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The Honorable Robert B. Zoellick, President

World Bank Group

Questioners: Martin Feldstein
Professor of Economics,
Harvard University

Henry Kaufman, President
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Andrew Tisch: Good afternoon everyone, and welcome to the 422nd meeting of the Economic Club of New York, now in our 105th year. The Economic Club is the nation's leading nonpartisan forum for economic policy speeches. More than 1,000 guest speakers have appeared before this club establishing a strong tradition of excellence. The tradition has been supported by contributions from the 166 members of the Club's Centennial Society. Their names are listed in the program and we thank you. This morning we'd also like to welcome students who are here with us today from the University of Bridgeport, from Barnard College, Hofstra, and The New School. Their attendance here is made possible by our membership.

I'm pleased to welcome Robert Zoellick who became the 11th president of the World Bank Group on July 1, 2007. Prior to joining the bank, Mr. Zoellick served as Vice-Chairman of Goldman Sachs Group. He served on the President's Cabinet as the 13th U.S. Trade Representative from 2001 to 2005 and as Deputy Secretary of State from 2005 to 2006. From 1985 to 1993 Mr. Zoellick served at the Treasury and State Departments as well as briefly in the White House. He earned a J.D. magna cum laude from Harvard Law School, an M.P.P. from the Kennedy School and a B.A. from Swarthmore College. Following Mr. Zoellick's remarks, he will be questioned by two of our designated club members. Anyway, Mr. Zoellick, welcome.

The Honorable Robert B. Zoellick: Well, thank you very much Andrew. And thank you very much for the invitation and for all of you coming. I thought I'd just start us off a little briefly

with some thoughts about economic change but also inaction in three areas: the developing world, the United States, and Europe.

In 2010 and 2011 China consumed an estimated 64 percent of the world's cement, 58 percent of the world's iron ore, 48 percent of the world's coal, about 45 percent of the world's steel and lead, and for those of you focused on lunch, about 44 percent of the world's pigs, 40 percent of the world's eggs, and 27 percent of the world's soybeans. Just take a minute to think about those numbers. They're absolutely extraordinary for one country. Now as China gets built, some of those numbers will obviously change. But India and others are still to come. Even sub-Saharan Africa grew about five to six percent a year for the decade before the financial crisis. It is now moving beyond pre-crisis levels.

We're very quickly moving to a world economy of multiple poles of growth. And just consider this as a reference point. Over the past five years two-thirds of the growth in the world have come from developing countries. And if you go back and look at the 90s, as recently as that period, those numbers would have been in the 20s. Now of course the types and sectors of growth in the developing economies will change.

For the first time in my recollection all the major advanced economies are stumbling at significantly below potential growth. So the structure of developing economies will need to focus increasingly on domestic demand. In some countries such as China that will be more on

the consumption side. In others, in Latin America or Southeast Asia, it may be on investment.

There's also still some very huge shifts ahead in topics like urbanization. The World Bank and China estimate that by the year 2030 China will go from about 50 percent urbanized today to 70 percent. And we forecast for South Asia which today is at about 30 percent urbanization that it will be 55 percent by 2050. And these have huge implications for not only infrastructure and water and sanitation and transportation and education and changes in the workforce. And these changes are going to lead to an increasing number of changes that shift people's thinking about emerging markets from a North-South paradigm to increasingly South-South, whether it be trade or investment or tourism or remittances. And those changes will create opportunities for people to think about supply chains and logistics changes, and I hope addressing some of the barriers that you still see at higher levels at the South-South level than you do in the South-North level.

Yet for all the upsides to this growth story, developing countries especially middle-income countries are concerned about the challenges of structural change. And so I would expect that all of us are going to hear more about topics such as the middle-income trap which is the tendency of developing countries' growth to flatten down or slow down significantly or even stall as they start to exhaust the basic gains they get from reallocating from one sector to another or technological catch-up.

In 1960 the World Bank analyzed the number of so-called middle-income economies and there

were about 101. In 2008, so almost 50 years later, only 13 of those economies had made it to high-income and one of those was Greece. So there's a recognition increasingly, and in some ways being led by China of the need to move to new growth models. The Bank did a report we released over the past few months, some of you might have seen the news stories, called China 2030. And even though China had grown 10 percent a year for 30 years, there was a recognition on the part of the Chinese authorities coming in that they were going to have to shift, that the model that worked so well in the past wouldn't necessarily work for the future. So part of this project was a joint effort to look at everything, from the fiscal system to urbanization, to environment, to the state-owned enterprise sector, to land, and others about how they would make these changes.

Well, second, if China is considering structural changes that are necessary for future growth, might this also be an appropriate topic for the United States? Much of today's commentary focuses on stimulus policies, whether they be fiscal or monetary. Yet I think one of the challenges that we're all going to have to face is that the record suggests that short-term stimulus have much less effect if countries are burdened with large debts. But long-term investors appear to be willing to accept short-term costs if they assess the future prospects favorably.

So I'd argue that the U.S. also needs a medium-term focus on structural reforms. Or you can call this the micra-economic agenda that goes along with fiscal adjustment creating the incentives for private finance and entrepreneuralism.

Now to put this in today's political economy context, my sense, and we've got some of the people here that have participated in this, was that in early 2009 the new administration expected a V-shaped economic recovery. So the priority the president set was one of changing the healthcare system. I think Rogoff and Reinhart didn't have their book out yet, and if they did we all would recognize that actually with that type of downturn it was most likely we were going to have a longer L-shaped recovery. And then I think if you looked early last year in 2011, the reports that Bowles and Simpson and Domenici and Rivlin put out were an opportunity to try to combine addressing some of the structural spending issues and debt issues with some of the microeconomic incentives. But that was the path not taken.

So my own suspicion combining some experience in markets and economics but also the political economy issues is that one of the reasons that the U.S. economy is growing but growing at perhaps more modest rates than any of us would like is some of the ongoing uncertainties that relate to the structure of microeconomic issues. For example, what will happen with the fiscal cliff, or what will happen with taxes, the uncertainty that comes out of the healthcare issues, financial regulation, energy and environmental regulation, some of the issues related to the NLRB and labor policy.

So without taking sides on these, I just think it's important as an analytical matter to realize these add up. In the trade agenda, it's the one I was actively involved in early in my career, which is a

great way to drive microeconomic and structural reform, and frankly it's stuck. So I believe the key issue the United States is going to be facing is not only the question coming into 2013 about the fiscal adjustment, but how one creates the right incentives for private businesses and energy and infrastructure and education and innovation.

Now third, how might this structural reform lens shed some light on the situation in the European Union? The European Union is struggling with three interconnected problems which is one reason why this is so difficult. On the one hand, it's a problem of sovereign debt. On the other hand, it's a problem of the banking system which is of course interconnected with the sovereign debt because if the banks hold the sovereign debt and the sovereign debt declines in value, that hits the banks' capital, and also for some countries their overall international competitiveness within a single currency.

So Greece is the topic in the news but I think the strategic question for this year for the Eurozone will be Italy and Spain. Perhaps France as well if there are some missteps because the new president, President Hollande has a very fine line to walk between the election and the National Assembly Election which will be later in June, and the policy for the Eurozone.

Now the good news is that both Italy and Spain are pursuing some very serious fiscal reforms and structural reforms. If you look at, for example, the Italian reforms in the pension market or some of the changes taking place in the labor market, these are very serious steps. But these

types of combined fiscal and structural reforms are devilishly difficult to do in a no-growth environment.

Now the German position has a logic. Countries can't fundamentally escape these reforms. But the challenge we're now into is the politics of reforms. How can you sustain them? Now I wouldn't expect Germany to pay for an offsetting expansion. One European leader said to me about a month ago that I had to keep in mind that in Germany economics is a branch of moral philosophy. So while we might have some American columnists that will urge a Keynesian solution, for Germany the moral philosophy will argue for rectitude and hard work and discipline, and I think those will predominate the German policy mix.

Yet I do think there's an opportunity, and I think you'll see some of this evolve over the next couple of months, to try to have some economic support linked to political support on the investment side. I had suggested a number of months ago to at least consider that the European Investment Bank which was actually having to shrink its operations could get, say 10 billion euro of additional capital which could leverage and then make investments that would complement some of the structural reforms. So I was trying to argue that the preoccupation with firewalls while I understood the logic actually risked overlooking some of these critical political economy issues.

Another opportunity for Europe is that the European Commission is sitting on over 80 billion

euro of what are called structural and cohesion funds. These are designed for some of the countries that came into the European Union, and frankly at a critical moment for the future of the Eurozone, the European Union, one would want to try to deploy these as quickly as you can.

And there are some interesting opportunities that go to the heart of the European goal of strengthening its position as a single market because there could be reforms in the service sector that would also create opportunities for southern as well as other countries. The movement in the labor market obviously isn't as flexible as you have in the United States. Part of this is language and culture but there could be things that could be done. You can read the stories about people actually taking the language courses trying to figure out information matching to move to some of the jobs that are available in Germany and elsewhere.

But having said this, while I think these steps will be ones that you'll see negotiated, particularly on the investment, in the European Investment Bank side over the coming months, I'm really not sure whether they offer enough medium-term support for the difficulties of the structural change. Clearly one other step will have to be the recapitalization as appropriate for some of the Spanish banks.

But I think there will be one other issue that will be hard to avoid, and that is thinking about the medium-term, my suspicion is there will be a need to assure investors that the sovereigns will have time for these reforms to take hold, that they can roll over the debt. Now there's various

ideas out there. One that I and some others suggested was the Hamiltonian Solution. And what this involves is, some of you know who know U.S. history will recall that when Alexander Hamilton became the first Secretary of the Treasury and you had very large state debts and a massive debt inherited from the revolution, the package that he put together assumed the state debts once. State debts are, from that point on, the responsibility of the states and the states' performance is reflected in the market. I actually think that's a good idea because it adds market discipline. But it's possible that one could use a euro bond financing for countries that were making the reforms at this one critical moment once.

A variation has been suggested by some of the European, actually it was a German think tank, would be to offer euro bond support for debt up to 60 percent of the GDP. Now the point is Germany understandably doesn't want to offer euro bonds for everybody's debt because it will lose the discipline of the overall reforms.

Another idea which Marty Feldstein wrote about recently and a back-up idea for Spain that I thought was very creative would be as an ultimate backstop that savers, if it was critical, would be able as opposed to being taxed, would be able to hold the Spanish debt. So it's a form of financial repression. It's not ideal. But as he outlined, the real purpose is to have it there to assure investors over the medium-term.

The basic point is that what we've seen happen to Europe up to this point which is when trouble strikes to try to solve it with a liquidity solution, so for example the European Central Bank

stepping in as it did late last year and early this year buys time but it won't solve the Eurozone's ultimate ills. Another possibility is you'll see that this mechanism, the European stability mechanism, might actually be a backstop for say, Spanish or Italian debt, and it would issue bonds which is a back-door way of doing euro bonds.

But the key point, I think, is that the Eurozone is still going to need the structural reforms on government spending and debt. It'll need the microeconomic competition and increased productivity. But the missing piece is still the funding assurances that will enable investors to see this medium-term outlook.

So let me close with just one more observation. I recently was visited by the new Foreign Minister of Australia, Bob Carr. And we've got Phil Scanlan here, the Counsel General from Australia. As he would tell you, Bob Carr was a very successful premier in New South Wales for many years. He's a great friend of the United States, a great student of American history. And when I asked him, what was the main message that he was bringing to Washington, he said something that really struck me and I just want to share it with all of you. He said his primary message was that the United States is one budget deal away from restoring its global preeminence. But he also said you have to recognize that in the Asia-Pacific there are others that are saying the United States isn't going to be able to handle this. It's not going to be able to get out of this hole and you better listen to us for the future.

I travel a lot, both with developed and developing countries, and I talk to leaders and I talk to their business community and their civil society groups and I try to engage their public, and I think Bob Carr is exactly right. The U.S. has amazing possibilities. You see the changes, for example, in the oil and natural gas market that I certainly wouldn't have believed in the forecast five, six years ago, totally different from what we have going on today, a combination of technology and innovation and possibilities. But these changes won't just happen. And from my experience, but I've served my public sector time primarily in the executive branch, I think ultimately this is going to be a question for the next president to put high on the agenda. And I think Bob Carr is right, what's important is that this is not only the U.S. economic future but its global standing, one budget deal away. Thank you.

QUESTION AND ANSWER PERIOD

ANDREW TISCH: Thank you. We're going to try something a little bit different today. We're going to take away the podium and put a couple of chairs out here and ask a couple of our members to have a conversation rather than a question and answer to get some dialogue going.

Anyway, we've asked Martin Feldstein who is a Professor of Economics at Harvard University and Henry Kaufman, former club treasurer and President of Henry Kaufman and Company, to just engage in the conversation. And if you want to lob some thoughts in, if you would just send

them to questions@econclubny.org. and our President Jan Hopkins will read them. Anyway, it's going to take us about two minutes to make this physical change so as they say on Saturday Night Live, talk amongst yourselves.

ANDREW TISCH: I didn't believe them when they said it was going to be two minutes, but it's been a minute and 45 seconds. Marty, you want to start and get this thing rolling?

MARTIN FELDSTEIN: Yes, well, I thought that I would ask you some questions about the World Bank and then some more general questions, and your very good speech certainly raised a wide range of other questions. But looking ahead you're going to finish your very successful tour of duty as President of the World Bank in just a few weeks and your successor is going to come in, what do you regard as the most significant challenge that Dr. Kim will have as the next President of the World Bank?

THE HONORABLE ROBERT B. ZOELLICK: Well, I think it involves a continuation of some of the changes that I've tried to institute at the bank, the most basic one being to focus on developing countries as clients. And this may seem obvious, particularly to a lot of people in the private sector, but just consider, some of you might have read some of the articles at the time of the discussion on my, the debate on my successor. And I was struck, you know, that there were voices that in my view were repeating some of the misperceptions of the past which is we come from a very elite university, we're very smart people, here's the three things that must be done

for developing countries.

And in my view, the starting point is to recognize that the countries have a sense of their problems but what's changed enormously in this world I've described is what the bank can bring to bear is the experience from other developing countries, whether it be on infrastructure development or efficient social safety net development or strengthening the private sector, and so the role of the bank is to try to understand the problems, not just as problems from an economic textbook solution but as trying to come up with political economy answers.

Now having said that, I think one of the areas that is connected to that, that we've tried to institute at the bank is a process of what we call democratizing development. And what I mean by that is when I used to go to fora like this, when I started the bank, there was often an economics professor that would come up to me and say, you know, you've got some incredible data resources at the bank but you continue to charge for them. And I would go back to our economic team and I would ask, how come we're charging for this? And you know how economists are, they would come back and say, well, there's some value added and we're able to, we need to be charged for this and so on and so forth. And what I learned was that there was actually a bureaucratic response which was just like a $3 million offset to the budget. And so once we overcame that problem we did something that has some really revolutionary potential. We opened up all the data sets, 7,000 data sets going back to, you know, the late 1940s. And we started to switch to try to come up with different ways that people could apply and access this

data. And then connecting it with people's own knowledge and learning and experience so that they can use it and add it to it in ways to help them work through the development solutions.

And just to give you a concrete example, you can now get on the website and you can call up a country and you can see where all our projects are and you can, you know, punch the button and see what the date is on that project and it won't be long before we actually will be able to have through mobile telephony and others people in the community being able to give feedback. So this is such a revolution from a top-down model of the past. So I think in its most institutional form, keeping this process of seeing the bank not solely in financial terms but in the knowledge and learning terms and recognizing, as I just touched on, kind of how the world has changed. The other part of it is, as my remarks already suggested, we're not out of the financial woods so that's going to be a challenge.

HENRY KAUFMAN: Well, let me piggyback a little bit on Marty. You have a new man coming into the World Bank. You're going out. You've had considerable experience. What advice would you give to your successor in managing this organization, some of the things that you have learned?

THE HONORABLE ROBERT B. ZOELLICK: Yes, I'm always a little reluctant on this one just because I have a slightly different view than some people do on some of this. I think when you leave, you leave, and you should let the next person do it. And it's my view that change is

good for an institution. There's things that I hope, as I answered to Marty's questions, that people will continue, but I think it's good for somebody to come in with fresh ideas.

But to try to be responsive for the audience, I guess, what I'll say is I've tried to make a broader point at the bank. And it's because my background is a little bit more on the historical side, and so I tend to look at these institutions in their historical context. And so when I think about the World Bank or the IMF or the WTO, I go back to why they were created. So many people in this audience may know, but some may not. These were institutions that were, at least in their original form, created in 1944 as World War II was still going on, with the idea that people didn't want to repeat the mistakes of the inter-war period between World War I and World War II. And they said, well, there are problems of beggar-thy-neighbor policies on currencies and foreign exchange rate disputes. There's trade protectionism. There's reconstruction, in that case from World War I, or then World War II. There's developing countries. And what's interesting is if you think of those topics, those topics remain very valuable today but the world has been totally transformed.

So part of what I've tried to see as our challenge is how do we modernize multilateralism. These institutions have their imperfections as any public or private institutions do, but rather than abandon them, the question is how do you make them work better? So we've done some things in trying to tap private sector capital flows. I created a subsidiary from IFC, our private sector arm, to tap sovereign funds and wealth funds with equity investments. We support private equity

funds.

So how do you keep in the forefront? And the relation of that to your core question is any big institution has to continue to be prodded for change. And public sector institutions are particularly vulnerable to doing tomorrow what they did today plus one. And multilateral institutions have an additional challenge because they have to reflect in our case 188 shareholders and there's always a temptation for processes and committees to overcome the impetus for change.

So just to give you one, my board of directors is 25 representatives of either countries or groups of countries. They're on site. They have a staff of about 300, a direct expense of about $70 million a year. And that's a slightly unusual governance structure. And so what you have to be careful is a lot of those people are talented. They bring good insights. But the bottom line is you have to keep pushing for change. And there's ways to do it that are more effective than disruptive. So my main advice, but I don't think this will be a challenge for Jim Kim because I think it's what he brings, is whether it's results-based financing, evidentiary-based aspects, information, to keep the learning loops but then keep the process of change because this world is adapting very quickly.

MARTIN FELDSTEIN: We used to hear a lot about the Washington Consensus. And it seems like not only do we hear less about it, but there seems to be a loss of faith in it. Do I read that

correctly? And if so, is it justified? And what's replacing it in the minds of developing countries and development experts?

THE HONORABLE ROBERT B. ZOELLICK: As you know, Marty, there's the Washington Consensus, the core points that were actually written down, and then there's the image of the Washington Consensus. If you go back and you look at, was it William...at the Peterson Institute, who did the...they remain pretty valid points. You know things like macroeconomic stability, things that Europe and the United States might wisely learn today because many of the emerging countries learned the lessons. I think that they are necessary but not sufficient. And I think kind of the lesson that's happened over time, let me give you a very practical example, we've tried to do it. If you go back to the financial crisis in the late 90s in Latin America and East Asia, one could see that macroeconomic stabilization wasn't enough. So that just getting the budget right, if for some reason children don't get proper nutrition particularly in very early periods, if kids don't go to school, you can literally lose a generation.

So one of the lessons that has been learned, and this again comes from some emerging market countries, Mexico was the first, and there's now, Brazil is another well-known example, to come up with something called conditional cash transfer programs. And so they basically help the bottom 15, 20 percent of the population with financial transfers on the condition that children have to go to school and people have to get health checkups. So it's probably done more for women's health than anything in the history of Mexico. The Bolsa Familia Program in Brazil is

based on the same model. But what's striking is this is all done for about a half of one percent of GDP. So if you compare that with U.S. or European social welfare programs, this is done quite efficiently. But we've taken that model and now expanded it to some 40 other countries. And what's, again it goes a little bit to how the bank operates. It's not just a question of the paper or the text, but we can put people in touch with the people who design the programs and the actual task of execution.

In coming out of this financial crisis, also one of the things that I've had our staff do is really to inventory every developing country. Get a sense of the basic safety nets because some countries may not have the capacity of this program but countries such as Ethiopia have done some very interesting things, with the idea that I think we're going to continue to live in a volatile, uncertain world. I don't think we're going to be able to control food or energy prices. We're not going to be able to deal with all of the vicissitudes. But what we can do is have efficient programs to try to make sure those at the bottom don't get crushed and that countries don't lose their human capital.

So I mention this as an example of the types of things that, that's not part of the Washington Consensus. So another idea would be the importance of governance. So I was talking with Donald Kaberuka, the Head of the African Development Bank, at our recent spring meetings. And don't hold me exactly to the numbers, but I think he mentioned to me that of the 54 countries in sub-Saharan Africa, 45 now have proven energy reserves.

Well, the real challenge for that is the lessons we've learned about transparency, governance, avoiding the Dutch disease, inclusive growth. So my view on the Washington Consensus is that it sometimes had an image that maybe would fit a different era. But the fundamentals of the macroeconomics and private property in __ markets remain good, but they're not enough.

HENRY KAUFMAN: Let met shift the conversation just a little bit. We are all held accountable. You raise a lot of money in the financial markets.

THE HONORABLE ROBERT B. ZOELLICK: With a Triple A rating I might add.

HENRY KAUFMAN: Well, the question is how do we judge the efficiency of the World Bank? We more or less know how to do this with private sector financial institutions. But how do we do it with your institution?

THE HONORABLE ROBERT B. ZOELLICK: Very good point. And it's another part of kind of the modernization that I've been trying to drive is that I think we have to be held accountable for results. So we've developed a scorecard that not only looks at our own sort of operational performance but looks at the results of the projects in the countries, and then even goes beyond and looks at the country's performance.

Now we have varying degrees of causation and effect on this. And that's combined with the

openness. So the other part of this open information agenda is that, you know, to try to make available everything. I instituted the first Freedom of Information Policy for Multilaterals based on the U.S. and the Indian examples. And so the notion of connecting a results focus, openness, and being accountable, and to connect this to the broader issue. And many people here who are committed to issues of dealing with poverty in developing countries I think will recognize this. What we have to fight against is the fact that the World Bank or any development organization will often draw some very committed people. And they're working their hearts out to try to deal with some of these problems. But you have to resist the human tendency to say, well, this could have worked. It would have worked. I wish it worked. But you have to be honest and say it didn't work.

So one of the principles I've tried to incorporate as an executive but also with our systems is to recognize that if poverty were so easy to overcome, somebody would have done it long ago. These are not easy issues. But you have to build in feedback loops and be honest and try to learn from the mistakes. And part of the point of the open information in a developing democracy is you also have to do it with the people there.

And so just to give a small other example, I'm sort of piloting a social accountability fund to try to help civil society groups be able to participate in the monitoring and evaluation of projects taking part in their countries. Now this is not only to lead to better performance, but frankly as we saw across North Africa, the pure economic growth isn't enough when people don't feel they

own it. And it's not enough for the leaders of the country to own it, but the people in the country have to feel that they own it. So this is part of a broader, in my view, kind of shift in trying to think about how one does development and comes up with development solutions.

MARTIN FELDSTEIN: You said a lot about China in your opening remarks and the scale of China and about your joint report with the Chinese. The Chinese often say they have a better strategy for development than the Western strategy –less dependence on markets, more central guidance, more public ownership. How does that go over in the developing world? And what's your own take on it?

THE HONORABLE ROBERT B. ZOELLICK: Well, the World Bank relationship with China is a very intriguing one. And it's also interesting for me with some of the broader, going back to the point about being open and sort of debate these issues with the broader public. The World Bank has an extremely good brand in China going back to Robert McNamara and Deng Xiaoping in 1980. And it turns out, these are the benefits that I inherited, that there were various points in the Chinese reform process where World Bank teams had long, analytic discussions. There's one that's gone down in lore of a three or four-day trip down the Yangtze River that was sort of a floating seminar. And these, I think, contributed to the type of process that is important for development where the Chinese owned it, but they were very open to taking ideas from others.

And so this recent report that we did, and this is a way of coming to your question, was intriguing to me because here's an economy, it's grown 30, you know 10 percent a year for 30 years, but the Chinese approached me two years ago and said, you know what, we're worried about some of these issues. And we would like you to propose to our leadership that we do some joint work on these and how to avoid the middle-income trap. And Li Keqiang, the man who is likely to be the next premier in a sense was the primary adopter of this. Xi Jinping and President Hu and all sort of blessed it, but he's the one who I regularly came back to. We did it with the Development Reform Council, research council, of the State Council which is the main think tank.

And actually, Marty, what I was struck by was that as opposed to having hubris, here they're coming out back to the World Bank, frankly I'm an American at the World Bank, and saying what else should we know? What else things could we think about? So I actually find China to be quite open to discussion and debate about ideas. And of course they reserve the right and they take account of things, but part of the challenge again for the bank actually is sharing some of that experience with others, and I think this is part of the transformation.

And just to give you, to put a bank issue in a political economy context, when I came to the bank one of the big issues are why are you dealing with middle-income countries? You should just deal with the poorest countries. If you view the World Bank as a multilateral institution as I do, as part of a larger system, you have sovereign states but these are the thin tissue that connect

them, it would be a mistake of huge historic proportions to push the middle-income countries out of the system because frankly my goal would be over time I want to also get their resources, their trade, their investment, their knowledge to help other countries. And that's the whole South-South agenda. To say nothing of the fact that about 70 percent of the people living under $2 a day are still in so-called middle-income countries.

So part of the institutional and executive challenge is how do you connect this experience to others? So when you asked how this goes down with others, well, frankly there's an interest in many emerging markets about how China worked. There's more recognition than people think about, you know, some of the downsides. And the Chinese are pretty open about, for example, the costs of environmental cleanup if you don't pay attention to environmental issues.

But just to give you a little example of the types of thinking that, I don't want to overstate but I think is possible out there, in the next five years there are going to be more people leaving the workforce in China than coming in. So one of the aspects of this study is that if you're going to have higher wage rates in China, you're going to have higher productivity growth, you're going to rely less on the low-wage labor model they've had before, and so there are aspects about innovation and it can relate to IPR and service sector and productivity, but another possibility is what opportunities does this create for other countries? So Justin Lin, our chief economist from China, hatched the idea, he mentioned that there's about an estimated 85 million low wage manufacturing jobs in China. If you take all of Africa, north and south, there's probably 8 to 10

million.

So what can we do in talking with the Chinese to create the right enabling environment, the right economic zones – energy, customs, logistics, property rights, labor training– to move some of these facilities. Now even if you just move 5 million of the 85 million, you've improved by 50 percent which could, as you know, the multiplier effects of these things start to become important in terms of knowledge and learning. And frankly when I came to the bank in 2007, one of my worries for sub-Saharan Africa was would China dominate this space so much that Africa wouldn't be able to do what the East Asian economies does. To show us how fast it's changing, and in very practical terms, you know, just again to give you one small example, there's a shoe operation from Guangdong, China which is a higher wage area moving forward, that's created about 500 jobs already in Ethiopia. They're going to do 2,500 by the end of the year and within a couple of years they expect 25,000 jobs. So these are the opportunities that one can create in the system.

HENRY KAUFMAN: Well, but let me go back...sorry...

ANDREW TISCH: If I may, I'm going to cut the conversation off here because lunch is about to be served. Anyway, gentlemen, I want to thank you very much for an interesting conversation. Thank you very much, Mr. Zoellick, for your remarks. Our next event is June 6. We have Gene Sperling at a lunch and he is the Director of the National Economic Council.

Anyway, gentlemen, again thank you very much for your insights and your observations, and lunch is served.