

Director's Dialogue with George Soros

Tony Giddens

I'm Tony Giddens, the Director of LSE. It's my pleasure to welcome you all to this event this afternoon. This event is a sort of experiment, this is my last academic year at the LSE, normally I stand on the stage here and I give these things called "The Director's Lectures" that I've given for the last five years, but to commemorate my passing I thought I'd try something different, hence these "Director's Dialogues". The idea of this is to have a public conversation with figures of notable world importance about issues of notable world importance in a fairly unstructured way. Later in the year we're hoping Javier Solana, the foreign policy chief of the EU will come. We hope that Joschka Fischer, the German foreign minister and leader of the Green Party will come and we've got, I hope, two other celebrity superstars lined up for these events.

Today it's a great pleasure for me to welcome George Soros who, I hope everyone here knows, is a graduate of the LSE. I don't think he had too much money when he originally came to the LSE but he's made himself a few bob or two since then. A lot of this is due to his encounters with Karl Popper and George has used the concept 'open society' not just for his foundation and institutes but it also forms an important part of his thinking about what we do in the current world juncture in relation to the relationship between the financial markets and other global institutions.

I'm not sure whether we'll have time for questions but if anybody wishes to pose questions would you like to write them down on slips of paper. If we do have time we'll answer, or try and answer one or two of them, but if you put your email address at least I will try to respond

to some of them. George won't give a guarantee that he will do the same but, you know, maybe he will be persuadable by one or two really good questions that really test him out.

Well, I thought, what we would do is to start with something moderately concrete and work from there to more general questions. What I had in mind starting with - something topical - the position of Latin America, Argentina and Brazil and Latin America. I was just sent yesterday a really interesting book called *The Internalisation of the Spanish Economy*. Well, I don't recommend that for a best selling title but the actual book is very good and the author of the book points out that in 1950 the GDP of Argentina, per head of population, was twice that of Spain. Today the GDP of Spain is almost six times as large in terms of current exchange rates as that of Argentina so there is a massive divergence in development here. Everybody is watching Argentina; of course at the moment everyone is watching Brazil too. The Brazilian elections are happening, it looks very likely that Mr De Silva will get a majority and he will become a leftist President of one of the biggest developing economies in the world so I thought we'd ask what this means.

Now, I thought maybe I'd speak to the inside bit a bit and then George might speak to outside a bit because I think there are certain policies which the incoming President will have to follow, but there are also certain responses from the wider global community which are necessary if Brazil is to avoid a lurch into a potentially disastrous situation. Internally, it seems to me crucial that Mr De Silva follows a policy of responsible leftism. I see nothing at all wrong, in fact I'm in favour of a left of centre government in Brazil. I think it's an example of insipient democratic process in Brazil that you have a different President, a different party likely to be dominant there; but that government in power must resist populism, must resist traditional statism, must, I think, carry on some of the successful

policies which President Cardoso has set in place. Under Cardoso, Brazil, I think, achieved more presence on the world stage; he certainly began to reform Brazilian institutions. President Cardoso is very fond of using the Spanish example of saying "Well, can Brazil follow the Spanish path?" because, you should remember also that Spain was modernised by left of centre party, by the Spanish Socialists after the Franco period. In Brazil you also have great achievements in reducing inflation, improvements in management of public finances, major innovations in education, anti poverty programmes and other areas and I feel the incoming government must continue some of those, or most of them. It will also want to try to regenerate economic growth and has to deal with the massive debt problem that Brazil has, which is largely an internal rather than external debt problem, at least in some key respects. The incoming government must also continue, I think, to expand attempts to cope with inequality in the country, but I think it is feasible to do this. I think a lot will depend on the response of the external community but a lot will depend also upon the new government that acts straight initially and therefore reassuring the wider investor community and other aspects of the global society.

George Soros

Well, I think the Brazilian government in fact is as close to an exemplary government as you can get, because they have done a lot in the area of social reform and at the same time they have followed the precepts of the Washington Consensus and they have been exemplary students of the IMF. Unfortunately this did not lead to growth. Growth has been languishing at 1½ per cent for the past four years or so and there is a general resentment against the Washington Consensus in Brazil and basically most of the candidates, except the Government candidate, are all actually left of ruler. So, you really have, in my opinion, a systemic failure looming in the case of Brazil. Some fault lines in the global capitalist system

have surfaced because apparently democracy is all right as long as you elect someone who is favoured by the financial markets, so that's not exactly...

Tony Giddens

That's too narrow a definition of democracy, as you say...

George Soros

... I think, acceptable and it is really also a failure of the system which, by its structure, favours the countries at the centre. For this purpose you may define countries at the centre as countries that can borrow in the financial markets in their own currency. That enables them to, let's say, engage in counter cyclical policies if they are in a recession and America actually stands as a shining example - most certainly by comparison to the European Central Bank - of actually moving in that direction, in other words, trying to be counter cyclical. But if you are at the periphery you can't do it, if you depend on the IMF, the IMF tells you that you've got to balance your budget and make sure that you can pay your debt. So now you have a serious problem because the currency has dropped, which has increased the burden of the dollar denominated debt and interest rates have sky rocketed where currently the Brazilian bonds - so called c-bonds which is sort of the leader - are 25% in dollar terms. Well, that means that you are insolvent.

Tony Giddens

The whole country can become insolvent.

George Soros

It's insolvent because it can't pay the debt. Now, Brazil has committed itself to a primary budget surplus of 3¾% and has a trade surplus. It has fairly large debts that have been accumulated partly because of the very high interest rates that Brazil has had to pay on its debts; they're now up to 60% of the GDP. With 3¾% surplus Brazil could pay up to 10% interest if it were growing at 3%. This is the equation where the debt would not be increasing in relation to the GDP. So, 10% is what Brazil can afford to pay; it cannot pay 25%. At 10% it's solvent, at 25% it's insolvent.

Now, this is where I think there has to be systemic intervention, there needs to be a lender of last resort, because if the system can't sustain a country like Brazil that has done all the right things then I think globalisation is going to break down and I think that there is now a very serious prospect of that happening, because I don't see the political will on the part of the authorities to provide this...

Tony Giddens

But you do think the external community can help Brazil, don't you, in respect of providing special conditions which it can control its debt and insolvency, because I think you need something from the outside and you need policies from the inside, you need them to mesh together as it were.

George Soros

Well, assuming that Brazil continues to maintain this 3¾% primary surplus I think that the IMF ought to guarantee the price of the debt. In other words open the discount windows using the central banks for financing purposes. But it is the IMF's responsibility to be willing to pay; to lend - let's say c-bonds sell at 45 – to lend 45. Now the bonds yield 25%, you have

no downside risk, you certainly are going to pay 60 or 65, then you could then raise the amount that the bank is willing to lend, introducing a margin and you could get the interest rate to 10%.

Tony Giddens

You suggested this in print, did anybody listen?

George Soros

They have listened, but it's not being seriously considered.

Tony Giddens

But in lieu of something like that you can see a major crisis looming?

George Soros

Well, the implication is, sort of there is these market fundamentalists who say "Well, if Brazil can't borrow then it should default." It should reorganise its debt. The conservatives that I've asked publicly, like Paul O'Neil, gave an answer was not quite intelligible, but...

Tony Giddens

He said put the money in a Swiss bank account?

George Soros

No, no, that was after that; but what I got out of his answer was that he's saying "Well, if the markets don't want to lend to Brazil, then Brazil has to reorganise its debt" and as you know

there are now proposals to make debt reorganisation less painful. This is the new trend to have some kind of international bankruptcy...

Tony Giddens

Yeah, even in the IMF it's being considered.

George Soros

This is now proposed at the IMF. Now, that will actually make reorganisation more likely because international debt is a very peculiar kind of debt. There is no security for it, except the pain that the country has to suffer if it defaults. But if you reduce the pain you reduce the security and so you in effect devalue the bonds and that is what's happening now. So, I think, there's probably better than a 50% chance that Brazil will have to reorganise its debt, through no fault of its own.

Tony Giddens

There is kind of restructuring of thinking going on though, isn't there? I mean, how far would you say the Washington Consensus is still a consensus? Amongst all these interesting things going on that we have to talk about is the impact of the debate on globalisation, which certainly has not left these organisations untouched. The people who have been protesting in the streets, it seems to me, are really the foot soldiers of the NGOs. The NGOs to some degree represent the conscious of humanity because they're saying, "Look, there are these things wrong with the world system, it's slanted towards the west, corporations have invaded public space, inequalities are much too big in the world." These things were largely ignored in the traditional marketplace consensus. The World Bank has changed a lot, the IMF seems to be changing, would you agree there is sort of progressive movement?

George Soros

Well, I think that the IMF has lost its way. Really it doesn't know quite what to do.

Tony Giddens

This is all going out around the world on the internet, so everyone will know this.

George Soros

Well, maybe I should...

Tony Giddens

...be careful what you say?

George Soros

...be careful what I say! But I have been saying it and I think it's necessary to say it, because it's important to have a local discussion and there needs to be a change, in other words there has to be some new thinking. Things don't work the way they used to. The IMF actually came through with a very large loan for Brazil. I can tell you that the markets were expecting \$24 billion and the IMF offered \$30 billion. Nevertheless, after a momentary rally the market went right back to lower than it was before. So, it means that the emperor has no clothes, the markets don't believe that the IMF is really in a position to, let's say, bail out countries in difficulties, because the IMF is now opposed to bail outs, you see, as a result of the '97-'98 crisis. There has been a shift in the IMF's position, a 180 degree shift. It used to be bail outs, now you're talk about bail ins and private sector participation. So, it's a big change. Now, actually the opposition to bail outs is very justified, because it meant that the IMF bailed out

the country in trouble to enable it to pay its debts, so the lenders got off scot free and the tax payers of the debtor countries had to pay the price. That was the case for instance in Mexico. So, it was unjust, but it kept the money going to the developing countries. Now, we have stopped the bail outs...

Tony Giddens

That's been cut off really hasn't it?

George Soros

... and as a result there is now a general lack of funding for what I call the periphery countries and the global system continues to suck up the savings of the world to the financial markets, but the financial markets and the multi-nationals no longer push it out to the periphery because the risk reward ratio has turned against the periphery. So, there is a new problem an inadequate supply of capital to the developing world and that problem is not yet recognised. I mean everybody can see it because since '97 there has been a continuing reverse flow of capital from the periphery to the centre. So, you can observe it, but you attribute it to temporary factors, whereas I argue that it's structural, it's in the nature of the system and therefore the system needs to be reformed.

Tony Giddens

Well, yes, I agree with almost to all of that, but then the question is what kind of policy responses should western governments, international organisations and developing countries themselves make? A lot of people will have been to hear Joe Stiglitz when he came last year talking about his book. He has a whole range of proposals really about what developing countries should do and how the world should respond to a situation where essentially the old

ideology has really broken down and I think in large respects what we're describing is a breakdown of that consensus; a breakdown of that view of the world. And then you have questions like should - as Stiglitz seems to say in his book - poorer countries erect some kind of tariff to protect themselves, because his argument and many people's argument, I think, is that those countries that have been successful have not been successful behind the open, liberalised capital market system which the IMF promoted and therefore a poorer country now needs to build some kind of defensive mechanisms against invasion from financial crisis.

George Soros

Yes. I mean, basically if the system doesn't provide for you then you have to fend for yourself and so then you return to capital controls and go back from globalisation. Now, I think this would be a great pity for a number of reasons and that's why I would prefer to see the system actually be modified to take care of its members, which is not happening now. I mean take Brazil for instance, if the financial markets don't perform a miracle and drop interest rates, which I don't think they are going to do, then Brazil will be forced to impose capital controls. Now, I think that actually Brazil can make that change without much damage relatively. In fact it could probably grow faster by reorganising its debt, imposing capital controls and so on, but it would worse for the rest of the world, because you would then have a contagion...

Tony Giddens

A lot of people doing the same, you mean?

George Soros

I mean it would, for instance, affect Mexico - it already has affected Mexico. It would basically deny access to all of Latin America to the financial markets. So, Latin America would become a disaster area.

Tony Giddens

So what would be your main policy?

George Soros

And just to finish the thought, it would affect some of the international banks and could really also cause some trouble in the banking system, which is already under pressure.

Tony Giddens

Plenty of troubles there.

George Soros

So, we are in serious trouble and I don't think the authorities are paying attention to it.

Now, you are asking what could be done, I have now two major proposals: one, a gradual evolution of a lender of last resort to countries that are following sound policies like Brazil, and that would be opening the discount windows and making credit available at reasonable rates; and globally we are now, I think, flirting with deflation. We've had, you know, twenty years of globalisation against the background of a global bull market, basically with occasional interruptions. We now have a global bear market and then the flaws in the system, whatever can go wrong will go wrong in a bear market and that's where we are now.

So, we now face the prospect of deflation. That is what, let's say, has happened in Japan. When you have deflation then the burden of debt becomes larger, so companies have to work down their debt rather than invest and even then bad debts pile up. So, that's the Japanese problem.

Something similar could be happening now. So, you want to stop it and I think, actually, the US is doing whatever it can to stop it as far as the US economy is concerned, but for the global economy you need a new source, a new engine. The US economy has been the engine of the global economy, because as you can see it from the continuing current account deficits, the United States now runs a current account deficit equal to 5% of the GDP - \$500 billion a year, that's a very large amount...

Tony Giddens

Well, you can only do that if you're the US.

George Soros

Which America is actually spending, so it is a stimulus for the rest of the world. It creates an export market for the rest of the world. The motor is now faltering, so you need a new motor and you need to stimulate domestic led growth, not so much export led growth, in the developing world, and for that purpose I have proposed issuing these special drawing rights which are too complicated to explain, but is some kind of international...

Tony Giddens

They give you money that you can apply to poorer countries to help in key areas of development, essentially.

George Soros

And then...

Tony Giddens

And they're not too different from Gordon Brown's plan although he's getting it from different sources.

George Soros

Yeah, I mean Gordon Brown is arguing very passionately for \$50 billion a year. You could actually get that \$50 billion by issuing special drawing rights with the right countries donating their receipts for international assistance, and I think this is a proposal whose time has come because we have these, let's say, unused resources in the world. So, it would really not cost anything because you would only be putting resources to work, which are currently idle.

Tony Giddens

Well, can we go on and talk a bit about the issue of global inequalities, global poverty, because that's plainly one of the main concerns of the so-called Anti-Globalisation Movement. I think it's plain that the term Anti-Globalisation Movement is largely a press invention and you're talking about a movement, which is pressing among other things for a more equitable world.

Now, so far as I can see all our experience shows that there is only one way to leverage millions of people out of poverty and that is economic development in which the poor

participate. The difficulty for poorer countries is not just generating the economic growth that will promote that development, but making sure that the poor do participate and a kind of market orientated approach, which has been applied to so many countries really essentially, hasn't produced that. Therefore there is a lot to be said for Stiglitz's view that globalisation is not working in that context and we need to look for policies which will allow the kind of leverage which has certainly been achieved in some countries; I mean obviously some of the Asian economies - Vietnam is often quoted as an example of a developing country where levels of inequality have not actually gone up and we need to look for a package of policies which will allow the use of the kind of resources that you're mentioning more fruitfully.

George Soros

Yes.

Tony Giddens

It seems to me, quite a few of those have to still be on the supply side because you must spend on education, you must spend on local community renewal, you must get women into the labour force, you must to some extent attack the traditional family which imprisons women and produces a demographic trend which developing countries must overcome, but do you think there's anything else that should be done, I mean you must have debt remission I think because...

George Soros

Well, I think, you see, coming back to the anti globalisation movement, I think that they have picked on some real defects in globalisation. Now, some of them have gone on to argue for the abolition of the international institutions we have. I think that has been a big, big mistake,

because we need those institutions and we need to reform them and improve them and not abolish them.

Tony Giddens

There's a left and a right which says get rid of the institutes.

George Soros

Particularly, actually the World Bank which has been subjected to very severe criticism. Some of it, as I say, justified but it comes at a time when it is under the leadership of Tim Wolfenson, who is really trying to move it into creating social capital rather than building dams. But, the World Bank remains damned for its past dams and not appreciated for trying to change it's ways. So, I think the big mistake of the anti globalisation people is to blame the international institutions whereas the main source of poverty in the world is actually bad government. In other words, in my opinion, there are two major sources for poverty, one is bad government and the other one is bad location. I visited Mongolia and it actually has very good government, good human resources, it's got wonderful, lovely people...

Tony Giddens

That's why the LSE campus has been so poor for many years – bad location, bad government – all improved now.

George Soros

This is the LSE so you can't do too much about bad location, but you can do something about bad government and that is where the focus ought to be. In other words, you ought reinforce countries that have good governments and penalise countries that have bad governments but

you can't really go too far in the penalisation direction because you have the principle of sovereignty and you can't interfere in the internal affairs of countries. However, you can offer incentives if they voluntarily move and use those incentives and that is what we don't do enough, because that goes against the sort of, the market fundamentalist belief that, you know, you are now supposed to give goodies to anybody.

Tony Giddens

Yes, and I think there is a new consensus emerging: that reform of government, reform of institutions and creation of public trust is crucial to economic development. It is easy to say "do this", but there are difficulties in doing it in a lot of countries around the world because a lot of the problems I think the developing world faces are not to do with globalisation, they're from the cold war period. I can think of an example, I recently went to Guatemala. Guatemala had this horrendous, partly US financed civil war in which half a million people in a country of 12 million people died and you had death squads roaming around the country. The country is trying to recover, but it's a cash crop economy, the price of coffee, its main cash crop, has been devastated on world markets recently. There's still General Montt in the background who kind of runs the government. They are trying to create a democratic system but it's extremely hard to do it against a backdrop which is so common.

George Soros

I set up a foundation in Guatemala when there was a change of government, because I believe in reinforcing society, in moving towards what I call an open society and I thought there was an opening in Guatemala; but windows were shutting because the repressive right wing is reasserting its power and the whole process of reconciliation is running out of steam in Guatemala.

Tony Giddens

They actually have a President there called Portillo and everybody knew about Michael Portillo in Guatemala because of the similarity between the names of Michael Portillo and the President of Guatemala; they seemed to be trying to get legitimacy from Michael Portillo which is a strange thing to do.

Anyhow, there are these serious problems, I think there are no magic bullet solutions, but I think it is pretty obvious that in a lot of developing countries it is the state that is the problem, not markets, and the state is very hard to reform.

George Soros

Take the issue of Africa which is now receiving a lot of attention and I must say that you have a real leadership from your government here. I mean...

Tony Giddens

Well, especially now Gordon Brown been...

George Soros

Both Blair and Gordon Brown, you know. I hear a lot about differences between them but I find that both of them are actually very much engaged in these arguments, they put it on the agenda for the G8 meeting and so on and there is, in fact, something called NEPAD which is a New Economic Partnership for...

Tony Giddens

Development.

George Soros

Whatever, but if you look at Africa you've got countries which are resource rich and countries which are resource poor. When you look at the people living there, they are miserable in practically all of the countries, except the resource rich countries have more corrupt governments than the resource poor countries. You find good governments in countries like Senegal, Mali...

Tony Giddens

Mozambique.

George Soros

Mozambique now – and then you have got the Congo and you have got Angola where an enormous amount of oil and the money is being stolen. So, you have to deal with that problem. I support an NGO called Global Witness that launched a campaign called “Publish What you Pay”, which requires the resource companies to disclose how much they are paying to the government. From this, you could add it together and could then hold the governments responsible. In the case of Angola, you have a gap of certainly in excess of \$1 billion a year. So Angola could, now that the civil war is over, really become a prosperous country. It could certainly, let's say, be as prosperous as Botswana, which is also relatively resource rich and has a relatively good government. But we have to get there and that is where you need the international institutions and the international public opinion to weigh in.

Tony Giddens

Yeah, and more debt remission I would say too. I think the case of Africa does show first of all that it is possible to get your act together, even from relatively unpropitious circumstances because, if you look at Mozambique for example, that was, to me, pretty much like Guatemala; a war torn country with terrible, terrible problems, but they did manage internal political reform and it might surprise people to know that of the 20 fastest growing economies last year, seven of those are in Africa. So Africa is certainly not completely 'all of a type' but there is no doubt that somehow you can make political reforms. I think, though, that it's quite difficult to spot the cases of countries where you can make these reforms and where you can't, in Guatemala I think it would be very difficult to do it, whereas Mozambique in a way was worse than Guatemala, but it still managed to reform itself...

George Soros

A lot depends on the leadership, the local leadership. Mozambique has a Prime Minister, who's a doctor and I met him in the context women's reproductive rights, there's a global organisation and he's part of that organisation. So, obviously an enlightened...

Tony Giddens

Yes, well he must be an LSE graduate.

George Soros

Well, it doesn't surprise me.

Tony Giddens

I don't know that it's true!

George Soros

And so leadership is very important. And then democracy is terribly important too, in other words free elections, and more than just free elections, independent and so on.

Tony Giddens

But can you be a bit more precise about what in your view the west should do about Africa? I think there are a range of possible programmes which all of us should try to support. You mentioned disclosure by corporations helping governments to transform themselves by actively providing benchmarking, involvement of the west, debt remission, I think you could think of five or six other concrete policies. I mean aid is obviously...

George Soros

Well, you actually have a lot of good things, in the embolic stage. Even the Millennium Challenge Account that the United States has put out is promising - until it gets maybe fouled up, but it is conceptually promising. This idea is promising. Now, it's very important to have a civil society leg to it, because it is based on the idea of peer review: that the Presidents of the countries are going to admonish each other to be good boys - and you see what's happened in Zimbabwe. But it has broken down before it has started, because the countries in the neighbourhood didn't deal with the problem of the stolen elections. So, you have problems, but I think you also have some understanding of the problems and as I say it's very important to get civil society involved in the process. If you leave it only to governments it won't work, and actually my foundation network has this as its major objective: to mobilise civil society to participate and keep the governments honest. You know, it's early days but that is actually our objective.

Tony Giddens

Well, do you think we could zip back to financial markets and then go to Europe and then go to the hyper power, the US to finish with?

What's wrong with global financial markets, the way they function? Because you have a particular position.

George Soros

I have this theory that the concept of equilibrium is not applicable to financial markets because financial markets don't deal with known quantities. You know, if you deal with widgets you can calculate where the equilibrium is, but when you're dealing with the future and the future is contingent on how you deal with it at present, you're not dealing with something known. There is a genuine uncertainty in financial markets, and one has to recognise that and there is this, sort of, feedback mechanism, which I call reflexivity, which can...

Tony Giddens

...I call it reflexivity as well, because...

George Soros

Right, in fact that's how we really, our first conversation started, on the concept of reflexivity.

Tony Giddens

It was, yeah.

George Soros

We arrived at it from different directions.

Tony Giddens

Anyway, please go on.

George Soros

So, basically, financial markets tend to be self-reinforcing until they go to an extreme, which becomes unsustainable and then you have a reversal.

Tony Giddens

As they just did?

George Soros

As they just did. So we just had a perfect boom-bust sequence in the last five years with the internet and telecommunications and the whole market, you see, and now we are in the morning after and it's less stimulating and enjoyable than the feast.

Tony Giddens

Yeah, but what would be the morning after pill? I mean what...

George Soros

Well, as I say, I think that for instance, the NEPAD would be very helpful.

Tony Giddens

Well, that might protect poorer countries but how is that going to deal with a Keynesian type phenomena of...

George Soros

Well, Keynes lives again. This is Keynes situation and you need monetary stimulation and you need fiscal stimulation and the United States actually is indulging in both, because preparing for war...

Tony Giddens

Starting a war?

George Soros

So, actually the US economy is not in such a bad shape. It's relatively much better than the financial markets would lead you to believe. I have not really seen an economy in the depression when you are gearing up for war, I mean, I have to be very careful because of the drawing any parallels, I mean I remember Nazi Germany was actually quite prosperous as it was gearing up for war.

Tony Giddens

You've got to be very careful.

George Soros

But I'm not a minister so I don't have to resign, but there is...

Tony Giddens

But, I mean, can you think of any circumstances in which hot money going to developing country helps that country?

George Soros

Hot money?

Tony Giddens

Yeah. Money that zips in and zips out again because that's the gist of a lot of people's critique of how financial intersect with development.

George Soros

Well, I mean, you have, for instance, China now, that's not hot money, because...

Tony Giddens

Well, China kept out a lot of the...

George Soros

Yeah, well, China now attracts half the direct investment in the world, it's coming up very strong.

Tony Giddens

But it protected itself from financial contagion...

George Soros

Yes, but it's not hot money, it's not money.

Tony Giddens

It did not follow IMF policies in that...

George Soros

No, hot money is...

Tony Giddens

Doesn't help anybody much, does it?

George Soros

...dangerous. When I was a student at LSE I remember the studies of the interwar period, published at the League of Nations something or other, explaining all the detriments of hot money. So it's not a new problem, it was also there in the interwar period.

Tony Giddens

But we don't seem to have solved it.

George Soros

No, we haven't.

Tony Giddens

It's got worse because of globalisation essentially, wouldn't you say?

George Soros

That's right, and that's why you need a strengthening of the International Monetary Fund to be able to provide a counter cyclical, to be a lender of last resort when the financial markets panic.

Tony Giddens

Well, maybe we could just take a quick swing through Europe, because you mentioned strong deflationary tendencies. It's a serious issue for the world economy and Germany is one of the countries which seems to be close to a Japanese style scenario. It was only about a year ago I went to a meeting - I think there's another one next week - of *The Economist* at which people were still talking about the possibility of Europe being a motor of the world economy as the US slows down. Well, that hasn't happened at all. Growth rates in Germany are very, very low and Germany is the central economy in Europe. There are big questions about the economic reforms necessary in the EU countries if the EU is going to play some part in, not just counter balancing the US, but also not contributing to a world deflationary scenario. I'm being a bit hard, but I can't quite see at the moment where that's going to come from. I think, basically, that the UK has got its economic act right against the backdrop of the world economy; it's made the right kind of reforms; but Germany hasn't yet; France hasn't yet; the EU economies haven't. There's not sign of these countries injecting the sort of dynamism that they could inject.

George Soros

Well, I would say this that the European economy is in worse shape than the American economy and also that the economic leadership is worse in Europe than in America. When you look on the financial side the ECB – European Central Bank – basically drives with rear view mirrors. The Federal Reserve is sometimes right, sometimes wrong, but at least it's

looking forward and tries to anticipate; whereas there are institutional constraints on the ECB not allowing it to look forward because it has to, for instance, bring inflation down to a certain level before it can...

Tony Giddens

Well, can the ECB ever be like the Federal Reserve? If you don't have a Federal Europe can the ECB ever be like the Fed?

George Soros

It could be because it's marching orders could be changed, in other words: the mission of the ECB is to fight inflation; the mission of the Federal Reserve is not just to fight inflation and maintain price stability but also to maintain growth. The ECB has made it clear that it is not its mission to maintain growth. Now, you know, since it was created at a period when you had inflation for the last 40 years, it does seem to make sense. But if you now face a world where deflation is a much of a threat as inflation then this framework is not the right framework. So, there is some problem there with the policies of the ECB. I think the ECB should be lowering interest rates much more aggressively than it has done.

Tony Giddens

Yeah, I mean personally, I think there are two problems, a problem of getting people to interpret what the ECB does because of its somewhat ambiguous and its rather closed and non-transparent nature and then the problem of how, with the current policy, you can possibly stimulate demand and therefore provide a mode for growth in Europe. At the moment I can't see without reform it's going to do either of those things so it's difficult to see Europe stepping in to fill the gap.

George Soros

No, you also have the stability pact which puts...

Tony Giddens

Well, that puts a brake on the amount of money you can invest...

George Soros

...on fiscal stimulus and then you have the structural problems, which are the most serious, the social security system for instance in Germany that needs reforming because it functioned well in a more isolated economy and doesn't function in a more global economy, so you have structural rigidities that you need to overcome. So those are the three areas and the result is, I think, that Europe is weaker, the economy is weaker, the banking system is weaker, the financial system is weaker. You see a lot more strain for instance in German banks and in European insurance companies than you do in America.

Tony Giddens

I agree with some of that, I think it's a bit one sided because there are lots of strengths in Europe and I think the European social model is still real, it still creates societies with more solidarity and protection than is true in the US. The problem is to try and reconcile that with generating recent and decent growth rates and levels of employment. We know in some EU countries that this has been done - mostly the smaller ones - I think we should defend the European social model; you wouldn't want to just juxtapose it to the US.

Can we just finish by discussing the hyper power? I mean here we are in a world with the US militarily dominant and it will be so for the foreseeable future. It's now got a Republican government that has a particular stance in relation to the wider world. This idea sits uneasily alongside the EU. The EU is not just, I think, morally committed to multi-lateralism; it is an expression of the idea that in a globalised world you need trans-national institutions. The current US regime seems directly opposed to that very idea and we're on the verge of potential violent conflict in the Middle East, so, what should happen?

George Soros

Well, I happen to be really quite exercised about this because...

Tony Giddens

Well, we all bloody should be exercised about it!

George Soros

There's no question that the United States is the dominant power in the world today; but it's misusing its dominant position. It wants to reinforce its dominance instead of taking care and providing some leadership in developing the institutions that you need for a global economy and a global society. So, the United States has a tremendous responsibility because nothing can be done in the way of international cooperation without the agreement and cooperation of the United States; but the United States has gone out of its way to renounce international cooperation - the Bush administration even before September 11 sent signals, renouncing the Kyoto Treaty, renouncing the Biological...

Tony Giddens

International Criminal Court and...

George Soros

Well, the International Criminal Court is really quite outstanding because not only did we not participate, but we have really gone out of our way to sabotage it...

Tony Giddens

Subvert it.

George Soros

To subvert it. So, there is this very definite anti multi-lateral, anti cooperationist view and at the same time you have a new doctrine, 'the Bush doctrine', which basically has two pillars: one is pre-emptive strikes; and the other is a determination to maintain our military superiority. That means that we are basically establishing two classes of countries, or two classes of sovereignty. There's the sovereignty of the United States, it is sacrosanct and cannot be infringed by international treaties and then there's the sovereignty of everybody else which is subject to America's right of pre-emption and its determination to maintain unquestioned superiority. I think this is a very, very dangerous doctrine. I don't believe that is what America stands for and I'm very hopeful that the people in America will shake off their fears that after the terrorist attacks there is a sense in that we are endangered in our existence. We must realise that we are the leading nation in the world and if we only care about our own survival then how will civilisation survive? In other words, I think that there is a real danger here.

Tony Giddens

So do I, I think it is very, very serious. I mean everyone should remember the US is a fifty-fifty society and 50% of the population voted for a different kind of leadership from the one the US has...

George Soros

Yes, but you now have 70% or 75% lined up behind the President because of the terrorist attacks and, you know, the perceived threat that...

Tony Giddens

Well, you don't have that completely, because only 20% of the American population support unilateral American intervention in the Middle East.

George Soros

Yes, yes.

Tony Giddens

That's only 20%.

George Soros

No, it's more than that.

Tony Giddens

Twenty percent, they did this big, big survey and we discussed it very recently, it's only just over 20%.

George Soros

I thought it was basically a third.

Tony Giddens

No, because the interesting thing about this survey was it was more or less the same percentage in Europe and the US. Everyone who said the US is different from Europe will find that it didn't look so different in these surveys which I thought was very interesting.

Can we just say a few words about Russia?

George Soros

No, but I think before we go to Russia we should talk about all that.

Tony Giddens

Well, we're going to finish.

George Soros

Okay, we will leave Russia, because this is...

Tony Giddens

Quite a few significant Russian members of the audience though, so I felt we had to...

George Soros

You want to go to Russia?

Tony Giddens

Well, I mean it's bound up with hyper power of the US, so it's just another angle on it.

George Soros

Well, okay, I think that Putin loves this geo-political game proposed by the Bush administration; they are made for each other. It's actually very positive for Russia because being closer to the United States there is a geo-political alliance, an alternate source of oil, because after all oil is very important in this whole situation.

Tony Giddens

We did notice that.

George Soros

And it's important in Iraq. One of the reasons why we are so concerned with Iraq, although we don't talk about it, is because we have lost confidence in, and don't want to rely on, Saudi Arabia as the supplier of oil - we don't want to be dependent on Saudi Arabia. If we have Iraqi oil and Russian oil we are no longer dependent on Saudi Arabia. So, there is this geo-political alliance, which I think is very positive for Russia. I think it gives people in Russia an opportunity to fight for an open society, to build an open society. Even though the United States is not going to be particularly concerned with issues of democracy and human rights and what happens in Chechnya and so on; nevertheless the fact that Russia is part of the world gives an opportunity for Russian society to develop, and there you need to develop what I call horizontal structures to interrelate with the vertical structures that Putin is re-establishing. In other words after the revolution you are now in the phase of restoration: a restoration of the state power and if you leave it to the state then of course it will re-establish

vertical controls. So people actually have to become engaged in developing institutions which are not independent of the state. So, it's a very exciting time in Russia.

Tony Giddens

I mean there isn't necessarily an unholy alliance between Bush and Putin...

George Soros

It's not unholy, I mean...

Tony Giddens

...because, surely the Russians could play a role in, and will play a role in...

George Soros

No, absolutely, and I think that this comes back to Iraq. I think there is pretty universal recognition that Saddam is a bad guy and we ought to get rid of him or contain him; him having weapons of mass destruction is a real danger to the world. But we have to deal with it in a lawful manner and that's where Russia comes in. And to end on a hopeful note I think it could really work out all for the better, because even though you have got these cowboys in the US administration there is still constraints on them: reality constraints. There's American public opinion, world public opinion, etc. I think the administration will prefer to go through the United Nations and I think that the United Nations is likely to pass a severe enough regime of inspection to ensure that Saddam can't use those weapons and I think there is also a good chance that actually Saddam will succumb and actually allow the inspections to take place. Now, there are people in the US government that don't want that outcome...

Tony Giddens

Sure, about half of them.

George Soros

...Because that still leaves Saddam there. However, I think that would be a very positive outcome because it would mean that the United Nations has exercised serious control over a rogue state. It would be a victory for international governments.

Tony Giddens

We do have to stop actually. Sitting in the front there is Professor David Held who's got a very good series on American power in the 21st century, starting at the LSE next term and there will be multiple discussions of, I think, all of the issues that have been raised here. I must say I have thoroughly enjoyed it, I hope you weren't all too bored and can you please give George a big round of applause for coming here.

ENDS