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THE “WAR AFTER THE WAR,” THE RELENTLESS RUSH OF GLOBALIZATION, AND THE UNITED STATES OFF TRACK

Annual Forecast

Marvin Zonis

Professor Emeritus

Graduate School of Business

The University of Chicago

Marvin Zonis offers his Annual Forecast for 2005.

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THE “WAR AFTER THE WAR,” THE RELENTLESS RUSH OF GLOBALIZATION, AND THE UNITED STATES OFF TRACK

Annual Forecast

*by Marvin Zonis, Professor Emeritus
Graduate School of Business
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The biggest surprise of 2004 - and the greatest failure of my forecast for this year — has been the success of the uprising in Iraq and the failure of the United States to control and win "the war after the war." Many factors account for this U.S. failure. Planning for the post-Saddam era was woefully inadequate with the Defense Department taking over the two year State Department post-war planning operation and scrapping its findings. Reconstruction has also been woefully inadequate, with the U.S. having spent, 20 months after the overthrow of Saddam, less than 6 percent of the funds allocated by Congress. Intelligence has also been catastrophically wrong. The administration based its policies largely on the findings of the Office of Special Plans in the DOD. They argued that the Iraqi people would welcome their liberation from Saddam with flowers for the Americans. This intelligence came from self-serving Iraqi defectors like Ahmad Chalabi, long ago rejected by the CIA as utterly unreliable and now known to be in cahoots with the Iranians. U.S. troop levels have also been stunningly insufficient to clear areas of insurgent control, prevent the re-emergence of insurgents in those areas and begin the reconstruction of those places.

Another major surprise for me in 2004 has been the startling and relentless spread of globalization and outsourcing — more and more of the world is being swept up into the nexus of global capitalism and markets. Marx was right about the transforming capacity of Capitalism. The utterly staggering rise of China is the most dramatic example. But more and more of the world is participating in the global economy. Lesotho, for example, is a small country in southern Africa that has become a center for garment manufacturing and export to the United States. Fabrics imported from Pakistan and Bangladesh are cut and sewn in factories owned by Taiwanese and staffed by Lesotho workers. The output is shipped to U.S. retailers.

The rush to outsourcing is another. We have long been familiar with the outsourcing of fairly low level jobs — call centers in India and Ireland, for example. Outsourcing of basic software development to India and the Philippines is another example. Back office processing is still another. But we are now witnessing the outsourcing of ever more sophisticated business processes and even the highest level business functions such as research and development. And more and more of the world are participating in outsourcing. Russia, China, Hong Kong, India, Canada, the Philippines, Israel are all in the game.

The good news of outsourcing is that more and more of the world's people are participating in the global economy and becoming wealthier in the process. Global inflation is reined in. Companies become more efficient and raise profits and wages. Consumption is higher than it would have been absent globalization. But the downside of globalization is that it makes the challenges for the United States ever more difficult to meet. Jobs are disappearing. What can be done in the U.S. better than in other countries? That question is harder and harder to answer.

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What will be the major issues the United States will confront in 2005? What surprises are in store? Here's my forecast:

THE UNITED STATES

The most important story of our era is the declining relative economic competitiveness of the U.S. since the U.S. bubble burst in 2000. Since then, U.S. exports have increased by 13 percent. Other traditional exporters have done much better. Germany has increased its exports by 39 percent and Japan, by 32 percent. (These figures are based on local currencies and changes in their values account for only a very small percentage of export growth.) An even more worrisome development is that most countries in the world increasingly buy goods and services from countries other than the U.S. The percentage of U.S. imports as a percent of total imports for each of the U.S.'s major trading partners is dramatically declining. Another disturbing phenomenon: In 1992, U.S. exports were running at 94 percent of imports. For the last 12 months, exports have been only 67 percent of imports.

Our current account deficit is at record levels and the willingness of the world to finance our budget and trade deficits is diminishing. A lower value for the dollar and slower U.S. economic growth in 2005 are both inevitable.

President Bush has made it clear that his electoral victory has given him the political capital he needs to implement his 'Bush Revolution.' The components of that revolution are not in doubt - a vastly increased role for religion in U.S. public life; appointments of justices to the Supreme Court who will vote with Antonin Scalia and Clarence Thomas far more often than with Ruth Bader Ginsburg; a Constitutional amendment that bars gay marriage; partially privatized social security; lower taxes; lower government spending for entitlements and social services, including education; less government regulation of business; more oil, less conservation; more coal, less concern with global warming and the environment; more unilateralism in foreign policy; more spending for the military and the intelligence agencies.

The United States is increasingly seen around the world as a menace. In a survey of over 7,500 Europeans in 2003, some 53 percent of the respondents believed that Iran, North Korea, and the United States were equally threats to world peace. In a more recent poll, more than 70 percent of Turks, Nigerians, Indonesians, Pakistanis, and Russians said they worried about a U.S. military threat to their countries. The Department of Defense Science Advisory Board recently excoriated U.S. public diplomacy as woefully inadequate. The Board concluded that America's capability to win "hearts and minds," especially in the Muslim world, is virtually zero. With the sharp tongued and very undiplomatic Condoleezza Rice as the new Secretary of State, there will be no improvement in our greatest foreign policy challenge.

But the U.S. continues to damage its own self-interest in other ways. One of the most significant has been the government's clampdown since 9/11 on immigration and the issuance of visas to enter the United States. The result has been a significant decline in the immigration of precisely the kinds of new arrivals the U.S. needs the most. For FY 2003, immigration of 'professionals with advanced degrees or exceptional ability' was down an astounding 65 percent from the year before. 'Skilled workers' were down 47 percent. 'Priority workers' were down 57

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percent. (All were below the 1997 numbers.) Total immigration to the U.S. was down from 1.1 million to 706,000 or 34 percent.

Reductions also occurred among visas granted to foreign students. The number of foreign students in 2003, 625,000, was down 12 percent since 9/11. U.S. students are shunning the sciences and engineering. The U.S. manpower deficit in those crucial areas has been compensated for by foreign students receiving advanced degrees at U.S. universities and staying in this country. But in 2005, the U.S. will find itself increasingly short of skilled workers, scientists and engineers. As a result, outsourcing will accelerate and skilled and high paying jobs will increasingly be done outside the United States.

The United States is pursuing the wrong policies for its need to improve the status of the American economy, especially to meet the challenges of India and China. As will be suggested in the rest of my forecast, it is also pursuing the wrong goals with the wrong means in its war against terrorism; in the need to bring about Middle East peace and reform; and in the need to build global coalitions to solve global problems.

CHINA

One key to understanding China is to appreciate the brittle sense of nationalism on which its government is based. Communism as an ideology has passed into the dustbin of history. What binds China together is an increasingly intense spirit of nationalism, on the one hand, and confidence, even grandiosity, derived from the last 25 years of the most robust economic growth in world history, on the other hand. One manifestation of these facts is China's profound reluctance to take orders from anyone; to be pressured into actions not seen as beneficial to itself. No greater pressure is now being administered than to get China to revalue its currency to diminish its extraordinary trade surplus with the U.S. - some \$150 billion in 2004, and heading up for 2005. All told, that represents some 25 percent of the total U.S. current account deficit. With the dollar plummeting recently against the euro and against the yen, only the yuan of the U.S.'s major trading partners is still weak.

But while China runs a major surplus with the U.S., its total current account is nearly in balance. In the first quarter of 2004, China imported so much from the rest of the world that it actually ran an overall trade deficit. China is no Japan. China is completely open to foreign investment; to imports; to foreigners owning local companies. No mercantilism there.

Given the near balance in its trade account and its resistance to foreign pressures, China is highly disposed to do nothing with its currency except maintain its value against the dollar. In 2005, China will take the line that the dollar/yuan relationship is not its problem but that of the U.S. The Deputy Governor of the Chinese Central Bank has already had harsh words for the U.S. "For the past 26 years," he suggested, "we have never put pressure or problems on the world. The U.S. has the reverse attitude; whenever they have a problem they blame others." He went on to say that China could not move "under heavy external pressure" and urged people to stop talking about the value of its currency.

But while blaming the U.S. for blaming China, the Chinese Central Bank has to cope with a different kind of pressure - speculators are rushing to convert dollars into yuan, expecting to make out on its revaluation. The flow has been so massive and increasing roughly at the rate of 33 percent per month, that the Bank has imposed a limit of \$10,000 per day per converter. It has also allowed emigrants to convert their Chinese savings in yuan into dollars when they leave the country.

But the huge flow of dollars being converted into the yuan continues as speculators bet that the regime will raise the value of its currency. The speculative frenzy and the huge flows of foreign direct investment are making it very difficult for China to neutralize the flows that enter the country and slow the economic boom that fosters inflation and vast overcapacity in a variety of industrial sectors, threatening a subsequent collapse. By the end of 2005, China will attempt some move to placate the U.S. without at the same time being perceived as caving in to speculators. The band in which the dollar/yuan trades will be slightly widened. The danger: speculative fever will be fed. China will be stuck in a currency bind in 2005.

IRAQ

Flawed as they will be, the nationwide elections will come off in Iraq by the end of January, 2005. Some 60 political parties have been approved to participate but there has yet to be any campaigning. There has been no indication that the Sunnis, the Shiites and the Kurds can work together or even cooperate. The Association of Muslim Scholars, which claims to represent 3,000 Sunni mosques in Iraq, has called for delaying the election and failing that, a total boycott. But if many Sunnis opt out of the vote, they will leave the field completely open to a Shiite victory and put the Sunnis in a weak position to negotiate on the post-election division of oil revenues and political power. The vast majority of the Iraqis are likely to vote in hopes of avoiding that fate.

The U.S. has tried to craft a unified slate of candidates made up of the members of its hand picked but now dissolved Governing Council. But that effort failed and, instead, Iraqi voters will be able to choose from many competing slates, all based on sectarian divisions. The result will be that the U.S. backed candidate, Prime Minister Iyad Allawi, will lose the vote and will lose power. Ayatollah Sistani, the leading Shiite cleric is putting together a Shiite ticket bringing all the largest Shiite parties together to insure that the next government is dominated by the Shiites.

The 2005 challenge in Iraq will be to insure that the new Shiite government can meet the demands of the Kurds and the Sunnis. This will be a formidable challenge given that the Kurds have enjoyed U.S. guaranteed virtual autonomy since 1991 and that the Sunnis have dominated every government in Iraq since its independence from the British. The challenge ultimately will prove impossible and the three groups will not be able to agree on the basic division of powers and revenues.

The U.S. adventure in Iraq is still off the tracks and is still likely to result in a debacle. As Anthony Cordesman of the Center for Strategic and International Studies put it on November 22, 2004, "We still have no clear public goals. We've never said to the Iraqis that we won't take their oil, that we won't steal their economy that we won't establish military bases that we'll leave when an elected government asks us to. We've never said that any government that is elected is OK with us. In short, there has never been a clear presidential-level statement that deals wit-

all the conspiracy theories [about America's designs on Iraq]."

For all these reasons, Iraqi stability will not return in 2005. Car bombs and insurgent attacks will continue. Oil exports will be interrupted by sabotage. The U.S. will begin to draw down its troop levels and the grand American plan to transform Iraq and the Middle East will continue to fail.

ISRAEL-PALESTINE

After Iraq, the second major U.S. problem in the Middle East is the Israeli-Palestinian conflict. One aspect of this problem is that the Iraq conflict and the Israeli-Palestinian conflict are ineluctably tied together in the minds of Arabs. If they doubt the connection, virtually every Arab TV station and newspaper makes the comparison day in and day out. What the U.S. does in Iraq is presented, throughout the Arab world, as identical to what the Israelis are doing to the Palestinians. We occupy Arab lands. The Israelis occupy Arab lands. We engage in assassinations. So do the Israelis. We torture Iraqi prisoners. So the Israelis torture Palestinians. And on and on. One very serious consequence is that the comparison generates more recruits for terrorist attacks against the United States. Another is that the comparison mobilizes more opposition to Israel.

These are obviously serious threats to both the U.S. and to Israel. It suggests that a vast amelioration of the plight of the Palestinians is a crucial step for achieving nearly all major U.S. foreign policy goals. President Bush has suggested that an independent Palestinian state could be created by the time he leaves office. With the death of Arafat, it is not at all clear why it should take four years to bring about a Palestinian state. To the contrary, what we have learned is that only the intense engagement of the U.S. President can move these two hostile parties to some sort of resolution. President Bush's time schedule suggests he will not be involved anytime soon.

Mahmoud Abbas, Arafat's second in command will win the election to head the PLO. But he has little real support among Palestinians and he will not be able to bring together the many feuding groups that seek to speak in the name of all the Palestinians. Abbas was one of the exiles with Arafat in Tunisia, from the expulsion of the PLO from Beirut in 1982 to their return to the West Bank in 1994. As a result, he is seen as an outsider by all the Palestinians who lived under Israeli occupation. He is viewed as corrupt. He is viewed as being Arafat's man. Stability for the Palestinian leadership will have to wait for a further shakeout and that will not occur in 2005.

Ariel Sharon is the most interesting of leaders. His Gaza pullout plan has managed to offend virtually everyone. The Israeli armed forces are concerned because they can't see - other than frequent invasions of the Gaza after their pullout — how they will prevent primitive rockets being shot into Israel. The settlers are opposed because they see the surrender of even one inch of any of the occupied lands as the precursor of the surrender of all the lands. Israeli "peaceniks" are nervous because the deal is not being done with the Palestinians. It will be another Israeli demarche, another Israeli fait accompli that they believe will not bring the stability that, they believe, can be accomplished only through negotiations with the Palestinians. The Palestinians, of course, are totally opposed because they see Sharon's Gaza withdrawal not

as the first stage in a series of withdrawals but as a stratagem to tighten irrevocably Israel control of the West Bank-the center of any future Palestinian independent state.

The evidence suggests that they are right. Sharon has launched something of a building boom on the West Bank. Permission to build 5,300 new homes in Jewish settlements has been approved and no move has been made to shut down the more than 100 outposts on the West Bank deemed "illegal" by the Israelis, most containing only a few trailers. The "security fence" is being built on the Palestinian side of the pre-1967 border of Israel with the West Bank in a manner that suggests that Israel will weaken any prospective Palestinian state by dividing the West Bank into cantonments.

So bet on little progress in 2005 towards a resolution of this mother of all conflicts.

IRAN

The hard-liners are in power in Iran and because they feel that they have consolidated their power against the so-called reformers, they are willing to negotiate with the U.S. But to this point, the conflicts within the Bush administration between the "neo-cons," who seek regime change in Iran, and the "realists," who seek to work out a viable relation with the clerics, has prevented the emergence of any new Iran policy. Instead the U.S. has outsourced its Iran policy to the UK and (surprise) to Germany and France. They, in turn, have made a deal — Iran will "suspend" its nuclear enrichment work in return for economic assistance. Actually, Iran has offered the U.S. a similar deal - to suspend its nuclear program and support for Hizbollah in Lebanon in return for U.S. diplomatic recognition and the lifting of U.S. sanctions. But the U.S. has not taken the offer seriously.

Developing nuclear weapons has been an obsession for many in Iran for decades. They support Iran's becoming a nuclear power to match their grandiose sense of themselves. So don't count on any deal which thwarts Iran's wishes to be in a position to go nuclear at a time of its choosing. Their agreement to suspend uranium enrichment will not last.

There is no useful military option to thwart Iran's nuclear ambitions. Its nuclear facilities are spread across the country in as many as 8 locations. Many are buried deep in bunkers. Others are located in the middle of Iranian cities. A military strike would be costly in terms of civilian casualties and would seal the hatred of Iranians towards the U.S. for the next 100 years. (Don't look for any repeat of the 1981 Israeli strike against Iraq. Iran is very far from Israel and the Israeli air force does not have the power to destroy the Iranian facilities. That would take U.S. heavy bombers flying from Diego Garcia in the Indian Ocean.)

Nor should Americans count on regime change in Iran any time soon. More than 70% of the Iranian people hate their government. But the regime is ruthless and eliminates any opposition the moment it appears. There are no opposition leaders who can challenge the regime. The clerics have already brought the press under control. Seeking to control the flow of all information, they have begun mass arrests among web bloggers and blocked hundreds of web sites. A senior cleric recently authorized the policy saying, web sites should be blocked if they "insult sacred concepts of Islam, the Prophet and the Imams" or if they publish "harmful and deviated beliefs to promote atheism or promote sinister books." (New York

Times, November 8, 2004) At the same time, prominent leaders of officially approved Non-Governmental Organizations are being arrested. Particularly targeted are the leaders of women's organizations that have worked on women's rights in the private sphere — child custody, inheritance, domestic violence and divorce issues.

As a result, the U.S. faces a massive challenge. Iran's developing nuclear weapons is certainly inimical to U.S. and European interests. It would ignite a nuclear arms race in the region - most definitely in Saudi Arabia. Worse, the most powerful military force inside Iran, the Revolutionary Guards Corps, like the Nazi SS, was created to protect the regime from its internal enemies. The Revolutionary Guards Corps is capable of staging a coup in alliance with a group of clerics even more "hard line" than those currently in charge. They might then well seek to transfer nuclear weapons to terrorist groups. Yet another challenge is the absence of a Khomeini like figure with unquestioned charisma and power. In 1988, Khomeini announced that he would "drink from the poison chalice" and accept defeat in Iran's 8 year war with Iraq. If the present Supreme Leader agreed to end Iran's nuclear program, it might very well precipitate a coup or even his assassination.

So the options for the U.S. are limited. A useful military option is out. Regime change is not imminent and cannot be made so. Negotiations are the only viable option. Iran is hurting economically and wants U.S. sanctions lifted and diplomatic relations established. It is time to see what the Iranians are willing to offer in return.

TERRORISM

The U.S. "War on Terrorism" will continue in 2005 with little likelihood that it will take the form of another actual war. No new countries will be invaded by the U.S. in 2005. But the terrorists have, in some ways, already won this war. The United States has made dealing with the terrorists a virtual obsession. Ten of billions of dollars are being spent and perhaps billions of people are being inconvenienced because of the tragedies of 9/11 and the Madrid train bombings. But despite the intentions of Osama Bin Laden and his many allies, terrorists have done very little actual damage. Yet they have succeeded in inflicting huge costs on the U.S. and the West. The terrorists have won because we have been terrorized. What is called for is putting the threat of additional terrorism in perspective. The dangers are real. But many other dangers exist that need more urgent attention than we have been able to give them. AIDS, new diseases such as Avian Flu, the conflict between Israel and the Palestinians, the U.S. dependence on foreign oil, the need to come to terms with the Islamic World, proliferation of weapons of mass destruction, the international drug trade, and especially the tragedy of failed states — the 60 countries in the world with 20 percent of world population that cannot manage to build institutions that can provide education, health care, the benefits of economic growth or prevent internal strife. All present greater threats to the U.S. than terrorism.

NORTH KOREA

North Korea, the other member of the troika in President Bush's "Axis of Evil," will be less quixotic in 2005. The Kim Jong Il paraphernalia are being removed from the country. This may indicate his loss of power. Or it may indicate his decision

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to do more to institutionalize his regime by bringing in other leaders. In either case, the four other countries mobilized by the U.S. to participate in dealing with North Korea - China, Russia, Japan, South Korea - will put more pressure on the North to surrender its nuclear weapons and allow intrusive international inspections. 2005 might just be the year it works.

RUSSIA

President Bush has declared three principal foreign policy objectives for the United States—spreading democracy, preventing the proliferation of weapons of mass destruction and fighting terrorism. Unfortunately, President Putin's policies have been working against all three U.S. objectives. He has consolidated his power at home and is building a more authoritarian and less democratic Russia. He is seeking to extend his control over former Soviet states and continues to support the recent fraudulent election in Ukraine. He has not fully secured Russia's nuclear material and he continues to transfer nuclear technology to Iran. His repression of the Chechens and their aspirations for autonomy has made the world as a whole less, and not more, secure.

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Inter-ethnic tensions are rising in Russia. Almost everywhere, Russia's Muslims are the subject of xenophobic language and graffiti. But after the Beslan tragedy, much more serious xenophobia has been reported around the country. Muslims who appear "different" or "strange" and who are outside the areas of cities or regions considered Muslim have reportedly been arrested and tortured.

Russia is already the world's second largest exporter of oil. With President Putin's decision to destroy Mikhail Khodorkovsky and with him the huge oil giant Yukos, the Russian state will have control over all major production and exports. But the role of Russia as an energy supplier is about to increase. Given the rapid growth in U.S. demand for natural gas - likely to run from 1.5 to 2.5 percent per year for the foreseeable future — and the declining likelihood of major new finds in this country or Canada, Russia is poised to become a major gas supplier to the U.S. New LNG terminals will be built in Nova Scotia and Ontario which will then pipe Russian gas bought from Gazprom, which the Russian state controls, down into the U.S. Russia, via Gazprom, already supplies 100 percent of the gas consumed in Finland, Estonia, Latvia, Lithuania, Slovakia, Romania, and Bulgaria. Russia supplies between 60 and 90 percent of the gas consumed in Turkey, the Czech Republic, Slovenia, Hungary, Poland, and Austria. Germany gets 44 percent of its gas from Russia. Italy, 31 percent. France, 24 percent. The future stability and dependability of Russia has become ever more significant to the global economy. Russia may be working against President Bush's principle foreign policy goals. But given its ever increasing importance to the U.S. as a supplier of energy, do not look for the President to criticize his "friend," Vladimir Putin, any time soon.

JAPAN

The single most important truth about the Japanese economy is that the wages of

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Japanese workers continue the decline, particularly for workers at small and medium-sized Japanese companies. The Japanese companies which have prospered are those with brand names known to Americans - Matsushita, Honda, Sony, Toyota, and the like. But as they have prospered, smaller Japanese firms have had the terms of trade turn against them. As a result, the wages of their workers have been in decline. Adding to the problems, higher pension contributions and tax hikes are scheduled for 2005. The result is that consumption levels have remained weak and even these levels will not be sustained in 2005. With the inventory build up generated by the low levels of consumption, Japanese corporations have pulled back on capital expenditures, further slowing the economy. But 2005 will have even more negative news for Japan. So far, the much touted economic recovery has been export led with Japanese exports to China now greater than Japanese exports to the United States. With China's economy sure to slow dramatically in 2005, so will Japanese exports. No economic recovery is in store for Japan in 2005.

OIL

OPEC is now producing more oil per day than the world consumes — somewhat more than 1.5 mmbd in excess supply. When that becomes clear to oil markets and oil traders, prices will fall in 2005, back to the low \$40 level or even to the high \$30s. That will be followed by a slowdown in OPEC oil production and a spiking of prices by the end of the year, back to the high \$40s. But unless the cutbacks are more drastic than now seem likely, oil prices are unlikely to be in the \$50 range in 2005. The slowdown in China and in the global economy will moderate demand pressures on OPEC supplies. But over time, demand pressure will return. For example, the U.S. now consumes about 20 mmbd. China, the world's second largest oil importer consumes about 6 mmbd. As China's economy continues to expand and auto sales continue to rise, its demand for oil will as well. By 2025, China's could well be consuming 20 mmbd while U.S. oil consumption will continue its relentless rise. Where is this oil going to come from? So far as we know, it has to come from the Persian Gulf. Political stability is not the hallmark of those oil exporting countries. By the next decade we may well see oil prices doubling from present levels.

EUROPE

The central challenge for Europe in 2005 will be its debate over the proposed EU constitution, laboriously written by a committee headed by ex-French President Valerie Giscard D'Estaing. If the national legislatures of all 25 member states approve the document, it will go into effect in 2007. But 9 countries — Britain, the Czech Republic, Denmark, France, Luxembourg, Ireland, the Netherlands, Portugal, and Spain — have decided to put the constitution to the voters. If only one of the 25 countries rejects the 265 page document, the constitution will be null and void. That is likely to happen in 2005. Even French voters, traditionally the most European - indeed the European Union has been largely a French project - may reject the new constitution. Laurent Fabius, a former French prime minister has threatened to vote no and lead his fellow Socialists to do likewise unless President Chirac moves the country sharply to the left. The Parti Socialiste will vote on the new constitution on December 1. Watch that vote, if the PS votes no, there is enough additional hostility to the constitution on the far left and far right of the French political spectrum to guarantee its defeat in the national referendum in 2005. Just what would follow from a rejection of the constitution by France or any

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of the 24 other member states is uncertain. But it would throw the EU into disarray and generate the greatest crisis in its history.

That crisis will not dissuade prospective new members from seeking membership. At the head of that list is Romania. The power of the EU to generate reforms in its would-be members will be demonstrated in Romania's presidential elections scheduled for late 2004. Romania is so eager for membership that vote fraud will be kept to a minimum and will be judged "clean" by EU standards. Membership talks will then proceed. So will EU deliberations with Turkey, which will become a member of the European Union in 2015.

The EU has been remarkably successful. It has been driven largely by political leaders but still has very little popular support, which is one reason the constitution is likely to be defeated. There is no one in the EU who wakes up in the morning and thinks of herself as a European first and a German, say, second. But the commitment of the elites to a common European homeland is very deep and very widespread and those leaders have already accomplished far more than any of us imagined 25 years ago. They will eventually fashion a constitution that will be approved. They have already fashioned a common currency that is rapidly becoming a global reserve currency and has strengthened remarkably against the dollar.

The strength of the euro has its costs. It will dampen economic growth in Europe in 2005 which will, in turn, disappoint voters in the European project and the new constitution. This will be felt especially deeply in Germany, still Europe's largest economy. Germany's economic growth will be less than any other G-7 country in 2005. Its unemployment rate will be above 10 percent so domestic consumption will be flat to down. Its exports will not increase much, given the strength of the euro and the weakness of the global economy. Instead, major German exporters will continue to move their production to less expensive areas. Germany desperately needs a more flexible economy which Chancellor Schroeder is struggling to deliver against immense odds. Some companies have worked out deals with their workers which give them more flexibility. But overall the economy will remain sclerotic in 2005.

Europe also has to deal with its immigrant issue. The Europeans initially welcomed Muslim immigrants. The Germans brought in millions of Turks and called them "guest workers," implying that they would not settle in Germany and return home. Instead they brought their families and now want citizenship. France has a similar problem. Millions of apparently dissatisfied Muslim youth living in ghettos, unable to find proper jobs. The better educated of them change their names - at least for professional purposes - to sound more French and less Arab. The most recent European tragedy shows the depth of the problem. The Netherlands - the country of legalized prostitution and legalized drugs - expected its large immigrant population to assimilate and melt away. Pim Fortuyn, an openly gay politician, won a seat to parliament campaigning that the Netherlands was "full" and immigration should be ended. He was subsequently murdered by a Dutch man. This year, Dutch television screened a film by Theo Van Gogh a relative of the painter, attacking the Muslim treatment of women. It contained images that many Muslims considered blasphemous. While riding his bicycle in Amsterdam, Van Gogh was shot 8 times and had his throat slit by a young Muslim who had been born in the country. In 2005, Europe will try to come to grips with this set of mixed messages about Muslim immigrants and their place in European society. But it will require a profound and painful reexamination of the bases of citizenship

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in European states. The challenge will be far from solved in 2005.

Another great challenge that will not be resolved in 2005 is that of European — American relationship. The EU is now split between "Euro-Atlanticists," led by Tony Blair joined by the Italians and the Poles, and the "Euro-Gaullists," led by President Jacques Chirac. Chirac seeks a Europe not merely independent of the U.S. but able to challenge the power of the United States. The division weakens both Europe and the U.S. and will not be either papered over or resolved in 2005 as both Presidents — Bush and Chirac - will stand by their mutual hostilities.

INDIA

India is on track for another banner year both politically and economically. Its new Congress led government was swept to power when Indian voters rejected the ruling BJP government on grounds that its economic benefits went to too few. The new Prime Minister, Manmohan Singh, was the architect of India's first market reforms in 1991 and will drive new reforms, despite depending on the votes of two communist parties to stay in power.

The GDP will grow some 6.5 percent in 2004. Watch for growth closer to 7 percent in 2005. Foreign Direct Investment in 2004 will be some 75 percent greater than it was in 2003. But India has a very long way to go. FDI into China in 2004 will be over \$50 billion. In India it will be \$4 billion.

THE DEATH WATCH

My top picks for the political leaders most likely to die - physically or politically - in 2004 were Osama Bin Laden and Saddam Hussein. I batted .500. My candidates for 2005:

The leader most likely to be assassinated by one of his own people: Ariel Sharon. Sharon has generated more hatred among Israeli settlers than did even the late Prime Minister Rabin. What will save Sharon's life are the vastly greater security procedures instituted since Rabin's murder.

The leader most wanted Dead or Alive: Osama Bin Laden remains at the head of the list followed closely by his Number 2 in al Qaeda, Ayman al-Zawahiri. The failure of either the U.S. or Pakistan to find him in 2004 when the administration pressed relentlessly for his capture before the elections and the recent withdrawal of the Pakistani military from the provinces bordering Afghanistan where he appears to be hiding, makes me less optimistic that these two criminals will be found in 2005.

CONCLUSION

The year 2005 will see world economic growth decline, oil prices subside from their 2005 highs, the "war after the war" continue to result in U.S. deaths, Iraq's political stability become more fragile, the Israelis and the Palestinians edging closer to a viable solution to their atrocity filled dispute, Europe and the U.S. remaining on a collision course as the U.S. continues its unilateralist foreign policy and President Chirac continues to argue for a multi-polar world, and China continues its relentless rise. Terrorists will continue to threaten our well-being.

If this is what the post-Cold War world has to offer the U.S., then maybe we should bring back the Soviet Union.