Since its formation in 1994, the Forum has examined the major economic and political concerns of the day, often bringing to light issues that were not yet front and center on the world stage.

If I think of the most vivid conversation in the history of the Forum, it was in Aspen on July 28, 1998. The speaker was Anthony Lake, who had served for several years as a national security advisor to President Clinton. His presentation was about how different national security was in 1998 in contrast to 1988, before the Berlin Wall came down.

At dinner later that night, Tony continued to talk informally about security threats: “The real bad guy in the world is not Saddam Hussein, as most Americans believe, but somebody that most of us have never even heard of. He’s from a wealthy construction family in Saudi Arabia. His name is Osama bin Laden.”

Indeed, most of us were not familiar with that name. Nine days later two US embassies in Africa were bombed and Osama bin Laden became headline news.

On this and other issues, the Forum has been way ahead of its time. We were talking about major events and potential crises before they were on the front page of the Wall Street Journal, before they were in the Economist every week.

In 1995 Peter Widmer hosted the Forum in Zurich and we got a firsthand look at the competitiveness of the European Union. In 2000 we went to China and saw how that country was preparing for membership in the World Trade Organization. In 2004, we were in Central Europe immediately after 10 new countries were welcomed into the EU.

In 1998, I hosted the Forum in Denver. That year was filled with the plot twists that would become routine in the next decade of US foreign policy. In 2000 we went to China and saw the economic power and their management practices. In 2004, we were in Central Europe immediately after 10 new countries were welcomed into the EU.

Credit goes to the Institute’s Global Advisory Board, a group of leading executives from different parts of the world, for helping to identify the issues that are relevant to the business community.

The Forums are where we bat ideas around with people who are working and living in the global economy and track shifts in the economic and political landscape that are destined to affect the way US businesses operate abroad. These ideas help shape our thinking and impact the programs we offer at the CIBER (Center for International Business Education and Research). We then try to influence university and business school faculty about the teaching of international business and its many facets.

To date the Forum has devoted 14 or 15 sessions to security issues. No other school in the 30-member CIBER network has done as much on this subject.

The Forum is unique among the CIBERs. It has enabled our Colorado CIBER to distinguish itself from Duke, Columbia, UCLA and other top CIBER schools. Nor does the university have another way of engaging the community like we do at these twice yearly sessions.

For better or worse?

When I started the Institute in 1988, the world looked much different than it does today. What occupied our attention then? And what forces have been at work in the intervening years that have shaped this changing world for better or worse?

In the 80s Japan was the dominant economic power and their management practices such as TQM-Total Quality Management, quality circles and teamwork were inspiring businesses around the globe. In the United States, we were reengineering and downsizing in an effort to improve productivity and meet the competitive threat coming from Japan.

On November 9, 1989 the Berlin Wall

Global Executive Forums are held twice annually, with each agenda focused on a global business theme as well as a geopolitical theme. Following each meeting, the sessions are summarized in a Global Executive Forum Report and disseminated to colleges of business across the nation. Information: Phone 303-556-4738; Fax 303-556-6276; Web http://www.cudenver.edu/inst_intl_bus/main.html
Donald L. Stevens is managing director of the University of Colorado at Denver and Health Sciences Center's Institute for International Business and director of the Institute's Center for International Business Education and Research (CIBER). He holds an appointment as professor of finance at the Business School, and was dean of UCDHSC's College of Business & Administration from 1981 until 1991. Prior to coming to Colorado, he served on the faculties of the University of Tennessee and the University of Illinois and received his Ph.D. in business administration/finance from Michigan State University.

China is a major economic force and like Japan in the 80s, it will dominate the way we think about business.

came down and since then West Germany has spent US$100 billion each year to integrate East Germany into the rest of the country.

In 1989 in China's Tienmen Square, the slaughter of protesting students reminded us that China was not a democracy. The hardliners and the military still held power. China was emerging as Asia's major economic power, replacing Japan and positioning itself to overtake the East Asian "tigers," (Singapore, Taiwan, South Korea, Thailand) which were enjoying tremendous economic growth.

A succession of happenings through 1990-91 led to the disintegration of the Soviet Union. I think now of this event as something like a grenade going off, with the countries that had been under the Soviet flag breaking away and heading in all directions politically and economically. Fortunately, many of those countries have coalesced and aligned in the direction of the European Union. Czechoslovakia split up into two countries, the Czech Republic and Slovakia.

Throughout the 90s, as the EU grew stronger, Japan's real estate bubble broke and they seemed unable or unwilling to move towards a restructuring of their economy. They decided to wait it out, and they're still waiting.

Looking back 10 to 15 years, these were some of the events that dominated our thinking.

Where are we today? Japan's economy remains stagnant, although it started to pick up this last year; China is the undisputed Super Tiger of Asia, and the EU has grown from its original 15 members to 25 and more countries are lining up to join. India is now a rising star, and globalization and terrorism dominate the news.

What should we be thinking about in the next 15 years? What's going to shape how we do business and how we live? Three major forces are at work.

European Union. The EU is a great force for peace and democracy with laws and institutions that are as strong as anywhere in the world. But what worries me is the social agreement the EU has made with itself guaranteeing labor generous retirement, health and vacation benefits. The yearly bill is too big for the EU to pay, especially given its rapidly aging societies and weaker economies of the new members. How the EU can renegotiate benefits while accommodating growth and dealing with tax and wage issues will be important not only to its future but to the future of Europe and the world.

China. The Forum started looking at China and the globalization of work long before either one became a big political issue. Jobs are very different today than they were a generation ago when they were US based and performed by US workers from start to finish. Today some or most of the processes that go into the manufacture of a product are outsourced to China, and workers here have to learn how to manage all of these processes.

Although China is a magnet for businesses looking for cheap labor, China has big work force issues of its own. Workers are disenchanted with low factory wages on the east coast and are looking for opportunities in the west, closer to their rural roots. China will not be without problems going forward, but this huge country will continue to dominate the way we think about business.

India. With one billion people and a per capita economic growth of 6 percent to 7 percent over the last decade, India has moved quickly into world class services. The infrastructure problems that China overcame to be competitive are problems that India needs to overcome to move its people towards the middle class. But these problems will take hundreds of billions of dollars and more than a decade to fix. So the development of India is going to be very, very different from what China experienced. Both countries have many millions of workers moving into the global work force: 800 million in China, 600 million in India. The US work force is about 140 million.

What's next for the Forum? We've been to Europe, we've been to China. Next January we will do a Forum in India. What is their high-tech sector all about? How have they been able to reinvent themselves as the service provider to the world? How are workers trained to meet the needs of US companies? What threats, if any, does their growth pose to US businesses?

We need to be on the ground to see for ourselves what works, what doesn't and what lessons we can take away.

The CIBER designation*

The Institute for International Business is partially funded by a grant from the U.S. Department of Education through its CIBER program. The U.S. Congress established the program to help a select group of universities provide U.S. companies with the internationally oriented education and research they need to successfully compete in a global economy. There are currently 30 institutions of higher education in the program nationwide.

The IIB serves as the institutional home of UCDHSC's CIBER. The U.S. Department of Education first designated IIB as a CIBER in 1993 and renewed this designation in 1996 and again in 1999. Later this year the IIB will once more be competing for a CIBER grant so we can continue to support both the business community and university faculty with programs designed to increase their effectiveness in matters of international business. The Global Executive Forum is one of these programs.

What do the next five years look like for our CIBER and for global economic and political issues? Regardless of where the world is headed, the Forum will be instrumental in keeping us informed and ahead of the curve.

*Center for International Business Education and Research
India: Opportunities and risks in a changing society

If there’s one word that defines India, it’s change. Back in the 80s the country was on the verge of economic collapse; today, after a series of policy changes reset the country’s direction, India is the fourth largest economy in the world (after US, China, Japan) as measured by purchasing power parity.

“In the 80s, there was no growth and unemployment was very high,” said Dipak Patel in his address to the Global Economic Forum. On top of that, “certain states wanted to declare themselves independent from India.” The country’s 28 states present unusual challenges. “Each state is different with its own language and its own way of dealing with people.” The clothes people wear and the ethnic composition also are different from state to state. “It’s like 28 different countries within a country.” However, “English is the language of business.”

As a result of reforms initiated in the 90s, the country began to grow. “So India has an economy that’s very new, only 10 years old,” said Patel. “Before that, it was just a country with a bunch of bureaucrats, a bunch of licensed businesses, lots of people, lots of entrepreneurs but no opportunities.” Patel, who travels there frequently, said, “Over the last 10 years so much has changed. Every time I go I feel like I’m in a different place.”

There are two annual events that impact the economy. One is the budget which is drawn up in March. “The government decides where they’re going to put the money, how they’re going to tax people, whom they’re going to tax.” The second event is unpredictable: it’s the monsoon. When it arrives on schedule it brings three months of rain which farmers depend on in a land lacking irrigation systems.

“Whether there’s too much rain or not enough rain, people’s spending habits change even if nothing has changed in the economy. Consequently, every industry suffers.” The importance of agriculture is being overtaken by the services sector, but agriculture still accounts for 24 percent of the GDP.

Opportunities

According to Patel, investment opportunities exist in every area, but the most attractive include banking/financial services, pharmaceuticals, retail, media and entertainment, hospitality and leisure, infrastructure.

■ Banking/financial services. The banking system is undergoing change as the government denationalizes the banks they nationalized in the 50s and 60s to keep them from going under. In the public sector, 60 percent are still owned by the government. The rest are private sector banks. “In the past, banks made only commercial loans but now they are willing to give personal loans. And they have ATM networks, credit cards, debit cards. So they offer a lot more services than they used to provide. Banks are just taking off, growing at 20 percent a year. And unlike the 80s when many of these banks had 20-25 percent nonperforming loans, that number is now less than 1 percent, said Patel.

■ Pharmaceuticals. Under the Indian Patent Act of 1970, patent protection on drugs lasts only seven years. This, and the fact that Indian drugmakers have been able to reverse-engineer drugs invented elsewhere, has made India a major producer of generic drugs. However, starting this year, as part of its admission to the World Trade Organization, patent protection will be extended to 20 years. Said Patel, “The protection will be on the process not on the drug formulation, which makes medicine affordable for Indians.”

■ Retail. “Department stores and malls are still very new to India,” said Patel. Except for three department store chains, most retail is characterized by mom-and-pop ownership. Pantaloon is the largest of the department stores with 13 Pantaloons stores, 9 hypermarkets and 13 Food Bazaars.

■ Media and entertainment. India’s entertainment industry is set to grow rapidly over the next few years, reaching $14 billion in revenues by 2010, according to a study by KPMG and the Confederation of Indian Industry. Growth is attributed to the affluence of a burgeoning middle class and its de-

Indian Pharmaceuticals Outsourcing

• $126 billion of US branded drugs going generic between 2004 and 2013.
• 30 years of intense domestic generic competition has resulted in world-class chemistry and manufacturing skills. Cost advantages are 50-70 percent of Western producers.
• India is already 2nd largest filer of generic drug applications with FDA, after US companies.
• India has largest number of FDA approved plants outside US.
• Entire Indian pharmaceutical industry trades for less than the market value of Israel-based TEVA Pharmaceutical Industries, which ranks in the top 25 of the largest generic pharmaceutical companies in the world.
• Pfizer, Eli Lilly, Bristol Myers, Squibb, Ivax, Mylan, Barr, Teva already sourcing substantial chemical ingredients from India.

Dipak Patel currently researches Indian equities at Passport Capital. Prior to that he worked as a senior analyst at Franklin Templeton Investments and covered Templeton’s global and emerging markets funds. He also researched small and mid-cap securities for a proprietary trading desk. Patel holds a bachelor of science degree in finance from New York University at the Stern School of Business.

“Over the last 10 years, so much has changed. Every time I go back I feel like I’m in a different place.”
Unlike the people from India Americans are likely to run into in the US, not everybody in India is well educated.

India snapshot
- 1 billion-plus population
- 50% of population is under 25 and this segment has heavy consumer demands.
- Consumers have increasingly Western tastes.
- The historically high savings rate is plummeting.
- Domestic goods are in demand.
- The population is mostly English speaking with Western business culture rooted in English common law.
- Corporate governance, management and transparency are improving.
- Personal savings are beginning to move from cash to consumption and investment.
- The middle class has been growing over the past 10 years.
- A graduate engineer earns $3,000 a year, not much by US standards but in India you can buy a house for $2,000.

-Dipak Patel

mands for more TV programs, music, books and Internet access. Also, the industry is a major exporter of both finished products and services.

- Hospitality and leisure. The advertising sector of this industry “is going very strong,” said Patel. Domestic travel is booming, again due to the middle class. The Hotel Benchmark Survey by Deloitte reported double-digit growth in the 12 months from March 2004 to February 2005. But growing the numbers of international tourists is a challenge due to the poor quality of India’s roads, ports, rails and airports.

- Infrastructure. Up until recently infrastructure improvements were stymied by a lack of political will and a lack of incentive in the private sector to invest in projects because of high interest rates and government regulations. That is now changing, said Patel. People are demanding roads and the government is responding with five-year grants to encourage private sector participation. Tolls on new paved roads that run nonstop from city to city are gaining acceptance as drivers find they save considerable time. A typical trip that used to take seven hours takes only three hours on a new toll road.

Patel named a couple of developing industries worth keeping an eye on:

- Autos. In the past, there were only two models of cars and three models of motorcycles available in the domestic market. “Now we have 30 models of motorcycles and 18 models of cars,” said Patel. “Fast-engine cars have become a status symbol. If you don’t have a car parked in front of your house, nobody is going to marry your girls. That’s something that has changed.”

- Power and energy. “India still has a long way to go before this industry becomes profitable because some of these power generation companies are still owned by the government and they’re very inefficient,” said Patel. Due to the way power is transmitted, it has been easy for people to acquire electricity without paying for it. “About 50 percent of the transmissions have been lost. That has come down to 30 percent and should go down to 10 percent by the end of the next decade. Companies are putting this additional income back into the business.”

Risk factors

On the one hand population growth will continue to produce more workers, outpacing Brazil, Russia and China by the year 2030. On the other hand, more people will put more pressure on systems that so far have proved inadequate for the masses. A guest said, “The large growth of population suggests there will be a large growth in the economy, but the country doesn’t have an education base to support it.”

Patel agreed. “Education is one of the bigger risk factors.”

Unlike the people from India Americans are likely to run into in the US, not everybody in India is well educated. The literacy rate has been rising, from 40 percent to nearly 65 percent, but that number doesn’t tell the story. “In most countries literacy is defined by the ability to read, write and do simple math. In India the person who is considered ‘literate’ can barely read.”

This is surprising considering that education is free until the 12th grade. College bound? The cost is no more than $50 for a whole year and is free for females. “You’d have to go to a private trust-funded college, not a school in the public sector. Unfortunately, it’s only the people in the middle class who have access to higher education. “If you’re in the lower class, you were born into poverty and it’s very hard to get out of it,” said Patel.

“If your father is a farmer you’ll become a farmer; if your father is a barber you’ll become a barber. It’s something India inherited from its caste system.”

A guest pointed out that only “43 percent of India’s women are literate compared to 85 percent in China. Chinese women working in a textile mill in China will produce 20 percent more than an Indian woman in an Indian plant, which is probably attributable to the quality of education,” said the guest. “This is a giant issue and something India is failing on right now.”

Without a doubt, education is linked to productivity, Patel said. “Everybody thinks China has the cheapest labor in the world but actually India has the cheapest labor. The product delivery is not as high as in China so that’s why it comes out more expensive.”

Among the other risks are the pace of reforms which could slow or stop altogether, and the specter of AIDS. “One half of 1 percent of the population is infected with AIDS, which is lower than other parts of Asia. But the disease, which used to be an urban disease until just five years ago, is spreading to the rural areas. This could be the largest risk to India’s story because there is no education about it,” said Patel.

“There may be a lot of problems in India but when we’re looking at market opportunities there are a lot of people there that have purchasing power,” said a guest.

“The society is changing,” said Patel. “People are wanting more for their lives. We are changing out blue collar workers to white collar workers. It’s an enormous task because their education system has failed to train them so now businesses have to do the job. And that’s a cost added to your P&L.”
Except for China and Russia, the beer market is a pretty stagnant business around the world. There’s zero growth.

Global beer brewing industry and the Coors Molson merger

The global beer industry is consolidating, said Peter Swinburn in his address to the Global Executive Forum. “Consolidation started 10 years ago and probably has 10 more to go before it winds down.”

With the top 10 brewers vying for the No. 1 position, competition and the pressure to “do lunch or be lunch” is driving mergers and acquisitions around the world, he said. “However, antitrust issues are going to inhibit consolidation as the deals get too big and too complex,” said Swinburn.

Beer is one of the biggest consumer goods categories in the world, just short of $200 billion in retail value and 1.45 billion hectoliters in volume. “We use volume as a proxy for sales because it’s very difficult to get up-to-date, reliable financial information on any company. And many of these companies have other interests as well, such as soft drinks, so it’s hard to separate out the beer portion of the revenue.”

China is the biggest market for beer followed by the US, Germany, Brazil, Russia, Japan, UK, Mexico, South Africa and Spain. “The paradox in China is that although the retail price of beer is very low in terms of the market, it has very high profit margins as far as international players are concerned.”

Having said that, Swinburn noted that “except for China and Russia, the beer market is a pretty stagnant business around the world. There’s zero growth.” “Why then,” a guest asked, wouldn’t you look for higher growth businesses to diversify into?”

“I’m not sure we wouldn’t do that going forward,” Swinburn said. But he pointed out that most of the recent history of beer companies that diversified their holdings had results that fell short of expectations. “When they diversified they lost focus and the availability of capital became extremely tight. But even in static industries, you do get growth spurts along with plateaus and declines.” Despite the zero growth, Swinburn described the dynamics of the beer industry as “pretty incredible. There are brands that are growing spectacularly.”

International player

The marriage of Coors and Molson created a company with an annual volume of 60 million hectoliters and net sales of more than US$6 billion. The new company is the fifth largest global brewer, with brands that include Coors Light, Molson Canadian, Molson Dry, Carling, Kaiser, Coors and Zima XXX. Molson Coors Brewing Company is the leading brewer in Canada, the second largest in the UK, and the third largest brewer in the US.

“We’re a relatively small No. 5 in the US; we have only 11 percent of the market. That’s not a good place to be in your home market. The merger gives us a huge advantage because basically our home now becomes Canada and we’ve got 42 percent of a very profitable market there. But there are a couple of problems the company has to solve before it can move up in the global ranks.

The first is a lack of international management experience and processes. The second is the size of the Coors brewery. “Coors is the biggest brewery in the world and the most inefficient, which piles on production costs. Efficient breweries produce about 8 million-10 million hectoliters maximum; ours produces 30 million hectoliters,” said Swinburn. “And because it’s stuck in the middle of nowhere the distribution costs are high. But with the merger we’ve now got breweries across the whole northern United States and that solves a huge amount of production and distribution issues.

“Two years ago Coors was just in four of the top 10 markets -- China, the US, UK and Japan. We’re now in seven of the top 10 and we’d like to be in eight pretty quickly. If you want to be an international brand, you have to be where people are drinking beer,” said Swinburn. Coors Light is the only chance we have of becoming an international brand. Possibly Carling can make that leap as well. So that’s what we need to concentrate on and we’re pretty focused. We’re learning how to be successful.”

### Top 10 global brewers after Coors Molson merger*

<table>
<thead>
<tr>
<th>Rank</th>
<th>Brewery</th>
<th>Volume</th>
<th>Ownership</th>
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<tbody>
<tr>
<td>1</td>
<td>InBev</td>
<td>200</td>
<td>Public/family control</td>
</tr>
<tr>
<td>2</td>
<td>Anheuser-Busch</td>
<td>143</td>
<td>Public</td>
</tr>
<tr>
<td>3</td>
<td>SABMiller</td>
<td>109</td>
<td>Public</td>
</tr>
<tr>
<td>4</td>
<td>Heineken</td>
<td>103</td>
<td>Public/family control</td>
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<tr>
<td>5</td>
<td>Molson Coors</td>
<td>60</td>
<td>Public/family control</td>
</tr>
<tr>
<td>6</td>
<td>Carlsberg</td>
<td>51</td>
<td>Public/foundation control</td>
</tr>
<tr>
<td>7</td>
<td>Scottish &amp; Newcastle</td>
<td>48</td>
<td>Public</td>
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<tr>
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<td>Asahi</td>
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<tr>
<td>10</td>
<td>Tsingtao</td>
<td>22</td>
<td>Public/government control</td>
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*Prior to the merger, in 2003/04 Coors was ranked at No. 8. The top five players account for 41 percent of the market.

*Source: Peter Swinburn*
India’s software services sector is growing by 20-25 percent a year; the US accounts for 65 percent of this growth.

Globalization of work: Outsourcing and offshoring

First it was manufacturing that crossed borders and oceans in search of cost efficiencies, now it’s the service sector that’s making the leap in increasingly larger numbers, said Martin Kenney in his address to the Global Executive Forum.

Just as China is the manufacturing center of the world, India is fast becoming the country of choice for the services sector. “We might think of physical work being outsourced to China and mental work to India” said Kenney.

“Services have been globalized and any activity not requiring direct interaction with the local marketplace or immediate physical delivery is susceptible to offshoring.”

Kenney clarified the terms offshoring and outsourcing. When a company in the United States contracts with another US company to perform specified functions, it’s called outsourcing. When a US company outsources to a company overseas, it’s called offshoring. “Offshoring can be accomplished either through a subcontractor such as Accenture or Tata Consultancy Services, or through a wholly owned foreign subsidiary or a captive unit in an existing overseas firm.”

The big growth in offshoring has been in services. “If you have kids, you probably don’t expect them to be a production engineer or a factory worker. You expect them to go into some of the service sectors, and that’s where the growth has been in the US economy, accounting for nearly 40 percent of private employment in 2003.

“And that’s why India is so interesting and why national companies to look for ways to shave costs. India became the solution, with labor costs at 25-40 percent of what they are in the United States. The savings are not limited to just entry level or call center jobs, for example, in the US someone with five years of Java EE experience and a CS/EE degree earns $55,000-$80,000 plus benefits; in Bangalore the salary is $6,000 including benefits. A Ph.D. statistician in India earns $30,000-$40,000 a year compared to $200,000 in the US. Furthermore, Indian workers are skilled in a wide range of categories and are willing to perform the more mundane tasks that US workers are less inclined to do.

Being able to realize significant savings is motivating more and more corporations to centralize certain global processes in India. IBM, Hewlett-Packard, Accenture, Dell, HSBC, Citicorp are all growing their Indian operations by 50 percent a year. JP Morgan Chase and Progeon are growing at 50 percent.

The processes being relocated go beyond software services. They include call centers, R&D, medical image analysis, data entry, equity analysis, financial analyses, human resources, global purchasing management. “We’re starting to see some pretty sophisticated equity analyses going on in India.”

Kenney talked about a multinational corporation that offshores its finance and non-finance processes to India. A whole spectrum of functions falls under those headings: sales administration, revenue accounting, accounts payable/receivable, vendor data management, inventory accounting, a customer re-

Can the US economy adjust?

A remarkable aspect of service offshoring is the rapidity with which it can occur. Manufacturing’s movement offshore was a gradual migration that began in the early 1960s. Though punctuated by dramatic factory closings, there was an opportunity for the US economy to adjust. This may not be true in services where the “objects” are pixels and electronic pulses that can be transmitted by photons and radio waves (Cohen et al. 2000; Kenney 1997). A number of the firms we studied in India experienced vertiginous growth as they expanded from start-up to 5,000 employees in less than three years. When a large number and variety of firms experience such growth rates, the cumulative effect can be enormous indeed.

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--Moving Services Offshore: A Case Study of an U.S. High-Technology Firm

Martin Kenney & Rafiq Dossani
Senior Research Scholar
Asia-Pacific Research Center, Stanford University
sponse center and much more.

As multinational companies ramp up their activities in India, they are beginning to give select workers decision-making responsibilities, “something that two years ago I didn’t think would happen,” Kenney said. “They are not making the final decision but they’re doing judgment-based work. So they’re going beyond the preparation of statistical reports and other routine work.”

To keep this development in perspective Kenney stressed that “we’re still talking about very small numbers, one-tenth of 1 percent of the Indian population.”

A pressing issue

How and to what extent offshoring will affect the career paths of US college graduates in the future is a pressing issue. Kenney was told by a woman from a major international bank that the bank is increasingly hiring junior analysts in India whereas it used to hire graduates from the top Ivy League schools in the US. A graduate with an economics degree would become a junior analyst at a starting salary of $45,000 a year and move up rapidly from there.

The bank will still hire in the US, Kenney was told, but the new hires won’t be paid bonuses anymore because they’ll be working on the same team with Indians who are being paid far less. Looking down the road 10 years, she said it won’t make sense economically to have a junior analyst in the US.

How can American university graduates develop the skills they need to become senior decision makers of an organization if they can’t get work at the entry level?

“Many universities are thinking about what the American engineer of the future looks like,” said Kenney. “He or she probably looks more like a networker that pulls together different elements from different locations around the world. How many of those jobs will be available is another issue, but those are the kinds of things educators are now thinking about, particularly in engineering. In the social sciences, we have not yet started to think about the effects of services offshoring on the students of the future.”

All is not rosy

India’s continued growth depends on how it deals with challenges that are clamoring for attention.

“Indian universities are in trouble because they’re losing their smartest mathematicians, statisticians, etc. to global companies with offices in India,” said Kenney. “An Indian professor gets paid little more than a call center employee and can be hired away for $20,000-$25,000 a year.

“The best graduate students in India have come to the United States because, generally, the graduate level education in India is poor to mediocre.

“The Indian government is aware of the problem; whether they can do something about it is another question.” Lacking adequate funds, the government is moving slowly in making improvements to its university system. The Chinese government, meanwhile, is making a huge investment in upgrading its universities, knowing that’s the only choice if they’re going to compete in the global arena.

“Another problem for India is a lack of seasoned middle level management, a condition that also afflicts China. But it’s particularly evident in the services sector where the growth is so rapid that you’re a seasoned manager if you have a year or two experience.

“How large will this services offshoring be? It will be a repeat of manufacturing. How fast will it develop? Operations are growing at 30 percent per annum so it could be very fast if it continues.

“Nowadays a Silicon Valley venture capitalist tells an entrepreneur that they must have a strategy about India and China,” said Kenney. “As a result, firms are global almost from their inception. The team starts in the valley but almost immediately they’re building a software operation in India as back office and they’re thinking about manufacturing in China.”

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Policy dilemmas at state and local levels

The relocation of services offshore has the potential to reorganize the global economy in the same way as the movement of manufacturing to China has been emblematic of a reorganization of goods production. For the developed nations already reeling from the continuing loss of manufacturing jobs, the emergence of India and the Philippines as outsourcing options for firms aiming to lower the costs of providing services creates significant policy dilemmas. State and local governments are considering laws forbidding the offshoring of government-related services. These protectionist responses may increase if the current trends continue but are unlikely to affect private sector decisions.

--The Impacts of Service Offshoring on Nonmetro America: Thinking about the Future Kenney & Dossani
China is reluctant to control consumption of key resources through pricing based on supply and demand.

**China’s trade strategies:** Searching for critical resources

In response to China’s growing demands for resources and its inefficient consumption of those resources, the government has adopted a two-pronged strategy to conserve existing supplies and develop new sources of energy and water, said Minxin Pei in his address to the Global Executive Forum.

“One is what I call internal response and the other revolves around external strategies,” said Pei.

**Internal strategies**

The internal response encompasses limited policy reforms to increase efficiency. “China is going to impose one of the world’s most enlightened energy efficiency measures which will set relatively high standards for vehicles,” said Pei. “Toyota is going to manufacture its Prius in China on a very large scale, and the use of hybrids will be encouraged.”

To boost energy production, China plans to expand the number of nuclear plants in the country, said Pei. Right now nuclear plants generate only 2.3 percent of all energy production. The government hopes to increase that to 6 percent by 2020. Meeting this goal is an expensive undertaking, “involving building something like two nuclear plants a year for the next 15 years” at an estimated cost of US$48.3 billion.

“If the massive inefficiencies in the system can be corrected, the results are going to be very, very impressive,” said Pei, pointing out that China can achieve 10-20 percent savings in electricity usage if good standards are introduced and enforced.

Inefficiencies are only half the problem; consumption is the other half. Market mechanisms would help control consumption of key resources based on established principles of supply and demand, but the country is reluctant to employ these, Pei said.

“For example, gasoline prices in China are lower than gasoline prices in the US. Today in California we paid $2.40 a gallon; in China the price is $1.70 a gallon. Why? Because there’s no tax on gasoline. And industrial use of water is ridiculously priced at the lower end.

“China is a believer in administrative solutions so introducing efficiency improvements is viewed as much more important than using market methods to cut down on usage.”

Administrative solutions are evident in some large infrastructure activities the government has initiated: power plants, pipelines to pump natural gas from central Asia to China’s east coast, a water transfer project to move water from the south to the north. Pei calls these undertakings a “brute force approach that is risky and fails to deal with the source of the problem, the lack of a market mechanism to curb demand and consumption.”

**External strategies**

Resource constraints will determine the pace of

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**Demand for resources outpacing supply**

“China is short on all kinds of resources -- oil, water, minerals,” said Minxin Pei. And demand is outpacing the country’s ability to supply the needed resources in an efficient, timely manner.

“One of the reasons China is now bumping up against resource constraints is because it has chosen a manufacturing-led growth model. The industry & construction sector accounts for 52.9 percent of the country’s GDP. (This sector is 28.4% in India, 19.7% in US.) And of course manufacturing is enormously energy intensive.

“China is one of the least efficient users of energy. Its energy consumption per unit of GDP is eight times greater than Japan, six times greater than the US and three times greater than India.

“The country’s steelmaking production capacity is 216 billion tons — more than the US, Japan and Germany combined. To support that production you need a lot of power plants.

“Oil production has peaked at little more than 3 million barrels per day, but demand is going to continue to grow.

“China has the largest coal reserve in the world, but its production capacity is already at 1.9 billion tons a year and there are limits to additional production. Furthermore, the coal mines are in the north while the bulk of demand is in the industrialized parts of the south. So the coal has to be transported from north to south. And because there’s no water in the north to wash the coal, it has to be transported dirty. It’s not a very economical way of getting energy.”

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China's growth, which is why the country has extended its global reach and scope in securing supplies of critical resources.

"China appears to have a very high level of tolerance for risk, both political and financial," said Pei. "They have used very aggressive tactics to try to buy equity in companies all over the world, placing more importance on direct control of assets than on potential financial returns.

Another tactic that China favors is entering into long-term contracts that establish fixed pricing "because the government is loathe to subject itself to the miseries of fluctuations in market prices."

Political risks involve some of the countries China does business with, such as the "pariah states of Sudan, Iran and Venezuela. China imports 70,000 barrels per day of oil from Sudan. China also has multi-billion dollar supply contracts from Canada and Australia, which are far more stable.

"The Chinese government has given the quest for external resources its highest attention," said Pei. "President HU Jintao has turned himself into China's chief acquisition officer. On his first trip abroad he visited Gabon to secure contracts and supplies."

"Wherever China wants makes a serious effort to gain access or control of a desirable asset, it gets squeezed out by established players and multinational corporations," said Pei.

"China wanted to buy a piece of a really nice oil field and BP and other petroleum firms said no. China will always bid much lower for developmental rights, thus squeezing the profit margins of companies with which they contract.

There are foreign policy implications to China's strategy; China's interests are impinging on America's interests; the US doesn't like the fact that China is investing in Iranian oil fields and getting on friendly terms with countries that are antagonistic to the US. "China has been very careful not to provoke a foreign policy response in the US Congress," said Pei.

"Because of its aggressive tactics, China is arousing fear, resentment and resistance in developed countries and setting itself up for a backlash in developing countries."

Despite the problems, Pei sees a brighter side to China's future, provided it introduces more market mechanisms, improves energy efficiency and shifts the economic base from manufacturing to a strong services sector which is far less reliant on resources. Pei believes that this shift will occur in the next five to 10 years.

"If these adjustments are made, "China is going to do better than I think my fears would first lead me to believe." ◆

### China's resources

<table>
<thead>
<tr>
<th>Resource</th>
<th>Population: 1.3 billion</th>
<th>Industrial production growth rate: 17.1% (04 est)</th>
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<tbody>
<tr>
<td>Electricity</td>
<td>Production: 1.91 trillion k Wh (03)</td>
<td>Consumption: 1.63 trillion k Wh (03)</td>
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<tr>
<td>Oil</td>
<td>Production: 3.392 million bbl/day (03 est)</td>
<td>Consumption: 4.956 million bbl/day (02)</td>
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<tr>
<td>Natural gas</td>
<td>Production: 3.5 billion cu m (03 est)</td>
<td>Consumption: 29.18 billion cu m (03 est)</td>
</tr>
<tr>
<td></td>
<td>Proved reserves: 2.23 trillion cu m (04)</td>
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</tr>
</tbody>
</table>

Source: CIA World Factbook 2005

### India's resources

<table>
<thead>
<tr>
<th>Resource</th>
<th>Population: 1.1 billion</th>
<th>Industrial production growth rate: 7.4% (04 est)</th>
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<tbody>
<tr>
<td>Electricity</td>
<td>Production: 547.2 billion k Wh (02)</td>
<td>Consumption: 510.1 billion k Wh (02)</td>
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<td>Oil</td>
<td>Production: 780,000 bbl/day (04 est)</td>
<td>Consumption: 2.13 million bbl/day (01 est)</td>
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<tr>
<td>Natural gas</td>
<td>Production: 22.75 billion cu m (01 est)</td>
<td>Consumption: 22.75 billion cu m (01 est)</td>
</tr>
<tr>
<td></td>
<td>Proved reserves: 542.4 billion cu m (04)</td>
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Source: CIA World Factbook 2005

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**Internationally, competition for resources is fierce. As a latecomer to the game, China is often outmaneuvered.**

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**Investment-led growth to continue**

China will continue to have investment-led growth for the foreseeable future, said Minxin Pei, citing infrastructure needs -- housing, energy, roads, etc. -- that will drive demand and consumption.

- Enormous needs for infrastructure in the inland areas as the government tries to stimulate growth in these previously overlooked sections of the country. The government is now allocating capital and granting more favorable policies to inland areas in order to attract investment.

- Rapid and massive migration of rural residents into towns and major cities. In the next 20 years 200-300 million people will move out of the countryside into urban cities, which will generate enormous demands for infrastructure that will sustain the demand side.

- Although China is moving up quite rapidly, its income level is low compared to developed countries and its level of consumption, while growing within the borders, is also low when compared to the developed world. So there’s a lot of ground to be made up and a lot of opportunity for investors.

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—Minxin Pei
China’s biggest hurdle for sustained high growth is a population that will start retiring 10 years from now.

The rise of China and India: Lessons for the West

Forum members and guests joined panelists in a discussion of China, India and the missing ingredients in US business schools.

Panelists:
- Saptha Chapalapalli, Martin Kenney, Dipak Patel, Minxin Pei

Moderator: James Rooney

James Rooney is chairman of J.P. Rooney & Associates, Ltd., a business advisory firm offering corporate and financial advisory services throughout Asia, and Taxplan Ltd., a subsidiary which provides US tax services in Bangkok, Singapore and Manila. He is a director of Bangkok Airways, Thai Country Club, American Universities Association Language Center, Bangkok YMCA, and has served as a member or director of other business and community organizations.

Martin Kenney, is a professor at the Department of Human and Community Development, and senior project director of the Berkeley Roundtable on the International Economy at the University of California, Davis. (Complete bio P. 6)

Dipak Patel currently researches Indian equities at Passport Capital. (Complete bio P. 3)

Minxin Pei is a senior associate and director of the China Program at the Carnegie Endowment for International Peace in Washington, D.C. (Complete bio P. 8)

DIPAK PATEL: Progress in India is slow but there’s a real commitment by the government and privately owned businesses to create a growth-friendly environment. Businesses have to make money and that’s a very good incentive for them to make it happen. The working population of India is going to be very large going forward 10-15 years and will last for a good 40 years. And if irrigation projects go as planned in the next 10, 25 years, that will have a beneficial effect on the economic base.

MINXIN PEI: For China the biggest hurdle for sustained high growth is the demographics because China’s growth is driven by high savings and that will disappear when the demographic picture changes — when the aging process accelerates very quickly 10 years from now because of the one-child policy. How do you deal with a country that grows old before it grows rich? India will have that problem 20 years from now. Developed economies find themselves vulnerable to external competition. But a developing economy in today’s globalized world also finds itself very vulnerable to external shocks. China faces many potential external shocks, energy being one of them.

Richard Bard, Forum member: Is it your assessment that the Chinese are spending money on the wrong projects to allow their economy to have the kind of productivity gains that would support the population that is all of a sudden going to retire in 10 years – what a lot of us refer to as the 2015 syndrome?

PEI: No, I don’t. I think these projects are absolutely necessary in order for China to continue to grow. The problem with China is that in terms of investment, there’s not enough balance and you can’t overinvest in infrastructure. The government plays too much of a role and the marketplace plays, at best, a secondary or tertiary role. China has skewed its education policy toward higher education so it produces a lot of engineers and other professionals. But China has been shortchanging its basic education. So in 10 years you may have quite a few good people at the top but the lower level of society is nowhere educated enough. And that will have a very negative impact on average productivity. So it’s not that China is misusing its money, it’s that the balance is not exactly right.

ROONEY: What type of accord or relationship do you see China developing with the countries in Southeast Asia? Because right now in Thailand and Malaysia, the comments are that there is really nothing that can be manufactured in these and other Southeast Asia countries that cannot be done more efficiently and at a lower cost in China.

PEI: The countries in Southeast Asia seem to have accepted China’s preeminence in the region. Southeast Asia is very crucial to China in political terms because China is competing with Japan for leadership in Asia. That’s why China was the first country to propose a free trade agreement in the region. Then Japan jumped in, then India. And now the US is getting very worried because for 10 years the US paid too little attention to Southeast Asia, especially after the ’97-’98 economic crisis.

ROONEY: China and all the developing Asian nations are piling up surpluses, mostly in US dollars. How wise is this? Do you have a view on what the alternatives might be?

PEI: There are two different issues. One is the exchange rate mechanism. I think it’s quite clear that China will re-peg its currency to a basket of currencies rather than to a single currency. And that can take political heat off China because China today is the big bad boy in Washington; it gets blamed for all kinds of problems. The second issue is that China
We’re not very good at educating and training business students in the context of a global economy.

should not accumulate that much foreign exchange reserve. For a developing country to have $600 billion dollars sitting in low-yielding assets makes no economic sense.

**Forum guest:** How much mobility is there in India's free enterprise system? Can somebody who's got an idea for a business get the capital to create a company like Microsoft or Intel?

**PATEL:** In India in the 50s and 60s there were about 800 publicly traded companies. Today there are roughly around 4,600. If you have an idea there is money available. But you have to have an idea because the competition is fierce. You really have to be very aggressive in marketing yourself.

**Guest:** One of the things that most impressed me when I went to India was how many strong enterprises there are in the business sector, unlike in China. Many of these enterprises will be moving into the global economy and will be as recognizable as GE and GM. Saptha, could you comment and summarize what Tata is up to?

**SAPTHAGIRI CHAPALAPALLI:** The Tata Group comprises 91 operating companies in seven business sectors: information systems and communications; engineering; materials; services; energy; consumer products; and chemicals. The Tata Group was started in 1868, and today we operate in close to 50 countries.

In the past few years the focus of the group has been to become a global player in the sectors we operate. In India all Tata group companies are expected to be market leaders (No. 1 or No. 2) in their respective segments. All the Tata group companies are required to have a global strategy in their business plan. There are signs of that happening already. This strategy is not limited to the Tata Group; it’s happening with the major Indian companies. The whole Indian private sector is looking to play a bigger role in the world rather than be limited to just India.

**Bard:** The issue that might be interesting to talk about is the role of US universities in teaching students the management skills they need to function globally. Because one of the things I’m seeing as a limitation to economic growth in China and India is the scarce resource called management.

**MARTIN KENNEY:** Business schools in the US think they know a lot about training managers. But whatever that set of skills is, it's not valuable unless it's effective in running a plant in Shanghai with Chinese workers. Business schools focus time and research on refining business tools, such as an MBA, down to micron levels, but they never look at what happens when you take the tools from a US environment to an Indian environment. In other words, the context in which the tools are used has never been developed very well. Now in a global economy it is the context that seems to make the difference and we’re not very good at educating and training in that dimension. There aren’t many professors who have firsthand international experience.

**Donald Stevens, Institute managing director:** For faculty members, nothing compares to the firsthand experience of standing in a foreign factory and asking workers where they came from, what they want to do with their lives.

**KENNEY:** I think the context comes from having international students enrolled because they take the tool box and deploy it in different environments. Foreign students give us their experiences, we give them ours. Since 9/11, the US has been denying entry to many Chinese and Indians. From a policy point of view, we’ve got to turn that around in order to be more competitive in this world.

**Stevens:** I teach a graduate course in globalization. Two years ago I had 27 students, last year I had 14. The difference was in the number of foreign students in the program. Foreign students have a hard time getting into our graduate schools now because of immigration/visa restrictions. Over the next two generations, the negative effects of this immigration policy will be as acute as the positive effects of the GI Bill which allowed hundreds of thousands of servicemen to get an education after WW II.

**CHAPALAPALLI:** We hire 12,000 people every year and they work in different countries. In the US, we find that many executives have limited knowledge of other cultures. Consequently, it’s hard to operate without the risk of miscommunication. But as Martin said, if you had a bunch of classmates who came from other countries, you could learn from them.

**PEI:** The world has changed dramatically in just the last 50 years. I don't think there's one perfect model that can teach international business or business.

**Stevens:** Whatever the model of the future is, online teaching will have a role. And if you put it together with what we’ve been hearing the last decade about having to make job and career changes every five to seven years, maybe business school isn’t a place you go for a year or two to do a bunch of things intellectually. Maybe education should be thought of as a tool that becomes an ongoing process.
The global vs. domestic wine industry

Tom Shelton is president and CEO of Joseph Phelps Vineyards and has over 30 years of experience in the wine industry. He served on the board of directors of the Napa Valley Vintners Association from 1996-2000 and served as president of the trade organization in 1999. As one of the founders of Free the Grapes, Shelton has endorsed reform of the mandatory three-tier system of wine distribution in the United States.

He holds a bachelor of science degree in politics from Wake Forest University and took graduate course work at the University of Maryland.

Tom Shelton began his address to the Global Executive Forum by saying “California wineries are notoriously poor exporters.” The reason, he said, is because “the domestic markets have been so vibrant and the growth in those markets so robust that exporting was always an afterthought.”

When he started working at Joseph Phelps Vineyards in 1992 he pitched the idea of overseas markets to Joe Phelps and the board of directors. They asked him, “Why do you want to do that?” After all, it takes time and money to pursue the global export trade.

“The globalization of our wine industry demands that we attack the export markets in a serious way. I’ve had a hard time convincing my board of directors of how important this is,” said Shelton. “I personally believe that we should be spending a lot more of our resources on export.”

He has been successful to some extent. “Our exports have grown from virtually nothing to about 15 percent of our business today.” He would like to see that number increase to 25-30 percent. “We’ve expanded our relationships to 26 different countries and we’ve been very aggressive in trying to develop more countries.”

The wine business in the United States is relationship-driven, a “belly-to-belly business,” said Shelton. “Relationships are even more important when I travel the export markets.”

Shelton said many of his longtime customers have become personal friends whom he visits every year, squeezing out enough dollars from the budget to allow him to travel. He also invests money in customers’ markets by bringing over their top sales people to visit Napa Valley. “It is very important for us to be able to continue those kinds of activities but it has been difficult for small companies to do it.

Joseph Phelps is considered a small winery, producing about 100,000 cases a year. “At that level you really have to have a distribution network. You can’t do it yourself through mailing lists and things like that,” said Shelton. “There are probably about 10 wineries in that category in the Napa Valley.”

Consolidation is occurring in the wine industry just as it is in the beer industry and Shelton said he is concerned about the “future viability of independent producers. We find ourselves having to form strategic partnerships just to maintain our position.”

About five years ago, Shelton entered into a strategic partnership with Kobrand Corp. out of New York. “This is a marketing group that creates packages of similarly positioned brands to sell to export customers. That has worked fairly well for us and it’s one reaction to the globalization of the industry.

“We’re definitely feeling the pressure from these consolidations and not only in the export markets but in the domestic markets as well.

The industry

Phelps provided an overview of the scope and worth of the wine industry.

California is the fourth largest wine producer in the world and the fourth largest world market in terms of consumption, said Shelton. “Although wine is produced in all 50 states, 95 percent of wine exports from America come out of California where the industry has created about 207,000 full time jobs.”

The industry’s annual economic impact on the state is $45.4 billion; it has grown nearly 40 percent from 1998 to 2002 according to a report from MKF Research for the Wine Institute and California Association of Winegrape Growers.

“One of the problems we see for the medium sized domestic producer is that ever country is trying to get into wine production in a very significant way and they all look to the US market for their sales,” said Shelton. Chile and South Africa are very aggressive and Europe has owned a significant portion of the US marketplace for a long, long time. However, European brands in the US are declining at a very rapid rate as consumers switch to Australian and Chilean wines.

Australia is becoming one of the largest wine producing nations on the planet. They export about 85 percent of their production. Foster of Australia was having a difficult time accessing American markets so they bought the Beringer brand which gave them a good distribution network in the US. Fosters paid a premium for the brand but in some cases the value of the network is more important than the value of the brand.”

The European Union currently represents the largest export opportunity for the US. The value of US exports is $794 million right now, which seems small but it has been growing at 20-25 percent annually.

“When the dollar was strong, we were really suffering. In 2001 and 2002, Joseph Phelps Exports declined precipitously due to the high value of the dollar and the Iraq war. When the US went into Iraq our sales in Europe went right to the floor and Phelps has not fully recovered in that market.”

“In 2001 and 2002, Joseph Phelps Exports declined precipitously due to the high value of the dollar and the Iraq war. When the US went into Iraq our sales in Europe went right to the floor and Phelps has not fully recovered in that market.”
Global business, economics, politics
Perspectives from Europe, Asia and the US

Globalization has produced new challenges in Europe, Asia and the United States. Discussing the issues that are impacting the economies and direction of these regions are panelists Peter Widmer, James Rooney and Richard Bard.

**Peter Widmer**

**Europe: The gap widens**

Peter Widmer is financial advisor to a small number of wealthy European families. He previously was chairman of Julius Baer Investment Management, Inc. and Member of the Executive Board of Julius Baer Holding in Zurich, responsible for the company’s institutional investment activities outside Switzerland. Prior to working for Julius Baer, Widmer was with Swiss Bank Corporation and London & Dominion Trust and Thomson-Schwaub & Co. He holds the Commercial Diploma from the Swiss Business Association.

Slow growth describes the European Union economy for 2005, an average of 1.5-2.0 percent for the 25 member states as a whole, said Peter Widmer in his address to the Global Executive Forum. However, the figures are brighter for the 10 new members (Estonia, Latvia, Lithuania, Poland, Czech Republic, Slovakia, Hungary, Slovenia, Malta, Cyprus), when looked at as a separate bloc. For the 15 old countries, which were admitted May 1, 2004, “The average GDP growth for this year is estimated at 5.0-5.5 percent, which is above original expectations,” said Widmer noting that this points to the “widening gap between the new and the old Europe.”

It’s clear to many why this is happening. “The ECB (European Central Bank) rightly points out that the basic problem with growth lies in rigid labor markets, overregulation and taxation.” This is particularly true in France and Germany.

Germany, which had been the biggest economy in Europe, is now a drag on the EU’s GDP, with one of the slowest growing economies in the euro zone. Its deficit has risen above the euro zone’s debt limit of 3 percent of the GDP as required by the stability pact. According to Widmer, “the March meeting of the European Council in Brussels set new guidelines for the stability pact, basically rendering the old one obsolete and making it easier for new member states to join the euro. The softer guidelines specify 14 exemptions (vs. 3 previously) to the stability pact to allow for unexpected cyclical downturns in the local economy. The EC also modified the 2000 reform agenda which called for the EU to become the world’s most competitive economy by 2010, and agreed upon more realistic goals.”

Before it can get its economy growing again, Germany has to solve a multitude of problems: integrating the eastern German economy into the rest of the country, chronic high unemployment, an aging population that has pushed social security payments in excess of contributions from workers, and a rigid labor market that has made it too costly for companies to do business there.

“Germany’s social program issues are very hard to work with,” said Widmer. “If you want to fire someone you have to give them 12 months notice.” On top of that, the labor force has an attitude problem. “The Germans believe they deserve to win. Many companies are moving out of the country because of these conditions.

Where are they moving to? Poland, Czech Republic and other central European countries that offer a much more friendly and flexible environment for business. France, too, has a more competitive business environment and more reasonable worker attitudes. “The people in France want to work. So country by country you’ll find very different attitudes.”

The new member states have come a long way in just 12 months. Their economies are looking good and “politically they are beginning to make an impact,” said Widmer. “In Brussels at the various committee meetings, they are all in the liberal Tony Blair camp which is for free markets and opening up the EU to the outside world.” This is counter to the French and German camp “which resists more liberal, outward looking and market oriented economic policies.”

Europe’s growth will come from the EU 10, said Widmer. “That’s where the pressure has to come from to nullify some of the rules within the old EU countries.” Above average rates of growth are expected in Slovakia, Latvia and Lithuania. Ukraine, Albania, Romania and Bulgaria, candidates for membership, are also expected to enjoy above average rates of growth.

“The ECB (European Central Bank) rightly points out that the basic problem with growth lies in rigid labor markets, overregulation and taxation.”

Romania and Bulgaria have signed the accession treaty, paving the way to become the 26th and 27th members on Jan. 1, 2007; however, entry could be delayed by the lack of progress they have made on issues such as corruption and border controls.

Turkey’s entry has been pushed back by 10-15 years to allow it time to comply with EU standards relating to corruption, intellectual property rights, freedom of the press and women’s rights. No problem with its economy, though. Turkey’s growth rate of 9.9 percent last year makes it the fastest growing economy of all the EU countries and on a par with China. The per capita income in Turkey is US$7,000, only 50 percent of the average of the new member states. This is the highest it has ever been, but the income is very unevenly distributed.

“I think it was wise of the EU to set a timetable of 10-15 years for Turkey to become a member because there’s no phase-in period. On Day One, all members have to accept all existing EU legislation.”

Despite the fact that EU entry requirements are so stringent, it does not deter new candidates from knocking on the door. “The attractiveness of the EU to these countries is freedom, open markets, reliable political and economic structures,” said Widmer. “Ukraine has made a very strong declaration that they would like to join the EU as soon as possible.”

The EU stands in sharp contrast to Russia, “which is increasingly seen as authoritarian, unreliable, hostile. So they’re in a hurry to get under the umbrella of the EU and into NATO.”

And what’s the prognosis for the EU
constitution which went through several drafts before member states agreed to put it before their respective electorates? “Under the guidance of France’s former President Valery Giscard d’Estaing, the constitution aims at securing the smooth running of the EU in its expanded form today and as it continues to expand into the future,” said Widmer. “French President Jacques Chirac is terrified that a ‘No’ result on May 29 would be interpreted as a vote of no confidence against him and his government.

“If the constitution fails, a less ambitious, simpler and less detailed version would then be drawn up, but there is no Plan B at present. In the meantime, the euro will not crumble; you don’t need a constitution to do business.” ♦

Note: On May 29, 2005, French voters rejected the EU constitution, and on June 1 voters in the Netherlands also turned it down.

James Rooney
Asia: Year of the Rooster
James Rooney is chairman of J.P. Rooney & Associates, Ltd., a business advisory firm offering corporate and financial advisory services throughout Asia, and Tazplan Ltd., a subsidiary which provides US tax services in Bangkok, Singapore and Manila. He is a director of Bangkok Airways, Thai Country Club, American Universities Association Language Center, Bangkok YMCA, and has served as a member or director of other business and community organizations.

As Southeast Asia looks for ways to ensure its economic growth, it must deal with “serious issues concerning country-to-country relationships, the global economic slowdown and oil prices,” James Rooney said in his address to the Global Executive Forum.

Relationships. The Southeast Asian countries (Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand, Vietnam) have a positioning problem relating to the major -- and often unpredictable -- powers of China, Japan and the United States.

Tensions exist between China and Japan, between China and the US, and between Japan and the US. “How does Southeast Asia avoid getting caught up in a conflict between any of those relationships? It’s a very difficult position for them to play.”

Even if Southeast Asia can successfully sidestep being drawn into other nations’ disputes, it must still contend with the separate interests and clout of the three powers while defending its own interests in the region.

“China is the big kid on the block, Japan is a grandfather figure whose best days may be behind her but who can still be counted on for support, and the US on any given day might be Southeast Asia’s best friend or worst critic,” said Rooney.

“There is a feeling in Southeast Asia that it’s probably better to have the US as a mistress than as a wife because the relationship with the US can be a very rocky one. The US will praise you one day and will criticize you the next day. In Southeast Asia, you never know when you wake up in the morning whether the US will be your friend that day or your critic.”

The US stance on China’s currency is problematic for Southeast Asia. “The US is pushing China to devalue its currency so Southeast Asians fear such a move will throw the Asian currency markets into a state of chaos,” said Rooney. “Do they try to get the US to reevaluate their position or do they stand back and do nothing?”

Free trade agreements in Asia are another source of anxiety. Thailand is currently negotiating free trade agreements with Japan and the US. China has negotiated a free trade agreement with ASEAN (Association of Southeast Asian Nations) which covers a broad number of industries and includes a sensitive industries list specifying those industries that the respective countries are not ready to open. The Chinese have been much more clever in trade than most people give them credit for. They’ve learned how to use non-tariff barriers very effectively to let things in that they want and to make it difficult for other goods to get into the country. So the free trade agreement has not been quite as free as some of the Southeast Asian countries had hoped it would be.

“In a sense, China is not playing the game fairly, but it’s hard for small countries to stand up to the big kid on the block and tell him he’s not following the rules. So they have to look at other mechanisms to try to make this relationship work.”

Southeast Asia’s relationship with Japan is also difficult. “Japan is important to Southeast Asia in two ways: It is a very significant contributor of capital investment and it represents a significant market in some areas for the Southeast Asian nations, and they don’t want to throw this away. So when China and Japan argue, Southeast Asia is a bit worried. There’s a great phrase in Asia that when elephants fight, the grass gets trampled. And these small Southeastern countries are the grass.

“I think the greatest concern, which overrides everything else with the Southeast Asian nations, is how they can eventually strike economic cooperation agreements with China. Because China, in a blink of the eye, could wipe out all the export markets for any of these nations with the exception perhaps of Indonesia which has hydrocarbons.

“We are all realizing that we’re no longer living in an era where economic change is gradual and predictable. You have to be much quicker to react to external changes and have definitive policies to deal with them when they occur.”

Global slowdown, oil prices. Based on the global slowdown and rising oil prices, GDP growth rates in Southeast Asia this year may fall as low as 3.5 percent in some countries from their current high of 5.5-6.5 percent. If global economic growth drops to around 4 percent, as recently forecast by the World Bank, this would hurt Southeast Asia because the region is dependent both on foreign direct investment and on exports,” said Rooney.

“Inflation, while still relatively low, will likely increase by 1.0-1.5 percent in most of the Southeast Asian countries as a direct result of oil prices. But for the moment, with varying degrees of success, the region has gotten past the 1997-98 economic collapse.

“At this time, Southeast Asia sees its future linked more strongly to China than to India. However, if India does develop into a global economy they will be looking to India as a potential market. But I don’t think we can expect to see the types of capital flows between Southeast Asian nations and India that we see between Southeast Asia and China.

So it’s shaping up to be a classic Year of the Rooster, which is supposed to be a
confrontational year with a number of changes along the way.”

Richard Bard

US: Okay but not robust

Richard Bard is founder and manager of Bard Capital Partners LLC, a private investment company that has been involved in the acquisition and operation of several significant private and publicly traded businesses and real estate investments over the last 20 years. He is also chairman and CEO of WG Global, Inc., a privately owned company which is the leading global provider of surface preparation solutions and equipment to the automotive, aerospace and foundry industries throughout the US, Europe and Asia. He has served as chairman of the board of the Federal Reserve Bank of Kansas City and is now the deputy chair. Bard has an MBA in finance from Bernard M. Baruch College at the City University of New York and a bachelor of science degree in civil engineering from The Pennsylvania State University. In 2001, he was elected by the University of Colorado Board of Regents to receive the degree of Doctor of Humane Letters.

To gain insights into how the US economy looked from the perspective of business people in the trenches worldwide, Richard Bard sent written surveys to the management team of two global companies Blastrac Global and Wheelabrator Group, Inc. “About 50 middle managers gave me a personal view of what they see for the economy in 2005, 2006,” said Bard, addressing the Global Executive Forum.

“I didn’t see the word ‘robust’ anywhere in the survey responses. Across the board, the feeling is that there is a slowing of the economy because of energy costs. The auto industry and the pressure it’s putting on suppliers is huge. One of our major foundry customers went bankrupt last week.”

Most people are surprised to learn that “Canada, not Saudi Arabia, is the largest supplier of oil to the United States,” said Bard, adding “Canada has tremendous natural resources.”

It’s not just the cost of energy that’s putting a damper on the economy and corporate earnings, said Bard. “I think there are a lot of non-monetary issues, perhaps non-liquidity issues that are affecting business and business decisions.”

Among these is “the price of health care, which is gigantic. The cost of insurance has been going up, and there’s a huge swelling of supply chain costs. Virtually every supplier is attempting to put some price increases through the system. The costs of steel and some basic commodities are up 100 percent in some cases from January 2004.”

As far as the Federal Reserve Bank is concerned, “the economy remains robust. For the past 23 months manufacturing in the US has shown growth. The April numbers showed a slowing in manufacturing growth but still growth. It’s pretty much the same for retail. Retail sales are up; in fact shopping center growth across the country is huge.

“Home building permits, new home starts, resales have all been strong. There’s a nice curve in terms of growth in non-defense capital spending.”

In his own companies, Bard said, “The infrastructure businesses have been the strongest. The rail industry has probably been our biggest growth engine. The aerospace industry is strong, particularly the military sector.” Nevertheless, Bard believes “a soft patch is coming because of the burden of operating costs on corporate earnings.”

Other pressures

In addition to what Bard calls “cost inflation,” other pressures are impacting corporate earnings. “There is strong pent-up demand for employees raises and bonuses, which wasn’t an issue a couple of years ago when there was an acute shortage of jobs.

“The strongest hiring market is in the northwest; the weakest in the south and southeast which have lost many of their manufacturing companies to Mexico, China and Southeast Asia. So I think the south and southeast may be looking at different growth curves than the rest of the US.

“The word ‘outsourcing’ showed up in many different survey responses. The question is not if a company will outsource but where they will outsource. So the growth of the outsourcing trend will continue to be big.”

During the most recent US economic slump, consumers’ spending habits prevented the economy from sliding too deeply into recession. But that has a downside. “I think there is now some worry about the high debt burden and low savings of the average consumer,” said Bard. “It’s a pretty interesting phenomenon in terms of people living off the equity in their homes and accumulating debt.”

Looking to the future of the global economy, Bard sees the US maintaining its leadership role. “Europe will return as a dominant trading partner which is good for the US in the long term. Certainly China will be a strong economic player, as will India in time.”

Colorado looking good

The turnaround in the Colorado economy is accelerating, said Richard Bard. “In March of this year, Colorado created 14,000 new jobs, which was 10 percent of the growth of the whole United States.” The state is rich in natural resources and “the prices of uranium and iron ore and coal are driving more exploration and more mining investment in Colorado.

“The real estate market has been strong from retail to industrial. Downtown Denver has been the strongest part of the commercial real estate market. We still have a soft patch up towards Boulder, but mountain properties have done very well,” said Bard. People are buying homes in Vail and Beaver Creek and Aspen. Prices in these communities were up 11 percent last year.

According to the Colorado Office of Economic Development and International Trade, “Colorado companies shipped $6.7 billion in manufactured, agricultural and mineral products to international markets during 2004, breaking the previous record of $6.6 billion set in 2000.” Exports to Canada, the state’s largest international market, increased by 16 percent in 2004. Exports to Mexico, Colorado’s second largest market, rose by 21 percent. Exports to China (including Hong Kong), the state’s third largest market, jumped by 41 percent.

“So generally speaking, the Colorado economy looks pretty good,” said Bard.
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