particularly that within the financial world there are different businesses. Banks and insurance companies are not the same.

SWITZERLAND

Celebrating 100 years in the U.S. market

Believing that historical success is not sufficient, Zurich Financial Services Group looks to its future: one offering new, streamlined products for U.S. consumers.

Zurich, one of the first-tier partners at this year's Davos summit, is one of the world's largest insurers, with over 60,000 employees worldwide. More than half of them are employed in the United States, giving the Swiss insurance group a significant footprint in the world's largest and most important insurance market.

By entering the U.S. market, in 1912 Zurich became the country's first foreign-based insurer. In the United States, Zurich insures commercial lines customers, including many of America's Fortune 500 companies. On the personal lines side, Zurich owns Farmers Group, Inc., which provides non-claims management services to the Farmers Exchanges, which are owned by their policy holders. Farmers is the third-largest personal lines insurance group in the country, serving over 15 million customers across forty-one states.

Zurich has already achieved many accolades in the U.S. market, including being the largest construction insurer in North America, with more than 50,000 customers; the largest insurer of franchised auto dealers; and the second-largest commercial auto writer. Additionally, Zurich is also one of the leading writers of program business in the United States, the second-largest writer of commercial liability insurance, and the third-largest writer of fidelity and surety. 2011 was an award-winning year for the company, as it was awarded top place among many competitors in two categories: Best Trade Insurer in North America, by Trade Finance magazine, and Best Overall Commercial Insurance Provider, by the National Underwriter, in May last year.

Now, for the first time since 2003, the company is introducing new Zurich-branded products in the United States through its Global Life business segment. U.S. insurance customers will be able to have the confidence of another Zurich product. Corporate Life & Pensions teams are providing group benefit packages to U.S. corporations with international operations and workforces. They are also offering specialized wealth transfer and business insurance products in the affluent segments of the market.

Another avenue for revenue growth in North America was announced last October, when Zurich announced a new relationship with Stanford Hospitals & Clinics Risk Consulting (SRC) to provide innovative health-care risk management solutions. This relationship will enable Zurich to offer integrated, advanced, and flexible solutions for the health-care industry to its professional liability policy holders.

"As cost, technology, and demographic pressures on health care increase, providers are continuously trying to improve the quality of care, reduce cost, and increase patient safety, all at the same time," said a spokesperson for Zurich. "Our health-care customers can have access to SRC's services at a special Zurich rate to empower them with tools, knowledge, training, and strategies to help them manage critical risks in today's health-care industry

and to measure their results. These services complement Zurich's expertise."

While these are significant developments for Zurich, they may still not be enough for CEO Martin Senn. Celebrating his second anniversary as the company's chief executive this month, he plans to further simplify the company and deliver even more profitable growth. "Our strategy is to focus on insurance, and we do not deviate from that or take a conglomerate approach by offering banking products or asset management services," he explained. "Having said that, we do aspire to do that with high financial strength, and to a certain extent the recent financial crisis has been an opportunity for us."

The old adage "What does not kill you makes you stronger" certainly rings true for Senn. "Although we are still operating in a crisis mode, we are stronger than ever before," Senn noted. Zurich did weather the crisis without a single quarterly loss and has been able to pay attractive and competitive dividends throughout. "What we are pursuing in terms of strategy is to have global scale and scope. For this, we need to have continued financial strength and to be in a position to generate strong cash flows."

Having had the opportunity to simplify Zurich's structure and create agility, one of Senn's strategies is to deliver profitable growth in fast-growing economies. Currently, Zurich generates up to 85 percent of its business-operating profit in mature markets, with up to 45 percent of that coming from the United States. However, new markets in Latin America, the Middle East, and the Asia-Pacific are increasing their contribution to Zurich's profit. With the International Program Zurich (IPZ), the company is carrying this strategy and insurance distribution even further. In the same vein, Zurich last year struck a deal with global banking behemoth Santander that allows it to marry its insurance expertise to Santander's distribution network, further opening the Latin American market.

This alliance has seen Zurich acquire 51 percent participation in the life insurance, pension, and general insurance operations of Santander in Brazil, Mexico, Chile, Argentina, and Uruguay, combined with an exclusive distribution agreement for a term of twenty-five years. "This alliance with Banco Santander is another milestone in the implementation of Zurich's emerging-market strategy in both Global Life and General Insurance," Senn noted.

The figures speak for themselves. Had Zurich and Santander been combined, during 2010 they would have produced \$3.9 billion in gross written premiums and \$2.9 billion in pension contributions. As Senn also pointed out in a 2011 press release, "Santander's Latin American insurance operations offer a rare combination of high growth potential and strong cash flow generation."

But none of this means less focus on the U.S. market. As Senn explained, the changing regulatory environment in the United States is presenting a challenge for financial institutions, one that he must take on. "As we at Zurich are successfully weathering the financial crisis, we are credible and well positioned to make our voice heard by policymakers, regulators, and international institutions, and we very much look forward to continuing that dialogue," he explained. This point is directed specifically at U.S. policymakers, as their country will remain vitally important for Zurich's future.

SWITZERLAND

The SWISS touch makes the difference for passengers**A CONVERSATION WITH
Harry Hohmeister***CEO of SWISS International
Air Lines*

To what extent can an airline symbolize relations between two countries?

I consider the relationship between the United States and Switzerland to be strong and mutually beneficial. When you take a look at the liberalization of the airline sector, or at the “open skies” policy, you see that Switzerland and the U.S. were among the first countries to sign up to the Europe and North Atlantic agreement in the mid-1990s, and then the rest of Europe followed. As part of Star Alliance, we also maintain very healthy relations with the U.S. member carriers such as United/Continental and US Airways.

How important are the Switzerland–U.S. routes for the airline?

These routes are very important to SWISS. They account for a great deal of our premium traffic, and we continue to invest heavily in U.S. destinations. The U.S. is currently a very important cargo market for us. Other areas of the world are showing impressive growth, but the U.S. remains the world’s

largest economy, and this means cargo traffic. As cargo generates between 14 and 15 percent of our revenues, the cargo traffic between Switzerland and the U.S. will remain very important to us, and as cargo increases tend to be a prelude to increasing passenger numbers on the same routes, we are excited about the growth prospects of the U.S. market.

Why do you think SWISS is winning so many awards?

First, our customers continue to vote for us, and that is because we do not consider ourselves to be in the transport industry; we prefer to think of ourselves as being in the service industry. It is really important that you put the right focus on the service process and define what is important to the customer. Often it is the little details that make the difference. We pride ourselves on being a premium carrier, and that means always offering the best to our first, business, and economy (coach) class passengers. Passengers flying to and from this year’s Davos summit will be experiencing the best of Swiss hospitality, like they would all year round. Furthermore, we pride ourselves on our consistent punctuality, and our customers like this.

What are you hoping for from the new image you started rolling out last fall?

A new logo was adopted last October. It features a SWISS tailfin with its Swiss-cross design, enabling SWISS to be instantly recognized as “the airline of Switzerland,” even from afar. It is also a symbol of our self-confidence and pride. It allows us to stand out in the marketplace.

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Cantons compete with each other for investment

Switzerland may only be twice the size of New Jersey, but it is too easy to make the mistake of thinking that there are no noticeable differences between its cantons (states)—all twenty six of them.

Switzerland is competing with every other European country for a share of the business of many international companies. Each canton is using what they call hard and soft incentives to make their point. All too often it is the hard incentives, which refer to tax and financial enticements, which make all the headlines, when it is really the soft incentives that ultimately win the day. These incentives are additional reasons to choose a particular canton based on quality of life, infrastructure, education, and working hours, and the cantons know that every company looks very closely at these issues when deciding on where to set up shop.

When relocating to Switzerland, one will inevitably have to consider Zurich as one of the first options. “The canton of Zurich has an image that attracts foreign talent, as the presence of Google and IBM demonstrates,” says Ernst Stocker, minister of economy of the canton. Furthermore, “there is a reason why we are the heart of the Greater Zurich Area: we are a major northern transport hub thanks to our airport and rail hub, but we also are one of the educational centers of Switzerland; that is the reason for the success of the canton.”

Close to Zurich, Schwyz is a canton that has been very successful in attracting business over the years. Well situated, with a major airport nearby, for many years it has enjoyed good relations with both local and international companies. For Kurt Zibung, the canton’s minister of economic affairs, one reason why is that it is close to what is perceived to be the economic center of the country, Zurich. “Schwyz is embedded in the greater Zurich area. That puts us in a good location for business because of our close position to what is a well-known international city with one of Europe’s major airports,” he said. Zibung went on to add that the quality of higher education on offer is second to none.

But Schwyz’s main advantage is the lower tax burden, which is sustained by the wealth of the canton. The lowest taxes in the entire country are in its locality of Freienbach. “We have

very low taxes for companies and individuals, and my aim is to continue with the low tax regime to continue our fast growth,” he said.

Traditionally known for its tourism, the canton of Valais is home to the world-famous Verbier resort. But the canton does employ other strategies to attract business, and minister of economic affairs Jean Michel Cina wants Valais to be known for these lesser-known advantages. “I constantly have to remind people that the canton of Valais is second in the country for biochemical, life sciences, and chemical plants, and that we host some major corporations like Huntsman,” he explained.

But where the canton really excels is in energy production. Most of Switzerland’s hydroelectricity is produced thanks to its high mountains and gravity dams. The canton is in fact home to the world’s highest gravity dam, the Grande Dixence. As the minister pointed out, the canton is well on its way to becoming the country’s main hub for green energy research.

Even in Switzerland, it is a little known fact that Valais is so industrialized. But that does not detract from the canton’s scenery. “I like to say that we are the most beautiful industrial canton in Switzerland,” added Mr. Cina. Furthermore, with the added benefit of most residents speaking four languages (French, Italian, German, and English) the canton is an ideal place for call centers, and Sion realized just that when it set up its Nespresso call center here.

The canton of Solothurn is another strong economic center in Switzerland. It is also the epitome of “small is beautiful.” “We are in the middle of the large economic hub of Basel, Zurich, and Zug,” said minister of economic affairs Esther Gassler. The small size of the canton does not stop it from punching above its weight. In 2010, this small (in U.S. terms) canton exported over \$700 million dollars worth of goods to the U.S. When it comes to its advantages, Gassler was clear: “We have a combination of low taxes and less expensive real estate, which makes us an attractive base to live and work. We would be excited to welcome more American companies and we appreciate the long relationship we have with the United States.”

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High quality of life and optimal infrastructure



Graubünden is where global leadership begins

Forty-one years ago, this canton opened its doors to host the first-ever World Economic Forum (WEF). This year, the canton shows yet again that it is synonymous with success and leadership.

Sometimes associated with the rich and powerful, sometimes with groundbreaking negotiations, but always with world leaders, Graubünden has carved a very influential path for itself.

Curiously, however, those looking at the canton from overseas need the names of St. Moritz and Davos to position the area, whereas to Swiss residents the name Graubünden needs no introduction. The canton's minister of economic affairs, Hansjörg Trachsel, is now determined to bring the canton's name to the forefront of the minds of visitors and investors so they can make the most of the advantages the region has to offer.

"Even though we host one of the world's most prestigious events every year, it has been very difficult to communicate our canton's advantages to the end user overseas," Trachsel explained. "We have many advantages for tourists and businesses: we are close to Zurich airport, we have spectacular scenery, a very healthy environment, and we have the available land necessary for businesses to build on and expand their operations."

Minister Trachsel is keen to promote the canton as a business destination and, seeing as Graubünden is the country's largest and arguably most diverse canton, he is right to do so. "We would like to see more industrial growth, as I believe we have great potential for developing an industrial sector in our economy and we are particularly keen on our potential in the high-tech sector," he explained.

Life sciences and mechanical engineering already feature highly in the canton's economy, and across all sectors several globally recognized names are located in Graubünden, including Hamilton Bonaduz, Würth, Valser Spring (Coca-Cola), and Integra Biosciences.

The canton offers a moderate tax regime that many international companies would find favorable, a highly skilled workforce, first-rate infrastructure, and, perhaps most importantly, Switzerland's best quality of life based on the number of residents in terms of jobs, spending power, education, leisure facilities, and personal security. "Here people also speak two or three languages: German, Italian and English. You have a lot of people who even speak four languages," he added, pointing out another advantage.

The recently revised tax law has greatly reduced the tax burden on individuals and legal entities. Graubünden has drastically lowered taxes on profits, and many special duties on the capital of residents and businesses have been abolished altogether. For businesses, the maximum tax on profits will be lowered to 16.8 percent. They also offer a liberal policy that allows for the amortization of up to 80 percent in the year of acquisition or for the following twelve months, which also helps companies achieve significant tax savings. Graubünden also grants tax relief for a limited period of time to companies new to the canton.

So the challenge for Trachsel is clear: "We are not known for how good we are. So do come to the WEF, enjoy our resorts, but also consider enjoying the canton for your business. If you are thinking of investing in Switzerland, put us on your short list."

10 GOOD REASONS FOR GRAUBÜNDEN

- Highest quality of life in Switzerland (Cantonal rating, FACTS 2006)
- Moderate tax rates (2010; 8.5% - max. 16.8% of net profit before taxes)
- Highly qualified, well educated and loyal employees
- 25% Lower wage and real estate costs than in the Swiss metropolitan areas
- Central European location (on the North-South-axis Stuttgart/Munich-Milan)
- Proximity to the international airports in Zurich, Altenrhein, Lugano, Agno and Milan
- Excellent education system with private and international schools in Tamins, Buchs and Triesenberg
- Renowned Universities of Applied Sciences and Universities in the vicinity
- Various research institutes in the canton
- Unbureaucratic and company-friendly government

Testimonial: Andreas Wieland, CEO Hamilton Bonaduz AG

"Graubünden is an ideal location due to the low tax rates and land prices. It's a great plus for Hamilton's recruiting that our high qualified staff can work where others enjoy their holidays. Due to the high quality of education at the local universities and research institutes this region is ideal for innovation-oriented technology companies. The airport at Zurich is only 80 minutes away by car".

The U.S. company Hamilton is a global leader in laboratory automation, sensor and medical technology. Since 1966, the company runs product development and manufacturing in Bonaduz. In 2009 it opened a new development and manufacturing facility with 16'000m², adding 150 new jobs and bringing the total number of employees to 750.



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SWITZERLAND

Cleantech capital by 2025

A CONVERSATION WITH

Andreas Rickenbacher*Berne's Minister of Economic Affairs*

The canton of Berne, home of the Swiss federal government and famous for the Bernese Oberland, has been riding on the success of their cluster policy, which is now driving growth.

"The advantage of Berne is that you get to test your products among the two most important continental cultures, French and German," says Rickenbacher, stating that many American corporations such as eBay, PepsiCo, and Mattel are already taking advantage of the canton's economic assets.

Berne has "clusters for cleantech, precision industry, and medical and ICT sectors," he explained. These four clusters alone make a strong contribution to the canton's economy. He plans for Berne to become the cleantech capital by 2025.

Enterprises in the solar industry, like the Meyer Burger Group, or projects like the "Spirit of Biel" solar car—winner of the World Solar Challenge in Australia—are examples of how Berne is thriving in the cleantech arena.



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Innovation-Based Success

A CONVERSATION WITH

Dr. Daniel Vasella*Chairman of Novartis*

What symbolizes Swiss-U.S. relations?

There is a strong connection between the two countries ranging from business and research to innovation and science. At all ranks there is a high level of engagement. Novartis is an excellent example of this: we are so integrated in the U.S. market that in some aspects we are more American than Swiss.

Is Novartis appreciated in the U.S.?

Very much so. One third of our global business comes from the U.S. market. We have worked very closely with the U.S. government, and in 2009 the Department of Health and Human Services awarded Novartis the contract to build the first manufacturing plant for the cell-based influenza vaccine.

What is the driving force behind Novartis's success?

From the very beginning innovation has been our driving force. In our industry you cannot survive without being innovative. It is our lifeblood. Innovation has led to our success; innovation has led to Novartis being awarded more FDA approvals than any other pharmaceutical company in the last ten years.

How do you continue to be innovative?

We have always been known for, and will continue to be known for, going to where the best talent is and recruiting the best scientists. We then give them the resources and the time needed to come up with the best products, and it has paid off for us.

Will the U.S. always contribute to this innovation?

I hope so, but there are a few warning signs. If the U.S. gives up on science-based research and scientific production and sends it offshore, then I would be less optimistic. The U.S. must maintain its strength in scientific innovation and keep it in the U.S.



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SWITZERLAND

Innovation has a name – Oerlikon**A CONVERSATION WITH
Dr. Michael Buscher**

CEO of OC Oerlikon



Switzerland has always been associated with precision and innovation, and one company that is building on the country's reputation and making these virtues its own is Oerlikon.

This is no accident. Six of the company's business units are active in machine and plant engineering—for textile machines, thin film coating, thin film silicon solar modules, drive systems, and “advanced technologies.” Oerlikon is turning itself into a leading global company in its field of activities and adopted the tagline “Innovation has a name—Oerlikon” in early 2011.

Cutting-edge technology is the name of its game. It invests more than \$200 million each year in research and development (R&D), and the company has at its disposal 1,200 highly qualified developers and scientists around the world.

CEO Michael Buscher explained the company's goals: “We want to be seen as an innovative company. At the start of last year we introduced this new tagline, and it sums up our commitment across our broad high-tech product range.”

The company has strong Swiss roots and, with its one-hundred-year history, is very keen to be seen as truly Swiss, as it is a label that stands for quality. The company also has a large international footprint. “Our international presence is very important to us. We operate more than 150 sites across 38 countries,” explained Buscher.

It might seem odd, then, that the company talks of having to build up their reputation. Not really. When the global credit crunch hit in 2008, Oerlikon's financials started to lose their shine. A comprehensive refinancing in 2010 cleaned up the balance sheet. Buscher, who joined Oerlikon in May 2010, developed a consistent program to achieve operational excellence, reduce costs, and streamline the product portfolio, as well as enter new markets. “We are on the way to a sustainable comeback, and our goal is to become best-in-class in all our businesses,” Buscher told us, adding that “it is not sufficient to be the technology leader—we have to create value for all our stakeholders.”

The company has turned the corner. By the end of the first nine months of 2011, the 17,000 worldwide employees had generated sales just shy of \$3.1 billion—a sales growth of 24 percent on the same period the previous year.

Normalized for currency impact, the growth would have been 42 percent. Revenue growth has come from the restructuring but also from an increased presence in emerging markets and a strong product pipeline. Even more important: Oerlikon is generating record profits that have already exceeded historical best margins. “We were able to increase our profitability outlook twice this year,” Buscher mentioned.

Even though the U.S. market is not the largest by sales percentage for the company, Buscher was keen to point out that it remains a very interesting proposition for them and that he sees key levels of growth coming out of the company's interests in the U.S. “The U.S. is interesting for us as it offers many opportunities. We have a lot of know-how and specialized products that are fitting to the needs of the U.S. customers who demand highly sophisticated products,” he said.

It has been mainly thanks to their drive systems that Oerlikon has a very strong footprint in the U.S. They have manufacturing sites in the U.S. for gears, gear solutions, and transmission systems. Industrial coatings and vacuum pump applications in the U.S. also provide strong growth opportunities.

This growth could also come from the solar market sector, where Buscher sees strong potential in the U.S. In fact, in September 2011 Oerlikon Solar launched a new record-breaking module with 154 (peak) watts (W) of stabilized module output and 10.8 percent efficiency. This represents an increase of 8 percent over the previous peak value. The record module will be ready for use on Oerlikon Solar's existing ThinFab™ lines by early 2013.

The company is clearly an important member of the innovation and high-tech food chain. Global names and customers of Oerlikon such as Sony, Bosch, ABB, Ferrari, and Caterpillar buy production technologies and components from Oerlikon to achieve their own success with high-tech products.

The company holds the U.S. in esteem, in particular as a testing ground for some of their new technologies. “U.S. customers are highly educated, and you have to convince them with your technology,” Buscher explained. “So in that sense, if you can prove in one of the most demanding markets in the world that your technology works, you can take that same technology to other parts of the world and achieve success.”

That said, the current growth is driven by emerging markets. Asia has already gained a revenue share of nearly 50 percent. With nearly 6,000 employees, Oerlikon already has a strong presence in this fast-growing area. Consequently, Oerlikon recently announced it will move its headquarters and select top management, including the CEO and CFO of its textile business, to Shanghai.

If one thing is clear, it is that the company has come through a rough patch, and like many others with solid leadership, it has come through in better shape than when the global crisis started. It is another example of Swiss innovation, determination, and precision—all of which lead U.S. customers to want and need their products.

Why invest in the Valais?

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SWITZERLAND

ABB stays ahead of global growth trends**A CONVERSATION WITH
Joseph Hogan**

CEO of ABB



The global financial crisis that began in 2008 triggered knock-on effects, the commercial consequences of which are still coming to the fore and adversely affecting many global corporations. However, one company dug in and, under the astute leadership of its CEO, bucked the trend, in the process engineering a strong position for itself.

ABB, as ever a major participant at Davos, is the leading global power and automation technology group, with global revenues of \$31.6 billion in 2010 and more than 124,000 employees. CEO Joe Hogan explained why they have been so successful in a difficult market: "We may be Swiss-based, but we are a very broad company. We are also extremely international and we have taken advantage of areas in the world where there has been strong growth."

As one of the leading grid-making companies, ABB has found markets where governments have invested in infrastructure upgrades to help boost their economies. Emerging economies in the Far East and the rush to install

greener technologies have also helped. "We supply a lot of equipment to projects like e-mobility, electrical trains, wind turbines, and solar farms. As you use more renewable energy, more pressure is put on the grids, and that's where we come in," he explained.

It is easy to see why Hogan is confident about the future. Halfway through 2011, the company reported a 43 percent increase in second-quarter net profits thanks to strong industrial growth, higher earnings in the Power Systems division, and contributions from recent acquisitions.

ABB is yet another example of the strong U.S.-Swiss relationship. The company has built the world's most powerful battery storage system, which provides emergency power in Alaska, and ABB technology is used NASA's Scramjet facility for simulating speeds up to Mach 8. Pennsylvania-educated Hogan is cognizant of the direction of the relationship between the two countries: "They want the same things and ultimately they want to grow together," he added.

A new and powerful Swiss-U.S. partnership has recently emerged after ABB and IO of Phoenix, Arizona, agreed to jointly deliver the world's first direct current (DC)-powered data center module. This new module will be 10 to 20 percent more energy efficient than traditional alternating current technology and will meet the increasing demand for DC data centers.

"This is a perfect market segment for us because it is a combination of power and automation. The software capability, the power, and the delivery of power is something ABB is expert in," said Hogan. This is proof of Swiss and Americans working together on yet another groundbreaking project.

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The Future of History

Can Liberal Democracy Survive the Decline of the Middle Class?

Francis Fukuyama

Something strange is going on in the world today. The global financial crisis that began in 2008 and the ongoing crisis of the euro are both products of the model of lightly regulated financial capitalism that emerged over the past three decades. Yet despite widespread anger at Wall Street bailouts, there has been no great upsurge of left-wing American populism in response. It is conceivable that the Occupy Wall Street movement will gain traction, but the most dynamic recent populist movement to date has been the right-wing Tea Party, whose main target is the regulatory state that seeks to protect ordinary people from financial speculators. Something similar is true in Europe as well, where the left is anemic and right-wing populist parties are on the move.

There are several reasons for this lack of left-wing mobilization, but chief among them is a failure in the realm of ideas. For the past generation, the ideological high ground on economic issues has been held by a libertarian right. The left has not been able to make a plausible case for an agenda

other than a return to an unaffordable form of old-fashioned social democracy. This absence of a plausible progressive counter-narrative is unhealthy, because competition is good for intellectual debate just as it is for economic activity. And serious intellectual debate is urgently needed, since the current form of globalized capitalism is eroding the middle-class social base on which liberal democracy rests.

THE DEMOCRATIC WAVE

Social forces and conditions do not simply “determine” ideologies, as Karl Marx once maintained, but ideas do not become powerful unless they speak to the concerns of large numbers of ordinary people. Liberal democracy is the default ideology around much of the world today in part because it responds to and is facilitated by certain socioeconomic structures. Changes in those structures may have ideological consequences, just as ideological changes may have socioeconomic consequences.

Almost all the powerful ideas that shaped human societies up until the past

FRANCIS FUKUYAMA is a Senior Fellow at the Center on Democracy, Development, and the Rule of Law at Stanford University and the author, most recently, of *The Origins of Political Order: From Prehuman Times to the French Revolution*.

Francis Fukuyama

300 years were religious in nature, with the important exception of Confucianism in China. The first major secular ideology to have a lasting worldwide effect was liberalism, a doctrine associated with the rise of first a commercial and then an industrial middle class in certain parts of Europe in the seventeenth century. (By “middle class,” I mean people who are neither at the top nor at the bottom of their societies in terms of income, who have received at least a secondary education, and who own either real property, durable goods, or their own businesses.)

As enunciated by classic thinkers such as Locke, Montesquieu, and Mill, liberalism holds that the legitimacy of state authority derives from the state’s ability to protect the individual rights of its citizens and that state power needs to be limited by the adherence to law. One of the fundamental rights to be protected is that of private property; England’s Glorious Revolution of 1688–89 was critical to the development of modern liberalism because it first established the constitutional principle that the state could not legitimately tax its citizens without their consent.

At first, liberalism did not necessarily imply democracy. The Whigs who supported the constitutional settlement of 1689 tended to be the wealthiest property owners in England; the parliament of that period represented less than ten percent of the whole population. Many classic liberals, including Mill, were highly skeptical of the virtues of democracy: they believed that responsible political participation required education and a stake in society—that is, property ownership. Up through the end of the nineteenth century, the franchise was limited by property and educational requirements in virtually all parts of

Europe. Andrew Jackson’s election as U.S. president in 1828 and his subsequent abolition of property requirements for voting, at least for white males, thus marked an important early victory for a more robust democratic principle.

In Europe, the exclusion of the vast majority of the population from political power and the rise of an industrial working class paved the way for Marxism. *The Communist Manifesto* was published in 1848, the same year that revolutions spread to all the major European countries save the United Kingdom. And so began a century of competition for the leadership of the democratic movement between communists, who were willing to jettison procedural democracy (multiparty elections) in favor of what they believed was substantive democracy (economic redistribution), and liberal democrats, who believed in expanding political participation while maintaining a rule of law protecting individual rights, including property rights.

At stake was the allegiance of the new industrial working class. Early Marxists believed they would win by sheer force of numbers: as the franchise was expanded in the late nineteenth century, parties such as the United Kingdom’s Labour and Germany’s Social Democrats grew by leaps and bounds and threatened the hegemony of both conservatives and traditional liberals. The rise of the working class was fiercely resisted, often by nondemocratic means; the communists and many socialists, in turn, abandoned formal democracy in favor of a direct seizure of power.

Throughout the first half of the twentieth century, there was a strong consensus on the progressive left that some form of socialism—government control of the commanding heights of the economy in

The Future of History

order to ensure an egalitarian distribution of wealth—was unavoidable for all advanced countries. Even a conservative economist such as Joseph Schumpeter could write in his 1942 book, *Capitalism, Socialism, and Democracy*, that socialism would emerge victorious because capitalist society was culturally self-undermining. Socialism was believed to represent the will and interests of the vast majority of people in modern societies.

Yet even as the great ideological conflicts of the twentieth century played themselves out on a political and military level, critical changes were happening on a social level that undermined the Marxist scenario. First, the real living standards of the industrial working class kept rising, to the point where many workers or their children were able to join the middle class. Second, the relative size of the working class stopped growing and actually began to decline, particularly in the second half of the twentieth century, when services began to displace manufacturing in what were labeled “postindustrial” economies. Finally, a new group of poor or disadvantaged people emerged below the industrial working class—a heterogeneous mixture of racial and ethnic minorities, recent immigrants, and socially excluded groups, such as women, gays, and the disabled. As a result of these changes, in most industrialized societies, the old working class has become just another domestic interest group, one using the political power of trade unions to protect the hard-won gains of an earlier era.

Economic class, moreover, turned out not to be a great banner under which to mobilize populations in advanced industrial countries for political action. The Second International got a rude wake-up call in 1914, when the working classes of Europe

abandoned calls for class warfare and lined up behind conservative leaders preaching nationalist slogans, a pattern that persists to the present day. Many Marxists tried to explain this, according to the scholar Ernest Gellner, by what he dubbed the “wrong address theory”:

Just as extreme Shi’ite Muslims hold that Archangel Gabriel made a mistake, delivering the Message to Mohamed when it was intended for Ali, so Marxists basically like to think that the spirit of history or human consciousness made a terrible boob. The awakening message was intended for classes, but by some terrible postal error was delivered to nations.

Gellner went on to argue that religion serves a function similar to nationalism in the contemporary Middle East: it mobilizes people effectively because it has a spiritual and emotional content that class consciousness does not. Just as European nationalism was driven by the shift of Europeans from the countryside to cities in the late nineteenth century, so, too, Islamism is a reaction to the urbanization and displacement taking place in contemporary Middle Eastern societies. Marx’s letter will never be delivered to the address marked “class.”

Marx believed that the middle class, or at least the capital-owning slice of it that he called the bourgeoisie, would always remain a small and privileged minority in modern societies. What happened instead was that the bourgeoisie and the middle class more generally ended up constituting the vast majority of the populations of most advanced countries, posing problems for socialism. From the days of Aristotle, thinkers have believed that stable democracy rests on a broad middle class and that societies with extremes of wealth and

Francis Fukuyama

poverty are susceptible either to oligarchic domination or populist revolution. When much of the developed world succeeded in creating middle-class societies, the appeal of Marxism vanished. The only places where leftist radicalism persists as a powerful force are in highly unequal areas of the world, such as parts of Latin America, Nepal, and the impoverished regions of eastern India.

What the political scientist Samuel Huntington labeled the “third wave” of global democratization, which began in southern Europe in the 1970s and culminated in the fall of communism in Eastern Europe in 1989, increased the number of electoral democracies around the world from around 45 in 1970 to more than 120 by the late 1990s. Economic growth has led to the emergence of new middle classes in countries such as Brazil, India, Indonesia, South Africa, and Turkey. As the economist Moisés Naím has pointed out, these middle classes are relatively well educated, own property, and are technologically connected to the outside world. They are demanding of their governments and mobilize easily as a result of their access to technology. It should not be surprising that the chief instigators of the Arab Spring uprisings were well-educated Tunisians and Egyptians whose expectations for jobs and political participation were stymied by the dictatorships under which they lived.

Middle-class people do not necessarily support democracy in principle: like everyone else, they are self-interested actors who want to protect their property and position. In countries such as China and Thailand, many middle-class people feel threatened by the redistributive demands of the poor and hence have lined up in support of authoritarian governments

that protect their class interests. Nor is it the case that democracies necessarily meet the expectations of their own middle classes, and when they do not, the middle classes can become restive.

THE LEAST BAD ALTERNATIVE?

There is today a broad global consensus about the legitimacy, at least in principle, of liberal democracy. In the words of the economist Amartya Sen, “While democracy is not yet universally practiced, nor indeed uniformly accepted, in the general climate of world opinion, democratic governance has now achieved the status of being taken to be generally right.” It is most broadly accepted in countries that have reached a level of material prosperity sufficient to allow a majority of their citizens to think of themselves as middle class, which is why there tends to be a correlation between high levels of development and stable democracy.

Some societies, such as Iran and Saudi Arabia, reject liberal democracy in favor of a form of Islamic theocracy. Yet these regimes are developmental dead ends, kept alive only because they sit atop vast pools of oil. There was at one time a large Arab exception to the third wave, but the Arab Spring has shown that Arab publics can be mobilized against dictatorship just as readily as those in Eastern Europe and Latin America were. This does not of course mean that the path to a well-functioning democracy will be easy or straightforward in Tunisia, Egypt, or Libya, but it does suggest that the desire for political freedom and participation is not a cultural peculiarity of Europeans and Americans.

The single most serious challenge to liberal democracy in the world today

The Future of History

comes from China, which has combined authoritarian government with a partially marketized economy. China is heir to a long and proud tradition of high-quality bureaucratic government, one that stretches back over two millennia. Its leaders have managed a hugely complex transition from a centralized, Soviet-style planned economy to a dynamic open one and have done so with remarkable competence—more competence, frankly, than U.S. leaders have shown in the management of their own macroeconomic policy recently. Many people currently admire the Chinese system not just for its economic record but also because it can make large, complex decisions quickly, compared with the agonizing policy paralysis that has struck both the United States and Europe in the past few years. Especially since the recent financial crisis, the Chinese themselves have begun touting the “China model” as an alternative to liberal democracy.

This model is unlikely to ever become a serious alternative to liberal democracy in regions outside East Asia, however. In the first place, the model is culturally specific: the Chinese government is built around a long tradition of meritocratic recruitment, civil service examinations, a high emphasis on education, and deference to technocratic authority. Few developing countries can hope to emulate this model; those that have, such as Singapore and South Korea (at least in an earlier period), were already within the Chinese cultural zone. The Chinese themselves are skeptical about whether their model can be exported; the so-called Beijing consensus is a Western invention, not a Chinese one.

It is also unclear whether the model can be sustained. Neither export-driven growth

nor the top-down approach to decision-making will continue to yield good results forever. The fact that the Chinese government would not permit open discussion of the disastrous high-speed rail accident last summer and could not bring the Railway Ministry responsible for it to heel suggests that there are other time bombs hidden behind the façade of efficient decision-making.

Finally, China faces a great moral vulnerability down the road. The Chinese government does not force its officials to respect the basic dignity of its citizens. Every week, there are new protests about land seizures, environmental violations, or gross corruption on the part of some official. While the country is growing rapidly, these abuses can be swept under the carpet. But rapid growth will not continue forever, and the government will have to pay a price in pent-up anger. The regime no longer has any guiding ideal around which it is organized; it is run by a Communist Party supposedly committed to equality that presides over a society marked by dramatic and growing inequality.

So the stability of the Chinese system can in no way be taken for granted. The Chinese government argues that its citizens are culturally different and will always prefer benevolent, growth-promoting dictatorship to a messy democracy that threatens social stability. But it is unlikely that a spreading middle class will behave all that differently in China from the way it has behaved in other parts of the world. Other authoritarian regimes may be trying to emulate China's success, but there is little chance that much of the world will look like today's China 50 years down the road.

Francis Fukuyama

DEMOCRACY'S FUTURE

There is a broad correlation among economic growth, social change, and the hegemony of liberal democratic ideology in the world today. And at the moment, no plausible rival ideology looms. But some very troubling economic and social trends, if they continue, will both threaten the stability of contemporary liberal democracies and dethrone democratic ideology as it is now understood.

The sociologist Barrington Moore once flatly asserted, “No bourgeois, no democracy.” The Marxists didn’t get their communist utopia because mature capitalism generated middle-class societies, not working-class ones. But what if the further development of technology and globalization undermines the middle class and makes it impossible for more than a minority of citizens in an advanced society to achieve middle-class status?

There are already abundant signs that such a phase of development has begun. Median incomes in the United States have been stagnating in real terms since the 1970s. The economic impact of this stagnation has been softened to some extent by the fact that most U.S. households have shifted to two income earners in the past generation. Moreover, as the economist Raghuram Rajan has persuasively argued, since Americans are reluctant to engage in straightforward redistribution, the United States has instead attempted a highly dangerous and inefficient form of redistribution over the past generation by subsidizing mortgages for low-income households. This trend, facilitated by a flood of liquidity pouring in from China and other countries, gave many ordinary Americans the illusion that their standards

of living were rising steadily during the past decade. In this respect, the bursting of the housing bubble in 2008–9 was nothing more than a cruel reversion to the mean. Americans may today benefit from cheap cell phones, inexpensive clothing, and Facebook, but they increasingly cannot afford their own homes, or health insurance, or comfortable pensions when they retire.

A more troubling phenomenon, identified by the venture capitalist Peter Thiel and the economist Tyler Cowen, is that the benefits of the most recent waves of technological innovation have accrued disproportionately to the most talented and well-educated members of society. This phenomenon helped cause the massive growth of inequality in the United States over the past generation. In 1974, the top one percent of families took home nine percent of GDP; by 2007, that share had increased to 23.5 percent.

Trade and tax policies may have accelerated this trend, but the real villain here is technology. In earlier phases of industrialization—the ages of textiles, coal, steel, and the internal combustion engine—the benefits of technological changes almost always flowed down in significant ways to the rest of society in terms of employment. But this is not a law of nature. We are today living in what the scholar Shoshana Zuboff has labeled “the age of the smart machine,” in which technology is increasingly able to substitute for more and higher human functions. Every great advance for Silicon Valley likely means a loss of low-skill jobs elsewhere in the economy, a trend that is unlikely to end anytime soon.

Inequality has always existed, as a result of natural differences in talent and character. But today’s technological world vastly

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magnifies those differences. In a nineteenth-century agrarian society, people with strong math skills did not have that many opportunities to capitalize on their talent. Today, they can become financial wizards or software engineers and take home ever-larger proportions of the national wealth.

The other factor undermining middle-class incomes in developed countries is globalization. With the lowering of transportation and communications costs and the entry into the global work force of hundreds of millions of new workers in developing countries, the kind of work done by the old middle class in the developed world can now be performed much more cheaply elsewhere. Under an economic model that prioritizes the maximization of aggregate income, it is inevitable that jobs will be outsourced.

Smarter ideas and policies could have contained the damage. Germany has succeeded in protecting a significant part of its manufacturing base and industrial labor force even as its companies have remained globally competitive. The United States and the United Kingdom, on the other hand, happily embraced the transition to the postindustrial service economy. Free trade became less a theory than an ideology: when members of the U.S. Congress tried to retaliate with trade sanctions against China for keeping its currency undervalued, they were indignantly charged with protectionism, as if the playing field were already level. There was a lot of happy talk about the wonders of the knowledge economy, and how dirty, dangerous manufacturing jobs would inevitably be replaced by highly educated workers doing creative and interesting things. This was a gauzy veil placed over the hard facts of deindustrial-

ization. It overlooked the fact that the benefits of the new order accrued disproportionately to a very small number of people in finance and high technology, interests that dominated the media and the general political conversation.

THE ABSENT LEFT

One of the most puzzling features of the world in the aftermath of the financial crisis is that so far, populism has taken primarily a right-wing form, not a left-wing one.

In the United States, for example, although the Tea Party is anti-elitist in its rhetoric, its members vote for conservative politicians who serve the interests of precisely those financiers and corporate elites they claim to despise. There are many explanations for this phenomenon. They include a deeply embedded belief in equality of opportunity rather than equality of outcome and the fact that cultural issues, such as abortion and gun rights, crosscut economic ones.

But the deeper reason a broad-based populist left has failed to materialize is an intellectual one. It has been several decades since anyone on the left has been able to articulate, first, a coherent analysis of what happens to the structure of advanced societies as they undergo economic change and, second, a realistic agenda that has any hope of protecting a middle-class society.

The main trends in left-wing thought in the last two generations have been, frankly, disastrous as either conceptual frameworks or tools for mobilization. Marxism died many years ago, and the few old believers still around are ready for nursing homes. The academic left replaced it with postmodernism, multiculturalism,

Francis Fukuyama

feminism, critical theory, and a host of other fragmented intellectual trends that are more cultural than economic in focus. Postmodernism begins with a denial of the possibility of any master narrative of history or society, undercutting its own authority as a voice for the majority of citizens who feel betrayed by their elites. Multiculturalism validates the victimhood of virtually every out-group. It is impossible to generate a mass progressive movement on the basis of such a motley coalition: most of the working- and lower-middle-class citizens victimized by the system are culturally conservative and would be embarrassed to be seen in the presence of allies like this.

Whatever the theoretical justifications underlying the left's agenda, its biggest problem is a lack of credibility. Over the past two generations, the mainstream left has followed a social democratic program that centers on the state provision of a variety of services, such as pensions, health care, and education. That model is now exhausted: welfare states have become big, bureaucratic, and inflexible; they are often captured by the very organizations that administer them, through public-sector unions; and, most important, they are fiscally unsustainable given the aging of populations virtually everywhere in the developed world. Thus, when existing social democratic parties come to power, they no longer aspire to be more than custodians of a welfare state that was created decades ago; none has a new, exciting agenda around which to rally the masses.

AN IDEOLOGY OF THE FUTURE

Imagine, for a moment, an obscure scribbler today in a garret somewhere trying to outline an ideology of the future that

could provide a realistic path toward a world with healthy middle-class societies and robust democracies. What would that ideology look like?

It would have to have at least two components, political and economic. Politically, the new ideology would need to reassert the supremacy of democratic politics over economics and legitimate anew government as an expression of the public interest. But the agenda it put forward to protect middle-class life could not simply rely on the existing mechanisms of the welfare state. The ideology would need to somehow redesign the public sector, freeing it from its dependence on existing stakeholders and using new, technology-empowered approaches to delivering services. It would have to argue forthrightly for more redistribution and present a realistic route to ending interest groups' domination of politics.

Economically, the ideology could not begin with a denunciation of capitalism as such, as if old-fashioned socialism were still a viable alternative. It is more the variety of capitalism that is at stake and the degree to which governments should help societies adjust to change. Globalization need be seen not as an inexorable fact of life but rather as a challenge and an opportunity that must be carefully controlled politically. The new ideology would not see markets as an end in themselves; instead, it would value global trade and investment to the extent that they contributed to a flourishing middle class, not just to greater aggregate national wealth.

It is not possible to get to that point, however, without providing a serious and sustained critique of much of the edifice of modern neoclassical economics, beginning

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with fundamental assumptions such as the sovereignty of individual preferences and that aggregate income is an accurate measure of national well-being. This critique would have to note that people's incomes do not necessarily represent their true contributions to society. It would have to go further, however, and recognize that even if labor markets were efficient, the natural distribution of talents is not necessarily fair and that individuals are not sovereign entities but beings heavily shaped by their surrounding societies.

Most of these ideas have been around in bits and pieces for some time; the scribbler would have to put them into a coherent package. He or she would also have to avoid the "wrong address" problem. The critique of globalization, that is, would have to be tied to nationalism as a strategy for mobilization in a way that defined national interest in a more sophisticated way than, for example, the "Buy American" campaigns of unions in the United States. The product would be a synthesis of ideas from both the left and the right, detached from the agenda of the marginalized groups that constitute the existing progressive movement. The ideology would be populist; the message would begin with a critique of the elites that allowed the benefit of the many to be sacrificed to that of the few and a critique of the money politics, especially in Washington, that overwhelmingly benefits the wealthy.

The dangers inherent in such a movement are obvious: a pullback by the United States, in particular, from its advocacy of a more open global system could set off protectionist responses elsewhere. In many respects, the Reagan-Thatcher revolution succeeded just as its proponents

hoped, bringing about an increasingly competitive, globalized, friction-free world. Along the way, it generated tremendous wealth and created rising middle classes all over the developing world, and the spread of democracy in their wake. It is possible that the developed world is on the cusp of a series of technological breakthroughs that will not only increase productivity but also provide meaningful employment to large numbers of middle-class people.

But that is more a matter of faith than a reflection of the empirical reality of the last 30 years, which points in the opposite direction. Indeed, there are a lot of reasons to think that inequality will continue to worsen. The current concentration of wealth in the United States has already become self-reinforcing: as the economist Simon Johnson has argued, the financial sector has used its lobbying clout to avoid more onerous forms of regulation. Schools for the well-off are better than ever; those for everyone else continue to deteriorate. Elites in all societies use their superior access to the political system to protect their interests, absent a countervailing democratic mobilization to rectify the situation. American elites are no exception to the rule.

That mobilization will not happen, however, as long as the middle classes of the developed world remain enthralled by the narrative of the past generation: that their interests will be best served by ever-freer markets and smaller states. The alternative narrative is out there, waiting to be born. 🌐

The Democratic Malaise

Globalization and the Threat to the West

Charles A. Kupchan

A crisis of governability has engulfed the world's most advanced democracies. It is no accident that the United States, Europe, and Japan are simultaneously experiencing political breakdown; globalization is producing a widening gap between what electorates are asking of their governments and what those governments are able to deliver. The mismatch between the growing demand for good governance and its shrinking supply is one of the gravest challenges facing the Western world today.

Voters in industrialized democracies are looking to their governments to respond to the decline in living standards and the growing inequality resulting from unprecedented global flows of goods, services, and capital. They also expect their representatives to deal with surging immigration, global warming, and other knock-on effects of a globalized world. But Western governments are not up to the task. Globalization is making less effective the policy levers at their disposal

while also diminishing the West's traditional sway over world affairs by fueling the "rise of the rest." The inability of democratic governments to address the needs of their broader publics has, in turn, only increased popular disaffection, further undermining the legitimacy and efficacy of representative institutions.

This crisis of governability within the Western world comes at a particularly inopportune moment. The international system is in the midst of tectonic change due to the diffusion of wealth and power to new quarters. Globalization was supposed to have played to the advantage of liberal societies, which were presumably best suited to capitalize on the fast and fluid nature of the global marketplace. But instead, mass publics in the advanced democracies of North America, Europe, and East Asia have been particularly hard hit—precisely because their countries' economies are both mature and open to the world.

In contrast, Brazil, India, Turkey, and other rising democracies are benefiting

CHARLES A. KUPCHAN is Professor of International Affairs at Georgetown University and Whitney Shepardson Senior Fellow at the Council on Foreign Relations. This essay is adapted from his forthcoming book *No One's World: The West, the Rising Rest, and the Coming Global Turn* (Oxford University Press, 2012).

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from the shift of economic vitality from the developed to the developing world. And China is proving particularly adept at reaping globalization's benefits while limiting its liabilities—in no small part because it has retained control over policy instruments abandoned by its liberal competitors. State capitalism has its distinct advantages, at least for now. As a consequence, it is not just the West's material primacy that is at stake today but also the allure of its version of modernity. Unless liberal democracies can restore their political and economic solvency, the politics, as well as the geopolitics, of the twenty-first century may well be up for grabs.

DEER IN THE HEADLIGHTS

Globalization has expanded aggregate wealth and enabled developing countries to achieve unprecedented prosperity. The proliferation of investment, trade, and communication networks has deepened interdependence and its potentially pacifying effects and has helped pry open nondemocratic states and foster popular uprisings. But at the same time, globalization and the digital economy on which it depends are the main source of the West's current crisis of governability. Deindustrialization and outsourcing, global trade and fiscal imbalances, excess capital and credit and asset bubbles—these consequences of globalization are imposing hardships and insecurity not experienced for generations. The distress stemming from the economic crisis that began in 2008 is particularly acute, but the underlying problems began much earlier. For the better part of two decades, middle-class wages in the world's leading democracies have been stagnant, and economic inequality has been rising sharply as globalization has handsomely

rewarded its winners but left its many losers behind.

These trends are not temporary byproducts of the business cycle, nor are they due primarily to insufficient regulation of the financial sector, tax cuts amid expensive wars, or other errant policies. Stagnant wages and rising inequality are, as the economic analysts Daniel Alpert, Robert Hockett, and Nouriel Roubini recently argued in their study "The Way Forward," a consequence of the integration of billions of low-wage workers into the global economy and increases in productivity stemming from the application of information technology to the manufacturing sector. These developments have pushed global capacity far higher than demand, exacting a heavy toll on workers in the high-wage economies of the industrialized West. The resulting dislocation and disaffection among Western electorates have been magnified by globalization's intensification of transnational threats, such as international crime, terrorism, unwanted immigration, and environmental degradation. Adding to this nasty mix is the information revolution; the Internet and the profusion of mass media appear to be fueling ideological polarization more than they are cultivating deliberative debate.

Voters confronted with economic duress, social dislocation, and political division look to their elected representatives for help. But just as globalization is stimulating this pressing demand for responsive governance, it is also ensuring that its provision is in desperately short supply. For three main reasons, governments in the industrialized West have entered a period of pronounced ineffectiveness.

First, globalization has made many of the traditional policy tools used by liberal

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democracies much blunter instruments. Washington has regularly turned to fiscal and monetary policy to modulate economic performance. But in the midst of global competition and unprecedented debt, the U.S. economy seems all but immune to injections of stimulus spending or the Federal Reserve's latest moves on interest rates. The scope and speed of commercial and financial flows mean that decisions and developments elsewhere—Beijing's intransigence on the value of the yuan, Europe's sluggish response to its financial crisis, the actions of investors and ratings agencies, an increase in the quality of Hyundai's latest models—outweigh decisions taken in Washington. Europe's democracies long relied on monetary policy to adjust to fluctuations in national economic performance. But they gave up that option when they joined the eurozone. Japan over the last two decades has tried one stimulus strategy after another, but to no avail. In a globalized world, democracies simply have less control over outcomes than they used to.

Second, many of the problems that Western electorates are asking their governments to solve require a level of international cooperation that is unattainable. The diffusion of power from the West to the rest means that there are today many new cooks in the kitchen; effective action no longer rests primarily on collaboration among like-minded democracies. Instead, it depends on cooperation among a much larger and more diverse circle of states. The United States now looks to the G-20 to rebalance the international economy. But consensus is elusive among nations that are at different stages of development and embrace divergent approaches to economic governance. Challenges such as curbing

global warming or effectively isolating Iran similarly depend on a collective effort that is well beyond reach.

Third, democracies can be nimble and responsive when their electorates are content and enjoy a consensus born of rising expectations, but they are clumsy and sluggish when their citizens are downcast and divided. Politics in which governance depends on popular participation, institutional checks and balances, and competition among interest groups appear to be better at distributing benefits than at apportioning sacrifice. But sacrifice is exactly what is necessary to restore economic solvency, which confronts Western governments with the unappetizing prospect of pursuing policies that threaten to weaken their electoral appeal.

ONE PROBLEM, THREE FLAVORS

In the United States, partisan confrontation is paralyzing the political system. The underlying cause is the poor state of the U.S. economy. Since 2008, many Americans have lost their houses, jobs, and retirement savings. And these setbacks come on the heels of back-to-back decades of stagnation in middle-class wages. Over the past ten years, the average household income in the United States has fallen by over ten percent. In the meantime, income inequality has been steadily rising, making the United States the most unequal country in the industrialized world. The primary source of the declining fortunes of the American worker is global competition; jobs have been heading overseas. In addition, many of the most competitive companies in the digital economy do not have long coattails. Facebook's estimated value is around \$70 billion, and it employs roughly 2,000 workers;

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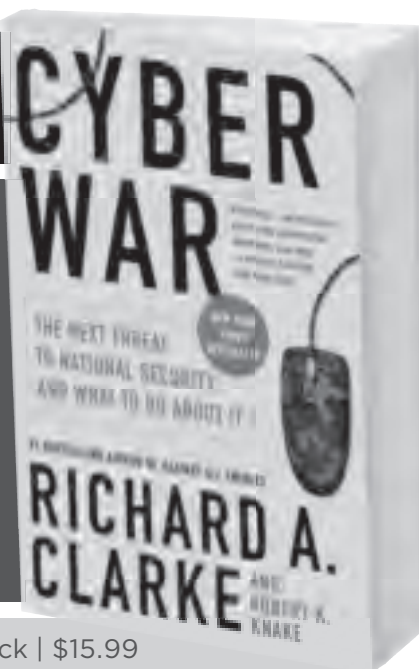
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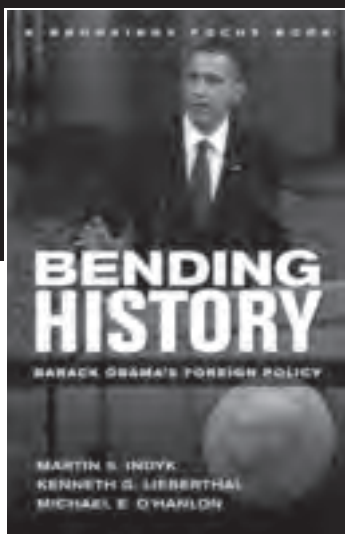
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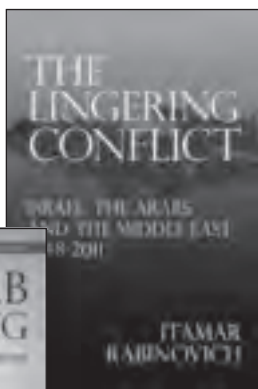
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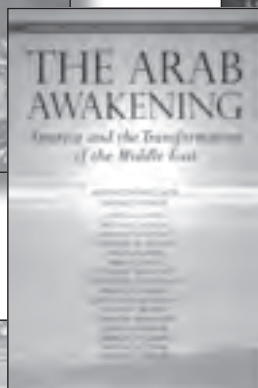


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The Democratic Malaise

compare this with General Motors, which is valued at \$35 billion and has 77,000 employees in the United States and 208,000 worldwide. The wealth of the United States' cutting-edge companies is not trickling down to the middle class.

These harsh economic realities are helping revive ideological and partisan cleavages long muted by the nation's rising economic fortunes. During the decades after World War II, a broadly shared prosperity pulled Democrats and Republicans toward the political center. But today, Capitol Hill is largely devoid of both centrists and bipartisanship; Democrats campaign for more stimulus, relief for the unemployed, and taxes on the rich, whereas Republicans clamor for radical cuts in the size and cost of government. Expediting the hollowing out of the center are partisan redistricting, a media environment that provokes more than it informs, and a broken campaign finance system that has been captured by special interests.

The resulting polarization is tying the country in knots. President Barack Obama realized as much, which is why he entered office promising to be a "post-partisan" president. But the failure of Obama's best efforts to revive the economy and restore bipartisan cooperation has exposed the systemic nature of the nation's economic and political dysfunction. His \$787 billion stimulus package, passed without the support of a single House Republican, was unable to resuscitate an economy plagued by debt, a deficit of middle-class jobs, and the global slowdown. Since the Republicans gained control of the House in 2010, partisan confrontation has stood in the way of progress on nearly every issue. Bills to promote economic

growth either fail to pass or are so watered down that they have little impact. Immigration reform and legislation to curb global warming are not even on the table.

Ineffective governance, combined with daily doses of partisan bile, has pushed public approval of Congress to historic lows. Spreading frustration has spawned the Occupy Wall Street movement—the first sustained bout of public protests since the Vietnam War. The electorate's discontent only deepens the challenges of governance, as vulnerable politicians cater to the narrow interests of the party base and the nation's political system loses what little wind it has in its sails.

Europe's crisis of governability, meanwhile, is taking the form of a renationalization of its politics. Publics are revolting against the double dislocations of European integration and globalization. As a consequence, the EU's member states are busily clawing back the prerogatives of sovereignty, threatening the project of European political and economic integration set in motion after World War II. As in the United States, economic conditions are the root of the problem. Over the past two decades, middle-class incomes in most major European economies have been falling and inequality has been rising. Unemployment in Spain stands at over 20 percent, and even Germany, the EU's premier economy, saw its middle class contract by 13 percent between 2000 and 2008. Those who slip through the cracks find a fraying safety net beneath them; Europe's comfortable welfare systems, which have become unsustainable in the face of global competition, are being dramatically scaled back. The austerity stemming from the ongoing debt crisis in the eurozone has only made matters

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worse. Greeks are as angry about the EU-enforced belt-tightening as Germans are about having to bail out Europe's economic laggards.

Europe's aging population has made immigration an economic necessity. But the lack of progress in integrating Muslim immigrants into the social mainstream has intensified discomfort over the EU's willingness to accept more outsiders into its midst. Far-right parties have been the beneficiaries of this anxiety, and their hard-edged nationalism targets not only immigrants but also the EU. Generational change is taking its own toll on popular enthusiasm for European integration. Europeans with memories of World War II see the EU as Europe's escape route from its bloody past. But younger Europeans have no past from which to flee. Whereas their elders viewed the European project as an article of faith, current leaders and electorates tend to assess the EU through a cold—and often negative—valuation of costs and benefits.

The collective governance that the EU desperately needs in order to thrive in a globalized world rests uneasily with a political street that is becoming decidedly hostile to the European project. Europe's institutions could descend to the level of its politics, which would effectively reduce the EU to little more than a trade bloc. Alternatively, national politics could again be infused with a European calling, which would breathe new legitimacy into an increasingly hollow union. The latter outcome is much preferable, but it will require leadership and resolve that, at least for now, are nowhere to be found.

Japan, for its part, has been politically adrift since Junichiro Koizumi stepped down as prime minister in 2006. There-

after, the Liberal Democratic Party (LDP), which had dominated Japanese politics throughout most of the postwar era, stumbled badly, losing power to the Democratic Party of Japan (DPJ) in 2009. The consolidation of a two-party system had the potential to improve governance but instead produced only gridlock and declining public confidence. Japan has cycled through six prime ministers in the last five years. This past summer, public approval of the DPJ stood at 18 percent. The DPJ and the LDP are as internally divided as they are at loggerheads. Policy-making has ground to a halt even on urgent issues; it took over 100 days for the Diet to pass legislation providing relief to the victims of last year's earthquake, tsunami, and nuclear disaster.

The trouble began with the bursting of Japan's asset bubble in 1991, a setback that exposed deeper problems in the country's economy and led to a "lost decade" of recession. Japanese manufacturers suffered as jobs and investment headed to China and the "Asian tigers." The country's traditional social compact, by which corporations provided lifetime employment and comfortable pensions, was no longer sustainable. The past two decades have brought a long slide in middle-class incomes, rising inequality, and a spike in the poverty rate from roughly seven percent in the 1980s to 16 percent in 2009. In 1989, Japan ranked fourth in the world in terms of per capita GDP; by 2010, its rank had plummeted to 24th.

It was to address such problems that Koizumi embarked on ambitious efforts to liberalize the economy and reduce the power of bureaucrats and interest groups. His charisma and ample parliamentary support made for significant progress, but

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his LDP and DPJ successors have been too weak to keep the process moving forward. Japan is therefore stuck in a no man's land, exposed to the dislocations of a globalized economy yet not liberalized or strategic enough to compete effectively.

BITTER MEDICINE

It is not by chance that the West's crisis of governability coincides with new political strength among rising powers; economic and political vigor is passing from the core to the periphery of the international system. And while the world's most open states are experiencing a loss of control as they integrate into a globalized world, illiberal states, such as China, are deliberately keeping a much tighter grip on their societies through centralized decision-making, censorship of the media, and state-supervised markets. If the leading democracies continue to lose their luster as developing countries chart their rise, the unfolding transition in global power will be significantly more destabilizing. Conversely, a realignment of the international pecking order would likely be more orderly if the Western democracies recouped and provided purposeful leadership.

What is needed is nothing less than a compelling twenty-first-century answer to the fundamental tensions among democracy, capitalism, and globalization. This new political agenda should aim to reassert popular control over political economy, directing state action toward effective responses to both the economic realities of global markets and the demands of mass societies for an equitable distribution of rewards and sacrifices.

The West should pursue three broad strategies to meet this challenge and thus better equip its democratic institutions for

a globalized world. First, when up against state capitalism and the potent force of global markets, the Western democracies have little choice but to engage in strategic economic planning on an unprecedented scale. State-led investment in jobs, infrastructure, education, and research will be required to restore economic competitiveness. Second, leaders should seek to channel electorate discontent toward reformist ends through a progressive brand of populism. By pursuing policies that advantage mass publics rather than the party faithful or special interests, politicians can not only rebuild their popularity but also reinvigorate democratic institutions and the values of citizenship and sacrifice. Third, Western governments must lead their electorates away from the temptation to turn inward. As history makes clear, hard times can stoke protectionism and isolationism. But globalization is here to stay, and retreat is not an option.

None of these strategies will be easy to implement, and embracing all of them together will require extraordinary leadership and the political courage to match. But until such an agenda is devised and realized, the democratic malaise will persist. 🌐



Ghana: Broadening horizons

A fast-growing country that can now boast premium quality oil among its many natural resources, Ghana is on investors' radar for good reason.

An English-speaking nation with a forward-looking government headed by President John Evans Atta Mills, this safe, stable, and democratic West African country has created an inviting business climate and is working hard to ensure the new wealth brought in by the energy sector helps build a sustainable economy.

Kweku Andoh Awotwi, CEO of the Volta River Authority (VRA), Ghana's electricity-generating company, explains how the transformation is affecting the country's energy industries. "All the investments from the oil and gas sector mean there is a lot of money being pumped into the economy," he says. "There are requirements for jobs, infrastructures, and services to support this brand-new industry, and of course, there has to be enough electricity to cope. Over the last five years, we have recorded a 6 percent compounded average growth in the demand for electricity. In the last two years, it was more than 10 percent, and that was recorded with a GDP growth of less than 10 percent.

"The government is really committed to 100 percent universal access to electricity by 2020—the challenges are getting a reliable network and managing a system of new investors."

Joint ventures with foreign players will be a crucial part of keeping up with demand. VRA has been enormously important to Ghana's development over the past fifty years: it built the first hydroelectric facility back in 1966, with a capacity of 580 MW—ten times more than the country needed—and provides 60 percent of the country's requirements today. Ghana is the regional leader in electricity, in terms of access and kilowatt-hours consumed by each person—something Awotwi is extremely proud of.

"VRA is a very well-run organization and already one of the biggest utility companies in sub-Saharan Africa," he says. "We are ready to compete and have had a key function in creating the requisite environment to attract independent power producers."

The dynamic CEO, who has turned the company into a profit-making entity since he took over in 2009, is excited about its achievements with renewable energies—"we produced 100 MW of wind energy in the last three months and 10 MW of solar energy more recently"—and the possibility of more collaboration with the United States. "Historically, the U.S. has been a top player in Ghana and has made the largest investments in the country. There

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is no question that it still has an important role to play in our development.”

Meanwhile, the CHADECO Group has entered into a purchase agreement with Tema Oil Refinery. Highly internationalized, the petroleum company boasts a complete industrialized chain and a marketing ability that exerts great influence in the industry.

“We have six segments: exploration and production, crude oil, fuel oil trading and trading and distribution, light oil and distribution, warehousing, and logistics and refining,” Prince Charles Dedjoe, CHADECO’s executive chairman, explains. “Our plan is to have a third key product; we want to build a storage tank of around 500,000 cubic meters and to be the biggest in Africa—we want to drill, refine, stock, distribute, and also export, but for that we need a lot of foreign investors.”

A private limited-liability company since 2001, CHADECO’s chief is looking forward to going public after the Petroleum Agreement is ratified in Parliament. “When that happens, 60 percent of the company’s shares will be available on the London and Ghana stock markets,” he says. “We want to seize and enhance our business portfolio by optimizing the industrial and profitability opportunities in the energy sector, mining sector, and plant-pooling sector to achieve synchronized growth. We want to do commercial, merchant, and investment banking to make this possible.”

During a news conference at the Great Houston Partnership in June this year, as part of a visit to promote Ghana’s new energy opportunities, Ghana’s vice president, John Dramani Mahama, said, “With this trip, we’re going to build a partnership between Ghana and Texas.” Total annual trade between Houston and Ghana jumped to \$244 million in 2010 from \$159 million in 2009.

“These kinds of partnerships are very strategic,” Dedjoe explains. “CHADECO can take advantage of that opportunity and see if other partners are willing to invest, willing to do business with us. The Ghana Investment Promotion Center Act, 1994, protects all investors and allays any frustrations and fears.

Amid the buzz around the energy sector, Minister of Finance and Economic Planning Kwabena Duffuor is keen to ensure other sectors don’t miss out on foreign investment. The cocoa industry, he points out, is still very important, and it is going to increase “massively” in the next five to ten years.

“Ghana was saved from the global economic crisis, because our two major commodities, cocoa and gold, experienced major price increases,” he says. “So while other economies were going down, ours grew by 7.3 percent. The U.S. could not find a better partner in Africa than Ghana, and we still count the U.S. as our number one partner.”

“Ghana was saved from the global crisis because cocoa and gold experienced major prices increases.”

Kwabena Duffuor, Minister of Finance and Economic Planning

Finally, the state-owned Agricultural Development Bank (ADB) is calling for medium- to long-term financing that will help it develop the infrastructure and machinery needed to grow the sector. The bank finances 35 percent of the agricultural industry and was recognized as Bank of the Year by the Africa Investor Agribusiness Awards in Durban, South Africa. Profits grew by 162.20 percent last year, assets by 36.9 percent, advances by 54 percent, and deposits by 26.1 percent.

“ADB’s strategic orientation this year is to ensure the consolidation of the gains made so far by upgrading the IT platform,” says ADB’s managing director, Stephen Kporzih. “We are also pursuing aggressive deposit mobilization and commitment to gradually increasing the share of agriculture in ADB’s credit portfolio to 40 percent during the current strategic cycle.”

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Review Essay

The Strange Triumph of Liberal Democracy

Europe's Ideological Contest

Shlomo Avineri

*Contesting Democracy: Political Ideas
in Twentieth-Century Europe.* BY
JAN-WERNER MÜLLER. Yale
University Press, 2011, 304 pp. \$45.00.

*How to Change the World: Reflections
on Marx and Marxism.* BY ERIC
HOBSBAWM. Yale University Press,
2011, 480 pp. \$35.00.

Any intelligent observer of Europe in the 1930s would have been hard-pressed not to feel that its future belonged to either communism or fascism. Liberal democracy, besieged on the left by Stalin's Soviet Union and on the right by Hitler's Germany and Mussolini's Italy, seemed to stand no chance of survival. Most central and eastern European countries had already succumbed to

authoritarianism or different variations of fascism, and the Great Depression suggested that the activist solutions implemented by both extremes were better than the feeble nostrums liberalism could offer. Back then, the notion that by the beginning of the twenty-first century, Europe would be democratic from the Tagus and the Ebro to the Danube and the Vistula would have seemed utterly ridiculous.

And in fact, liberal democracy's triumph was hardly inevitable. Two recent books, by authors with greatly differing worldviews and methodologies, try to explain why history worked out as it did. In *Contesting Democracy*, Jan-Werner Müller, a German-born, British-educated

SHLOMO AVINERI is Professor of Political Science at the Hebrew University of Jerusalem and the author of, among other books, *The Social and Political Thought of Karl Marx*. He served as Director General of Israel's Foreign Ministry in the first cabinet of Prime Minister Yitzhak Rabin.

The Strange Triumph of Liberal Democracy

political scientist who teaches at Princeton, traces the central ideological narratives of European politics during the century, arguing essentially that the postwar order emerged and has proved durable because it offered novel and satisfactory answers to major problems. In *How to Change the World*, meanwhile, the great Marxist historian Eric Hobsbawm grapples with why Marxism lost out and what it might still have to offer.

THE BATTLE FOR EUROPE

Müller's book is at once a political history of Europe since World War I, an inquiry into why Europe failed to achieve consolidated liberal democracies between the two wars yet was able to do so after 1945, and a collection of essays on some important European political thinkers. Although the volume's chapters show signs of their origin as separate articles, its overall message, complex and sometimes highly original, is clear. In a nutshell, post-1945 democratic development in Western Europe was not achieved easily, nor was it just the reestablishment of the previous political order. It grew out of the lessons learned from the brittleness of interwar democracy and the legacies of some of the nondemocratic interwar movements. It was helped, moreover, by the urgency and cohesion supplied by the broader Cold War environment.

As Müller tells it, the weakness of the post-1918 European democratic regimes derived primarily from the reordering caused by World War I. By suddenly bringing about the collapse of four empires (the Hapsburg, the German, the Russian, and the Ottoman), most of which were multiethnic, the conflict tore down a well-established conservative and hierarchical

order and replaced it with a series of weak republican regimes. Many of these regimes were based on the principle of national self-determination, but at the same time, they were burdened with serious ethnic minority problems, irredentist movements, and contested borders.

Germany's Weimar Republic, created in 1919, was the prime example of such a troubled republic, and given his German background and the country's centrality in Europe, Müller naturally devotes significant space to it. Here was a defeated country that, having lost significant territories in the west and the east, adopted an extremely liberal democratic constitution, only to have its elites—bureaucratic, military, ecclesiastical, and academic—view the republican regime as illegitimate. Müller explores Weimar Germany through the prism of the thinking of the sociologist Max Weber, showing how now canonical and seemingly timeless works, such as the essay "Politics as a Vocation," were actually produced in response to the challenges of a unique political and historical context—the legitimacy crisis facing the Weimar Republic after 1919, exacerbated by violent left-wing revolutionary attempts, such as those in Bavaria.

At the time, Germany, like several other countries, was rapidly embracing a democratic ethos, just as the Great War and its aftermath had centralized much of the economy, expanded voting rights, and fostered Wilsonian ideas of national self-determination. It should have been no surprise that the newly established democracies would have so much difficulty juggling these contradictory realities and principles. Müller explains how under such conditions, ideologies—especially

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redemptive and totalistic ones, such as fascism and communism—could for the first time transcend merely intellectual discourse and capture the imagination of the masses, who thought the formalistic democratic structures failed to respond to their needs and aspirations.

In contrast to his respectful treatment of Weber's measured attempt to combine order, legitimacy, and representation in his theory of a modern nation-state, Müller offers a not very complimentary, but fascinating, characterization of the Hungarian philosopher György Lukács. Müller credits Lukács with an insightful and sophisticated reading of Karl Marx, which made him the preeminent Marxist philosopher of the interwar period, but also exposes his political immaturity during Hungary's 1919 communist revolution, his opportunistic turnarounds during the Stalinist period, and his final turn as a role model for the New Left in the 1960s. Müller also describes him as one of "many scions of highly assimilated Jewish businessmen . . . [who] became part of a free-floating, self-radicalizing intelligentsia moving around Europe on generous allowances (from their usually despairing fathers)." This may not be entirely wrong, yet such a stereotyping of the social origins of revolutionary intellectuals echoes, in gentler terms, what many right-wing anti-Semites were shouting from the rooftops at the time: that it was rich Jewish intellectuals, cosmopolitan and deracinated, who were undermining Europe's social order.

In his account of fascism, Müller rightly underlines the enormous impact that the philosopher Georges Sorel's ideas had on Mussolini and the French radical right, especially his concept that mass

political action depended on a "social myth." As the historian Zeev Sternhell has shown, nationalist myths gave content and motivation to the deracinated masses, who felt alienated from the formal institutional structures of modern democracies. This popular foundation distinguished fascist mythmaking from elitist traditionalist conservatism, something many liberals and Marxists failed to see. Far from being agents of the conservative, bourgeois order, fascism and Nazism were revolutionary and supremely modern movements. Much of their appeal lay in their claim to be more democratic than the democracies.

After World War II put an end to fascism, Müller argues, Western Europe set about the task of political reconstruction. Political leaders understood that they had to do more than simply revive the interwar order, which had failed so miserably. So instead they crafted what he calls "constrained democracy," a system that took the formal institutions of parliamentarianism, universal suffrage, and multiple political parties and added a number of constraints. Trade unions negotiated directly with the state, which recognized them as legitimate constitutive elements of the political system (and not just as partisan representatives of socialist parties), allowing employers, employees, and the government to haggle over salaries and wages. Unelected constitutional courts acted as an elitist brake on the majoritarian *vox populi*, protecting human rights from unbridled populism. Last but not least, these constrained democracies adopted a modified Keynesian approach to state intervention in the economy, which added an element of security to the political structure—

something that Europe had lacked before 1939.

In this context, Müller helps readers understand postwar Europe by highlighting the enormous contribution made by Christian Democrats. Italy's Alcide De Gasperi, Germany's Konrad Adenauer, and France's Robert Schuman transformed their parties from enemies of democracy into crucial pillars of it. Before 1939, many Christian parties had allied themselves with antidemocratic forces, and only the horrors of World War II and the Holocaust convinced them that such complicity with fascism ran contrary to their religious principles. Here, the writings of the French Catholic philosopher Jacques Maritain were crucial in reorienting Christian parties toward democratic liberalism. By joining with liberal and social democratic parties to embrace and even help lead the new order, Christian Democrats gave the system the sort of cross-class support of broad public majorities that the interwar republics had never had.

MARXISM'S TURN

One of the most surprising twists in Europe's political evolution is the reversal of fortunes that has befallen Marxism, a school of thought that once seemed a formidable ideological contender. Hobsbawm's latest book, *How to Change the World*, chronicles its influence over the twentieth century and tries to make a case for its contemporary relevance. Hobsbawm is one of the giants of the historical profession and the author of an impressive list of magisterial studies. Even those who disagree with his Marxist outlook know that his sophisticated use of Marxist theory has greatly enriched

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the study of industrialization, the modern working class, various revolutionary movements, and the emergence of empire. No doubt his cosmopolitan background—from Alexandria through Vienna and Berlin to London—underpinned by his breadth of knowledge, generosity of spirit, and mastery of languages and topics, has helped him avoid the narrow and doctrinaire approach so common among lesser Marxist historians.

Yet as in the case of Goethe's *Faust*, there are, alas, two souls dwelling in his breast. There is Dr. Hobsbawm, the towering historian, using the tools of the Marxist tradition to explore history, and there is Comrade Eric, the revolutionary, who, despite distancing himself from debilitating party orthodoxies, is still captive to ideology. *How to Change the World*, which includes more than a dozen essays written between 1956 and 2009, some published here for the first time in English, brings out this duality. Although the volume's title is slightly misleading—this is not a compendium for revolutionary praxis—the book is one of the best accounts showing how Marx's thought did in fact change the world.

Hobsbawm traces Marx's influence on everything from politics to art in several countries from the late nineteenth century to the present. He shows how, despite Marxism's aversion to nationalism, Marxist analysis helped develop and sustain nationalist movements among some oppressed peoples. And his chapter on Antonio Gramsci will make this influential Italian Marxist thinker seem less esoteric and enigmatic to the English reading public.

Of greatest contemporary interest is the opening essay, "Marx Today," in

which Hobsbawm brings his acute mind to bear on the post-Cold War era. He claims that the demise of Soviet-style Marxism has paradoxically made the study of Marx more relevant, liberating Marxism from the straitjacket imposed on it by its status as the official ideology of a repressive regime. Yet he also concedes that Marx's vision of the proletariat "expropriating the expropriators" is irrelevant today (although he contends that Marx's understanding of the dynamism of capitalist society is helpful in addressing capitalism's crises, such as the current global economic recession). Hobsbawm is determined not just to salvage Marx from the detritus of the Soviet catastrophe but also to help him regain his place in the pantheon of modern thinkers able to develop comprehensive and adaptive understandings of human affairs. Perhaps because he does not want to sound doctrinaire or old-fashioned, Hobsbawm refrains from calling this unique quality of Marx's thought "dialectical," but this is precisely its chief characteristic.

Still, as masterful as his analyses are, Hobsbawm remains unwilling to address certain problematic facts. Take ethnicity. Given his Jewish background, Hobsbawm is rightly sensitive to the role of Jewish intellectuals in various Marxist movements, focusing in particular on those in Germany and Austria-Hungary. He tersely castigates most non-Jewish intellectuals in Germany after unification, in 1871, for being "profoundly committed to the Wilhelmine Empire." This allegiance left the German social democratic movement bereft of intellectual leadership and thus thrust such Jews as Eduard Bernstein, Karl Kautsky, and Rosa Luxemburg into

The Strange Triumph of Liberal Democracy

leadership positions. Similarly, the emergence of various nationalist movements within the Austro-Hungarian Empire in the late nineteenth century drove many Jewish intellectuals to socialism or Zionism, the only places where they could feel at home.

Hobsbawm describes all this with acuity but does not really grapple with the problem it poses for his broader framework. According to Marxist theory, class background should determine where people end up politically. But it was the Jewish background of these activists, not their identity as bourgeois intellectuals, that brought them to the shores of Marxism. This suggests that all history is not class history (as Marx would have had it), that national, ethnic, and religious affiliations matter, too. But if Hobsbawm admitted that, he would have to reject a major facet of theoretical Marxism, something he is unwilling to do.

A more serious omission concerns the Soviet elephant in the room. Hobsbawm's 2002 autobiography dealt with his changing attitudes toward the Soviet Union over the years, and in many cases, he acknowledged the inner tensions of his relationship to the Soviet experience and the havoc that experience created among Western Communists. But he shied away from grappling with the fundamental question: Did Russia's 1917 Leninist coup lead inexorably to Soviet tyranny, and was the attempt to force a socialist vision on a preindustrial society doomed from the very beginning? Readers will not find a definitive answer to this question in any of Hobsbawm's past work, nor in this volume, either.

This elephant casts other shadows. Hobsbawm discusses Marxist intellectuals

in the 1930s without mentioning their reactions to the 1939 Molotov-Ribbentrop Pact, between the Soviet Union and Nazi Germany. In his autobiography, Hobsbawm came to terms with the fact that he himself justified the pact at the time, with the usual language then prevalent among Communists. But he does not mention the pact here, and ignoring such an episode in a historical account of Marxism in the 1930s is simply inexcusable.

On a certain level, one can commiserate with Hobsbawm, a prominent member of the mainly (although of course not exclusively) Jewish interwar intelligentsia that believed in the redemptive vision of Marxism. The Soviet Union became a beacon of hope for this group after the slaughters of World War I and the collapse of European democracies and economies in the 1920s and 1930s. The tendency to close one's eyes at first to blemishes in the Soviet system was understandable. But this pose became an intellectual and moral prison when what initially could have been viewed as childhood illnesses of the revolution transmogrified into the hideous crimes of Stalinism. Some had the courage to liberate themselves; others clung to their hopes even as darkness descended at noon.

Hobsbawm tried to maintain both his integrity as a historian and his beliefs. He should be thanked for the historical gifts he has bestowed on his readers. But at the end of the day, he never adequately addresses the fact that Marxism failed utterly as a revolutionary movement, not once but three times—in the West, where no proletarian revolution occurred; in the East, where what was supposed to be an emancipatory redemption ended up as a hellish nightmare;

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and in the developing world, where communist regimes brought misery wherever they gained power.

THE CRISIS THIS TIME

The recent global financial crisis has once again shaken people's faith in the ability of capitalism to provide a sustainable flow of broad-based economic benefits to the public at large. It serves as a reminder of the fragility of the post-World War II order Müller describes. Recent demonstrations in Europe and the United States, meanwhile, attest to the failures of democratic governments to respond adequately to the crisis or satisfy public demands for action. Müller is aware that the hard-won postwar equilibrium should not be taken for granted, and he holds up the crisis of 1968 as an indication of its brittleness.

Today's economic crisis is also a reminder of the contemporary relevance of the issues that Marx and his disciples, including Hobsbawm, have agonized over. Dialectically (if one is still allowed to use the term), Hobsbawm's suggestions for how elements of Marxist thinking can inform solutions to the crisis might still rescue the approach from total relegation to the dustbin of history. As the crisis has made clear, market fundamentalism, radical privatization, and a universal fear of state power are overly simplistic answers to the question of how to sustain a modern, globalized economic order. One way of looking at Marx, after all, has always been to see him in the context of the Enlightenment project and the German tradition of *Bildung*, as a thinker who, when faced with the horrors of early industrial capitalism, tried to bring about a world of

universal justice, solidarity, fairness, and humanity. In his own way, Hobsbawm continues to speak to that dream.

The two books are helpful in unsettling the ideological complacency of contemporary neoliberalism, which helped pave the way for the crisis even as it never imagined such a thing could happen. As both Müller and Hobsbawm show, the triumph of liberal democracy was made up of many ingredients, and neglecting any one of them is an invitation to trouble. 🌐

The Changing Face of International Affairs Education

“International affairs” has traditionally carried the connotation of diplomacy, national security, and state-to-state engagement. The multidisciplinary international affairs degree first appeared after World War I, but it really came into its own in response to World War II.

Leaders in the public and private spheres in the United States recognized the need to educate more Americans about the world around them, prepare them for America’s new leadership role in the world, and successfully “fight” the Cold War. The fall of the Soviet Union, coupled with the technological revolution, has allowed for a rapid globalization of, well, everything. As a result, multidisciplinary programs in international affairs have exploded since 1989, and the difficult task has become to define the study of international affairs when today every discipline seems to have an international dimension.

As I reflect on the growth and future of this type of degree, I find myself going back to the traditional ideas of diplomacy and translation—not translation of language to allow for dialogue, but translation of ideas and needs across disciplines to allow for greater collaboration in

tackling the world’s most pressing problems. At its core, despite all the changes, international affairs programs are still training “diplomats” and “translators”—professionals with broad knowledge of the world who see and can navigate the interconnectedness of the private, public, and NGO sectors. Today, international affairs schools must train their students to understand a far more complicated world—one in which we cannot shy away from studying the roles of science and technology, the global economy, or the role of governments’ policies to improve or hinder the environments in which we operate.

Leigh Morris Sloane

Association of Professional Schools of International Affairs (APSIA)

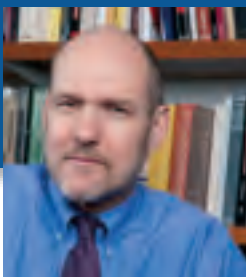
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A CONVERSATION WITH



Stephen Walt

Robert and Renée Belfer Professor of International Affairs
Harvard Kennedy School

Harvard Kennedy School has put the G in International Affairs: International & GLOBAL Affairs

How does the Harvard Kennedy School approach the teaching of international affairs?

The Harvard Kennedy School teaches students how to understand complex policy environments and to operate effectively within them. World politics today isn't just what national leaders say or do to one another: it's a more complicated interplay between governments, institutions, markets, NGOs, technology and the natural environment.

We created a new concentration in International and Global Affairs (IGA) to help our students make sense of this increasingly complex world, and we continue to revise our course offerings to reflect an ever-changing agenda of global problems.

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What are the School's unique strengths in this area? Why should an ambitious student choose Harvard?

For starters, we offer an unmatched combination of academic excellence and real-world experience. Three IGA faculty members were ranked among the "twenty most influential scholars" in a recent survey of the field, yet our faculty also features accomplished practitioners such as former Undersecretary of State Nicholas Burns and NSC staffer

Meghan O'Sullivan. Colleagues such as Graham Allison, Joseph Nye and John Ruggie have made seminal academic contributions and have extensive policy experience as well. And that's just scratching the surface.

The extraordinary students who show up each year are another strength. Today, roughly forty-five percent of our students hail from overseas, which enables them to learn how the world looks from different vantage points and to build professional contacts that cross national boundaries.

Finally, the Kennedy School is Harvard's window to the world. Prominent policymakers, journalists and academic experts visit every week, allowing our students to get "up close and personal" with the world leaders whose shoes they are going to fill.

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A CONVERSATION WITH



Dr. Gerhard Loibl

Professor, LL.B., one of the two Academic Directors of the ETIA program
Diplomatic Academy of Vienna
Vienna School of International Studies

Think Global, Act Global: International Environmental Management 20 Years after the RIO Earth Summit

Environmental problems and challenges do not stop at geographical and political borders, and they cannot be solved and managed in a single approach. In view of our complex world, interdisciplinarity is imperative for tackling global environmental phenomena.

The Master of Science Programme “Environmental Technology and International Affairs” (ETIA)—created in 2007 by the Diplomatic Academy of Vienna (the Vienna School of International Studies) and the Vienna University of Technology as one of the very first programs of its kind—offers a unique opportunity to learn about environmental decision-making from both the political and technological sides. The program is run by two Academic Directors: Professor Dr. Gerhard Loibl, representing the Diplomatic Academy of Vienna (the Vienna School of International Studies), and Professor Dr. Hans Puxbaum, representing the Vienna University of Technology. This pairing reflects the essential idea of ETIA—not merely bringing together two fundamentally different academic disciplines and approaches, but also creating a unique interdisciplinary program reflecting our need for a new kind of leader.

What made the Diplomatic Academy of Vienna and the Vienna University of Technology create an innovative program like the MSc in Environmental Technology and International Affairs?

With the RIO summit in 1992, it became clear that environmental challenges have taken on a new urgency on the local, regional, and global levels. This puts increasing demands on decision-makers, who require a broad knowledge and understanding of the political, legal, economic, and technical issues involved.

What is so unique about ETIA?

Studying environmental issues both from the technical and the international relations points of view mirrors the ambitious goal—achieving sustainable development—that the international community has set for itself. ETIA is one of the first programs to educate students to become decision-makers with a profound understanding of the legal, economic, and technical issues. This view is shared by the sponsors of the program. The Honorable Professor Dr. Christoph Scharff, CEO of ARA Altstoff Recycling Austria AG and sponsor of ETIA, sees ETIA as a unique opportunity to educate future leaders. For him, environmental protection and resource management are cross-cutting issues that require new expertise, and ETIA is the ideal program to train the experts needed in the industry: highly qualified, competent, and responsible decision-makers who will tackle the technical, economic, legal, and political challenges we are facing today.

How does the ETIA programme effectively prepare students for a career?

ETIA offers students a structured multi- and interdisciplinary approach that teaches them the academic and practical knowledge necessary to pursue a career in the area of environmental protection and sustainable development. ETIA students come from all kinds of disciplines. Ira Stanic-Maruna, graduate of the first ETIA promotion, in 2009, works as an environmental consultant. The ETIA program helped her achieve her long-standing aspiration to work in the environmental sector, even though her background was a completely different one—translation studies. By gaining knowledge in the field of environmental technology she learned to speak the “language” of natural scientists and engineers. This enabled her to get her present job as an environmental consultant at VERBUND, Austria’s leading electricity company.



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Bund der Höheren Schulen Österreichs & Europas

Vienna School of International Studies
Diplomatic Academy of Vienna
www.da-vienna.ac.at
info@da-vienna.ac.at
+43 1.505.72.72 x120

A CONVERSATION WITH



Rachel Kyte

The World Bank, VP and Head of Network, Sustainable Development

The Fletcher School at Tufts University

Global Master of Arts Program (GMAP), Class of 2002

Preparing a Leader for How the World Really Works

Since 1933, The Fletcher School has prepared the world's leaders to become innovative problem-solvers in government, business, and nongovernmental organizations. From the reconstruction of postconflict societies and the creation of markets in emerging economies to the analysis of terrorist threats and the promotion of human rights, today's issues transcend borders and disciplines. Fletcher's interdisciplinary approach allows students to develop unique curricula across multiple areas of concentration, tailored to their professional interests. The Fletcher School is continually at the forefront of educating for the changing global landscape; its Master of International Business (MIB) and Master of Laws in International Law (LLM) programs, in addition to traditional international affairs degree programs (MA, MALD, and PhD), are examples of that.

How did attending The Fletcher School prepare you to take on the complex challenges you face in your position at The World Bank?

A critical challenge I face at The World Bank Group is how to help our clients build sustainable lives and communities in the midst of a pace of change unprecedented in history. At Fletcher, I learned that a collaborative, cross-disciplinary approach is a must for achieving solutions to today's complex global challenges. It is not enough to examine an issue simply from a financial or political perspective. I needed to have a thorough grounding in politics, economics, business, and legal matters and then translate that into practical action engaging the public, private, and nongovernmental sectors. I am continually reminded through my work at The World Bank Group that I am living out what my classmates and I explored at Fletcher.

Why did you choose to attend The Fletcher School's Global Master of Arts Program (GMAP)?

I wanted to obtain my master's degree while pursuing my career with The World Bank Group, and I knew I didn't want an MBA or a traditional international relations degree. When I researched GMAP, it spoke to me in terms of the challenges I was facing in my job at that time. I could see that it would provide me with the interdisciplinary coursework I needed to advance to the next step in my career, and the program's hybrid Internet-mediated/residency program was appealing.

Local has become global and global has become local; team projects completed with my classmates while we were spread out geographically and across time zones were a harbinger of the way I work now. Through Fletcher, I learned the basic skills I needed for building coalition and consensus in today's technology-driven world.

What has been the most surprising outcome of your Fletcher School experience?

When I think of my time at Fletcher, I think of what I learned, the quality of the faculty, my impressive classmates. But what surprises me most about my experience at Fletcher are the extraordinary friendships I made during that time. It's rare and unusual to establish such close friendships at midlife and with people from such diverse backgrounds. My classmates were representative of the world; they were entrepreneurs, bankers, businesspeople, diplomats, and individuals working in public and private organizations. The friendships we made continue today and they remind me of how my experience at Fletcher shaped and changed me for the better.



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fletcher.tufts.edu

fletcheradmissions@tufts.edu

617.627.3040



Dorothy Bassett, PhD

Dean of the School of Leadership and Professional Advancement
Duquesne University

Preparing Global Leaders

Your graduate program is online. How do the students interact with one another and with the professor?

Many of our students are professionals juggling work and family in addition to their studies, so we place a strong emphasis on the use of asynchronous tools. Our students interact with one another and with their professors through the course website as well as through other tools such as Skype, Facebook, email, and chat.

Our program director, David McGeehan, works closely with our faculty and frequently integrates guest speakers from other countries in the courses to provide students with a deeper understanding of the subject matter as it is experienced by their counterparts abroad. Additionally, one of our core faculty members recently spent four months in Africa and gathered videos, photos, and audio recordings. Much of this on-the-ground content will be used in the next course offering.

Who are your students?

Our students are primarily professionals who come from a variety of government, corporate, and nonprofit organizations throughout the United States and abroad. Some want to deepen their knowledge for their current international positions, while others are interested in obtaining the degree to advance their careers or position themselves for new professional opportunities. The program is particularly popular with some military service members, as their frequent overseas deployments have led them to recognize the value of a degree that focuses on international leadership.

Our current student cohort includes individuals working in the fields of health care, international sports, finance, government, and education. Many of our students value not only learning from the faculty, but also the opportunity to network with their fellow students and to learn from their experiences.

One emphasis of your curriculum is “international leadership skills.” Why did you place such an emphasis on that?

Many individuals who are promoted to leadership positions in international or global organizations or departments tend to possess strong technical knowledge (e.g., knowledge of IT, agriculture, or engineering), but do not have the necessary skills to be effective leaders even in their home countries. When an international layer is added, their likelihood of effectiveness as leaders of global operations is greatly diminished.

The curriculum is designed to develop students’ leadership skills, sense of “global-mindedness,” and capacity for intellectual humility, integrity, and empathy, enabling them to adjust their leadership and operational approaches in order to be more successful.

You offer a course called “Leading International Teams.” Why do you think this topic is essential to the curriculum?

Given the increasing globalization of our work world, it is not at all uncommon for leaders to be called upon to work with individuals from other nations on short- or long-term projects, whether that means heading up a group of international employees in a face-to-face setting or coordinating the efforts of a virtual team and leveraging technology to bring together individuals from around the globe as they work on a common initiative. The ability to effectively lead such teams and to draw upon and benefit from the strengths, abilities, and cultural viewpoints that each individual offers is a critical skill for leaders of all organizations today.



www.duq.edu/global
leadership@duq.edu
800.283.3853

A CONVERSATION WITH



David J. Jhirad

Director of the Energy, Resources and Environment Program and HRH Prince Sultan bin Abdul Aziz Professor of Environmental Policy
The Johns Hopkins University, Paul H. Nitze School of
Advanced International Studies (SAIS)

Problem-Solving in the Era of Globalization

With campuses in Washington, DC, Bologna, Italy, and Nanjing, China, SAIS is the only international relations graduate school of its kind. Students have the unique advantage of experiencing our three strategically located centers.

SAIS graduates are recognized for their abilities in economics, diplomacy, and languages—an excellent foundation for engagement in the international domain, whether in the public, private, or nonprofit sector.

For seven decades, SAIS has attracted the best and brightest applicants, eager to learn from our superb faculty and to prepare for a leadership role in solving complex global problems.

How do you capture the interconnections among energy, environment, water, climate change, and agriculture in teaching students from diverse academic and professional backgrounds?

SAIS's Energy, Resources and Environment (ERE) Program aspires to educate “specialized integrators” to lead the institutions that will shape the twenty-first century's energy and environmental future. The Fundamentals of Energy and Environment course and electives prepare students to implement secure and resilient solutions, drawing on innovations in policy, technology, governance, and finance.

Our program focuses on the critical challenges of stabilizing greenhouse gas emissions, reducing the risk of oil disruption and nuclear weapons proliferation, eliminating energy poverty for 3 billion people, reversing the deterioration of the world's ecosystems and mobilizing \$22 trillion in capital investment for energy infrastructure by 2030. With rising food prices, extreme weather, and global hunger in world news headlines, SAIS has designated 2011–2012 the “Year of Agriculture”—prompting us to add feeding a world population of 9 billion by 2050 to the issues we are exploring. Understanding the energy/water/food nexus is pivotal in finding sustainable solutions to these challenges.

One of your own research projects uses the communications revolution as a springboard for a clean-energy revolution. How are your students supporting this groundbreaking work?

ERE is a global knowledge hub for a Rockefeller Foundation initiative, “Smart Power for Environmentally-sound Economic Development” (SPEED). Our goal: to bring clean, affordable, and reliable power to 1.4 billion rural people. We are encouraging cell tower owners in developing countries to use electricity from renewable sources, rather than costly diesel, and we envision the towers becoming “anchor customers” for mini-utilities that provide electricity to both the towers and surrounding villages. ERE will lead the analysis of lessons learned from pilot projects in India and apply them to a global rollout of the SPEED approach. Research assistantships are provided to students throughout the academic year and over the summer.

How does ERE's International Energy and Environmental Practicum prepare graduates to bridge the worlds of theory and practice—a hallmark of the SAIS degree?

The course combines theory with action to construct solutions to global energy and environmental concerns. Consulting for a client organization, students conduct a research project from conceptualization through the final presentation, in the process developing problem-solving, team-building, and leadership skills.

Currently, one team is investigating black-carbon emissions from brick kilns in India, looking at barriers facing firms entering this market and identifying emission-reducing technologies and measures. Students will travel to India to test their hypotheses. Another team is examining the causes of degraded land in Brazil and, through field research and international best practices, will recommend incentives for forest restoration.



The Johns Hopkins University
The Paul H. Nitze School
of Advanced International Studies
www.sais-jhu.edu/problemsolvers
admissions.sais@jhu.edu
202.663.5700

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A CONVERSATION WITH



Roger Vickerman

Dean and Professor of European Economics
Brussels School of International Studies
University of Kent

Study with Academics, Practitioners, and Policymakers

How is the Brussels School preparing its students for the challenges of an increasingly globalized world?

As one of the few wholly interdisciplinary postgraduate schools of international studies in the world, and being based in a global capital, we are excellently placed to offer twelve-month programs that will enable students to deal with the challenges of an increasingly complex society. Our lecturers include both academics and practitioners. Most have either worked or are currently working in the EU institutions, NATO, or one of the many companies or organizations that are clustered around them. Their research, knowledge, and experience allow us to develop our portfolio of programs to meet the needs of both our students and their potential employers. In consultation with our alumni, we have recently extended our portfolio to include such subjects as development, migration, energy security, and transitional justice. These areas are highly topical and provide our graduates with the tools they need to excel in today's workplace.

Could you provide us with some examples?

All of our programs are built on an interdisciplinary framework, allowing students to tailor them to suit their own career plans, interests, and backgrounds. For instance, our MA in International Development offers courses on the politics of development, project appraisal, and development economics, as well as the law of development. The interaction of these disciplines, along with the different approaches of the academics, practitioners, and policymakers who teach the program, enables our students to discover all aspects of a

particular subject. In a similar vein, our MA in International Migration examines international and European migration law as well as trafficking, the humanitarian aspects and theories of migration, and the issues surrounding identity and belonging.

I assume Brussels offers some excellent internship opportunities. Are you able to help with this?

Absolutely. We have developed a network of business contacts with the EU institutions, lobbying firms, NATO, NGOs, and think tanks in Brussels, and these help students secure internships that allow them to gain practical experience in the subject they are studying and enhance their CV. We also have our own dedicated careers advisor.

Do you have exchanges with other institutions?

Being based in the capital of Europe, we have developed partnerships with universities in the other global capitals so that our students can learn about international affairs at specialist campuses located next to globally significant policy- and decision-making institutions. At present we are working with the China Foreign Affairs University in Beijing and Virginia Tech and George Mason University in the Washington, DC, area to establish double-award "two capitals" programs in which, through two years of study, students can obtain both a Kent master's and a master's from the partner institution. For someone hoping to gain understanding about a future complex world, this program seems an obvious choice. We are currently exploring other links in Brazil, Russia, and Japan.



www.kent.ac.uk/brussels
bsis@kent.ac.uk
 +32 2.641.1721
 Skype: bsisbrussels

A CONVERSATION WITH



Alain Lempereur

Alan B. Slifka Professor and Director of the graduate program in Coexistence and Conflict
The Heller School for Social Policy and Management
Brandeis University

There Can Be No Development without Peace

As the Alan B. Slifka Chair of the graduate programs in coexistence and conflict, how do you define your mission?

There are still too many violent conflicts in the world. Our humanity cannot accept this indignity. Our responsibility is to bring lasting peace in conflict-affected areas, but how? We need a new generation of professionals who can leverage the strategies and skills that have proven effective. In a nutshell, peace-leading is the mission of our school. Our programs aim to wage peace globally and locally, by preparing peacemakers to prevent, manage, and resolve conflicts. Our students and our alumni become agents of change, from conflict to coexistence.

How do you see your role as a professor at the Heller School for Social Policy and Management?

Every faculty member at the Heller School is a bridge-maker between theory and practice. We go to the field not simply to study it, but to advance the cause of social justice. Personally, on the theoretical side, I have developed worldwide programs in research and education to further responsible leadership. On the practical side, I have been involved as a mediator, locally in Burundi and the Congo, and globally as facilitator of the International Dialogue on Peacebuilding and Statebuilding.

How do you build peace?

Peacebuilding involves transforming a conflict-affected society and achieving peaceful coexistence. We start with the social reality, then we analyze it, extract the best practices, and learn from failure. We then bring these experiential theories to our students, who return as reflective practitioners to the field. In this way, more finely tuned practices emerge, which in turn further a more sustainable peace.

What will a student learn from your programs?

Our students, who are 80 percent international, spend one year in residence at Heller. They study with experts in the fields of conflict strategies, dialogue and mediation processes, civil society movements, race relations, international politics, human rights, and ethnic conflict. Students then spend three months in the field, in governmental, intergovernmental, and nongovernmental organizations. This fieldwork is more than an internship; it links theory and practice. Students enter an organization, audit their courses of action, and assess the results. Our future graduates' observations help conflict practitioners and then bring stronger, more informed skills and strategies back to the Heller community, through their field thesis and the capstone.

What about the dual degree with the program in sustainable international development?

There is no development without peace, and no peace without development. That is why Heller offers the unique option of a dual master's degree with the program in sustainable international development. Through an additional year in residence, students develop the skills necessary to undertake and engage in development and aid work under conditions involving violent conflict.

Where do the alumni of your programs work?

Our graduates work with organizations as diverse as the UN High Commission for Refugees in Kosovo; the UN Peacekeeping Mission in Sudan; the UNDP Crisis Prevention and Recovery Program, USAID Democracy and Governance Program in Southern Sudan; the National Unity and Reconciliation Commission (NURC) in Rwanda; the EastWest Institute for Stability and Development in Serbia; and the Eurasia Foundation of Central Asia in Tajikistan.

The Heller School
for Social Policy and Management

Brandeis University
www.Brandeis.edu/Heller/
HellerAdmissions@Brandeis.edu
781.736.3820



Sean Jacobs

Assistant Professor, Chair of the Media and Culture Concentration
Graduate Program in International Affairs
The New School for Public Engagement

Media and Education for Global Change

Your program is celebrating its tenth anniversary. Hasn't the media landscape shifted radically during the past decade?

It's a totally different environment. On 9/11, if you wanted information, you stayed by your television. Now there's Twitter, Facebook, and mobile technology. The technology is cheaper and easier to use—it's more democratic. Media outlets are cutting foreign correspondents and "news" is about entertainment, but our program is about empowering students to use media to address serious global issues.

Has the curriculum changed to reflect the new media paradigm?

Our director, Michael Cohen, stresses the importance of mixing theory and practice. It's my job to make that real for students.

We introduced a documentary video course that takes students from conceptualization through distribution; we're starting a new course on social media; and we're introducing students to resources like Ushahidi, an open-source software first used in Kenya to track emergencies like earthquakes and political violence.

One of our students wanted to apply new media techniques as a journalist in his native Spain. Because we're in New York City, he got a great internship with a documentary production company. The technical and storytelling skills we teach are transferable when students go on to work at the UN, Human Rights Watch, MSNBC, etc.

Classes we've taught for years, such as photography and human rights, propaganda and media, and Hollywood and the world, continue to be relevant.

What place does culture have in international affairs?

Politics isn't just about diplomats, conferences, and summits. As Joseph Nye wrote, it's very much about "soft power." I teach a course called Global Soccer, Global Politics. Soccer is a way to understand the world. Egypt recently hired the former U.S. national team coach for its national team. No Arab country had ever hired an American coach. Would that have happened before Barack Obama introduced a new outlook in U.S. foreign policy? That's the kind of thing we should consider.

Your students come from all over the world. Do they bring different perspectives to the classroom?

Absolutely. And I bring my own. I was born in South Africa and grew up under a racial dictatorship. I lived through the transition from state censorship to new media and cell phones. I bring that into class. I insist that students take a global perspective. In our International Field Program, they develop that perspective in collaborations with partners around the world.

Our program is part of the Milano School of International Affairs, Management, and Urban Policy. In addition to their core courses, our students can take classes in other New School graduate programs, which can range from nonprofit management to sound production to sociology.

We know we don't have all the answers, but we can find solutions if we work in teams with different people with different skills. That's what I like about this place. We don't believe in prefab solutions. We allow for experimentation and heterogeneous ways of thinking and responding.

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A CONVERSATION WITH



Minoru Masuda

Associate Dean and Professor
Ritsumeikan University
Graduate School of International Relations

Past and Present, Theory and Practice: Aiming for Interdisciplinarity in the Study of International Relations

How do you approach international relations as an interdisciplinary field of study at the Graduate School of International Relations of Ritsumeikan University?

In our English-based Global Cooperation Program (GCP), we aim to introduce students to the field of international studies by providing a multilevel interdisciplinary approach.

The world that we experience today has been shaped by our past experiences. In order to understand today's problems, we need to understand the past, and, equally, in order to understand the past, we need to comprehend the present. By applying both historical and contemporary approaches to the problems of international society, we can achieve one level of interdisciplinarity.

A second level requires combining theoretical and practical approaches. We face a number of problems in today's international system; some of us may want to find immediate practical solutions to those problems, while others will pause first to think about the problems' theoretical background. Neither of these approaches works if tackled separately. Theory and practice must go hand in hand if you wish to adopt an interdisciplinary approach.

Here at GSIR Ritsumeikan, faculty is trained in all the above fields. To expand students' perspectives, courses on the history of global society approached from political, sociological, and cultural viewpoints are combined with courses on various areas of contemporary global society. Courses on the theories of international relations and international economy can enhance what is learned in courses on practical aspects in international relations.

In what ways can your research activities help develop students' academic interests?

I currently study and teach the history of European integration, from both short- and long-term perspectives, as well as its implications on the future of regional cooperation in East Asia. By combining the short-term and long-term historical approaches and comparing European experiences with Asian experiences, I am aiming to achieve some level of interdisciplinarity within the genre of international history.

Seen from the short term, the process of European integration began as a central part of the Cold War's development in the region, while from the long-term perspective, it is important to view an integrated Europe as a product of nation-building in modern Europe. This process, in itself, is an interesting research topic, but it also has deep implications for East Asian regional relations.

It is helpful for those students who are interested in the subject of East Asian or trans-Pacific regional integration to learn more about the process of European integration and its political background. For example, one of my MA students in the GCP course is from Canada, and his dissertation is about the future of European integration in terms of geographical expansion. He has learned a lot from comparing the recent and long-term pasts of Europe and Asia while ironing out his thesis. I really enjoyed supervising his dissertation and I believe he has enjoyed the process as well.

I look forward to meeting other students like him in the future at the Graduate School of International Relations at Ritsumeikan University.



Ritsumeikan University
Graduate School of
International Relations

www.ritsumei.ac.jp/acd/gr/gsir/eng/ir-adm@st.ritsumei.ac.jp
(+81) 75.465.1211



Mary Zweifel

Director of Administration
Master of Arts in International Studies (MAIS) Program
University of San Francisco

Establishing a Global Community

Many say the world is getting smaller. Through my work with the Master of Arts in International Studies (MAIS) Program at the University of San Francisco, I see that it is, in fact, expanding. Our potential for collaboration grows exponentially as we become increasingly more interconnected. Drawn by a deep, immutable desire to positively impact the world, the MAIS student body joins us from all corners. From the Congo to Egypt to Norway to Thailand to Venezuela, students bring their valuable and varied experiences and perspectives into our classrooms to learn how to create a more humane and just future.

How does the MAIS curriculum challenge students to generate solutions to global issues and problems?

As an interdisciplinary program, the MAIS curriculum draws on anthropology, economics, history, law, political science, sociology, and other fields to examine topics such as the political and economic aspects of globalization, human rights, peace and conflict, development and the environment, and international law and organizations. Students gain skills in conflict resolution, legal advocacy, policymaking, and strategies for real economic development. It is the synthesis of theories and approaches that creates space for innovation in MAIS.

Our faculty come from various departments, professional involvements, and geographic origins, and their expertise enables our delivery of a rigorous 28-unit curriculum. Faculty serve as individual advisors during the capstone of the program, in which students produce a thesis or research project. Through this collaboration, students refine a topic, develop an argument, conduct research, and compose a compelling analysis of issues ranging from corporate social responsibility to the impact of economic deregulation on food consumption in Mexico to teenage pregnancy in Sierra Leone to the question of U.S. diplomacy in Afghanistan.

Do students have the opportunity to learn about issues firsthand?

Yes! Many students conduct research domestically and abroad, and all of our students are required to complete an internship with an organization in a related field. Through this component of the program, theory attained in coursework is applied to practical professional experience. Our annual Internship Forum is one of my favorite events of the year. Students share challenges, breakthroughs, and ultimately the ways in which knowledge acquired will shape their careers. One student reflected, "I gained practical experience in a professional research environment...and implement[ed] a plan of completion based on various brainstorming sessions with members of the Brookings Institute, the World Bank, the Government of India, and top private city planners and researchers. This experience is essential to my own goals of implementing proper mechanisms to relieve rapidly growing cities of the inevitable cycle of informal settlements."

How do alumni translate their MAIS experience to life after USF?

Internship connections and faculty relationships are complemented by the creation of lasting colleagues. The cohort model fosters dialogue that develops in seminars and continues throughout graduate school. MAIS alumni carry these networks into their professional lives, securing employment in international development organizations, global human rights groups, consulting firms, global health organizations, and venture capital groups aimed at poverty alleviation. Embodying the mission of San Francisco's oldest university, MAIS graduates are equipped with the tools to establish an inclusive global community.



www.usfca.edu/mais
mais@usfca.edu
415.422.5541

Directory

Brandeis University

The Heller School for Social Policy and Management

www.Brandeis.edu/Heller/
HellerAdmissions@Brandeis.edu
781.736.3820

Diplomatic Academy of Vienna

Vienna School of International Studies

www.da-vienna.ac.at
info@da-vienna.ac.at
+43 1 .505.72.72 x120

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Graduate Program in Global Leadership

www.duq.edu/global
leadership@duq.edu
800.283.3853

Harvard University

John F. Kennedy School of Government

www.hks.harvard.edu
admissions@hks.harvard.edu
617.495.1155

The Johns Hopkins University

The Paul H. Nitze School of Advanced International Studies (SAIS)

www.sais-jhu.edu
admissions.sais@jhu.edu
202.663.5700

University of Kent

Brussels School of International Studies

www.kent.ac.uk/brussels
bsis@kent.ac.uk
+32 2.641.1721
Skype: bsisbrussels

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Graduate Program in International Affairs

www.newschool.edu/ia8
nsadmissions@newschool.edu
800.292.3040

Ritsumeikan University

Graduate School of International Relations

www.ritsumei.ac.jp/acd/gr/gsir/eng/
ir-adm@st.ritsumei.ac.jp
(+81) 75.465.1211

University of San Francisco

Master of Arts in International Studies (MAIS) Program

www.usfca.edu/mais
mais@usfca.edu
415.422.5541

Tufts University

The Fletcher School

fletcher.tufts.edu
fletcheradmissions@tufts.edu
617.627.3040

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The Association of Professional Schools of International Affairs (APSIA) comprises more than 60 members and affiliated programs around the world dedicated to the improvement of professional education in international affairs and the advancement there by of international understanding, prosperity, peace, and security.

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other higher education institutions, the international affairs community, and the general public.

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Essays



A carefully managed U.S.
attack on Iran would prove less
risky than trying to contain a
nuclear-armed Islamic Republic.

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Time to Attack Iran

Why a Strike Is the Least Bad Option

Matthew Kroenig

IN EARLY October, U.S. officials accused Iranian operatives of planning to assassinate Saudi Arabia's ambassador to the United States on American soil. Iran denied the charges, but the episode has already managed to increase tensions between Washington and Tehran. Although the Obama administration has not publicly threatened to retaliate with military force, the allegations have underscored the real and growing risk that the two sides could go to war sometime soon—particularly over Iran's advancing nuclear program.

For several years now, starting long before this episode, American pundits and policymakers have been debating whether the United States should attack Iran and attempt to eliminate its nuclear facilities. Proponents of a strike have argued that the only thing worse than military action against Iran would be an Iran armed with nuclear weapons. Critics, meanwhile, have warned that such a raid would likely fail and, even if it succeeded, would spark a full-fledged war and a global economic crisis. They have urged the United States to rely on nonmilitary options, such as diplomacy, sanctions, and covert operations, to prevent Iran from acquiring a bomb. Fearing the costs of a bombing campaign, most critics maintain that if these other tactics fail to impede

MATTHEW KROENIG is Stanton Nuclear Security Fellow at the Council on Foreign Relations and the author of *Exporting the Bomb: Technology Transfer and the Spread of Nuclear Weapons*. From July 2010 to July 2011, he was a Special Adviser in the Office of the U.S. Secretary of Defense, responsible for defense strategy and policy on Iran.

Time to Attack Iran

Tehran's progress, the United States should simply learn to live with a nuclear Iran.

But skeptics of military action fail to appreciate the true danger that a nuclear-armed Iran would pose to U.S. interests in the Middle East and beyond. And their grim forecasts assume that the cure would be worse than the disease—that is, that the consequences of a U.S. assault on Iran would be as bad as or worse than those of Iran achieving its nuclear ambitions. But that is a faulty assumption. The truth is that a military strike intended to destroy Iran's nuclear program, if managed carefully, could spare the region and the world a very real threat and dramatically improve the long-term national security of the United States.

DANGERS OF DETERRENCE

YEARS OF international pressure have failed to halt Iran's attempt to build a nuclear program. The Stuxnet computer worm, which attacked control systems in Iranian nuclear facilities, temporarily disrupted Tehran's enrichment effort, but a report by the International Atomic Energy Agency this past May revealed that the targeted plants have fully recovered from the assault. And the latest IAEA findings on Iran, released in November, provided the most compelling evidence yet that the Islamic Republic has weathered sanctions and sabotage, allegedly testing nuclear triggering devices and redesigning its missiles to carry nuclear payloads. The Institute for Science and International Security, a nonprofit research institution, estimates that Iran could now produce its first nuclear weapon within six months of deciding to do so. Tehran's plans to move sensitive nuclear operations into more secure facilities over the course of the coming year could reduce the window for effective military action even further. If Iran expels IAEA inspectors, begins enriching its stockpiles of uranium to weapons-grade levels of 90 percent, or installs advanced centrifuges at its uranium-enrichment facility in Qom, the United States must strike immediately or forfeit its last opportunity to prevent Iran from joining the nuclear club.

Some states in the region are doubting U.S. resolve to stop the program and are shifting their allegiances to Tehran. Others have begun to discuss launching their own nuclear initiatives to counter

Matthew Kroenig

a possible Iranian bomb. For those nations and the United States itself, the threat will only continue to grow as Tehran moves closer to its goal. A nuclear-armed Iran would immediately limit U.S. freedom of action in the Middle East. With atomic power behind it, Iran could threaten any U.S. political or military initiative in the Middle East with nuclear war, forcing Washington to think twice before acting in the region. Iran's regional rivals, such as Saudi

**Deterring Iran would
come at a heavy price.**

Arabia, would likely decide to acquire their own nuclear arsenals, sparking an arms race. To constrain its geopolitical rivals, Iran could choose to spur proliferation by transferring nuclear technology to its allies—other countries and terrorist groups alike. Having the bomb would give Iran greater cover for conventional aggression and coercive diplomacy, and the battles between its terrorist proxies and Israel, for example, could escalate. And Iran and Israel lack nearly all the safeguards that helped the United States and the Soviet Union avoid a nuclear exchange during the Cold War—secure second-strike capabilities, clear lines of communication, long flight times for ballistic missiles from one country to the other, and experience managing nuclear arsenals. To be sure, a nuclear-armed Iran would not intentionally launch a suicidal nuclear war. But the volatile nuclear balance between Iran and Israel could easily spiral out of control as a crisis unfolds, resulting in a nuclear exchange between the two countries that could draw the United States in, as well.

These security threats would require Washington to contain Tehran. Yet deterrence would come at a heavy price. To keep the Iranian threat at bay, the United States would need to deploy naval and ground units and potentially nuclear weapons across the Middle East, keeping a large force in the area for decades to come. Alongside those troops, the United States would have to permanently deploy significant intelligence assets to monitor any attempts by Iran to transfer its nuclear technology. And it would also need to devote perhaps billions of dollars to improving its allies' capability to defend themselves. This might include helping Israel construct submarine-launched ballistic missiles and hardened ballistic missile silos to ensure that it can maintain a secure second-strike capability. Most of all, to make

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containment credible, the United States would need to extend its nuclear umbrella to its partners in the region, pledging to defend them with military force should Iran launch an attack.

In other words, to contain a nuclear Iran, the United States would need to make a substantial investment of political and military capital to the Middle East in the midst of an economic crisis and at a time when it is attempting to shift its forces out of the region. Deterrence would come with enormous economic and geopolitical costs and would have to remain in place as long as Iran remained hostile to U.S. interests, which could mean decades or longer. Given the instability of the region, this effort might still fail, resulting in a war far more costly and destructive than the one that critics of a preemptive strike on Iran now hope to avoid.

A FEASIBLE TARGET

A NUCLEAR IRAN would impose a huge burden on the United States. But that does not necessarily mean that Washington should resort to military means. In deciding whether it should, the first question to answer is if an attack on Iran's nuclear program could even work. Doubters point out that the United States might not know the location of Iran's key facilities. Given Tehran's previous attempts to hide the construction of such stations, most notably the uranium-enrichment facilities in Natanz and Qom, it is possible that the regime already possesses nuclear assets that a bombing campaign might miss, which would leave Iran's program damaged but alive.

This scenario is possible, but not likely; indeed, such fears are probably overblown. U.S. intelligence agencies, the IAEA, and opposition groups within Iran have provided timely warning of Tehran's nuclear activities in the past—exposing, for example, Iran's secret construction at Natanz and Qom before those facilities ever became operational. Thus, although Tehran might again attempt to build clandestine facilities, Washington has a very good chance of catching it before they go online. And given the amount of time it takes to construct and activate a nuclear facility, the scarcity of Iran's resources, and its failure to hide the facilities in Natanz and Qom successfully, it is unlikely

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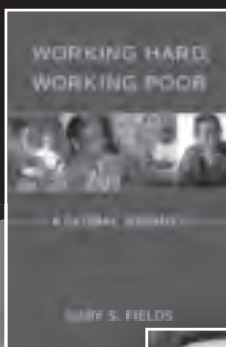
that Tehran has any significant operational nuclear facilities still unknown to Western intelligence agencies.

Even if the United States managed to identify all of Iran's nuclear plants, however, actually destroying them could prove enormously difficult. Critics of a U.S. assault argue that Iran's nuclear facilities are dispersed across the country, buried deep underground and hardened against attack, and ringed with air defenses, making a raid complex and dangerous. In addition, they claim that Iran has purposefully placed its nuclear facilities near civilian populations, which would almost certainly come under fire in a U.S. raid, potentially leading to hundreds, if not thousands, of deaths.

These obstacles, however, would not prevent the United States from disabling or demolishing Iran's known nuclear facilities. A preventive operation would need to target the uranium-conversion plant at Isfahan, the heavy-water reactor at Arak, and various centrifuge-manufacturing sites near Natanz and Tehran, all of which are located aboveground and are highly vulnerable to air strikes. It would also have to hit the Natanz facility, which, although it is buried under reinforced concrete and ringed by air defenses, would not survive an attack from the U.S. military's new bunker-busting bomb, the 30,000-pound Massive Ordnance Penetrator, capable of penetrating up to 200 feet of reinforced concrete. The plant in Qom is built into the side of a mountain and thus represents a more challenging target. But the facility is not yet operational and still contains little nuclear equipment, so if the United States acted quickly, it would not need to destroy it.

Washington would also be able to limit civilian casualties in any campaign. Iran built its most critical nuclear plants, such as the one in Natanz, away from heavily populated areas. For those less important facilities that exist near civilian centers, such as the centrifuge-manufacturing sites, U.S. precision-guided missiles could pinpoint specific buildings while leaving their surroundings unscathed. The United States could reduce the collateral damage even further by striking at night or simply leaving those less important plants off its target list at little cost to the overall success of the mission. Although Iran would undoubtedly publicize any human suffering in the wake of a military action, the majority of the victims would be the military personnel, engineers, scientists, and technicians working at the facilities.

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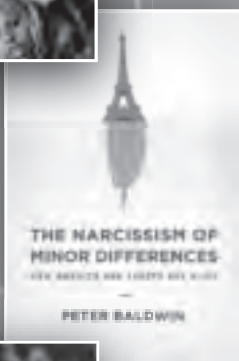


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Matthew Kroenig

SETTING THE RIGHT REDLINES

THE FACT that the United States can likely set back or destroy Iran's nuclear program does not necessarily mean that it should. Such an attack could have potentially devastating consequences—for international security, the global economy, and Iranian domestic politics—all of which need to be accounted for.

To begin with, critics note, U.S. military action could easily spark a full-blown war. Iran might retaliate against U.S. troops or allies, launching missiles at military installations or civilian populations in the Gulf or perhaps even Europe. It could activate its proxies abroad, stirring sectarian tensions in Iraq, disrupting the Arab Spring, and ordering terrorist attacks against Israel and the United States. This could draw Israel or other states into the fighting and compel the United States to escalate the conflict in response. Powerful allies of Iran, including China and Russia, may attempt to economically and diplomatically isolate the United States. In the midst of such spiraling violence, neither side may see a clear path out of the battle, resulting in a long-lasting, devastating war, whose impact may critically damage the United States' standing in the Muslim world.

Those wary of a U.S. strike also point out that Iran could retaliate by attempting to close the Strait of Hormuz, the narrow access point to the Persian Gulf through which roughly 20 percent of the world's oil supply travels. And even if Iran did not threaten the strait, speculators, fearing possible supply disruptions, would bid up the price of oil, possibly triggering a wider economic crisis at an already fragile moment.

None of these outcomes is predetermined, however; indeed, the United States could do much to mitigate them. Tehran would certainly feel like it needed to respond to a U.S. attack, in order to reestablish deterrence and save face domestically. But it would also likely seek to calibrate its actions to avoid starting a conflict that could lead to the destruction of its military or the regime itself. In all likelihood, the Iranian leadership would resort to its worst forms of retaliation, such as closing the Strait of Hormuz or launching missiles at southern Europe, only if it felt that its very existence was threatened. A targeted U.S. operation need not threaten Tehran in such a fundamental way.

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To make sure it doesn't and to reassure the Iranian regime, the United States could first make clear that it is interested only in destroying Iran's nuclear program, not in overthrowing the government. It could then identify certain forms of retaliation to which it would respond with devastating military action, such as attempting to close the Strait of Hormuz, conducting massive and sustained attacks on Gulf states and U.S. troops or ships, or launching terrorist attacks in the United States itself. Washington would then need to clearly articulate these "redlines" to Tehran during and after the attack to ensure that the message was not lost in battle. And it would need to accept the fact that it would have to absorb Iranian responses that fell short of these redlines without escalating the conflict. This might include accepting token missile strikes against U.S. bases and ships in the region—several salvos over the course of a few days that soon taper off—or the harassment of commercial and U.S. naval vessels. To avoid the kind of casualties that could compel the White House to escalate the struggle, the United States would need to evacuate nonessential personnel from U.S. bases within range of Iranian missiles and ensure that its troops were safely in bunkers before Iran launched its response. Washington might also need to allow for stepped-up support to Iran's proxies in Afghanistan and Iraq and missile and terrorist attacks against Israel. In doing so, it could induce Iran to follow the path of Iraq and Syria, both of which refrained from starting a war after Israel struck their nuclear reactors in 1981 and 2007, respectively.

Even if Tehran did cross Washington's redlines, the United States could still manage the confrontation. At the outset of any such violation, it could target the Iranian weapons that it finds most threatening to prevent Tehran from deploying them. To de-escalate the situation quickly and prevent a wider regional war, the United States could also secure the agreement of its allies to avoid responding to an Iranian attack. This would keep other armies, particularly the Israel Defense Forces, out of the fray. Israel should prove willing to accept such an arrangement in exchange for a U.S. promise to eliminate the Iranian

Attempting to manage a nuclear-armed Iran is not only a terrible option but the worst.

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nuclear threat. Indeed, it struck a similar agreement with the United States during the Gulf War, when it refrained from responding to the launching of Scud missiles by Saddam Hussein.

Finally, the U.S. government could blunt the economic consequences of a strike. For example, it could offset any disruption of oil supplies by opening its Strategic Petroleum Reserve and quietly encouraging some Gulf states to increase their production in the run-up to the attack. Given that many oil-producing nations in the region, especially Saudi Arabia, have urged the United States to attack Iran, they would likely cooperate.

Washington could also reduce the political fallout of military action by building global support for it in advance. Many countries may still criticize the United States for using force, but some—the Arab states in particular—would privately thank Washington for eliminating the Iranian threat. By building such a consensus in the lead-up to an attack and taking the outlined steps to mitigate it once it began, the United States could avoid an international crisis and limit the scope of the conflict.

ANY TIME IS GOOD TIME

CRITICS HAVE another objection: even if the United States managed to eliminate Iran's nuclear facilities and mitigate the consequences, the effects might not last long. Sure enough, there is no guarantee that an assault would deter Iran from attempting to rebuild its plants; it may even harden Iran's resolve to acquire nuclear technology as a means of retaliating or protecting itself in the future. The United States might not have the wherewithal or the political capital to launch another raid, forcing it to rely on the same ineffective tools that it now uses to restrain Iran's nuclear drive. If that happens, U.S. action will have only delayed the inevitable.

Yet according to the IAEA, Iran already appears fully committed to developing a nuclear weapons program and needs no further motivation from the United States. And it will not be able to simply resume its progress after its entire nuclear infrastructure is reduced to rubble. Indeed, such a devastating offensive could well force Iran to quit the nuclear game altogether, as Iraq did after its nuclear program was

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destroyed in the Gulf War and as Syria did after the 2007 Israeli strike. And even if Iran did try to reconstitute its nuclear program, it would be forced to contend with continued international pressure, greater difficulty in securing necessary nuclear materials on the international market, and the lurking possibility of subsequent attacks. Military action could, therefore, delay Iran's nuclear program by anywhere from a few years to a decade, and perhaps even indefinitely.

Skeptics might still counter that at best a strike would only buy time. But time is a valuable commodity. Countries often hope to delay worst-case scenarios as far into the future as possible in the hope that this might eliminate the threat altogether. Those countries whose nuclear facilities have been attacked—most recently Iraq and Syria—have proved unwilling or unable to restart their programs. Thus, what appears to be only a temporary setback to Iran could eventually become a game changer.

Yet another argument against military action against Iran is that it would embolden the hard-liners within Iran's government, helping them rally the population around the regime and eliminate any remaining reformists. This critique ignores the fact that the hard-liners are already firmly in control. The ruling regime has become so extreme that it has sidelined even those leaders once considered to be right-wingers, such as former President Ali Akbar Hashemi Rafsanjani, for their perceived softness. And Rafsanjani or the former presidential candidate Mir Hossein Mousavi would likely continue the nuclear program if he assumed power. An attack might actually create more openings for dissidents in the long term (after temporarily uniting Iran behind Ayatollah Ali Khamenei), giving them grounds for criticizing a government that invited disaster. Even if a strike would strengthen Iran's hard-liners, the United States must not prioritize the outcomes of Iran's domestic political tussles over its vital national security interest in preventing Tehran from developing nuclear weapons.

STRIKE NOW OR SUFFER LATER

ATTACKING IRAN is hardly an attractive prospect. But the United States can anticipate and reduce many of the feared consequences of such an attack. If it does so successfully, it can remove the incentive

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for other nations in the region to start their own atomic programs and, more broadly, strengthen global nonproliferation by demonstrating that it will use military force to prevent the spread of nuclear weapons. It can also head off a possible Israeli operation against Iran, which, given Israel's limited capability to mitigate a potential battle and inflict lasting damage, would likely result in far more devastating consequences and carry a far lower probability of success than a U.S. attack. Finally, a carefully managed U.S. attack would prove less risky than the prospect of containing a nuclear-armed Islamic Republic—a costly, decades-long proposition that would likely still result in grave national security threats. Indeed, attempting to manage a nuclear-armed Iran is not only a terrible option but the worst.

With the wars in Afghanistan and Iraq winding down and the United States facing economic hardship at home, Americans have little appetite for further strife. Yet Iran's rapid nuclear development will ultimately force the United States to choose between a conventional conflict and a possible nuclear war. Faced with that decision, the United States should conduct a surgical strike on Iran's nuclear facilities, absorb an inevitable round of retaliation, and then seek to quickly de-escalate the crisis. Addressing the threat now will spare the United States from confronting a far more dangerous situation in the future. 🌐



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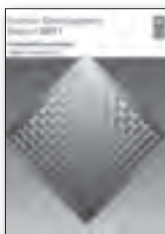
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Publisher: United Nations
Publication Date: December 2011
ISBN: 9789210612845 Pages: 816 Price: \$155.00

Talking Tough to Pakistan

How to End Islamabad's Defiance

Stephen D. Krasner

ON SEPTEMBER 22, 2011, Admiral Mike Mullen, then chairman of the U.S. Joint Chiefs of Staff, made his last official appearance before the Senate Armed Services Committee. In his speech, he bluntly criticized Pakistan, telling the committee that “extremist organizations serving as proxies for the government of Pakistan are attacking Afghan troops and civilians as well as U.S. soldiers.” The Haqqani network, he said, “is, in many ways, a strategic arm of Pakistan’s Inter-Services Intelligence Agency [ISI].” In 2011 alone, Mullen continued, the network had been responsible for a June attack on the Intercontinental Hotel in Kabul, a September truck-bomb attack in Wardak Province that wounded 77 U.S. soldiers, and a September attack on the U.S. embassy in Kabul.

These observations did not, however, lead Mullen to the obvious conclusion: Pakistan should be treated as a hostile power. And within days, military officials began walking back his remarks, claiming that Mullen had meant to say only that Islamabad gives broad support to the Haqqani network, not that it gives specific direction. Meanwhile, unnamed U.S. government officials asserted that he had overstated the case. Mullen’s testimony, for all the attention it received, did not signify a new U.S. strategy toward Pakistan.

STEPHEN D. KRASNER is Professor of International Relations at Stanford University and a Senior Fellow at Stanford’s Freeman Spogli Institute for International Studies and at the Hoover Institution. He was Director of Policy Planning at the U.S. State Department in 2005–7.

Stephen D. Krasner

Yet such a shift is badly needed. For decades, the United States has sought to buy Pakistani cooperation with aid: \$20 billion worth since 9/11 alone. This money has been matched with plenty of praise. At his first press conference in Islamabad following his 2007 appointment as chairman of the Joint Chiefs, Mullen called Pakistan “a steadfast and historic ally.” In 2008, then Secretary of State Condoleezza Rice even said that she “fully believed” that Pakistan “does not in any way want to be associated with terrorist elements and is indeed fighting to root them out wherever [Pakistani officials] find them.” Meanwhile, U.S. leaders have spent an outsized amount of face time with their Pakistani counterparts. As secretary of state, Hillary Clinton has made four trips to Pakistan, compared with two to India and three to Japan. Mullen made more than 20 visits to Pakistan.

To be sure, Mullen was not the first U.S. official to publicly point the finger at Islamabad, nor will he be the last. In 2008, the CIA blamed Pakistan’s ISI for aiding the bombing of the Indian embassy in Kabul. In July 2011, two months after U.S. Navy SEALs raided Osama bin Laden’s compound near the prestigious Pakistan Military Academy, Admiral James Winnefeld, vice chair of the Joint Chiefs, told the Senate Armed Services Committee, “Pakistan is a very, very difficult partner, and we all know that.” And in an October press conference with Afghan President Hamid Karzai, Clinton noted that the Obama administration intended to “push the Pakistanis very hard,” adding, “they can either be helping or hindering.”

Washington’s tactic—criticism coupled with continued assistance—has not been effectual. Threats and censure go unheeded in Pakistan because Islamabad’s leaders do not fear the United States. This is because the United States has so often demonstrated a fear of Pakistan, believing that although Pakistan’s policies have been unhelpful, they could get much worse. Washington seems to have concluded that if it actually disengaged and as a result Islamabad halted all its cooperation in Afghanistan, then U.S. counterinsurgency efforts there would be doomed. Even more problematic, the thinking goes, without external support, the already shaky Pakistani state would falter. A total collapse could precipitate a radical Islamist takeover, worsening Pakistani relations with the U.S.-backed Karzai regime in Afghanistan and escalating tensions, perhaps even precipitating a nuclear war, between Pakistan and India.

Talking Tough to Pakistan

WEIGHING OF DEEDS

THE U.S.-PAKISTANI relationship has produced a few modest successes. Pakistan has generally allowed NATO to transport supplies through its territory to Afghanistan. It has helped capture some senior al Qaeda officials, including Khalid Sheik Mohammed, the 9/11 mastermind. It has permitted the United States to launch drone strikes from bases in Baluchistan.

Yet these accomplishments pale in comparison to the ways in which Pakistan has proved uncooperative. The country is the world's worst nuclear proliferator, having sold technology to Iran, Libya, and North Korea through the A. Q. Khan network. Although Islamabad has attacked those terrorist groups, such as al Qaeda and the Pakistani Taliban, that target its institutions, it actively supports others, such as the Haqqani network, the Afghan Taliban, and Hezb-i-Islami, that attack coalition troops and Afghan officials or conspire against India. Pakistan also hampers U.S. efforts to deal with those groups; although many Pakistani officials privately support the drone program, for example, they publicly exaggerate the resulting civilian deaths. Meanwhile, they refuse to give the United States permission to conduct commando raids in Pakistan, swearing that they will defend Pakistani sovereignty at all costs.

A case in point was the raid that killed bin Laden. Rather than embrace the move, Pakistani officials reacted with fury. The police arrested a group of Pakistani citizens who were suspected of having helped the United States collect intelligence prior to the operation and delayed U.S. interrogations of bin Laden's three wives for more than a week. Lieutenant General Ahmed Shuja Pasha, head of the ISI, condemned the U.S. raid before a special session of parliament, and the government passed a resolution pledging to revisit its relationship with the United States. Of course, the operation was embarrassing for the Pakistani military, since it showed the armed forces to be either complicit in harboring bin Laden or so incompetent that they could not find him under their own noses. But Pakistan could easily have saved face by publicly depicting the operation as a cooperative venture.

The fact that Pakistan distanced itself from the raid speaks to another major problem in the relationship: despite the billions of dollars the

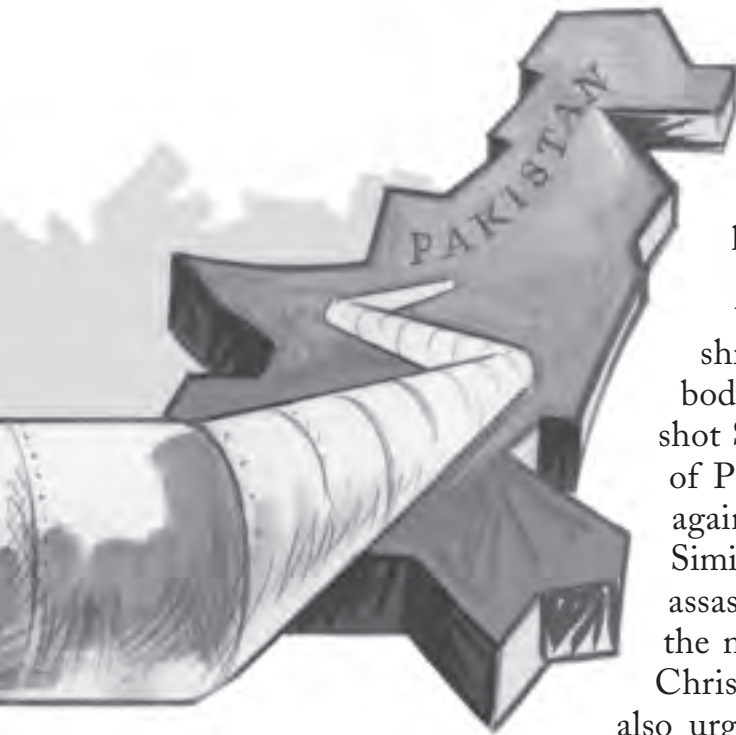


United States has given Pakistan, public opinion there remains adamantly anti-American. In a 2010 Pew survey of 21 countries, those Pakistanis polled had among the lowest favorability ratings of the United States: 17 percent. The next year, another Pew survey found that 63 percent of the population disapproved of the raid that killed bin Laden, and 55 percent thought it was a bad thing that he had died.

Washington's current strategy toward Islamabad, in short, is not working. Any gains the United States has bought with its aid and engagement have come at an extremely high price and have been more than offset by Pakistan's nuclear proliferation and its support for the groups that attack Americans, Afghans, Indians, and others.

RATIONAL CHOICE

IT IS tempting to believe that Pakistan's lack of cooperation results from its weakness as a state. One version of this argument is that



much of Pakistan's civilian and military leadership might actually want to be more aligned with the United States but is prevented from being so by powerful hard-line Islamist factions. Its advocates point to the fact that public officials shrank from condemning the bodyguard who in January 2011 shot Salman Taseer, the governor of Punjab, who had spoken out against Pakistan's blasphemy law. Similar silence followed the March assassination of Shahbaz Bhatti, the minorities minister and only Christian in the cabinet, who had

also urged reforming the law. Presumably, the politicians held their tongues out of fear of reprisal. Another explanation of the weakness of the Pakistani state is that the extremists in the government and the military who support militants offer that support despite their superiors' objections. For example, the May 2011 terrorist attack on Pakistan's naval air base Mehran, which the top military brass condemned, was later suspected to have been conducted with help from someone on the inside.

Still, there is a much more straightforward explanation for Pakistan's behavior. Its policies are a fully rational response to the conception of the country's national interest held by its leaders, especially those in the military. Pakistan's fundamental goal is to defend itself against its rival, India. Islamabad deliberately uses nuclear proliferation and deterrence, terrorism, and its prickly relationship with the United States to achieve this objective.

Pakistan's nuclear strategy is to project a credible threat of first use against India. The country has a growing nuclear arsenal, a stockpile of short-range missiles to carry warheads, and plans for rapid weapons

Stephen D. Krasner

dispersion should India invade. So far, the strategy has worked; although Pakistan has supported numerous attacks on Indian soil, India has not retaliated.

Transnational terrorism, Pakistanis believe, has also served to constrain and humiliate India. As early as the 1960s, Pakistani strategists concluded that terrorism could help offset India's superior conventional military strength. They were right. Pakistani militant activity in Kashmir has led India to send hundreds of thousands of troops into the province—as many as 500,000 during a particularly tense moment with Pakistan in 2002. Better that India sends its troops to battle terrorists on its own territory, the Pakistani thinking goes, than march them across the border. Further, the 2008 Mumbai attack, which penetrated the heart of India, was a particularly embarrassing episode; the failure to prevent it, and the feeble response to it, demonstrated the ineffectuality of India's security forces.

Pakistan's double game with the United States has been effective, too. After 9/11, Pakistan's leaders could hardly resist pressure from Washington to cooperate. But they were also loath to lose influence with the insurgents in Afghanistan, which they believed gave Pakistan strategic depth against India. So Islamabad decided to have things both ways: cooperating with Washington enough to make itself useful but obstructing the coalition's plans enough to make it nearly impossible to end the Afghan insurgency. This has been an impressive accomplishment.

CARING BY NEGLECTING

AS MULLEN'S comments attest, U.S. officials do recognize the flaws in their country's current approach to Pakistan. Yet instead of making radical changes to that policy, Washington continues to muddle through, working with Pakistan where possible, attempting to convince its leaders that they should focus on internal, rather than external, threats, and hoping for the best. For their part, commentators mostly call for marginal changes, such as engaging the Pakistani military more closely on the drone program and making the program more transparent, opening U.S. textile markets to Pakistani trade, helping Pakistan address its energy deficit, focusing on a peaceful resolution of the Kashmir dispute, and developing closer ties to civilian officials. Many

Talking Tough to Pakistan

of these suggestions seem to be based on the idea that if millions of dollars in U.S. aid has not been enough to buy Pakistani support, perhaps extra deal sweeteners will be.

The one significant policy change since 2008 has been the retargeting of aid to civilians. Under the Obama administration, total assistance has increased by 48 percent, and a much higher percentage of it is economic rather than security related: 45 percent in 2010 as opposed to 24 percent in 2008. The Enhanced Partnership With Pakistan Act of 2009, which committed \$7.5 billion to Pakistan over five years, conditioned disbursements on Pakistan's behavior, including cooperation on counter-terrorism and the holding of democratic elections.

Despite Pakistan's ongoing problematic behavior, however, aid has continued to flow. Clinton even certified in March 2011 that Pakistan had made a "sustained commitment" to combating terrorist groups. Actions such as this have undermined American credibility when it comes to pressuring Pakistan to live up to its side of the bargain. The United States has shown that the sticks that come with its carrots are hollow.

The only way the United States can actually get what it wants out of Pakistan is to make credible threats to retaliate if Pakistan does not comply with U.S. demands and offer rewards only in return for cooperative actions taken. U.S. officials should tell their Pakistani counterparts in no uncertain terms that they must start playing ball or face malign neglect at best and, if necessary, active isolation. Malign neglect would mean ending all U.S. assistance, military and civilian; severing intelligence cooperation; continuing and possibly escalating U.S. drone strikes; initiating cross-border special operations raids; and strengthening U.S. ties with India. Active isolation would include, in addition, declaring Pakistan a state sponsor of terrorism, imposing sanctions, and pressuring China and Saudi Arabia to cut off their support, as well.

Of course, the United States' new "redlines" would be believable only if it is clear to Pakistan that the United States would be better off acting on them than backing down. (And the more believable they are, the less likely the United State will have to carry them out.) So what would make the threats credible?

First, the United States must make clear that if it ended its assistance to Pakistan, Pakistan would not be able to retaliate. The United States could continue its drone strikes, perhaps using the stealth versions

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of them that it is currently developing. It could suppress Pakistani air defenses, possibly with electronic jammers, so as to limit military deaths and collateral damage. And even if Pakistan shot down some drones, it could not destroy them all. The United States might even be able to conduct some Special Forces raids, which would be of such short duration and against such specific targets that Pakistan would not be able to retaliate with conventional forces. Pakistan might attempt to launch strikes against NATO and Afghan forces in Afghanistan, but its military would risk embarrassing defeat if those campaigns did not go well. Pakistan might threaten to cut off its intelligence cooperation, but that cooperation has never really extended to sharing information on the Afghan Taliban, one of the United States' main concerns in Afghanistan. Moreover, if Pakistan started tolerating or abetting al Qaeda on its own soil, the country would be even more at risk. Al Qaeda could turn against the state and attempt to unseat the government. And the United States would surely begin striking Pakistan even more aggressively if al Qaeda found haven there.

Second, the United States must show that it can neutralize one of Pakistan's trump cards: its role in the war in Afghanistan. Washington must therefore develop a strategy for Afghanistan that works without Pakistan's help. That means a plan that does not require transporting personnel or materiel through Pakistan. Nearly 60 percent of the NATO supplies sent into Afghanistan are already routed through the north, through Russia and Central Asia. The U.S. military is hoping to increase that number to 75 percent. Without Pakistan, therefore, the coalition could still support a substantial force in Afghanistan, but not one as big as the current one of 131,000 troops. The basic objective of that force would necessarily be counterterrorism, not counterinsurgency. Counterterrorism is less personnel- and resource-intensive because it aims only to prevent the country from becoming a haven for Islamist extremists, not to transform it into a well-functioning democracy. Given the Obama administration's current plans to withdraw 24,000 U.S. troops by the summer of 2012, with many more to follow, such a strategy is already inescapable.

Finally, Washington must shed its fear that its withdrawal of aid or open antagonism could lead to the Pakistani state's collapse, a radical Islamist takeover, or nuclear war. Pakistanis, not Americans, have always determined their political future. Even substantial U.S. investments in

Talking Tough to Pakistan

the civilian state and the economy, for example, have not led to their improvement or to gains in stability. With or without U.S. aid to Pakistan, the Pakistani military will remain the most respected institution in the country. In a 2011 Pew poll of Pakistanis, 79 percent of respondents said that the military was having a good influence on the country's direction, compared with 20 percent who said that the national government was.

As for the possibility of an Islamist takeover, the country's current power centers have a strong interest in maintaining control and so will do whatever they can to keep it—whatever Washington's policy is. It is worth remembering that Pakistan has already proved itself able to take out the terrorist networks that threaten its own institutions, as it did in the Swat Valley and the district of Buner in 2009. Moreover, government by radical Islamists has not proved to be a popular choice among Pakistanis. In the last general election, the Muttahida Majlis-e-Amal, a coalition of Islamist parties, won only seven out of 340 seats in the National Assembly.

The possibility that nuclear weapons could wind up in the hands of terrorists is a serious risk, of course, but not one that the United States could easily mitigate whatever its policy in the region. Pakistan's nuclear posture, which involves rapid dispersion, a first-strike capability, and the use of tactical weapons, increases the chances of the central government's losing control. Even so, Pakistan will not alter that posture because it is so effective in deterring India. Meanwhile, previous U.S. efforts to help tighten Pakistan's command-and-control systems have been hampered by mutual distrust. Any new such efforts would be, too. Finally, since India has both a first- and a second-strike capability, Pakistan would not likely strike India first in the event of a crisis. In any case, even if things did escalate, there is not much that the United States, or anyone else, could do—good relations or not.

From a U.S. perspective, then, there is no reason to think that malign neglect or active isolation would make Pakistan's behavior or problems any worse.

HEADS I WIN, TAILS YOU LOSE

EVEN AS the United States threatens disengagement, it should emphasize that it would still prefer a productive relationship. But it should also make clear that the choice is Pakistan's: if the country ends its

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support for terrorism; works in earnest with the United States to degrade al Qaeda, the Taliban, and the Haqqani network; and stops its subversion in Afghanistan, the United States will offer generous rewards. It could provide larger assistance programs, both civilian and military; open U.S. markets to Pakistani exports; and support political arrangements in Kabul that would reduce Islamabad's fear of India's influence. In other words, it is only after Pakistan complies with its demands that the United States should offer many of the policy proposals now on the table. And even then, these rewards should not necessarily be targeted toward changing Pakistan's regional calculus; they should be offered purely as payment for Pakistan's cooperation on the United States' most important policies in the region.

A combination of credible threats and future promises offers the best hope of convincing Islamabad that it would be better off cooperating with the United States. In essence, Pakistan would be offered a choice between the situation of Iran and that of Indonesia, two large Islamic states that have chosen very different paths. It could be either a pariah state surrounded by hostile neighbors and with dim economic prospects or a country with access to international markets, support from the United States and Europe, and some possibility of détente with its neighbors. The Indonesian path would lead to increased economic growth, an empowered middle class, strengthened civil-society groups, and a stronger economic and social foundation for a more robust democracy at some point in the future. Since it would not directly threaten the military's position, the Indonesian model should appeal to both pillars of the Pakistani state. And even if Islamabad's cooperation is not forthcoming, the United States is better off treating Pakistan as a hostile power than continuing to spend and get nothing in return.

Implicit in the remarks Mullen made to the Senate was the argument that Washington must get tough with Pakistan. He was right. A whole variety of gentle forms of persuasion have been tried and failed. The only option left is a drastic one. The irony is that this approach won't benefit just the United States: the whole region, including Pakistan, could quickly find itself better off. 🌐

CHINA GROWS UP

*After 10 years in the
WTO, China's economy
is shifting gears.*

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A center of commerce:
A view of Shanghai
on the Yangtze River
at night.

WHEN YOU THINK about U.S. corporations' operations in China, chances are three words come to mind: low-cost labor. That's what has lured thousands of American companies into the country and enriched their gross margins. But now China's economy has arrived at an inflection point. Over the next decade, China's siren song will be these three words: enormous middle class.

"Anyone who's taken advantage of this cheap labor over the last several decades has done remarkably well. But as China develops, those opportunities recede. Rather than sourcing, China—with its emerging middle class—is becoming a place for selling products," says Christian Lundblad, an associate professor of finance at Kenan-Flagler Business School at the University of North Carolina at Chapel Hill.

In theory this transition will play out beautifully.

China will add an estimated 1 billion people to the middle class over the next decade, nearly one-third of the world's expected middle tier by 2020. With a huge new product market in China, U.S. firms can swiftly grow exports, correcting America's trade deficit in the process.

The risks? Inflationary pressures in China might push up costs in the short term. Increasing income disparity might cause instability. And the steady improvement in business conditions wrought by China's membership in the World Trade Organization (WTO) could slow, or possibly reverse.

After joining the WTO in 2001, China cranked open the trade gates by revising thousands of laws and administrative processes, cutting import tariffs by nearly 40%, almost eliminating import licenses and quotas, relaxing ownership restrictions on foreign businesses, and allowing non-Chinese companies entry into previously off-limits sectors.

This cascade of market-opening moves—the latest in China's long-term effort to become part of the modern world economy—has generated eye-popping statistics. U.S. exports to China have grown 468%, to \$91.9 billion, since 2000. Trade has increased from less than 10% of China's GDP to 64% over the same period. Surges in Chinese demand account for roughly 50% of export growth of Hong Kong, Japan, and Taiwan.

"Foreign trade has grown rapidly, and foreign investment has poured into the country," says John Frisbie, president of the U.S.-China Business Council (USCBC). "The trend has created jobs, helped to raise incomes, and contributed to China's extraordinary growth."

The WTO's membership requirements lowered several key barriers for U.S. companies, including UPS. "The liberalization of express delivery services has been particularly important to the growth of UPS in China, as it allowed us to service

Since 2000,
U.S. exports
to China have
grown

468%

SOURCE: BUREAU OF ECONOMIC ANALYSIS

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LET'S SOLVE WATER.

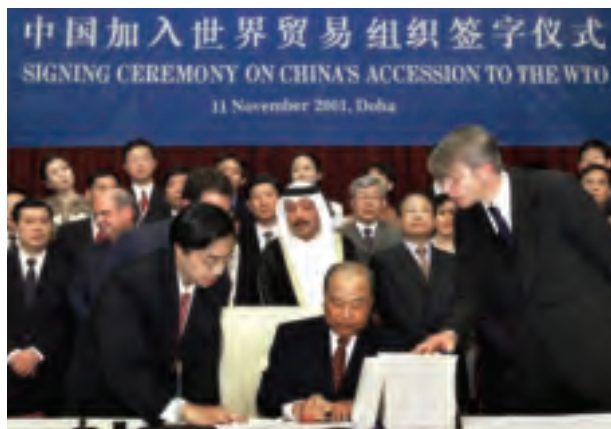
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Minister Shi Guangsheng signs China's WTO accession documents at a ceremony in Doha on Nov. 11, 2001.



China is now America's third-largest export market—

\$118

billion in 2010 when Hong Kong is included.

SOURCE: BUREAU OF ECONOMIC ANALYSIS

our customers directly and provide greater efficiency and improved visibility for their supply chains," says Chris Grubb, vice president of marketing for UPS's Asia Pacific region. China also dropped its average tariff rate for medical devices and pharmaceuticals from 14% to about 6% in 2000. That move, along with removing its import quota for medical devices, encouraged UPS to increase its investment in health care logistics in China.

Since 2002, UPS has invested a hefty \$900 million in the country. Between 2008 and 2010 it opened hubs in Shanghai and Shen-

zhen, and a shared center in Hefei, Anhui Province. Today the carrier operates out of 45 locations, serving 330 cities, and employs some 6,000 workers.

Similarly, Xylem Inc. has positioned itself to reap the benefits of China's meteoric rise. The \$3.8 billion water business that was spun off of ITT Corp. last month and renamed as a stand-alone company—is an old hand in China, where one-quarter of the total population lacks access to safe drinking water.

"China's five-year plan for infrastructure investments aims to provide China's population with improved

access to clean water and superior wastewater treatment," says Bob Wolpert, head of Xylem's businesses in China and India, as well as president of the company's flow control business. "We've been doing business in China for more than 20 years, and we will continue to support these newest goals with our global water and wastewater transport and treatment business."

Xylem's history in China includes an award-winning effort it still operates called Watermark. Starting in 2009, Watermark and its charitable partners have designed and installed solar-powered safe water pumps, hand-washing stations and latrines for more than 8,000 students and teachers; taught a disaster risk-reduction course for an international NGO, and hosted a competition for Chinese students to find innovative solutions to water supply problems and pollution.

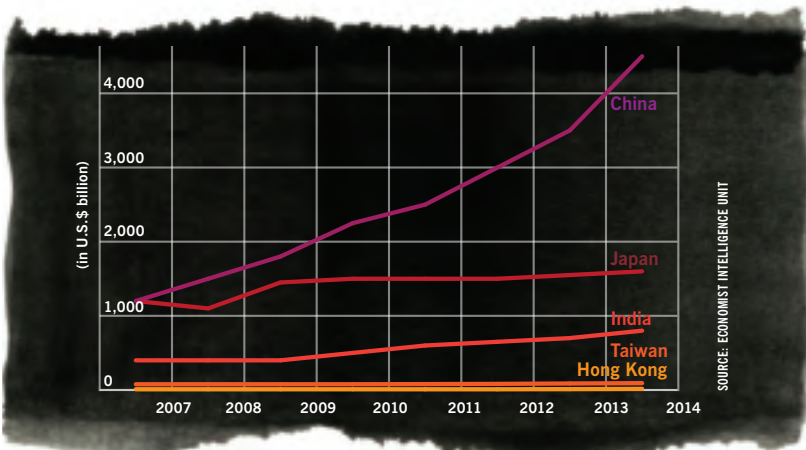
MATURING MARKET

During the last decade, relaxed trade regulations have paid off handsomely for most U.S. companies. Nearly 90% of USCBC members responding to a council survey in 2010 said that their China operations were profitable and that profit margins are the same or better than other ventures worldwide.

As China's economy matures, its emerging middle class is both a boon to U.S. corporations and a potential time bomb. Chinese with disposable income are already ringing cash registers for U.S. consumer goods companies. Yum!

RINGING UP RETAIL SALES

China's retail sales growth has helped offset declines in other Asian markets.





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A bustling middle class shops on the world-famous Nanjing Road in Shanghai.

Brands, based in Louisville, had more than 3,400 KFC and Pizza Hut restaurants in China in the first quarter of 2010. Starbucks has 700 outlets there and plans to open 80 shops per year going forward, making China the company's second-largest market.

One measure of the middle class's rapid growth: cellphone usage. China Telecom, which is a dominant carrier in China with broadband access to all 31 provinces and 70% of the country's Internet market, had some 28 million mobile subscribers in 2008. By August of this year, the figure had more than quadrupled, to 113.5 million.

The Chinese are hungry for America's big-ticket items too. GM, which held its first board of directors meeting in China this year, sold more light vehicles—16.6 million—in China last year than it did in the U.S. Back in 2000 it sold just over 1 million. That torrid pace will

China's actual consumption will increase by more than six times by 2027 to as much as \$10 trillion annually.

SOURCE: BUREAU OF ECONOMIC ANALYSIS

continue. J.D. Power and Associates predicts that in just seven more years, the Chinese market will reach 33 million vehicles. Needless to say, GM, Volvo, and other foreign and Chinese car companies are racing to build factories there.

Apart from autos, food, and beverages, the industries with the greatest growth prospects in China include retail, agricultural goods, processed foods, aviation, natural resources (particularly lumber, coal, wheat, and corn), entertainment, and tractors and trucks.

Alongside the growth in

middle-class consumers is a significant rise in small and medium-size businesses. SMEs, as they are known (for Small to Medium Enterprises), contribute 60% of industrial output and 80% of jobs in China. Currently suffering from shortages of electricity, capital, and labor, as well as soaring costs, many of the country's SMEs are facing the toughest conditions in years. The country's new national growth plan for SMEs calls for addressing these problems and other growth impediments by simplifying legal business structures, easing hiring rules and boosting development of targeted industries (including nanotechnology, biotechnology, defense, and pharmaceuticals) through incentives and other moves.

AliExpress, a new online wholesale marketplace launched by Alibaba.com, highlights the business-to-business opportunities in the SME market. Alibaba.com, which describes itself as the world's largest business e-commerce marketplace connecting buyers and suppliers, created AliExpress to enable consumers and businesses globally to buy products at wholesale prices. Through the integration of UPS technology and shipping services, AliExpress customers can manage their shipping and tracking processes on AliExpress's website.

GROWING PAINS

Amid the exciting prospects in China, however, new risks are growing. The country has been grappling with inflationary pressures. Loath

to revisit the 20% inflation rate that prevailed during the late 1980s, China has put the brakes on monetary policy during the last year or so. But the current global economic slowdown, which has triggered a significant contraction in China's growth, calls for the opposite: stimulus policies.

Walking this fine line will be all the more challenging as millions of Chinese continue to migrate from rural to urban areas. "A global economic slowdown makes it more difficult for the government to employ these interior workers who are moving to the coast," says UNC's Lundblad. Over the next 14 years, some 250 million Chinese will migrate, on top of the 200 million who've moved during the past 20 to

30 years. Income inequality, which has grown very rapidly, particularly from region to region, drives much of the movement and could be a threat to China's stability.

For companies already doing business in China, the chief concern is, as always, achieving equal footing in the country. The USCBC's members cited competition with state-owned enterprises, intellectual property rights enforcement, and licensing, business, and product approvals from regulatory authorities among their top 10 concerns, in last year's survey. The rise of protectionist voices in China and the U.S., which could roll back recent market-opening measures if the voices become loud enough, concerns the US-

CBC's Frisbie.

"The terms of China's WTO entry agreement cannot be the end of the story," he says. "Services sector reforms and market openings, innovation and technology transfer policies that are based on global best practices for Chinese and foreign companies are all areas that will be crucial."

Clearly, doing business intelligently in China is getting more complicated as its economy matures. But the country's siren song is harder than ever to ignore. Who said growing up was easy? ●

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Riding the Middle-Class Boom

Whether you're a car maker or one-shop retailer hunting for opportunities in China, the first thing you're likely to do is make a phone call or send an e-mail to a prospective partner. That explains why revenue for China Telecom Americas, the first overseas subsidiary of China Telecom Corp., has been growing at an average breakneck speed of 40% per year for the past five years.

"Trade and investment flows between China and the U.S. have been growing quickly since China joined the WTO," says Donald Tan, president of CT Americas. "We have the dominant position in China,

with 60% to 70% of the broadband and trans-Pacific submarine cable system. So we're able to provide high quality and reasonable pricing for our products and services."

Admittedly, CT Americas and the other two international subsidiaries of China Telecom still contribute just a fraction of their parent company's \$33.4 billion in annual revenues. But as China's emerging middle class attracts heavy investment by companies such as Coke, GM, Procter & Gamble and other megabrands, CT Americas stands ready to provide essential connection and expertise. The company's customers in the Americas aren't standing still either.

"Sterigenics and Perficient, like many of our customers, continue to invest and expand in China, while Chinese companies, like Bank of China, are increas-

ing their investments in the Americas," says Tan. When you own an information highway like China Telecom's, the more traffic, the better.



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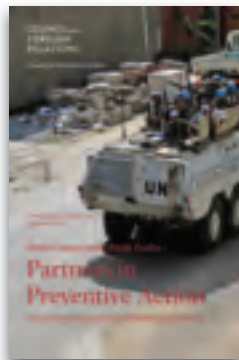


Report Warns States on China's Periphery Are Potential Sources of Regional Instability

China's growing global engagement and presence has increased the number of conceivable places and issues over which it could find itself at odds with the United States, but potential developments in the territories immediately adjacent to China remain the most likely—and the most worrisome—sources of friction. In this Center for Preventive Action study, *Managing Instability on China's Periphery*, CFR scholars provide policy options for preventing a major crisis and mitigating the consequences in North Korea, Myanmar, Pakistan, and Central Asia.



www.cfr.org/china_periphery_memos



Report Calls for Strengthening Global Architecture to Prevent Deadly Conflict

With the U.S. military overstretched and Washington facing acute fiscal pressures, CFR scholars **Paul B. Stares** and **Micah Zenko** urge the United States to nurture effective international partnerships to help prevent and manage violent conflicts that threaten U.S. interests. By actively improving the global architecture for preventive action—that is, the ability of leading international institutions to carry out conflict prevention—"the United States will have more effective partners in instances where it has a major stake and lessen the need for U.S. involvement when it does not."



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Balancing the East, Upgrading the West

U.S. Grand Strategy in an Age of Upheaval

Zbigniew Brzezinski

THE UNITED STATES' central challenge over the next several decades is to revitalize itself, while promoting a larger West and buttressing a complex balance in the East that can accommodate China's rising global status. A successful U.S. effort to enlarge the West, making it the world's most stable and democratic zone, would seek to combine power with principle. A cooperative larger West—extending from North America and Europe through Eurasia (by eventually embracing Russia and Turkey), all the way to Japan and South Korea—would enhance the appeal of the West's core principles for other cultures, thus encouraging the gradual emergence of a universal democratic political culture.

At the same time, the United States should continue to engage cooperatively in the economically dynamic but also potentially conflicted East. If the United States and China can accommodate each other on a broad range of issues, the prospects for stability in Asia will be greatly increased. That is especially likely if the United States can encourage a genuine reconciliation between China and Japan while mitigating the growing rivalry between China and India.

ZBIGNIEW BRZEZINSKI was U.S. National Security Adviser from 1977 to 1981. His book *Strategic Vision: America and the Crisis of Global Power*, from which this essay is adapted, will be published this winter by Basic Books.

Zbigniew Brzezinski

To respond effectively in both the western and eastern parts of Eurasia, the world's central and most critical continent, the United States must play a dual role. It must be the promoter and guarantor of greater and broader unity in the West, and it must be the balancer and conciliator between the major powers in the East. Both roles are essential, and each is needed to reinforce the other. But to have the credibility and the capacity to pursue both successfully, the United States must show the world that it has the will to renovate itself at home. Americans must place greater emphasis on the more subtle dimensions of national power, such as innovation, education, the balance of force and diplomacy, and the quality of political leadership.

A LARGER WEST

FOR THE United States to succeed as the promoter and guarantor of a renewed West, it will need to maintain close ties with Europe, continue its commitment to NATO, and manage, along with Europe, a step-by-step process of welcoming both Turkey and a truly democratizing Russia into the West. To guarantee the West's geopolitical relevance, Washington must remain active in European security. It must also encourage the deeper unification of the European Union: the close cooperation among France, Germany, and the United Kingdom—Europe's central political, economic, and military alignment—should continue and broaden.

To engage Russia while safeguarding Western unity, the French-German-Polish consultative triangle could play a constructive role in advancing the ongoing but still tenuous reconciliation between Poland and Russia. The EU's backing would help make Russian-Polish reconciliation more comprehensive, much as the German-Polish one has already become, with both reconciliations contributing to greater stability in Europe. But in order for Russian-Polish reconciliation to endure, it has to move from the governmental level to the social level, through extensive people-to-people contacts and joint educational initiatives. Expedient accommodations made by governments that are not grounded in basic changes in popular attitudes will not last. The model should be the French-German friendship after World War II, which was initiated at the highest

Balancing the East, Upgrading the West

political levels by Paris and Bonn and successfully promoted on the social and cultural level, as well.

As the United States and Europe seek to enlarge the West, Russia itself will have to evolve in order to become more closely linked with the EU. Its leadership will have to face the fact that Russia's future will be uncertain if it remains a relatively empty and underdeveloped space between the rich West and the dynamic East. This will not change even if Russia entices some Central Asian states to join Prime Minister Vladimir Putin's quaint idea of a Eurasian Union. Also, although a significant portion of the Russian public is ahead of its government in favoring EU membership, most Russians are unaware of how exacting many of the qualifying standards for membership are, especially with regard to democratic reform.

The process of the EU and Russia coming closer is likely to stall occasionally and then lurch forward again, progressing in stages and including transitional arrangements. To the extent possible, it should proceed simultaneously on the social, economic, political, and security levels. One can envisage more and more opportunities for social interactions, increasingly similar legal and constitutional arrangements, joint security exercises between NATO and the Russian military, and new institutions for coordinating policy within a continually expanding West, all resulting in Russia's increasing readiness for eventual membership in the EU.

It is not unrealistic to imagine a larger configuration of the West emerging after 2025. In the course of the next several decades, Russia could embark on a comprehensive law-based democratic transformation compatible with both EU and NATO standards, and Turkey could become a full member of the EU, putting both countries on their way to integration with the transatlantic community. But even before that occurs, a deepening geopolitical community of interest could arise among the United States, Europe (including Turkey), and Russia. Since any westward gravitation by Russia would likely be preceded and encouraged by closer ties between

If the United States does not promote the emergence of an enlarged West, dire consequences could follow.

Zbigniew Brzezinski

Ukraine and the EU, the institutional seat for a collective consultative organ (or perhaps initially for an expanded Council of Europe) could be located in Kiev, the ancient capital of Kievan Rus, whose location would be symbolic of the West's renewed vitality and enlarging scope.

If the United States does not promote the emergence of an enlarged West, dire consequences could follow: historical resentments could come back to life, new conflicts of interest could arise, and shortsighted competitive partnerships could take shape. Russia could exploit its energy assets and, emboldened by Western disunity, seek to quickly absorb Ukraine, reawakening its own imperial ambitions and contributing to greater international disarray. With the EU passive, individual European states, in search of greater commercial opportunities, could then seek their own accommodations with Russia. One can envisage a scenario in which economic self-interest leads Germany or Italy, for example, to develop a special relationship with Russia. France and the United Kingdom could then draw closer while viewing Germany askance, with Poland and the Baltic states desperately pleading for additional U.S. security guarantees. The result would be not a new and more vital West but rather a progressively splintering and increasingly pessimistic West.

THE COMPLEX EAST

SUCH A disunited West would not be able to compete with China for global relevance. So far, China has not articulated an ideological dogma that would make its recent performance appear universally applicable, and the United States has been careful not to make ideology the central focus of its relations with China. Wisely, both Washington and Beijing have embraced the concept of a "constructive partnership" in global affairs, and the United States, although critical of China's violations of human rights, has been careful not to stigmatize the Chinese socioeconomic system as a whole.

But if an anxious United States and an overconfident China were to slide into increasing political hostility, it is more than likely that both countries would face off in a mutually destructive ideological conflict. Washington would argue that Beijing's success is based on

Balancing the East, Upgrading the West

tyranny and is damaging to the United States' economic well-being; Beijing, meanwhile, would interpret that U.S. message as an attempt to undermine and possibly even fragment the Chinese system. At the same time, China would stress its successful rejection of Western supremacy, appealing to those in the developing world who already subscribe to a historical narrative highly hostile to the West in general and to the United States in particular. Such a scenario would be damaging and counterproductive for both countries. Hence, intelligent self-interest should prompt the United States and China to exercise ideological self-restraint, resisting the temptation to universalize the distinctive features of their respective socioeconomic systems and to demonize each other.

The U.S. role in Asia should be that of regional balancer, replicating the role played by the United Kingdom in intra-European politics during the nineteenth and early twentieth centuries. The United States can and should help Asian states avoid a struggle for regional domination by mediating conflicts and offsetting power imbalances among potential rivals. In doing so, it should respect China's special historic and geopolitical role in maintaining stability on the Far Eastern mainland. Engaging with China in a dialogue regarding regional stability would not only help reduce the possibility of U.S.-Chinese conflicts but also diminish the probability of miscalculation between China and Japan, or China and India, and even at some point between China and Russia over the resources and independent status of the Central Asian states. Thus, the United States' balancing engagement in Asia is ultimately in China's interest, as well.

At the same time, the United States must recognize that stability in Asia can no longer be imposed by a non-Asian power, least of all by the direct application of U.S. military power. Indeed, U.S. efforts to buttress Asian stability could prove self-defeating, propelling Washington into a costly repeat of its recent wars, potentially even resulting in a replay of the tragic events of Europe in the twentieth century. If the United States fashioned an anti-Chinese alliance with India (or, less likely, with Vietnam) or promoted an anti-Chinese militarization in Japan, it could generate dangerous mutual resentment. In the twenty-first century, geopolitical equilibrium on the

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Asian mainland cannot depend on external military alliances with non-Asian powers.

The guiding principle of the United States' foreign policy in Asia should be to uphold U.S. obligations to Japan and South Korea while not allowing itself to be drawn into a war between Asian powers on the mainland. The United States has been entrenched in Japan and South Korea for more than 50 years, and the independence and the self-confidence of these countries would be shattered—along with the U.S. role in the Pacific—if any doubts were to arise regarding the durability of long-standing U.S. treaty commitments.

The U.S.-Japanese relationship is particularly vital and should be the springboard for a concerted effort to develop a U.S.-Japanese-Chinese cooperative triangle. Such a triangle would provide a structure that could deal with strategic concerns resulting from China's increased regional presence. Just as political stability in Europe after World War II would not have developed without the progressive expansion of French-German reconciliation to German-Polish reconciliation, so, too, the deliberate nurturing of a deepening Chinese-Japanese relationship could serve as the point of departure for greater stability in the Far East.

In the context of this triangular relationship, Chinese-Japanese reconciliation would help enhance and solidify more comprehensive U.S.-Chinese cooperation. China knows that the United States' commitment to Japan is steadfast, that the bond between the two countries is deep and genuine, and that Japan's security is directly dependent on the United States. And knowing that a conflict with China would be mutually destructive, Tokyo understands that U.S. engagement with China is indirectly a contribution to Japan's own security. In that context, China should not view U.S. support for Japan's security as a threat, nor should Japan view the pursuit of a closer and more extensive U.S.-Chinese partnership as a danger to its own interests. A deepening triangular relationship could also diminish Japanese concerns over the yuan's eventually becoming the world's third reserve currency, thereby further consolidating China's stake in the existing international system and mitigating U.S. anxieties over China's future role.

Given such a setting of enhanced regional accommodation and assuming the expansion of the bilateral U.S.-Chinese relationship,

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three sensitive U.S.-Chinese issues will have to be peacefully resolved: the first in the near future, the second over the course of the next several years, and the third probably within a decade or so. First, the United States should reassess its reconnaissance operations on the edges of Chinese territorial waters, as well as the periodic U.S. naval patrols within international waters that are also part of the Chinese economic zone. They are as provocative to Beijing as the reverse situation would be to Washington. Moreover, the U.S. military's air reconnaissance missions pose serious risks of unintentional collisions, since the Chinese air force usually responds to such missions by sending up fighter planes for up-close inspection and sometimes harassment of the U.S. planes.

Second, given that the continuing modernization of China's military capabilities could eventually give rise to legitimate U.S. security concerns, including over U.S. commitments to Japan and South Korea, the United States and China should engage in regular consultations regarding their long-term military planning and seek to craft measures of reciprocal reassurance.

Third, the future status of Taiwan could become the most contentious issue between the two countries. Washington no longer recognizes Taiwan as a sovereign state and acknowledges Beijing's view that China and Taiwan are part of a single nation. But at the same time, the United States sells weapons to Taiwan. Thus, any long-term U.S.-Chinese accommodation will have to address the fact that a separate Taiwan, protected indefinitely by U.S. arms sales, will provoke intensifying Chinese hostility. An eventual resolution along the lines of former Chinese leader Deng Xiaoping's well-known formula for Hong Kong of "one country, two systems," but redefined as "one country, several systems," may provide the basis for Taipei's eventual reassociation with China, while still allowing Taiwan and China to maintain distinctive political, social, and military arrangements (in particular, excluding the deployment of People's Liberation Army troops on the island). Regardless of the exact formula, given China's growing power and the greatly expanding social links between Taiwan and the mainland, it is doubtful that Taiwan can indefinitely avoid a more formal connection with China.

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TOWARD RECIPROCAL COOPERATION

MORE THAN 1,500 years ago, during the first half of the first millennium, the politics of the relatively civilized parts of Europe were largely dominated by the coexistence of the two distinct western and eastern halves of the Roman Empire. The Western Empire, with its capital most of the time in Rome, was beset by conflicts with marauding barbarians. With its troops permanently stationed abroad in extensive and expensive fortifications, Rome was politically overextended and came close to bankruptcy midway through the fifth century. Meanwhile, divisive conflicts between Christians and pagans sapped Rome's social cohesion, and heavy taxation and corruption crippled its economic vitality. In 476, with the killing of Romulus Augustulus by the barbarians, the by then moribund Western Roman Empire officially collapsed.

During the same period, the Eastern Roman Empire—soon to become known as Byzantium—exhibited more dynamic urban and economic growth and proved more successful in its diplomatic and security policies. After the fall of Rome, Byzantium continued to thrive for centuries. It reconquered parts of the old Western Empire and lived on (although later through much conflict) until the rise of the Ottoman Turks in the fifteenth century.

Rome's dire travails in the middle of the fifth century did not damage Byzantium's more hopeful prospects, because in those days, the world was compartmentalized into distinct segments that were geographically isolated and politically and economically insulated from one another. The fate of one did not directly and immediately affect the prospects of the other. But that is no longer the case. Today, with distance made irrelevant by the immediacy of communications and the near-instant speed of financial transactions, the well-being of the most advanced parts of the world is becoming increasingly interdependent. In our time, unlike 1,500 years ago, the West and the East cannot keep aloof from each other: their relationship can only be either reciprocally cooperative or mutually damaging. 🌐

The Failure of the Euro

The Little Currency That Couldn't

Martin Feldstein

THE EURO should now be recognized as an experiment that failed. This failure, which has come after just over a dozen years since the euro was introduced, in 1999, was not an accident or the result of bureaucratic mismanagement but rather the inevitable consequence of imposing a single currency on a very heterogeneous group of countries. The adverse economic consequences of the euro include the sovereign debt crises in several European countries, the fragile condition of major European banks, high levels of unemployment across the eurozone, and the large trade deficits that now plague most eurozone countries.

The political goal of creating a harmonious Europe has also failed. France and Germany have dictated painful austerity measures in Greece and Italy as a condition of their financial help, and Paris and Berlin have clashed over the role of the European Central Bank (ECB) and over how the burden of financial assistance will be shared.

The initial impetus that led to the European Monetary Union and the euro was political, not economic. European politicians reasoned that the use of a common currency would instill in their publics a greater sense of belonging to a European community and that the shift

MARTIN FELDSTEIN is George F. Baker Professor of Economics at Harvard University and President Emeritus of the National Bureau of Economic Research. He was Chair of the Council of Economic Advisers from 1982 to 1984. This article is adapted from an NBER working paper, "The Euro and European Economic Performance."

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of responsibility for monetary policy from national capitals to a single central bank in Frankfurt would signal a shift of political power.

The primary political motive for increased European integration was, and may still be, to enhance Europe's role in world affairs. In 1956, just after the United States forced France and the United Kingdom to withdraw their forces from the Suez Canal, German Chancellor Konrad Adenauer told a French politician that individual European states would never be leading global powers, but "there remains to them only one way of playing a decisive role in the world; that is to unite to make Europe. . . . Europe will be your revenge." One year later, the Treaty of Rome launched the Common Market.

The Common Market expanded in 1967 to form the European Communities, and then, in 1992, the Maastricht Treaty gave rise to the European Union, which created a larger free-trade area, provided for the mobility of labor, and set a timetable for adopting a single currency and an integrated European market for goods and services. The European Commission cast this arrangement as a steppingstone toward greater political unity and made the specious argument that the free-trade area could succeed only if its member countries used a single currency. (There is, of course, nothing in economic logic or experience that implies that free trade requires a single currency. The North American Free Trade Agreement, for example, has stimulated increased trade without anyone thinking that the United States, Canada, and Mexico should have a single currency.)

Germany resisted the decision to create a single currency, reluctant to give up the deutsche mark and the price stability and prosperity it had brought to the country's postwar economy. But Germany eventually gave in, and France and others succeeded in establishing a schedule that would lead to the launching of the euro in 1999. Germany was, however, able to influence some of the characteristics of the ECB: the bank's formal independence, its single policy goal of price stability, the prohibition on purchasing bonds from member governments, a "no bailout" rule for countries that became insolvent, and its location in Frankfurt. Germany also forced the creation of a stability agreement that established financial penalties for any country that had a budget deficit of more than three percent of its GDP or a debt that exceeded 60 percent of its GDP. When France and

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Germany soon violated these conditions, the Council of Ministers voted not to impose penalties, and the terms of the pact were weakened so that they became meaningless.

A DEATH FORETOLD

LONG BEFORE the euro was officially introduced, economists pointed to the adverse effects that a single currency would have on the economies of Europe. (See, for example, my *Economist* article from 1992, “The Case Against the Euro,” or my essay from these pages, “EMU and International Conflict,” November/December 1997.) Single currencies require all the countries in the monetary union to have the same monetary policy and the same basic interest rate, with interest rates differing among borrowers only due to perceived differences in credit risk. A single currency also means a fixed exchange rate within the monetary union and the same exchange rate relative to all other currencies, even when individual countries in the monetary union would benefit from changes in relative values. Economists explained that the euro would therefore lead to greater fluctuations in output and employment, a much slower adjustment to declines in aggregate demand, and persistent trade imbalances between Europe and the rest of the world. Indeed, all these negative outcomes have occurred in recent years.

Here is why: when a county has its own monetary policy, it can respond to a decline in demand by lowering interest rates to stimulate economic activity. But the ECB must make monetary policy based on the overall condition of all the countries in the monetary union. This creates a situation in which interest rates are too high in those countries with rising unemployment and too low in those countries with rapidly rising wages. And because of the large size of the German economy relative to others in Europe, the ECB’s monetary policy must give greater weight to conditions in Germany in its decisions than it gives to conditions in other countries.

The tough anti-inflationary policy of the ECB caused interest rates to fall in countries such as Italy and Spain, where expectations of high inflation had previously kept interest rates high. Households and governments in those countries responded to the low interest rates by increasing their borrowing, with households using the increased debt to

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finance a surge in home building and housing prices and the governments using it to fund larger social programs.

The result was rapidly rising ratios of public and private debt to GDP in several countries, including Greece, Ireland, Italy, and Spain. Despite the increased risk to lenders that this implied, global capital markets did not respond by raising interest rates on those countries with increasing debt levels. Bond buyers assumed that a bond issued by one government in the European Monetary Union was equally safe as a bond issued by any other government in the union, ignoring

Market dynamics put in motion a self-reinforcing process in which rising interest rates led countries to the brink of insolvency.

the “no bailout” provision of the Maastricht Treaty. As a result, the interest rates on Greek and Italian bonds differed from the rate on German bonds by only a small fraction of a percent.

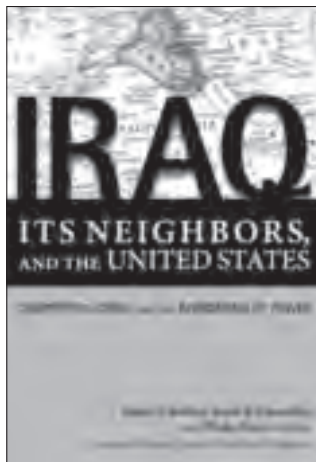
Before the monetary union was put in place, large fiscal deficits generally led to higher interest rates or declining exchange rates. These market signals acted as an automatic warning for countries to reduce their borrowing. The monetary union eliminated

those market signals and precluded the higher cost of funds that would otherwise have limited household borrowing. The result was that countries borrowed too much and banks loaned too much on overpriced housing.

When, in early 2010, the markets recognized the error of regarding all the eurozone countries as equally safe, interest rates began to rise on the sovereign debts of Greece, Italy, and Spain. Market dynamics put in motion a self-reinforcing process in which rising interest rates led countries to the brink of insolvency. In particular, the fear that Greece might have trouble meeting its debt payments caused the interest rate on Greek debt to rise; the expectation of higher future interest payments implied an even larger future debt burden. What started as a concern about a Greek liquidity problem—in other words, about the ability of Greece to have the cash to meet its next interest payments—became a solvency problem, a fear that Greece would never be able to repay its existing and accumulating debt. That pushed interest rates even higher and led eventually to a negotiated partial default, in which



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The Failure of the Euro

some holders of Greek sovereign debt agreed to accept a 50 percent write-down in the value of their bonds. In turn, the Greek experience raised the perceived risk of Italian government debt, causing the interest rate on Italian government bonds to rise from less than four percent in April 2010 to more than seven percent in November 2011—a rate that will cause government debt to rise faster than national income, pushing Italy to the brink of insolvency.

A different market dynamic affected the relationship between European commercial banks and European governments. Since the banks were heavily invested in government bonds, the declining value of those bonds hurt the banks. The banks then turned to their governments to protect their depositors and other creditors, thus magnifying the original problem. In Ireland and Spain, this cycle began with mortgage defaults, harming the banks and leading governments to guarantee the holdings of the banks' depositors and other creditors, thus adding to government debt. The banks' heavy investment in government bonds then meant that the weakness of Irish and Spanish government debt further hurt the banks.

THE EURO ON LIFE SUPPORT

BY THE fall of 2011, several European countries had debt-to-GDP ratios that were high enough to make default a serious possibility. Sharp write-downs in the value of their sovereign debts are not a feasible solution because they would do substantial damage to European banks and possibly to banks and other financial institutions in the United States.

European political leaders have proposed three distinct strategies to deal with this situation. First, led by German Chancellor Angela Merkel and French President Nicolas Sarkozy, eurozone officials agreed last October that commercial banks should increase their capital ratios and that the size of the European Financial Stability Facility (EFSF), which had been created in May 2010 to finance government borrowing by Greece and other eurozone countries, should be expanded from 400 billion euros to more than a trillion euros. This latter move was meant to provide insurance guarantees that would allow Italy and potentially Spain to access capital markets at reasonable interest rates.

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But the plan to increase the banks' capital has not worked, because banks do not want to dilute the holdings of their current shareholders by seeking either private or public capital, and so instead they have been raising their capital ratios by reducing their lending, particularly to borrowers in other countries, causing a further slowdown in European economic activity. Nor can the EFSF borrow the additional funds, since such a move is opposed by Germany, the largest potential guarantor of that debt. Moreover, even a trillion euros would not give the EFSF enough funds to provide effective guarantees to potential buyers of Italian and Spanish debt if those countries might otherwise appear insolvent.

The second strategy, advocated by France, calls for the ECB to buy the bonds of Italy, Spain, and other countries with high debt to keep their interest rates low. The ECB has already been doing this to a limited extent, but not enough to stop Greek and Italian rates from reaching unsustainable levels. Asking the ECB to expand this policy would directly contradict the "no bailout" terms of the Maastricht Treaty. Germany opposes such a move because of its inflationary potential and the risk of losses on those bonds. (Two German members of the ECB's executive board have resigned over this issue.)

The third strategy is favored by those figures, such as Merkel, who want to use the current crisis to advance the development of a political union. They call for a fiscal union in which those countries with budget surpluses would transfer funds each year to the countries running budget deficits and trade deficits. In exchange for these transfers, the European Commission would have the authority to review national budgets and force countries to adopt policies that would reduce their fiscal deficits, increase their growth, and raise their international competitiveness.

This transfer arrangement has already happened with Greece and Italy. The case of Greece has been the most dramatic. By last October, Greece was unable to borrow in the global capital market and therefore had to depend on credit extended by the ECB and the International Monetary Fund to pay civil servants and maintain its social welfare programs. Merkel and Sarkozy summoned Greek Prime Minister George Papandreou to Brussels and told him that he must abandon the plan he had announced to hold a national referendum on the austerity measures being imposed by the other eurozone members.

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They told him that instead he must persuade the Greek parliament to accept the tough strategy to reduce the budget deficit created by Merkel and Sarkozy or face expulsion from the eurozone. Papandreou agreed and forced the necessary legislation through parliament. He then resigned, and Lucas Papademos, a former vice president of the ECB, was appointed as a temporary prime minister with the responsibility of implementing the budget cuts designed in Brussels. But the subsequent parliamentary defections and public riots have shown how much the Greek people resent being forced by Germany to change their economic behavior, accept layoffs of government employees who thought they had lifetime jobs, and reduce demand at a time of double-digit unemployment and rapidly falling GDP. At the same time, many voters in Germany resent sending money to the Greeks and seeing the rules of the ECB undergo radical change.

The situation in Italy is different because Italy is not yet dependent on explicit transfers from the ECB or the International Monetary Fund. But Italy does depend on the support of the ECB to limit the rise of the interest rate for its government bonds. France and Germany pressured Italy to adopt new budget policies, leading to the resignation of Prime Minister Silvio Berlusconi in November and the appointment of a technocrat government committed to resolving Italy's fiscal problems. The euro has thus caused tensions and conflicts within Europe that would not otherwise have existed. Further steps toward a permanent fiscal union would only exacerbate these tensions.

GREECE'S IMPOSSIBLE MATH

GREECE'S BUDGET deficit of nine percent of GDP is too large to avoid an outright default on its national debt. With Greece's current debt-to-GDP ratio at 150 percent and the current value of Greece's GDP falling in nominal euro terms at an annual rate of four percent, the debt ratio will rise in the next year to 170 percent of GDP. Rolling over the debt as it comes due and paying higher interest rates on it would raise the total debt even more quickly.

Even if a more general write-down of Greek debt were to cut Greece's existing interest payments in half, the deficit would still be six percent of Greece's GDP and the debt-to-GDP ratio would rise to

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165 percent of GDP at the end of 12 months. And this does not even take into account the adverse effect the debt write-down would have on Greek banks. The Greek government would be forced to provide payments to Greek depositors, further increasing the national debt.

To achieve a sustainable path, Greece must start reducing the ratio of its national debt to GDP. This will be virtually impossible as long as Greece's real GDP is declining. Basic budget arithmetic implies that even if Greece's real GDP starts growing at two percent (up from the current seven percent real rate of decline) and inflation is at the ECB target of two percent, the deficit must still not exceed six percent of GDP if the debt ratio is to stop increasing. Since the interest alone on the debt is now about six percent of GDP, the rest of the Greek budget must be brought into balance from its current three percent deficit.

Cutting the interest bill in half and simultaneously balancing the rest of the budget would reduce the ratio only very slowly, from 150 percent now to 145 percent after a year, even if no payments to bank depositors and other creditors were required. It is not clear that financial markets will wait while Greece walks along this fiscal tightrope to a sustainable debt ratio well below 100 percent.

The situation in Italy is much better. Italy already has a slightly positive growth rate and a primary budget surplus, with tax revenues exceeding noninterest government outlays by about one percent of GDP. The country's total budget deficit is about four percent of GDP; a reduction of the deficit equivalent to two percent of GDP would be enough to begin reducing the ratio of debt to GDP. That should not be difficult to achieve, since government spending accounts for roughly 50 percent of GDP. The prospect of a declining budget deficit has already reduced the interest rate on new government borrowing from 7.5 percent to 6.5 percent. Eliminating the budget deficit and starting to shrink the debt ratio more rapidly could bring the interest rate back to the four percent level that prevailed in Italy before the crisis began.

TRADING PLACES

EVEN IF the eurozone countries reduced their large budget deficits and thereby alleviated the threat to the commercial banks that have invested in government bonds, another problem caused by the monetary union



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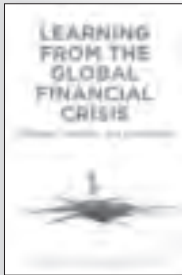


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would remain: the differences among eurozone members in terms of long-term competitiveness, which leads to sustained differences in trade balances that cannot be financed.

During the past year, Germany had a trade surplus of nearly \$200 billion, whereas the other members of the eurozone had trade deficits totaling \$200 billion. A more comprehensive measure that factors in net investment income reveals that Germany has a current account surplus of five percent of GDP, whereas Greece has a current account deficit of nearly ten percent of GDP. Put another way, Germany can invest in the rest of the world an amount equal to five percent of its GDP, whereas Greece must borrow an amount equal to nearly ten percent of its GDP to pay for its current level of imports.

If Greece were not part of the eurozone, its exchange rate would adjust over time to prevent this large and growing trade deficit. More specifically, the need to finance that trade deficit would cause the value of the Greek currency to decline, making Greek exports more attractive to foreign buyers and encouraging Greek consumers to substitute Greek goods and services for imports. The rising cost of imports would also reduce real personal incomes in Greece, leading to lower consumer spending and freeing up Greek goods and services to be exported to foreign buyers.

But since Greece is part of the eurozone, this automatic adjustment mechanism is missing. Greece faces the persistent problem of a rising current account deficit, which has now reached ten percent of GDP, because Greece's productivity (output per employee) increases more slowly than Germany's, causing the prices of Greek goods to rise relative to the prices of German and other European goods. More specifically, if output per employee in Germany increases by three percent a year, real wages can also grow by three percent. If the ECB keeps inflation in the eurozone at about two percent, German wages can rise by five percent a year. If Greek wages also rise by five percent a year while productivity in Greece grows by only one percent a year, the prices of Greek goods and services will increase two percent faster than the prices of German products. That increase in the relative prices of goods and services would cause Greek imports to rise and exports to stagnate, creating an increasingly large trade deficit. This problem could be avoided if the annual rise in Greek wages were limited to two

Martin Feldstein

percent less than the rise in German wages. This may, of course, be politically difficult in the highly unionized Greek economy.

But limiting the growth of Greek wages would address only further deterioration of Greek competitiveness in the future. Stopping a further decline in Greek competitiveness would not correct the existing annual current account deficit of nearly ten percent of GDP that Greece must continue to finance. Eliminating the existing current account deficit would require making Greek prices much more competitive than they are today, by reducing the cost of producing Greek goods and services by about 40 percent relative to the cost of producing goods and services in the rest of the eurozone. Since that is not likely to be achieved by increased productivity, it must be achieved by lowering real wages relative to the real wages of Germany and other countries in the eurozone. This would be a very painful process, achieved at the cost of years of high unemployment and declining incomes. Greece now has an official unemployment rate of 16 percent, and its real GDP is falling by seven percent per year. Continuing such poor performance for a decade or more is virtually unthinkable in a democracy. Moreover, since such a process would shrink the current account deficit only over a long period of time, Greece would need to continue borrowing to finance its current account imbalance. Even if Germany were willing to formalize such long-term financial assistance by establishing a transfer union to provide those funds, the controls that Berlin would demand to keep wages and incomes declining would create severe political tensions between Germany and Greece.

THE TEMPTATION OF DEVALUATION

THE ALTERNATIVE is for Greece to leave the eurozone and return to its own currency. Although there is no provision in the Maastricht Treaty for such a move, political leaders in Greece and other countries are no doubt considering that possibility. Although Greece is benefiting from its membership in the eurozone by receiving transfers from other eurozone countries, it is paying a very high price in terms of unemployment and social unrest. Abandoning the euro now and creating a new drachma would permit a devaluation and a default that might involve much less economic pain than the current course. This devaluation-and-default strategy has been the standard response of countries in Asia and

The Failure of the Euro

Latin America with unsustainably large fiscal and trade deficits; they were able to devalue because they were not part of a monetary union.

Germany is now prepared to pay to try to keep Greece from leaving the eurozone because it fears that a Greek defection could lead to a breakup of the entire monetary union, eliminating the fixed exchange rate that now benefits German exporters and the German economy more generally. If Greece leaves and devalues, global capital markets might assume that Italy will consider a similar strategy. The resulting rise in the interest rate on its debt might then drive Italy to in fact do so. And if Italy reverts to a new lira and devalues it relative to other currencies, the competitive pressure might force France to leave the eurozone and devalue a new franc. At that point, the EMU would collapse.

Even though Germany is prepared to subsidize Greece and other countries to sustain the euro, Greece and others might nevertheless decide to leave the monetary union if the conditions imposed by Germany are deemed too painful. Here is how that might work: although Greece cannot create the euros it needs to pay civil servants and make transfer payments, the Greek government could start creating new drachmas and declare that all contracts under Greek law, including salaries and shop prices, are payable in that currency; similarly, all bank deposits and bank loans would be payable in these new drachmas instead of euros.

The value of the new drachma would fall relative to the euro, automatically reducing real wages and increasing Greek competitiveness without requiring Greece to go through a long and painful period of high unemployment. Instead, the lower value of the Greek currency would stimulate exports and a shift from imports to domestic goods and services. This would boost Greek GDP growth and employment.

Withdrawing from the eurozone would of course be difficult and potentially painful. The announcement that Greece was leaving the eurozone would have to come as a surprise—otherwise, a bank run would be likely, as Greek depositors would have the time to move their euro-denominated funds to banks outside Greece or to withdraw them and hold euros in cash. Since some flight of deposits from Greek banks is already happening, Athens would have to act before this became a flood of withdrawals.

Another serious problem for Greece in making the transition to the new drachma would be the political risk of being forced out of the EU.

Martin Feldstein

Since the Maastricht Treaty provides no way for a member of the eurozone to leave, there is the risk that the other eurozone members would punish Greece by requiring it to leave the EU as well, causing Greece to lose the benefits that the EU offers of free trade and labor mobility. They might do so to discourage Italy and others from pursuing a similar exit strategy. But not all EU members would necessarily seek such a punishment, especially since ten of the 27 EU member countries do not use the euro and Greece's situation is clearly more desperate than that of Italy or Spain.

The primary practical problem with leaving the eurozone would be that some Greek businesses and individuals have borrowed in euros from banks outside Greece. Since those loans are not covered by Greek law, the Greek government cannot change these debt obligations from euros to new drachmas. The decline in the new drachma relative to the euro would make it much more expensive for Greek debtors to repay those loans. Widespread bankruptcies of Greek individuals and businesses could result, with secondary effects on the Greek banks that those individuals and businesses have borrowed from.

But as the experience of Argentina after it ended its link to the dollar in 2002 showed, domestic Greek debtors might end up paying only a fraction of those euro debts. For Greece, the option to leave the monetary union may therefore be very tempting.

Greece's departure need not tempt Italy, Spain, or others to leave. For them, the cost of leaving could exceed that of adjusting their economies while remaining inside the eurozone. Unlike Greece, they can avoid insolvency by adjusting their budget and trade deficits without radical changes in policy.

Looking ahead, the eurozone is likely to continue with almost all its current members. The challenge now will be to change the economic behavior of those countries. Formal constitutionally mandated balanced-budget rules of the type recently adopted by Germany, Italy, and Spain would, if actually implemented, put each country's national debt on a path to a sustainable level. New policies must avoid current account deficits in the future by limiting the volume of national imports to amounts that can be financed with export earnings and direct foreign investment. Such measures should make it possible to sustain the euro without future crises and without the fiscal transfers that are now creating tensions within Europe. 🌐

AUSTRALIA



AUSTRALIA

RESILIENT ECONOMY, ENDURING PARTNER

By The Honorable Kevin Rudd MP

Recent economic history looks different from the perspective of Australia. Unlike other developed countries, Australia emerged unscathed from the global financial crisis that struck in 2008, and our economy did not fall into recession.

An open investment climate, flexible markets, a diverse economy, and effective regulatory systems—these characteristics of our economy served us well. As other economies fell back, Australia was able to stimulate the economy without taking on dangerous levels of national debt.

This strength, in the



Kevin Rudd, Australian minister for foreign affairs

face of economic turmoil unprecedented for more than seventy years, was not something that came to Australia by chance.

It was the legacy of economic reforms undertaken by the Hawke and Keating governments in the 1980s: tearing down our tariff walls, opening our economy to international competition, opening us up to Asia.

By being unafraid of competition, and unafraid to make our own way in Asia, Prime Ministers Hawke and Keating gave our economy strengths that have served us so well in this decade. Their push for open regionalism

was exemplified through their proposing and championing of the foundation of APEC, giving us an economy deeply engaged with our region.

Australia's economic integration with Asia is now broadening and deepening. This century will be the Asian Century and Australia is well positioned for the opportunities and challenges that this will bring.

The remarkable evolution of our relationship with Asia is adding a new dimension to our relationship with the United States. In his recent visit to Australia, President Obama made it clear that the United States, too, has embarked on a strategic shift to the Asia Pacific.

President Obama's "Canberra Doctrine," as reflected in the context of his address to the Australian Parliament on November 17, 2011, that the United States will not reduce its strategic posture in the Asia Pacific (despite what reductions might occur elsewhere), will be regarded as a critical turning point in the history of the Asian hemisphere.

The success of Australian and American business owes much to well-established rules and an even playing ground, fostering open competition and ingenuity. Modern Asia understands the relationship between openness and growth—which is why we have seen the spread of liberalism and democracy through Asia since the end of the Second World War.

Through APEC, and now through the East Asia Summit,

we have the right forums, with the right mandate and membership, to continue to build security and prosperity in Asia.

The challenge for this Asia-Pacific century is to preserve the peace in order to build our common prosperity.

Australia, as the fourth-largest economy in Asia, is a

critical partner with the United States in achieving that goal.

And the key challenge for us both is to realize that goal through constructive, cooperative engagement with a China that remains open to both the region and the world. And therein lies the core task for the exciting century that lies before us.

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We generate hydropower and wind power in the state of Tasmania and trade electricity and energy-related environmental products in the Australian market.

We are also Australia's largest water manager.

Through our consulting arm Entura, we offer power engineering, renewable energy, water and environmental solutions to governments, utilities, developers and international companies in Australia and around the world with a strong presence in the Asia-Pacific region.

You can find out more about the Hydro Tasmania group at www.hydro.com.au

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Hotbed of life-saving innovation

While Australia's growth spree can be attributed to the massive global demand for its mineral resources and prudent fiscal policies, much credit is given to its focus on innovation, especially in the fields of renewable energy and biotechnology.

"Australia's true prosperity is based on how we have transformed our natural endowments to build an economy that relies on skills, knowledge, and innovation," said Prime Minister Julia Gillard.

Set up in 2004, Mesoblast specializes in adult stem-cell research, and has multiple products in middle-to-late stages across such diverse areas as cardiovascular disease, orthopedics, diabetes, and immune conditions.

In just seven years, it has become Australia's seventy-fifth-largest company and fourth-largest life science company, with a market capitalization of \$2.6 billion.

The company produces stem cells that trigger regenerative cells and support the local tissue to repair itself. These stem cells can be expended in very large

numbers from a tiny number of cells and do not activate the immune system when implanted from one person to another.

In terms of strategy, Chief Executive Professor Silviu Itescu has built a business model around a cell type that lowers risk by outsourcing different parts of the production process, which allows Mesoblast to focus on R&D.

From day one, it contracted manufacturing to leading biologics manufacturer Lansia and forged a partnership in cardiovascular and neurological applications with Cephalon, one of the world's top pharmaceutical distributors.

"Mesoblast is a late-stage life sciences company that has been substantially de-risked. We have global pharmaceutical distribution partners sharing the heavy load at the front end on cardiovascular and neurological programs. We are well resourced financially to unlock full value from our technology by accelerating new programs such as Type 2 diabetes and lung diseases," says Itescu.

"All of that creates the kind of

de-risking that allows us now to move to the next level as a real global biologics company. We are clearly the world's largest regenerative medicine company and the fact that we can do that in Australia says a lot about the strengths of Australian science and the strengths of Australian entrepreneurship," he adds.

With parliament passing a carbon emissions trading scheme, renewable energy has assumed greater importance to Australian industry.

In fact, the Gillard government is committed to ensuring that 20 percent of Australia's electricity supply will come from renewable energy by 2020.

Founded in Tasmania almost a century ago, Hydro Tasmania has become Australia's largest water resources manager, and currently supplies 46 percent of the country's renewable energy.

And since 1998, Hydro Tasmania has exported its expertise through its consultancy arm, Entura.

"We sell consulting services in Tasmania, in mainland Australia, and also internationally,

where there is significant hydro potential. For example, if you look at Africa, only 7 percent of the hydro potential is currently tapped, while in Southeast Asia, it is only 30 percent. That gives us a range of opportunities for Entura," says CEO Roy Adair.

Hydro Tasmania also specializes in other remote-area power supply solutions, whether it be wind, solar, or bio-diesel.

Adair believes that as Australia moves towards its "20 by 2020" goal, 70 percent of its energy supply will be wind generated. Therefore, Hydro Tasmania has consolidated its wind farms.

Through companies like Hydro Tasmania, Australia is well placed to show the world how to effectively combine renewable energy resources with nonrenewables.

"We'll be delighted to talk to any parties that are interested in tapping into the potential for sustainable energy production around the world by the use of the expertise that we have. We'll be delighted to share that expertise with them and utilize it so that we can build commercially sustainable solutions," said Adair.



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Australian education: a bridge in the Indo-Pacific age

With the Indian Ocean to its west and the Pacific Ocean to its east, Australia is, by a stroke of geographical fortune, located at the crossroads of an immense area that encompasses the global economy's high-growth regions: India and the Middle East, China, and the rest of East Asia.

As the Asian Century has evolved into the Asia-Pacific Century over the past decade, analysts have begun speaking of the advent of an Indo-Pacific age.

And in this increasingly interdependent global economy, governments have developed and promoted every industry to remain competitive. Even schools and universities have evolved from their original purpose—educating—to become multimillion-dollar contributors to national economies.

In resource-rich Australia, which has been supplying vital coal and minerals to rapidly developing China and India, the education sector has become the country's third-largest export earner, with Asian students emerging as the most significant contributor to the growth of revenue.

In fact, the country is widely regarded as a pioneer of commercialization of its educational institutions, which it has been undertaking since the mid-1980s.

While it's true that Australia is conveniently located, international students also come to the country because of the impressive reputation of its schools.

In the latest Times Higher Education World University Rankings, seven Australian universities made it to the top 200,

among them Australian National University, University of Sydney, and Monash University.

"It's not just the English-speaking environment; we have also the world's top universities. We have at least a half-dozen, and I don't think you can find many other universities in the East Asian hemisphere that are in the top 100," said Foreign Minister Kevin Rudd.

"Our university sector is mature but still rapidly expanding. One of the things the government has done in the last several years is to invest in the capital universities," Rudd added.

Australia's largest

Established in 1958, Monash University in Melbourne has attracted the largest number of students from within and outside Australia. It has grown to become the largest university in the country, with more campuses across the globe than any of its domestic counterparts.

Ranked in the top 1 percent of the Times Higher Education World University Rankings, Monash has six local campuses in the state of Victoria, established two campuses in Malaysia and South Africa, and set up international centers in Italy and India.

The school is renowned for its Masters in Business Administration, the flagship program of the Faculty of Business and Economics introduced in 1968.

"The Monash MBA program is generalist in nature and emphasizes breadth of business and management concepts and techniques rather than depth of knowledge in one or two areas,"

"It's not just the English-speaking environment; we have also the world's top universities. We have at least a half-dozen in the East Asian hemisphere that are in the top 100."

— Foreign Minister Kevin Rudd

said Dr. Jane Sherlock-Holcombe, MBA Program Manager.

"The program is designed to provide current and aspiring managers with an educational experience to prepare them for leadership positions within a variety of organizations. It is a professional degree that provides an environment where students are able to share and learn from each other's professional and organizational experiences," she added.

With the ever-changing business environment and new issues facing a highly-globalized and heavily-industrialized world, Monash MBA launched a new curriculum last year that gives a greater emphasis and integrated focus on ethics and sustainability, leadership, innovation and strategic decision-making.

To complement the comprehensive education of its students, Monash MBA has fostered links with business and industry, both in Australia and abroad, provid-

ing all its students with opportunities for experiential learning and research collaboration.

Among those partners are The Indian Institute of Technology Bombay (IITB), Neural Diagnostics, GlaxoSmithKline, Victoria Police, IBM, Oxfam, the Australian Senior Human Resources Roundtable, AusAID, GM Holden, the Australian Conservation Foundation, and China Aluminum Corporation.

It also has alliances with Warwick University and Newcastle Business School, both in the United Kingdom.

The country's first

The University of Sydney enjoys the prestige of being the first university in Australia. In over a century and half, the school has grown to become one of the world's premier learning institutions, in terms of size and range of disciplines.

"We are unusual in that we

CONTINUED ON FOLLOWING PAGE

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Australian education: a bridge in the Indo-Pacific age

CONTINUED FROM PRECEDING PAGE

teach everything—from astrophysics to speech pathology. That gives us unique opportunities to think about the problems the world is facing through a multidisciplinary perspective. And we are about to invest close to half a billion dollars in research and teaching,” said Dr. Michael Spence, vice chancellor and principal.

Founded in 1850, the University of Sydney runs ten campuses scattered across the city, and has about 50,000 students and 7,000 faculty members. Of its students, 11,000 are from outside Australia, with 6,000 of them coming from China.

Although the university has become a top preference for students from the region, the University of Sydney has maintained strong and long-standing ties with the United States, still a valuable source of information and cooperation.

“The U.S. Studies Center has been enormously successful, not only as a place for both business and public engagement and research and teaching of the United States, but also as a place for vari-

ous American academics to come and think about their own country from a distance,” Spence said.

“We have affiliation agreements with about fifty-six major research institutions across the U.S. The connection with the United States is very strong,” he added.

Among the flagship programs of the university is its business school. Spence believes that the University of Sydney holds a huge competitive edge borne out of its cultural heritage and geographical location.

“One of the things that is interesting in Australian business education is that it stands again between the European tradition of the university-based business school and the American business administration school,” Spence said.

Leading the political debate

Through its Asia Research Centre, Murdoch University has established an international reputation of being an expert on social, political, and economic changes taking place in contemporary Asia and the various forces, interests,

and conflicts driving this change.

Set up in 1991, the Asia Research Centre attracts continuous income via academic foundations, consultancy revenue, philanthropic donations, as well as support from Murdoch University in Perth.

The center produces high-quality academic research publications for international and domestic audiences, fosters the development of high-quality research graduates, and constructively contributes to public policy debate and public understanding of issues concerning contemporary Asia.

Scholars at Murdoch University are known for their distinctive theoretical approach to comparative political economy, which emphasizes dynamic social conflicts and alliances associated with contemporary forms of capitalist development.

Students also benefit from engagement with researchers and proponents of that approach through the Masters of Arts in Globalization and Governance, the Master of Arts in Development Studies, and the Master of

Arts in Security Studies.

The Murdoch School, as it is sometimes called, has also attracted many PhD students, which has resulted in important contributions to the refinement and extension of this evolving approach.

The Asia Research Centre is at the heart of a large and growing international research network that includes former faculty, PhD students, and other research colleagues.

In the past decade, much of the collaboration happened via alliances with counterpart research centers, which included those at City University of Hong Kong, University of Hong Kong, National University of Singapore, Warwick University, University of North Carolina, and the Institute of Social Studies at The Hague.

Recently, it received the Australian Development Research Award from the Australian Agency for International Development for its project “Achieving Sustainable Demand for Governance: Addressing Political Dimensions of Change.”

ANU – at the heart of politics

The School of Politics and International Relations at the Australian National University offers Masters and PhD programs in Politics and International Relations through coursework, research, or both.

The college has a vibrant community of students undertaking Masters and Doctoral degrees in International Relations and Globalization, Comparative Politics, Public Policy, Political Theory and Australian Politics with some of the best researchers in the world.

The school plans to launch, subject to approval, a multidisciplinary Masters program in Globalization in 2013 that will include options from anthropology, economics, environmental sciences, history, law, sociology, as well as politics and international relations.

Based in the Australian capital, Canberra, students are able to draw on key ANU centers, including those for European and Latin American

Studies, but also on the local diplomatic community and the Australian Government to give their studies further depth and context.

Students also have access to excellent research facilities at ANU as well as national facilities including the National Library and National Archives of Australia.



ANU has an exceptional international reputation for research in politics and international relations.

In the Excellence in Research for Australia’s assessment in 2010, ANU was the only university in the country to receive a score of five out of five, which denotes “outstanding performance well above world standards.”

In the 2011 Times Higher Education World University Rankings, ANU was ranked number one in Australia and number 10 in the world for the study of politics and international relations.



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The program's world standing is reflected in its accreditation by the Association of MBAs (AMBA), an international and impartial accreditation authority for postgraduate business education which sets a global standard for MBA programs.

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A unique core component of the new MBA program is the Corporate Project. Here, emphasis is placed on integrating a student's learning experience and introducing different disciplinary perspectives, together with a focus on actual business problems and the ethical, social and environmental challenges that such problems frequently involve.

For more information about the MBA program, visit www.mba.monash.edu.au



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Postgraduate Studies on Asian Politics at Murdoch University

Political science research at Murdoch University is organised primarily through the Asia Research Centre, one of the most productive concentrations of scholars on Southeast Asian politics worldwide. It pursues theoretically-driven and policy-relevant research on East and Southeast Asia analysing: political and economic regimes; environmental resource governance; ethnic, religious and national identities; media systems; and the sexuality of states and communities.

The Centre's lead role in major international collaborative projects has resulted in a range of highly innovative authored and edited books. This includes the *New Rich in Asia* book series (Routledge), various volumes of *The Political Economy of South-East Asia* (Oxford University Press) and the *Routledge Handbook of Southeast Asian Politics*. Current projects include work on: the political economy of aid effectiveness; natural resource disputes; and accountability reform.

www.arc.murdoch.edu.au

The Centre currently hosts a series of prestigious Australian Research Council fellowships: Australian Professorial Fellow Garry Rodan is researching the politics of representation across Southeast Asia; Future Fellow Veda Hadzi is investigating the politics of populist blame; Post-Doctoral Fellow Shahar Hameiri is analysing the governance of risk in Southeast Asia.

Throughout its twenty-year history, the Centre has been home to a vibrant community of postgraduate research students benefiting from collaborations with a global network of scholars. Murdoch PhDs in Politics include such eminent scholars as professors Armitav Acharya and Mark Beeson.

For more information on research at the Asia Research Centre, PhD programs or coursework postgraduate degrees, visit <http://www.arc.murdoch.edu.au>



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Geo-Graphics

A graphical take on geoeconomic issues, with links to news and expert commentary

Eurozone Bank Deposits Are Fleeing for Germany



Country-based bank regulatory and deposit-insurance schemes are untenable in a common currency area. As the graphic above shows, the market now values euros in a German bank well above euros in a Greek bank. A stable eurozone banking system will require a unified regulatory, resolution, and rescue regime.

Other Geo-Graphics include

- It’s Time to Euthanize Sovereign CDs
- The BRIC Twist Didn’t Work
- Is the U.S. Output Gap Overstated?
- China’s Imbalances Are Bigger than Reckoned

blogs.cfr.org/geographics



When Currencies Collapse

Will We Replay the 1930s or the 1970s?

Barry Eichengreen

THE INTERNATIONAL monetary system rests on just two currencies: the dollar and the euro. Together, they account for nearly 90 percent of the foreign exchange reserves held by central banks and governments. They make up nearly 80 percent of the value of Special Drawing Rights, the reserve asset used in transactions between the International Monetary Fund (IMF) and its members. Of all debt securities denominated in a foreign currency, more than three-quarters are in dollars and euros. The two currencies together account for nearly two-thirds of all trading in foreign exchange markets worldwide. They are the essential lubricants of global trade and finance. Were they not widely accepted, the global economy could not sustain current levels of international trade and investment.

That is why the problems now faced by both currencies are so alarming. Today, more than at any time in recent memory, analysts and investors are voicing doubts about the stability of the dollar and the euro and the international monetary system that depends on them. Consider first the dollar. Faith in its reliability was seriously undermined last summer when the debt-ceiling imbroglio in the United States revealed a seemingly unbridgeable gap between the political parties and raised concerns about the capacity of U.S. policymakers to put the country's financial house in order. Foreign investors, who hold

BARRY EICHENGREEN is George C. Pardee and Helen N. Pardee Professor of Economics and Political Science at the University of California, Berkeley.

Barry Eichengreen

slightly less than half of all marketable U.S. Treasury debt, saw the crisis as proof that members of Congress would rather let the country default on its obligations than compromise on their own partisan objectives. And foreign governments were spooked. As the debate reached a peak, Chinese officials lectured Washington on the need to act responsibly, China's state-run news agency disparaged the negotiations as a "madcap farce of brinkmanship," and Russian Prime Minister Vladimir Putin characterized Americans as "living like parasites off the global economy and their monopoly of the dollar."

Doubts about the euro are even graver. The eurozone is divided into a relatively vigorous northern tier with sound finances and a southern one with crushing debts and nonexistent growth prospects. Europe's indebtedness is no greater than the United States', but unlike the United States, Europe has no federal fiscal system to transfer resources from prosperous to troubled regions—and European leaders seem unwilling to create one. At the same time, they are hesitant to write down unsustainable debts for fear of destabilizing the banks that hold them.

The result is that southern Europe has been left to implement brutal fiscal cuts that are pushing its economies deeper into recession, further impairing their capacity to service their debts. Many southern Europeans, suffering severe hardship, have rebelled against their own governments and accused northern Europe of sacrificing their well-being. Many northern Europeans, meanwhile, see their southern neighbors as spendthrift, lazy, and corrupt. Those northerners have become increasingly vocal in saying so and have concluded that more rescue operations would amount to pouring money down a rat hole.

All this implies that the euro will at best remain the weak currency of a permanently troubled Europe. At worst, slow growth and tensions in the eurozone could ultimately lead countries to abandon the monetary union. Both scenarios would threaten the international monetary system.

Such systems have collapsed before: first in the 1930s and again in the 1970s. The 1930s collapse played a significant role in spurring a worldwide depression that crippled economic activity and fed political extremism. In contrast, the systemic failure of the 1970s, although potentially just as dangerous, had far less catastrophic effects; the global

When Currencies Collapse

economy was wounded, but not mortally. It is crucial to understand these two historical precedents in order to gauge what might happen today if there were full-blown crises of confidence in both the dollar and the euro.

THE 1930S: A DISASTROUS COLLAPSE

THE INTERNATIONAL monetary system of the late 1920s and early 1930s resembled the current system in important ways. It, too, was organized around two currencies: the British pound and the U.S. dollar. With the United Kingdom and the United States making sterling and dollars available—and other countries accumulating them—global foreign exchange reserves more than doubled between 1924 and 1930. Trade credit was readily available, allowing deficit countries to finance additional imports. As a result, during the 1920s, global trade rose twice as fast as global output of goods and services. International capital flows similarly expanded more rapidly than global output, peaking in early 1928.

The boom in trade and in the movement of capital created global imbalances similar to those of recent years. Some surplus countries, notably France, accumulated vast quantities of reserves. Others, such as the United States, recycled their surpluses by lending to the deficit countries of central Europe, mainly Germany. But the deficit countries spent the capital they imported on consumption rather than investment. The world saw the rapid expansion of credit and an alarming run-up in asset prices. As the decade drew to a close, doubts grew about the resilience of this precariously balanced system.

Today's international monetary system has produced similar conditions and concerns. A key difference between the two eras, however, is the role played by gold in the 1930s. At the close of the 1920s, central banks held between 60 and 70 percent of their international reserves in the form of gold. They used that gold, together with foreign exchange reserves, principally bonds issued by the U.S. and British governments and bank deposits in New York and London, as backing for their money supplies. They stood ready, as a matter of legal obligation, to convert their monetary liabilities into gold at a fixed domestic-currency price.

Barry Eichengreen

Concerned about the exuberance of financial markets, the U.S. Federal Reserve began raising interest rates in 1928. As a result, capital flows from the United States to the deficit countries fell off. To prevent their exchange rates from weakening, other central banks had to match the Fed basis point for basis point. As those central banks raised interest rates, credit markets tightened and growth slowed, leading to a reduction in U.S. exports. Economic activity in the United States peaked in the summer of 1929, and the autumn was punctuated by a violent stock market crash. By 1930, most of the world was in recession.

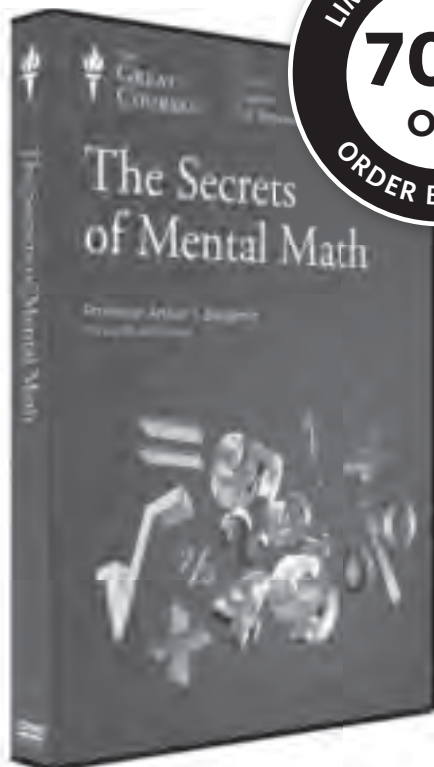
Initially, the international monetary system withstood these pressures. In 1931, however, what had been mainly a crisis of output and

It is crucial to understand the 1930s and the 1970s to gauge what might happen today.

employment suddenly acquired an alarming financial overlay. In May, there was a run on Austria's leading bank, the Creditanstalt. If a bank could go down in Vienna, investors concluded, the same could happen in Berlin, given the superficial similarity of the Austrian and German financial systems. As capital fled and foreign credit become unavailable,

the German government was forced to respond with exchange controls and an agreement, negotiated with foreign bankers, effectively freezing Germany's international loans. British banks had extended some of those loans. Uncertain about the condition of the British banking system, investors began shifting money out of London, steadily draining reserves from the Bank of England. After a pair of belated interest-rate hikes failed to lure back this fleeing capital, the imminent exhaustion of its gold reserves forced the Bank of England to abandon the gold standard in mid-September.

This marked the beginning of the international monetary crisis. Before abandoning the gold standard, the Bank of England had reassured foreign central banks and governments of its unwavering support for the prevailing sterling exchange rate. Having been burned once already, those banks were now not shy about liquidating their sterling balances. Although they could no longer convert them into gold at the Bank of England, they could still dispose of them on the foreign exchange market. The subsequent fire sale drove down the



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sterling exchange rate and magnified the capital losses incurred by holders of sterling. This underscored the risks of holding reserves in foreign currency.

If the United Kingdom could act this way, it was no longer inconceivable that the United States might, too. Thus, in the weeks after

The collapse of the Bretton Woods system in the 1970s did relatively little to slow economic growth.

the British dropped the gold standard, central banks rushed to redeem their dollars for gold at the Federal Reserve. The resulting gold losses forced the Fed to raise interest rates in October, even though the U.S. economy was already in a deep recession. By so curtailing the provision of credit, the Fed contributed to the wave of U.S. bank failures that hit toward the end of 1931. By the end of that

year, central banks had liquidated nearly half of all the foreign exchange reserves they had held a year earlier. The prevailing international monetary system had imploded.

As international liquidity grew scarce, central banks and private investors searched desperately for other assets, that is, alternatives to the dollar and sterling that were liquid and promised to hold their value. They found them in the currencies of countries still on the gold standard: Belgium, France, the Netherlands, and Switzerland. The share of foreign exchange reserves held in those countries' currencies rose from ten percent of the total in 1931 to 20 percent in 1932 and 30 percent in 1933.

The problem was that these were not large markets. As their larger trading partners adopted a beggar-thy-neighbor strategy of devaluing their own currencies, these smaller countries experienced more and more trouble competing. Countries still on the gold standard saw their exports stagnate and experienced rapidly rising unemployment. By 1933, these states, once seen as bastions of stability, looked increasingly vulnerable. Capital started flowing out, not in, as central banks moved to liquidate their balances in these countries to avoid further losses.

As doubts grew about the stability of the Belgian and French exchange rates, the share of foreign exchange reserves in currencies other than sterling and the dollar fell sharply in 1934, and then dropped again

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in 1936, when the last countries still on the gold standard abandoned it. As war clouds gathered in Europe, central banks shifted their reserves to safety in New York, prompting a modest recovery in the value of foreign exchange reserves held in dollars. But this movement was small relative to the earlier drop in dollar reserves. It was not enough to reconstitute a working international monetary system.

The resulting vacuum was disastrous. The chaotic liquidation of foreign exchange reserves made credit scarce and put upward pressure on interest rates at the worst possible time, making it hard for firms to finance not only international transactions but domestic investment, as well. Disorderly exchange-rate movements disrupted trade flows, making it harder for countries to export their way out of the Depression. Nations now losing gold and foreign exchange reserves imposed capital controls that hindered foreign investment. It took years, well into the post-World War II period, for international trade and investment to recover to the levels that had prevailed prior to the collapse of the international monetary system. After the loss of confidence in the system's two key currencies, the inability of other currencies to provide viable alternatives made this international monetary collapse a global catastrophe.

THE POSTWAR SYSTEM TAKES SHAPE

AT THE Bretton Woods Conference in 1944, representatives of 45 nations assembled with the goal of establishing a new international monetary system to replace the one that had fallen apart during the prior decade. In fact, the new system resembled the old one in key respects. Under the new system, currency values were still fixed, now against the dollar. Reserves were still held in a combination of gold and foreign exchange. Gold still accounted for the majority of total reserves. The dollar, which represented the majority of foreign exchange reserves, was still convertible into gold at a fixed price, set at \$35 an ounce.

There were some important innovations, however. Under the rules designed at Bretton Woods, exchange rates could be adjusted. A multi-lateral organization, the IMF, was established to oversee the system. In contrast to the earlier era, countries now restricted international

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capital inflows and outflows; only the United States had deep and liquid financial markets open to the rest of the world. And only official foreign holders were allowed to convert the system's key currency, the dollar, into gold; private holders were not permitted to do so. Lastly, by the time the Bretton Woods system took shape, the British pound was only a pale shadow of its former self. This system became fully operational at the end of 1958, when the principal European countries removed their remaining restrictions on the ability of foreign firms, banks, and governments to freely buy and sell their currencies for trade-related transactions.

But no sooner did the system become operational than observers began to worry about its collapse. As in the 1920s, the source of anxiety was the fixed price of gold. Not only did foreign exchange now account for a larger share of total international reserves than in the 1920s, but those foreign reserves were now backed by only U.S. gold reserves, as opposed to the combined gold holdings of both the United States and the United Kingdom. As the world economy grew, central banks sought to augment their foreign reserves as a buffer against shocks. In practice, that meant accumulating dollars. The gross foreign liabilities of U.S. monetary authorities, U.S. deposit banks, and the federal government first exceeded U.S. monetary gold reserves in 1960, creating the possibility of a run on the country's reserves. After barely a year, it was already clear that sustaining the system would require international action.

The solution was the London Gold Pool, established in 1961 by Belgium, France, Germany, Italy, the Netherlands, Switzerland, the United Kingdom, and the United States, with the goal of maintaining the link between the official U.S. price of gold and the price at which gold traded on the London market. These countries acted out of fear that were the market price of gold to significantly exceed the official price, the incentive for arbitrage would become irresistible and a run on U.S. gold reserves would ensue. The European countries agreed to provide half of however much gold had to be supplied to the market to prevent the price from rising, thereby sharing the burden with the United States.

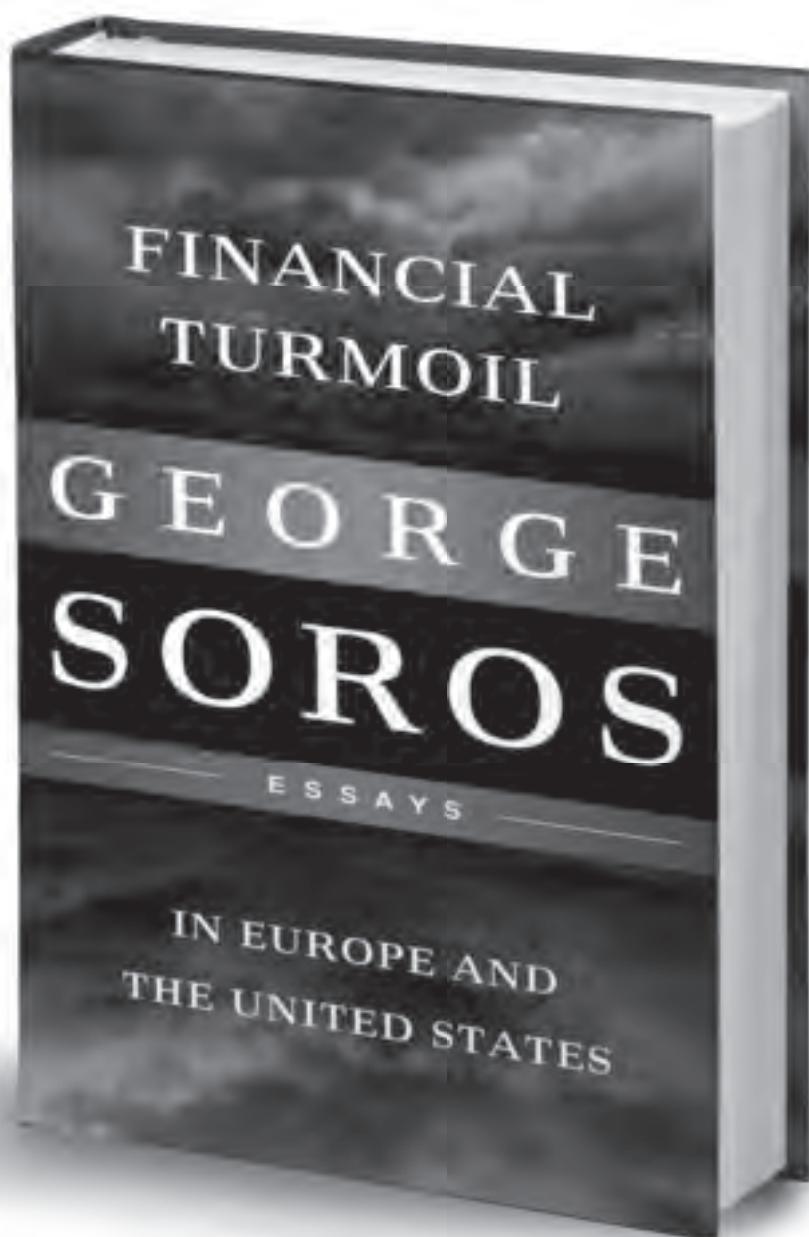
But the arrangement soon proved unworkable. European countries found the costs too high, and France pulled out in 1967. The following

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year, the London price of gold shot up. In effect, there was a run on the pool, and its operations were suspended. The private market price of gold was cut loose. This marked the advent of a two-tier market in which official transactions in gold took place at \$35 an ounce and private transactions took place at a higher price determined by supply and demand.

THE 1970S: A BENIGN COLLAPSE

THE ADVENT of the two-tier gold market heightened doubts about the stability of the dollar and prompted questions of whether it would be an adequate source for the safe and liquid assets required by an expanding world economy. Policymakers responded by deciding to create a synthetic reserve asset that could substitute for the dollar, or at least supplement it on the margin. But it took more than five years of difficult negotiations at the IMF to reach an agreement to create that asset, known as Special Drawing Rights. The United States, France, and Germany all had serious reservations about SDRs. The Americans worried that SDRs would accelerate the decline of the dollar, and the French objected that SDRs would artificially support the dollar; the Germans feared, as they did in response to almost every economic initiative, that SDRs would result in inflation. Owing to those concerns, only a modest \$3 billion worth of SDRs were issued in 1970.

Meanwhile, the imbalance between U.S. foreign dollar liabilities and gold reserves continued to grow. Doubts deepened about the viability of the two-tier gold market and the prevailing dollar exchange rate. Foreign central banks had to intervene, accumulating more dollars to prevent their currencies from rising. They took limited steps to diversify away from dollars, but there were few other currency markets that were sufficiently sizable and open. Moreover, the obvious targets of that diversification process, such as Germany and Switzerland, worried about the consequences for inflation and competitiveness and took steps to limit the banking and investment rights of foreign entities.

The end was a slow-motion train wreck. Switzerland redeemed \$50 billion of dollar paper for gold in July 1971. The United Kingdom

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made a similar demand in August. Two days later, U.S. President Richard Nixon responded by suspending the convertibility of dollars into gold at a fixed price, once and for all. A few months later, governments agreed to revalue other currencies upward by an average of 7.9 percent against the dollar. But with U.S. monetary and fiscal policies still highly expansionary, the underlying problem remained. One after another, other currencies were revalued against the dollar. Finally, in March 1973, all the other advanced-country governments abandoned their efforts to maintain dollar pegs. Foreign exchange markets were closed. When they reopened, currencies were allowed to float, and many floated upward against the dollar. The dollar-based Bretton Woods international monetary system was no more.

But the systemic consequences of this collapse were quite different from in the 1930s. The failure of the interwar system played a significant role in creating the Great Depression. In contrast, the collapse of the Bretton Woods system in the 1970s did relatively little to slow economic growth or undermine overall financial stability. The 1970s collapse contributed to the U.S. recession of 1973–75 but did not lead to anything remotely resembling the economic and financial crisis of the 1930s. U.S. monetary policy was inflationary, but in the absence of high instability, there was no mass flight from the dollar. On the contrary, the share of foreign exchange reserves held in dollars continued to rise. Indeed, throughout the decade, there was no shortage of liquidity to limit the growth of international trade and finance. The Organization of the Petroleum Exporting Countries added to its dollar balances in New York, there being few other available places to park its earnings. U.S. commercial banks used those balances to fund dollar loans to Latin America and Eastern Europe. Global trade grew twice as fast as global output over the course of the 1970s. International capital flows continued to expand among advanced countries and between the advanced and the developing world.

What accounts for the difference in how events unfolded in the 1930s and the 1970s? Part of the explanation is that, notwithstanding U.S. economic problems, there was no catastrophic loss of confidence in the dollar in the 1970s. Concerns about the currency peaked toward the end of the decade, when U.S. inflation soared into the double digits. But investors were reassured when Paul Volcker was appointed

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U.S. Federal Reserve Board chair in 1979 and wrung that inflation out of the economy by raising interest rates to high levels and sharply restricting the availability of credit.

There was also a lack of alternatives to the dollar. Other countries' financial markets were small in comparison to those of the United States, and their central banks continued to discourage purchases of their currencies for fear of inflation and reduced international competitiveness. In principle, SDRs might have substituted more extensively for the dollar. Three tranches of SDRs were issued, in 1970, 1971, and 1972. But even at the end of that process, SDRs still accounted for less than ten percent of the world's stock of non-gold reserve assets.

Although the linchpins of the old system—the fixed dollar price of gold and the fixed price of other currencies in terms of dollars—had been removed, international trade and finance did not collapse because confidence in the dollar remained strong enough for firms, banks, and governments to willingly use the currency to finance their international transactions. In this way, the experience of the 1970s showed that it is possible for prevailing international monetary arrangements to collapse without catastrophic consequences for global trade and finance.

A recent survey of central-bank reserve managers found a near-universal desire to diversify away from dollars and euros.

LET'S BE FRANC

THAT CONFIDENCE is precisely what is threatened today. As anxiety rises about the future of both the dollar and the euro, central banks and investors are confronting unappealing options similar to those faced by their predecessors in the 1930s and the 1970s. Should they flee to gold? Diversify into the currencies of smaller, more stable markets? Create a new synthetic reserve asset?

Gold has its advocates, as it always has. Ron Paul, the libertarian Republican U.S. representative and presidential candidate, advocates a gold-based system, as does Marine Le Pen, the leader of France's

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far-right National Front party. And there is some evidence that central banks, concerned about the stability of the euro and the dollar, are diversifying into gold. The central banks of Brazil, Russia, South Korea, and Thailand all significantly increased their gold holdings during the past year. Overall, central banks bought slightly more than 200 tons of gold in the first half of 2011, more than in any year since 1981. But those are drops in a very large reserve bucket. And no one in a position of authority is seriously talking about reinstating the nineteenth-century gold standard. Given gold's inherent price volatility, the idea that gold—or even claims on a broad-based commodity basket—could provide a basis for international commercial and financial transactions on a twenty-first-century scale is pure fantasy.

Less far-fetched is the notion that central banks might diversify their foreign exchange reserves into secondary international currencies that they believe are more stable, much as they sought to do in the 1930s. A recent survey of central-bank reserve managers conducted by UBS found a near-universal desire to diversify away from dollars and euros. Recent IMF data show that the share of total reserves accounted for by currencies other than the dollar and the euro rose from 11 percent to 13 percent between early 2010 and early 2011.

Still, 13 percent is a small fraction. And as in the 1930s, it is hard to imagine secondary currencies becoming a majority of foreign reserves. The Australian, Canadian, and Swiss bond markets are tiny compared with those of the United States and the eurozone. At current valuations, even Japan's large market in debt securities is only one-seventh the combined size of the United States' and the eurozone's.

Of course, by piling into, say, Swiss francs, investors could drive up the franc's exchange rate and increase the effective capitalization of the Swiss bond market measured in dollars and euros. So in principle, additional reserve diversification is possible. But large foreign purchases that push up exchange rates would create competitive difficulties for small economies, such as Switzerland, and ultimately lead reserves to flow back out—just as they did in the 1930s.

What is true of foreign reserves is equally true of other uses of currencies. If banks and firms conducted more of their international business in Swiss francs, they would need to hold larger working

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balances of that currency. Once again, Switzerland would experience uncomfortably large flows of finance into its small economy. These would be private rather than official flows, but the consequences for macroeconomic stability would be exactly the same. In addition, the presence of more foreign bank balances in Switzerland would raise the danger that the country's banking system would become too big to save, a prospect Swiss officials are already actively seeking to counter by forcing Swiss banks to hold more capital.

Simply put, Switzerland—or even a combination of Switzerland and other advanced economies perceived as well managed, such as Australia and Canada—cannot provide a stable basis for the international monetary system. Their currencies are unable to do more than modestly supplement the roles of the dollar and the euro. They do not provide a viable alternative.

CHINA TO THE RESCUE?

WITH MANY observers expecting China to overtake the United States in aggregate economic size over the next decade, it is logical to ask whether the yuan could provide an alternative to the dollar and the euro. Chinese officials are advancing this idea by promoting the international use of their currency. They have encouraged Chinese exporters and foreign firms exporting to China to price their goods in yuan. The value of cross-border yuan transactions was \$78 billion in 2010, the first full year in which they were permitted. By the end of the first quarter of 2011, such transactions were on pace to reach an annual total of \$220 billion, or seven percent of China's total trade—significant progress given that the starting point, two years ago, was zero.

Some 70,000 Chinese companies are now taking advantage of the new rules. Chinese officials see allowing their country's banks and firms to do international business in their country's own currency as a way of enhancing those companies' competitive advantage, since it enables them to avoid currency conversion costs and the risk of fluctuating currency values. There is every reason to believe, therefore, that they will support further movement in this direction.

Somewhat more slowly, the Chinese are building an infrastructure to enable the yuan to be used as a vehicle for international investment.

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The yuan earnings of firms exporting to China can be deposited in Hong Kong, where eight percent of all bank deposits are now accounted for by yuan-denominated accounts. The resulting pool of loanable funds is then tapped by firms such as McDonald's, which issue yuan-denominated bonds as a way of financing their investments on the mainland. This market tripled in size between mid-2010 and mid-2011. In August 2011, Chinese authorities announced a further liberalization of regulations on the use of yuan funds to finance direct foreign investment in China. In addition, the four big Hong Kong banks, along with banks in Macao and a few overseas banks, have been authorized to invest those funds in the bond market in China itself.

The final step will be encouraging central banks to hold reserves in yuan. China is working toward this goal by negotiating bilateral swap agreements, through which the People's Bank of China provides yuan to foreign central banks in exchange for their local currencies. In August 2010, central banks were permitted to acquire yuan and invest their holdings in Chinese bonds.

Still, it is unclear how quickly the yuan will gain market share in international financial transactions. Although China is a large economy, its financial markets remain underdeveloped. Its bond-market capitalization totals a bit over \$3 trillion, barely one-tenth that of the United States. As in Japan, the majority of government and corporate bonds are held to maturity by domestic investors. Market liquidity remains low. Annual turnover, measured by trading volume as a share of the value of outstanding bonds, is a tiny fraction of that in the United States and Europe. In other words, China is still far from having the kind of deep and liquid bond markets open to foreign investors that make the euro and, especially, the dollar attractive as vehicles for international trade and as forms of international reserves.

Chinese officials have set 2020 as the target date by which they aim to have transformed Shanghai into an international financial center. If that means significantly increasing the amount of international financial business conducted in the city, then the goal is achievable. But if it means transforming Shanghai into a first-tier international financial center and enabling the yuan to rival or supplant the dollar and the euro in the financial sphere, then the Chinese will have to eliminate essentially all restrictions on financial inflows and outflows and move

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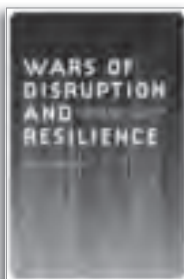


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to a fully flexible exchange rate. They would have to put Chinese banks on a commercial footing where they feel no pressure to engage in politically motivated lending. The authorities would need to remove all residual doubts about the security of foreign financial investment. Put simply, the Chinese government would be compelled to fundamentally transform not just the country's development model but its entire approach to foreign relations, an unlikely scenario, at least in the coming decade.

This is not to say that the yuan could not supplement the dollar and the euro as a source of trade finance in coming years. Firms will readily accept the currency of a large importer if it can be used to purchase that country's exports, and more so when that currency is expected to appreciate over time. China has already made significant progress in this area. But in its quest to make the yuan a vehicle for international investment and an attractive form of foreign reserves, progress will be much slower.

A GLOBAL CURRENCY

CENTRAL BANKS and investors are likely to conclude that neither a diversification into smaller currencies nor an embrace of the yuan can substitute for their reliance on the dollar and the euro. Might they instead push to create a new global reserve unit, as their predecessors did in establishing SDRs in the late 1960s and early 1970s? In 2009, the governor of the People's Bank of China, Zhou Xiaochuan, argued for replacing the dollar with SDRs as the world's primary international and reserve currency. A United Nations commission on reforming the international monetary and financial systems chaired by the Nobel Prize-winning economist Joseph Stiglitz similarly argued in 2009 for an expanded role for an international reserve unit, such as SDRs. In response to the U.S. debt-ceiling wrangle last summer, China's official news agency suggested that "a new, stable, and secure global reserve currency may also be an option to avert catastrophe caused by any single country."

This is not the first time that a synthetic unit, like SDRs, has been proposed as the basis for the international monetary system. The idea goes back to the Bretton Woods negotiations in 1944, when John

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Maynard Keynes argued for something along those lines. SDRs have existed for more than four decades, and yet they still account for barely three percent of international reserves. A fundamental reason is the difficulty of agreeing on how SDRs should be allocated. Should they be given to countries according to their weight in the world economy, in which case the majority would go to the rich countries? Or should they be allocated according to need, in which case many or all would presumably go to poor countries? What is the best way to measure weight in the world economy—or, for that matter, need? The difficulty of reaching agreement on these questions now, as in the 1970s, is the reason why the stock of SDRs remains small. It is why it will be hard to expand that stock sufficiently to replace the use of national currencies as international reserves.

It is even more far-fetched to imagine that SDRs could replace the dollar and the euro in their other international roles. For firms to accept payment for exports in SDRs, it would be necessary to create exchanges on which firms could convert SDR claims into local currencies or for commercial banks to provide such services. For each party that disposed of an SDR claim, someone else would have to be willing to hold it. Someone would have to create liquid markets in SDR forwards or futures, on which firms and investors could hedge against the risk of changes in the value of local currencies against SDRs. Banks would have to be willing to borrow and lend internationally in SDRs. Corporations issuing international bonds in SDRs would have to find willing buyers, but institutional investors, such as pension funds and insurance companies, would be unlikely to purchase SDR-denominated bonds whose value against local currencies might drop, since their contractual liabilities are denominated in those local currencies.

REDUX: 1930S OR 1970S?

BY PROCESS of elimination, the world is left with the dollar and the euro as the only instruments capable of supporting current levels of international transactions. If doubts about the stability of these currencies deepen further and central banks curtail their holdings of them, those central banks will have less capacity to intervene in financial

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markets and buffer the effects of volatile capital flows on their economies. In response, governments are likely to limit those flows via capital controls, as they did following the liquidation of foreign exchange reserves in the 1930s. Trade credit would become more costly, since commercial banks would demand additional compensation for holding dollar and euro investments. This situation would resemble the wake of the failure of Lehman Brothers in late 2008 and early 2009, when dollar credits became scarce and international trade declined precipitously. But what was then a temporary problem would instead be a permanent condition.

How serious would the impact on international trade and investment be? The answer depends on how severely confidence in the dollar and the euro eroded, and how reluctant those engaged in international trade and financial transactions became to accept dollars and euros. The experience of the 1930s suggests that in the worst case, international trade and financial flows would be severely depressed. The economic and financial globalization that has lent important impetus to economic growth in recent decades, especially in emerging markets, would be threatened. Alternatively, if the current economic and financial problems in the United States and Europe translate into nothing more than a few points of additional inflation and some depreciation of the dollar and the euro against other currencies, then the consequences will likely be similar to the relatively benign outcome of the collapse of the Bretton Woods system in the 1970s.

It is clear that the dollar will have to decline further in the medium term to restrain the growth of the U.S. current account deficit. To prevent that decline from precipitating a crisis of confidence, U.S. policymakers will have to put the federal government's finances on a sustainable footing. But critically, that fiscal consolidation must be done in a way that does not gut the federal government's support for basic research, education, infrastructure, and other programs on which the economy's growth depends. A country that does not grow its economy cannot continue to grow its financial markets—and cannot

A country that does not grow its economy cannot continue to grow its financial markets.

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provide adequate international liquidity to the global economy.

Whereas the United States must preserve financial stability, Europe must restore it—an even more daunting task. Doing so will require European policymakers to acknowledge that not just Greece's debt but those across much of southern Europe are unsustainable. It will require them to proceed with restructurings to remove the lingering uncertainty that is demoralizing global markets. Countries in crisis will have no choice but to proceed down the road of fiscal austerity. Banks will have to be forced to raise their capital-to-asset ratios well above the current target of nine percent, so that they can absorb losses on their holdings of government bonds—a step that will almost certainly require the injection of public funds. All this will be expensive, and the costs will have to be borne disproportionately by Europe's wealthy countries, such as Germany, which are the only ones with the necessary resources.

Reaching political agreement on these decisions will be difficult, to put it mildly. Countries with budgetary room for maneuver, such as Germany, will have to show far more willingness to use it. The European Central Bank must become more supportive of economic growth and less single-mindedly fixated on price stability. Southern European governments have already committed to putting pro-growth structural reforms in place, but even if those are implemented, it will take time for them to have any tangible effect. If Europe fails to grow, it will not be able to dig its way out of its debt hole and restore the confidence necessary for the euro to remain a significant source of international liquidity.

Which scenario will we see—that of the 1930s or that of the 1970s? The answer turns on the actions of policymakers in the United States and the eurozone. The fate of the global economy hangs in the balance. 🌐

Inside Rio de Janeiro

Ready for take-off

courtesy of the government of Rio de Janeiro / Santiago Calatrava



A sustained period of stable government and a responsible fiscal policy has helped Rio de Janeiro's economy spread its wings and reach for the sky.

If you have ever seen a chicken try to fly you have an idea of what Brazil used to look like: spindly legs hopping faster and faster, a flutter into the air, a hovering, then a crash back to Earth. This pattern repeated itself through much of the twentieth century. The economy would gather strength and speed, apparently poised for take-off, only to end with a *splat*.

What analysts called the *vôo da galinha* (chicken hops) were all the more frustrating because the potential of such a vast, populous and dynamic country was immense. Brazilian school-children were taught that they lived in the *país do futuro*, (country of the future) but political turmoil, hyper-inflation and reckless economic policies meant that that future never quite arrived.

But look at South America's giant today: that metaphor no longer applies. Latin America's largest economy is expanding at a record pace. With an annual rate of GDP growth of 8 percent in 2010 -- far higher than any of its neighbours -- Brazil is the emerging-market economy that has bounced back most quickly from the global economic meltdown. The selection of Rio de Janeiro as host of both the 2014 World Cup and the 2016 Summer Olympics is proof positive that Brazil has "made it". -- "I didn't think I would see this in my lifetime" -- said Marcelo Moura, a partner at Pinheiro Neto, one of Brazil's biggest law firms. -- "

I'm forty-six years-old and experienced the military dictatorship, the hyper-inflation and all the other problems. The country has changed." -

CCR, a private infrastructure concession group that administers highways and metro systems, is equally bullish -- "We are living in a very special moment," -- said CCR's director of finance and investor relations, Arthur Piotto Filho. -- "I think sustainable growth is here to stay." --

Although hosting the World Cup and the Olympics sporting events is certainly worth celebrating, the country still faces significant barriers that are hindering economic and social progress: onerous regulations, a creaking infrastructure and a huge informal sector that limit productivity -- not to mention a dependence on a large global appetite for commodities that at some point is bound to falter. Once we look beyond economic performance and focus on social progress and people's well-being, much more remains to be done to reduce the gaping wealth disparities that still exist and to meet the education, healthcare and living needs of Brazil's growing middle class.

The State of Rio de Janeiro has been working intensively to reorganize the state and to regain its

well-deserved position as one of the most important Latin American and global economies. A raft of measures put in place to improve good governance and create a better business climate is paying off as more and more international investors demonstrate their confidence in the awakening regional giant.

Today, Rio de Janeiro is no longer just one of the best tourist destinations in the world, it is also one of the best gateways to the Brazilian market. The state keeps up with Brazil's economic growth, which is currently the seventh largest economy in the world. The transformation stems from the tax reorganization of the state that made Rio, in 2010, the only sub-national government in South America to get the Triple A, the highest investment grade given by Standard & Poor's.



courtesy of the government of Rio de Janeiro

Rio de Janeiro: Reviving a reputation

At once a cinematic cityscape and a grimy urban front line, Rio de Janeiro, known as the *cidade maravilhosa* (marvelous city), is nothing if not exhilarating. Flanked by gorgeous mountains, white-sand beaches and verdant rainforests fronting deep blue sea, Rio occupies one of the most spectacular settings of any metropolis in the world.

The 1950s were heady times for Rio de Janeiro. Bossa nova was born; Hollywood stars flocked to the city's beaches; Rio was the glamour capital of one of the most glamorous places on earth.

Then in the 1960s, things changed. The Brazilian capital was transferred to Brasília and, soon

after, a military dictatorship took power. Gradually the so-called Golden Years lost their shine in this once vibrant, carefree seaside paradise. Politicians, foreign diplomats and businesses alike packed their bags and left.

The city has been on a long, downward spiral ever since. As urban violence ballooned, businesses fled

Now, however, Rio's state and municipal governments are turning things around, and working to transform the city into a thriving business capital with the slogan: "Rio: Arms open to business."

During the "Rio de Janeiro Investment Conference" that took place on the 30th of

November at the *Council on Foreign Relations*, Foreign Affairs brought together a group of Brazilian and U.S. business leaders, investors, and academic experts for important conversations on the successes and future challenges facing Rio de Janeiro as it approaches the 2014 World Cup and 2016 Summer Olympics, and the nation as it continues its remarkable growth.

With the recent discovery of huge oil deposits, the so-called pre-salt region off Brazil's south-eastern coast, companies from around the world that are linked to the energy sector are knocking on the governor's door.

An interview with Governor Sérgio Cabral Filho

After decades of Brazil being considered the country of the future, it is said to be the country of the present, despite the many challenges and structural problems that remain to be solved. At the moment, the bad news is not high inflation, but the crisis in Europe which should take global proportions soon. How does Brazil fit into the new global economic scenario?

Sérgio Cabral – Brazil in general, and Rio de Janeiro, in particular, is experiencing an extraordinary moment. Our country has reached an increasingly important position in the international arena. Since the reestablishment of democracy, in the late 80's, we've been proving to the world our seriousness and commitment to human rights and freedom of expression. In recent years, with the government of President Lula, we were able to maintain these commitments and strengthen the macroeconomic fundamentals that are so important to the country's development. Brazil has established a goal of reducing inflation and included in the consumer market 40 million people who left poverty and helped boost the economy. In this context, the country got stronger and it now ranks as the seventh largest economy in the world, heading to fifth place in the coming years. The economic growth of our country is consistent and we are today a safe market for foreign investments from worldwide.

Management Shock: in the last forty years, the Brazilian public administration has undergone major changes, particularly as a part of the transition to democracy. New practices and expectations of modernization have been developed, but many of its traditional features have



not been removed. True modernization will only come with effective reforms that redistribute power and resources and change the channels of communication between the people and its administration. How is the government of Rio de Janeiro walking the path of strengthening public administration and transparency and improving human resources management?

Sérgio Cabral – Our government has promoted a real management shock that made the state of Rio regain its financial health and the capacity to attract investments. Rio is experiencing today a moment of revival in development, with better security, improved health and education systems, major structural works, and employment and income generation. It's a very differ-

ent situation from what we found when we took office in 2007. As an example, the state had only R\$ 80 million available in its budget and therefore could not implement any policy. We invested heavily in capacity building and in increasing the agility of public management to expand revenues and optimize spending. In my first year of office, the prospected budget was R\$ 33 billion, in 2011, the budget was R\$ 55 billion and for next year we should exceed R\$ 63 billion. It is a very significant change. After eighteen years, Rio has once again created public exams for State Revenue Auditors. Since 2007, we created more than fifty thousand jobs through public exams in several areas. Along with the improvements in tax collection and public services, has come the valuing of our

servers, with annual wage increases. We also started to publish on the Internet all public spending and, since last year, we had our own system of trading sessions, all with true transparency. As a result of this administration, we received in 2010 the investment grade from Standard & Poor's. It's the first obtained by a subnational public entity in South America, and it has already been upgraded twice. In April this year, the Treasury of the State of Rio received the ISO 9001 quality certificate. We still have many challenges ahead but we are on the right track.

In the coming years, despite the financial contributions of the federal and the state governments and the private sector, the municipality of Rio will need many resources to carry out the necessary interventions for the sports mega-events. What are the plans of the state government to get them?

Sérgio Cabral – We have made a strong fiscal adjustment in the state, “cleaned up the house”, as we Brazilians say, and developed an alliance with the federal government to transform Rio de Janeiro and take the lead in the attraction of investments. Research from the Ministry of Economic Development shows that Rio was, in 2010, the Brazilian state that attracted the most investment, both domestic and foreign, with a volume of U.S. \$ 18 billion, almost the same value as that obtained by São Paulo and Minas Gerais together. Also, according to the latest study on investments from the Federation of Industries of Rio de Janeiro (FIRJAN), called “Decision: Rio”, our state will receive over the next three years U.S. \$ 102 billion in public and private investments. In addition to its privileged geographic location, Rio now attracts companies because we invest in infrastructure, provide tax incentives in certain economic sectors and have a strong public security policy. I always say that peace must be the first achievement because without it all other advances are not possible. Moreover, Rio has a very extensive calendar of major international events in the next few years. We will host the Rio +20 Conference on Sustainable Development (2012), the Confederations Cup (2013), the World Youth Day (2013), the World Judo Championship (2013), the World Cup (2014), and the Olympics and Paralympics (2016). We are carrying out structural interventions in areas such as security, health and urban mobility, among others, that will improve the quality of life of our people and benefit our visitors. By 2015, Rio will have a new subway line that will serve 240,000 people every day, an investment of R\$ 5 billion from our government. We will transform

the Maracanã, the site of the 2014 World Cup final, into the world's most modern and comfortable arena. In several years, we will have a more efficient transport system, be environmentally friendly and have a revitalized harbor area.

In the past few years, Rio de Janeiro has experienced a complete change in territorial civil security, decreasing crime rates and the largest action ever seen in taking back urban territories through police forces with the UPP. This has had a direct impact on the sense of security. Is there a firm plan in effect to permanently continue this security policy?

Sérgio Cabral – For sure there is. The Pacification Police Units (Unidades de Polícia Pacificadora or UPP) are a state policy, an achievement of the whole society, and they will not allow a setback in this area. Rio de Janeiro is experiencing its lowest crime rates two decades. In addition to the UPP, with the establishment of performance targets for our police officers, both civil and military, we are managing to reduce continually and consistently the main crime indicators throughout the state, such as homicides, burglaries and auto thefts. Currently, the state has eighteen UPPs that directly benefit more than 300,000 residents and indirectly, benefit more than 1 million people. There are still communities controlled by drug lords, it is still a big challenge, but we'll get there. We are facing crime on all fronts by prioritizing goals, strongly combating the misconduct within the police, and valuing the good officers – with bonuses for those who reach the goals set per semester. In addition to that, the Rio de Janeiro police are now among the best equipped in the country. We will increase the contingent of military police forces in the state, now at around 40,000 to 60,000 officers. By 2014, we will have qualified more than 20,000 men, investing, more than R\$ 15 million in training alone and all with a humanistic approach, aimed at the community and the police, bringing security officials and the public together. Bringing peace and citizenship to the population of Rio is our top priority. The UPP is a permanent policy and our commitment is that by 2014 there will be no more communities whose territory is controlled by armed bandits.

Twenty years after the UN Conference on the Environment and Development (UNCED/ ECO 92), Brazil will host the Rio +20 in 2012. Right now, Brazil is in 62nd position among all countries for management control of environmental pollution and natural resources, according to a ranking published by the World Economic Forum in Davos, Switzerland, ahead of other

BRIC countries, Russia (69) China (121) and India (123). What are the main and most effective actions that the government of Rio de Janeiro has been implementing towards greater success in this direction, with the City of Rio a reflection of Brazil as a whole?

Sérgio Cabral – Our government has developed a series of programs in the environmental area that will pursue sustainable development in the state. Our priorities are what we call the “pacts”: on sanitation; on vivacious bays and lagoons; on biodiversity; and against climate change. On the issue of sanitation is where there is still a great challenge. Until the beginning of our administration, only 33 percent of sewage was treated in Rio. We are undertaking major investments, both from our own resources, through the State Fund for Environmental Conservation (Fecam), and through funds raised by the World Bank and in partnership with the private sector – the order of grandeur is R\$ 4 billion by 2016. Our goal is to reach about 70 percent of treated sewage in the state in 2014. With the arrival of big companies and the settling of several industries in Rio, bringing in billions of dollars in investments, the pattern of environmental licensing already follows this ecologically correct bias. This has been pursued not only by requiring the use of new technologies to reduce the impact on the air and rivers, but also with environmental compensations, such as through commitments to the preserving of parks. The sports events we will host will also deliver an important legacy in this area. Among the commitments for the Olympic Games is the depollution of the Guanabara Bay. The state will invest R\$ 452 million in the recovery of the bay, which will benefit 1.6 million people. There is also the commitment to plant 24 million tree seedlings for the absorption of greenhouse gases that will be generated by all the major events we will host.

How will these new investments contribute toward social inclusion and the reduction of inequality, and improve the people's quality of life?

Sérgio Cabral – The public security policy is undoubtedly a major priority of our government. The turning point of Rio toward peace began as soon as we took office, in 2007, when we showed that there would not be any kind of agreement or tolerance of criminality. The UPPs sparked the hope that there is a path to peace, something that many believed was not possible for Rio de Janeiro. Taking back territories previously dominated by drug traffickers and returning them to the people has been our major challenge and a decisive factor for our state's economic development and for reducing inequality. The

old parallel-power culture is gone, we are establishing a paradigm shift in the fight against crime. Recently, we took back Rocinha, in the South Zone of our capital, rescuing 100,000 residents of the population of Rio de Janeiro in an exciting and historic day for Brazil. We know that there can be no sudden change in something that has been rooted for thirty years. But I'm sure that peace will soon be a reality for our entire population. We will also invest more in public health. The Emergency Care Units (Unidades de Pronto Atendimento or UPAs) are a national reference. How many people did no longer need to wait in a hospital for hours because they have the opportunity to be treated in an UPA, close to home? Another important point is education. After decades of neglect, our commitment is to improve the performance

of public schools of the state of Rio in the Basic Education Development Index (Índice de Desenvolvimento da Educação Básica or Ideb). Our goal is that by 2013, Rio de Janeiro will be among the top five states. For this, we have created a system of goals that has already been implemented, with bimonthly evaluations and the expansion of opportunities for postgraduate education and continuing education courses for teachers. Another important point is that we are investing in the training of manpower and creating opportunities. Rio now has the lowest unemployment rate in Brazil. With the Inter-cities Single Ticket program (Bilhete Único Intermunicipal), a state subsidy for the reduction of public transportation fares, residents of the metropolitan area pay much less than before to commute to work in oth-

er regions, increasing employability while reducing costs for the employers. There are now over 2 million beneficiaries. We also launched the Better Income program (Melhor Renda), which supplements the federal program Brazil Without Poverty through a financial benefit to families who are still below the poverty line.

How would you define the term leadership?

Sérgio Cabral – I think the key to true leadership is knowing how to convene an efficient team and give it autonomy so it can work and achieve the results previously set. No man or woman stands alone. Leadership is knowing how to put together talents and skills towards a major goal, which, in our case, is to improve the quality of life of our population.

Rio de Janeiro Investment Conference Foreign Affairs | New York | November 30, 2011



Presented by Think Link and media partner Foreign Affairs, the Rio de Janeiro Investment Conference took place on November 30, 2011 at the Council on Foreign Relations in New York. The conference hosted a broad range of senior investors, business leaders, politicians, policy-makers, and academics to debate and discuss the future of Brazil and Rio de Janeiro. With Foreign Affairs' characteristic clarity, wit, and 90-year history of challenging dogma, the forum offered fresh and incisive perspectives on the role, risks, and opportunities for Brazil and Rio de Janeiro in the new world economic order.

Following an inaugural speech by Governor of Rio de Janeiro Sérgio Cabral and an opening keynote panel, the audience participated in two breakout sessions. One evaluated current macroeconomic dynamics and their impact on infrastructure financing. The other discussed Brazil's

role as an emerging player in power generation, assessing the implications of investment in oil and gas exploration projects, renewable energy, and alternative power sources.

Some of the distinguished speakers included: David J. Rothkopf, President of Garten Rothkopf and visiting scholar at the Carnegie Endowment for International Peace; Ambassador Donna Hrinak, President of Boeing Brazil; Larry Rohter of The New York Times; Nicolas Aguzin, Chief Executive Officer of JP-Morgan Latin America; and Albert Fishlow, di-

rector of the Institute of Latin American Studies at Columbia University.

One of the main topics for discussion was the Oil Pre Salt discoveries: Deep in the South Atlantic, a vast industrial operation is under way that Brazil's leaders say will turn their country into an oil power by the end of this decade. If the ambitious plans of Petrobras, the national oil company, come to fruition, by 2020 Brazil will be producing 5million barrels per day, much of it from new offshore fields. That could make Brazil a top-five source of oil.

Managed wisely, this boom has the potential to do great good. Brazil's president, Dilma Rousseff, wants to use the oil money to pay for better education, health and infrastructure. She also wants to use the new fields to create a world-beating oil-services industry. But the bonanza also risks feeding some Brazilian vices: a spendthrift political system; an over-mighty state and over-protected domestic market; and neglect of the virtues of saving, investment and training.



The Future of the Yuan

China's Struggle to Internationalize Its Currency

Sebastian Mallaby and Olin Wethington

ACCORDING TO a growing chorus of pundits and economists, China—already the world's most prolific exporter, largest sovereign creditor, and second-largest economy—will someday soon provide the world's reserve currency. According to this view, just as the dollar dethroned the British pound in the interwar years, so the yuan will soon displace the dollar, striking a blow to U.S. interests. As the economist Arvind Subramanian recently wrote, the yuan “could become the premier reserve currency by the end of this decade, or early next decade.”

This view has gained traction as Chinese leaders have launched a concerted effort to internationalize the yuan. During the G-20 summit in November 2008, at the height of the financial crisis, Chinese president Hu Jintao called for “a new international financial order that is fair, just, inclusive, and orderly.” Beijing soon began to encourage the use of its currency in international trade, swap arrangements between central banks, and bank deposits and bond issuances in Hong Kong. During the first six months of 2011, trade transactions settled in yuan totaled around \$146 billion, a 13-fold increase over the same period

SEBASTIAN MALLABY is Director of the Maurice R. Greenberg Center for Geoeconomic Studies at the Council on Foreign Relations. OLIN WETHINGTON is Chair of Wethington International and previously served as Assistant Secretary for International Affairs and as Special Envoy on China at the U.S. Department of the Treasury. This essay draws on a collection of CFR working papers available at www.cfr.org/cgs.

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during the previous year. By mid-2011, yuan deposits in Hong Kong equaled \$85 billion, a roughly tenfold jump since Hu's 2008 statement.

The emerging narrative about the yuan's ascendance is mostly wrong.

The yuan is already accepted as a form of payment in Mongolia, Pakistan, Thailand, and Vietnam. Chinese authorities have indicated that as soon as 2015, they want the yuan to be included in the basket of major currencies that determines the value of Special Drawing Rights (SDRs), the reserve asset issued by the International Monetary

Fund. And Beijing has announced its intention to transform Shanghai into an international financial center by 2020.

There is also no denying that the dollar is vulnerable. Central banks traditionally hold foreign currency reserves to ensure their ability to buy imports. But today, more of the world's imported goods come from China than from the United States. Central banks also hold reserves to ensure their ability to service debt payments to foreigners. Yet such payments flow increasingly to China, and although China's lending is largely conducted in dollars, dominant creditors ultimately tend to insist on lending in their own currency. To make matters worse for the dollar, it is losing value—instead of storing it, as reserve currencies are expected to do. Measured against the currencies of the United States' main trading partners, the dollar has lost a quarter of its value since the advent of the floating currency system in 1973. Over the past four decades, it has lost four-fifths of its purchasing power as measured against a basket of consumer goods. This decline makes central bankers in emerging economies understandably nervous about holding dollar reserves.

Yet the emerging narrative about the yuan's ascendance is mostly wrong. The global rise of China's currency will be slower than commonly predicted, and the yuan is more likely to assume a place among secondary reserve currencies—the euro, the yen, the Swiss franc, and the British pound—than it is to displace the dollar as the dominant one. Nor is it even clear that China wants the yuan to replace the dollar. Beijing's steps toward currency internationalization reflect not a fully formed, coherent long-term strategy but rather an evolving process

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shaped by splits among China's policymakers over the scope and speed of financial reform. Far from confirming the inevitability of the yuan's rise, China's uncertain effort to internationalize its currency has exposed the profound struggles that lie behind the country's larger push to transform its economic model.

THE RELUCTANT RISE OF
INTERNATIONAL CURRENCIES

ONE MIGHT assume that as a country approaches great-power status, it will naturally attempt to internationalize its currency. In fact, rising powers have often done just the opposite. As the economist Jeffrey Frankel has shown, that is what the United States did in the interwar period and what Germany and Japan did in the 1970s, even though the currencies of all three countries later became international. In each of these cases, both the public and policymakers were initially skeptical of the benefits of allowing their currency to be used widely abroad.

Rising powers have had two reasons to fear the internationalization of their currencies. The first concerns competitiveness. When foreigners buy and hold a currency, they increase its value. This appreciation persists as long as the buyers hang on to the currency as a store of wealth. A stronger currency hurts a nation's exports by making its goods more expensive abroad and creates more competition for domestic companies by making imports cheaper for consumers.

The second reason to fear currency internationalization concerns control of the financial system. Like China today, Germany, Japan, and the United States all emerged as trading powerhouses at a time when their financial systems were tightly regulated. Governments capped interest rates on bank deposits and restricted the investment opportunities of pension and insurance funds so that capital remained cheap. But this "financial repression" stuck savers with low returns, and the demand for artificially cheap capital often exceeded the supply, leaving some borrowers frustrated. Currency internationalization threatened the cheap-capital development model by freeing savers and borrowers to find one another abroad, beyond the reach of regulators.

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These reservations about currency internationalization have contributed to long lags between a nation's emergence as a first-rank power and the widespread use of its money by foreigners. The United States became a larger economy than the United Kingdom in 1872, but the dollar did not begin to displace the pound as the reigning international currency until World War I, and the process was not completed until after World War II. Even then, the United States frequently appeared indifferent to its currency's newfound status. In the 1970s, President Richard Nixon abandoned the gold standard, sacrificing the international prestige of the dollar on the altar of domestic stimulus. Likewise, Japan resisted currency internationalization until the 1980s, when it became impossible to resist American pressure to allow U.S. financial firms to enter the Japanese market. The deutsche mark became a reserve currency because foreigners wanted to hold it, not because German authorities actively sought that outcome.

CHINA'S DOLLAR TRAP

IF OTHER rising powers have resisted the internationalization of their currencies, why is China's policy so different? The answer is that the recent global financial crisis confronted China with the dangers inherent in dollar hegemony. China's economic model had relied on boosting exports by keeping its exchange rate undervalued. This required China's central bank to purchase large quantities of dollars, reinforcing the dollar's status as the global reserve currency. But the crisis revealed that the benefits of this model were smaller than they appeared and that the costs could be significantly higher.

The crisis showed that by basing its growth on exports, China had laid itself open to a sharp reversal if foreign markets seized up. In the first quarter of 2009, collapsing demand in Europe and the United States caused China's annual growth rate to fall to 6.2 percent, after hitting ten percent or more in each of the previous ten quarters. The crisis also highlighted the potential costs to China of accumulating dollar reserves. To keep the yuan undervalued, China had bought \$1.5 trillion worth of U.S. financial assets, including about seven percent of all the bonds issued by government-linked lenders, such as

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the disastrously overleveraged Fannie Mae and Freddie Mac. The crisis convinced Beijing that it could one day take a serious loss on those investments.

China's leaders responded to the shock by criticizing the international financial system. The effort was launched by Zhou Xiaochuan, the governor of the People's Bank of China (the country's central bank). In an article posted on the bank's Web site in March 2009, he called for far greater use of SDRs as an alternative to the dollar. Other Chinese officials followed Zhou's lead, arguing that the basket of currencies that determines the value of SDRs should be expanded to include the yuan and that, in preparation for that change, the yuan should be internationalized. Echoing the complaints French leaders made in the 1960s about "exorbitant privilege"—a country's ability to borrow cheaply and seemingly without limit in its own currency—Chinese officials and scholars argued that the United States abuses its monetary freedom and passes on the costs to the rest of the world in the form of currency depreciation and financial instability. The U.S. Federal Reserve's subsequent quantitative easing and the U.S. Congress' chaotic efforts to grapple with the national debt only increased China's frustration.

Even before the crisis, China had been engaged in an internal debate about its export-led growth model. Several years ago, reformers began arguing that an excessive reliance on exports could be dangerous and that China needed to rebalance its growth by encouraging more domestic consumption. In place of financial repression and cheap capital, these reformers wanted savers to get a decent return, which might give them the confidence to consume more. In place of an artificially low exchange rate, they wanted to allow the value of the yuan to rise, which would reorient Chinese firms away from exports and toward the domestic market.

The reformers claimed a small victory in 2005, when China loosened its exchange-rate peg. But in general, the reform agenda has struggled. State-owned banks do not want to pay depositors market interest rates. Politically connected borrowers, such as the state-owned construction

The internationalization of the yuan has allowed people who disagree to unite—at least in the short term.

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companies that build China's impressive infrastructure, do not want to give up access to cheap capital. Politically connected exporters, on whom provincial governors count to create jobs in their regions, do not want to give up the competitive advantage created by a favorable exchange rate. Groups that have an interest in reform—savers who receive artificially low returns and consumers who pay a high price for imports—are no match for powerful producers.

Prior to the financial crisis, the case for reform was also tainted by the suspicion that it represented a capitulation to U.S. demands to let the yuan appreciate. But once the crisis exposed China's vulnerability, reform acquired a fresh patriotic gloss: advocates could paint themselves as challenging the dangerous hegemony of the dollar. This reframing was enough to tip the political center of gravity away from the status quo. Criticism of what Chinese scholars called "the dollar trap" became widely accepted, and by extension, internationalization of the yuan became an official goal, even though many of China's leaders continued to believe in export competitiveness, highly regulated capital markets, and a state-controlled banking system.

In effect, the government wanted to have it both ways: booming exports, but reduced accumulation of dollars; continued funneling of cheap loans to favored companies at the expense of savers, but also more domestic consumption. Internationalization of the yuan emerged as an official goal not because it resolved the long-running debate between reformers and mainstream opinion. Rather, it became policy precisely because it blurred that division, allowing people who disagreed to unite—at least in the short term.

OF CARTS AND HORSES

ONE CONSEQUENCE of these internal conflicts is an unorthodox sequencing of reform. As the economist Takatoshi Ito has explained, the best way to open a repressed, autarkic financial system is to begin with domestic financial reform. Before large amounts of foreign capital are permitted to flood in and out of a country's system, banks need to be well capitalized and competently regulated. Bond markets must be deep and liquid, so that they can absorb foreign money without experiencing dramatic price swings. The authorities must

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welcome a variety of investors, with differing time horizons, investment objectives, and worldviews—a form of diversity that reduces destructive herd behavior. Only once the domestic financial system has been fortified in this manner is it safe to open the economy to foreign capital inflows, allow the exchange rate to float, and let the country's money circulate offshore. Currency internationalization should be the endpoint of reform, not the starting point.

China is not following this sequence. Mainstream Chinese political opinion still resists rapid domestic financial reform and exchange-rate flexibility, so reformers have pushed forward with currency internationalization before the standard preconditions have been met. Since Hu's speech in 2008, China has signed largely symbolic central-bank swap agreements with 13 countries, including Argentina, Belarus, Indonesia, Malaysia, and South Korea. In September 2011, Nigeria's central bank announced that it would convert between five and ten percent of its reserve assets into yuan. But the most significant reforms began in April 2009, when China's government permitted five pilot regions—Dongguan, Guangzhou, Shanghai, Shenzhen, and Zhuhai—to begin conducting trade with Hong Kong in yuan on a trial basis. In June 2010, the experiment was extended to 20 provinces, cities, and autonomous regions. Last year, it was extended to the entire country. The resulting explosion of yuan-based trade has been hailed by some as a success. But as Peter Garber of Deutsche Bank has explained, the growth has been revealingly lopsided, resulting in some serious unintended consequences.

Because foreigners expect China's currency to appreciate against the dollar, they are eager to buy any yuan that reach Hong Kong, where the currency is called CNH, to distinguish it from the mainland currency, which is sometimes referred to as CNY. As a result, CNH tend to command a premium against the dollar, opening up a gap between the onshore yuan-dollar exchange rate, which the Chinese government manages, and the offshore CNH-dollar exchange rate, which it does not. This differential creates an incentive for Chinese importers to

The upshot of China's currency policy has been a classic demonstration of the law of unintended consequences.

Sebastian Mallaby and Olin Wethington

pay foreign suppliers in CNH, rather than in dollars purchased from the central bank at the lower official exchange rate.

As Chinese importers take advantage of the favorable Hong Kong exchange rate, they move money from the mainland into

The tensions in China's currency policy emerge clearly from the wide range of official statements intended to explain it.

CNH accounts in Hong Kong and then use those CNH to purchase goods from foreign exporters. The foreigners then either hold the CNH in expectation of appreciation or, if they are not interested in currency speculation, sell the CNH to other foreigners who are keen to take the bet. In this way, Chinese currency piles up in Hong Kong. Some market analysts predict that, having already grown tenfold since Hu's speech in 2008, Chinese currency deposits in Hong

Kong will quadruple from today's level by the end of 2012, rising to the equivalent of around \$340 billion.

That is not what Chinese policymakers intended. Technically, the deregulation of yuan-denominated trade payments applies to Chinese exporters as well as importers. If exporters took advantage of the new freedom, the pools of CNH building up in Hong Kong would be drained as quickly as they accumulated. But the incentives for exporters are the opposite of those facing importers. Rather than going through Hong Kong, exporters are better off taking payment in dollars and then selling the dollars to the central bank at the managed rate, which renders the dollar artificially valuable.

The upshot has been a classic demonstration of the law of unintended consequences. Before the opening of the Hong Kong CNH market, Chinese importers bought foreign exchange from China's central bank, reducing the bank's stock of dollar assets. Now, importers can obtain foreign exchange indirectly from foreign speculators in Hong Kong, leaving more dollars on the central bank's balance sheet. Put another way, Chinese importers' ability to pay foreigners in CNH has the effect of removing a significant source of dollar purchases from the world's currency market. Assuming that the central bank wants to maintain the yuan-dollar exchange rate, it must offset this effect by increasing its own dollar holdings. China's

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attempt to internationalize the yuan, which sprang partly from a desire to reduce the government's exposure to dollars, has actually had the reverse effect of increasing the central bank's already vast dollar holdings.

Even beyond this irony, the policy is proving costly. Assuming that China will one day stop holding down the value of its currency, China's central bank will eventually suffer a portfolio loss as the dollar falls to its natural exchange rate against the yuan. The more dollars the central bank accumulates, the larger this eventual loss will be. Moreover, as the central bank acquires additional dollars, it pays out yuan. To avoid inflation, this monetary expansion has to be "sterilized" by the issuance of bonds or the acceptance of bank reserves on which the government pays interest, imposing a further cost on the Chinese government. The challenge of sterilization grows when the money in CNH bank accounts is used to purchase CNH bonds and then the issuers of these bonds repatriate the capital to the mainland. As long as the Hong Kong market remains comparatively small, China can absorb these costs with little difficulty. But if the authorities are serious about internationalizing the yuan in a sustained way, the costs will quickly grow and the unintended consequences will likely become harder to manage, especially in the absence of domestic reform.

RISKS OR REWARDS?

THE TENSIONS in China's currency policy emerge clearly from the wide range of official statements intended to explain it. Some leaders openly state a preference for diversification away from the dollar but are careful not to call for the yuan's preeminence, even within the next several decades. Rather, they predict a lengthy and complex process of change in the international monetary system, with increased demand for yuan restricted mostly to East Asian markets. Other policymakers in Beijing advocate including the yuan in SDRs and believe that SDRs should ultimately displace the dollar as the world's main reserve asset. But even as they advance this vision of a radically transformed monetary order, these officials shy away from acknowledging a policy of currency internationalization, speaking

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instead of a more limited agenda of trade and investment facilitation. They suggest that their policy is a response to market demand; by allowing yuan to be used in trade transactions, these officials maintain, China is merely acceding to requests from importers and exporters. China has concluded swap agreements with foreign central banks only because foreigners requested them, they claim—despite the fact that foreigners have drawn down only a small fraction of the yuan swaps that Beijing has provided.

Yet even though China's leaders struggle to rationalize a conflicted policy, it would be wrong to conclude that yuan internationalization is doomed. After all, China has managed such contradictions successfully before, often pursuing reform not by tackling the status quo head-on but rather by allowing an alternative to grow up around it. For example, in the 1980s, during the early stages of the transition away from central planning, farmers were still required to meet Mao-era quotas and were paid at prices set by the central planners, but farmers were also allowed to sell anything they produced in excess of their quotas on the new free market. Today, private companies coexist with state-run firms and five-year plans exist alongside a capitalist free-for-all. In a similar fashion, China is allowing a free yuan capital market to grow up in Hong Kong in parallel with the largely unreformed, restricted capital market on the mainland. The policy mix might not be consistent, but it could ultimately prove effective.

Indeed, inconsistency might hold some advantages. It allows China to experiment with change while retaining the option to retreat if the side effects become intolerable. It could permit policymakers to foster the development of the Hong Kong market, so that the institutions necessary to make a currency market function can gradually take shape there. If Chinese and foreign companies issue greater volumes of CNH bonds of short and long duration, a market-driven yield curve will emerge, Chinese traders will learn the art of interest-rate arbitrage, and Chinese companies using this market will learn the ropes of treasury management. The system can be tweaked and tested before it is rolled out on the mainland, and in the meantime, it may generate price signals useful to China's government. If the CNH appreciates suddenly against the dollar, this will warn the authorities of rising pressure from speculation. If short-term interest rates rise

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relative to long-term ones, this might signal that investors have become pessimistic about the economic outlook. In time, the onshore and offshore markets could conceivably converge as capital controls are loosened.

Of course, there is a significant risk that a gradual approach—and the resulting tension between a free offshore market and a controlled onshore one—could prove hard for the Chinese government to manage. The rising cost to the central bank of purchasing dollars to offset foreign yuan holdings in Hong Kong might encourage foreign speculators to bet that the central bank will seek to reduce that cost by allowing faster yuan appreciation; the result could be even more speculative purchases of CNH, setting off a vicious cycle. Likewise, leakage of capital from Hong Kong to the mainland could fuel inflation; as the economist Robert McCauley has explained, this fate befell the United States when it clung to capital controls in the face of growing offshore dollar markets in the 1970s. But it is also possible that the benefits of China's experimental technique could outweigh its obvious costs and contradictions. Anyone who has watched China's extraordinary economic performance, achieved while it ignored many of the West's textbook development prescriptions, should be modest in predicting that China will inevitably trip up this time. But even if China's policy of gradualism with regard to its currency succeeds, the yuan is not going to displace the dollar anytime soon. The dollar enjoys an advantage that its predecessor, the pound, never had: formidably deep capital markets both inside and outside the United States, which operate mainly in dollars.

The chief purpose of a reserve currency in today's global economy goes beyond its traditional ones. Central banks hold foreign exchange war chests not just as a cover for essential imports and debt payments; they hold them as insurance against the virulent crises to which modern finance is susceptible. As capital markets have gone global, banks all over the world have borrowed in efficient dollar-based markets. As a result, when markets suddenly dry up, borrowers are

Even if China's gradualism succeeds, the yuan is not going to displace the dollar anytime soon.

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left screaming for dollars. So long as dollar funding remains attractive to private firms, central banks will hold a large proportion of their reserves in dollars, too. Even if the dollar loses value steadily, central banks will probably be prepared to absorb that cost, which amounts to an insurance premium.

Given China's economic strength and the likely appreciation of its currency in the future, the yuan might eventually emerge as a secondary reserve currency. If a reliable yuan bond market develops, first in Hong Kong and then perhaps on the mainland, foreigners will increasingly include yuan assets in their portfolios, alongside British pounds, euros, Swiss francs, and yen. Asian nations, with deep economic links to China, will be particularly likely to do so; the yuan already serves as an unofficial anchor for several of their exchange rates. But that is a far cry from displacing the dollar. China is rapidly catching up to the United States in terms of the overall size of its economy, and perhaps in other measures, too. But China's monetary dominance should not be assumed. If it ever does arrive, it will have been long in coming. 🌐

Reviews & Responses



ERIC SCHWAB/HULTON ARCHIVE/GETTY IMAGES

George Kennan in his State Department office, 1948

Kennan believed that language helped make policy and that vague, expansive language would lead to vague, expansive policy.

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Review Essay

Ideas Man

The Legacy of George F. Kennan

Nicholas Thompson

George F. Kennan: An American Life. BY JOHN LEWIS GADDIS. Penguin Press, 2011, 800 pp. \$39.95.

The first book to complicate the reputation of George Kennan came out in 1967. It was 600 pages long, and the cover would show a forlorn young man staring right at you. The tale was of an awkward boy from the Midwest who never quite fits in. He gains knowledge in the Foreign Service and becomes the United States' wisest Soviet analyst. Then, for a brief—but crucial—moment, he serves as the head of the State Department's Policy Planning Staff under President Harry Truman, helping remake the world after World War II. Along the way, he writes the "Long Telegram" and the "X" article, which laid out a strategy forever known as containment, and he plays a central role in designing the Marshall Plan. He writes beautiful memos that anticipate

the dangers of keeping Germany divided and starting an arms race. But soon he grows irritated with Washington, and Washington grows irritated with him. He becomes as bitter as he is brilliant, as frustrated as he is farsighted. The story ends with him out of power, despairing for the republic. The book hints that its subject might be anti-Semitic, depressed, and professionally inept.

The author of that book, *Memoirs 1925–1950*, was Kennan himself, as self-critical and personally reflective an autobiographer as his century had seen. More books followed (including one by the author of this review), peeling back the onion further and further. Each new round of discovered documents and diaries has reinforced what was known before. And now there is John Lewis Gaddis' magisterial, authorized account, *George F. Kennan: An American Life*. It is based on intimate interviews

NICHOLAS THOMPSON is Senior Editor at *The New Yorker* and the author of *The Hawk and the Dove: Paul Nitze, George Kennan, and the History of the Cold War*.

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with Kennan and access to all of his diaries, including the one in which he jotted down his dreams.

The Kennan who comes through in this new book is very much like the hero of *Memoirs 1925–1950*, only more so. He is wiser, and he broods more deeply. Kennan foresaw the arc of every major war of his lifetime. In 1940, he accurately predicted when the United States would engage Germany and how long it would take for his country to win; in the summer of 1950, he warned of giving too much power to General Douglas MacArthur in Korea; in 1966, he diagnosed the dangers of fighting in Vietnam and urged a dignified withdrawal. All the while, he wrote utterly scathing, and self-flagellating, notes to himself. Here is just one of several dozen diary entries that Gaddis cites: “There are times when I see myself as a spineless, somewhat infantile, futile little man.” Brilliance and self-contempt always interlock with Kennan. In early 1949, at the height of his influence, Kennan, considering whether to resign, wrote to Secretary of State Dean Acheson that he had no enthusiasm for “the wretched consolation of having been particularly prominent among the parasites on the body of a dying social order, in the hours of its final agony.” The same attitude manifested itself through the last 40 years of his life, when he was mainly a historian, essayist, and polemicist, declaiming against the folly of nuclear weapons.

As the book makes clear, he was never boring, and he was never bored. Kennan never seemed to pause—even when he was ill, which he frequently was. Nearly every minute of his adult life was spent thinking about how to make himself, or his country, better. And there were a lot

of productive minutes. He lived to 101 and published his last book when he was 96. In the mid-1950s, he wrote, “Men—or at least such men as I—are no good unless they are driven, hounded, haunted, forced to spend every day as though it were the last they were to spend on earth.”

ARCHITECT OF CONTAINMENT

Kennan had two really big ideas. The first was containment, which he presented in the “X” article, published in *Foreign Affairs* in 1947, but which he had been refining for years in speeches. The idea was that there is a middle ground between diplomacy and war. If the former fails, the latter is not inevitable. The United States didn’t have to remove the Communists from power in Moscow, and it didn’t need to roll them out of Eastern Europe. It just had to wait, and eventually the Soviet order would collapse. The insight was heavily shaped by Kennan’s study of *The History of the Decline and Fall of the Roman Empire*. Throughout his career, he would cite Edward Gibbon’s statement that “there is nothing more contrary to nature than the attempt to hold in obedience distant provinces.” The Soviets were overstretched, and communism was a wretched ideology. Washington just had to wait and quietly make Moscow’s relationships with its clients as difficult as possible.

From almost the moment of the article’s publication, policymakers were debating whether containment should be carried out through a series of political acts or through the threat of military force. Kennan had been ambiguous in this particular essay, but his speeches, other writings, and actions showed that his true preference was for the former. The article, however,

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was interpreted as mainly calling for the latter, and the United States' Cold War policy followed suit. This was a great source of stress for Kennan, and it left him with a complicated moral question after 1989. What do you do when your idea is misinterpreted—in a way that you find repulsive—but then leads to exactly what you hoped it would?

Kennan's second big idea wasn't original, but it was important. The word some political scientists use to describe it is "realism"; another way to put it is that Kennan was skeptical about American competence in foreign affairs. The United States, particularly when it did not follow his advice, could do little to change the world for the better. Given that, it was best to limit engagement and, when it was necessary to do something, to deal entirely with issues of power and interest. As he put it in 1951, he sometimes wondered whether American democracy was "uncomfortably similar to one of those prehistoric monsters with a body as long as this room and a brain the size of a pin." In 2002, as conflict in Iraq approached, he said, "War has a momentum of its own and it carries you away from all thoughtful intentions when you get into it. Today, if we went into Iraq, like the president would like us to do, you know where you begin. You never know where you are going to end."

Kennan recognized that his arguments were often futile and that presidents would rarely heed his advice. Containment turned militaristic, and every new administration would strut into office with ambitions to reshape the world. Still, he took solace in the notion that his ideas and books would live on. In a letter to Acheson, Kennan wrote that he wanted to be "one of those

teachers whose teachings rarely please people, and are no doubt often wrong, but of whom it is sometimes said, when they are gone: 'It is useful that he taught as he did.'"

DEFINING THE DIPLOMAT

In September 1982, Gaddis sat down to interview Averell Harriman about Kennan. Gaddis, then just over 40, had written a letter noting that he was working on a Kennan biography and he wanted to do it fast. Might the former ambassador and governor be available to talk soon? Harriman agreed, although the book would not come out for nearly three decades. Gaddis had other things to write, and he wanted to wait on this big project until Kennan had died.

Now the biography has arrived, and it is terrific. Gaddis, a historian at Yale University who has published ten books on the Cold War, always writes well, but here he writes particularly well. The narrative moves quickly and smoothly. It also helps that Gaddis isn't trying to provide new Cold War scholarship. There's no slowing down to examine freshly discovered, and tangentially related, documents from the Soviet archives. Gaddis is just trying to tell readers about one extraordinary man. And it always helps one's prose to be able to pop in vivid quotes from one's subject.

Gaddis' take on Kennan is more or less the conventional one, which is partly because Gaddis has played a major role in shaping people's perceptions of Kennan in the first place. But there are surprises, one of the most interesting of which comes when Gaddis defends Kennan against charges of anti-Semitism. In his memoir, Kennan was strikingly callous in describing how he turned a Jewish acquaintance

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away from the Prague legation at the time of the German occupation; he followed this with a far more sympathetic description of a German prostitute whose husband was a Nazi pilot. Gaddis, however, notes that Kennan actually worked hard at the time to get other Jews out of Berlin and Prague. Kennan, it seems, was the rare man who implied that he was more prejudiced than he actually was.

The book is also particularly compelling when Gaddis describes Kennan's distance from his own nation. Kennan was born in the United States, he served his government, and he would have died for Old Glory. But he viewed the country with the eyes of a disgruntled visitor. In 1936, for example, Kennan wrote a profoundly weird essay, arguing, among other things, for the disenfranchisement of women, blacks, and naturalized citizens. At about the same time, he wrote rapturously about the system of social insurance set up in Austria—apparently unaware that Franklin Roosevelt had passed something more robust right at home. His cultural knowledge was incomplete as well. In his diary in 1987, Kennan wrote of attending a dinner for Soviet President Mikhail Gorbachev and being seated at a table with “a lady of most striking appearance, who chain-smoked Danish cigars and appeared to be rather bored with the whole performance. . . . I was later told that I should have recognized her—as the widow of a famous rock star.” The star's name, he noted, was something like “Lenin.” *An American Life* is an apt subtitle, but also a curiously ironic one.

Gaddis argues with Kennan a lot, and he doesn't romanticize his protagonist. He spends many pages exploring Kennan's infidelities—which weren't particularly

common but were still more common than one might have thought given the buttoned-up image that Kennan presented. Gaddis also expresses frustration that Kennan seemed to feel such a kinship for John F. Kennedy but such animosity toward Ronald Reagan. The former, Gaddis argues, appointed Kennan as ambassador to Yugoslavia but then ignored his recommendations. Reagan never hired Kennan for anything, but their feelings of revulsion toward the arms race were quite similar. After describing Reagan's efforts to remove nuclear weapons from Europe, Gaddis writes of Kennan, “How could he have loved John F. Kennedy, who repeatedly rejected his advice, and loathed Ronald Reagan, whose actions in this and other respects were consistent with it?”

Still, in the end, Gaddis praises Kennan highly. Kennan's most important idea, containment, “illuminated the path by which the international system found its way from the trajectory of self-destruction it was on during the first half of the twentieth century to one that had, by the end of the second half, removed the danger of great-power war, revived democracy and capitalism, and thereby enhanced the prospects for liberty beyond what they ever before had been.”

KENNAN TODAY

The international system may now appear to be finding its way back toward the trajectory of self-destruction, and there is much that Kennan, were he still alive, would despair about—foremost, perhaps, the grim prospects for liberty in Russia. The foreign policy of Barack Obama's administration, however, closely resembles the foreign policy one would reach after a close study of Kennan's views.

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For starters, there is the gradual withdrawal from Afghanistan and Iraq. Kennan, as a good student of Gibbon, would have pushed for this drawdown to have started long ago, and he would certainly have supported it now. Combining withdrawal with targeted killings also seems like Kennan. He had his liberal side, but he was not squeamish. He cared little for the niceties of international law, and he did not fear the dark arts. He helped design the covert operations wing of the CIA and helped plan some of the agency's first secret escapades. In a way, the Obama administration has moved from a policy of trying to snuff out Islamic terrorism to one of trying to contain it. The stated goal is no longer to rid the world of al Qaeda; it is to limit the damage that it can do. The United States is no longer trying to wipe out the Taliban; it is talking to them.

Kennan loved rhetoric, and he would have felt a bond with Obama's use of words and his bookishness. Their speeches about the need to rid the world of nuclear weapons echo one another. But maybe more important, Kennan would have taken pleasure in this administration's abandonment of grand shibboleths. No longer does one hear the White House mentioning a "war on terror" or even a "war on drugs." Kennan believed that language helped make policy and that vague, expansive language would lead to vague, expansive policy. On these grounds, he opposed the Truman Doctrine. It sounded good to say that the United States would defend democracy anywhere, at any time. But there were many countries, he wrote, "where you could perfectly well let people fall prey to totalitarian domination without any tragic consequences for world peace in general."

Washington's change in discourse under Obama has also come with a change in attitude, and, no doubt, Kennan would have preferred the current president's humility to the swagger of George W. Bush or even Bill Clinton. Kennan would surely have criticized the main justification for international engagement in Libya—he never much cared about human rights—but he would have been glad that the United States let others lead the charge. When the country went to war against Muammar al-Qaddafi, it did so behind a genuine coalition. The uprisings in the Middle East have received only mild guidance from Washington. Kennan would have approved.

Or maybe he wouldn't have. As the book comes to a close, Gaddis seeks to portray the soul of the man he has been wrestling with for much of the past 30 years. In it, he finds "a profound uneasiness with complacency, or, to put it another way, a strong conviction that *we*—whoever 'we' were at the time—ought to be able to do better than *this*—whatever 'this' might turn out to be." Kennan's was a spirit that could never be satisfied.

That trait helps explain why Kennan could never stop moving, and why he ultimately didn't have the political influence he wanted. But it also explains why he left behind so many ideas, and such a powerful example of how to live and think. It is useful that he taught as he did. 🌐

Review Essay

War No More

Why the World Has Become More Peaceful

Timothy Snyder

The Better Angels of Our Nature: Why Violence Has Declined. BY STEVEN

PINKER. Viking, 2011, 802 pp. \$40.00.

As Steven Pinker observes, we recall the twentieth century as an age of unparalleled violence, and we characterize our own epoch as one of terror. But what if our historical moment is in fact defined not by mass killing but by the greatest levels of peace and safety ever attained by humankind? By way of this provocative hypothesis, the acclaimed psychologist and cognitive neuroscientist aims to liberate us from the overblown victimhood-by-contiguity of the present moment, maintaining quite credibly that we ought to be grateful for living when we do.

In his vivid descriptions of the distant and recent past, Pinker draws from a wide range of fields beyond his own to chart the decline of violence, which he says “may be the most important thing that has ever

happened in human history.” He argues that prehistory was much more violent than early civilization and that the past few decades have been much less violent than the first half of the twentieth century. He is opposing two common and related presumptions: that the time before civilization was a golden age and that the present moment is one of unique danger. Pinker rejects the idea that violence is “hydraulic,” a pressure within individuals and societies that at some point must burst through. He prefers to see violence as “strategic,” a choice that makes sense within certain historical circumstances. Thus, he describes two fundamental transitions: from the anarchy of hunting and gathering societies to the controlled violence of early states and then from a “culture of honor” associated with these states to a “culture of dignity” characteristic of the better moments of modernity. In

TIMOTHY SNYDER is Professor of History at Yale University. He helped Tony Judt compose the forthcoming book *Thinking the Twentieth Century*.

Timothy Snyder

Pinker's view, the state monopolizes violence and creates the possibility of fruitful trade and intellectual exchange, which in turn permit the development of a new, irenic individuality.

Pinker's first target is the tendency to romanticize the distant past. Since he believes that people fantasize about a peaceful prehistory, he deliberately over-emphasizes its violence, dwelling at length on the bloodiest passages of the Old Testament. His cheerful admission of this writerly tactic presages not only the friendly tone of the entire book but also one of its shortcomings. Although Pinker writes as a scientist, his approach in this book is discursive rather than deductive, charmingly but not quite persuasively advancing his *ex cathedra* views about life in general. The research of others, although abundantly and generously cited, too often seems to footnote Pinker's own prior assumptions. He is most likely correct that prehistoric life was more violent than life in agrarian civilizations and modern states, but the way he pitches the evidence raises suspicions from the very beginning. He provides horrifying descriptions of premodern killings, but not of their modern counterparts, which generates a certain narrative bias. The evidence of strikingly brutal premodern warfare and sacrifice is less conclusive than he suggests, since archaeologists are more likely to find the remains of people who die in unusual ways, beyond the reach of communal cremation or at the center of a communal ritual. The book features neat charts showing the relative decline of violence over time. But the sources Pinker cites for the numbers of dead are themselves just aggregates of other estimates, the vast majority of which, if one follows the thread

of sources to the end, turn out to be more or less informed guesses.

Yet even if Pinker is right that the ratio of violent to peaceful deaths has improved over time (and he probably is), his metric of progress deserves a bit more attention than he gives it. His argument about decreasing violence is a relative one: not that more people were killed annually in the past than are killed in a given year of recent history but that more people were killed relative to the size of the overall human population, which is of course vastly larger today than in earlier eras. But ask yourself: Is it preferable for ten people in a group of 1,000 to die violent deaths or for ten million in a group of one billion? For Pinker, the two scenarios are exactly the same, since in both, an individual person has a 99 percent chance of dying peacefully. Yet in making a moral estimate about the two outcomes, one might also consider the extinction of more individual lives, one after another, and the grief of more families of mourners, one after another.

Today's higher populations also pose a deeper methodological problem. Pinker plays down the technical ability of modern societies to support greater numbers of human lives. If carrying capacity increases faster than mass murder, this looks like moral improvement on the charts, but it might mean only that fertilizers and antibiotics are outpacing machine guns and machetes—for now.

There is also a more fundamental way in which the book is unscientific. Pinker presents the entirety of human history in the form of a natural experiment. But he contaminates the experiment by arranging the evidence to fit his personal view about the proper destiny of the individual: first,



to be tamed by the state, then, to civilize himself in opposition to the state. The state appears in Pinker's history only when it confines itself to the limited role that he believes is proper, and enlightenment figures as the rebellion of intelligent individuals against the state's attempt to exceed its assigned role.

SOLID STATE

Following a long tradition that he associates with Thomas Hobbes, Pinker emphasizes the durable coercive state as the fount of social order. States are important because they suppress the individual violence that occurs whenever people compete for limited resources. States solve the security dilemma: when one institution monopolizes violence, individuals or tribes do not have to worry incessantly that other individuals or tribes will strike them first and thus need not strike first themselves. So far, so good. But the creation of states necessitates a second level of analysis in the book, one that Pinker does not really sustain. If

the subject is violence, and states are in the picture, then the analysis requires a theory of interstate violence—war, in other words—as well as a sociological analysis of the development of pacific individuals within each state. After all, some of the very traits that maintain social order, such as the habit of obedience to authority, also make total wars and policies of mass killing possible. Instead of facing this problem squarely, Pinker conflates homicide and war. But as Pinker knows, states with low homicide rates have initiated horribly aggressive wars.

Pinker's account of the development of the state more or less stops around the French Revolution, in 1789, when his focus shifts to Enlightenment thinkers concerned with human rights and the protection of individuals from state power. The state begins as a solution for barbarians, then becomes a problem for intellectuals. Since Pinker's picture of the state is almost entirely restricted to its capacity to repress violence, it is not surprising that he focuses

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on the risks posed to a free society by the state's power to coerce. But the state is not just a machine for controlling the violence of individuals, and its institutional development did not end in the eighteenth century.

In Pinker's portrait of the modern era, the state is far in the background, even as it becomes far more capable of both good and evil. The main action is the advance of gentle commerce and human rights rhetoric, which Pinker presents as taking place apart from, or even despite, the state. But commerce is only gentle when a state can enforce property rights, overpower local rent seekers, and regulate trade. And human rights are enshrined and protected only through state action. Pinker, in a characteristically lucid formulation, notes that the emergence of the state transformed "warriors into courtiers." But his minimalist conception of the state does not include a crucial component: its ability to transform those courtiers into taxpayers. Elites who pay homage might be pacified on an individual basis, but those who pay taxes contribute to an entire system of pacification.

Throughout the book, Pinker pays surprisingly little attention to obviously relevant achievements of the state in the nineteenth and twentieth centuries, such as mass education, pollution control, and public health. He believes that literacy pacifies but does not dwell on how the masses learn to read. He admits toward the end of the book that the prospect of "additional decades of existence" makes people less violent but has little to say about how lives got longer in ways that do not involve the simple reduction of violence. Disease has always taken more lives than killing, so medical care affects

life expectancy more than homicide and war.

Instead of tracking modern political history, Pinker reduces it to a matter of good faith and good ideas. When people read the right things, he thinks, they have the right ideas, and they are less violent. Pinker argues that reading generates understanding for those different from oneself and thus a capacity for reflective empathy. This is no doubt true, but the empathy is not necessarily universal. It is impossible to imagine the Reformation and the Counter-Reformation—and thus the religious wars of the sixteenth and seventeenth centuries—without the advent of the printing press. Pinker treats that period as one of religious madness, but it is hardly satisfying to read a critique of ideas that does not acknowledge why they had appeal or how they spread, especially when the technique of propagation is supposed to bring peace. Nationalism, which Pinker thinks led to the deaths of "tens of millions" of people, is also inconceivable without books, especially bad history books. For Pinker, religion and nationalism are simply the wrong ideas, and he casts himself as a kind of referee of intellectual history, showing a red card and removing the bad players from the field.

THE WORLD WARS

A similar intervention Pinker makes in his own experiment is to dismiss the two world wars and the episodes of mass killing that took place in the first half of the twentieth century. Pinker describes these horrors powerfully and eloquently but claims they are irrelevant to his argument. He is right that historians often impose too much coherence on that time period, wanting all the violence to some-

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how make sense. But Pinker errs toward the other extreme, portraying the two world wars as “horribly unlucky samples from a statistical distribution,” and the major episodes of mass murder as resulting from “a few contingent ideas and events.” In other words, it was bad luck to have two big conflicts so close to each other, and more bad luck that they were associated with especially bad ideas. No doubt: but what does the brute fact that the wars happened mean for Pinker’s argument, and for the immediate future?

The central psychological virtue of modern civilization, Pinker claims, is “self-control.” Over the centuries, after people are pacified by the state, they learn to think ahead, to see the perspectives of others, and to pursue their ends without immediate violent action. Violence becomes not only impractical but also taboo. Nazi Germany, as Pinker seems to sense, represents a tremendous problem for this argument. Germany in the 1930s was probably the most functional state of its time, with low homicide rates and a highly literate population. Mastery of self was not the Nazis’ problem; self-control was in fact a major element of the SS ethos, as preached by Reinhard Heydrich and Heinrich Himmler. Even Adolf Hitler practiced his emotive speeches. Lack of self-control was also not the problem for Joseph Stalin’s executioners, or for Stalin and Stalinists generally. Individual Soviet NKVD men killed hundreds of people, one by one, in a single day; this can hardly be done without self-control of a very high order.

To rescue his argument from the problem posed by the mass killings of the mid-twentieth century, Pinker resorts to claiming that a single individual, in the German case Hitler, was “mostly

responsible.” Here, he misrepresents the historians he cites. It is true that most historians would subscribe to some version of “no Hitler, no Holocaust.” But what they mean is that Hitler was a necessary condition for such a calamity, not that he was a sufficient one. There were many other necessary conditions for Nazi racial imperialism. Take, for example, worries about the food supply. In the 1930s, food was highly valued in both Berlin and Moscow. This fact did not dictate which ideologies would define the two states. But in practice, both Hitler and Stalin were obsessed with mastering and exploiting fertile soil, the former to transform Germany into a self-sufficient, racially pure empire, the latter to finance the industrialization of the Soviet Union.

Without recognizing the importance of scarce resources, it is impossible to understand the very different plans for agrarian colonization that the Nazi and Soviet ideologies sanctioned. But Pinker dismisses any claim that resources (rather than bad ideas) were related to the bloodiest conflicts in modern history as a “nutball conspiracy theory.” This is an odd position for him to take, since his own history begins in a premodern world of conflict over resources. By insisting that ideas alone were to blame, he oversimplifies the issue. A more rigorous explanation would explain how political ideas interacted with scarcity, rather than insist that either one or the other must have been the problem.

Modern ideologies were not, as in Pinker’s metaphors, “toxic” forces that “drove” people to do this or that. They provided narratives to explain why some groups and individuals had better access to resources, and appealing visions of the future after an aggressive reordering.

Timothy Snyder

Nazi Germany and the Soviet Union were ideological states, but they cannot be dismissed from history simply because they were organized around the wrong ideas. Each of them had plans for economic development that were meant to privilege one group at the expense of others—plans that were inextricably entangled with justifications for why some people deserved more, others less, and others nothing but death (the extreme and unprecedented case being the Holocaust). These ideologies were effective in part because they motivated, and they motivated in part because they delivered, if not plenty, then at least visions of plenty.

We are different from the Nazis and the Soviets not because we have more self-control—we don't. We are different largely because postwar improvements in agricultural technology have provided the West with reliable supplies of food, our massive consumption of which says much about our limited self-control. But what if food were to become scarcer and more expensive, as seems now to be the trend? What if unfavorable climate change were to outrun our technical capacities? Or what if melting glaciers leave societies such as China without fresh water? Pinker claims, unpersuasively, that global warming poses little threat to modern ways of life. But it hardly matters whether he is right: states are already taking action to minimize its consequences. China, for example, is buying up land in Africa and Ukraine in order to compensate for its own shortage of arable soil. The fresh water of Siberia must beckon. If scientists continue to issue credible warnings about the consequences of climate change, it would be surprising if leaders did not conjure up new reasons for preemptive

violent action, positioning their states for a new age of want.

L'ÉTAT, C'EST NOUS

Treating Nazi Germany as a historical aberration also allows Pinker to sidestep the question of how Germans and central and western Europeans became such peaceful people after the demise of Nazism. This is a strange oversight, since European pacifism and low European homicide rates are where he begins the book. Today's Europe is Pinker's gold standard, but he does not ask why its levels of violence are the lowest in all of his charts. If, as he contends, the "pleasures of bourgeois life" prevent people from fighting, Pinker should also consider the place where these are most fully developed, and how they became so. Pinker persuasively relates how postwar economic cooperation among European states led to a pacifying interdependence, but he fails to stress that the postwar rebirth of European economies was a state-led enterprise funded by a massive U.S. subsidy known as the Marshall Plan. And he says very little about the concurrent development of redistributive social policy within those states. State power goes missing in the very places where states became preoccupied with welfare rather than warfare.

Pinker believes that people are more pacific when they have the time and the occasion to repeat interactions and reconsider their actions. Yet he has trouble acknowledging that, according to his own story, the one and only agent that can create that sort of cushioned society with educated minds and spare time has been the functional welfare state. This refusal seems rooted in Pinker's commitment to free-market libertarianism. His book's

War No More

vision of a coming age of peace is a good example of how two trends favoring political passivity—the narcissistic discursiveness of the American left and the antistate prejudices of the American right—conspire in the same delusion: that while we talk, talk, talk, markets do the work of history. Unlike the Enlightenment thinkers he lauds, Pinker fails to see that the state is not simply, as he puts it, “an exogenous first domino” that fell long ago, beginning a chain of events but remaining motionless itself. *L'état, c'est nous*: the state is what we do, how we vote, the military service we do or do not perform, the taxes we do or do not pay, the federal grants that we do or do not apply for.

Pinker shows his libertarian hand when he casually claims that “economic illiteracy” causes redistributive policies and thus “class conflict.” Many have made this claim, of course, but as he notes without seeming to realize he is disproving his own hypothesis, today’s redistributive European welfare states are the most peaceful in world history. Pinker, who exhibits no economic expertise, confuses economic literacy with a blind faith that unconstrained markets are a self-sustaining good.

A principle of the scientific method is to arrange experiments so that one’s own prior beliefs can be challenged. Pinker’s natural experiment with history generates instead a selective rereading, in which his own commitments become the guiding moral light for past and future. But of course libertarianism, like all other ideologies, involves a normative account of resource distribution: those who have should keep. There is nothing scientific about this, although again, like all other ideologies, libertarianism presents itself simply as a matter of natural reason, or,

in Pinker’s case, “intelligence.” Pinker goes so far as to suggest that libertarianism is equivalent to intelligence, since holding libertarian views correlates with high IQ scores. Since he believes that the need to regularly adjust IQ tests to preserve an average score of 100 means that we are growing more intelligent generation by generation, he deduces that we are becoming more libertarian. Pinker also conflates libertarian ideology with ethics, allowing him to conclude that we are therefore becoming increasingly moral. Each step in this argument is shaky, to say the least. As Pinker might have learned from Kant or Hume or any of the other Enlightenment figures he mentions, one cannot jump from reason to morals in this way. Even if each generation is brighter than the last, as Pinker believes, being smart is not the same thing as being just. To have an account of ethics, one needs to begin from ideas of right and wrong, not simply from mental habits that happen to be widespread in one’s own milieu and moment.

Pinker is to be praised for asking a crucial question—perhaps the crucial question—of modern history. But as he moves between the premodern world of violence and a postmodern style of discourse, he loses sight of the modern world in which we actually live. What he provides is less an answer to his question than a mode of reasoning that has little to do with the scientific study of the past and much to do with a worldview that happens to be his own. 🌐

Review Essay

Poor Choices

Poverty From the Ground Level

Timothy Besley

Poor Economics: A Radical Rethinking of the Way to Fight Global Poverty.

BY ABHIJIT V. BANERJEE AND ESTHER DUFLO. PublicAffairs, 2011, 303 pp. \$26.99.

More Than Good Intentions: How a New Economics Is Helping to Solve Global

Poverty. BY DEAN KARLAN AND JACOB APPEL. Dutton, 2011, 308 pp. \$26.95.

Portfolios of the Poor: How the World's Poor Live on \$2 a Day. BY DARYL COLLINS, JONATHAN MORDUCH, STUART RUTHERFORD, AND ORLANDA RUTHVEN. Princeton University Press, 2009, 312 pp. \$37.50 (paper, \$19.95).

Why are some countries rich and others poor? Differing accounts put more or less weight on the role of policies, geography, culture, history, and international interventions. Only by answering this question can one decide how best to reduce poverty in low-income countries. Yet few debates

about public policy are more contentious. More than half a century of intensive efforts to improve the lot of the poor in the developing world has had mixed success. Although some countries, such as China, have made enormous progress in reducing poverty, many others have languished. Today, most estimates suggest that more than one billion people live on less than \$1.25 per day.

Poverty presents both a moral and an intellectual challenge. No one can fail to be moved by seeing the slums that plague so many parts of the developing world. And the fact that one can travel a few hours by plane and find extremes of wealth and deprivation at either end of the journey is an insult to economists' notions of rationality, efficiency, and equity. There is no greater challenge to the discipline.

Yet traditional economics alone is not enough to grasp the problem fully.

TIMOTHY BESLEY is Kuwait Professor of Economics and Political Science at the London School of Economics.

Poor Choices

I learned this at a pivotal moment early in my career when a senior colleague asked me about my research interests. I proudly listed development economics among them—and was promptly deflated when he told me that he, too, had once been interested in development, until it dawned on him that most of the problems of the developing world were political and so he did not have the necessary expertise to study the issue. Thankfully, the field of economics has changed a lot in the years since, and issues of politics and economics are routinely interwoven when trying to understand persistent poverty.

Economists have been better able to understand poverty thanks to growing access to micro-level data and new decision-making models that incorporate psychological factors. Three engaging new books showcase these microeconomic advances: *Poor Economics*, by Abhijit Banerjee and Esther Duflo; *More Than Good Intentions*, by Dean Karlan and Jacob Appel; and *Portfolios of the Poor*, by Daryl Collins, Jonathan Morduch, Stuart Rutherford, and Orlanda Ruthven. Written in language sure to appeal to a general reader, they all focus on the micro level of poverty and on the human conditions that underlie it. Their authors make extensive use of vignettes—an unusual move for economists—introducing readers by name to real people whose stories illustrate broader concepts.

Informed by extensive experience in the field, their understanding of poverty is refreshingly bottom-up. Only by figuring out what happens on the ground, their thinking goes, can they unlock the bigger picture. The problem with such focused efforts, however, is that the authors largely set aside the role of politics and in so doing neglect much of the bigger picture. After

all, some of the greatest successes in raising living standards have come about not by altering individuals' choices but by altering decisions made by governments.

NEW ECONOMICS

Mainstream economics used to assume unquestioningly that the poor were rational decision-makers, *homines economici* who spent what little they had in an informed and farsighted way. But over the past 30 or so years, economists have increasingly taken into account the psychology of decision-making. They now acknowledge, for instance, that people frequently lack self-control, valuing future benefits but acting on short-term impulses. And they have begun to appreciate how poverty could create certain pathologies that might further distort thinking. For example, laboratory evidence suggests that choices made under stressful conditions tend to be worse than those made without stress. Such insights have opened up a whole new range of concerns that need to be taken into consideration when studying the behavior of the poor.

Economists have also become more interested in the impact of social constraints on behavior. A profession that was once suspicious of the power of culture and social structures to explain economic phenomena now routinely builds these factors into its models. This development has led to new insights, such as the idea that people do not save in part because they face social pressure to spend or support their relatives. Seemingly irrational expenditures on lavish weddings or funerals, for example, make more sense when one takes such demands into account.

Research methods are changing, too. One of the most important innovations

Timothy Besley

in economists' tool kits has been the use of randomized control trials to evaluate what works—studies, like those in medicine, that compare the outcomes for a randomly selected treatment group (which receives, for example, subsidized fertilizer) with those for a control group. Such research has become more commonplace thanks to the growth of nongovernmental organizations (NGOs); governments are generally reluctant to leave a control group unaided. This development is also part of a wider movement toward evidence-based policy-making, and such research is now being conducted at organizations such as MIT's Poverty Action Lab and the NGO Innovations for Poverty Action. Three of the authors of the books under review—Banerjee, Duflo, and Karlan—played leading roles in establishing these institutions.

As befits their research backgrounds, Banerjee and Duflo and Karlan and Appel explicitly embrace three new developments in the study of poverty: behavioral models of decision-making, an appreciation of social constraints, and randomized experiments. Consider how the authors treat the question of health and nutrition. Sicknes reduces productivity and hence exacerbates poverty, so economists have tried to understand why the poor sometimes make puzzlingly unhealthy choices. Banerjee and Duflo recount the story of a man named Oucha Mbarbk, who lives in a remote village in Morocco. When they ask Mbarbk what he would do if he had more money, he replies that he would spend it on food. "We were starting to feel very bad for him and his family," they write, "when we noticed a television, a parabolic antenna, and a DVD player in the room where we were sitting. We asked him why he had bought all these things if he felt the family

did not have enough to eat. He laughed, and said, 'Oh, but television is more important than food!'" To dismiss such preferences as simply irrational would be an error. As Banerjee and Duflo point out, alleviating boredom can be a central priority of poor people.

Banerjee and Duflo also show how societal constraints, such as superstitious beliefs and a lack of reliable information, deter poor people from taking advantage of low-cost medical advances with high returns, such as vaccinating their children—proverbial dollar bills on the sidewalk, waiting to be picked up. Without a proper understanding of the underlying constraints, public health campaigns, such as attempts to raise vaccination rates, are unlikely to work well.

Throughout their book, Banerjee and Duflo examine all facets of the behavior of the poor through this microscopic lens and discuss how certain types of interventions can make things better. They unapologetically propose a solution they acknowledge to be paternalistic: outside interventions by those who know best. But that type of policy makes sense only after detailed investigations of the conditions under which the interventions will occur, and Banerjee and Duflo are careful to tailor their recommendations to the circumstances on the ground.

MANAGING MONEY

Karlan and Appel, in their entertaining and quirky book, take a similar approach to analyzing poverty, emphasizing faulty decision-making and laying out the evidential findings that have guided successful development projects. They boldly offer a list of seven ideas that work and hence, they argue, should be scaled up:



REUTERS

Help Wanted: a two-year-old at a hospital in Sudan, April 2010

micro-savings accounts, which help the poor hold on to their income; reminders to put money away, which boost savings rates; commitment devices, which lock up savings for a specified period; prepaid fertilizer sales, which allow farmers to invest in future improvements in crop yields; deworming treatments, which keep children in school; remedial-education programs, which focus on the lowest-achieving students; and chlorine dispensers, which provide clean water.

Karlan and Appel frequently discuss the specific studies—many of them randomized control trials—that support these claims. Consider the problem of securing savings. They recount a randomized experiment in Kenya that found that when women were offered non-interest-bearing savings accounts, a remarkable proportion of them agreed to set one up. It also revealed that the accounts helped women cope better with periods of illness, since having these

savings gave the subjects an alternative to pulling capital out of their businesses.

Portfolios of the Poor is more specific. As Collins, Morduch, Rutherford, and Ruthven summarize their argument, “Not having enough money is bad enough. Not being able to manage whatever money you have is worse.” Their book is a detailed effort to understand how poor people manage—and, frequently, mismanage—the meager resources at their disposal. They draw on more than 250 financial diaries collected in Bangladesh, India, and South Africa that tracked how money was earned and spent, along with interviews with the diarists. The result is a unique window onto what poverty means for these households.

The data reveal a rich web of financial arrangements and document daily decisions about saving and borrowing. Readers meet a married couple from Bangladesh, Hamid and Khadeja, who have accumulated \$175 in savings through

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six different instruments but owe \$223 to shopkeepers, their family, their landlord, and Hamid's employer. The complexity of these arrangements turns out to be typical of what the authors find elsewhere. Their subjects must struggle not only with the fact that their incomes are low but with the fact that they are unpredictable and irregular, too; many of the world's poor rely on seasonal earnings from agriculture. Helping the poor, the authors conclude, is thus a matter not only of raising their incomes but also of finding better ways to help them manage the uncertainty they face in their daily lives.

The problem of financial management among the poor comes up in the other two books as well. Development economists have made much of the difficulty of borrowing, but until recently, they paid relatively little attention to the difficulty of saving. Individuals might find the cost of visiting a bank and having to wait in line too burdensome, or give in to demands for cash from friends and relatives, or remain ignorant of the wonder of compound interest, or simply lack the patience for long-term returns. Understanding these deterrents to saving requires a focus on the micro level. To encourage saving among the poor, the three books suggest a reorientation away from microcredit, the original focus of flagship programs such as Muhammad Yunus' Grameen Bank, toward microfinance, which provides easier-to-access saving opportunities with the possibility of regularizing such decisions.

THE DEVELOPMENT-DRIVEN STATE

Over the past 25 years, the greater use of microdata to generate insights into decision-making and societal constraints has transformed development economics.

Scholars know far more than ever before about who the poor are, how they behave, and the constraints they face. But another major innovation in development economics gets little attention in these three books: an increasing focus on political factors in shaping development. Only Banerjee and Duflo offer any real discussion of political economy, and this appears only at the end, largely as an afterthought. And even here, when treating broader political questions, their approach is essentially focused on the micro level. In line with their general focus, they argue for progress "at the margin," where incremental change is feasible. They are largely dismissive of institutions at regional and national levels, which they regard as too unwieldy. But there is no getting away from the fact that public action at the higher tiers of government matters when it comes to sound policymaking.

Thus, the authors of these books could be criticized for paying insufficient attention to issues of political economy. One of the central challenges in developing states is getting the government to direct public resources toward public goods rather than toward special interests—in the form of corruption, white elephants, or narrowly targeted transfers for the benefit of elites. Arguably, this shift in priorities has been the chief achievement of many modern states, and it is one that poorer countries must emulate if their governments are to become servants of the public interest. If governments build tax and legal systems and direct public spending toward the needs of their populations, then they will be able to foster growth and human and social development—and, with that, reduce poverty. Although the means by which governments can make this shift

are complex, the subject is simply too important for economists to dismiss.

One place to look for lessons is in China. Over the past three decades, the country has grown remarkably quickly—achieving, in the process, what is probably the largest reduction in mass poverty the world has ever seen. The World Bank estimates that around 600 million fewer Chinese live in chronic poverty today than did in 1980. China managed this by transforming itself into a developmental state, one that is geared toward transforming the economy and the lives of its citizens, funneling significant resources into public goods such as education and infrastructure.

China's experience is reminiscent of the improvements in the provision of public goods made by governments in the industrialized world during the late nineteenth and early twentieth centuries. In city after city, residents saw their lives transformed by access to drinking water, functioning sanitation systems, and electricity. As in China, an increasingly strong and well-organized state drove economic development, with municipal governments cooperating with higher tiers of government. This process created a symbiotic relationship with private-sector development: governments educated the labor force and built roads, railways, and bridges, which, in turn, encouraged the private sector to invest in factories and create new jobs. Although the benefits were sometimes uneven, the impact on the living standards of many citizens was immense.

But there is no magic formula for building a developmental state. Many countries have tried and failed. The trick is getting political and economic structures to work in tandem, as China has managed to do so far. The Chinese government

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has institutionalized its rule through a one-party system that constrains power with internal checks and balances and that gives policymakers an incentive to take a long-term view. The economic success that this system has delivered has muted citizens' calls for political change, establishing a social contract that hinges on continued growth. But the model is vulnerable to an economic slowdown or demands for change as a larger middle class seeks political liberalization as an end in itself. The result could be either the democratization of the system or an increasingly brutal regime. Only in rare cases have governments been able to keep democratic demands at bay indefinitely by providing ever more public goods. China's best hope is to open the political system gradually while increasing the constraints on executive power. But managing such a feat will not be easy.

For all these reasons, the Chinese model is not an easy or attractive model for other countries to follow as they seek to build effective states and thereby reduce poverty. Yet the western European model is problematic, too, since up until World War II, it emerged largely out of the need to fight countless wars. That said, Europe does demonstrate how institutional constraints on executive power, along with a more or less free press, can prevent strong states' abuse of power. European states have also learned over the past 150 years that their survival as strong states rests on their ability to orient themselves around meeting their citizens' social and economic needs. Even this change, however, may have been linked in part to the need to ensure that their populations were fit enough to fight; in 1906, the British government gave local councils the power to

provide free school meals to poor children in part because it had had such a hard time recruiting able-bodied men to fight in the Second Boer War. Although the example does show how the public's sense of common goals can foster a national identity and a stronger state, nobody, of course, would contend that fighting more is a serious prescription for state development in the modern world.

In fact, no one really knows how to get a state to start recognizing and addressing the core needs of its population. This outcome seems more likely to happen in countries where a parliamentary system diffuses power, where built-in institutions oversee public policies, and where a strong civil society keeps the state in check. But the recent history of the developing world suggests that these features are not easily obtainable. The vast majority of post-colonial countries have done their best to dismantle any checks and balances that they inherited, and many have replaced parliamentary systems with presidential ones that concentrate political power. Crippled by weak institutions, developing states have frequently been captured by favored elites rather than ruled by broad-based coalitions. Political violence, in the form of either political repression or civil war, has become endemic.

Outside donors have tried to help such fragile states by lavishing them with foreign aid, but as admirable as the intention behind such largess may be, it often ends up entrenching governments that do little to promote development. And when outsiders try to use their leverage to spur political reform, it raises many difficult questions; for one, the legacy of colonialism ensures that the international community will always be wary of pushing too hard

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for social or political transformation in developing states.

The alternative is to give up on existing state structures. For example, multilateral donors and aid agencies could try to build independent agencies to deliver public services in the developing world, institutions that would operate on a larger scale than NGOs currently do and adopt the mantra of evidence-based policymaking. But if states are to remain legitimate in the eyes of their populations, then such agencies will eventually have to be absorbed by the government. Or perhaps they could remain quasi-independent and democratically governed, the way that school boards and hospital trusts are. Such a setup, however, has yet to be tried in the developing world on a systematic basis.

SCALING UP

None of these lessons suggests that there is much low-hanging fruit to be had when it comes to eradicating poverty. Still, economists need to at least try to understand what goes into making states better at fostering development. As Torsten Persson and I argued in our book, *Pillars of Prosperity*, economists have neglected larger questions of politics and taken state effectiveness as a given rather than as something to be explained.

Nonetheless, there is plenty of value in stepping back from the complex politics of macroeconomic policymaking and drilling down into the nitty-gritty of development. The three books reviewed here are attractive for precisely that reason. Their straightforward prescriptions are based on what the authors have seen on the ground, and they deliberately eschew any complex political strategizing. This bottom-up perspective lends the

books special credibility, and the authors' work has already made a real difference to the lives of the poor—and will continue to do so whether or not these economists start wading into big-picture debates.

Moreover, these books' focus on ground-level strategies to tackle poverty contributes to the larger effort of building better states. Demonstrating that certain interventions work on a small scale highlights just how much could be achieved if a more effective state were to try them on a larger scale. Expanding programs that work could trigger a virtuous cycle, with initial successes leading to further ones, as was the case in western Europe. States there first became strong thanks to the exigencies of war. Having entrusted the government with providing security, citizens later came to support directing resources toward health care, education, and social insurance. Thanks to the demonstrated success of the early movers, pretty much every country in western Europe has embraced universal health care. Such success has widened the domain of state intervention and involvement.

There is inherent value, then, in demonstrating what types of poverty-reduction strategies work at a micro level. In order for those strategies to be pursued on a larger scale, however, the people who make things happen, policy wonks and regular citizens alike, must be convinced of their worth. Thus, the authors of these books should be commended for stepping out of their academic warrens to write them. Readers will realize that making the world a better place requires more than good intentions; it takes hard evidence, too. And they will gain a deeper understanding of poverty, one informed by conditions on the ground. 🌍

Response

Can the Center Hold?

Understanding Israel's Pragmatic Majority

Yossi Klein Halevi

A majority of Israelis—around 70 percent, according to a recent poll by the Truman Institute for the Advancement of Peace, in Jerusalem—support a two-state solution. Yet that same majority is deeply skeptical of Palestinian intentions. To understand this seeming contradiction and the psyche of the Israeli mainstream, one should read the two articles that recently appeared in these pages on the Palestinian question—“The Problem Is Palestinian Rejectionism,” by Yosef Kuperwasser and Shalom Lipner, and “Israel’s Bunker Mentality,” by Ronald Krebs (November/December 2011)—not as a debate but as complementary arguments. Centrist Israelis endorse Krebs’ argument that the occupation is an existential threat to the Jewish state. They understand that ending it would ease the demographic challenge to Israel’s Jewish majority and allow Israel to retain both its Jewish and its democratic identities.

A two-state solution would also deflate the growing international movement to delegitimize not only the occupation but also the existence of Israel itself.

Yet centrist Israelis also embrace the contention made by Kuperwasser and Lipner: that the Palestinian national movement, from Hamas to the Palestinian Authority, rejects Jewish sovereignty over any part of the land from the Mediterranean Sea to the Jordan River. Centrist Israelis see PA President Mahmoud Abbas as merely a tactical moderate who opposes terrorism only because it has harmed the Palestinian cause. They base their suspicions on speeches such as his address to the UN General Assembly last September, when Abbas condemned “63 years” of Israeli occupation—implicating the founding of Israel in 1948, not just the occupation of Gaza and the West Bank, which began in 1967. For centrists, the greatest obstacle to

YOSSI KLEIN HALEVI is a Fellow at the Shalom Hartman Institute in Jerusalem and a contributing editor to *The New Republic*.

Can the Center Hold?

peace is the demand of Palestinian leaders, including Abbas, for the right of return of descendants of Palestinian refugees not just to a Palestinian state but also to Israel proper. These Israelis see Abbas' insistence on this right as proof that the Palestinian leader seeks to destabilize Israel from within and does not accept the right of the Jewish people to their own sovereign nation.

Such fears inhibit centrist Israelis from fully embracing the peace process, since they believe it will lead to an irredentist Palestinian state sitting on Israel's borders. Rocket attacks from the West Bank could make daily life in Israel's main population centers unbearable. If the Israeli army re-invaded to stop the attacks, Israeli officials and soldiers could find themselves charged with war crimes, just as they were after Israel attacked Gaza in 2008. And so although centrists understand how damaging to both sides the occupation has become, they view ending it before the Palestinians accept Israel as a Jewish state as an even greater existential threat. Indeed, according to the Tel Aviv University Peace Index, a monthly public opinion survey, in January 2011, nearly 70 percent of Israelis polled moderately or strongly accepted the claim that even if a peace agreement were signed, the Palestinians would continue their struggle against Israel.

This is but one of the paradoxes with which centrist Israelis grapple. Another is the way they understand their country to be both a David and a Goliath: Goliath toward the Palestinians, but David toward the Arab and Muslim worlds. Israel remains the strongest military power in the Middle East. But in recent years, the balance has begun to shift. Iran, through its terrorist allies—Hezbollah in Lebanon and Hamas in Gaza—has established a presence in

two enclaves on Israel's borders. These organizations, equipped with tens of thousands of rockets, can now target all of Israel's population centers, many of which are directly threatened for the first time in the history of the Jewish state. And with Iran pursuing nuclear weapons, Israel might soon lose its status as the sole nuclear power in the Middle East, which has been its main strategic advantage for decades. Then there is the emergence of a government in Turkey with Islamist roots and the growing power of the Muslim Brotherhood in Egypt and Jordan, which are eroding Israel's regional alliances. These factors—not the occupation, as Krebs writes—have created Israel's "bunker mentality."

Centrist Israelis realize that the Jewish state cannot indefinitely remain both an occupier and a member in good standing of the Western club of liberal democracies. Yet they are acutely aware that Israel is the only country threatened with destruction by some of its neighbors. And they face a Palestinian national movement whose goal, they believe, is not only the creation of its own state but also the displacement of its occupier's. Arguably, no other occupier has had to worry, as Israel does, that withdrawing will not merely diminish but destroy it.

The international community fails to acknowledge Israel's unique dilemma, reducing its options to a simplistic choice between occupation and peace, as Krebs implicitly does. This failure further undermines Israeli confidence in the peace process. The old slogan of the Israeli left, "Peace is better than the complete land of Israel," has turned out to be a mockery. Neither peace nor the complete land of Israel, centrists suspect, was ever a realistic option.

Yossi Klein Halevi

THE MAKING OF THE ISRAELI CENTER

Until the late 1980s, support for a Palestinian state could be found only on Israel's far-left fringe. Most Israeli Jews saw Palestinian sovereignty as inconceivable, especially after the Palestine Liberation Organization (PLO) adopted the "phased plan" in 1974, which stated that it would use any territory evacuated by Israel as a base from which to destabilize and eventually destroy it.

Under these circumstances, the Israeli mainstream argued about not whether to settle in the West Bank but where. Labor Party leaders such as Yitzhak Rabin and Shimon Peres hoped to transfer most of the West Bank to Jordan while supporting Israeli settlement of underpopulated areas. Almost all Israeli Jews agreed that the territories had been acquired legitimately in a war waged to defend themselves against destruction. The convergence of security needs with Israel's historical claims to biblical Judea and Samaria, birthplace of the Jewish people, resonated broadly. And the occupation appeared relatively cost-free. For years after 1967, the territories were mostly quiet, there were no army road-blocks, and most Palestinians had jobs.

The first intifada, the uprising in the territories that began in late 1987 and lasted into the early 1990s, ended the illusion of a benign occupation. Street battles with civilians throwing rocks and Molotov cocktails scarred a generation of Israeli soldiers. Meanwhile, much of the Israeli public came to realize that the occupation meant suppressing a hostile population and was therefore untenable. For the first time, mainstream Israelis began speaking of separating from the Palestinians.

This transformation led to Israel's acceptance of the Oslo peace process. Since the

right had failed to bring security through territorial expansion, Israelis reasoned, perhaps the left would succeed in bringing peace through territorial concessions. Through the 1990s, increasing numbers of Israelis, including some on the right, came to accept the inevitability of a two-state solution and its attendant compromises, such as the division of Jerusalem.

But just as the first intifada ended the fantasy of Greater Israel, the second intifada, which began in September 2000, ended the fantasy of land for peace. Krebs notes that the second intifada "left Israelis frustrated and disillusioned." In fact, the Israeli reaction more closely resembled rage and despair. The left had promised that if only Israel would offer the Palestinians statehood based on the 1967 lines, the result would be peace. And Prime Minister Ehud Barak did precisely that when he accepted the "Clinton parameters" of December 2000, which proposed a contiguous Palestinian state on almost all the territories with its capital in East Jerusalem. But the violence escalated into the worst wave of terrorism in Israel's history. For the first time since 1948, the Israeli home front became the main front. The suicide bombings seemed to vindicate those on the right who warned that the phased plan remained the strategy of the Palestinian national movement.

The second intifada shattered the Israeli left at precisely the moment when the government had adopted its policy. Newspapers published interviews with leading left-wing politicians and journalists who, having struggled for decades to convince their skeptical fellow citizens of the need to negotiate with the PLO, confessed their naiveté. The Israeli journalist Amnon Dankner compared the effect of the second

Can the Center Hold?

intifada on the Israeli left to the impact on the world communist movement of Soviet Premier Nikita Khrushchev's anti-Stalin "secret speech" in 1956. The peace camp had won the ideological war against the settlers only to be discredited by its Palestinian partner. Except for a small group of true believers, most Israelis concluded that their country no longer bore the chief moral responsibility for the occupation. The Palestinian cause lost one of its greatest assets: the guilty Israeli.

HAWKS TO THE MIDDLE

Still, for centrist Israelis, the consequences of the second intifada did not negate what they had learned in the first intifada. Indeed, those two traumatic events came to define the current centrist worldview. As the center saw it, the left had correctly diagnosed the impossibility of long-term occupation and the right had seen the folly of expecting to achieve peace with a group that denies Israel's legitimacy. The result was paralysis.

The most ambitious centrist attempt to break out of that stalemate and reject permanent occupation came in 2005, when Israeli Prime Minister Ariel Sharon unilaterally withdrew from Gaza and uprooted 21 Israeli settlements. Sharon, elected half a year after the outbreak of the second intifada, was the first Israeli public figure to successfully embody the new center. As the father of the settlement enterprise, he made for an unlikely centrist hero. But he understood that Israelis wanted a leader who adopted a hard line on security and a pragmatic line on territory.

The Gaza withdrawal expressed the centrist mood. If Israel could not occupy the Palestinians or make peace with them, then it needed to extricate itself from the

territories on its own terms. To the shock of the settlement movement, whose leaders had assumed that the second intifada confirmed the logic of their enterprise, a majority of Israelis supported Sharon's move. His successor, Ehud Olmert, hoped to unilaterally withdraw from most of the West Bank, as well. But Hamas and other militant groups launched thousands of rockets from Gaza into southern Israel immediately after the withdrawal there, forcing many committed unilateralists to acknowledge that continued West Bank occupation was preferable to unchecked missile fire.

The Kadima Party that Sharon founded to implement the withdrawal from Gaza has floundered in his absence. But the center remains a powerful force—a fact demonstrated by Israeli Prime Minister Benjamin Netanyahu's attempt to assume its mantle. Although Netanyahu received scant credit for it abroad, many Israelis saw his endorsement of a two-state solution in 2009 as a breakthrough, bringing the Likud Party, however fitfully, into the mainstream consensus regarding a Palestinian state. Indeed, there is no longer any major party—including the hawkish Yisrael Beitenu (Israel Our Home), the party of Israeli Foreign Minister Avigdor Lieberman—that rejects the principle of a two-state solution. And although much of the international community dismissed Netanyahu's unprecedented ten-month settlement freeze as insufficient, centrist Israelis applauded it.

Some centrists have criticized Netanyahu for refusing to endorse the 1967 borders as a starting point for negotiations. But they fault him for tactical reasons, not strategic ones. By accepting the Clinton parameters, of which the 1967 borders are a

Yossi Klein Halevi

key principle, centrist commentators have argued, Netanyahu could have exposed Palestinian intransigence. But few Israelis believe that any initiative at this point would be met by the Palestinian concessions necessary for peace. So long as Hamas remains ascendant and Palestinian leaders from all factions insist on the right of return to Israel proper, no Israeli prime minister will sign a peace agreement.

Despite its deep skepticism of Palestinian intentions, the centrist majority continues to support a two-state solution. For the sake of a peace agreement that will grant Israel legitimacy, centrist Israelis are prepared to uproot dozens of West Bank settlements and concentrate the rest in settlement blocs along the 1967 borders. But the experience of two previous failed attempts to end the occupation has convinced centrists that the settlements are not the main obstacles to an agreement. The Clinton parameters, and an even more far-reaching peace plan presented by Olmert to Abbas in 2008, would have resolved the settlement issue. True, Israel constructed settlements throughout the territories to prevent a contiguous Palestinian state. And the infrastructure that sustains these communities, such as roads and military installations, is substantial. But as the Gaza withdrawal demonstrated, settlements can be dismantled and infrastructure left behind.

If a Palestinian leader emerges who is prepared to accept the legitimacy of Jewish nationhood, his most likely peace partner would be another incarnation of Sharon: a onetime hawk who has moved toward the center. It is no coincidence that it took two hawks—Menachem Begin and Sharon—to initiate Israel's two substantive territorial withdrawals. Israelis feel most

secure with a hawkish leader, especially when embarking on a dovish initiative; although the Labor Party first advocated a unilateral withdrawal from Gaza during the second intifada, Israelis trusted only Sharon to carry it through. The Gaza withdrawal offers a political model for a future West Bank pullout: a formerly right-wing leader galvanizing a centrist majority to implement a left-wing vision.

For that to happen, Israelis will need to see a shift in the mindset of the Palestinian national movement. Centrist Israelis have made the conceptual breakthrough required to heal the conflict, recognizing that it is a struggle between two legitimate national narratives. The Palestinians must demonstrate that they, too, are ready to grapple with the complexity of the struggle. Were Palestinian leaders to accept the right of the Jewish people to national sovereignty and agree to confine the right of return for Palestinian refugees to a Palestinian state, they would open the path to statehood. As Kuperwasser and Lipner imply, the way to convince centrist Israelis to empower the Palestinians is for Palestinian leaders to accept the legitimacy of Jewish empowerment. 🌐

Response

The Great China Debate

Will Beijing Rule the World?

The Wobbly Dragon

DEREK SCISSORS

Arvind Subramanian claims that China will unquestionably replace the United States as the dominant global power in the next two decades (“The Inevitable Superpower,” September/October 2011). He is right that if the U.S. economy continues on its current trajectory, the United States will not be able to maintain its position of global leadership. But he is far too bullish on China. Subramanian overlooks Chinese policies that will complicate the country’s economic rise and ignores the possibility that Chinese growth will simply stop. And he uses a definition of “dominance” that bears little resemblance to the U.S.-style preeminence he sees China assuming.

Consider how Subramanian measures China’s growing power. He cites the ability of Beijing to convince African countries to recognize it instead of Taipei, but out-muscling Taiwan diplomatically is hardly a sign of global leadership. He sees the ease with which China undervalues the yuan by pegging it to the dollar as proof of the

country’s strength, but hiding behind a foreign currency is not a sign of economic might. He forecasts that China in 2030 will have an economy that is one-third larger than the United States’, yet he admits that it will remain only half as wealthy. These are notable trends, to be sure, but not ones that indicate China will attain anything close to the position the United States has held over the past 60 years.

The biggest flaw in Subramanian’s index of dominance is the importance he assigns to China’s status as a net creditor. Based on this alone, he is prepared to say that China’s economic strength is already comparable to that of the United States. But China’s creditor status does not make up for the fact that its economy is presently less than half the size of the United States’ and its people are barely one-tenth as wealthy as Americans.

Creditor status is also a misleading metric by which to judge China because it is usually used to describe financially open economies, and China is largely closed. Countries with open economies can invest their money in many places. Beijing, because it cannot spend its foreign reserves at home, is forced to keep buying U.S. Treasury bonds.

Subramanian and His Critic

China's creditor status arises largely from its weaknesses, not its strengths. The country's \$3.2 trillion worth of foreign currency holdings represents an imbalance between investment and consumption. Instead of loaning money to rich countries, China should be importing capital in order to speed its domestic development and meet its sizable needs, starting with properly capitalized pension and financial systems.

China's financial books are strictly divided, with huge assets in foreign currency (primarily dollars) on one side and huge liabilities in local currency on the other. Local governments have incurred high debts by spending heavily on programs such as railroad expansion and by borrowing to fund the 2009 stimulus (which came mostly from local, not national, government coffers). Beijing should be paying down this debt and addressing other domestic shortfalls with its mountain of foreign currency, but it cannot do so under its present balance-of-payments rules, which are designed to keep foreign currency in the hands of the national monetary authorities. Due to a closed capital account, domestic holders cannot send money overseas, and foreign currency can be converted to yuan only through the state financial system.

The Chinese government has not let money flow freely because doing so would undermine its control of domestic interest rates, reducing its ability to influence economic cycles, and it would expose the domestic banking sector to devastating competition. If domestic entities were allowed to send money abroad, hundreds of billions of dollars would flee the country for financial institutions that operate commercially, unlike Chinese banks. Such a stark fear

of competition does not suggest a country ready to exert dominance anytime soon.

Lastly, Subramanian inflates China's financial influence over the United States, forgetting that influence in a buyer-seller relationship is determined not by what-if scenarios but by who has better alternatives. The United States has already diversified away from Chinese debt by having the Federal Reserve flood the U.S. financial system with liquidity. This is hardly ideal, but it has driven down the Chinese share of U.S. debt while keeping interest rates historically low. In contrast, Beijing, despite its best efforts to diversify, still holds 70 percent of its foreign currency reserves in dollars. The reason is simple: those reserves are so large and growing so quickly that there is no alternative. The United States needs China to keep U.S. interest rates below historic norms; China needs the United States to maintain its entire balance-of-payments system.

Even if Subramanian acknowledges that China's lopsided financial system is holding the country back now, he assumes that Beijing will soon rewrite its balance-of-payments rules and become an open economy. This assumption underestimates the Communist Party's antipathy to change. In fact, the principal advocate for such reforms has been Washington, which hopes to encourage China's transformation from an investment-led to a consumption-led economy. Such a transition would undermine China's net creditor status—what Subramanian sees as its main claim to dominance. But implementing market reforms would also allow China to keep growing at its blistering pace and surpass the United States in GDP. If China

insists on maintaining government control over development, on the other hand, its long-term growth prospects will be dim.

Salvatore Babones (“The Middling Kingdom,” September/October 2011) warns against drawing conclusions about China’s trajectory by simply projecting its growth rates forward. Indeed, it is entirely possible that Chinese GDP growth will simply stop. Growth depends on land, labor, capital, and innovation. China has depleted its ecology, its labor surplus will soon begin to erode, and vast over-spending has driven down the return on capital—all discouraging trends from the standpoint of growth.

As for innovation, Subramanian praises China’s growing technology sector and its ability to absorb new advances. But a true economic leader must create, not absorb, and Beijing’s favoritism toward large state firms will hinder innovation. Moreover, the quality of the Chinese higher-education system is poor and not necessarily improving. A no-growth scenario is a genuine danger—just ask the Japanese.

By underemphasizing or ignoring China’s various weaknesses, Subramanian underestimates the United States’ ability to influence the competition with China. That said, his criticisms of the United States are valid; indeed, his baseline prediction of U.S. growth at 2.5 percent annually may be too optimistic. Crippled by debt, the United States faces a period of stagnation. If the overall economy remains sluggish, a lack of import growth will cause trade to lag and further reduce the United States’ global influence.

Still, the Chinese dragon will not fly forward indefinitely, as Subramanian

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Subramanian and His Critic

suggests; it may even crash. For the foreseeable future, China will not attain the kind of dominance the United States has long held. The world should not expect to crown a new global leader but prepare for the absence of one.

DEREK SCISSORS is *Research Fellow in Economics at the Asian Studies Center of the Heritage Foundation and Adjunct Professor of Economics at George Washington University.*

Subramanian Replies

Derek Scissors argues that my article prematurely heralds the rise of China and overstates the dominance that it will achieve. Above all, he takes issue with the importance I give to China's status as a net creditor and disputes my assessment of the country's prospects for growth and reform.

For starters, Scissors is simply wrong to claim that my characterization of China's economic might is driven by its status as a net creditor. In the index I designed to measure economic dominance, I give net creditor status a weight of just five percent; the size of a country's economy and the amount it trades account for the rest. I argue not that China's dominance in 2030 will depend on the country's remaining a creditor nation but rather that it will mostly stem from China's economy and trade outpacing those of the United States by nearly 50 percent.

That said, history is replete with examples of countries whose status as creditors has given them great power. After World War II, for example, the

United States used its position as Europe's major creditor to design the rules of the International Monetary Fund, which, not coincidentally, favored the United States. Today, Europe is assiduously courting the world's new major creditor, China, in the hope that Beijing will put up the money for an EU bailout fund. If it does, it will surely use this leverage to shape the rules of international finance and trade.

Scissors also argues that China's creditor status reflects an underlying weakness because it is caused by "an imbalance between investment and consumption." But China's creditor status is the result of a strategy that has delivered humanity's most dramatic economic transformation in the shortest period of time, posting unprecedented rates of growth and consumption. That is hardly a sign of weakness.

Still, it is true that this strategy has distorted the economy, especially the prices of capital and foreign exchange. Keeping these prices artificially low will certainly entail future costs. Moreover, when China's exchange rate reverts to normal levels, its hoard of foreign reserves will lose value in terms of yuan. But whether these future costs will prove catastrophic for China, as Scissors contends, depends on the country's prospects for growth, since rapid growth makes all problems manageable.

On this issue, Scissors alleges that I am being too bullish; I would argue that he is being far too pessimistic. My central growth forecast assumes that China will grow at a rate of seven percent over the next two decades, about 40 percent slower than its current growth rate of 10.5 percent. This is a conservative estimate.

The Great China Debate

Plenty of countries at China's level of economic development have posted that kind of growth. And as long as China's standard of living remains lower than those of Western countries, its wages will stay low. This will continue to make China an attractive destination for investments and exports and will spur more growth. For this reason, Scissors' Japan analogy is misleading: at the time of its slowdown in the 1990s, Japan had already achieved Western standards of living and exhausted its catch-up possibilities. China, by contrast, has a GDP per capita that is only about 20–25 percent of the United States', which means China will remain internationally competitive for the foreseeable future.

Scissors nonetheless insists that China's growth could soon stop because the Communist Party will resist making necessary financial reforms. But China's policymakers know that delivering steady growth, which their legitimacy hinges on, will require reform. And although growth could always be derailed by developments overseas (such as a European crisis), China has shown that it can ably counteract such problems. In 2008, when the financial crisis caused Chinese exports to collapse, Beijing implemented a mammoth stimulus package to offset the shock in a way that few other countries could. As this suggests, China still has both the political will and the fiscal ability to grapple with problems as they arise.

Finally, Scissors argues that China will not be able to exercise economic dominance in the way that the United States has so long as it lacks the ability to create technology. True, innovation can give a country a unique kind of influence by inspiring others to want what it wants.

As long as China remains politically closed, with a state-dominated economy and a lackluster technology sector, it cannot hope to attain this kind of dominance.

But my article focuses on a different kind of dominance: the ability to get others to do what you want or to prevent them from forcing you to do what you do not want. With its large and rapidly growing economy, China already wields such power. Consider, for example, how China's depressed exchange rate hurts economies from the United States to Bangladesh. Yet despite protests from across the world, Beijing continues to do what it wants. If that's not dominance, what is? 🌐

Responses

Both Sides of the COIN

Defining War After Afghanistan

Theory Versus Practice

CHRISTOPHER SIMS

In his analysis of the shortcomings of the U.S.-led war in Afghanistan, Bing West offers a compelling assessment that, as he writes, “counterinsurgency as nation building became a Sisyphean mission” (“Groundhog War,” September/October 2011). But the real problem is not with counterinsurgency doctrine itself but rather with how it is being applied. U.S. military planners and officers should not entirely abandon counterinsurgency, as West predicts they will; instead, they should return to counterinsurgency’s guiding principles and make sure they are properly implemented on the ground.

For starters, West argues that Western handouts have led to a culture of entitlement in Afghanistan, which, in turn, has bred opportunism rather than patriotism or a desire for self-improvement. This is a real concern: in 2010, foreign aid was equivalent to approximately 90 percent of Afghanistan’s total GDP. To show the granular extent of such a culture of largess, West quotes a

Danish soldier in the movie *Armadillo* encouraging his fellow soldiers to “give [food] to the children as a sign of goodwill.” These handouts generate a sense of entitlement, and as West observes, the soldiers are soon “inundated with entreaties for money day after day.”

But such actions do not comport with the underlying tenets of counterinsurgency doctrine. For example, engaging children is contrary to the advice given by David Kilcullen in “Twenty-eight Articles,” the influential 2006 essay that established many of the fundamental principles of counterinsurgency. Kilcullen writes that to win over local families, foreign military forces should “engage the women, beware the children,” because “children are sharp-eyed, lacking in empathy, and willing to commit atrocities their elders would shrink from.”

Similarly, U.S. and NATO troops have gone out of their way to remain distant from Afghan women, citing cultural mores and Afghanistan’s traditional patriarchy. As one British officer says in the BBC’s documentary series *Our War*, “We got told certain things what not to do. . . . You don’t talk to the women.” Such instructions

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are widespread among U.S. and NATO forces in Afghanistan. But this, too, flies in the face of counterinsurgency's basic guidelines as outlined by Kilcullen, who writes that "in traditional societies, women are hugely influential in forming the social networks which insurgents use for support," and thus, winning the hearts and minds of local women is paramount. Constructive engagement sends a more powerful message than does the blind acceptance of cultural norms. Thankfully, the U.S. military may finally be catching on: in 2010, aware that its attempts at cultural sensitivity were hindering its broader counterinsurgency mission, the U.S. military created "female engagement teams," which are all-female patrols dedicated to engaging local women.

The schizophrenia often found in counterinsurgency tactics is especially apparent in the distribution of money. Some analysts believe money to be an important part of counterinsurgency: in 2004, for example, the U.S. Marine Corps' First Regimental Combat Team handed out cash payments as compensation for property damage inflicted during their operation to secure Fallujah. Yet in the documentaries West reviews, *Restrepo* and *Armadillo*, there is no clear logic to such payments; money is withheld in one case and given in another. In one scene in *Restrepo*, U.S. military officers are approached by Afghans wanting remuneration for a cow killed by U.S. forces. The soldiers refuse; instead, they say they will offer an equivalent value in food but no dollars. In *Armadillo*, meanwhile, a Danish officer provides cash to a man whose house was leveled and whose mother and daughter were killed in a NATO bombing raid. The discrepancy between these two scenes shows the difficulty in

determining how to quantify, and thus redress, the misery of a war zone.

Counterinsurgency doctrine also calls for limiting collateral damage as a central element of winning the support of the population. This led, for example, to the controversial 2009 decision of General Stanley McChrystal, then the top U.S. commander in Afghanistan, to focus on protecting Afghans during military operations above all other objectives. But what officers call "courageous restraint" is not always so easy to implement during the adrenalin-fueled confusion of a firefight. As the Danish platoon commander in *Armadillo* tells his troops, if you cannot distinguish between an insurgent reaching for a weapon and one reaching his hands out to surrender, then shoot. Nation building is not what most infantry soldiers sign up for. "Imagine if our tour . . . was just boring patrols. It would be a lame way to go home," one soldier says in *Armadillo*.

Counterinsurgency doctrine has evolved, but most soldiers do not keep up, meaning that innovations in strategy often do not work their way down to the tactical level. For example, in a 2007 interview with *The New York Times*, U.S. Army Colonel Martin Schweitzer observed, "In '02 we used to kick in doors. In '07 the Afghan army or Afghan police knock on the door and request to come in." Yet in *Armadillo*, Danish troops blast into a civilian compound to hunt for insurgents, and in *Restrepo*, a U.S. air strike kills civilians during an anti-Taliban operation. Too few soldiers are familiar with the changing theories and guidelines of counterinsurgency. As one military intelligence officer in Afghanistan says in the 2007 documentary *Taxi to the Dark Side*, "I was working 16-hour days,

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so to sit down and read a field manual was not top of my priorities over there.”

Lastly, it is worth remembering that Afghanistan and Iraq were not the chosen wars of the warrior-intellectuals who came to be counterinsurgency’s greatest champions. A project of nation building in which the central government is neither reflective of nor responsive to the needs of the people is not the desired terrain; Kilcullen, for example, has criticized the decision to invade Iraq. Yet the anthropological position that he and others created—modern counterinsurgency doctrine—turned out to be a remedy for a seemingly incurable malady. It should not be abandoned because it has not been implemented effectively or homogeneously; it is an invaluable intellectual reservoir that the U.S. military should draw on, adapt, and modify for the future.

CHRISTOPHER SIMS *is a doctoral candidate in the Department of War Studies at King’s College London.*

Beyond Groundhog Day

FERNANDO LUJÁN

Bing West uses a pair of documentary films, *Restrepo* and *Armadillo*, to illustrate grim realities in Afghanistan and to argue that the principles of counterinsurgency will soon “be rejected by the younger generation of company-grade officers who had to execute a flawed doctrine.” But as a member of this younger generation of U.S. military officers, I disagree; in fact, I can speak for many of my peers in arguing that a wholesale rejection of

counterinsurgency after Afghanistan and Iraq would be a grave error that would put the U.S. military on the path to irrelevance.

Whereas West has certainly served his time on the ground, the reader has probably not, and so should be cautioned that the experience of the soldiers in *Restrepo* is far from universal. (Indeed, trying to extrapolate lessons about counterinsurgency in Afghanistan from one documentary about a single platoon in the Korengal Valley is akin to trying to understand U.S. city life by renting an apartment in Detroit.) My most recent tour in Afghanistan serves as a counterpoint: from June 2010 to July 2011, I served on a small team of counterinsurgency advisers made up of U.S. Special Forces, cultural experts, and governance and development specialists. We embedded for weeks at a time with Afghan, U.S., and NATO units, with the aim of helping them apply the theory of counterinsurgency to their unique local circumstances, often under fire and among hostile populations.

The reality we observed—gleaned from the struggles of over 100 platoons in combat at the height of the Afghan surge—was much more complex and nuanced than any film or journalist can portray. To be sure, we saw many of the same frustrations that West describes: soldiers seen as spacemen by locals, “Groundhog Day” patrols that accomplish nothing, and a focus on fighting the enemy instead of training Afghan partners or co-opting local village leaders. But at the same time, we saw many places where coalition and Afghan units had broken this pattern and started to win the population’s support. Oftentimes, local conditions made the difference. *Restrepo*’s Korengal Valley is an example of one place where a perfect storm of

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unforgiving terrain and hostile tribes has made counterinsurgency virtually impossible. But just as important was the initiative, cultural savvy, and experience of the soldiers on the ground. When those dynamics come together, West's claim that "no matter their skills and good intentions, foreign troops cannot persuade the people of another nation to reject insurgents in their midst" does not hold up. Even in some of the most tightly controlled, longest-standing Taliban strongholds, U.S. and Afghan units working closely together have been able to draw the local populations to their side. This is an undeniable reality in large parts of Helmand and Kandahar, where villagers are responding to the presence of U.S. and Afghan troops and the relentless targeting of insurgent networks by returning to homes they have long abandoned, attending local weekly *shuras* (councils), offering information about the Taliban, and committing their own sons to the Afghan security forces.

The most successful military units have been those that learned the secret to overcoming the "Groundhog Day" phenomenon: stop trying to do it all yourself. Instead, reduce the footprint of foreign soldiers on patrols and coach Afghan soldiers and police on taking the lead. Ten Afghans and six U.S. soldiers can be infinitely more effective at approaching locals than the same ten Afghans with 100 U.S. soldiers in support.

U.S. units that only halfheartedly work with their Afghan counterparts become blind to their surroundings. Of course, a young lieutenant on his first tour overseas will feel like every patrol is the same if he does all the talking with villagers and his first question is always,

"Have you seen the Taliban?" Instead, junior leaders should learn the names of the Pashto-speaking soldiers in the Afghan unit that sleeps in camp with them, and every day before they step on patrol, they should develop a plan together: let's tell people about the Taliban improvised explosive device that killed three children yesterday, let's find out who lives in the compounds on the south side of the village and build a relationship, let's see if we can get permission for the Afghan soldiers to pray in the local mosque.

At the same time, the most adept U.S. units have learned to stop playing Santa Claus with projects and aid money—every dollar spent, every well dug or school built, is predicated on getting local leaders to step forward to make decisions as a community and then on connecting them to the Afghans working at the district center a few miles away. This often means forgoing expensive, high-profile projects built by outside contractors in favor of inexpensive mud huts built by local hands. The approach is aimed solely at promoting basic governance and has nothing to do with getting locals to like the foreign troops in their area.

The implication of these battlefield observations is that when it comes to counterinsurgency, less can be more. The recent surge of U.S. troops and resources in Afghanistan has brought many short-term gains, enabling coalition forces to reverse much of the Taliban's momentum, giving the Afghan government desperately needed breathing room, and expanding security deep into critical areas in the south. Yet this very abundance of resources can also inhibit the long-term viability of these achievements. More U.S. troops,

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for example, can mean less incentive to train Afghan counterparts; after all, why work through Afghans if you can do it yourself and do it better? More money for development projects, if not tied closely to promoting local governance, can create more opportunities for corruption and extortion by the Taliban or local power brokers. These various phenomena are the military version of what economists call “the resource curse”—the more you have, the less you diversify and prepare for the future.

The rush to condemn counterinsurgency doctrine as a failed experiment is based on two myths. The first is that counterinsurgency is nothing more than a contest for hearts and minds, a squishy theory that looks to turn the army into the Peace Corps or buy popularity in conflict zones with lollipops and Band-Aids. The second is that counterinsurgency is nation building on a massive scale, reliant on tens of thousands of U.S. soldiers to succeed. Both of these myths transform the debate into a false dichotomy: counterinsurgency versus counterterrorism, hard tactics versus soft. To the men and women closest to the fight, counterinsurgency is about control and legitimacy on the ground, not popularity contests, and it is best done by small expert teams, steeped in local languages and cultures, comfortable with ambiguity, working in concert with indigenous forces. As important as shaping perceptions in villages or fostering governance is what special operations forces call “network overmatch,” or killing and capturing irreconcilable fighters in order to dismantle the enemy’s ability to organize.

It is also a mistake to see the counterinsurgency campaigns in Afghanistan

and Iraq as anything more than one extreme of a long continuum of policy options, undertaken only when rapidly collapsing host governments and burgeoning insurgencies left policymakers the choice of failed states or massive reinforcements. One should not forget that the United States has been fighting insurgencies—engaging in what the U.S. Marines call “small wars”—almost continuously over its entire history, from the Indian Wars of the late 1700s to the interventions in Colombia and the Philippines, among other places, today. Such operations, with a small number of troops and resources, are conducted quietly over many years, using Special Forces, intelligence operatives, foreign-area specialists, aid workers, and host-country military or police units, and are far removed from nation building. Yet they represent the very essence of counterinsurgency: helping a foreign government develop its security apparatus and deny sanctuary to armed insurgent groups and terrorists.

The real danger as the United States withdraws from Afghanistan and Iraq is that U.S. military commanders and civilian policymakers will purge the whole experience of counterinsurgency from institutional memory, as occurred in the aftermath of Vietnam, resetting the U.S. armed forces to fight large-scale wars against conventional enemies. This would only hurt the United States. Young, sharp military and civilian leaders who thrived in counterinsurgency operations over multiple deployments will be redirected toward preparing for tank battles, artillery duels, and traditional diplomacy. Hard-earned lessons will be unlearned; the competitive adaptation of tactics, procedures, and operational

techniques, discarded. Yet no matter how much the various institutions of the U.S. military may prefer wars in which the enemy wears uniforms and fights in large formations, the United States is certain to face insurgencies again. The U.S. defense establishment must be prepared to deal with them effectively, with very limited resources, or face irrelevance.

Rather than demonizing a false, straw-man version of counterinsurgency that calls for tens of thousands of troops and a commitment to nation building, West and other defense leaders and theorists should focus on how to institutionalize the adaptations of the past decade and increase the military's capability for smaller-scale, but equally complex, counterinsurgency and stabilization efforts. To do any less is to embark on a "Groundhog Day" of the military's own making, denying the nature of today's security environment and condemning U.S. soldiers to repeat the mistakes of the past.

FERNANDO LUJÁN *is an International Affairs Fellow at the Council on Foreign Relations based at the Center for a New American Security. He is a Major in the U.S. Special Forces and served in the Pentagon's AfPak Hands program.*

West Replies

Christopher Sims essentially argues that counterinsurgency theory is sound; the problem, he says, lies with the soldiers who do not know how to implement it. He observes that modern counterinsurgency doctrine was conceived by "warrior-intellectuals" who applied lessons from

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West and His Critics

cultural sensitivity and anthropology and urged soldiers to act as therapists and conflict managers.

But such concepts are fundamentally incompatible with the reality of everyday combat. I spent many years on the battlefields and in the villages of Vietnam, Iraq, and Afghanistan. From what I saw at the ground level, counterinsurgency was—and is—a branch of warfare. War is the orchestration of violence in order to force your enemy to agree to your terms. U.S. soldiers carry rifles rather than check-books for a basic reason: to kill the enemy. To treat counterinsurgency as social science is to deny that violence remains at its essential center.

Military force is the ultimate arbiter of Afghanistan's future—and today, the Taliban are the superior fighting force. They have not won hearts and minds; most Pashtuns dislike them. But the Afghan army cannot yet stand up to their enemy due to poor civilian and military leadership, tribal affiliations, and corruption. Yes, the defects of the Kabul government are deplorable. Many states, however, have weathered insurgencies without building an honest government responsive to the people. Afghanistan can survive with a weak government and a subsistence economy, provided its armed forces can keep the Taliban at bay. Conversely, the country cannot survive with a weak military, regardless of the quality of the central government and the economy.

This means that the Taliban must be beaten on the battlefield. Of course, this task will require the Pashtun tribes to, at the very least, not actively support the Taliban. This requires that Afghan security forces actively protect the population. That is the fundamental military

task of counterinsurgency. There should be no mincing of words about the role of force and violence. If Afghan soldiers shirk from patrols, refuse to drive down mine-laced roads, or avoid villages that fly Taliban flags, they will lose. The essential problem in Afghanistan is that the Taliban are a fierce, dedicated enemy, willing to risk death and to kill.

As the historian Victor Davis Hanson wrote in his 2001 book *Carnage and Culture*, “Military history must never stray from the tragic story of killing.” Hanson argued that “to speak of war in any other fashion brings with it a sort of immorality.” He continued: “Euphemism in battle narrative or the omission of graphic killing altogether is a near criminal offense of the military historian.” In other words, the very term “warrior-intellectual” is an oxymoron because it suggests that killing is not the basic mission of the soldier challenged to battle.

Fernando Luján, meanwhile, argues that counterinsurgency as “nation building on a massive scale” is a “myth.” He objects to “demonizing a false, straw-man version of counterinsurgency that calls for tens of thousands of troops and a commitment to nation building.”

But like it or not, nation building has been the reality, not the myth. In Afghanistan, there are now 100,000 U.S. soldiers and 44,000 soldiers from other NATO countries responsible for safeguarding the Pashtun population while improving governance, combating corruption, delivering economic projects, and instituting the rule of law. These tasks are carried out in compliance with the joint U.S. Army–Marine Corps Field Manual 3-24, entitled *Counterinsurgency*. That manual was signed in 2006 by

Both Sides of the COIN

General David Petraeus, now the director of the CIA, and General James Amos, currently the commandant of the Marine Corps. On the first page, the manual states, “Soldiers and Marines are expected to be nation-builders as well as warriors.”

Luján argues that those units most successful at counterinsurgency “have learned to stop playing Santa Claus.” Not quite. The U.S. military in Afghanistan has carried out 16,000 development projects since 2001. Overall, the United States has disbursed more than \$18 billion in aid over the same period. Aid from Western countries accounts for most of Afghanistan’s national budget and economic growth (aside from the annual opium crop).

As for what Luján identifies as the “undeniable reality” that “U.S. and Afghan units working closely together have been able to draw the local populations to their side” in large parts of Helmand and Kandahar, this would indeed be marvelous news, given that those regions are the heartland of the Taliban movement. But until U.S. forces depart, it is impossible to know how reliable the allegiance of local populations to the Kabul government actually is. After all, as Petraeus observed last year, the rural Pashtun people have survived through the years by being “professional chameleons.”

On the whole, Luján’s observations amount to a recommendation for fewer conventional battalions and for more Special Forces advisory teams. On that point, he and I are in complete agreement. In both Afghanistan and Iraq, the U.S. military should have concentrated from the start on building strong indigenous armed forces. But this did not happen; neither the U.S. Army nor the Marine Corps gave proper attention to the

development of a U.S. adviser corps. Only recently has this changed. The current U.S. commander in Afghanistan, General John Allen, faces the challenge of increasing the number of military advisers while decreasing the size of the overall force.

Luján correctly points out that a robust advisory effort is a necessary but far from sufficient requirement for success, which is minimally defined as preventing the Taliban from taking over major Afghan cities. Without advisers, the Afghan security forces are likely to fall apart. Advisers must share the risks on the battlefield. “Having advisers outside the wire—in the fight—is not optional,” General Allen told me last August. “It is required.” With advisers, the military situation will remain perilous as long as Pakistan provides shelter to the Taliban and other terrorist organizations.

It is impossible to predict how the situation in Afghanistan will unfold, given that the outcome depends on Afghans and Pakistanis, not Americans. What is predictable, however, is that the younger generation of U.S. Army and Marine officers will reject the definition of counterinsurgency as requiring wholesale nation building. In Afghanistan, the U.S. military tried to do too much. 🌐

Recent Books on International Relations

Political and Legal

G. JOHN IKENBERRY

Negotiating With Evil: When to Talk to Terrorists. BY MITCHELL B. REISS.

Open Road Integrated Media, 2010, 324 pp. \$14.99.

Should states negotiate with terrorists? This is one of the most fraught questions of modern diplomacy. Reiss' important book offers some of the most lucid and sensible reflections yet on the topic. A scholar of international security and a former diplomat, Reiss led American participation in the peace talks over Northern Ireland. He argues against simplistic views that either favor or oppose engagement. Sometimes negotiations work, and sometimes they make the situation worse. Reiss suggests that states need to know whether a terrorist adversary is capable of evolving and abandoning its violence and whether its leadership has the authority to make binding deals. Often, the negotiations need to be secret, and governments need to be willing to walk away. Reiss sifts through the encounters that Western governments have had with some of the most notorious terrorist groups, including the Irish Republican Army, the Basque separatist group ETA, and Sri Lanka's

Tamil Tigers. As in Ireland, successful negotiations can take decades, during which states must continue efforts to degrade the terrorist organization and look for leaders who want to transform it into a more traditional political movement.

What's Left of the Left: Democrats and Social Democrats in Challenging Times.

EDITED BY JAMES CRONIN, GEORGE ROSS, AND JAMES SHOCH. Duke University Press, 2011, 424 pp. \$99.95 (paper, \$29.95).

Center-left and social democratic parties across the advanced industrial world have fallen on hard times. In this collection of essays, distinguished scholars offer reflections on the past struggles and accomplishments of left-leaning parties in Europe and the United States and speculate about their future. The golden era of postwar Western social democracy ended in the 1970s as economies stagnated, the Keynesian consensus broke down, and economic globalization placed limits on national governments' ability to manage their economies, protect workers, and provide social services. The neoliberalism of the Reagan-Thatcher years emerged as a rival vision of society and the market. Bill Clinton's "New Covenant" and Tony Blair's "New Labour" showed that center-

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left parties could achieve electoral success by combining neoliberal economics with traditional social liberalism. The book makes the important point that as advanced societies navigate the current moment of global economic uncertainty, liberals and social democrats have a new opportunity to regroup and rethink policies that promote economic security and social justice.

Human Rights Activism and the End of the Cold War. BY SARAH B. SNYDER.

Cambridge University Press, 2011,
304 pp. \$85.00.

Snyder provides a fascinating account of the Helsinki Final Act, signed by the Soviet Union and Western governments in 1975, and the transnational network of human rights activists that it spurred into action. Building on Daniel Thomas' book *The Helsinki Effect*, Snyder shows how the "Helsinki process" triggered by the agreement influenced both Western and Eastern governments to pursue policies that facilitated the rise of organized dissent in Eastern Europe and built pressure for human rights reform in the Soviet Union. Forgotten U.S. officials, such as Representative Millicent Fenwick and Arthur Goldberg, U.S. ambassador to the United Nations, play a role in the story, as do countless figures inside the Soviet bloc who found common cause in creating a network of groups that could monitor compliance with the Helsinki commitments and expose human rights abuses. In this rendering, it was not containment that won the Cold War but the relentless efforts of activists, journalists, lawyers, minority-rights advocates, and diplomats who worked across borders to set the stage for the political earthquakes that followed.

The Logic of Positive Engagement. BY MIROSLAV NINCIC. Cornell

University Press, 2011, 224 pp. \$39.95. When the United States seeks to change the behavior of rival or adversarial states, what are the available tools and strategies? In this provocative study, Nincic observes that American foreign-policy makers tend to resort to "negative pressures," such as the use of force, coercive diplomacy, and economic sanctions. Less appreciated and less understood, Nincic argues, are the tools and strategies of "engagement," policies that use positive inducements to alter the incentives and orientations of other states. Nincic is surely correct: policymakers know more about the use of sticks than carrots. The book seeks to explain the bias in American foreign policy toward threats and punishments and argues that it is a legacy of the Cold War, which taught politicians to worry about charges of appeasement. Nincic also sees biases in the American security-studies community, where, he claims, realist understandings of the world shift attention away from nonmilitary tools of influence. The book's most useful contribution is to spell out how strategies of engagement and positive inducements can work, using the United States' experiences with Cuba, Iran, Libya, North Korea, and Syria as case studies.

The Pseudo-Democrat's Dilemma: Why Election Monitoring Became an International Norm. BY SUSAN D.

HYDE. Cornell University Press, 2011,
248 pp. \$35.00.

As Hyde notes, the practice of inviting foreign observers to monitor elections has become so widespread that it has turned into an international norm. Today, elections

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that are not observed are widely seen as undemocratic, as Iran discovered in 2009. Hyde is especially puzzled by “electoral autocrats,” such as Vladimir Putin, who welcome foreign monitors to judge their elections even though doing so risks repudiation. The book’s argument is that leaders invite election observers as a “costly signal” to the outside world that their political system meets international standards, expecting that benefits will follow. Behind this argument is a more general observation that states adopt international norms not out of moral obligation but rather out of rational self-interest. Hyde speculates about how this logic might apply to a wider array of international norms that have spread within the developing world, including the adoption of gender quotas in government, the establishment of central banks, the hiring of credit-rating agencies, and the presence of international weapons inspectors. Unfortunately, this more general account of the rise and spread of international norms remains largely implicit.

Economic, Social, and Environmental

RICHARD N. COOPER

Climate Change and Global Energy Security: Technology and Policy Options. BY MARILYN A. BROWN AND BENJAMIN K. SOVACOO. MIT Press, 2011, 456 pp. \$58.00 (paper, \$29.00).

Once one gets through the unnecessarily alarmist introductory material, this book offers a levelheaded discussion of possible measures to abate greenhouse gas emissions and the economic, social,

and political obstacles to adopting those measures. Unlike many studies on climate change, it discusses significant sources of emissions other than the burning of fossil fuels, such as deforestation and agriculture. It also includes a brief but informative treatment of geoengineering, a range of unorthodox approaches that might be able to offset global warming more rapidly or extensively than conventional means. The authors conclude that the obstacles to abatement are numerous and diverse—but so are the possibilities for overcoming or bypassing them. Rather than a top-down global scheme, a “polycentric” approach to abatement—many actions organized by many different individuals or organizations in multiple cultural environments—will be desirable and indeed necessary. (The two are not mutually exclusive, so long as one does not discourage the other.) The book offers eight illuminating case studies, from Singapore’s control of traffic to Bangladesh’s distribution of solar power to rural areas, to illustrate the effective use of diverse approaches.

Realeconomik: The Hidden Cause of the Great Recession (and How to Avert the Next One). BY GRIGORY YAVLINSKY. Yale University Press, 2011, 192 pp. \$26.00.

Yavlinsky, a reform-minded economist and sometime Russian presidential candidate, offers his take on what caused the financial crisis of 2008, the ensuing Great Recession, and the current weak recovery. He points to a lack of moral guidance for modern capitalism. Every well-functioning society, he argues, follows certain rules of behavior, sometimes embodied in law but often rooted in informal conventions that developed over a long period of time.

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Neglect of these rules can lead to serious deficiencies in economic mechanisms, above all in the financial sector. He acknowledges the difficulty in proving his case with hard data but offers examples to illustrate his main points, including an interesting discussion of increasing nonproductive rent seeking over intellectual property of dubious social value. The book involves more diagnosis and lamentation than prescriptions, since Yavlinsky is fully aware that moral behavior cannot be built, or rebuilt, with a stroke of the pen. He does not, unfortunately, contemplate the possibility that the main actors in the financial crisis thought that their behavior was above reproach and socially valuable but were badly misled by a flawed antiregulatory doctrine.

Juggernaut: How Emerging Markets Are Reshaping Globalization. BY URI

DADUSH AND WILLIAM SHAW.

Carnegie Endowment for International Peace, 2011, 272 pp. \$49.95 (paper, \$19.95).

Populations and economies are both growing, but at different rates. When will India overtake China to become the world's most populous country? When will China overtake the United States to become the world's largest national economy? This sobering, usefully quantitative book provides reasonable, if necessarily speculative, answers. In a bit of futurology, the authors imagine the world in 2050, when today's rich countries, especially European nations and Japan, have receded in relative importance, and today's emerging markets have become more powerful—all while the world's population has continued to grow, resulting in increased demand for food, energy, water, and much else. The increased pressures on the world's resources

and environment will require new and deeper forms of international cooperation. But the list of countries whose cooperation will be essential for effective results will be substantially different from the list of today's great powers.

Foreign Direct Investment and Development:

Launching a Second Generation of Policy

Research. BY THEODORE H. MORAN.

Peterson Institute for International

Economics, 2011, 256 pp. \$27.95.

Multinational corporations arouse high emotions, whether they are seen as exporters of jobs, exploiters of workers, or transmitters (or withholders) of valuable technology. Moran reviews and synthesizes the latest research on the various impacts of the foreign direct investment made by multinationals in developing countries. Few sweeping generalizations hold up. The circumstances surrounding particular investments are of paramount importance and are usually influenced by the policies and negotiating skills of the governments in the target countries. There are important differences among various forms of foreign investment—in natural resources, infrastructure, manufacturing, and services. At least one generalization does seem to hold, although perhaps not universally: investment abroad by U.S.-based multinationals does not reduce employment in the United States. On the contrary, it generally supports employment at home. Moran believes much of the available research on multinationals is inadequate. He strongly urges supplementing cross-country regression analysis with case studies, including comparative case studies, which yield deeper insights into what is actually happening.

Recent Books

The Quest: Energy, Security, and the Remaking of the Modern World. BY DANIEL YERGIN. Penguin Press, 2011, 816 pp. \$37.95.

Yergin writes for nontechnical readers, and this engaging book is easy, even fun, to read. It addresses not only the full spectrum of energy sources, from coal to photovoltaic cells, but also the rich history and politics of the industry. The book contains many colorful anecdotes involving figures who shaped the energy business and influenced how the public understands energy, including Svante Arrhenius, who in 1894 became the first to conjecture that there was a relationship between atmospheric carbon dioxide and the earth's temperature but, as a Swede who had lived through cold Nordic winters, welcomed the prospect of global warming as people burned more coal. The book is perhaps most illuminating when Yergin narrates major historical events, including the collapse of the Soviet Union and the rise of Hugo Chávez in Venezuela, from the perspective of the oil industry.

Military, Scientific, and Technological

LAWRENCE D. FREEDMAN

Can Intervention Work? BY RORY STEWART AND GERALD KNAUS. Norton, 2011, 236 pp. \$23.95 (paper, \$15.95).

This book consists of a joint introduction followed by an essay from each contributor. Knaus writes about Bosnia, a relatively successful case of international intervention. His essay is worthy and informative,

although he sometimes seems to advocate approaches that the introduction suggests are unwise. Stewart's essay is persuasively and elegantly written. Stewart mocks formulaic approaches to intervention and rejects almost all policy prescriptions for Afghanistan other than extracting foreign troops as soon and as gracefully as possible. His basic aim is to warn against meddling in societies without a deep knowledge of their languages, politics, and cultures. Stewart swears he is not nostalgic for a time when colonial administrators ruled foreign lands and remained in their posts for decades. Nonetheless, as a former soldier, diplomat, adventurer, academic, and now parliamentarian, he does cut a rather nineteenth-century figure. One imagines Stewart would have been at home dispensing wise, if occasionally rough, justice in the outposts of the British Empire, working with local people whose customs and power structures he had learned to respect.

Intelligence and U.S. Foreign Policy: Iraq, 9/11, and Misguided Reform. BY PAUL R. PILLAR. Columbia University Press, 2011, 432 pp. \$29.50.

Fixing the Facts: National Security and the Politics of Intelligence. BY JOSHUA ROVNER. Cornell University Press, 2011, 280 pp. \$35.00.

Germ Gambits: The Bioweapons Dilemma, Iraq and Beyond. BY AMY E. SMITHSON. Stanford University Press, 2011, 384 pp. \$95.00 (paper, \$29.95).

What intelligence analysts loathe more than anything is when policymakers misrepresent intelligence reports or put analysts under pressure to change inconvenient assessments. The most egregious contemporary examples of both phenomena

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took place during the Bush administration's push for an invasion of Iraq in 2002 and 2003. As a member of the U.S. National Intelligence Council, Pillar was responsible for some of the estimates the administration used to justify the war. He provides a vigorous and hard-hitting insider's account, drawing particular attention to prescient prewar assessments of what postconflict Iraq would look like and the likely regional consequences of war. As information is always incomplete and has to be supplemented by broader judgments, Pillar is wary of the concept of intelligence "failures" and offers some trenchant observations on inquiries into them, such as the 9/11 Commission, which he suggests lead to misguided reforms that do little to prevent the politicization of intelligence.

This issue is addressed in a neat and systematic manner by Rovner, who considers, in addition to the Iraq case, other notorious examples of politicization: the assessments based on body counts that supported spurious claims of progress during the Vietnam War, the dubious assertions regarding Soviet missile developments that the Nixon administration used to justify its antiballistic missile program, and the Team B exercise of 1976, in which the Ford administration asked a group of Cold War hawks to develop an alternative analysis of the Soviet threat. Team B took a much grimmer view than the CIA; more important, however, its directly ideological challenge missed an opportunity to demonstrate how raw information alone can support different interpretations of a threat. Somewhat against contemporary trends, Rovner argues that intelligence assessments would be more likely to remain politically uncontaminated and therefore more useful to policymakers if they were kept completely

secret. But that particular genie might now be out of the bottle, a victim of the politicization of all policy advice—not just intelligence—that is characteristic of an increasingly transparent system.

Those who wonder why veteran Iraq hands wrongly believed that Saddam Hussein was concealing weapons of mass destruction in 2003 should read Smithson's riveting account of UN weapons inspectors struggling to find out the truth after the 1990–91 Persian Gulf War. The book reveals how the inspectors became sleuths, combining forensic skills with scientific expertise to outfox Iraqi authorities who pretended that there was nothing to be found. Of particular value is the story of the 1995 defection of Saddam's son-in-law Hussein Kamel al-Majid, whose revelations turned out to be of scant value compared with the information the Iraqis willingly made available on the mistaken assumption that the defector was telling all. Smithson reveals just how much work it takes to verify disarmament in the face of lying regimes and stresses the need for individual scientists to accept full responsibility when dealing with deadly materials and processes.

American Force: Dangers, Delusions, and Dilemmas in National Security. BY

RICHARD K. BETTS. Columbia

University Press, 2011, 384 pp. \$29.50.

Betts describes himself as a Cold War hawk who became a post-Cold War dove. In this collection of essays, he addresses all the central issues of recent U.S. strategy: the maintenance of primacy and the prospective rise of China, humanitarian intervention and the struggles in Afghanistan and Iraq, and the problems posed by weapons of mass destruction, terrorism, and the possibility of a link between the two. This is not

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mainstream international relations scholarship. Betts combines serious thought, common sense, and deep historical knowledge, rather than simply applying abstract theories, and his conclusions are expressed in plain English, rather than with mathematical models. His judgments are therefore contingent, but they are always considered and often incisive. Betts is not opposed to the occasional use of force for the right purposes, and he explains why it is difficult to get strategic policy right. But he deplores the persistent American tendency toward military activism, especially in pursuit of what he describes as a “liberal empire.” As he himself recognizes, he is by no means a lone voice arguing for American restraint, but he is certainly among the most articulate.

The United States

WALTER RUSSELL MEAD

Liberty's Surest Guardian: American Nation-Building From the Founders to Obama.

BY JEREMI SURI. Free Press, 2011,
368 pp. \$28.00.

Nation building, perhaps the most complex task of statecraft, has gotten the best of many U.S. officials and thinkers over the years. And it seems that nation building is almost as hard to write about as it is to do. Suri's book explores many of the complexities and ambiguities surrounding the task, examining a broad range of historical examples, including the Reconstruction era in the American South and recent U.S. efforts in Afghanistan and Iraq. Suri does a decent job of identifying highlights, low points, and continuing dilemmas. But the

historical complexity of each episode is given short shrift by superficial narrative summaries, and Suri's analysis can be puzzling. The deepest confusion may result from his failure to distinguish sufficiently between nation building among consenting Americans, such as the creation of the American republic from the original 13 colonies, and attempts to build foreign nations around American values. Still, Suri's core conclusion is sound: nation building is difficult, expensive, and unpleasant, and at best it can be only partially successful—but it is often unavoidable.

Five Chiefs: A Supreme Court Memoir. BY JOHN PAUL STEVENS. Little, Brown, 2011, 304 pp. \$24.99.

Stevens' understated and lucid memoir, organized around the five chief justices who led the Supreme Court during his career, will instruct and entertain novices and legal experts alike, as Stevens lifts the curtain to show readers how the judicial sausage is made. He is always humane and courteous in his approach, but this does not prevent the occasional deft insertion of a stiletto between the ribs of various judges with whom he served. Whether he is lifting an eyebrow at the gold stripes with which Chief Justice William Rehnquist adorned his robe, deploring the Court's increasing bias toward the prosecution in capital cases, or probing the weak spots of originalism, Stevens is always clear and frequently entertaining. Future chief justices would do well to read this book in preparation for their duties. The rest of us should thank Stevens for a lifetime of service and for the rarest kind of political book: a genuinely memorable memoir.

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That Used to Be Us: How America Fell Behind in the World It Invented and How We Can Come Back. BY THOMAS L. FRIEDMAN AND MICHAEL MANDELBAUM. Farrar, Straus and Giroux, 2011, 400 pp. \$28.00.

A decade ago, foreign policy experts like Friedman and Mandelbaum were focused on the changing global order. Now, they are increasingly concerned that the American power on which that order rests must be renewed at home, or else it will fail abroad. Although noting the achievements of other countries, especially China, the authors believe that the United States does not need to imitate others so much as renew its commitment to policies and ideas rooted in its own past. In particular, the authors propose a return to the idea of a strong national government, committed to sound finance and acting as the partner of and advocate for a vigorous private sector. They support substantial public investments in infrastructure (including high-speed rail) and alternative methods of energy generation, and they want to see social welfare entitlements rationalized and trimmed. This is a book that the Tea Party and Occupy Wall Street will both reject. But the authors, bent on appealing to centrists and moderates on both sides of the aisle, are not too worried about persuading those further out on the left and the right.

Hitler and America. BY KLAUS P. FISCHER. University of Pennsylvania Press, 2011, 344 pp. \$29.95.

This book has a great premise and opens with great promise. An analysis that showed how Adolf Hitler's views of the United States affected key policy decisions would be an important work of intellectual

and political history. Unfortunately, after a strong beginning, in which Fischer looks at Hitler's exposure to German writers on the United States, such as Karl May, a chronicler of cowboy stories, the book loses its focus and discipline. This is understandable: there are so many dimensions to the interactions between Hitler and the United States that foreign policy, economic planning, anti-Semitism, and military history all have a part to play. But Fischer gets so caught up with the complexities of the subject that he never manages to pull together an integrated portrait of Hitler's view of the United States. As a result, this interesting and well-researched book never quite fulfills its potential.

The Concise Princeton Encyclopedia of American Political History. EDITED BY MICHAEL KAZIN. Princeton University Press, 2011, 672 pp. \$35.00.

One purpose encyclopedias serve is to assemble knowledge about the past. By what their authors select and how they treat it, they often provide a window onto the spirit of their own times. Today, they face an additional challenge, as free Web sites, such as Google and Wikipedia, are usurping the traditional place of reference books. This well-edited and attractively presented volume provides readers with significantly more thoughtful and wider-ranging information than they will easily find on the Web; students in particular would be wise to consult it. Except in its language, which is uniformly accessible and mercifully free of the jargon that plagues contemporary scholarship, this encyclopedia reflects the atmosphere and the concerns of the contemporary academic community as effectively as

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Diderot's encyclopedia reflected the French Enlightenment. Whether early-twenty-first-century American political science will hold up as well as eighteenth-century French Enlightenment thought is a separate question altogether.

Western Europe

ANDREW MORAVCSIK

Mamma Mia! Berlusconi's Italy Explained for Posterity and Friends Abroad. BY BEPPE SEVERGNINI. Rizzoli Ex Libris, 2011, 200 pp. \$22.50.

The Liberty of Servants: Berlusconi's Italy. BY MAURIZIO VIROLI. Princeton

University Press, 2011, 200 pp. \$27.95. After ruling Italy for most of the past 17 years, Silvio Berlusconi seems to have left office for good. But the questions raised by his rule remain. Severgnini, a prominent Italian columnist, has made a career of cross-cultural interpretation, explaining Italy to Anglophones and Anglo-Saxon life to Italians. He is a savvy and engaging writer, and this conversational book is a solid, if somewhat predictable, introduction to the Berlusconi saga. For all of Berlusconi's faults—indeed, in large part because of them—he came across to many Italians as simpatico. The more he partied, acquired material possessions, and fooled around (while praising his family), the more people seemed to like him, at least up to a point. As prime minister, he exploited a remarkable knack for salesmanship and seduction. His professed religiosity and anticommunism tapped into a deep postwar conservative vein in Italy. The literate Italian public—meaning those who regularly read newspapers and books, watch

serious TV news, and browse the Web—is surprisingly small, a trend exacerbated by Berlusconi's control over the media. Normal checks and balances did not work, because the Italian legal process could neither convict him of corruption nor force him to divest himself of his media empire, and left-wing parties were too divided and bereft of new ideas to compete.

Viroli, a political philosopher, is less interested in explaining Berlusconi's political longevity. Instead, he holds up Berlusconi's success as a mirror, asking what it tells us about modern democratic societies everywhere. Viroli believes it calls into question the fashionable libertarian conviction that freedom alone is enough to optimize politics, the belief that the state should defend only "negative liberties," leaving us alone to enjoy our property, opinions, and rights. That narrow conception of freedom is compatible with the enormous concentration of power, both public and private, that leads to a progressive debasement of public virtues and degenerate social behavior. A pervasive culture of lying and cynicism saps the active engagement of citizens in their communities. Individuals become sycophants, and politicians become manipulators. These are problems that infect not just Italy but all Western democracies, to varying degrees. That is the troubling lesson of Berlusconi.

An Honourable Englishman: The Life of Hugh Trevor-Roper. BY ADAM SISMAN.

Random House, 2011, 672 pp. \$40.00. One might expect the biography of an Oxford historian to recount tempests in teapots. Yet Sisman, a serial biographer of famous Englishmen, has produced a book that captivates the reader. Hugh

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Trevor-Roper, a country doctor's son, rose through England's brutal public schools and private universities to become a prominent public intellectual and an establishment snob, riding to hounds by day, drinking claret by night, and marrying an earl's daughter. Precocious and brilliant, yet rash and arrogant, Trevor-Roper embodied the contradictions of the worldly academic. He achieved celebrity by exploiting his wartime experiences as an intelligence officer to publish *The Last Days of Hitler*. Thereafter, he penned popular pieces for the London *Times* and brilliant critical essays but failed to produce a magnum opus, perhaps fearing vengeful criticism from those he had earlier provoked. His career ultimately ended in ignominy after he vouched for the authenticity of phony Hitler diaries. They just do not make historians, or public lives, like this anymore.

Nationalism in Europe and America: Politics, Cultures, and Identities Since 1775. BY LLOYD KRAMER. University of North Carolina Press, 2011, 272 pp. \$65.00 (paper, \$24.95).

Many believe that Europe and the United States exhibit fundamentally different forms of nationalism. Americans, it is said, reside in a nation of immigrants and are thus civic nationalists, committed to a constitution and political values. Europeans reside in nations of blood and memory and are thus cultural or ethnic nationalists, committed to distinctive languages, territories, and cultures. Americans, living on an isolated continent, remain intensely proud, whereas Europeans, having lived through the long-term project of European integration, are now comfortably post-national. American nationalism is bound

up with militarism; European nationalism is based more on social welfare ideals. Kramer takes aim at such simple dichotomies. He rejects the notion of a purely civic U.S. nationalism, noting that Americans are just as attached as Europeans to specific geographic attributes, historical memories, cultural traits, and political habits. A reexamination of American and European nationalisms calls for a great book; unfortunately, this is not it. Kramer deserves credit for challenging reductive shibboleths, but he too often glides over the surface of important questions, glossing over history in a questionable manner.

Immigrant Nations. BY PAUL SCHEFFER. Polity Press, 2011, 300 pp. \$79.95 (paper, \$29.95).

The Netherlands offers a striking example of the dilemmas that immigration creates for Western societies. Despite its small size, it is not, and never was, a unitary polity. Rather, it is a divided nation that traditionally has managed complex religious, regional, and ideological differences through political institutions intricately designed for conflict resolution and power sharing. Scheffer argues that over the past two decades, these institutions have been undermined in part, but not solely, by immigration, and he believes the Netherlands and other Western countries must recognize that multiculturalism has failed. They must reconsider and broaden their conceptions of national identity, based on liberal democratic pluralism, and draw up stricter selection criteria for immigrants consistent with those values. Lest Americans crow about the superiority of their system, Scheffer points out that the American and European experiences are more

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similar than different and stresses that work needs to be done on both sides of the Atlantic. The book is in some ways self-indulgent, ranging too broadly across history, philosophy, and personal experience. Still, the result should be required reading for those engaged with this important issue.

Turkey's European Future: Behind the Scenes of America's Influence on EU-Turkey Relations.

BY NATHALIE TOCCI. New York

University Press, 2011, 240 pp. \$55.00.

Many observers believe that the United States lacks sufficient leverage to influence Turkey significantly and that the major external determinants of Turkish foreign policy are Turkey's relationships with Europe (its largest trading partner and continued interlocutor in discussions over EU membership) and with its regional neighbors. Tocci disagrees and argues that the United States exercises a significant hidden influence over EU-Turkish relations, largely through diplomatic pressure and back-channel discussions with Europe. She concludes that U.S. pressure was "critical" in moving Turkey's EU candidacy along between 1998 and 2006, despite disagreements over the Iraq war. But her evidence does not support this claim: outspoken diplomacy failed outright, and quiet diplomacy was not nearly as important as domestic electoral change within Europe. As right-wing parties opposed to Turkey's bid for EU membership gained power in Europe during the past decade, U.S. influence declined. Despite its suspect conclusions, this book is an interesting study of the enduring closeness between Europe and the United States. Their political discourses dovetail, facilitating steady cooperation that overcomes occasional disagreements.

Western Hemisphere

RICHARD FEINBERG

Fixing Haiti: MINUSTAH and Beyond.

EDITED BY JORGE HEINE AND
ANDREW S. THOMPSON. United
Nations University Press, 2011,

276 pp. \$35.00.

Demonstrably unable to govern itself, Haiti is now a permanent de facto international trusteeship, depending on the United Nations for its security and international donors for its economy. The United Nations Stabilization Mission in Haiti (MINUSTAH) is more vigorous than previous international efforts to assist the Haitians. It includes substantial numbers of Argentines, Brazilians, and Chileans, marking a new phase of regional self-assertiveness and collective responsibility. The authors in this volume oscillate between recognizing the urgency of a large international role in a fragile or failed state and arguing that local ownership and national institution building are required for lasting change. Two Chilean military commanders attached to MINUSTAH provide an unusually candid account of the challenges facing international peacekeepers in a lawless, distrustful society. In contrast, a Brazilian diplomat takes snide swipes at the United States and nongovernmental organizations, inadvertently raising doubts about whether Brazil is genuinely prepared to play a constructive leadership role. The editors' concluding chapter neatly sums up the many dilemmas facing nation building in Haiti, conceding an absence of civic-mindedness and social capital among

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Haitians but nevertheless advocating a long-term international commitment.

Notas Sobre Economía Cubana. BY JOSÉ LUIS RODRÍGUEZ GARCÍA. Ruth Casa Editorial, 2011, 160 pp. \$10.00.

This tightly constructed, analytic memoir, whose title translates as Notes on Cuban Economy, offers a rare glimpse into the thinking of a former senior member of the Central Committee of the Cuban Communist Party. After receiving a doctorate in economics in the Soviet Union, Rodríguez served as Cuba's minister of economy and planning from 1995 until 2009. In terse but devastating prose, he discusses the difficulties of transplanting Soviet-style planning into a underdeveloped economy in the tropics, making it dramatically evident that at least some members of the top Cuban leadership are well aware of the country's economic shortcomings. Rodríguez recounts various cycles of tepid reform but fails to elucidate why those reforms were not pursued with greater vigor. Evincing some frustration, he asserts that questions of power and politics regularly took precedence over economics. Since coming to power in 2006, Raúl Castro has begun yet another round of economic reforms. Unlike previous attempts, these reforms appear to be gaining momentum. During Rodríguez's years in power, the international community failed to support Cuban reformers. Now, it has an opportunity to do better.

Cuba Since the Revolution of 1959: A Critical Assessment. BY SAMUEL FARBER.

Haymarket Books, 2011, 400 pp. \$24.00. For some left-socialists like Farber, no society seems to have measured up since the Paris Commune of 1871. But patient

readers will be rewarded by his frequent insights, stimulating historical comparisons, and command of the data relating to Cuba's economic and social performance. Many have faulted Cuba's Stalinist bureaucratic centralization, but few critiques are as replete with concrete examples of foolishness and foul-ups. Farber harshly criticizes Cuba's treatment of blacks, homosexuals, and political dissidents and exposes the Castro regime's practice of obfuscating policy debates through character assassination. But he takes seriously Raúl Castro's economic reform agenda, seeing it as a variant of the Sino-Vietnamese model of state capitalism combined with political authoritarianism. The big winners, Farber speculates, could be senior officials of the Cuban military and the Communist Party, the foundations of a new managerial and technocratic class that could conceivably form an alliance with the more moderate wing of Cuban American capitalists based in Florida.

Adiós Muchachos: A Memoir of the

Sandinista Revolution. BY SERGIO RAMÍREZ. Duke University Press, 2012, 264 pp. \$84.95 (paper, \$23.95).

Ramírez, a celebrated novelist, served as Daniel Ortega's vice president during the chaotic era of Sandinista rule in Nicaragua in the 1980s. In this poignant memoir, Ramírez extols the idealism of the youthful Sandinistas, too many of whom fell as martyrs in their bloody battles against the tyrannical Somoza dynasty. At the same time, he recognizes the many errors the inexperienced revolutionaries committed once in power. Ramírez paints vivid portraits of those Latin American leaders who assisted the Sandinistas. As he so often does, Fidel

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Castro emerges as a master realist; the Panamanian strongman Omar Torrijos, it is shown, took his fill of liquor and women yet functioned as a savvy strategist. Ultimately marginalized by internal Sandinista intrigues, Ramírez disdains the new materialism of his putatively socialist ex-comrades (the “*muchachos*”). In yet another twist of history, the Nicaraguans recently reelected Ortega, in part because he has built a working relationship with the private sector, cemented by common interests in a growing economy. More pragmatic now, Ortega has raised the living standards of the Nicaraguan poor by drawing on funding from both the World Bank and the oil-rich Venezuela of Hugo Chávez.

Eastern Europe and Former Soviet Republics

ROBERT LEGVOLD

Post-imperium: A Eurasian Story. BY DMITRI TRENIN. Carnegie Endowment for International Peace, 2011, 242 pp. \$49.95 (paper, \$19.95).

In addition to acute intelligence, Trenin has two other rare qualities: a remarkable ability to deal clearly with the complexities of Russia’s politics and external behavior and a capacity to get outside his Russian skin when examining his own country. Both qualities are on full display in this latest of his many books. Russia, he argues, has moved beyond the analytic clichés of Western observers. No longer do its leaders or people suffer from the phantom

pain of a lost empire or harbor dreams of restoring what they lost. Russia’s dilemma is post-imperial: how to keep a sprawling, unwieldy, half-remade country intact, when the only popularly tolerated solution—quasi-authoritarianism—risks marginalizing the country and leaving it squeezed between two more powerful and dynamic continents, Europe and Asia. With a measured mastery, Trenin probes the many aspects of this dilemma, from Russia’s changing relations with its neighbors and the great powers to the effect of the country’s identity crisis on its economy, demographics, and culture.

The Russian Origins of the First World War.

BY SEAN MCMEEKIN. Belknap Press, 2011, 344 pp. \$29.95.

An entirely new take on the origins of World War I comes as a surprise. If war guilt is to be assigned, this book argues, it should go not only (or even primarily) to Germany—the long-accepted culprit—but also to Russia. In the conventional view, Russia was trapped into fatal military moves by Austria’s blundering and Germany’s predatory aims. But McMeekin contends that Russians close to the tsar had long hungered to strip control of the Black Sea straits from a collapsing Ottoman Empire. McMeekin places the blame squarely on Russia’s foreign minister, Sergei Sazonov, and a coterie of military officials who were willing to watch the 1914 Balkan crisis spiral into general war, as long as France and the United Kingdom were ready to checkmate Germany and allowed Russia to pursue its ambitions. As Europe’s map shattered, the Russians might have been motivated by apprehension over who would get what. But their actions were bald and aggressive,

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as McMeekin demonstrates through a bold reading between the lines of history.

Afgantsy: The Russians in Afghanistan, 1979–89. BY RODRIC BRAITHWAITE. Oxford University Press, 2011, 432 pp. \$29.95.

Compassionate yet critical, this is the most comprehensive portrait of the morass Soviet leaders got themselves and their army into when they invaded Afghanistan in December 1979. Braithwaite was the British ambassador to the Soviet Union during the last two years of the war and the first two years of its messy aftermath. Like a film director zooming in on details and then pulling away to survey the larger scene, he captures the misery of war in Afghan villages and valleys, along with the confused deliberations in the halls of the Kremlin, while not losing sight of the war's effect on Soviet society, especially the badly damaged military. *Afgantsy* is the Russian term for the Soviet soldiers who fought the war, and Braithwaite recounts many of their individual stories with special empathy. His book is a big, vibrant canvas painted with skill and humanity.

Inventing the Enemy: Denunciation and Terror in Stalin's Russia. BY WENDY Z. GOLDMAN. Cambridge University Press, 2011, 336 pp. \$85.00 (paper, \$29.99).

The mind-numbing scale of Stalin's purges in the 1930s is well known: the torture and the trials, the barbarism of the prison camps, the monstrous murder quotas. Much less is known about how the terror was experienced by ordinary people—especially the roles played by the victims' desperate friends, families, neighbors, and co-workers. Goldman fills that gap by reconstructing the actions of workers in

five major factories between 1936 and 1938, the most intense phase of the purges, as revealed in the stenographic records of Communist Party workplace meetings. The book is an excruciating account of how victims (and potential victims) enlarged and sped the killing machine: workers denouncing workers, family members betraying family members, and lovers sacrificing lovers in vain attempts to save themselves, as Stalin and his lieutenants ordered each new wave of purges.

Soviet Baby Boomers: An Oral History of Russia's Cold War Generation. BY DONALD J. RALEIGH. Oxford University Press, 2011, 432 pp. \$34.95.

Contemporary historians have failed to systematically collect the memories and self-explanations of people who lived through the Soviet experience and are now free to talk about it. With this book, Raleigh has done his part to correct this neglect, by conducting interviews with 60 members of the 1967 graduating classes of two elite high schools, one in Moscow and one in Saratov, a southern city. What emerges is an oral history of their generation, the Soviet Union's version of the baby boomers. They are the children of professionals and midlevel authorities, and they remember their childhoods and school days fondly and with some pride. They grew up without the kind of suffering that their parents had known as young people. Reaching adulthood during the Brezhnev era, they jostled against the regime's strictures in minor ways by aping Western fads. As the Soviet system deteriorated, they married and divorced and struggled with careers, all the while developing a vague, unfocused cynicism. This book is a collective biography that will fascinate its

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subjects' grandchildren, to whom the world it depicts will seem like a distant planet.

Middle East

L. CARL BROWN

The 9/11 Wars. BY JASON BURKE. Penguin Global, 2011, 500 pp. \$20.00.

This big book details the diverse conflicts that shaped the decade after 9/11: not only the wars in Afghanistan and Iraq but also Europe's struggles with jihadist terrorism and the uneasy U.S.-Pakistani relationship. After opening with the U.S. action against Afghanistan after 9/11, the story treats the early years of the U.S. invasion of Iraq before moving on to Europe in mid-decade (in the chapter "Bombs, Riots, and Cartoons") and Iraq during the "surge." In what is perhaps the strongest portion of the book, Burke returns to Afghanistan and adds Pakistan to the narrative, which culminates in the dispatching of Osama bin Laden in May 2011. Throughout, Burke reconstructs and judges what the different protagonists, especially the United States and al Qaeda, were thinking and doing. He argues convincingly that the political realities of the post-9/11 era are best captured not by focusing on would-be centers of global terrorism but by examining the different circumstances of communities within the wider Muslim world, including Muslims living in the West.

The Struggle for Egypt: From Nasser to Tahrir Square. BY STEVEN A. COOK. Oxford University Press, 2011, 424 pp. \$27.95.

After a brief overview of Egyptian political history from the British occupation in 1882 to the military coup in 1952 that overthrew

King Farouk, Cook tells the story of Egypt's last 60 years in terms of three presidential monarchs: Gamal Abdel Nasser, who ruled until his death in 1970; Anwar al-Sadat, who followed as president until his assassination in 1981; and Hosni Mubarak, whose reign lasted three long decades, until his overthrow last year. Under all three, Egypt remained a military regime that, despite early signs of dynamism, soon slipped into a sluggish and brutal authoritarianism. Cook stresses the Egyptian fear of domination by outsiders, rooted in a long history of foreign occupations, and reveals the smoldering Egyptian resentment of the United States, which in the 1970s replaced the Soviets as Egypt's great-power patron. His final chapter tells of the 18 days of upheaval that ended Mubarak's rule—a popular revolt, but one whose coup de grâce was delivered by the military. Cook concludes that although Egypt's future remains very much in doubt, the United States should "take a hands-off approach as Egyptians build a new political system on their own terms."

The Crimean War: A History.

BY ORLANDO FIGES. Metropolitan Books, 2011, 608 pp. \$35.00.

Drawing on military analysis and diplomatic history alike, this lengthy book details the three years of 1853–56, when war pitted France, the Ottomans, and the United Kingdom against Russia, and also offers a history of the decades leading up to and following the war. Figes introduces into his story not only leaders but also people of all classes; his settings are not only capitals but also far-flung territories. The four empires get equal attention, and he shows the impact of a changing domestic situation in each—changes

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catalyzed, in some cases, by the spread of the telegraph and the advent of “unembedded” foreign reporting by journalists such as the London *Times* war correspondent William Russell. Florence Nightingale gets her due, and so, too, does Russia’s Nikolai Pirogov, “the first surgeon to employ anesthesia in a field operation.” Figes emphasizes the powerful role of religion in predisposing the parties to conflict, but it was more Orthodox versus Catholic than Christian versus Muslim. This elaborate mosaic of contending leaders, armies, peoples, and ideologies is the most comprehensive history available of the Crimean War.

Shattering Empires: The Clash and Collapse of the Ottoman and Russian Empires, 1908–1918. BY MICHAEL A. REYNOLDS. Cambridge University Press, 2011, 324 pp. \$90.00 (paper, 31.99).

This book brings a usefully different perspective to the final years of great-power entanglement in the Ottoman Middle East. Rather than highlighting the Balkan Wars, Gallipoli, the Arab revolt, and “the twice-promised land,” Reynolds moves eastward to concentrate on the clash between those two old enemy empires, the Russians and the Ottomans, both destined to die by the decade’s end. Their disputed border cut through a “belt of mixed population,” home to Christians and Muslims: Armenians, Azerbaijanis, Circassians, Georgians, Kurds, and others. In this region, Reynolds argues persuasively, both empires were guided more by *raison d’état* than by religious solidarity or nationalism. That fact led to wartime ironies (the Ottomans pushing the Transcaucasians to assert an independence about which the Transcaucasians were dubious)

and turned multiple groups into the victims of tragic massacres (most of all the Armenians, but the Kurds and others as well). With a fine objectivity, Reynolds draws on both Ottoman and Russian sources and reveals how the actions and attitudes of the two declining empires shaped the post-imperial paths of Turkey and the Soviet Union.

Troubled Triangle: The United States, Turkey, and Israel in the New Middle East. EDITED BY WILLIAM B. QUANDT. Just World Books, 2011, 159 pp. \$18.00.

Was there ever a strategic triangle linking Israel, Turkey, and the United States? If so, has it become troubled? Those questions are addressed in this useful volume by experts on the foreign policies of the three countries and the domestic politics that shape those foreign policies. A number of interpretations emerge. The triangle was never equilateral. Washington “provided the incentive and the glue” that held it together. The Israeli-Turkish “alliance” is troubled, but neither side seeks a complete break. The pro-Israel commentariat in the United States has shifted from supporting to attacking Turkey. Changes in Turkish foreign policy are better understood as a response to post-Cold War realities than as resulting from the rise of the Justice and Development Party (AKP), the party with Islamist roots that has been in power since 2002. The AKP’s leaders believe the United States “went to war in Iraq to create a Kurdish state and divide Turkey.” Iranians (the subject of a separate chapter) continue to believe that the “ultimate interest of the United States is regime change.”

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Asia and Pacific

ANDREW J. NATHAN

America's Challenge: Engaging a Rising China in the Twenty-first Century.

BY MICHAEL D. SWAINE. Carnegie Endowment for International Peace, 2011, 673 pp. \$49.95 (paper, \$19.95).

Swaine comprehensively reviews the U.S.-Chinese relationship, which he sees as marked by an awkward combination of suspicion and interdependence. When it comes to the medium term, he is judiciously nonalarmist, arguing that dialogue will trump confrontation over economic issues and that China will not displace the United States as the dominant military power in the western Pacific in the foreseeable future. He also reports the views of more than 50 current and former U.S. officials on what ails the Asia policy process. The problems include bureaucratic rivalries (especially between the State Department and the Pentagon) and the failure of the National Security Council to perform its coordinating function. The White House views Congress as disruptive, and Congress suspects the White House of manipulation and deception. Still, Swaine maintains that the United States' China policy has essentially been on the right track and should continue to be defined by a combination of cooperative engagement and hedging. Over the long term, however, the United States must do a better job of managing its problems at home, or, Swaine says, it might be forced into a cooperative security arrangement with China in the Asia-Pacific region.

Chinese Religious Life. EDITED BY

DAVID A. PALMER, GLENN SHIVE, AND PHILIP L. WICKERI. Oxford University Press, 2011, 296 pp. \$99.00 (paper, \$29.95).

Religious life is flourishing in China, Hong Kong, and Taiwan. People practice various forms of Buddhism, Christianity, Confucianism, Islam, Taoism and even Bahaism, Mormonism, and Russian Orthodoxy—sometimes in combination with one another and alongside folk religions and homegrown faiths such as Falun Gong. The religious revival is driven by a hunger for moral meaning arising from rapid social change and the decay of official ideology. This lucid, accessible survey by a collection of academic experts describes the religious practices of the new urban middle class, the Buddhist revival in Taiwan, religious philanthropy, and a host of other topics. In the villages, everyday life is infused with a mix of feng shui, ancestor veneration, worship of local deities, propitiation of ghosts, and divination. In the cities, people evince a growing sense of religious individualism, maintaining, as one informant puts it, that “what I believe is nobody’s business but my own.” Religious activity helps mend the tattered fabric of social trust, and in that way, it contributes to the government’s goal of social harmony. But it also challenges the state’s policy of constraining religious practice, creating the threat of independent social action.

Asia's Space Race: National Motivations, Regional Rivalries, and International Risks.

BY JAMES CLAY MOLTZ. Columbia University Press, 2011, 288 pp. \$35.00.

Space programs are surprisingly common across Asia, although not all of them are

technologically advanced. China seeks to ban weapons in outer space but meanwhile has developed antisatellite and manned space flight capabilities. Japan has long had the region's most sophisticated space program for peaceful purposes, but in 2008, the Japanese parliament lifted a ban on the use of space for defense. India's space program has also adopted a more militaristic orientation, building satellites for reconnaissance, intelligence, and navigation, with potential applications for missile defense. South Korea's space program is a latecomer, developed largely in cooperation with other states and spurred in part by the need for surveillance of North Korea's missile activity. Smaller space programs exist in nearly a dozen other nations in the region, making Asia a new epicenter of space activity. Moltz deftly melds technological expertise with history and political analysis. He warns that the region's competitive dynamic is bringing military applications to the fore instead of peaceful activities such as geographic sensing, weather forecasting, and telecommunications.

Human Rights in Asia. EDITED BY
THOMAS W. D. DAVIS AND BRIAN
GALLIGAN. Edward Elgar Publishing,
2011, 256 pp. \$115.00.

Asian governments no longer reject the universality of human rights in principle, as some did as recently as the 1990s. Instead, they seek to interpret those norms in ways that are consistent with priorities such as political stability and interethnic harmony. Many governments have adopted new laws and established human rights commissions or other national human rights institutions. But these have been powerless to prevent such abuses as the revival of extrajudicial killings in the

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Philippines under former President Gloria Macapagal Arroyo and the unchecked use of violence by the police during the war on drugs in Thailand under former Prime Minister Thaksin Shinawatra. Governments throughout the region continue to justify repression with a mix of culturalist and security arguments. Nonetheless, the group of mostly Australia-based contributors to this book believe that pressure from local civil-society groups and transnational advocacy networks are gradually strengthening the force of the human rights idea in the region.

From Iron Rice Bowl to Informalization: Markets, Workers, and the State in a Changing China. EDITED BY SAROSH KURUVILLA, CHING KWAN LEE, AND MARY E. GALLAGHER. Cornell University Press, 2011, 248 pp. \$39.95.

Under increasing pressure in a liberalizing economy and abetted by local governments hungry for growth, Chinese enterprises have shifted an estimated 39 percent of China's urban work force from permanent employment to the "informal" sector, where workers get lower pay, forgo job security and benefits, and experience frequent violations of labor standards. The central government, fearing political instability, responded recently with an updated labor-contract law and pension reforms. Perversely, however, those measures have actually intensified the incentives for enterprises to avoid long-term labor commitments, entrenching what one contributor to this insightful volume calls a state of "permanent temporariness." Worker pushback has taken the form of petty sabotage, work slowdowns, demonstrations, strikes, and fragile efforts to organize independent labor organizations.

As a whole, this collection suggests that if China cannot balance the need for flexibility in the job market with the demand for social justice, it will be hard for the country to continue its rapid economic growth while maintaining political stability.

No Enemies, No Hatred: Selected Essays and Poems. BY LIU XIAOBO. EDITED BY PERRY LINK, TIENCHI MARTIN-LIAO, AND LIU XIA. Belknap Press, 2012, 400 pp. \$29.95.

Although the Nobel Peace Prize recipient Liu has been unable to publish anything since his most recent detention, which began in late 2008, Link, his co-editors, and a superb group of translators have assembled an impressive sampling of Liu's courageous and insightful writings from the past two decades in this remarkable, highly readable new book. Liu's critical essays and moving prison poetry combine to form a fascinating portrait of China during a period of rapid development and political change. If there was ever any doubt that Liu deserved the Peace Prize, this book erases it.

In addition to Liu's penetrating dissections of China's inscrutable one-party state, the book includes the full text of "Charter 08," the now-famous manifesto that led to his current 11-year prison sentence for "inciting subversion of state power." These, along with Liu's memorable trial statements, make clear why the Communist Party believes his peaceful words are so dangerous. The book also includes Liu's lesser-known but equally important critiques of U.S.-Chinese relations and reflections on Chinese society and culture, including a particularly vivid essay on the commercialization and sexualization of

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Chinese life and the impact of those changes on politics and morality. Neither China specialists nor newcomers will soon forget this powerful book. Unfortunately, the Chinese people will not get to read it, since Liu's work has long been banned in China.

JEROME A. COHEN

Deng Xiaoping and the Transformation of China. BY EZRA F. VOGEL. Belknap Press, 2011, 928 pp. \$39.95.

China scholars might think they have read enough about Deng Xiaoping. After all, at least three biographies of Deng were available prior to the release of this massive new book. But Vogel, one of the world's preeminent Asia scholars, has produced the most comprehensive and authoritative account of Deng's career as a revolutionary, party leader, and architect of China's reform. Meticulously researched and highly readable, the book is not a typical biography. It does not dwell much on Deng's personal life. Instead, the focus of the book is Deng's unusual career trajectory, his unique style of rule, and the strategic choices he made during and after the Cultural Revolution. Vogel considers the extent to which Deng fundamentally and irreversibly transformed China's society, governance, and relations with the outside world. In Vogel's view, "no other leader in the twentieth century" did more to improve the lives of more people or had such a large and lasting influence on world history. Although he believes that Deng's overall role in history has been underestimated, Vogel argues convincingly that Mao Zedong's hand-picked successor, Hua Guofeng—and not Deng—was the true harbinger of China's reform and opening. The book

could have paid more attention to the downsides of the changes Deng wrought, such as omnipresent corruption and a rapid decline in social morality. Nevertheless, this book should be read by anyone who wants to understand the domestic and international dynamics that have led to China's rise as a great power.

YANZHONG HUANG

Africa

NICOLAS VAN DE WALLE

Consuming the Congo: War and Conflict Minerals in the World's Deadliest Place.

BY PETER EICHSTAEDT. Lawrence Hill Books, 2011, 272 pp. \$24.95.

Congo Masquerade: The Political Culture of Aid Inefficiency and Reform Failure. BY THEODORE TREFON. Zed Books, 2011, 176 pp. \$107.95 (paper, \$22.95).

Two new books survey the contemporary Democratic Republic of the Congo (DRC), following close to two decades of state collapse and civil conflict. Eichstaedt's book focuses on the conflicts in the eastern DRC in 2006–9. Through interviews with soldiers, politicians, and businesspeople, along with ordinary people, the book explores the role that resources such as gold and coltan played in fueling the conflict. One particularly fascinating chapter narrates a decadelong struggle between rival warlords and their foreign backers, including the Ugandan government, to control a lucrative gold mine. Coltan, a mineral widely used in advanced electronics, such as cell phones, has emerged as a convenient symbol of the West's complicity in the wars in the DRC. Eichstaedt diligently traces the supply chain, from primitive mines

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in the forest to the subsidiaries of major Western corporations. But he notes that probably less than ten percent of the world's coltan comes from the DRC and reports that many companies have responded to the negative publicity by adopting voluntary codes of practice that aim to mitigate the worst abuses associated with coltan mining.

Trefon takes a broader view of the DRC, examining the country's sociopolitical dynamics and its failing institutions. His book has no heroes. It is sharply critical of the DRC's rapacious political class. But Trefon is perhaps even more critical of the aid efforts of the United Nations, various bilateral and multilateral donors, and international nongovernmental organizations, all of whom he suggests might actually be making things worse, by perverting institutional incentives for reform. The Congolese state, meanwhile, remains essentially collapsed, unable to provide social services or ensure law and order. The uncoordinated proliferation of donor projects weakens the state apparatus by hiring away the few available competent Congolese administrators and by providing various perks and resources to a class of local middlemen who now live off foreign aid.

Southern Africa: Old Treacheries and New

Deceits. BY STEPHEN CHAN. Yale

University Press, 2011, 304 pp. \$30.00.

The main subject of this sometimes rambling but always readable account of the recent history of southern Africa is the close relationships between the region's political leaders. Although Botswana and Zambia make occasional appearances, Chan focuses on South Africa and Zimbabwe and emphasizes the many links between them, from the attempts

by former South African President Thabo Mbeki and the current president, Jacob Zuma, to broker a peace deal in their northern neighbor to the three million or so Zimbabwean refugees currently living in South Africa. Chan, a longtime observer of African politics, considers how the shared worldviews of such leaders as Mbeki and Zimbabwe's autocrat, Robert Mugabe, stem from their similar educations and experiences in the long anticolonial struggle. Chan is fascinated by the personal foibles of the region's long-standing leaders and has an eye for telling details, such as Mbeki asking whether he needs to wear "ridiculous shirts" like Nelson Mandela in order to enjoy the former leader's levels of popularity and the \$65,000 wristwatch worn by the governor of the Reserve Bank of Zimbabwe, even as the country's currency disintegrated.

Making War in Côte d'Ivoire. BY

MIKE MCGOVERN. University of

Chicago Press, 2010, 240 pp. \$75.00

(paper, \$25.00).

Under the leadership of President Félix Houphouët-Boigny, who managed Côte d'Ivoire's transition to independence, the country was perceived as one of West Africa's few success stories, at least until the late 1980s. Domestic political stability and close relations with France aided steady growth in the economy, which was based on agricultural exports, most notably cocoa. By the time Houphouët-Boigny died, in 1993, the Ivoirian miracle had already been seriously tarnished after a collapse in cocoa prices. But few predicted the country's descent into ethnic polarization and civil conflict. McGovern demonstrates how ethnic identities became entrenched over the decades, as a result of the mass

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migration of northerners encouraged by the government to find work in southern cocoa-producing regions. When the economy stalled in the 1990s, politicians such as Laurent Gbagbo took advantage of the resentments generated by conflicts over land and social inequalities. McGovern skillfully unmaskes the financial interests at stake in the country's politics: the cocoa sector continues to generate substantial revenues, which the state elite controls through an opaque web of public and semipublic organizations.

South Africa Pushed to the Limit: The Political Economy of Change. BY HEIN MARAIS. Zed Books, 2011, 544 pp. \$126.00 (paper, \$45.00).

This book, by one of South Africa's most prominent progressive journalists, is a thought-provoking analysis of the weaknesses and failures of the country's leadership since the end of apartheid. After reviewing the ruling African National Congress' record on economic policymaking, HIV/AIDS, education, and antipoverty measures, the book examines the country's coalition politics and details the ascent of President Jacob Zuma in recent years. Not everyone will agree with Marais' assessment that governance has suffered from the excessive influence of corporate capital. Although he concedes that policymakers have succeeded in some areas, Marais argues that barring an unlikely radical break with the tradition

of corporate power, the government's initiatives are doomed to have a limited effect on economic growth and people's welfare. Perhaps as a result, the book offers few prescriptive solutions to the policy failures it identifies with passion and at great length.

FOR THE RECORD

In "Surgical Strikes in the Drug Wars" (September/October 2011), a sentence on the number of U.S. congressional sponsors of a marijuana legalization bill should have noted that, at the time of writing, the bill had nine sponsors.

In "Is Indonesia Bound for the BRICS?" (November/December 2011), a sentence on the percentage of Indonesia's population that is under the age of 30 should have read 54 percent, a sentence on Indonesia's 2004 peace settlement with Acehese separatists incorrectly identified the separatists as Javanese, and a sentence on Indonesia's main exports should have included metal ores. 🌐

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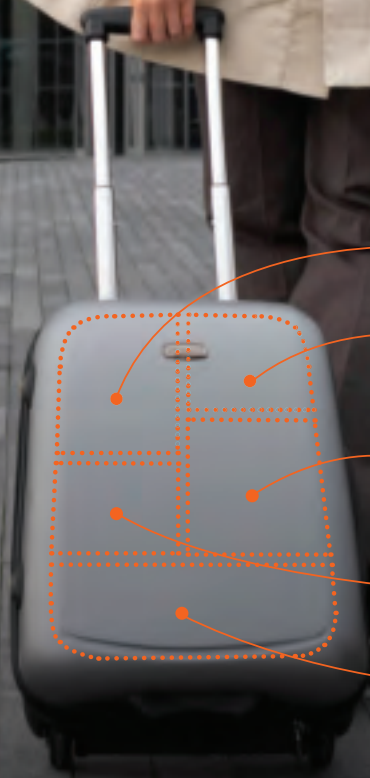


ForeignAffairs.com Top Ten

The top-ranking online articles from winter 2011.

1. *Why Only Germany Can Fix the Euro.* BY MATTHIAS MATTHIJS AND MARK BLYTH. As the eurozone's biggest economy, it was Germany's job to stabilize the system when the first signs of financial trouble appeared. Instead, it did precisely the opposite. ForeignAffairs.com/Matthijs_Germany
2. *Why Obama Should Take Out Iran's Nuclear Program.* BY EDELMAN, KREPINEVICH, AND MONTGOMERY. Iran is closer to having nuclear weapons than is widely assumed. The Obama administration must use military force to prevent that—and soon. ForeignAffairs.com/Edelman_Iran
3. *The Trans-Pacific Partnership and the Rise of China.* BY BERNARD K. GORDON. The United States is preparing for an Asian century. Officials hope that the TPP, a free trade agreement soon to include Japan, will help solidify the U.S. economic role in Asia. ForeignAffairs.com/Gordon_Partnership
4. *Why Occupy Wall Street is Not the Tea Party of the Left.* BY SIDNEY TARROW. Unlike other movements, the rallies across the United States have no distinct constituency and a shifting configuration of supporters. They are something new. ForeignAffairs.com/Tarrow_OWS
5. *The Fight for 'Real Democracy' at the Heart of Occupy Wall Street.* BY HARDT AND NEGRI. The movement is gaining traction because it is exposing a larger failure of democratic representation. ForeignAffairs.com/Hardt_OWS
6. *The Grooming of Rahul Gandhi.* BY SUMIT GANGULY. There is little doubt Rahul Gandhi will become India's next Prime Minister. Only, as he seems destined to inherit a political mess, is two years enough to prepare him for the challenge of a lifetime? ForeignAffairs.com/Ganguly_Gandhi
7. *How Cutting Pentagon Spending Will Fix U.S. Defense Strategy.* BY BENJAMIN FRIEDMAN. The Pentagon's boosters are right that big budget cuts will limit military capabilities. What they fail to recognize is that would actually be a good thing. ForeignAffairs.com/Friedman_Pentagon
8. *Why Netanyahu Made the Prisoner Swap Deal with Hamas.* BY DANIEL GORDIS. The deal Jerusalem made for Gilad Shalit's freedom represents a return to Israel's core values—especially its pledge never to leave a soldier behind. ForeignAffairs.com/Gordis_Swap
9. *Obama Takes on the LRA.* BY SCHOMERUS, ALLEN, AND VLASSENROOT. Obama's recent announcement that he would send a small number of troops to Uganda is only the latest chapter in a feeble, decades-long U.S. attempt to take out Joseph Kony and his militia. ForeignAffairs.com/Schomerus_LRA
10. *How Private Companies are Transforming the Global Public Health Agenda.* BY SONIA SHAH. Over the last three decades, public funding for global health organizations has dried up. Private companies are writing checks to fill the gap. ForeignAffairs.com/Shah_Health

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