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Moderators:

IZAK ATIYAS
Professor
Sabancı University

KEMAL KIRISCI
TUSIAD Senior Fellow
The Brookings Institution

Featured Speaker:

KAUSHIK BASU
Senior Vice President and Chief Economist
The World Bank

Other Speakers:

GÜLER SABANCI
Chair of the Board of Trustees
Sabancı University

STROBE TALBOTT
President
The Brookings Institution

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P R O C E E D I N G S

MR. TALBOTT: Welcome. I'm Strobe Talbott and it is my great honor and pleasure to welcome all of you. And I'm going to turn over my shoulder and say all of our friends in Istanbul, to the 9th Annual Sabancı Lecture. This is going to be an interactive conversation brought to us by the wonders of technology.

Now, over the last eight years I have learned always to append to this statement the word "inshallah" because I know that the first time I fail to say that the screen is going to go blank and it won't be quite as interactive as we would hope. So, inshallah. But we have great confidence in our technological colleagues.

I want to, of course, welcome all of you who are here in the Falk Auditorium at the Brookings Institution, and also to pass my greetings and thanks to our friends on the other side of the video bridge at Sabancı University in Istanbul. And in particular, to a personal friend, a friend of this institution and to so many of us on both sides of this transaction today, and that's Güler Sabancı, who has made this nearly decade old tradition possible. And I would say an ongoing success. She is, as I think everybody knows, the chair of the board of Sabancı University. She is the niece of the late Sakıp Sabancı, who was a shrewd entrepreneur, a champion of Turkey's economic and democratic reforms, and a

philanthropist to whom this lecture is a living memorial. Special greetings as well to his daughter, Dilek Sabancı, and also to Professor Izak Atiyas, who will be moderating the conversation on the Istanbul side.

Here at Brookings I want to say how terrific it is to have Nehat Bakur with us once again on this side of the bridge. He's occasionally been on the screen but it's wonderful to have him here today. And of course, Fuat Keyman, who is the director of the Istanbul Policy Center and has already contributed to the conversations that have been going on here in Washington over the last 24 hours.

And Timor bey, if I may say so, Timor Suelemas, who is the chargé of the Turkish Embassy here in Washington, has made his own contribution to these proceedings. Thank you for being with us this morning -- or this afternoon in the case of our friends on the other side.

A word of gratitude to the 2013 Sabancı Lecture. Kaushik Basu, who is the chief economist of the World Bank, and also formerly the chief economic advisor to the Government of India. Kaushik is a renowned academic, an expert on development strategies and emerging markets. And this is definitely the year for us to be discussing that topic.

As we all know, this is the era of globalization, which by definition is an era in which geopolitics is now often driven by geo-economics. The emerging economies have grown faster in their GDPs to

the tune of about three times faster over the last quarter of a century than the developed world. And prime examples of that phenomena are, of course, Turkey, and Dr. Basu's native land, India. In the 1960s, both of those countries had what were essentially closed economies. Since then, however, they have become both beneficiaries of and contributors to the very process of globalization. Both have produced global companies, a prime example of which is the Sabancı group.

Another point about the nexus between geo-economics and geopolitics. Turkey and India are members now of what might be called the Board of Directors of the world by virtue of the G-20 and other forums to which they belong. They are also both playing constructive roles in their own neighborhoods, and both, it can be said, they have zero neighbors with no problems. I suspect that will be part of the context of what we hear from Dr. Basu, including in his conversation with all of you, which will be moderated in Istanbul by Professor Atiyas and here at the Brookings Institution by my colleague Kemal Kirisci, our TUSIAD senior fellow and director of our Turkey project.

Now, usually at this point in my ceremonial duties I ask everybody to turn off their mobiles. I'm not going to do that today. I'm simply going to ask that you put your mobiles on silent but that you use them if it's for purposes of tweeting. The Twitter handle or hashtag I

guess it's called to participate in the Twitterverse in this conversation and to make sure that as much of the world knows about it as possible is #Sabancı13. Not quite sure why 13, but never mind. We'll keep that number in mind. Lucky 13. Sabancı13. And with that I'm now going to turn the proceedings over to Güler Hanim.

MS. SABANCI: Good morning, Washington, and thank you Strobe.

Before going into the lecture which we all look forward to Dr. Kaushik Basu's comments and lecture and discussion on that, I would like to take this opportunity for those who have contributed for the successful - the ninth anniversary of the Sakıp Sabancı lecture. I do feel really privileged and proud that both institutions -- Brookings Institution and Sabancı University -- where it has accomplished a partnership I can say under Strobe Talbott, my friend's leadership. Kemal Dervis is there, and Dr. Kirisci has joined them. And from our side, Frot Cayman and Professor Nyatbeke who is this year in Washington and I'm here in Istanbul. I'm also very proud and honored that this relationship, this partnership successfully achieved its ninth year.

For those of you who all know my late Uncle Sakıp Sabancı, this lecture is in the honor of his memory and of his lifelong accomplishments. We will try to honor and cherish his legacy through this

lecture and to connecting two worlds -- Washington and Istanbul -- through Brookings Institution and Sabancı University, and that he would love to hear and see this. And I'm sure he's feeling this.

He was a man who understood that without morals, without ethics, without genuine commitment to the well-being of the community and the society at large, no enterprise could possibly succeed and no growth would be long term and sustainable. He strongly believed in this. And as the Sabancı family, we hold these values true to our hearts. And today I am very pleased to hear that we will be hearing from Kaushik Basu, who has been -- Dr. Basu has been the champion as Strobe Talbott has just introduced -- he has been the champion of these values, who committed himself to the prosperity of the world community. So I'm looking forward to this lecture and the discussion afterwards, and thank you again for those of you who come and will join us and are looking forward to this lecture. Thank you.

(Applause)

MR. BASU: Strobe Talbott, Güler Sabancı, distinguished members of the Brookings fraternity over here, and also students, faculty, friends in Istanbul at Sabancı University. I had been to Sabancı years ago but curiously enough only for a meal. There was a small conference dinner that was organized but it is now good for me to be able to interact

long distance with you all.

Let me stress that for me this is a great honor to be delivering the Sakıp Sabancı Lecture. There are some industrialist who through their, of course, enterprise that you need to be a successful industrialist, but moral courage, convictions can play a role in steering a nation. Sakıp Sabancı was a person of great stature, played a major role along those lines. There have been similar characters in the country where we stand. I can think of my country, India, there are similar characters who have played a major role. And once again, thank you very much for Kemal, from whom I first got the invitation -- Kemal Dervish for the invitation to give this lecture. Thank you very much.

We live in interesting times. As Strobe and I were walking in he was saying, oh, the burdens of living in interesting times, which is true; that these are risky times. News composing at a pace that is alarming. News which is occasionally and often more frequently news of downs keeps pouring in. What's happening? And that's what I want to pitch my lecture, is about the changing structure and nature of the social world. What's happened over I would say the last 50 years is perhaps the most dramatic change in the social world -- social I use broadly to include economics, politics, and society -- then maybe ever before. In particular, economic globalization has gone on almost hand-in-hand with politics and

decision-making remaining balkanized and fragmented. The strange combination of balkanized politics and globalized economics has given rise to tensions, challenges of a kind that we have not seen before.

About the globalization, economic globalization, I find the debate on whether it is good or bad pretty futile because it's similar to debating whether gravity is good or bad. You can tear your hair over whether gravity is good or bad but there isn't very much you can do about that. Globalization is something similar. No one individually plans to have globalization. It is millions and billions of individuals taking their own little decisions, new technologies sprouting up that has led to globalization. It's a part of life that we have to live with.

We can do something about decision-making, which is fragmented policymaking, which is fragmented, and that's where I'm going to focus the lecture about the policy challenges. And in doing so, I'm going to use a combination of my own background from completely academic economics to being plunged four years ago into the thick and turmoil of Indian policymaking and now in the World Bank, a concern with the developing countries, emerging economies all around the world. And I've been arguing in the World Bank that we also ought to be engaged with the industrialized countries simply because the world cannot be thought of along the partition lines that we once did.

When I went to India first, to begin on a personal note, when you have discussions at the level of the policymakers, the top bureaucrats sitting in New Delhi, it'll be the same in Istanbul where I've been several times in many different forums, it feels like as if you're in Washington or London or anywhere else. It's the same language being talked about. The people have broadly been educated in the same places, and really there is very little to distinguish. And I've just been traveling in Africa, in Senegal and South Africa, and once again it's a similar feeling that when you sit with the elites, it's the same newspapers being read, the same journals being read, so the language and everything seems similar. So what is different in a developing country, in an emerging economy from an industrialized country, for me there was the occasional reminder, dramatic reminder that I was in a totally different setting, completely trivial, and I have written about this already but it sort of stands out in my psyche.

In Delhi, I had once a pest control problem in my home, so I called in a pest control agency. A man came, a gentlemen with lots of cans and cylinders, all kinds of chemicals, and started spraying my home. And he was working very hard so I came in and said, you know, you are working very hard but will you get rid of the termites and pests? He said with a grin, "Sir, have no worries whatsoever. These chemicals are very strong stuff. They are totally banned in the United States." (Laughter)

By the time he was finishing his sentence I was beginning to edge out of the room. So for him what was a source of comfort, in many places it would be a source of great discomfort. But years have passed and nothing dreadful happened, so I'm taking his lack of caution was fine. But small reminders like that would come every now and then that we live in a very, very different economy.

I would, for instance, when doing my Indian job -- this could happen anywhere. This could happen in the U.S. -- people's understanding of the economy, who does what, is still very, very rudimentary. I would occasionally get a phone call from an aunt in Calcutta saying that prices have gone up once again. What is it that you're doing? So they would go to a market and find that the fish price has gone up, and there's the presumption that somehow sitting in Delhi you can manage it all, so that fretting, which actually you see here, as if a few people are managing this and causing this, is everywhere, which makes it important to bring a lot of professional knowledge into the management of the economy. This does create difficulties. I should tell you a difficulty and an element of suspicion which you will see in the U.S., which you will see in the Turkey, which I saw in India, that for a lot of people it is not possible to understand the intricacies of policymaking. And you do worry at times that is policymaking being hijacked by a small group

in their own interest? And that's not impossible. When a small group has specialized knowledge it is possible, but the best guard against that is general education. People have to understand as well as possible some of the intricacies of policymaking so that ordinary human beings can be watchdogs about what is happening and what decision is being taken.

I'm going to begin by giving you a very quick glimpse of the changing structure of the global economy and then go into some policy challenges. Let me give you one chart which I've been using, which is the BRICs economy.

Do you have -- okay, I'm going to do it. Yeah.

So you will see over here the GDP proportion fraction of the world GDP, which is the BRIC countries' GDP. They're okay in Sabanci. They're doing fine. They're seeing the same chart I'm assuming, right? Yeah, hopefully. If you're not seeing the same chart, well, then just two or three, you can think of something else while I get back again to talking.

You will see, this is quite a dramatic chart so I took the case of BRICs because BRIC countries are being tracked -- that from somewhere like 15 percent of global GDP -- 15-16 percent in 1990, the BRICs constitute today a little over 26 percent -- 27 percent of global GDP. We are talking of percent. So the share of the hundred, a rise of this kind is rarely seen. So the emerging economies, you are seeing a

very, very dramatic rise. Turkey over the last 10 years I know has been growing at just short of 5 percent -- 4.7 percent or so -- which for a country which is reasonably well off -- I mean, \$10,000 per capital income, a growth of 4.7-4.8 percent sustained over a 10-year period is a remarkable performance.

Indeed, I remember sitting in India. Of course, I would be watching the industrialized countries all the time because it mattered a lot what was happening in Europe, what was happening in the U.S., but I was also -- we were watching Turkey a lot because I have to say that to the credit of the Turkish policymakers, particularly the central bank, they've been very creative or experimental. This is a word one usually uses with some caution about the central bank. Central banks are meant to be very traditional, but I do this with some appreciation that the Turkish Central Bank has brought in some innovative ideas, made moves that were controversial, but they were sort of testing the waters. And what better than to watch another country test the waters sitting far away and see what happens. So Turkey was a country that I used to watch a lot, especially its tackling of inflation. And one continues to actually appreciate the fact that it's been a very innovative environment in terms of macroeconomic policymaking.

South-south trade. I want to give you a quick glimpse now of

the increase of that. Here is a picture of south-south trade, and you will see the growth of trade of the southern countries with southern countries, so developing and emerging economies with developing and emerging economies, 1960, just short of 15 percent of imports of developing countries would be from developing countries. Developing -- I'm using developing and emerging. And by early 2000, it was just short of 30 percent, and some recent data crunching by the World Bank shows that between 2010 and 2011 southern countries -- imports from southern countries have just crossed 50 percent.

So there is an element of resilience beginning to build up. And I'm going to come onto this theme about southern resilience, which is needed in today's troubled world, but I want to warn you that it is very easy to begin to think that the resilience is huge, which it is not. It is a very interconnected world. And I'll show you the lemon crisis, which is quite fascinating. It's basically think of this as borrowing cost of developing countries' sovereignties. Lemon crisis takes place in the U.S. and the borrowing cost for developing country governments just shoot up. It's a sign of the interconnected world.

And let me give you one example where I was hands-on working, and this is going to link me up with some very important and interesting intricacies of the interconnected world. In August 2011, I was

still in Delhi doing my previous job as chief economic advisor to the government when S&P downgraded the U.S. U.S. investment was downgraded by S&P and I remember the evening when the news came. I was in Delhi. We got the news and we were wondering what's going to happen. The U.S. economy is going to be rocked a bit. India should be fine in the short run but we will feel the pressures in the long run. But what happened was actually fascinating. Money started flowing into the United States treasuries. So after S&P's downgrade of the U.S., money is flowing into U.S. treasuries, so you are seeing this effect on the exchange rate in India. You are seeing this in Brazil. You are seeing this in South Africa, even Europe, barring Germany is seeing money being pulled out and going into the U.S. treasuries. What has happened?

Analyzing that gives you a glimpse of the changing structure of the world economy. This is investors looking for safety, and where do you find safety? Well, you want to put your money into bonds of governments, which also have the assurance that the government can pay you back. This means that if there is a weak economy, you worry about that. Or if you have an economy which may be strong but without its own central bank, you worry about that economy's ability to pay you back. So putting money in U.S. treasuries is safe because you know that the U.S. has access to a central bank. And the last thing that the U.S. would want

is to default on an international investment that has been made in the U.S. The central bank, the Fed is going to step in.

This had gone from Europe by this time. There are European countries which are by any global standard strong global economies, but they don't have their own central banks anymore. If you put in money with Spain or France or Italy, when the time comes to pay back, they don't have that access anymore. Printing money to pay back is not a good idea, but it's a last measure that if there is a central bank that you could get that bank to do it; if you don't have a central bank you don't have an assurance. So money which earlier would have gone into Europe did not go into Europe because it's a different Europe. It's the eurozone with one central bank.

I should stress over here I do believe that the eurozone experiment is the right experiment. It's the right direction to go. Just that. When you make such a big, deliberate construction of an economic structure, it's not surprising that fault lines will show. Most of the economic practices that you see today in the world have evolved slowly over time, and the forces of evolution have buffeted them, corrected them so over time the rules that we follow in terms of the management of the economy through evolutionary processes, if not through understanding, have gotten corrected and the bad practices have fallen out. Europe was

a deliberate construction. It did not have the advantage of 100 years of evolutionary correct, so it's not surprising that fault lines would show and fault lines did show. So money rushed into the U.S. at that time and we, for the first time, we see this happening -- the exchange rate in India beginning to move and we realized that globalization has changed the landscape.

Let me turn to one picture I'll show and then I want to move on and do a little bit without pictures. This is the eurozone. I like this picture because it illustrates a dramatic feature of what happened in the eurozone and the fault line that I was talking about. I want you to understand this and you'll give an intuitive understanding even without getting into the details.

What I'm tracking here is from 1999, borrowing costs of eurozone countries. So roughly think of this as sovereign borrowing costs of the sovereigns. On the formation of the eurozone, people, not only policy makers -- they did not understand, no one probably understood, even investors, treated all the eurozone countries roughly the same. So you invest money in Spain, you invest money in Germany. The safety of that is the same because now they are one common currency idea, the eurozone.

So the borrowing cost of Spain and the borrowing cost of

Italy and borrowing cost of Germany was the same, and so in the beginning, if you look at the borrowing costs, they are virtually the same from 1999 to roughly 2008. In 2008, it dawns on people that yes, their eurozone is a monetary union but each country can default separately. Spain can default when Germany does not default, so the risk of lending to these countries should not be treated as the same, and once that realization came the borrowing cost suddenly fanned out. Some countries would have to pay a huge interest to be able to borrow because people realized they are risk; others would have to pay a very low interest to be able to borrow because they were not risky. This realization that came came in some ways too late because what happened before that was that because of the lowered cost of borrowing for many economies, which should have had a higher cost of borrowing, they over borrowed.

So by the time we wake up in 2009, there has been fiscal profligacy, a huge fiscal profligacy on the part of our whole host of countries, and now we are grappling with that. And I do agree that jumping to austerity is not the right way to go. There has been fiscal profligacy in the past. You can see this in the debt GDP ratio, and in terms of many other fiscal indicators, but you have to use a combination of very well crafted policies.

So with that I want to -- where do we stand today and what

do we expect to see over the next few years, and then I want to turn to a couple of policy challenges. And once again, putting those policy challenges from the point of view of the developing countries.

You know, forecasting is such a hazardous task that one hesitates to do that. What will the next two years look like? But let me stick my neck out. In the early 1960s, in Calcutta, in an uncle's home there used to be a letter from President Kennedy congratulating this uncle for correctly predicting Kennedy's election victory in 1960, the famous election victory, for correctly forecasting. My uncle used to display it very proudly in his home. And we, the cynical nephews and nieces believed that the uncle had managed to get that letter from Kennedy by sending an identical letter to Nixon predicting his victory as well, so that no matter who won, my uncle would get a letter for his wall.

Now, that's strategy that economists sometimes use. You hedge your bets by saying so many things that no matter what happens you'll be right. There's another ploy -- not quite ploy -- there are some people who will always predict doom and then sometimes when the doom happens, of course they've got it right. Or some people always predict a boom, and when that happens you've got it right. Let me not do those and let me stick my neck out and try to give you a relatively clear belief and with all the question marks the future has answered. I believe that this

crisis-like situation will last for at least another two years. And the reason for that belief is that what we are seeing around the world, policy moves which are right but they are not solving anything. The injection of liquidity that you're seeing around the world from Japan, the United States, Bangkok, England, Swiss National Bank, all the injections are buying time.

The ECB, they are buying time, but they are not solving problems. And some of this injection took place in huge doses at the end of 2011 and at the beginning of 2012. In fact, 1.3 trillion Euros injected -- sorry \$1.3 trillion -- no, \$1.3 trillion, yes, about 1 trillion Euros -- I was getting the currencies wrong -- injected into banks in Europe which will have to be paid back three years down the road, at the end of 2014-2015. There is no sign that these are being invested in ways where the repayment is going to be easy, so there is a very good chance that there will have to be one more round of injection at that time to again keep the banks buoyant.

So the injection of liquidity that has taken place, and if I was at the helm making these decisions I would do the same, is what had to be done, but they've bought us time. They have not cured any of the problems. The two big problems that we need to attend to, one is fiscal coordination in Europe, better fiscal coordination in Europe, and the other is banking union. Very structured banking union. We do know that this

creates some strange political problems of within eurozone countries taking one view and E.U. countries, which are not in the eurozone taking another view because it will be a united banking union of one group. So there are tensions. We don't know whether that will happen.

But there are other policies that we have to go in for to meet this challenge of the current times. Look at the fallout of this for the world of not being able to solve the problem. This injection of liquidity does create certain kinds of problems which Turkey has faced, India has faced, China has faced. It's around the world. There has been generally, over the last three years if you look at the global economy, it's a strange kind of stagflation. It's not stag and flation in the same place but stag in some places and flation in some places. Most industrialized countries are stagnating. The eurozone is technically in recession, so Japan has been stagnant for a very, very long time.

But developing countries, emerging economies where growth has been extremely buoyant, Turkey, last year's growth was not good but before that Turkey was growing extremely well for a very long time. India, last year's growth was not good but before that India was growing phenomenally well. But all these countries -- Vietnam, even China, growing well but with a problem of inflation. Earlier, what macroeconomic policymakers were doing in emerging economies was that

they were responding to the injection of liquidity in the industrialized world by trying to drain the liquidity in emerging economies, which was giving rise to a strange tension, liquidity being injected at one end and being taken out at another end.

That policy has begun to change. Most emerging economies are not doing that anymore. You are beginning to see the lowering of interest rates, repo rates, call money rates are beginning to go down in emerging economies so they are not doing what they were doing earlier. And this is giving rise to a new set of problems. Where should we go from here to solve the global problem and my interest really is from the point of view of emerging economies for the following reason. Industrialized countries, even if they grow slowly, they are rich countries. Slow growth for them is not a dramatic event, except in the unemployment situation. And I will comment on that.

If a country like the United States, Europe, if they can grow at 2 percent per annum, which would be considered extremely bad performance for an emerging economy or a developing country, 2 percent per annum would be very good performance. For me that would be moving towards a stable world with a fair amount of employment -- the employment situation is much better.

The probably really is in developing countries that even

though they are growing well, they are growing well still with a mass of poverty. In a country like India about 30 percent of the population is below the poverty line and a poverty line that is drawn very, very low. \$1.25 per person per day, about 30 percent of the population is below that line. Sub-Saharan African, 48.5 percent of the population below that line of \$1.25 per day. At times you hear from activists saying why do you draw the poverty line so low? Indeed, that's a valid question but you must realize that if even after drawing it so low you find so much of the population below that line, that is a worrying feature of the world. So the present crisis of the world economy is, true, the crisis is brewing in industrialized countries but our primary focus has to be the developing countries and the low income countries where the consequence of this, even if it's a tiny growth change, the consequence of this can be quite dramatic.

What should be the policy move? I have three suggestions but the third one is slightly technical and I'm going to look at my time and then I'll certainly give you the first two thoughts that I have and the third one I may or may not give you.

First of all, I feel that in today's world the need for macroeconomic policy coordination is greater than ever before, and one fact which I keep pointing to but I think it's just so very important for us to

understand that when in the 17th century these central banks were coming up, one after another, Ricks Bank in Sweden, Bank of England 1694, there was an understanding that a single economy ought to have a single money creating authority. That's one domain where you don't want competition. However, so lots of banks came up around the world. I think there must be more than 200 central banks around the world. One nation, one economy, one central bank. But since then something else changed in the global economy which I began with.

The globalization in economics of the world means the world is increasingly becoming like a single economy. I know that there are still lots of restrictions and barriers but capital does flow fairly easily, goods flow not quite as easily, but goods do flow increasingly and maybe over the last 20 years, last 15 years labor is beginning to flow easily, at times by the workers moving, at times with the job moving to where the workers are sitting. So it's a very united economy the global economy is becoming. But we've created lots of central banks.

So the predicament that we have tried to get out of in the 17th century, one economy with one central bank, we are backed again into a situation where you have one economy with lots of central banks because the walls fell off somewhere along the lines. We are not going to very soon see the creation of a single central bank. The one experiment

in Europe has put a bit of a slowdown to the process of the creation of a single central bank, but we do need policy coordination. I think that's extremely important.

Take the current situation. Japan injecting liquidity. I have to say I personally believe that if you look at the last sort of 10 years of the Japanese exchange rate, Japan had to do it. It is a highly overvalued exchange rate which was slowing down the economy and slowing down the world. Japan has made that move with a gusto let me say in terms of injecting liquidity, but what that has resulted in is that others are sitting up and there will probably be similar moves. We are seeing first of all in Japan the latest data coming in is that most economic activity, industrial activity is going up, so the injection of liquidity is playing a role. But I don't think it's going to play a role for a very long time because other countries are going to make similar moves of injection of liquidity and yes, each country will talk in terms of boosting domestic demand but this also has implications for the exchange rate every time you are doing that.

One thing we do need minimally is a cluster of large economies, and this includes not just the industrialized economies but must include emerging economies, even the poorer but large economies, their central banks have to come together and think in terms of a coordinated central bank policy so that if it could be announced that 20

countries with their 20 central banks sat down and they have laid out the following costs for the global economy for the next three months, in the beginning country X is going to inject liquidity, then one month later country Y will inject a certain amount of liquidity. A roadmap gets laid out. I've been told in the World Bank not to name countries too many times so I'm staying with X and Y, which countries will be given that advice.

So X is told to inject some liquidity, Y is told to inject some liquidity a little bit later. If you can lay out a roadmap of this kind, the speculation that comes with a country unilaterally declaring a policy is going to go down. Also, the exchange rate movement that you get, if it can be a coordinated move, the movement on the exchange rate can go down so the creation of greater liquidity in your country can take place without that injection of liquidity.

Also, in terms of carry trade, today there are huge concerns. I know Turkey is extremely worried about that -- that with these interest rate variations that come with central bank policy variations across the world, it's possible to go and borrow in one country where the interest rate is low and then use it in a country where the interest rate is high. You're borrowing at a very low interest rate and using it in a country where interest rates are high or even through secondary channels, lending it in a country where interest rates are high, which means you're arbitraging on

the interest rate. India, where capital account convertibility is limited, we know that in indirect ways a certain amount of carry trade and interest rate arbitrage takes place, so there is great need for that coordination.

Second policy, which again the whole world needs to puts its mind together, the labor problem I feel is going to get worse over time. What we are seeing in the world -- Michael Spence has done some calculations -- that the total wage bill as a share of the global GDP is shrinking, so the income that comes through work, pure labor, that income is becoming a smaller part of the global GDP pie, which means people are now earning money through many other sources. You're earning profit. You've got a piece of paper which gives you returns, so the labor share is decreasing. This is going to be a long-run challenge for the world to do with the shifts in tectonic plates of the world that I was talking about earlier. As the demand for labor goes down in the world, the first pressure for this will be felt in industrialized countries where the wages are higher and you are seeing that pressure. So the high unemployment that are being seen around the world, Europe is now at, what, 12.1 percent unemployment. The U.S. is 7.7 percent unemployment, which does not sound that high but you have to remember that off that 7.7 unemployed in the U.S., 39.5 -- just short of 40 percent of those unemployed are long-term unemployed, which is very unusual in the U.S. In the U.S., the

unemployment is typically of people falling into that and then getting out of it, whereas now there are 40 percent of the unemployed are long-term unemployed and there are studies which show that you begin to deskill when you are long-term unemployed, so when you go back to the labor force you are not quite as effective.

I think the labor situation is quite dire. Part of this comes from the changing structure of the global labor force, but a part of this also has to do with policy, which can be attended to once again through a little bit of a coordinated special policy intervention. And this is the policy intervention that you need in industrialized countries. When you inject this liquidity into the economy, industrialized country economy, as I just said, it will typically go with interest rates going very low and interest rates are indeed very, very low. Interest rates are high in countries in emerging economies with the carry trade problem which they have to face. But when interest rates go so low, think of a firm in the United States or in Europe. Your capital cost is going down because liquidity is being injected. So tiny calculation changes begin to take place on the margin that labor is relatively more expensive than capital because capital cost has gone down. So the incentive to employ more labor does not take place when there is so much liquidity injection taking place. That needs to be corrected. Here you have to be very cautious -- and I don't want to put

down anything as a sort of final word on how that needs to be corrected, but my view is that when liquidity is being injected through asset purchase, which is what typically central banks tend to do -- you buy mortgage-backed securities or something else, \$85 billion per month that for instance the United States is doing -- one way to begin to correct the asymmetry in the cost of labor and capital that this gives rise to is to inject a part of this money to make hiring of labor more worthwhile for firms. This has to be a strategic intervention on the marginal cost of borrowing. The subsidy for employment is the direct way to do it on the margin for a temporary period. If you do it for six months, one year, so of the \$85 billion being injected, part is being done to get the demand for labor buoyed up. If this can be done in Europe, if this can be done in the U.S., Japan, across the world, you will begin to create greater employment. Once you create the greater employment, since apart of the problem today is a trap, it's an equilibrium in which these economies are caught, once the workers begin to work, they will create demand for goods. And that's a much better way to create demands for goods by workers actually going and wanting to buy more instead of trying to do it through liquidity, pure liquidity injection. So tilting this in a particular way can do it.

The third topic that I would have talked of is somewhat disjointed so I will not talk about it. It's on the nature of central bank

interventions, and it probably is to do with a little bit more theory since Kemal had first corresponded with me about this topic. And I know Kemal's background as a mathematical economist. I had a few pictures to demonstrate how central banks will intervene but I've just given you a foretaste by telling you that I have that with me but I will not present that over here.

But with these words let me stop here and I'll be happy to continue with questions, comments, or however you want to do it. Thank you very much.

(Applause)

MR. KIRISCI: Dr. Basu, I would love to thank you for such an enriching and enlightening presentation here, but I think I also need to make a confession that I wish the organizers had given us an extra 10-15 minutes to digest the presentation, particularly the technical aspects of it, the parts that relate to policy recommendations.

However, as I was listening to your policy recommendations, particularly the very first one on sequencing of injections, I couldn't help but think that somewhere along the line politics need to be taken into consideration. And wondered how countries are going to be able to agree upon who is going to be the first one to go.

The way we are going to proceed with the rest of the

program today is I'll turn the floor to my colleague, Izak Atiyas at Sabancı University. We will be taking two or three questions. I suspect there will be a number on the Istanbul side of this event, and surely from the audience here as well.

I do have lots of questions in mind. One of them is at times I've heard you say that experts know so much more than nonexperts is how little experts know in general. I remain very puzzled with that statement, particularly as I listened to your presentation.

But let me turn to my good friend and colleague, Izak. Hello, Izak. And hi to everybody at Sabancı University's campuses. I would especially love to salute the students there, Güler Sabancı, who is an old schoolmate of mine from back in Ankara, as well as the rest.

Izak, the floor is yours.

MR. ATIYAS: Thank you very much, Kemal. And thank you Kaushik for a wonderful presentation, very thought-provoking presentation.

At the risk of sounding provincial, maybe just a small comment on Turkey. You mentioned its very remarkable performance, and indeed, it was remarkable the last decade, especially compared to the earlier decades. And another remarkable aspect of this high growth rate is that it was very much productivity-driven. In other words, when you look

at productivity growth, whether you measure it as labor productivity or sort of active productivity, it's high. It's high in international comparison, and it's high relative to the earlier decades as well. So that's happy news, I guess.

However, when you look into the dynamics behind this productivity growth, when you decompose it this way or that way, you find out that a lot of it is really reallocation of resources, especially labor, from low productivity agriculture, to high productivity industry and services, rather than productivity growth within these industries. So there was a lot of structural change going on. And the same with exports. There was a lot of structural change going on. With exports, we used to export mainly garments, textiles, food and beverages, and now we export a lot of automobiles, steel, and chemicals. But still, when you look at the details of those exports you find that Turkey still does not export a lot of sophisticated goods. The share of sophisticated goods, the share of high technology goods is still low.

So there are lots of economists in Turkey. On the one hand we are happy about the growth performance over the last decade. At the same time there's a lot of talk about whether we're still facing -- I don't know whether to call it the middle income trap, but it seems as if Turkey is on the verge of a threshold and a lot depends on what type of policies are

adopted from now on. And I wonder if you have any words of wisdom related to that.

And having said that, let me turn to the audience here and see -- look for questions.

Okay. If you could please introduce yourself as well.

SPEAKER: Hi, my name is Kohan Kocheck and I'm a first-year master student at Sabancı University.

I'd like to ask you, referring to the ongoing disputes regarding the famous paper by Reinhart and Rogoff, *Growth in a Time of Debt*, and keeping in mind the speed with which northern European countries recovered from the financial crisis years of austerity, would it be safe to say that the austerity versus stimulus debate is finally over?

MR. ATIYAS: Thank you Kohan.

I'll take one more question and then I'll switch it over to Kemal.

Okay, over there.

MS. KEEFER: Hi, Kaushik. This is Meryl Keefer.

I have two questions to you. Should emerging nations have any controls on the flow of capital in and out of their countries? What about the problem of hot money issue? And second question, would it be a wise idea for emerging nations to consider joining currency union like

the E.U. or has that now been shown to be a bad idea?

MR. ATIYAS: Thank you very much. And over to you, Kemal.

MR. KIRISCI: Thank you.

MR. ATIYAS: Or Kaushik, if you want to respond.

MR. KIRISCI: Dr. Basu, you have the questions. We look forward to the comments.

MR. BASU: Very good. Let me respond briefly to Kemal, Izak, and then the two questions, the last one from a friend of mine from Cornell, Meryl Keefer.

Let me -- the politics of this which you're referring to is of course there beneath the surface all the time. And if you are naïve, you realize that by going into a policymaking domain. I don't think I was naïve, so when I went into Indian policymaking I realized the importance of politics. A decision that in a closed room the policymakers will all be able to agree. But they can't take that decision because that immediately has ramifications in terms of the votes, in terms of electoral response of the electorate. So that's extremely important and it sort of merges with how you manage to carry these out.

The reason I'm hopeful that we will get better macroeconomic policy coordination today is at times a pain is a sufficient

trigger. When there is pain, that becomes a trigger for change, that change for which is the politics you are not being able to implement, you may be able to do so. So I believe there is a chance now that politics will be overcome because the economic pain is becoming large.

Izak, you know, Turkey I used to follow and I said I probably overstated that. I can't really get into the details of Turkish policy to say whether the range of policies followed till now will continue to serve the country well. What I do know is that say around 2010, 2011, what was quite remarkable about Turkey was that it was growing first of all very rapidly. I mean, 8-9 percent per annum. It was getting that growth with the current account deficit which is very high. And so, in fact, we kept thinking that this was going to be a destabilizing level of current account deficit. In Turkey, if I'm not mistaken, the current account deficit touched 10 percent once, came down to 9, 8, 7, but all these are extremely high. Turkey was managing through that.

And one particular move that Turkey made around that time was in the middle of this inflation, the central bank lowered the interest rates and we were all watching that to see what will that do. Is it going to give another boost to inflation? It did not really do that. Inflation continued to fall after that and the growth remained buoyant. So the policies which we watched over 10 and 11 were pretty good policies.

But whether this will carry on, whether the growth will continue, that's another deeper question for which I don't have enough deep knowledge of Turkey, but one gentle wisdom I will bring from the world. You know, I used to treat one textbookish theory as a textbookish theory and nothing else, which is the relationship between growth and investment. Whether you talk of Harrod-Domar or Solo and Swan, this is there in our textbooks. But for emerging economies and for developing countries -- this will not hold, by the way, for industrialized countries -- the relationship between hired investment, especially if it can be infrastructural investment -- and growth is very, very strong. In the case of India, this was just extremely visible. India used to be a low saving country. To the '50s, '60s, early '70s, India's savings rate picked up very rapidly through the 1970s. India's growth picked up slowly from the 1980s. India's savings rate in the early 2000, 2001, '02, '03, really picked up and India was beginning to save and invest like East Asian countries -- 35-36 percent of the national income was being invested. And two years after that India was growing at 9.5 percent per annum for three consecutive years. The relation comes whether you look at Korea, whether you look at Malaysia, Thailand, Singapore, a bit earlier, China. It comes -- I think China does overinvest a little bit so it gets a lot of bang for the buck of its investment, but the last bit of China's investment probably does not get

enough bang for the buck because it is investing about 50 percent.

But Turkey's figures I do not know, but infrastructural investment, investment which increases productivity, Izak, I take it that that's what you were referring to in terms of keeping productivity high and getting into more sophisticated sectors. Indeed, that is important.

With that, let me go into the question, the first student who asked about the austerity debate, is it over? No. The newspaper debate, the magazine debate usually takes place in such simplistic terms. Is austerity good or bad? You know, a question like that really strictly cannot be answered. It depends on what kind of austerity you're talking about. One thing has to be kept in mind -- that if your debt-to-GDP ratio is 100 percent or 120 percent which it is for several countries in the world, going up to 200 percent for Japan, if there has been such a big buildup of debt, you have to go the direction of trying to wind that down, which does mean a certain form of austerity. But that form is extremely important. To me, the critical question is not whether you go for austerity or not, but it's the distribution of austerity. When you're trying to correct for overconsumption in the past, what you have to make sure is that the burden does not go on the weakest and the poorest sections of your society.

The World Bank is engaged -- going to be engaged with this in one particular way because the World Bank has declared that a new

attention is going to be paid by the World Bank to the bottom 40 percent of every country, including the industrialized countries. And the policy of the kind that I'm talking about is when you go for austerity, the austerity that the richer segments will have to do some curbing, I think that is true, but the poorer segments of the society should not have to do that. So the critical change in the debate I think which will hopefully come out of the huge controversy that you saw over the last recourse is that the austerity debate is going to become more sophisticated a discussion because to put the fiscal house in order you have to do that. But how you put that fiscal house in order and how do you coordinate it with other countries is the critical question. In fact, my hope is that what was a very, very naïve debate will now, in fact, become a more sophisticated debate, the austerity debate.

Meryl, your question about capital flows. Well, I do believe that emerging countries, developing countries, you have to use a certain amount of judicial controls on capital flows. You can't just open the door and say let capital come sloshing in, capital go sloshing out freely. It does lead to kinds of problems that you have to worry about.

Having said that, this has to be kept in mind by any government that once you give government the plate that this is a domain in which you intervene, there is very often a tendency to over-intervene, so

this has to be a very well-planned intervention that you don't allow for excessive volatility of capital. And that, indeed, does closely connect to the question that you asked -- is it worthwhile for emerging economies to move towards currency unions? My belief, and this is very similar to a belief that was expressed in the late 18th century. Stanley Jevons, the British economist, wrote about global currencies. This is not a very well-known work, and maybe he was a bit too early writing about that so it got no traction when Jevons wrote about it. But the idea is that economies that are similarly placed, for them to move towards a currency union I think is the right direction to go. So though we've had our fingers burned through the eurozone experiment, broadly for economies at similar levels to move towards currency unions or currency coordination of certain kinds I feel is the direction in which you have to go for the reason that I mentioned during the lecture. We understood this in the 17th century, that if you have your borders open to labor, to capital, to goods, to have money creating authorities -- have multiple money creating authorities is destabilizing, and we are in that period in the world, so some move towards currency unions, even in these difficult times with the eurozone experiment, is a direction in which we have to go. Hopefully, we've taken lessons from the eurozone, so many of the fault lines we will avoid on this occasion.

MR. KIRISCI: Thank you very much, Dr. Basu.

I can't help again wonder whose currency it's going to be, and that may also reflect (inaudible).

The way we would like to go this, if you could just briefly present yourself, introduce yourself, and then brief questions, two or three questions.

MR. SHERRETTA: Robert Sherretta with *International Investor*.

I'd like you to address the issue of contagion. We've seen both the World Bank and the IMF continue to ratchet down their projections for World GDP growth. You mentioned in one of your charts that south-on-south trade is growing but they still depend to a significant degree on trade with the developed world, sending their commodities, et cetera. So as the developed world has slowed down, are you still concerned that the contagion effect will slow down many other economies as well?

MR. KIRISCI: Right here in the front. It's coming, the microphone.

MR. SHIN: Hi, Richard Shin with *Economist, Inc.*

I have a question about your international macroeconomic policy coordination. Obviously, Dr. Kirisci mentioned in the political side of

it and how difficult it is, but also there's a difficulty coming to an economic understanding among these countries and you mentioned developing countries and emerging countries, but they have different incentives. How do you coordinate that within that group? How would you overcome that? That's the first question.

And then the related question is that you mentioned that liquidity could be interjected into labor-intensive firms or sectors to create more jobs and henceforth kick start your growth. But on the other hand, if you do more labor-intensive liquidity, that will be more domestic-oriented and therefore, less international interaction. Therefore, that may reduce the need for international macroeconomic coordination. So I'd like to know what's the balance there that you were trying to reach with your two policy recommendations.

MR. KIRISCI: Okay, Dr. Basu.

MR. BASU: Robert Sherretta, on the contagion, first let me take on that. The increase in south-south trade -- I'm actually familiar with the suggestion in your question. It gives you a little more resilience but just a little bit more. The trade with the north is extremely important. Also, it's very different kind of products and services with which you trade with the north. And if I again look at the country that I know very well from my last experience, take India's software and information technology sector.

Of the exports that go out of India, 60 percent is to the U.S. alone, so the importance of that relation is absolutely critical. South-south relation is not going to make up for that very quickly, so that is well taken.

On contagion, here is the point. The real contagion in terms of a slowdown in growth affecting another party, because of these factors that trade goes down your scope for export goes down, yes, that's going to happen but there's another aspect to contagion which is more worrying and less understood is financial contagion. This takes place through very strange psychological roots. You know, there's a lot of rather abstruse writing in economics on financial contagion, but we must not push that aside as abstruse writing. There is something to be said on how these financial contagions take place. If you remember, in 1997, the East Asian crisis, it was barking from one country to another and in more distant countries, suddenly Russia is getting affected by what's going on in East Asian countries and you can't quite track it through trade routes. But it is the investor psychology.

What happens basically is when one is lending to a particular country or a particular corporation, if you know that other people are lending also to this organization or to this government, without doing too much homework about whether it is safe to lend or not, you continue to lend because you know that others are lending. So when you want to

pull out, it's easy for you to pull out. But this kind of reasoning leads to a very strange brew. Everyone is lending because everybody else is lending. And this can suddenly fuse and vanish when everyone pulls out of it because it's the interdependence. This kind of contagion, which happens in the finance world, because everyone is watching every other investor as to how they are behaving is a more worrying part of the contagion and that sort of underlies my statement about the capital account controls which I talked about earlier. We don't fully understand the financial contagion. As I mentioned, there is abstruse work in finance trying to get to grips with it, but we are not at grips with it.

In the meantime, what you want is some relatively ham handed measures, like some minimal capital controls which you can use to suddenly bring into check a contagion which is spreading from one country to another. You do want that instrument to be there with the central bank and with the government.

Policy coordination. To clarify, the developed countries and emerging countries, the coordination. The coordination does not mean -- and I should have clarified on that -- that everybody is doing the same thing. So it is not that these 20 countries which will have say 10 industrialized countries, 5 emerging economies, 5 developing countries, large developing countries -- say Indonesia, India, Brazil -- you're not

going to say that all of them are going to tie to liquidity. You sit down like in a G-20 type forum and take a decision that, well, we feel that in this situation India can go in for an injection of liquidity of tightening of liquidity whereas the U.S. should behave in a different way. So there are different lines that you take. But if this comes out with a collective announcement, then immediately the speculation that countries are at war with one another, that is going to go out because it's a collective decision.

How do you take this collective decision? There is going to be a lot of arm-twisting, we know that. As soon as you sit in a room with the big and the powerful and the relatively weaker, there will be arm twisting, but it is choosing between two evils. Completely free flowing decisions being taken in different units in a world which is a strange world where the economies come together but there are lots of central banks -- we are getting this in another domain by the way, taxation. You are seeing sudden corporate races in terms of corporate taxation beginning to take place in the world. Tax havens being created. OECD has been writing about this, so you do need this even in the taxation domain. Once again, it does not mean that you are going to recommend the same policies for the rich and the poor countries, but it's a coordinated -- some semblance of a coordinated announcement will make a difference.

The labor injection, the liquidity that I'm talking about, it's not

that you do it only on the domestic sector. You do it within your country but that does not mean that it's not going to affect your trade sector, your import sector. It's going to indeed go across the board within your country.

MR. KIRISCI: Thank you, Dr. Basu.

Izak, I think we still have a little bit of time for another two questions really quickly and snappily.

MR. ATIYAS: It's coming. Don't forget to introduce yourself.

SPEAKER: (off mic)

MR. ATIYAS: We're not hearing the question.

SPEAKER: Hi, I'm an international student from Pakistan, and my question is how can Turkey's possible inclusion into the E.U. affect its economic performance? Is it still wise for it to be part of the E.U., keeping in mind E.U.'s economic crisis? Thank you.

MR. ATIYAS: Very good. This is a question we've been pondering about for some time.

MS. HAMM: Thank you. Rae Hamm. I'm a junior studying economics.

You have put a lot of emphasis on the need for global policy coordination and we have also talked about the E.U. having a problematic experience with implementing policy coordination. However, I would like

to ask how much the recent experience of the E.U. in responding to global crisis hindered the feasibility of having a policy coordination in the international level in the future?

MR. ATIYAS: Very good question.

Dr. Basu.

MR. BASU: Okay.

MR. KIRISCI: Thanks, Izak.

MR. BASU: Thank you very much. For the first question from the student from my neighboring country, Pakistan.

I hope your question had remained pantomime so that I hadn't heard it. Then I wouldn't have to answer it. The question about whether Turkey should join the E.U. or not. You know, I can't give you an answer on that because I really just don't know enough of the details on the ground but I can give you some of the logic that Turkey has to weigh in taking a decision of this kind. It is the following thing that has to be kept in mind.

Your trade channels open up hugely. That's a big benefit, but your exchange rate correction methods go down. You get great limitations on what you can do. There is a lot of new literature on fiscal devaluations but we know that there are limits to the fiscal devaluation. This is the big tradeoff that has to be weighed. Think of the East Asian

crisis 1997. The crisis was deep when it hit in 1997. Two years later the crisis was virtually over. Yes, it lingered on for a while in Indonesia but most countries pulled out. What happened during this time was massive exchange rate corrections, so deep crisis, huge exchange rate corrections, you pull out of this.

Once you are a part of a union, that correction method of course goes because you can't make that kind of an exchange rate correction anymore. But on the other hand there's an advantage of a marketing opening up and my instincts are always in terms of trade. The more open that you can be -- goods flowing easily from one region to another, one country to another -- is beneficial, but there is a tradeoff involved and I will leave this hard question for you to ponder about and take a decision on.

Rae Hamm, if I got your name right, again, you're right. Every setback in a major experiment, like the eurozone experiment -- I think of the eurozone experiment as the second biggest deliberate human experiment in terms of economic structures. The biggest deliberate experiment was the formation of the communist economy. The second biggest is the eurozone economy. I think the eurozone experiment is a move in the desirable direction, in the right direction, but with this huge experiment and the fault lines that showed up, this indeed is a setback for

future coordination, but here is what I would tell the policymakers at the helm. That, you know, we are lucky that this experiment took place and the fault lines showed up, and really some of these fault lines, as the borrowing chart of sovereign bonds demonstrated, that till 2008 we were blissfully unaware of the fault lines. Then comes the lemon crisis and we understand what the fault lines are. Next time when there is policy coordination going on you don't have to worry about those particular fault lines because we've understood that. So it is a huge experiment which has given us a level of understanding that we could never have got. So, in fact, instead of shying away from future policy coordination, if we are rational, if we have wisdom out of this, we will, in fact, now move boldly towards a few more steps in policy coordination because we've learned from the failures -- or not quite failures but the stumbling blocks that the eurozone hit upon.

MR. KIRISCI: I know this is not going to be very diplomatic but I feel a little bit let down with the answer you gave to our Pakistani friend. I thought you were going to say an unequivocal yes. Leave it at that.

We have a little more time for two questions. Yes, please.

MS. DARNELL: Hi, I'm Jane Darnell from the International Monetary Fund.

You drew a pretty grim outlook for developing economies. You mentioned that the crisis is going to continue and things won't be looking up for a while. You mentioned the hyper-connectivity. Given that advanced economies won't be doing very well, it's going to affect developing economies. And then Professor Izak mentioned the middle income trap and in the longer term, you know, given how we came to the high growth rates, it doesn't look very good that they'll continue.

Now, these are fundamentally two different ways of presenting the outlook. One is a bit more cyclical. The advanced economies aren't doing very well and that's why developing economies won't be either versus regardless of the crisis and regardless of the emerging markets the development model of developing economies was in a way inherently built to slow down. How do we square these two? Which one do you think weighs more?

MR. BASU: Let me clarify. Actually --

MR. KIRISCI: Can we take one more question?

MR. BASU: Sure. Please, go ahead.

MR. KIRISCI: Yes, please.

MR. SITILIDES: Thank you. John Sitilides with *Trilogy*

Advisors.

Sir, you opened your presentation with a discussion about

the fact that we live in a world marked by economic globalization and fragmented politics, and yet I hear in your remarks and those of many others in distinguished positions about the call for greater union -- fiscal union, currency union, banking union, and yet we also see around the world the strong preference of societies, of nation states, for sovereign democratic politics. And I ask you how do address this inherent tension between the call of the elite for more union and the call of people for sovereign democratic politics as a means of free expression? Thank you.

MR. KIRISCI: While I have you I have a question that I've been dying to ask. As I listen to Strobe Talbott and you two made references to the '60s, I did most of my learning in the '70s and at that time for the south a very grim picture used to be drawn. And the likelihood of the south playing a major role in the world economy was not being brought up. If anything, it was doomsday scenarios. What brought us here if a quick answer is possible?

MR. BASU: Thank you. Not a quick one but I'll try.

The first question from the IMF, just to clarify, I feel in terms of the description of the terrain ahead it's not that we are going to dip into a crisis. There was a fear I think the end of 2011, early 2012, that Europe was going to plunge into a crisis. That has abated. If you look at financial indicators in particular, yes, we have got an occasional sudden sharp

crisis like the Cyprus one happened and has abated for a while, but most financial indicators suggest that there is an improvement in terms of the financial risk which can come very quickly, very sharp. The real economy risks usually don't move as sharp. I am saying that what is a disappointing scenario is the growth seen in front of us. See, I was very hopeful that the U.S. was going to pull out very quickly.

What has got me a bit worried is one particular indicator which people don't pay too much attention to but to me actually it's extremely important, which is retail purchases by consumers and consumer confidence. There is this thing which gets tracked by Reuters and the University of Michigan on retailer confidence. Last year that was doing pretty well for the U.S. so I was hoping that this is going to begin to pull the U.S. out quicker but that confidence indicator has taken a dip over the last couple of months, which is a bit of a warning sign, and the employment, in particular the long-term employment is worrying. And in Europe, as I said, the injection of liquidity has bought itself time. It has caused the financial crisis risks to abate, but the growth scenario does remain grim. So the growth scenario is what remains grim.

Now, the connection between the industrialized world and the developing and the emerging world, I feel, and this is talking about the very long run, is there is a shift in tectonic plate taking place. In some

sense the driver of the global economy, that baton has been passed on from industrialized countries to emerging economies. When you have in a relay race, also when you see a baton actually being passed, there's a bit of a slowdown that takes place for both the person passing and the person picking it up. And that's the best analogy that I can give. So right now the entire world is being rocked and the slowdown in growth that you are seeing is not just in industrialized countries where it's zero, low negative or 0.3 in the U.K., so it's hovering around zero growth, but there's a slowdown everywhere. Brazil is down to 2 percent, less than 2 percent. India is down to around 5 percent. China is down to 7.7 percent, so it is down everywhere it's taking place.

But I feel we are going to come out of this not in the next two years but after that when we come out of it my expectation is we are going to see faster growth resume in the emerging economies. Which ones? I don't quite know, but there will be a bunch of emerging economies that will really become the drivers of global growth. The best scenario we can go back to, and I'm optimistic that we will go back to that, is that industrialized countries get back to a 2 percent growth per annum which for rich countries is if they can hold that stable with decent employment and emerging economies go back to again the kinds of growth that you were seeing -- 8 percent, 9 percent -- 7 to 9 percent growth for a couple of

powerful emerging economies, two or three years down the road I feel is a very, very possible scenario.

John, banking union and democracy.

MR. KIRISCI: Sovereign democracy.

MR. BASU: Sovereign democracy. This is a big question.

You know, we would always say, even in the older times of Washington consensus, that to a developing country you go and say, look, you people must vote. You people must choose your own policy. And here are the policies that you will choose. There's a contradiction in terms when you do that. We lived with that contradiction, and the currency union, the only way that I can talk to this is -- and I would face that actually in India because there would be civil society protests about some of these policies moves that yes, sitting in New Delhi you would go for. The best way to handle this where you try to keep it with a lively democracy is a continuous engagement with civil society.

One of the things that I did feel good about my own tenure in India is that I had lots of friends in civil society, activists in civil society, and to keep up that conversation so that after some time there is a bit of a joint voice that some of these global unions, they begin to appreciate the activists -- the grassroots activists that you need that. You can't do without that because of the transformation in the global world. That is

what you have to strive towards.

Kemal, your question on the south. Indeed, it's fascinating what happened, and it was really unthinkable. The '70s, yes, I was a student in the early '70s in London. The south was a depressed zone and no one was expecting the kind of rise that we saw. I feel actually over here two countries played a major role and then other countries joined in. The East Asian boom was already taking place by the '70s. Phenomenal growth in South Korea, as well was taking place. But the country that was completely dormant was India, so I feel India plays a major role.

China is interesting. If you look at China's growth pattern, we talk in terms of 1978-1980 being the break that China begins to grow very rapidly after that, but actually, if you study Chinese data carefully, it's not quite a dramatic break in terms of average growth. China was already growing fairly fast, even before 1978, but it was a tumultuous rise and fall that was taking place. So if you look at the period before 1978 in China, you will get a couple of years of 18 percent growth, 17 percent growth, the sort of growth you can't imagine in most big countries. But then you also get another year of minus 17 percent growth. The economy just crashes through. The totalitarian control did help that you could take the economy through this kind of rise and fall.

What changed in China after 1978, after 1980, is that you

don't get these fluctuations anymore. It's a steady growth around 10 percent per annum. Before that you were getting a growth of about 7 percent per annum in China, but that 7 percent was really a mean with huge fluctuation. So China changes from '78, '80, into a steadier growth.

India's was actually, I believe, the more unexpected story. Very few people were expecting this to happen in India. There were two things which happened, and it's a bit of instruction that we have to take off our ideological hat. People put on their ideological hats and then they try to explain everything with that. India's savings rate and savings and investment picked up in the, as I mentioned, early 1970s, and that happened for a very strange reason. Indira Gandhi nationalized India's banks in 1969. With that she passed a rule that these banks will have to open up branches in remote rural areas so that ordinary people can save money. And with this move, savings rate in India went down. Fortunately, India soon after that opened up the banking again. The nationalization was removed and private banks came in. So one fallout of Indira Gandhi's move -- very mixed move was the savings rate did go up. So there, you like that move or not? It did have that side effect. Luckily, the government of India was sensible enough after that to open up that sector so that played a role.

Then something else happened in 1991. The big reforms --

pro market reforms opened up India's economy, and by then one thing had happened. Overeducated and underemployed Indians were a pool that was waiting to be picked up. So people had come out of these IITs with unemployment. Those days, IITs were associated with unemployed. Overeducated unemployed youngsters. Silicon Valley takes off, and with the takeoff in Silicon Valley, India has already a catchment of people who could be tapped into and by mid-1994 India is growing at 7 percent per annum. This was just unthinkable. So when India joined the bandwagon of growth by 1994, a slight slowdown in 1997 and again a massive pickup in 2003, soon after that it goes into a 9 percent growth trajectory, the southern landscape is really beginning to change. And the big countries -- China first coming in, India, before that the East Asian countries -- changed the landscape in a way where I don't think it was really predictable. So what you saw in the '70s, what I saw in the '70s, I think I was with you viewing a similar view of the world which was a bleak view of the world which changed.

MR. KIRISCI: Well, I think on behalf of Izak I suspect and on behalf of them I'd like to say (speaking in foreign language), a grand thank you. And on behalf of us here, an even grander thank you. I think you have left us with lots of questions and comments to ponder on. And I suspect at Sabancı they will await for you for something greater than just a

passing meal at the campus. Would you agree with me?

MR. ATIYAS: Certainly.

MR. KIRISCI: Thank you. I think we're done.

(Applause)

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I, Carleton J. Anderson, III do hereby certify that the forgoing electronic file when originally transmitted was reduced to text at my direction; that said transcript is a true record of the proceedings therein referenced; that I am neither counsel for, related to, nor employed by any of the parties to the action in which these proceedings were taken; and, furthermore, that I am neither a relative or employee of any attorney or counsel employed by the parties hereto, nor financially or otherwise interested in the outcome of this action.

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