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RAGHURAM RAJAN:
HOW MARKETS AND THE STATE LEAVE THE COMMUNITY BEHIND

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P R O C E E D I N G S

MR. WESSEL: Good morning. I'm David Wessel. Welcome to the Hutchins Center on Fiscal and Monetary Policy here at Brookings. I'm kind of amazed that anybody's here given that your choices were staying home and watching Michael Cohen or watching Bob Lighthizer, who's testifying on U.S.-China at this time, our own Bill Gale is testifying at this moment on the tax cuts. And the only good thing about the Kim-Trump summit is that they're sleeping now, so we don't have to worry about that. (Laughter) So it's really remarkable.

I'm very pleased to welcome Raghu Rajan back to Brookings. Raghu's one of the most thoughtful economists I've encountered in my career. He was, of course, born in India, grew up around Asia because, as I understand it, his dad was in the Indian analog to the CIA.

He got originally his undergraduate degree in electrical engineering, but he came to his senses and got a Ph.D. from the Sloan School at MIT. He's been a professor off and on at the Booth School of Business at the University of Chicago since the early '90s, but in between he's been chief economist of the International Monetary Fund and the Central Bank governor in India.

Raghu has proven that if you're just right once in a high-profile place, you can live on that for almost the rest of your career. (Laughter) So when the Federal Reserve potentates gathered at Jackson Hole in 2005 to celebrate Alan Greenspan and how the great the world economy was and what a wonderful job they'd done convincing the rest of the world that they ought to adopt the American financial system, Raghu asked a question has financial development made the world riskier, his answer was yes. He got booed, shouted down. Larry Summers called him a Luddite. And it turned out he was right.

In 2010, he did a really interesting book which really made an impact on me called "Fault Lines." And one of the things that he pointed out was that when government and the elites in the United States were unable to deliver rising income, rising wages to lots

of people, one easy answer was help them borrow a lot of money. And that's one way why there was so much political support, he argues, for doing things like making mortgages to people who had no prayer of ever paying them back because it was a way to compensate for the fact that their incomes weren't rising.

So Raghu's new book, which comes out -- is it today, Raghu?

MR. RAJAN: Yesterday.

MR. WESSEL: Yesterday, "The Third Pillar: How the Markets and the State Leave the Community Behind," is a very broad, you might almost say sprawling book that I think does lots of things. On one hand, it's a fascinating, easy-to-read economic history of the world going back to ancient times, the Old Testament and beyond, about how the world changed. But it's also in a way Raghu's argument is to why we've seen the rise of populism and what needs to happen to respond to that. And one of his bottom lines is we shouldn't overthrow capitalism, we should improve it, as you'll hear.

So our plan now is Raghu's going to speak from the podium for a while. I'll join him on stage and ask him a few questions and then we'll turn to you. And if Trump is impeached before it's over, we'll put a news flash so nobody has to feel like they've missed the headlines. (Laughter)

MR. RAJAN: Thank you very much, David. It's a pleasure to be back at Brookings. And to some extent this book is my take on why capitalism worked and why it's not working so well today. So that's why the history and I'll show you one draft which encapsulates the entire history, one chart which encapsulates that in just a minute.

Let me start first with these are three covers. The left cover is the UK edition, the center cover is the U.S. edition which you have, some of you, and the right cover is the India edition. And it's interesting that all three have a different take on what the title means. The UK has this graphic. The U.S. is much more sort of down to earth.

In fact, there were two aces and a deuce. We converted it to the king reflecting the state and the jack reflecting commerce and the deuce reflecting the community

at the bottom. And, of course, the third is -- that squiggly thing on the left is actually people holding hands. That's Warli art from the Warli tribal community in Maharashtra. So different takes.

What this book is about is the standard view of capitalism is essentially about free competitive markets. And if you're from Chicago, that's all you need. (Laughter) If you're not from Chicago, you say, well, we also need a government, not just to enforce contracts and property rights, but also to do some other things. But essentially this has been the view of capitalism, the back-and-forth between how much government, how much markets.

And I believe this neglects the third pillar, which has been essential to the success of capitalism, which is the community directly. Directly in the sense of preparing people for capitalism, for entering the markets, as also accepting them when the market ejects to provide a kind of safety net. The community is very important. That's the direct effect.

And the indirect effect, by allowing for people to organize and becoming a fundamental sort of point through which democracy expresses itself, I think these aspects of the community make it central to why capitalism works for many and, in turn, why capitalism is sustainable because many support capitalism. I would argue that the post-war structure that was so successful in Western countries, the liberal market democracy, reflects this interplay between the community, the state, and markets, and not just the state and markets alone.

Now, what I argue is that social change happens every so often in a very big way, typically affected by either deep calamity or technological change, and we're in the midst of yet another huge technological event, which has affected some communities very adversely. And of course, we see today around us capitalism is under attack, whether it's from the populists of the right or the populists of the left. And of course, we see even in this country, the bastion of free market capitalism according to some, a lot of talk which is anti-

rich, anti-trade, anti-immigration.

Now, one of the things I will come to, and this is the last point in the outline, that many of the answers to the problems we face today are not at the national level and that if we try and solve it at the national level, we're missing the varied problems that different communities have. And many of the answers lie in fortifying the community at the local level. And of course, the communities that are adversely affected were also communities which are struggling to adapt to the technological change that is affecting us, so decentralized, what I call inclusive localism. I'll come to that a little later.

So here are the three pillars just to get definitions straight because people sometimes get confused about what you mean by different things. Markets, of course, the goods markets, labor markets, capital markets, all that stuff, but also including firms, the private sector. And the function of markets, as is well known, I mean, many functions, but let's focus on productivity, enhancing productivity, and expanding choice for people.

The state consists of the usual triad -- the executive, the judiciary, the legislative -- but typically I'm thinking of this at the central -- at the federal level: provides security and justice. And also, in this day and age, provides you premarket support, builds your capability: schooling, education. That's part of what the state provides in many countries, and often post-market support, a safety net if you fall off, whether it's unemployment insurance, whether it's health insurance, or whether it's Social Security.

And finally, the community. And here I'm very specific in this book about focusing on the proximate community, the people around you, the neighborhood, the village, the municipality, and typically including local government as well as local institutions, like schools. So that's definitions for you just to say that we're on the same page.

Now, why is the community important today? I mean, I get emails from my colleagues saying, you know, I've never seen a person the last few weeks. I'm happy to work off the Internet and I don't need to see people. Well, the community still has a very important role. It is a source of identity and values even today.

Of course, it complements the state by helping security. I mean, just think about Neighborhood Watches in your communities. Sometimes in a more primitive, but also in close-knit communities, justice, punishment for transgression by ostracism, for example, enhances your capabilities. The community still in many places teaches you very young, before you go to school, but sometimes also the school is an integral part of the communities where you learn, community colleges sometimes in some localities.

And, of course, safety net. Even though the government provides a safety net, when that dries up, when that breaks down, it's people getting together collecting clothes for the less well-off, collecting food when there's a recession for the people who don't have it. That still happens again in India, where we don't have a lot of social security. When workers get fired, they go back to the village because they know what they have at home in the village. And that's true across a number of countries.

What the community does differently from the government, remember those four things are exactly what the government also does, what the community does differently from the government is it works on relationships, not some kind of an explicit contract with the state. It's because of who you know and who you are that you get that support, not because of what you're worth or what you're capable of. It fills holes.

And to that extent, it's a very important addendum even in this modern age. Earlier, of course, it used to be the entirety. The entirety of social security used to be a community. There was no official Social Security from the government. Today it fills in the holes.

And finally and perhaps an important facet of the community is political; that it is the way -- it's the easiest way to organize. After all, remember, President Obama was a community organizer. That was his first step into, in a sense, politics.

Now, the need for community means that even today, even in developed countries, we constantly find ways of building community as the old ways erode. So when we moved from -- when you're in India, what is the community? It's the apartment building

you live in, everybody running in and out of each other's houses. That's sort of the community in a city.

Here it happens less. Where do people interact, for example, in Hyde Park, is through the school because parents meet each other, then start going to each other's houses. That's the form in which we -- so there are constantly ways we build social engagement. It seems to matter even in this day and age.

So why do I talk about local community? I'm still at just trying to explain the notion of community. Why not virtual communities? After all, we have easy ways of engagement. And I emphasize local community, much easier to build trust, much easier to have longer term, deeper engagement. With the virtual community you can build light engagement with a lot of people, but you can also back off very quickly.

And the notion of who you are is becoming less and less clear as you communicate. You can be somebody very different from your online personality. I think there still is a role for the real person.

Interestingly, the two combine. And in the book I talk about this community, a Toronto development called Netville, which does the ideal experiment that economists want. The developer connected half the community and for technical reasons couldn't connect the other half on the Internet. So half the community had Internet facilities -- this was in the early 2000s -- the other half didn't. And the developer basically said I can't connect the rest.

And one enterprising sociologist went in to study how social networks built up. And what he discovered was in the place that had Internet they actually built much stronger social ties. You would think the opposite, right? In this day and age, people spend time -- don't spend time with each other. It turned out the Internet is a very good device for crossing closed doors; that you can arrange to have a neighborhood party, you can arrange to search for a neighborhood dog which is missing. All that can be done much more easily. You can traverse closed doors.

And so in that sense, I think it's not that the virtual community crowds out the real community. It may actually add on. My children keep in much closer touch with their friends through Facebook, et cetera, than we could in the past when we were relying on the phone.

And finally, the reason I focus on the real proximate community is I think going forward the problem of loneliness will become increasingly important in country after country. And the real community will be, in many ways, the solution to that; will create the kinds of even jobs that address that. So that's why I emphasize the real community.

And finally, there is a -- you know, why don't I talk about imagined communities, in Anderson's wonderful words, like nation. In a sense the book says we should deemphasize some of these imagined communities. And I would argue that the reason for that is as these direct communities break down, we need something to temper passion. And passion gets elevated when it becomes engaged by grand ideals without the tempering at the local level. And I'll come back to that in a bit.

So here is the entire book in one diagram or at least my entire view of why capitalism works in one diagram. So we have the state, markets, and the community. And what I argue is the blue lines are what we've always known and talked about. Right? The state providing legislation, regulation, antitrust property rights, and that is how it regulates markets, how it regulates the community's security, justice capabilities, safety net, all that it gives to the people at large. But there are other connections that we miss.

For example, I mean, the markets also is pretty clear. Markets provides productivity and choice. But the community goes back into markets by giving the markets a sense of what to value and the norms that the market should follow. And in the book I trace out how once upon a time, what today is exalted in the markets -- shareholder value maximization -- was actually the sin of avarice in medieval times. We have changed a lot. Now we actually say go be greedy, for good reason and, of course, there are reasons why that makes sense. But it is very different from you should not charge a price other than the

just price, which was the medieval admonition. So values and norms go back from the community and markets.

The key different aspects that I want to emphasize are that the markets themselves, when they're competitive, constrain the state. An independent private sector acts as a check and balance on the state. That's an important facet that I emphasize in the book and that's why I think it's very hard to not -- to have authoritarian capitalism. It's much easier to have democratic capitalism because there is, in a sense, daylight between the state and the private sector. That's a big part of what the book emphasizes.

And the second aspect is that what makes it possible to create daylight between the state and the private sector is the democratic community, which pushes for open access, which prevents the state from coalescing with the private sector into crony capitalism. That is the biggest danger that most capitalist economies face. It's a danger that is ever present in emerging markets. It's something that a number of industrial economies have gotten away from. I don't think they get away permanently, but they certainly have gotten away. And I think it's very important to think of the role of democracy there; the role of various populist movements, for example, in the United States in pushing for strong antitrust, stronger regulation to separate the private sector from markets.

So that's sort of the basic picture I want to talk about. And I want to say what happens when we perturb it. What causes the perturbations? What causes us to move away from the liberal democratic balance that we have? Basically, serious calamity. The Black Death, as some of you who have studied history know, had a major change on social structures in Europe, including some would argue the demise of feudalism. The Great Depressions: 1873 to 1893, that was the first Great Depression; the second Great Depression, 1929 to 1939, again, had an enormous impact.

The one I want to talk about, however, today is the technological revolution, which has been with us largely since 1970. One of the bigger problems with this technological revolution is that its disruptive effects have come before its productive effects.

And, therefore, we have to deal with some of these disruptive effects before we get the growth to paper over some of the problems.

So here are three ways it has changed. It has changed the markets. First because it has facilitated trade. We all know about the fact that we now can have global supply chains with products being manufactured where it is most efficient to manufacture. That's different from in the past when because industrial countries had R&D, because they had marketing finance, everything, here manufacturing also benefited from that by being localized here.

Once it became possible to create these global supply chains that you could monitor using ICT technology, that you could send goods very cheaply across through container technology. Essentially manufacturing could move abroad. You could get just-in-time manufacturing. You move goods back and forth across borders. And that has certainly hit manufacturing hubs in industrial countries because the worker is no longer protected by the add-ons of services which earlier held the industry within country. That's one aspect.

But many economists would argue that a bigger aspect of technology on jobs is not so much through trade and job losses, but through automation and job losses. And certainly, we've seen that automation creating job losses at the middle, more jobs at the extremes, really low-skill jobs as well as high-skill jobs. But you also have seen the rise, the domination of industries by superstar firms, which have scaled economies through those global supply chains, but also can manage really big operations through the increased span of control that technology gives them; but also the fact that certain kinds of property which weren't protected as well earlier are protected much more strongly today, like intellectual property.

Finally, effects of technology on markets is the rise of superstar jobs. The lady on the left is Elizabeth Billington, who was a star of the London Opera in 1801. She earned the princely sum of in today's money 1 million pounds. She was the highest paid sort of artist at that time. And she was a superstar at that time. But because she sang only

in the London Opera House, the amount she earned was limited. So I'm talking \$1 million in today's money, but it was at that time about 15,000 pounds.

The lady on the right, anybody? Taylor Swift, right? Taylor Swift earned \$170 million. That's 170 times in today's money what Elizabeth Billington earned. And why? Because she has 3-1/2 billion hits for her song on the Internet. She addresses an audience much bigger than Elizabeth Billington did.

The broader point is we have superstar professions now and, therefore, rising incomes in those areas. And that does essentially increase the incentives to get the kinds of skills that get you into those areas. It's not just artists. It's lawyers, it's doctors. There is a superstar nature about a variety of professions.

So first, the previous slide was the ICT revolution changing markets. The ICT revolution has changed the state. And one of the themes in the book is that markets and the state go together. As markets grow, as they integrate, the state follows. Right? And, you know, there's back-and-forth because when the state creates a bigger environment in which it maintains security, the market expands into that environment. So they actually grow together rather than are opposed as most common sort of dialogues go.

As markets have become more integrated, governance powers have migrated up, partly because the state sometimes provides against volatility of markets. If markets grow bigger, the state has to grow bigger to absorb that kind of volatility, that's one. But also governance matters and the state grows bigger to provide that governance.

Example: bank capital, which some of you are familiar with. Bank capital used to actually be determined city by city in the United States. There were norms for different cities based on their population. Then it became, well, we need a statewide regulation on bank capital. This is how much any bank in the States should have. And then it became a national level of bank capital. And of course, today, bank capital is largely determined in Basel. Ostensibly, countries have a say on that, but ultimately, it comes down from the international arena.

So in a sense, the governance of bank capital has moved from the bottom to the top over time. And that's consistent with the fact that markets for banks have grown from local to regional to national to international. And, therefore, the governance has moved. So that's the second point I want to make, the ICT revolution has changed the state.

And the third is the ICT revolution has disrupted the community. First the effects of trade have been very differentially felt. The effects of technology have been differentially felt. Clearly, if you're living in a rural, semi-urban area in France today, you're one of the *gilets jaunes* protesting on the street because you have been left behind. If, on the other hand, you're in Paris or you're in New York or you're in San Francisco, even Washington, you're doing very well because the coastal areas, the big towns have essentially benefited from the technology revolution. So very differential effect.

Technological change has also increased the returns to capabilities. That was what we just saw, superstar professions, superstar firms. Which then increases the importance of good schooling, increases the importance of a college premium. And I would argue that this market-led increase in the demands of education essentially has led to a disintegration of the mixed community. You can thirdly see it in the numbers in the United States.

And I would say it starts with the question where do I get the best schooling for my kids? Certainly I want my kid to have good early childhood preparation. That means I'm going to do everything I can within the family to do it. But when that kid goes to school the preparation of that kid's classmates also matters. Do they come from families that have prepared them well? And if everybody's well prepared, the class moves up very well. It's a strong class, they all learn.

So what this does is give a great incentive to sort. I don't want to be in a community where other parents don't prepare their kids very well because my kid will suffer when he goes to school. Let me move to a better community where preparation is much stronger, where, in fact, my kid will have the best chance of success. So if I'm a parent, I

move to the community, the best community that I can afford because that's where my kids will get the best education that they need to compete in the superstar economy.

So in a sense, I call it the secession of the successful. Mixed communities are breaking down because of the demands of the market. We are separating into successful communities and not so successful communities. You can see it in the data. Much of the transformation is driven primarily by parents with kids who want to move to where their kids can have the best school.

And that creates a problem because the people left behind don't have the same opportunities, the same chance of success as the people who have moved into neighborhoods of their own. And we can't follow them because zoning laws keep the relatively poor and relatively well-to-do out. And that's sort of one of the problems that the book talks about.

What the consequence of this is a feeling of powerlessness translates into anger against the elite. They corner economic opportunity. They don't let us have access to the same capability, building institutions. If I go to a school which is relatively weak, I have no capability of going to college or even if I get into college, finishing it in finite time without incurring an enormous amount of debt.

So these create impediments to capability building, but also, as I document in the book and I'm not going to go into that now, we've also in a sense limited the kind of professions they can go into, the kind of enterprises they can open. Opportunity has also closed down as some of these large firms dominate the economy.

And, of course, the elite also have their own favorites. They have the favorites as immigrants. They have the favorites as minorities. They create all sorts of structures for them at the expense of me, the long-suffering. And there is some merit, of course, in the many books we've seen post Great Recession in describing this kind of feeling.

So there are anti-elite populist movements. Populist nationalism says we

really need to think about the majority group and why it's suffering. And the reason it's suffering is not because we need to upgrade capabilities, et cetera, because we've been hit by this enormous technological revolution. It's because we're favoring other groups. And let's favor them less; even the playing field. Whether it's favoring the outsider, the foreigner through trade, or the minorities or the immigrants, once we level the playing field, it'll all be honky-dory. The problem is it's not likely to be honky-dory because technology has increased the demands from people in terms of capabilities.

The populism of the left, of course they talk about opportunity, but they also talk very loudly about redistribution. And what you see in this kind of environment is the community can lash out against what seems like a no-brainer opportunity. Think of Amazon being rejected by Long Island City, Queens.

Now, everybody thinks, you know, at the face of it this is wonderful: 25,000 good jobs, average pay \$150,000 going to this area. Why would they be crazy enough to reject it? Well, they're crazy enough to reject it if they feel they would not benefit at all for the most part. Twenty-five thousand jobs that I can't get because I don't have that kind of education to work in Amazon. I don't have that kind of capability.

They're going to increase rents in my neighborhood. How does that help me? You know, there may be a few jobs here and there that are created, but my schools, I mean, they're going to create schools of their own. My kids won't be able to go in. And whatever good kids are in my school, in my public school, are going to leave to go to their schools. We're going to have the division again created with community. Do I really want that?

So what I'm arguing is what seems like a no-brainer from the center, many more jobs, what seems like a no-brainer from the state government, we're going to give \$3 billion in tax benefits, doesn't seem so much like a no-brainer right down there when you're confronted with some of the constraints that people feel.

So the problem, however, is that the answers people provide to the situation

are not going to help. How does leveling the playing field, reducing some of the privileges other communities have, barriers to trade help us deal with technological change, which is coming regardless of what barriers you put to trade? So in that sense, that's going to happen.

Population aging and high unfunded entitlements mean that almost every industrial country has to focus on how it is going to have immigration rather than how it's going to stop immigration. You need people to pay their taxes down the line. We need that because there's nobody else waiting to pay the taxes. In the U.S., we're in a much better situation because we had immigration in the past, because we have a relatively young population. Think about Germany. Think about Japan. They are now dealing with the problem that, in fact, they need somebody to pay the bills and they don't have those people. They have to start thinking about it in much more effective ways.

Of course, there's the growth of the rest. We're trying to erect trade barriers at a time when because of aging demand is slowing in industrial countries. Why would we do that? The demand is going to be in the rest of the world. That's where growth is going to be. If you erect barriers today, what are they going to do to your goods down the line when you want to sell it to them because demand is there? You need your factories to keep going to fulfill that demand.

And finally, we have global problems, like climate change. I don't need to talk to this audience and tell you how important it is that we have a global dialogue on it. I met a number of students from SAIS before this talk, many of whom were focusing on this very issue. So these are all reasons why we can't afford a populist, nationalist take on this.

I think what needs to happen, and I'm going to very quickly go through the solution part, essentially we need in -- for countries that are already diverse, we need a nationalism which is a means of integrating diverse communities rather than dividing them, but also accepting the fact that there might be ethnically concentrated communities within the country, also. We have to revive the communities that are failing, primarily by increasing

economic activity, but economic activity that they choose to have, not what we think they should have. So more bottom-up focused to improve their own security capabilities and safety net. I talk about the community of Pilsen, which I'll come back to, which has done some of this locally in Chicago to try and rebuild a sense of identity, political engagement, and security.

Now, all this involves trade-offs. There are no pure solutions. So some people come to this book thinking I'm going to talk about community and the community's going to be a solution to everything. No more state, no more markets. We're going to locate it in Montana, far from everywhere else. And it's going to be wonderful. We'll have free choice of everything we want.

That's not what I'm about. I'm about how we get the community for the world of tomorrow, an engaged community, a community which works to restore the kind of system that we had, but while having opportunity broadly for all in the face of technological change.

So a number of elements of this balance. I think it's important we push power back. Power has migrated to the international level. And to some extent, some of the resentment, the resentment, for example, in Europe against the European Union, comes from the sense of we don't have any powers. It's all migrated up. We need to push powers back from the international to the national to the regional to the community to the extent we can. This is the Europeans call it the principle of subsidiarity.

It's more observed in the breach. We should actually observe it. Push powers back to the lowest level where it needs to be so that people have a sense of agency, communities have a sense of agency that also brings the community together and makes it a more effective organization.

At the national level I would argue, therefore, we need to restore sovereignty over some matters that have been taken away, but it has to be a responsible kind of sovereignty. It has to be, yes, you get to decide, but keep in mind the larger interests

of the globe on occasion when you think about this.

At the national level a kind of civic nationalism open national markets that integrate the communities together. And finally, at the community, localism; more power locally, but not those old communities entrenched, parochial, sort of intolerant communities that we sometimes envision in the past, but communities with relatively low walls. A lot of flows back and forth across the community border that engage communities. That's what I think is important.

So the words I use is "inclusive localism," seems like a contradiction in terms, but it's as much of a contradiction as competition and property rights. Both are essential for capitalism. "Property rights" means very much keeping people out of my property. "Competition" means a free entry into the competitive arena. I think both are important for capitalism. Similarly, localism is important, more power in the community, but it has to be an open community, which is the inclusive part.

So we need for this at least five things, community leadership, local powers to foster engagement. In this day of technology, and one of the themes in the book is how technology can be used to do things differently than in the past, you can get engagement from the bottom up. For example, in Chicago, when we see a pothole there's an app called SeeClickFix. You click, here's the location of the pothole, and the authorities are supposed to tell you when they fix it. So there is -- I mean, do they work as efficiently as one would want? Probably not, but at least there is some opportunity to have control over them.

And similarly, engagement of the community in other ways, in Pilsen, one of the communities I talk about in the book, how when there is crime, people in Pilsen, which was a very crime-ridden neighborhood, used to come out and swarm the streets so that essentially they crowded out the crime. There was no possibility for the criminal to be more -- to do more. These are the ways the community can engage.

But the community can also monitor their officials far more effectively. But the government can also monitor local officials likely through the use of technology. What

funds have you sent? How have they been spent? Has there been wastage? If so, if there's grand wastage, can we intervene?

Infrastructure, there are so many communities in the United States today which don't have broadband. I mean, that in this day and age is like almost a fundamental right. If you need economic access, you have to have broadband. And so, I mean, there are many things we can do in fixing infrastructure and connecting communities up and bringing economic activity.

And finally, more funding should be decentralized. Let the community have the powers to decide, but also be able to put some money to work on that, so that they can build whatever they need to improve their lot. Some of them may want to build more capabilities, better community colleges, better schools. Some of them may want, you know, a different kind of tool shop, so that small entrepreneurs can create economic activity.

The second part of inclusive localism is inclusive. The state and markets are important here. They should keep the walls around communities relatively low. So I say more part of the community, this is where the trade-off comes. You can't let the community build a wall around it. So the kind of zoning, the exclusionary zoning that we have, is something that is worth reexamining. Yes, it gets the community more of a sense of identity, but it does keep out people from coming in, especially relatively poor people, and leads to the kind of segregation that in the long run is detrimental for the country.

So that's where a trade-off comes. Prefer low walls, prefer more inclusion here, rather than localism. Is that a contradiction? No. We make trade-offs all the time. We make trade-offs in capitalism. We have to make trade-offs here so that we get the best of both worlds. We get the local part, but we also get inclusion.

And technology, as I said, can help with new solutions, monitoring local officials from the top and bottom, teaching students at different levels. One of the biggest concerns in some of these schools is, as I said, kids coming with different levels of preparation. Increasingly, technology can address that. Because we don't subject the kids

in school to the same lecture, they go and study the material at home. Come to school and get help with different problems at different levels targeted at each student. That sort of breaks the need, which has been there since the time of Aristotle, that we have to teach the average in the class or teach to the top or teach to the bottom, each of which leaves some kids either bored or clueless. And with new technology we can address that.

So the broader point in this book is technology's part of the problem, but technology's also part of the solution. Enlisting technology as part of the community can actually create useful infrastructures, new forms of engagement, and new answers to the problems that we have. And I'm very hopeful that we can address it. I think we need to. I think going the direction that we're going is completely senseless. But we have the capacity to do it.

And I'll just leave you with this quote from Chinua Achebe. (Applause)

MR. WESSEL: It's kind of hard to know where to begin. There are some seats down here if the people who are standing in the back want to come. I won't call on you. There's a number on that side of the room.

So I think that I want to ask you a couple questions about your diagnosis, several questions about your solutions to make sure I understand the trade-off well. And then I thought I'd take advantage of your being here to ask you about a couple of current events before we turn to the audience.

Let me start with the diagnosis. So how is it that the -- what is the relationship between the breakdown of the community and these social structures and the kind of rise of populism we see here and in Europe and other places? What was the relationship between that -- what's the causal relationship?

MR. RAJAN: Well, I would argue, and I'm certainly not the first to talk about this, Hannah Arendt, for example, has written about this, that once the local community starts breaking down, once economic activity disappears -- I talk in the book about how it disappeared first in the black communities in the U.S., and people said why is there social

breakdown? Why are there teenage pregnancies? Why are families breaking?

That exact same phenomenon is now found in the white communities in some of these semi-rural areas, where, again, economic activity has disappeared. The man is less worth marrying because he doesn't have a job or a stable sort of occupation. And, therefore, the stable structure breaks down.

Once that stable structure breaks down, the sense of identity in the community, do I really want to be associated with more of a dysfunctional community which is more known for social dysfunctionality than for being a healthy community, and then I'm looking for other sources of identity. One of these sources of identity that appeals at times like this is a national identity. You are part of this grand tradition. Why don't we make thus and such country great again?

And it's you. It's a very broad definition of who belongs, but there have to be people outside because there has to be somebody who you are opposed to, to show that you are included. So the opposed are usually immigrants, minorities. Those are the guys who don't belong. And we find this broad trait that makes you part of the included.

MR. WESSEL: All right. So in that chain it starts with some kind of economic shock.

MR. RAJAN: I would argue it starts with economic shock. Now, of course, overlaid on that are issues of status and so on. We start slipping as you fall down economically. And so you say, well, I used to be so up in the world and now I'm no different from these other people. Why is that I'm no different? Well, it's not because of me. It's because these other people are favored.

MR. WESSEL: And what's the role of culture in the family in this chain?

MR. RAJAN: Well, there's some of it. I mean, I think there's this very nice book by Ross Douthat and Reihan Salam which talked about the fact that when you're losing your control over the strong family, even though it's breaking down, even though the divorce rate is up, even though there are teenage pregnancies, you still hold on to some of these

cultural sort of icons because that's all you have left. You're slipping and you're sort of grabbing on to them. You hold onto them more strongly than perhaps people in the cities who have higher incomes and, therefore, are able to have more stable sort of structures. It looks like it's hypocritical, but it's an attempt to survive.

MR. WESSEL: Hold on to something. So I'm trying to understand where you draw the line, what things we really do have to do at the national and global level and what things can be delegated to the community.

So climate change is obviously one that seems to be a global thing requires. In the book I think you kind of advocate health insurance to be universal. Right?

MR. RAJAN: But not necessarily single payer. Whichever way you want to structure it, people should have basic health insurance in a country that can afford it.

MR. WESSEL: Right. And you were suggesting in your remarks that somehow we ought to have -- every community ought to have broadband, which presumes that somebody -- and so what are the other things that you think we have to do at the national level? Then we can talk about which ones you want to send back.

MR. RAJAN: At the national level, clearly, you know, keeping the markets relatively open across communities, having a sense of what the laws are that will prevent discrimination and enforcing those kinds of laws, that would be quite important. Infrastructure, again, not necessarily the state providing it, but ensuring that there is infrastructure whether privately provided or state provided. People take it as a right that they have road out of their village. They should also take it as a right that they have broadband and access to broadband.

MR. WESSEL: Okay. And standards for K through 12 education?

MR. RAJAN: Some standards may be necessary. What you can do is allow a lot of flexibility for the locality to figure out what else they want wired. And you have to be a little tolerant of what people want. Clearly, some people in a more religious community will want more religion in there to the extent that passes muster in a country with

the national laws. France doesn't allow it, but some other countries allow it. And they may want more learning about local history, local culture. That's fine provided these basic standards are met.

So my sense is people will find ways to, in a sense, prepare their kids better for the kinds of needs that they have as they have more control. Often we think what do they know? How can they determine it? That's a very, I think, high-on professional feeling we, the professional educators, know. What do those local parents know? I think you can give them guidance, but let them figure out what they want.

MR. WESSEL: Okay. So in the book you nicely state a question that occurred to me as I read this about this notion that we're going to decentralize. We're going to let people choose where they want to live. We're going to sing a lot of songs about why can't we all get along, so anybody can move into any community. You can't bar somebody. But on the other hand, you see some value in people being able to choose to live with people who share their values. Right?

And you say in the book, correctly, "This does raise the specter of a country dotted with segregated communities, each with its own race, national origin, cultural traditions, and totally barred to outsiders. We must make sure this is not the default outcome, not by forcing people to mix, but by emphasizing, if necessary through laws, that in the nation all communities are open to the flows of people, goods, services, capital, ideas, both in and out. Some communities will be thoroughly mixed, especially the cosmopolitan cities, because of the myriad advantages of mixing. At the same time, many neighborhoods or even within cities will be more representative of a certain religion or national origin simply based on the choices of who moves in or out without any overt discrimination."

So that strikes me as you're really threading the needle here. Right? So I don't quite understand how we avoid an archipelago of segregated communities where we can say that there's a law that says you don't sell to -- you can't forbid black people from moving in, but you basically make them feel unwelcome; where there's a cross on every

street post, so Muslims and Jews think, well, we're not welcome here. I don't quite understand how this tension is resolved.

MR. RAJAN: Right. So, again, the question is how much the laws protect your sense of openness while allowing you to choose where you want to go. On the cross on every corner, there could be and there are in some countries certain rules on religious observation and where it can be placed. I don't want to an excessively intrusive government, also, on everything. I think common decency sometimes deals with these problems.

I think what I have in mind is a sense of some neighborhoods that we see in every American city. You know, one neighborhood, the Pilsen neighborhood, one side is Hispanic-American, the other side is African-American. Do they cross? Yes, they do cross. Are there marriages across the street? Yes, there are marriages across the street. But they largely live together.

Over time, they start mingling. So now, for example, as Pilsen is getting richer, there is some gentrification. A number of whites are moving in, but it is still predominantly a Mexican-American community with a Museum of Mexican-American History. But it celebrates common festivals, like July 4th.

I think for the moment that is often, you know, as much as we can expect. Over time, mixing will increase and then we won't have the problem as much because the sense will be the culture we want to propagate is really the more mixed culture. I think that's a matter of time. I think today there are many communities that used to be separate, take Italian-American, take Irish-American. They are now fully integrated into the mainstream. It's a matter of time. You just have to make sure that nobody kills each other while we're getting there.

MR. WESSEL: Is that a local phenomenon or a national? (Laughter) So give me -- I admit there's some skepticism, but okay.

MR. RAJAN: What is the addition, I'm suggesting, to what we already

have?

MR. WESSEL: Yes, yeah.

MR. RAJAN: I'm suggesting give that neighborhood a greater sense of empowerment. Let it do more things that it currently is.

MR. WESSEL: Give me an example of something that you think --

MR. RAJAN: Schools. For example, schools.

MR. WESSEL: The schools in the U.S. are incredibly decentralized, right? We have local school boards. We have districts that are about the size of this room.

MR. RAJAN: We have bureaucratized a lot. There is the ability to intervene. Actually it depends, also, on which community you are in. Some communities you have more ability to intervene. Other communities you have much less. The poorer communities you have much less ability to say here is what we want and here is how we want to do it.

But more than that, also, issues like funding. Can we get that? Do I have to get permission all the way up to the state capital or national capital in order to improve this particular aspect of my community? I think more sort of pushing down is important.

On the segregation, I think we really do have to take a serious look at zoning in this country and the ability to keep out, you know, multifamily homes from certain communities because poorer people come into those homes.

MR. WESSEL: So you can teach -- I'm going to give you more freedom to teach what you want in your schools, but you're not going to be able to forbid apartment houses in your city because that keeps people moving.

MR. RAJAN: So that's why I said trade-offs. We can't have, you know, you're completely free, then you get to the segregated community.

MR. WESSEL: Right.

MR. RAJAN: And you don't benefit from the national market, from the variety of people, and you get anger as the rich communities keep out the poor communities,

inequality increases. So, again, we need to figure out how to manage these trade-offs.

And when people look at trade-offs, they say this is not pure. This is not pristine. You're confused. No, you're not confused. The real world is full of trade-offs.

That's the nature of the beast.

MR. WESSEL: Right. I'm just trying to get the terms of the trade-off clear.

MR. RAJAN: Yeah, yeah.

MR. WESSEL: So let me ask you about the role of different segments. What's their responsibility here? And I'm particularly interested for the moment in what's the role of big corporations?

I think you make a distinction in the book that is worth talking about, about you suggest that profligate maximization may have gone a little bit too far and you talk about the concept of value maximization. So if this were a room of Fortune 500 CEOs, what would you tell them they ought to be doing differently than they're doing now?

MR. RAJAN: Actually I would tell them many of them are doing what I suggest they could be doing, except they don't talk about it that way. And this, I think, is shooting themselves in the foot.

Milton Friedman talked about the only job of a corporation is to maximize profits. And he said that at a time when corporations were asked to hold prices because inflation was high. It was their national duty to keep prices low. And of course, to a person from Chicago, that's waving a red rag in front of them. You're trying to intervene in prices? They're supposed to tell you where, in fact, you should be producing. You're eliminating the price signal by fixing prices.

But more than that, Friedman believed that all this corporate social responsibility was being proposed by activists through the back door for what they couldn't get through the front door through Congress, here are things corporations should do. I think those are reasonable arguments to think about.

Where I think he went wrong was in saying the primary duty of the

corporation is to maximize shareholder value. And the reason he said that was, if you think about it theoretically, shareholders are the residual claim. Everybody else has fixed claims, like the debtholders, like the workers. They get paid a wage, which is fixed. And, therefore, if you're maximizing the residual, you're maximizing the whole. So from society's perspective that was the right thing in his view.

The reality, however, is that shareholders are not the only residual claimant. I as a worker, if I have strong skills and I'm not a commodity, I'm not commodity labor, I become a partner in the enterprise. I get some share of the future profits. So I become effectively a stakeholder in the firm. And if as manager of the firm I have to maximize the value for the whole, you have to take the interest of long-term workers who are stakeholders also into account. You can't just say shareholders. If you fire the workers when, in fact, retaining them would be better for the whole than firing them, perhaps that's the right decision to make for the whole.

And maximizing the whole actually maximizes the value of the shareholders, also. So it's not contrary to what they do.

So to your first point, what is it that I would tell them to do differently? I would tell them to think about the broader perspective, not necessarily about how I'm going to sort of do good for society or so on, but how I'm going to do good for the corporation and the stakeholders in the corporation. Focus the corporation on what it's supposed to do -- efficiency, choice -- but you can do that by taking a broader view. And that, I think, would sell much better.

Today a lot of people are worried that in the interests of shareholders you're sacrificing the interests of others who make investments in the firm, like the workers. And I think there is a case to be made that their investments are as important as the investment shareholders make. They also ought to be protected. Occasionally there will be a reason to fire workers because it's better for the whole.

MR. WESSEL: And as I read the book and as you've discussed, you don't

expect the leaders of the corporations to shy away from the worst of crony capitalism, from trying to capture their regulators. That's kind of in their DNA. It's the responsibility of the state to push back and make sure that doesn't happen.

MR. RAJAN: And the community, too, of democracy to constantly shine the light on this stuff and keep the separation clear. Again, the book is about each has its role. And by confusing the roles, we sometimes get a worse outcome. By telling corporations you should play the role of government, you should build roads, you should build the schools in the community, that's in industrial countries the job of the government.

MR. WESSEL: Right.

MR. RAJAN: Focus on them doing it. Push them to do it. But the corporations should be about efficiency.

MR. WESSEL: Right, but I think where the tension here is that you're going to say that the community can do some things that other people think that the nation should do.

MR. RAJAN: Yeah.

MR. WESSEL: Some of it may be in -- you know, there's not very many communities that are going to be to deal with patent thickets and regulatory capture in pharmaceuticals. And there'll be arguments about is it okay to have a community that bans gay marriage? You can say that would be one we do or we don't.

I mean, you have one thing where I thought it was a little bit hard to follow, where you said it was okay for the community to have rules on production. And your example is it's okay to have a \$15 minimum wage. But it was not okay for the community to have non-tariff barriers. That is you couldn't say they could only sell organic food. Right? And that seemed to me like it's a little hard to distinguish. So could you have a tax on non-organic foods? Can you give a rebate for recyclables?

MR. RAJAN: Yeah. Look, when you get to the micro it gets a little tenuous. Right? So what is the principle behind these? The principle is we want a community

included in the country.

MR. WESSEL: Right.

MR. RAJAN: You don't want communities to erect barriers to goods everywhere else. And the easiest way you can do that is what we call non-tariff barriers. You cannot sell food here which is not manufactured under these, these, these conditions. Surprise, surprise, those conditions exist only in your community and nowhere else. That would be a way of excluding every other entity from selling.

MR. WESSEL: Right.

MR. RAJAN: So I'm saying broadly the spirit should be --

MR. WESSEL: But it's hard to incentivize things.

MR. RAJAN: Nothing is really easy. But I think --

MR. WESSEL: I think those are the two worlds of economists. One is the answer to any question is it depends. (Laughter) And the second is it's never easy.

(Laughter)

MR. RAJAN: Well, it isn't.

MR. WESSEL: That's true.

MR. RAJAN: But I guess the broader point I want to make is you need to take the principle and think about what that means.

MR. WESSEL: Right.

MR. RAJAN: And once you get into the weeds, yes, some decisions will become difficult.

MR. WESSEL: Okay. So help me think through Brexit in the frame that you did. You made the point earlier that the European Union has this principle of subsidiarity, which, as I understand it, means things that should be done locally, should be done locally; and things that should be done at the center, should be done at the center. And the problem is that Brussels thinks everything should be done at the center and the voters in Dover think everything should be done in Dover.

So is this an example of a community trying to reassert itself or is it an example of the ugly nationalism that you describe as a consequence of neglecting a community?

MR. RAJAN: It's both. It's both, right? I mean, certainly, many people were worried about the uncontrolled immigration that they faced in Britain as a result of the rules of the Union they had to obey, the Four Freedoms: capital, labor, et cetera, et cetera. That was one.

But also it was the sense that we have no control. And we have no control -- I mean, the example I give in the book is often a laughed at example where the Union sent out rules on the curvature of cucumbers. You cannot sell cucumbers which are curved more than this certain angle because that doesn't meet the requirement of what a cucumber should be. I mean, that's a nutty rule, right? It's wasteful, but I'm sure there was a rationale that the bureaucrats had.

MR. WESSEL: Right, right.

MR. RAJAN: But that's what gives you the sense of central rulemaking which becomes disreputable.

MR. WESSEL: So you're okay with them pushing back against the cucumber rule.

MR. RAJAN: Yeah.

MR. WESSEL: But the idea that they're going to put up walls and not have immigrants, you're not so comfortable, right?

MR. RAJAN: I don't think that was the intent. I think it was more control over immigration. We don't want to be completely open. I think that's a reasonable thing for a country to have. I am not okay with sort of walls within the country around communities, preventing people from different areas from moving. But around the country I think you have to have some sense of who you're comfortable letting in.

MR. WESSEL: I want to make sure that wasn't a quiet endorsement of

Trump's wall. (Laughter)

MR. RAJAN: No. Look, again, I would say that I have no sort of views on the suitability of the wall or not. I think most people sort of reject it because it's really not effective, forget everything else.

But that said, I would say that a country has still, because of where we are, the right to control flows into the country. And it's not a bad thing for a country to want to regain that control. And that's what I see Brexit as. But I also think that some of it is driven by the fact that our sense of powerlessness is augmented not just by the people flooding in, but by the fact that we can't determine very much because everything is constrained by Brussels.

MR. WESSEL: And then you make this interesting point in the discussion of India and China, that basically India has an underdeveloped state and China has just the opposite, an overdeveloped state. So talk to me a little about that and which one -- I mean, sometimes, you know, it's rather frightening sometimes. We like to believe that our values are right and we figured this thing out, and then the Chinese seem to be doing pretty good doing it their way. And it leads other people to think like what made us so sure that we have the right recipe?

MR. RAJAN: Yeah. I would say that what I try and argue in the book is that China has a system which is very effective to get to middle income. Pushing building roads, building bridges, building highways is easy when you have that kind of system, a more centralized authoritarian system where you don't get a protest at every street if you take land away. I'm not talking about the moral or the ethical structures. I'm talking just about can they produce growth?

I think the next stage from middle income to developed country status is much harder with that kind of system. And I make some arguments in the book for why there is -- given that the party require legitimacy, there's the constant incentive to intervene in markets when they go south to protect that sense of legitimacy. And eventually, that

makes you go a little too far in too many directions.

So I would argue that for that reason, but also for the reason I talk about in the book, the need to separate the state from the private sector, that a more democratic structure, whatever Chinese form of democracy there is, would serve them well in the next phase of growth.

I think India has a great system for the movement from middle income to First World, but it first needs to get to middle income. (Laughter) And that's where we're finding it harder because, you know, you want to acquire land, you've got a whole bunch of people protesting, rightfully. This is a democratic protest. We have a reasonable NIMBY movement in India, also. And so it becomes harder to get that infrastructure to get to that first stage.

What do you do about it? I wouldn't give up India's system. I think there's a lot of value and it prevents the harder transition once we get to middle income. It does mean that we get to middle income a little more slowly. We have to work on that.

MR. WESSEL: So you mean -- explain the first part. You think they're well equipped to get from middle income to success because they have democracy, they have a higher education system.

MR. RAJAN: Well, not so -- I think the Chinese education system today is fantastic. I just think the democratic environment, the openness to dialogue --

MR. WESSEL: Creativity to new ideas and stuff, yeah.

MR. RAJAN: The openness, all that, yes, we need to improve our higher education system, but we have the apparatus, the political apparatus, to handle that next phase. And that's why I say, you know, I personally don't believe that it's a given that China will just chug along at this pace without altering its political system, not because it's good, but simply because it is needed as they get to that next stage.

MR. WESSEL: Well, let me just ask you one final question because it is the Hutchins Center on Fiscal and Monetary Policy. So I think you believe in politically

independent central banks. And you made a number of changes in India to put them on a course to having a central bank that looks a lot more like the ones in successful capitalist democracies. But there seems to be some hesitation in India. You weren't reappointed. Your successor was basically fired. Why is that happening and how serious a threat is that for India's growth?

MR. RAJAN: Well, I would say this is part of the broader -- sort of just taking it more broadly and what's happening in the world, the sense of populism, that the people have a right to determine things, and, therefore, the government should have more of a say. Checks and balances are constraints on the government. And once the people have elected it, that view says there should be relatively few checks and balances. Our view is supreme because the people gave us our vote. Well, we know that that's not the way effective societies work, that we need to respect checks and balances.

I think in India it's a process of creating these institutions. I think it's not -- you know, you need directions? We go forward a little bit, we go backwards a little bit, but generally there is progress.

Take, for example, our Election Commission. Elections were not that clean in India earlier. There used to be a notion of boot capturing. Thugs would come and chase the government officials away and start, you know, marking the ballot box. It doesn't happen anymore because we had one strong election commissioner who then got the army -- not the army, the paramilitary forces to actually man the boots. So this guy with a semiautomatic rifle is sitting there and, you know, you don't grab the ballot boxes without some risk to your life.

So in that sense, that fixed elections. That made it much cleaner. And every election commissioner has followed that, so we build institutions. It takes time. It's not always unidirectional. But over the long run, we do.

MR. WESSEL: Okay, let's take some questions. We have a couple of people with mics. I have a couple of requests. One is there are a lot of people here, so

keep your question brief and make it a question.

And I'm going to do like in groups of three. And we'll start there. Yeah, groups of three. So start off by telling us who you are.

MR. THAKKER: Sure. My name is Aman Thakker and I work on India at CSIS. My question is about the universal basic income. That seems to be a proposed solution to a lot of the problems that you raised. But from your presentation it didn't seem like the community had much of a role or empowerment in the implementation of a universal basic income. Is that your sense, as well? And if so, how can the community play a bigger role in implementing such a solution?

QUESTIONER: Hello, Dr. Rajan. Thank you for your presentation.

MR. WESSEL: Tell us who you are.

QUESTIONER: My name is Pollock. I am a student at Johns Hopkins SAIS. And my question is that when you were the governor, your last address you mentioned that India's led on to become like -- the economy has led on to become a one-eyed king in a world of blind people. So how do you think that's changed?

MR. RAJAN: I'm sorry, what was the last?

QUESTIONER: You said that India's economy has led on to become a one-eyed king in a world of blind people. So how do you think that's changed since you left? Thank you.

MR. WESSEL: Okay, there are fewer kings. (Laughter) The gentleman right next to you here. Can you pass -- oh, okay, fine.

MR. MURDOCK: Hi, John Murdock. I'm something of a recovering law professor with a little time on my hands. So a couple weeks ago, I was at AEI and heard from Tim Carney talking about his book, *Alienated America*, which touches on many of these community themes. And his major focus was on the importance of religion, which I didn't hear a lot about from you, so I'd like to hear about that. Thank you.

MR. WESSEL: Okay. All right. So let's start with UBI. Good idea? Bad

idea? Local or national?

MR. RAJAN: Well, I talk in the book about the Beveridge plan in the United Kingdom, which basically meant that we give a very low level of support, but that people pay for over time. It's part of a suite of things that people should have access to in order to preserve body and soul together. That's basically it. It's not -- most people when they think of universal basic income it's at a much higher level. It's a substitute for a decent job.

So I think that if you can afford it, it's a travesty if somebody is on the street and has nothing. I can understand there are people who say this is part of the capitalist system. I would argue that perhaps using the community to give more support is probably also warranted over and above a very basic minimum.

So, for example, have shelters, et cetera, et cetera, but over and above that, the community can be involved, which gets the community engaged in the people who are more unfortunate. And that can be a good thing to bring the community together. So that I would be supportive of.

I think it's too early for universal basic income as a substitute for jobs because they're being automated away. And the reason I say that is it's not clear to me that we know for sure these jobs are going away never to come back. I mean, clearly, there are jobs around. They may not be the jobs that everyone wants, but there are jobs. And how do you -- once you start that universal basic income level at a high enough level, how do you make sure that people don't sort of move out of the labor force permanently even when new jobs are created?

So, for example, if we get driverless cars, at least the belief is a whole lot of truck drivers, a whole lot of Uber car drivers will become unemployed. But maybe new opportunities open up. For example, we have a crying need for healthcare. So somebody able to put into a software system what your symptoms are after six months' training, that may broaden healthcare for a lot of people. You can use AI together with moderately educated people to provide much more healthcare more widely.

MR. WESSEL: So you believe in a somewhat stronger safety net than we have now in the United States, I think.

MR. RAJAN: No, I would argue that where there is a hole, I would fix it.

MR. WESSEL: Okay.

MR. RAJAN: Where there's a hole today, I would fix it. I would argue for universal healthcare because I think it's just -- the system we have is terribly costly without (inaudible) --

MR. WESSEL: But you also speak favorably in the book about the Singapore plan where everybody gets a certain -- a voucher to get training for their whole life.

MR. RAJAN: No, I think, again, it depends. So we want to be careful about overeducating the population and forcing everybody to get degrees that they don't need. So I argue that we have to think about what level of education is reasonable for the current circumstances.

MR. WESSEL: Right. And you say community college might be.

MR. RAJAN: It might be. I don't know enough to say that is the level.

MR. WESSEL: Right.

MR. RAJAN: It is certainly true in the United States high school education is free. And that created an enormous advantage for the United States in the first phase of the post-Industrial Revolution, in the second industrial and third industrial revolution. The question we have to ask ourselves is do we have to move up one more stage?

MR. WESSEL: Right.

MR. RAJAN: And I think the experts have to think about that, but if the answer -- I don't want everybody getting Ph.D.'s.

MR. WESSEL: Neither do we, that's fine.

MR. RAJAN: Overeducated for the jobs that there are and you get degree inflation. Instead, let's figure out what makes sense.

MR. WESSEL: Okay. I asked you about culture. I didn't ask you about religion.

MR. RAJAN: So UBI, not yet.

MR. WESSEL: Okay, got that. Religion? Not yet?

MR. RAJAN: No, religion -- (Laughter) I have no views for or against. I think it's something that people believe in that is the source of organization. In some communities the church is the biggest sort of organization of force. I mean, that's a good thing. I don't think that -- I'm not sure whether you should have policies about it, but I think to the extent it plays that burning role, it's a very important structure.

MR. WESSEL: And I'm not familiar with your speech about the one-eyed king.

MR. RAJAN: Ah, yes. That wasn't my last speech. It was --

MR. WESSEL: You have a lot of speeches.

MR. RAJAN: It was taken -- somebody asked me about how India was doing. And I said we're doing okay, but we're a little bit like the one-eyed man in the land of the blind. There was a time when the world economy wasn't doing that well and, you know, people sort of thought I was criticizing India for saying one-eyed.

I mean, look, we could be -- we're at 7 percent growth. I don't know which GDP numbers sort of make most sense. There's been a lot of revision, but I think that, broadly speaking, I'm more worried not about the GDP growth numbers, but about the job situation in India and the fact that 25 million people are applying for 90,000 jobs. I keep saying that because that is my strongest indicator that we need more jobs.

MR. WESSEL: Can we go to the back? We should take the two people, the three people on the aisle there. Yeah.

QUESTIONER: Thank you both for a very good presentation. Dr. Rajan, in the 1980s I worked for two people in the Chicago schools: Alan Wass and George Shultz. I would like to ask you about immigration. You stated, I think, that countries have a right to

limit immigration. I think most of the people in this room would agree that the current administration has a poor or limited policy on immigration. How would you characterize the effect of immigration on economic growth?

MR. WESSEL: Okay, thank you. Will you pass it there? Can you make sure the mic's on? Haowen, can he have the other mic?

MR. TRAN: Hung Tran, formerly with the IAF and now with the Atlantic Council. In your presentation schools is a very important component of your third pillar, the community. So how do you think about the impact of the growth of home school movement in the U.S.? And what would that do to the effort rebuild communities here?

MR. WESSEL: Okay. And the guy right on the edge there. Thanks.

MR. WHITAKER: Stu Whitaker. I work primarily in transportation now, but I'm interested in your question about broadband in rural areas. It seems to me the only way you can achieve that is through subsidies. And there's been work for decades to subsidize communication and transportation in those rural areas. It seems inefficient. So I'm curious about the fact that that recommendation seems to be a non-economic solution.

MR. WESSEL: Right, okay. So immigration, what are the economic pros and cons of immigration?

MR. RAJAN: Well, I think I'm reasonably persuaded that immigration has been broadly helpful for countries. Again, not an uncontrolled process of immigration, but immigration in general has been very beneficial. Even one could argue that whether legal or illegal, in some countries where the illegal in moderate, it performs certain functions that the country wants to be performed and hasn't got good processes to get people in.

That said, I would still say it's the democratic right of the people to decide how much immigration they want and to send that right to some international body which say this is the amount of immigration that you should have or these are the people you should let in. It essentially gives up the sovereign right over flows.

MR. WESSEL: If immigration is largely beneficial to a country like the

United States, as you pointed out, an aging society needs more workers, we know how many companies in Silicon Valley were created by entrepreneurs and how many Nobel Prizes have been awarded to immigrants, and all that, why is it so controversial? Why is it that the President has done such a good job of capitalizing on the anxiety about “the other?”

MR. RAJAN: Well, I think there is this two-pronged attack. One is on the illegal immigration and that’s where I think you’re using the fact that, hey, guys, do you want some control over it or not? And if ask people that question they would say, yes, I don’t want anybody who wants to walk into the country to have the ability to do that. And, of course, that’s always tinged with they’re going to move onto public support very quickly.

I cite an interview by some Harvard scholars which says the belief of the extent of immigration as well as the extent of immigrants on public support is always much greater than the actual numbers. But that’s the kind of imagery that’s promoted. If you’re for immigration it means you’re for illegal immigration by guys who are going to quickly go on public support.

I mean, the notion of legal immigration which is managed I think is certainly something that is less controversial. I think some of these voices when pushed to the corner will say, yes, we support that. In private, they’re pushing the other imagery which I talked about, the populist nationalism. Those people don’t look like us, the Asian CEOs of Silicon Valley companies, and they should be, you know, different.

MR. WESSEL: Right.

MR. RAJAN: So I think there are two dialogues in parallel going along or maybe three or four. And broadly, immigration is beneficial. Broadly, you should have the right to control that immigration and you make your democratic choice.

MR. WESSEL: I’m going to resist the opportunity to argue. Home-schooling, have you thought about that at all?

MR. RAJAN: No. Look, I don’t know enough about -- on the home-schooling movement. My sense is that many parents who teach their kids at home would

also find ways to, you know, get their kids to actually have social company outside. I don't know how that is done enough to comment on whether that's a good thing or a bad thing.

In general, these are parents who really feel strongly about giving their kids a good education. I think that's a worthwhile thing.

MR. WESSEL: Okay. And I think the question --

MR. RAJAN: Broadband subsidies.

THE WITNESS: We've been talking about subsidizing broadband ever since I came to Washington.

MR. RAJAN: Yeah. Look, I don't want to get into the issue of whether you can have private provision, public provision, subsidy or not, et cetera. All it seems to me is that today this is like having a road. If you don't have a road to access the broader world, you're locked in. And it seems to me that we have to find a way to get broadband to communities which don't have broadband.

MR. WESSEL: There's a woman here. Why don't you start with the woman in the pink? And then the guy in the red sweater and then the woman in the leather jacket. Go ahead.

QUESTIONER: Hi. I'm an international student from Taiwan at George Mason. My question is what might be the potential that Asia democracy can contribute to the third pillar of community, either from their lifestyle or their culture? Thank you.

MR. WESSEL: So the question is what is Asia's future if it doesn't strengthen the community pillar?

QUESTIONER: I mean, what is the potential that Asia democracy can contribute from their culture or lifestyle? Maybe more creative than Western democracy can contribute to this third pillar.

MR. WESSEL: Okay, yeah. The guy in the red sweater, can you just stand up so Haowen can see you?

MR. BLANK: Martin Blank, formerly president of the Institute for

Educational Leadership. Amazon left New York, walked away, in part I believe because the community was demanding that there be an opportunity for workers to unionize. In your whole discussion this morning I see no reference to labor unions, which historically use their power to influence the behaviors of corporations.

MR. WESSEL: Right, right.

MR. BLANK: And it seems to me that the market and the state over the last 30 years have diminished the power of unions, leaving aside for the moment the question of some of the problems with the union (inaudible).

MR. WESSEL: Right, good question. That was on the list of things I didn't get to.

And the woman right in front of you, can you stand up? The woman in the glasses. Yeah.

QUESTIONER: Hi, I'm Sonali. I'm from India. I'm studying here at the University of Maryland. My question is about in your presentation you talk about the superstars in the economy. According to (inaudible) in the economy we should only have stars. The question really is how do we incentivize people to be superstars, to keep doing what they are doing, but not just incentivize them through money? But what could be the other factors in incentivizing people to keep them motivated?

MR. WESSEL: Okay. So I think the first question, Raghu, was -- I'm probably misinterpreting it, but I'm going to frame it anyways. Is there something about the culture of Asian societies that makes it different, makes it harder for them to strengthen this third pillar? Or is it just it's not a cultural thing, it's just a question of stage of development and will to do it?

MR. RAJAN: Well, I don't think it's a cultural thing. Of course, communities emphasize different things in different societies. The American sort of archetypical frontier village is very different from a village in India today. But the sense of getting together, sense of local government, all that is pretty much there everywhere.

I would argue that in India we probably have crowded out local government much more through over-weeding bureaucracy of the central government over the many years. But now there's a movement towards more decentralization which is picking up.

MR. WESSEL: On unions, there are about six or seven references to unions in the book, so we didn't forget them, but you didn't talk about them. And I wonder if you could talk about them in two respects. One is to what extent are they a countervailing force? And secondly, are they sometimes a kind of community that you have not given enough weight to?

MR. RAJAN: Yeah. So let me take the second. I mean, there are different sources of bonds between people: professional bonds, social bonds, union bonds, and so on. So I haven't gone into the entire sort of structure, but clearly, there are different ways these social organizations can emerge, sometimes as economic organizations, sometimes professional organizations. A union is certainly one of them and it could be a source of countervailing power, certainly.

Certainly, as technology changes there's an argument for whether some of these, what do you call it, the Uber drivers and so on, the --

MR. WESSEL: The gig economy?

MR. RAJAN: The gig economy, whether you need something like a national union to protect their rights. I think we'll have all these debates. I don't have a strong view one way or the other. It just seems to me that it is an important other aspect of social organization.

MR. WESSEL: Right. But I think behind the question is, is one of the problems -- is the decline of unions one of the reasons that we have some of these problems? Because it was one mechanism for the worker as a community to get this whole discussion of the falling labor shares.

MR. RAJAN: Yes and no. To some extent, the fact that you have fewer commodity workers, but more specialized workers has sometimes. So, for example, your

Bain consultant is an equity partner in the firm. It doesn't require a union to protect themselves because now, because of the key capabilities, they're not owner versus partner. They have an equity claim.

One could argue that with the service economy more and more workers are in that category. Again, I don't want to say this is the entirety. I would just say more.

MR. WESSEL: Right, right.

MR. RAJAN: We professors don't need a union. We have --

MR. WESSEL: Well, you have tenure, you don't need a union, yeah.

(Laughter)

MR. RAJAN: Well, maybe a union for (inaudible). Good point.

MR. WESSEL: All right. And finally, I think the young lady raised a good question. So my impression is the creation of superstars, whether they're superstar firms or superstar in professions, is a reflection of technological change and we shouldn't try and discourage that. To the extent that companies are becoming supersized by cheating, by breaking the rules, by screwing their competitors, that's a bad thing. But is there some way to -- should we have more incentives for superstars? Should we tax them? Since some of this, as you point out, is not a return to their town. It's a fact that Taylor Swift has a huge audience and your opera singer didn't. That's wasn't anything -- she might have been even more talented than Taylor Swift.

MR. RAJAN: Right.

MR. WESSEL: I never heard her sing, so I don't know. (Laughter)

MR. RAJAN: Yeah, they didn't have recording at that time.

Look, I think there are many ways that society operates. One, yeah, taxes we can debate and I'm sure the debate is hot in Washington on how much you can tax people without it creating disincentives and so on. That's ongoing.

But I also think society eventually changes its value system, and that is part of what happens. So your point about should we value superstars, well, to the extent that it

becomes very concentrated we might start valuing something else. And that's why I wanted to show in the book how attitudes changed towards the economy, towards the money, towards making money, towards greed. And that is part of society's development. That's the third pillar reacting.

And to the extent you think that it's growing too concentrated, too wieldy, there is a certain amount of opprobrium to that kind of wealth. So think of The Giving Pledge, which Bill Gates is going around selling. I mean, you could think of that as being the goodness of their heart of a lot of very wealthy people.

It could also be that they don't feel so comfortable socially in having it all or themselves and they don't feel comfortable giving it to their kids. That's part of societal change, and maybe some people want it to go faster. It's just that it seems to me society also reacts. I'm not saying that you should exclude this whole debate about taxation, but there's also other ways society reacts.

MR. WESSEL: It seems to me that the mark of a good teacher and a good book author is someone who leaves you with -- helps you think about things in a way you haven't thought of before and often leaves you with more questions than answers at the end of the conversation. So I think by that measure both the book and this hour and a half have been a great success. (Laughter)

And I want to thank Raghu for coming and all of you for coming. (Applause)
I think we're -- Anna, is Raghu going to sign books out there or not?

QUESTIONER: Yeah. Yeah, just right out front.

MR. WESSEL: Right out front where you came in. And if, in the sense of us building a healthy community here, if there's a coffee cup or a piece of paper at your feet, you could put it in the collective wastebasket in the back, and we will be a strong community as a result. (Laughter)

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