The U.S. Role in the World Economy

An Interview with Dr. C. Fred Bergsten, Director, Peterson Institute for International Economics


C. Fred Bergsten

EDITORS' NOTE *Fred Bergsten has held his current post since he created the Peterson Institute for International Economics in 1981. Dr. Bergsten was Assistant Secretary for International Affairs of the U.S. Treasury from 1977 to 1981. He also functioned as Under Secretary for Monetary Affairs from 1980 to 1981, representing the United States on the G-5 Deputies and in preparing G-7 summits. From 1969 to 1971, Dr. Bergsten coordinated U.S. foreign economic policy in the White House as Assistant for International Economic Affairs to Dr. Henry Kissinger at the National Security Council. He has been a Senior Fellow at the Brookings Institution (1972-76), Carnegie Endowment for International Peace (1981) and Council on Foreign Relations (1967-68). Dr. Bergsten has authored, co-authored, or edited 40 books on international economic issues including most recently* The Long-Term International Economic Position of the United States. *Dr. Bergsten has received the Meritorious Honor Award of the Department of State (1965), the Exceptional Service Award of the Treasury Department (1981) and the Légion d'honneur from the Government of France (1985). Dr. Bergsten received M.A., M.A.L.D., and Ph.D. degrees from the Fletcher School of Law and Diplomacy, and a B.A. magna cum laude and honorary Doctor of Humane Letters from Central Methodist University.*

ORGANIZATION BRIEF *The Peterson Institute for International Economics (www.iie.com) is the only major research institution in the United States devoted to international economic issues. It has been called "the most influential think tank on the planet" and the first comprehensive survey of 5,465 think tanks around the globe recently concluded that the institute was tied for "Top Think Tank in the World" in 2008 (with the Brookings Institution). It has a staff of about 60, averages two or three publications per month, and holds at least one conference or policy meeting every week.*

You have been with the Peterson Institute for International Economics from its inception. What was the mission then, and has it evolved or changed?

The Institute for International Economics, as we called it for the first 25 years, was created to fill a huge gap in the network of U.S. think tanks or intellectual endeavors. At that time, the U.S. had no dedicated effort to study the impact of the world economy on our own economy and on our foreign policy. A group that Pete Peterson and I led concluded that we needed to fill that gap. So we created a new research center devoted to the world economy and the U.S. role in it, to try to figure out its impact on our economy and our foreign policy, and to try to promote constructive policy responses to further a successful, stable, growing world economy and the U.S. role in it. That mission remains our core today.

We have amended the ways we approach it and the specific topics we address, but that founding objective turned out to be quite accurate and successful.

How broad is your area of focus?

We constantly update what we call our rolling agenda. One of the reasons for our success has been our ability to anticipate major issues that are going to come onto the policy agenda over the next two to three years, undertake projects to analyze them, and propose responses to them before the issues hit the front burner and become central concerns of policymakers and the policy community.

We do that through constant consultation with our own board, our advisory committee, the policymaking community, the alert media, and private sector leaders – we're constantly updating our assessment of what the key issues will be, about which better understanding and policy suggestions are needed.

The specific topics change from time to time, but there are several overriding themes. One is the increasing impact the globalization of the world economy has, not only on the U.S., but on practically every other country in the world as well. There are huge debates about whether globalization is good or bad, and about its distributional effects, both among countries and within countries.

Over the past decade, our focus has been on the fundamental shift in global economic power: the move away from the traditional high-income G7 countries toward the emerging market powerhouses, like China in particular, but also India, Brazil, South Korea, and Mexico, which are all moving to the forefront and which, as a group, now account for half the world economy.

We focus on what we call the trillion-dollar club – the group of developing economies that have now reached a trillion dollars or more of GDP.

Were you surprised at the speed and severity of the economic crisis and where are we today in terms of recovery?

We were surprised by the depth of the fall off in economic activity worldwide, and the subprime loan crisis in the U.S. that triggered it. But we had been warning, from 2000, that the buildup of big international economic imbalances was creating a situation that was likely to lead to a crisis: the big trade deficit of the U.S. and its dependence upon foreign financing kept our monetary conditions loose and held our interest rates down. The corresponding big surpluses in China, Germany, and a few other countries; and the buildup of problems that had occurred in the '80s and that led to big problems then too; all created the conditions for the overleveraging that brought on the crisis.

We're currently in a three-part world recovery. The emerging markets – China, India, and Latin America – are doing quite well. The emerging markets' growth as a whole is averaging above 6 percent; in Asia, it's above 8 percent. They're having to put on the brakes because their economies are, in fact, moving too fast.

At the other extreme is Europe, which is now growing at 1 percent or less. They are in very weak shape, and need to expand but they can't do it because so many of their member countries have faced sovereign debt crises. They have to tighten their belts.

The U.S. is running growth between 3 and 4 percent – by traditional standards, not bad, but pretty weak for recovery from a deep recession. Unemployment is still very high and it's problematic, and one of our focal points should be the direction of U.S. policy: should it continue to stimulate the economy due to fear of falling back into a double-dip recession, or given the huge build up in our deficits and debt, do we need to start stepping on the brakes?

We've done a huge amount of work on the outlook for the U.S. foreign debt position, which is at least as daunting as the outlook for the buildup in total national debt, and that is a real constraint on U.S. policy going forward as we pay the piper for our past profligacy.

At what stage are countries like Brazil, China, or India no longer considered emerging markets?

China probably will pass the U.S. as the world's largest economy within the next 20 years on current trends, and by some standards, it has already emerged. China, and India coming in its wake, are unique economic superpowers – they combine huge economic weight, given their population and rapid growth, but they are still poor countries in per capita income terms.

So that raises unique problems of how to assimilate them into the world economy itself, because for a long time, they will continue to think of themselves as poor countries.

Many talk about the U.S. losing its edge as a global leader, both in entrepreneurship and innovation. Is there merit to that concern and what needs to be done for us to retain our edge?

We have done a lot of studies that show, on different measures, that U.S. competitiveness has declined. Our global market shares have declined, and, beyond what you might expect from the normal convergence process where China and India are naturally catching up, the U.S. is clearly losing its leadership position.

At the heart of that is our deficient K through 12 educational system, and that means that our human capital is not developing at the pace we need.

Our national saving rate is very low. That means we have to rely on borrowing from the rest of the world, which builds up our foreign debt. The in-flow of that foreign money keeps our exchange rate higher than would be justified by our fundamental economic situation, and that makes it harder for us to compete in the world.

Our tax policy is an issue. Corporate taxes were among the lowest in the world 30 years ago, and now they're the second highest among all the rich countries. That is a discouragement for investment here, for foreigners to bring their plants here, to do R&D and innovative investment here.

With our traditional complacency about our role in the world, we have not kept up to speed like everybody else.

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Why has it been such a challenge to bring about the kind of education reform that is necessary, and is the dialogue there to create reform?

The underlying systemic problem is that we do not have a U.S. education policy. Education policy is determined by 15,000 local school boards rather than the federal, or even state, governments. Successive administrations have realized the problem and have tried to do things about it but they can only pursue that effort through inducements by offering federal money. But federal money is a modest share of the total funding for education in the country, and money is not even the main problem – it's changing the ways of operation in the school systems, and that cannot be centrally directed or coordinated.

In addition, other countries, most of whom have centrally directed national education policies, are able to move much faster than we are and have done so. So until somebody takes on the monumental political challenge of altering the decision-making structure of our education system it is going to be very hard to reverse or even slow down the U.S. loss.

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You have put a heavy focus on climate change. Is the right dialogue taking place around that issue and are we making progress?

There is progress being made. Practically every country, including China and India, have undertaken very important new policies to limit their use of energy and reduce their emission of pollutants. So efforts are underway in most countries, albeit not yet under a binding international treaty.

The fundamental problem is there is no international institution dealing with climate change, or the environment more broadly, the way there is on trade with the World Trade Organization or international finance with the International Monetary Fund, for instance.

About 15 years ago, we proposed a Global Environmental Organization (GEO) that would develop an agreement on a basic motivating doctrine and conceptual foundation for what you're trying to do, and then write a body of rules to implement those concepts and put an institution in place to enforce the rules and have a dispute settlement mechanism. Without something like this, we'll never get a handle on the problem.

When you look at so many of the issues we're facing, is it tough to be optimistic looking forward?

It does concern me, but I'm not pessimistic. The forward movement of policy understanding and thinking, and international cooperation, despite the obvious problems, is quantum leaps ahead of where they were.

There were three big lessons that were learned from past recessions and not repeated: do not tighten budgets in the face of an economic turndown, as the U.S. did in the '30s; do not tighten monetary policy in the face of a turndown, as the Federal Reserve did in the '30s; and internationally, do not erect trade controls to try to export your problem to the other guy because it will just bring everybody down.

In immediate response to the crisis, there was virtual unanimity on what to do in those areas, and there was a constructive institutional development.

The group of 20 leading economies, the G20, has brought in the Chinese, Indians, and Brazilians with the traditional economic powers with remarkable cohesion and cooperation, and policies were instituted, which got the economy turning around pretty quickly after only six months of global turndown. Major countries, led by China, started to recover. The situation is not yet satisfactory but this was a huge success for the global cooperation process.

The story is not over. There are three different elements of the world economy moving at different paces, so it's harder now to coordinate and get the thing right. But the experience of the past two years has been a huge success.

When you think back to the creation of the institute in 1981, could you have imagined 30 years later that you would be playing such a critical role in these issues?

I was an optimist in undertaking the venture in the first place because it was not only a challenge but a risk. But we were not even within the ballpark in imagining how successfully we would develop, including the size of our operation and, particularly, the impact we would have. Many think tanks have been created explicitly on our model, and sometimes with our help.

We're still relatively small by think tank standards but we're more productive than most. We believe we have a pretty good cost/benefit ratio. ●